

## Board Meeting Agenda

5 December 2019

9.20 am to 5.15pm

XRB Offices, Level 7, 50 Manners Street, Wellington

| Est. Time                    | Item                 | Topic  | Objective |       | Page |
|------------------------------|----------------------|--|-----------|-------|------|
| <b>A: NON-PUBLIC SESSION</b> |                      |  |           |       |      |
| <b>B: PUBLIC SESSION</b>     |                      |  |           |       |      |
| 11.15 am                     | <b>4</b>             | <b><u>ISA (NZ) 315 (Revised)</u></b>                 |           |       |      |
|                              | 4.1                  | Board meeting summary paper                          | Note      | Paper |      |
|                              | 4.2                  | ISA (NZ) 315 (Revised) clean                         | Approve   | Paper |      |
|                              | 4.3                  | ISA (NZ) 315 (Revised) mark up from ISA 315          | Consider  | Paper |      |
|                              | 4.4                  | Conforming amendments clean                          | Approve   | LATE  |      |
|                              | 4.5                  | Conforming amendments mark up from IAASB             | Consider  | LATE  |      |
|                              | 4.6                  | Signing memo   | Approve   | Paper |      |
| 12.15 pm                     | <b>5</b>             | <b><u>Update on joint report with FMA</u></b>        |           |       |      |
|                              | 5.1                  | Board meeting summary paper                          | Note      | Paper |      |
| 12.30 pm                     | <i>Lunch</i>         |  |           |       |      |
| 1.00 pm                      | <b>6</b>             | <b><u>NZ SRE 2410</u></b>                            |           |       |      |
|                              | 6.1                  | Board meeting summary paper                          | Note      | Paper |      |
|                              | 6.2                  | Issues paper   | Consider  | Paper |      |
|                              | 6.3                  | NZ SRE 2410 (mark-up)                                | Consider  | Paper |      |
| 2.15 pm                      | <b>7</b>             | <b><u>Small NFPs</u></b>                             |           |       |      |
|                              | 7.1                  | Board meeting summary paper                          | Note      | Paper |      |
|                              | 7.2                  | Issues Paper   | Consider  | Paper |      |
| 2.45 pm                      | <i>Afternoon tea</i> |  |           |       |      |
| 3.00 pm                      | <b>8</b>             | <b><u>NAS and Fees</u></b>                           |           |       |      |
|                              | 8.1                  | Board meeting summary paper                          | Note      | Paper |      |
|                              | 8.2                  | Issues-NAS   | Consider  | Paper |      |
|                              | 8.3                  | Issues-Fees  | Consider  | Paper |      |
| 3.30pm                       | <b>9</b>             | <b><u>Group audits</u></b>                           |           |       |      |
|                              | 9.1                  | Board meeting summary paper                          | Note      | LATE  | -    |
|                              | 9.2                  | Issues paper   | Note      | LATE  | .    |
| 4.00 pm                      | <b>10</b>            | <b><u>IAASB conforming amendments IESBA Code</u></b> |           |       |      |
|                              | 10.1                 | Board meeting summary paper                          | Note      | Paper |      |
|                              | 10.2                 | Draft submission                                     | Approve   | Paper |      |
|                              | 10.3                 | IAASB ED   | Consider  | Paper |      |
|                              | 10.4                 | NZ ITC ED Conforming amendments                      | Consider  | Paper |      |

| Est. Time                    | Item      | Topic                                      | Objective |       | Page |
|------------------------------|-----------|--|-----------|-------|------|
| 4.30 pm                      | <b>11</b> | <b><u>Modified audit report update</u></b> |           |       |      |
|                              | 11.1      | Board meeting summary paper                | Note      | Paper |      |
|                              | 11.2      | Summary of modified reports                | Note      | Paper |      |
| 4.35 pm                      | <b>12</b> | <b><u>Environmental Scanning</u></b>       |           |       |      |
|                              | 12.1      | International monitoring update            | Note      | Paper |      |
|                              | 12.2      | Domestic monitoring update                 | Note      | paper |      |
| <b>C: NON-PUBLIC SESSION</b> |           |  |           |       |      |

Next meeting: 12 February 2020, Wellington

## NZAuASB Board Meeting Summary Paper

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**AGENDA ITEM NO.** 4.1  
**Meeting date:** 5 December 2019  
**Subject:** ISA (NZ) 315 (Revised)  
**Date:** 22 November 2019  
**Prepared by:** Peyman Momenan

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☒ **Action Required**

☐ **For Information Purposes Only**

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### Agenda Item Objectives

1. The objective of this agenda item is for the Board to:
  - APPROVE International Standard on Auditing (New Zealand) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*, and Conforming Amendments to ISAs (NZ) and Other Pronouncements
  - APPROVE the signing memorandum.

### Background

#### Domestic

2. Detailed discussion of the background and an analysis of the comments made in the NZAuASB submission and their related disposition by the IAASB was presented at the September 2019 NZAuASB meeting. This discussion is also summarised in the draft signing memorandum at agenda item 4.4. No compelling reason amendments were identified by these discussions.
3. Extant ISA (NZ) 315 contains two NZ paragraphs in the application material.
4. NZ A1.1 was amended by the NZAuASB to be consistent with changes made by the NZAuASB within ISA (NZ) 580, *Written Representations*. To remain consistent with the changes previously made in New Zealand to ISA (NZ) 580, we recommend including a reference to management and where relevant those charged with governance when obtaining written representations. Refer to paragraph NZ A51 in agenda item 4.2.
5. In extant ISA (NZ) 315, the NZAuASB had added an additional paragraph as follows:

“NZ A25.1 Ownership and Governance arrangements such as:

  - The role of the board of directors and those charged with governance in determining policies for the levels of risk that the entity is willing to accept in its daily operations.

- The role of senior management in designing, implementing and monitoring effective risk management systems to implement the policies prescribed by the board of directors.
  - The presence of non-executive directors on the board and an independent compensation committee that reviews incentive plans, including commissions, discretionary bonuses, directors' service contracts and profit-sharing plans.
  - The role of line management in carrying out the prescribed procedures and control activities.
  - The strength of the internal audit function and the audit committee and the audit committee and their role as an independent appraisal function.
  - The strength of other significant committees, for example, risk management committee, asset and liability management committee, or general management committee.
  - The adequacy of segregation of duties.
  - Prior period financial reporting disclosures include the form, classification, terminology, basis of amounts and level of detail provided."
6. We consider that these matters are now included with ISA 315 (Revised) in paragraph A59 and A60 and therefore there is no longer a need to add a New Zealand paragraph within ISA (NZ) 315 (Revised).

#### Australia

7. The AUASB is yet to approve ASA 315 (Revised). Approval of ASA 315 (Revised) is not on the AUASB Agenda for their December meeting and the AUASB is likely to consider the standard for approval in their March 2020 meeting.

#### **Matters to Consider**

8. The Board is asked to CONSIDER and APPROVE ISA (NZ) 315 (Revised) and related Conforming Amendments to ISAs (NZ) and Other Pronouncements and APPROVE the signing memorandum.
9. ISA 315 (Revised) and the Conforming Amendments to ISAs are yet to be approved by the PIOB (scheduled for approval in the PIOB November 2019 meeting). Staff will ensure that the ISA (NZ) 315 and the Conforming Amendments to ISAs (NZ) agree with the final standards once final approved standard and conforming amendments are available. The Board will be notified of late editorial changes that may be made.
10. The draft ISA (NZ) 315 (Revised), agenda item 4.2, and Conforming Amendments to ISAs (NZ) and Other Pronouncements, agenda item 4.4, will be gazetted once approved by the Board.
11. The Financial Reporting Act 2013, section 22(2) requires that the External Reporting Board consult with the Privacy Commissioner where an accounting or assurance standard is likely to require the disclosures of personal information. No such consultation is required in relation to this standard.

### **Material Presented**

|                 |   |
|-----------------|---|
| Agenda item 4.1 | Board meeting summary paper   |
| Agenda item 4.2 | Draft ISA (NZ) 315 (Revised) (clean for approval)   |
| Agenda item 4.3 | Draft ISA (NZ) 315 (Revised) (mark up to consider)  |
| Agenda item 4.4 | Draft Conforming Amendments to ISAs (NZ) and Other Pronouncements (clean for approval) <b>(LATE PAPER)</b>  |
| Agenda item 4.5 | Draft Conforming Amendments to ISAs (NZ) and Other Pronouncements (mark up to consider) <b>(LATE PAPER)</b> |
| Agenda item 4.6 | Draft signing memorandum (for approval)   |



NZ AUDITING  
AND ASSURANCE  
STANDARDS BOARD

## INTERNATIONAL STANDARD ON AUDITING (NEW ZEALAND) 315 (Revised)

### Identifying and Assessing the Risks of Material Misstatement (ISA (NZ) 315 (Revised))

This Standard was issued on ?? by the New Zealand Auditing and Assurance Standards Board of the External Reporting Board pursuant to section 12(b) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on ??.

An auditor that is required to apply this Standard is required to apply it for audits of financial statements for periods beginning on or after 15 December 2021. However, early adoption is permitted.

In finalising this Standard, the New Zealand Auditing and Assurance Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued as a result of International Standard on Auditing 315 being revised.

This Standard, when applied, supersedes International Standard on Auditing (New Zealand) (ISA (NZ)) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

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## INTERNATIONAL STANDARD ON AUDITING (NEW ZEALAND) 315 (Revised)

**IDENTIFYING AND ASSESSING THE RISKS OF MATERIAL MISSTATEMENT***Issued by the New Zealand Auditing and Assurance Standards Board***CONTENTS**

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Appendix 6: Considerations for Understanding General IT Controls

Accompanying Attachment: Conformity to the International Standards on Auditing

**International Standard on Auditing (New Zealand) (ISA (NZ)) 315 (Revised), “Identifying and Assessing the Risks of Material Misstatement” should be read in conjunction with ISA (NZ) 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (New Zealand).”**

## History of Amendments

### Table of pronouncements – ISA (NZ) 315 (Revised) *Identifying and Assessing the Risks of Material Misstatement*

This table lists the pronouncements establishing and amending ISA (NZ) 315 (Revised).

| Pronouncements   | Date approved | Effective date   |
|--|---------------|--|
| International Standard on Auditing (New Zealand) 315 (Revised) | December 2019 | Effective for audits of financial statements for periods beginning on or after 15 December 2021. |

## Introduction

### Scope of this ISA (NZ)

1. This International Standard on Auditing (New Zealand) (ISA (NZ)) deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements

### Key Concepts in this ISA (NZ)

2. ISA (NZ) 200 deals with the overall objectives of the auditor in conducting an audit of the financial statements,<sup>1</sup> including to obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level.<sup>2</sup> Audit risk is a function of the risks of material misstatement and detection risk.<sup>3</sup> ISA (NZ) 200 explains that the risks of material misstatement may exist at two levels:<sup>4</sup> the overall financial statement level; and the assertion level for classes of transactions, account balances and disclosures.
3. ISA (NZ) 200 requires the auditor to exercise professional judgement in planning and performing an audit, and to plan and perform an audit with professional scepticism recognising that circumstances may exist that cause the financial statements to be materially misstated.<sup>5</sup>
4. Risks at the financial statement level relate pervasively to the financial statements as a whole and potentially affect many assertions. Risks of material misstatement at the assertion level consist of two components, inherent and control risk:
  - Inherent risk is described as the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
  - Control risk is described as the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's system of internal control.
5. ISA (NZ) 200 explains that risks of material misstatement are assessed at the assertion level in order to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence.<sup>6</sup> For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk and

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<sup>1</sup> ISA (NZ) 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

<sup>2</sup> ISA (NZ) 200, paragraph 17

<sup>3</sup> ISA (NZ) 200, paragraphs 13(c)

<sup>4</sup> ISA (NZ) 200, paragraph A36

<sup>5</sup> ISA (NZ) 200, paragraphs 15–16

<sup>6</sup> ISA (NZ) 200, paragraph A43a and ISA (NZ) 330, *The Auditor's Responses to Assessed Risks*, paragraph 6

control risk is required by this ISA (NZ). As explained in ISA (NZ) 200, inherent risk is higher for some assertions and related classes of transactions, account balances and disclosures than for others. The degree to which inherent risk varies is referred to in this ISA (NZ) as the ‘spectrum of inherent risk.’

6. Risks of material misstatement identified and assessed by the auditor include both those due to error and those due to fraud. Although both are addressed by this ISA (NZ), the significance of fraud is such that further requirements and guidance are included in ISA (NZ) 240<sup>7</sup> in relation to risk assessment procedures and related activities to obtain information that is used to identify, assess and respond to the risks of material misstatement due to fraud.
7. The auditor’s risk identification and assessment process is iterative and dynamic. The auditor’s understanding of the entity and its environment, the applicable financial reporting framework, and the entity’s system of internal control are interdependent with concepts within the requirements to identify and assess the risks of material misstatement. In obtaining the understanding required by this ISA (NZ), initial expectations of risks may be developed, which may be further refined as the auditor progresses through the risk identification and assessment process. In addition, this ISA (NZ) and ISA (NZ) 330 require the auditor to revise the risk assessments, and modify further overall responses and further audit procedures, based on audit evidence obtained from performing further audit procedures in accordance with ISA (NZ) 330, or if new information is obtained.
8. ISA (NZ) 330 requires the auditor to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.<sup>8</sup> ISA (NZ) 330 further explains that the auditor’s assessment of the risks of material misstatement at the financial statement level, and the auditor’s overall responses, is affected by the auditor’s understanding of the control environment. ISA (NZ) 330 also requires the auditor to design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level.<sup>9</sup>

#### Scalability

9. ISA (NZ) 200 states that some ISAs (NZ) include scalability considerations which illustrate the application of the requirements to all entities regardless of whether their nature and circumstances are less complex or more complex.<sup>10</sup> This ISA (NZ) is intended for audits of all entities, regardless of size or complexity and the application material therefore incorporates specific considerations specific to both less and more complex entities, where appropriate. While the size of an entity may be an indicator of its complexity, some smaller entities may be complex and some larger entities may be less complex.

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<sup>7</sup> ISA (NZ) 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*

<sup>8</sup> ISA (NZ) 330, paragraph 5

<sup>9</sup> ISA (NZ) 330, paragraph 6

<sup>10</sup> ISA (NZ) 200, paragraph A65a

## Effective Date

10. This ISA (NZ) is effective for audits of financial statements for periods beginning on or after 15 December 2021.

## Objective

11. The objective of the auditor is to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement.

## Definitions

12. For purposes of the ISAs (NZ), the following terms have the meanings attributed below:
  - (a) *Assertions* – Representations, explicit or otherwise, with respect to the recognition, measurement, presentation and disclosure of information in the financial statements which are inherent in management representing that the financial statements are prepared in accordance with the applicable financial reporting framework. Assertions are used by the auditor to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement. (Ref: Para. A1)
  - (b) *Business risk* – A risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity’s ability to achieve its objectives and execute its strategies, or from the setting of inappropriate objectives and strategies.
  - (c) *Controls* – Policies or procedures that an entity establishes to achieve the control objectives of management or those charged with governance. In this context: (Ref: Para. A2–A5)
    - (i) Policies are statements of what should, or should not, be done within the entity to effect control. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions.
    - (ii) Procedures are actions to implement policies.
  - (d) *General information technology (IT) controls* – Controls over the entity’s IT processes that support the continued proper operation of the IT environment, including the continued effective functioning of information processing controls and the integrity of information (i.e., the completeness, accuracy and validity of information) in the entity’s information system. Also see the definition of IT environment.
  - (e) *Information processing controls* – Controls relating to the processing of information in IT applications or manual information processes in the entity’s information system that directly address risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information). (Ref: Para. A6)

- (f) *Inherent risk factors* – Characteristics of events or conditions that affect susceptibility to misstatement, whether due to fraud or error, 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 other fraud risk factors<sup>11</sup> insofar as they affect inherent risk. (Ref: Para. A7–A8)
- (g) *IT environment* – The IT applications and supporting IT infrastructure, as well as the IT processes and personnel involved in those processes, that an entity uses to support business operations and achieve business strategies. For the purposes of this ISA (NZ):
  - (iii) An IT application is a program or a set of programs that is used in the initiation, processing, recording and reporting of transactions or information. IT applications include data warehouses and report writers.
  - (iv) The IT infrastructure comprises the network, operating systems, and databases and their related hardware and software.
  - (v) The IT processes are the entity's processes to manage access to the IT environment, manage program changes or changes to the IT environment and manage IT operations.
- (h) *Relevant assertions* – An assertion about a class of transactions, account balance or disclosure is relevant when it has an identified risk of material misstatement. The determination of whether an assertion is a relevant assertion is made before consideration of any related controls (i.e., the inherent risk). (Ref: Para. A9)
- (i) *Risks arising from the use of IT* – Susceptibility of information processing controls to ineffective design or operation, or risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information) in the entity's information system, due to ineffective design or operation of controls in the entity's IT processes (see IT environment).
- (j) *Risk assessment procedures* – The audit procedures designed and performed to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.
- (k) *Significant class of transactions, account balance or disclosure* – A class of transactions, account balance or disclosure for which there is one or more relevant assertions.
- (l) *Significant risk* – An identified risk of material misstatement: (Ref: Para. A10)
  - (i) 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 inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur; or

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<sup>11</sup> ISA (NZ) 240, paragraphs A24–A27

- (ii) That is to be treated as a significant risk in accordance with the requirements of other ISAs (NZ).<sup>12</sup>
- (m) *System of internal control* – The system designed, implemented and maintained by those charged with governance, management and other personnel, to provide reasonable assurance about the achievement of an entity’s objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. For the purposes of the ISAs (NZ), the system of internal control consists of five inter-related components:
  - (i) Control environment;
  - (ii) The entity’s risk assessment process;
  - (iii) The entity’s process to monitor the system of internal control;
  - (iv) The information system and communication; and
  - (v) Control activities.

## Requirements

### Risk Assessment Procedures and Related Activities

13. The auditor shall design and perform risk assessment procedures to obtain audit evidence that provides an appropriate basis for: (Ref: Para. A11–A18)
  - (a) The identification and assessment of risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels; and
  - (b) The design of further audit procedures in accordance with ISA (NZ) 330.

The auditor shall design and perform risk assessment 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. A14)
14. The risk assessment procedures shall include the following: (Ref: Para. A19–A21)
  - (a) Enquiries of management and of other appropriate individuals within the entity, including individuals within the internal audit function (if the function exists). (Ref: Para. A22–A26)
  - (b) Analytical procedures. (Ref: Para. A27–A31)
  - (c) Observation and inspection. (Ref: Para. A32–A36)

### Information from Other Sources

15. In obtaining audit evidence in accordance with paragraph 13, the auditor shall consider information from: (Ref: Para. A37–A38)
  - (a) The auditor’s procedures regarding acceptance or continuance of the client relationship or the audit engagement; and

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<sup>12</sup> ISA (NZ) 240, paragraph 27 and ISA (NZ) 550, *Related Parties*, paragraph 18

- (b) When applicable, other engagements performed by the engagement partner for the entity.
- 16. When the auditor intends to use information obtained from the auditor's previous experience with the entity and from audit procedures performed in previous audits, the auditor shall evaluate whether such information remains relevant and reliable as audit evidence for the current audit. (Ref: Para. A39–A41)

*Engagement Team Discussion*

- 17. The engagement partner and other key engagement team members shall discuss the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement. (Ref: Para. A42–A47)
- 18. When there are engagement team members not involved in the engagement team discussion, the engagement partner shall determine which matters are to be communicated to those members.

**Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework and the Entity's System of Internal Control** (Ref: Para. A48–A49)

*Understanding the Entity and Its Environment, and the Applicable Financial Reporting Framework* (Ref: Para. A50–A55)

- 19. The auditor shall perform risk assessment procedures to obtain an understanding of:
  - (a) The following aspects of the entity and its environment:
    - (i) The entity's organisational structure, ownership and governance, and its business model, including the extent to which the business model integrates the use of IT; (Ref: Para. A56–A67)
    - (ii) Industry, regulatory and other external factors; (Ref: Para. A68–A73) and
    - (iii) The measures used, internally and externally, to assess the entity's financial performance; (Ref: Para. A74–A81)
  - (b) The applicable financial reporting framework, and the entity's accounting policies and the reasons for any changes thereto; (Ref: Para. A82–A84) and
  - (c) How inherent risk factors affect susceptibility of assertions to misstatement and the degree to which they do so, in the preparation of the financial statements in accordance with the applicable financial reporting framework, based on the understanding obtained in (a) and (b). (Ref: Para. A85–A89)
- 20. The auditor shall evaluate whether the entity's accounting policies are appropriate and consistent with the applicable financial reporting framework.



*Understanding the Components of the Entity's System of Internal Control* (Ref: Para. A90 – A95)

Control Environment, the Entity's Risk Assessment Process and the Entity's Process to Monitor the System of Internal Control (Ref: Para. A96–A98)

Control environment

|   |   |
|---|---|
| <p>21. The auditor shall obtain an understanding of the control environment relevant to the preparation of the financial statements, through performing risk assessment procedures, by: (Ref: Para. A99–A100)</p>   |   |
| <p>(a) Understanding the set of controls, processes and structures that address: (Ref: Para. A101–A102)</p> <ul style="list-style-type: none"> <li>(i) How management's oversight responsibilities are carried out, such as the entity's culture and management's commitment to integrity and ethical values;</li> <li>(ii) When those charged with governance are separate from management, the independence of, and oversight over the entity's system of internal control by, those charged with governance;</li> <li>(iii) The entity's assignment of authority and responsibility;</li> <li>(iv) How the entity attracts, develops, and retains competent individuals; and</li> <li>(v) How the entity holds individuals accountable for their responsibilities in the pursuit of the objectives of the system of internal control;</li> </ul> | <p>and</p> <p>(b) Evaluating whether: (Ref: Para. A103–A108)</p> <ul style="list-style-type: none"> <li>(i) Management, with the oversight of those charged with governance, has created and maintained a culture of honesty and ethical behaviour;</li> <li>(ii) The control environment provides an appropriate foundation for the other components of the entity's system of internal control considering the nature and complexity of the entity; and</li> <li>(iii) Control deficiencies identified in the control environment undermine the other components of the entity's system of internal control.</li> </ul> |

The entity's risk assessment process

|   |  |
|---|--|
| <p>22. The auditor shall obtain an understanding of the entity's risk assessment process relevant to the preparation of the financial statements, through performing risk assessment procedures, by:</p>  |  |
| <p>(a) Understanding the entity's process for: (Ref: Para. A109–A110)</p> <ul style="list-style-type: none"> <li>(i) Identifying business risks relevant to financial reporting objectives; (Ref: Para. A62)</li> <li>(ii) Assessing the significance of those risks, including the likelihood of their occurrence; and</li> <li>(iii) Addressing those risks;</li> </ul> | <p>and</p> <p>(b) Evaluating whether the entity's risk assessment process is appropriate to the entity's circumstances considering the nature and complexity of the entity. (Ref: Para. A111–A113)</p> |

23. If the auditor identifies risks of material misstatement that management failed to identify, the auditor shall:
- (a) Determine whether any such risks are of a kind that the auditor expects would have been identified by the entity's risk assessment process and, if so, obtain an understanding of why the entity's risk assessment process failed to identify such risks of material misstatement; and
  - (b) Consider the implications for the auditor's evaluation in paragraph 22(b).

The entity's process to monitor the system of internal control

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| 24. The auditor shall obtain an understanding of the entity's process for monitoring the system of internal control relevant to the preparation of the financial statements, through performing risk assessment procedures, by: (Ref: Para. A114–A115)   |  |
| <p>(a) Understanding those aspects of the entity's process that address:</p> <ul style="list-style-type: none"> <li>(i) Ongoing and separate evaluations for monitoring the effectiveness of controls, and the identification and remediation of control deficiencies identified; (Ref: Para. A116–A117) and</li> <li>(ii) The entity's internal audit function, if any, including its nature, responsibilities and activities; (Ref: Para. A118)</li> </ul> <p>(b) Understanding the sources of the information used in the entity's process to monitor the system of internal control, and the basis upon which management considers the information to be sufficiently reliable for the purpose; (Ref: Para. A119–A120)</p> | <p>and</p> <p>(c) Evaluating whether the entity's process for monitoring the system of internal control is appropriate to the entity's circumstances considering the nature and complexity of the entity. (Ref: Para. A121–A122)</p> |

Information System and Communication, and Control Activities (Ref: Para. A123–A130)

The information system and communication

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| 25. The auditor shall obtain an understanding of the entity's information system and communication relevant to the preparation of the financial statements, through performing risk assessment procedures, by: (Ref: Para. A131)   |   |
| <p>(a) Understanding the entity's information processing activities, including its data and information, the resources to be used in such activities and the policies that define, for significant classes of transactions, account balances and disclosures: (Ref: Para. A132–A143)</p> | <p>and</p> <p>(c) Evaluating whether the entity's information system and communication appropriately support the preparation of the entity's financial statements in accordance with the applicable</p> |

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| <p>(i) How information flows through the entity's information system, including how:</p> <ul style="list-style-type: none"> <li>a. Transactions are initiated, and how information about them is recorded, processed, corrected as necessary, incorporated in the general ledger and reported in the financial statements; and</li> <li>b. Information about events and conditions, other than transactions, is captured, processed and disclosed in the financial statements;</li> </ul> <p>(ii) The accounting records, specific accounts in the financial statements and other supporting records relating to the flows of information in the information system;</p> <p>(iii) The financial reporting process used to prepare the entity's financial statements, including disclosures; and</p> <p>(iv) The entity's resources, including the IT environment, relevant to (a)(i) to (a)(iii) above;</p> <p>(b) Understanding how the entity communicates significant matters that support the preparation of the financial statements and related reporting responsibilities in the information system and other components of the system of internal control: (Ref: Para. A144–A145)</p> <ul style="list-style-type: none"> <li>(i) Between people within the entity, including how financial reporting roles and responsibilities are communicated;</li> <li>(ii) Between management and those charged with governance; and</li> <li>(iii) With external parties, such as those with regulatory authorities;</li> </ul> | <p>financial reporting framework. (Ref: Para. A146)</p> |
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## Control activities

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| <p>26. The auditor shall obtain an understanding of the control activities component, through performing risk assessment procedures, by: (Ref: Para. A147–A157)</p>   |   |
| <p>(a) Identifying controls that address risks of material misstatement at the assertion level in the control activities component as follows:</p> <ul style="list-style-type: none"> <li>(i) Controls that address a risk that is determined to be a significant risk; (Ref: Para. A158–A159)</li> <li>(ii) Controls over journal entries, including non-standard journal entries used to record non-</li> </ul> | <p>and</p> <ul style="list-style-type: none"> <li>(d) For each control identified in (a) or (c)(ii): (Ref: Para. A175–A181)</li> <li>(i) Evaluating whether the control is designed effectively to address the</li> </ul> |

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| <p>recurring, unusual transactions or adjustments; (Ref: Para. A160–A161)</p> <p>(iii) Controls for which the auditor plans to test operating effectiveness in determining the nature, timing and extent of substantive testing, which shall include controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence; and (Ref: Para. A162–A164)</p> <p>(iv) Other controls that the auditor considers are appropriate to enable the auditor to meet the objectives of paragraph 13 with respect to risks at the assertion level, based on the auditor's professional judgement; (Ref: Para. A165)</p> <p>(b) Based on controls identified in (a), identifying the IT applications and the other aspects of the entity's IT environment that are subject to risks arising from the use of IT; (Ref: Para. A166–A172)</p> <p>(c) For such IT applications and other aspects of the IT environment identified in (b), identifying: (Ref: Para. A173–A174)</p> <p>(i) The related risks arising from the use of IT; and</p> <p>(ii) The entity's general IT controls that address such risks;</p> | <p>risk of material misstatement at the assertion level, or effectively designed to support the operation of other controls; and</p> <p>(ii) Determining whether the control has been implemented by performing procedures in addition to enquiry of the entity's personnel.</p> |
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### *Control Deficiencies Within the Entity's System of Internal Control*

27. Based on the auditor's evaluation of each of the components of the entity's system of internal control, the auditor shall determine whether one or more control deficiencies have been identified. (Ref: Para. A182–A183)

### **Identifying and Assessing the Risks of Material Misstatement** (Ref: Para. A184–A185)

#### *Identifying Risks of Material Misstatement*

28. The auditor shall identify the risks of material misstatement and determine whether they exist at: (Ref: Para. A186–A192)
- (a) The financial statement level; (Ref: Para. A193–A200) or
  - (b) The assertion level for classes of transactions, account balances and disclosures. (Ref: Para. A201)
29. The auditor shall determine the relevant assertions and the related significant classes of transactions, account balances and disclosures. (Ref: Para. A202–A204)

*Assessing Risks of Material Misstatement at the Financial Statement Level*

30. For identified risks of material misstatement at the financial statement level, the auditor shall assess the risks and: (Ref: Para. A193–A200)
- (a) Determine whether such risks affect the assessment of risks at the assertion level; and
  - (b) Evaluate the nature and extent of their pervasive effect on the financial statements.

*Assessing Risks of Material Misstatement at the Assertion Level**Assessing Inherent Risk (Ref: Para. A205–A217)*

31. For identified risks of material misstatement at the assertion level, the auditor shall assess inherent risk by assessing the likelihood and magnitude of misstatement. In doing so, the auditor shall take into account how, and the degree to which:
- (a) Inherent risk factors affect the susceptibility of relevant assertions to misstatement; and
  - (b) The risks of material misstatement at the financial statement level affect the assessment of inherent risk for risks of material misstatement at the assertion level. (Ref: Para. A215–A216)
32. The auditor shall determine whether any of the assessed risks of material misstatement are significant risks. (Ref: Para. A218–A221)
33. The auditor shall determine whether substantive procedures alone cannot provide sufficient appropriate audit evidence for any of the risks of material misstatement at the assertion level. (Ref: Para. A222–A225)

*Assessing Control Risk*

34. If the auditor plans to test the operating effectiveness of controls, the auditor shall assess control risk. If the auditor does not plan to test the operating effectiveness of controls, the auditor's assessment of control risk shall be such that the assessment of the risk of material misstatement is the same as the assessment of inherent risk. (Ref: Para. A226–A229)

*Evaluating the Audit Evidence Obtained from the Risk Assessment Procedures*

35. The auditor shall evaluate whether the audit evidence obtained from the risk assessment procedures provides an appropriate basis for the identification and assessment of the risks of material misstatement. If not, the auditor shall perform additional risk assessment procedures until audit evidence has been obtained to provide such a basis. In identifying and assessing the risks of material misstatement, the auditor shall take into account all audit evidence obtained from the risk assessment procedures, whether corroborative or contradictory to assertions made by management. (Ref: Para. A230–A232)

*Classes of Transactions, Account Balances and Disclosures that Are Not Significant, but Which Are Material*

36. For material classes of transactions, account balances or disclosures that have not been determined to be significant classes of transactions, account balances or disclosures, the

auditor shall evaluate whether the auditor's determination remains appropriate. (Ref: Para. A233–A235)

### *Revision of Risk Assessment*

37. If the auditor obtains new information which is inconsistent with the audit evidence on which the auditor originally based the identification or assessments of the risks of material misstatement, the auditor shall revise the identification or assessment. (Ref: Para. A236)

### **Documentation**

38. The auditor shall include in the audit documentation:<sup>13</sup> (Ref: Para. A237–A241)
- (a) The discussion among the engagement team and the significant decisions reached;
  - (b) Key elements of the auditor's understanding in accordance with paragraphs 19, 21, 22, 24 and 25; the sources of information from which the auditor's understanding was obtained; and the risk assessment procedures performed;
  - (c) The evaluation of the design of identified controls, and determination whether such controls have been implemented, in accordance with the requirements in paragraph 26; and
  - (d) The identified and assessed risks of material misstatement at the financial statement level and at the assertion level, including significant risks and risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence, and the rationale for the significant judgements made.

### **Application and Other Explanatory Material**

#### **Definitions** (Ref: Para. 12)

#### *Assertions* (Ref: Para. 12(a))

- A1. Categories of assertions are used by auditors to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement. Examples of these categories of assertions are described in paragraph A190. The assertions differ from the written representations required by ISA (NZ) 580,<sup>14</sup> to confirm certain matters or support other audit evidence.

#### *Controls* (Ref: Para. 12(c))

- A2. Controls are embedded within the components of the entity's system of internal control.
- A3. Policies are implemented through the actions of personnel within the entity, or through the restraint of personnel from taking actions that would conflict with such policies.
- A4. Procedures may be mandated, through formal documentation or other communication by management or those charged with governance, or may result from behaviours that are not mandated but are rather conditioned by the entity's culture. Procedures may be

<sup>13</sup> ISA (NZ) 230, *Audit Documentation*, paragraphs 8–11, and A6–A7

<sup>14</sup> ISA (NZ) 580, *Written Representations*

enforced through the actions permitted by the IT applications used by the entity or other aspects of the entity's IT environment.

- A5. Controls may be direct or indirect. Direct controls are controls that are precise enough to address risks of material misstatement at the assertion level. Indirect controls are controls that support direct controls.

*Information Processing Controls* (Ref: Para. 12(e))

- A6. Risks to the integrity of information arise from susceptibility to ineffective implementation of the entity's information policies, which are policies that define the information flows, records and reporting processes in the entity's information system. Information processing controls are procedures that support effective implementation of the entity's information policies. Information processing controls may be automated (i.e., embedded in IT applications) or manual (e.g., input or output controls) and may rely on other controls, including other information processing controls or general IT controls.

*Inherent Risk Factors* (Ref: Para. 12(f))

**Appendix 2** sets out further considerations relating to understanding inherent risk factors.

- A7. Inherent risk factors may be qualitative or quantitative and affect the susceptibility of assertions to misstatement. Qualitative inherent risk factors relating to the preparation of information required by the applicable financial reporting framework include:
- Complexity;
  - Subjectivity;
  - Change;
  - Uncertainty; or
  - Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk.
- A8. Other inherent risk factors, that affect susceptibility to misstatement of an assertion about a class of transactions, account balance or disclosure may include:
- The quantitative or qualitative significance of the class of transactions, account balance or disclosure; or
  - The volume or a lack of uniformity in the composition of the items to be processed through the class of transactions or account balance, or to be reflected in the disclosure.

*Relevant Assertions* (Ref: Para. 12(h))

- A9. A risk of material misstatement may relate to more than one assertion, in which case all the assertions to which such a risk relates are relevant assertions. If an assertion does not have an identified risk of material misstatement, then it is not a relevant assertion.

*Significant Risk* (Ref: Para. 12(1))

- A10. Significance can be described as the relative importance of a matter, and is judged by the auditor in the context in which the matter is being considered. For inherent risk, significance may be considered in the context of how, and the degree to which, inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur.

**Risk Assessment Procedures and Related Activities** (Ref: Para. 13–18)

- A11. The risks of material misstatement to be identified and assessed include both those due to fraud and those due to error, and both are covered by this ISA (NZ). However, the significance of fraud is such that further requirements and guidance are included in ISA (NZ) 240 in relation to risk assessment procedures and related activities to obtain information that is used to identify and assess the risks of material misstatement due to fraud.<sup>15</sup> In addition, the following ISAs (NZ) provide further requirements and guidance on identifying and assessing risks of material misstatement regarding specific matters or circumstances:

- ISA (NZ) 540 (Revised)<sup>16</sup> in regard to accounting estimates;
- ISA (NZ) 550<sup>22</sup> in regard to related party relationships and transactions;
- ISA (NZ) 570 (Revised)<sup>17</sup> in regard to going concern; and
- ISA (NZ) 600<sup>18</sup> in regard to group financial statements.

- A12. Professional scepticism is necessary for the critical assessment of audit evidence gathered when performing the risk assessment procedures, and assists the auditor in remaining alert to audit evidence that is not biased towards corroborating the existence of risks or that may be contradictory to the existence of risks. Professional scepticism is an attitude that is applied by the auditor when making professional judgements that then provides the basis for the auditor's actions. The auditor applies professional judgement in determining when the auditor has audit evidence that provides an appropriate basis for risk assessment.

- A13. The application of professional scepticism by the auditor may include:

- Questioning contradictory information and the reliability of documents;
- Considering responses to enquiries and other information obtained from management and those charged with governance;
- Being alert to conditions that may indicate possible misstatement due to fraud or error; and

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<sup>15</sup> ISA (NZ) 240, paragraphs 12–27

<sup>16</sup> ISA (NZ) 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

<sup>17</sup> ISA (NZ) 570 (Revised), *Going Concern*

<sup>18</sup> ISA (NZ) 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*



- Considering whether audit evidence obtained supports the auditor's identification and assessment of the risks of material misstatement in light of the entity's nature and circumstances.

*Why Obtaining Audit Evidence in an Unbiased Manner Is Important* (Ref: Para. 13)

A14. Designing and performing risk assessment procedures to obtain audit evidence to support the identification and assessment of the risks of material misstatement in an unbiased manner may assist the auditor in identifying potentially contradictory information, which may assist the auditor in exercising professional scepticism in identifying and assessing the risks of material misstatement.

*Sources of Audit Evidence* (Ref: Para. 13)

A15. Designing and performing risk assessment procedures to obtain audit evidence in an unbiased manner may involve obtaining evidence from multiple sources within and outside the entity. However, the auditor is not required to perform an exhaustive search to identify all possible sources of audit evidence. In addition to information from other sources<sup>19</sup>, sources of information for risk assessment procedures may include:

- Interactions with management, those charged with governance, and other key entity personnel, such as internal auditors.
- Certain external parties such as regulators, whether obtained directly or indirectly.
- Publicly available information about the entity, for example entity-issued press releases, materials for analysts or investor group meetings, analysts' reports or information about trading activity.

Regardless of the source of information, the auditor considers the relevance and reliability of the information to be used as audit evidence in accordance with ISA (NZ) 500.<sup>20</sup>

*Scalability* (Ref: Para. 13)

A16. The nature and extent of risk assessment procedures will vary based on the nature and circumstances of the entity (e.g., the formality of the entity's policies and procedures, and processes and systems). The auditor uses professional judgement to determine the nature and extent of the risk assessment procedures to be performed to meet the requirements of this ISA (NZ).

A17. Although the extent to which an entity's policies and procedures, and processes and systems are formalized may vary, the auditor is still required to obtain the understanding in accordance with paragraphs 19, 21, 22, 24, 25 and 26.

**Examples:**

Some entities, including less complex entities, and particularly owner-managed entities, may not have established structured processes and systems (e.g., a risk assessment process or a process to monitor the system of internal control) or may have

<sup>19</sup> See paragraph A37 and A38.

<sup>20</sup> ISA (NZ) 500, *Audit Evidence*, paragraph 7

established processes or systems with limited documentation or a lack of consistency in how they are undertaken. When such systems and processes lack formality, the auditor may still be able to perform risk assessment procedures through observation and enquiry.

Other entities, typically more complex entities, are expected to have more formalized and documented policies and procedures. The auditor may use such documentation in performing risk assessment procedures.

- A18. The nature and extent of risk assessment procedures to be performed the first time an engagement is undertaken may be more extensive than procedures for a recurring engagement. In subsequent periods, the auditor may focus on changes that have occurred since the preceding period.

*Types of Risk Assessment Procedures (Ref: Para. 14)*

- A19. ISA (NZ) 500<sup>21</sup> explains the types of audit procedures that may be performed in obtaining audit evidence from risk assessment procedures and further audit procedures. The nature, timing and extent of the audit procedures may be affected by the fact that some of the accounting data and other evidence may only be available in electronic form or only at certain points in time.<sup>22</sup> The auditor may perform substantive procedures or tests of controls, in accordance with ISA (NZ) 330, concurrently with risk assessment procedures, when it is efficient to do so. Audit evidence obtained that supports the identification and assessment of risks of material misstatement may also support the detection of misstatements at the assertion level or the evaluation of the operating effectiveness of controls.
- A20. Although the auditor is required to perform all the risk assessment procedures described in paragraph 14 in the course of obtaining the required understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control (see paragraphs 19–26), the auditor is not required to perform all of them for each aspect of that understanding. Other procedures may be performed when the information to be obtained may be helpful in identifying risks of material misstatement. Examples of such procedures may include making enquiries of the entity's external legal counsel or external supervisors, or of valuation experts that the entity has used.

*Automated Tools and Techniques (Ref: Para. 14)*

- A21. Using automated tools and techniques, the auditor may perform risk assessment procedures on large volumes of data (from the general ledger, sub-ledgers or other operational data) including for analysis, recalculations, reperformance or reconciliations.

<sup>21</sup> ISA (NZ) 500, paragraphs A14–A17 and A21–A25

<sup>22</sup> ISA (NZ) 500, paragraph A12

*Enquiries of Management and Others within the Entity* (Ref: Para. 14(a))

## Why Enquiries Are Made of Management and Others Within the Entity

- A22. Information obtained by the auditor to support an appropriate basis for the identification and assessment of risks, and the design of further audit procedures, may be obtained through enquiries of management and those responsible for financial reporting.
- A23. Enquiries of management and those responsible for financial reporting and of other appropriate individuals within the entity and other employees with different levels of authority may offer the auditor varying perspectives when identifying and assessing risks of material misstatement.

**Examples:**

- Enquiries directed towards those charged with governance may help the auditor understand the extent of oversight by those charged with governance over the preparation of the financial statements by management. ISA (NZ) 260 (Revised)<sup>23</sup> identifies the importance of effective two-way communication in assisting the auditor to obtain information from those charged with governance in this regard.
- Enquiries of employees responsible for initiating, processing or recording complex or unusual transactions may help the auditor to evaluate the appropriateness of the selection and application of certain accounting policies.
- Enquiries directed towards in-house legal counsel may provide information about such matters as litigation, compliance with laws and regulations, knowledge of fraud or suspected fraud affecting the entity, warranties, post-sales obligations, arrangements (such as joint ventures) with business partners, and the meaning of contractual terms.
- Enquiries directed towards marketing or sales personnel may provide information about changes in the entity's marketing strategies, sales trends, or contractual arrangements with its customers.
- Enquiries directed towards the risk management function (or enquiries of those performing such roles) may provide information about operational and regulatory risks that may affect financial reporting.
- Enquiries directed towards IT personnel may provide information about system changes, system or control failures, or other IT-related risks.

## Considerations Specific to Public Sector Entities

- A24. When making enquiries of those who may have information that is likely to assist in identifying risks of material misstatement, auditors of public sector entities may obtain information from additional sources such as from the auditors that are involved in performance or other audits related to the entity.

<sup>23</sup> ISA (NZ) 260 (Revised), *Communication with Those Charged with Governance*, paragraph 4(b)

## Enquiries of the Internal Audit Function

**Appendix 4** sets out considerations for understanding an entity's internal audit function.

Why enquiries are made of the internal audit function (if the function exists)

- A25. If an entity has an internal audit function, enquiries of the appropriate individuals within the function may assist the auditor in understanding the entity and its environment, and the entity's system of internal control, in the identification and assessment of risks.

Considerations specific to public sector entities

- A26. Auditors of public sector entities often have additional responsibilities with regard to internal control and compliance with applicable laws and regulations. Enquiries of appropriate individuals in the internal audit function may assist the auditors in identifying the risk of material non-compliance with applicable laws and regulations, and the risk of control deficiencies related to financial reporting.

*Analytical Procedures* (Ref: Para. 14(b))

Why Analytical Procedures Are Performed as a Risk Assessment Procedure

- A27. Analytical procedures help identify inconsistencies, unusual transactions or events, and amounts, ratios, and trends that indicate matters that may have audit implications. Unusual or unexpected relationships that are identified may assist the auditor in identifying risks of material misstatement, especially risks of material misstatement due to fraud.
- A28. Analytical procedures performed as risk assessment procedures may therefore assist in identifying and assessing the risks of material misstatement by identifying aspects of the entity of which the auditor was unaware or understanding how inherent risk factors, such as change, affect susceptibility of assertions to misstatement.

Types of Analytical Procedures

- A29. Analytical procedures performed as risk assessment procedures may:
- Include both financial and non-financial information, for example, the relationship between sales and square footage of selling space or volume of goods sold (non-financial).
  - Use data aggregated at a high level. Accordingly, the results of those analytical procedures may provide a broad initial indication about the likelihood of a material misstatement.

**Example:**

In the audit of many entities, including those with less complex business models and processes, and a less complex information system, the auditor may perform a simple comparison of information, such as the change in interim or monthly account balances from balances in prior periods, to obtain an indication of potentially higher risk areas.

A30. This ISA (NZ) deals with the auditor's use of analytical procedures as risk assessment procedures. ISA (NZ) 520<sup>24</sup> deals with the auditor's use of analytical procedures as substantive procedures ("substantive analytical procedures") and the auditor's responsibility to perform analytical procedures near the end of the audit. Accordingly, analytical procedures performed as risk assessment procedures are not required to be performed in accordance with the requirements of ISA (NZ) 520. However, the requirements and application material in ISA (NZ) 520 may provide useful guidance to the auditor when performing analytical procedures as part of the risk assessment procedures.

#### Automated tools and techniques

A31. Analytical procedures can be performed using a number of tools or techniques, which may be automated. Applying automated analytical procedures to the data may be referred to as data analytics.

**Example:**

The auditor may use a spreadsheet to perform a comparison of actual recorded amounts to budgeted amounts, or may perform a more advanced procedure by extracting data from the entity's information system, and further analysing this data using visualisation techniques to identify classes of transactions, account balances or disclosures for which further specific risk assessment procedures may be warranted.

#### *Observation and Inspection* (Ref: Para. 14(c))

#### Why Observation and Inspection Are Performed as Risk Assessment Procedures

A32. Observation and inspection may support, corroborate or contradict enquiries of management and others, and may also provide information about the entity and its environment.

#### Scalability

A33. Where policies or procedures are not documented, or the entity has less formalised controls, the auditor may still be able to obtain some audit evidence to support the identification and assessment of the risks of material misstatement through observation or inspection of the performance of the control.

**Examples:**

- The auditor may obtain an understanding of controls over an inventory count, even if they have not been documented by the entity, through direct observation.
- The auditor may be able to observe segregation of duties.
- The auditor may be able to observe passwords being entered.

<sup>24</sup> ISA (NZ) 520, *Analytical Procedures*

## Observation and Inspection as Risk Assessment Procedures

A34. Risk assessment procedures may include observation or inspection of the following:

- The entity's operations.
- Internal documents (such as business plans and strategies), records, and internal control manuals.
- Reports prepared by management (such as quarterly management reports and interim financial statements) and those charged with governance (such as minutes of board of directors' meetings).
- The entity's premises and plant facilities.
- Information obtained from external sources such as trade and economic journals; reports by analysts, banks, or rating agencies; regulatory or financial publications; or other external documents about the entity's financial performance (such as those referred to in paragraph A79).
- The behaviours and actions of management or those charged with governance (such as the observation of an audit committee meeting).

## Automated tools and techniques

A35. Automated tools or techniques may also be used to observe or inspect, in particular assets, for example through the use of remote observation tools (e.g., a drone).

## Considerations Specific to Public Sector Entities

A36. Risk assessment procedures performed by auditors of public sector entities may also include observation and inspection of documents prepared by management for the legislature, for example documents related to mandatory performance reporting.

## *Information from Other Sources* (Ref: Para. 15)

### Why the Auditor Considers Information from Other Sources

A37. Information obtained from other sources may be relevant to the identification and assessment of the risks of material misstatement by providing information and insights about:

- The nature of the entity and its business risks, and what may have changed from previous periods.
- The integrity and ethical values of management and those charged with governance, which may also be relevant to the auditor's understanding of the control environment.
- The applicable financial reporting framework and its application to the nature and circumstances of the entity.

### Other Relevant Sources

A38. Other relevant sources of information include:

- The auditor's procedures regarding acceptance or continuance of the client relationship or the audit engagement in accordance with ISA (NZ) 220, including the conclusions reached thereon.<sup>25</sup>
- Other engagements performed for the entity by the engagement partner. The engagement partner may have obtained knowledge relevant to the audit, including about the entity and its environment, when performing other engagements for the entity. Such engagements may include agreed-upon procedures engagements or other audit or assurance engagements, including engagements to address incremental reporting requirements in the jurisdiction.

Information from the Auditor's Previous Experience with the Entity and Previous Audits (Ref: Para. 16)

Why information from previous audits is important to the current audit

A39. The auditor's previous experience with the entity and from audit procedures performed in previous audits may provide the auditor with information that is relevant to the auditor's determination of the nature and extent of risk assessment procedures, and the identification and assessment of risks of material misstatement.

Nature of the Information from Previous Audits

A40. The auditor's previous experience with the entity and audit procedures performed in previous audits may provide the auditor with information about such matters as:

- Past misstatements and whether they were corrected on a timely basis.
- The nature of the entity and its environment, and the entity's system of internal control (including control deficiencies).
- Significant changes that the entity or its operations may have undergone since the prior financial period.
- Those particular types of transactions and other events or account balances (and related disclosures) where the auditor experienced difficulty in performing the necessary audit procedures, for example, due to their complexity.

A41. The auditor is required to determine whether information obtained from the auditor's previous experience with the entity and from audit procedures performed in previous audits remains relevant and reliable, if the auditor intends to use that information for the purposes of the current audit. If the nature or circumstances of the entity have changed, or new information has been obtained, the information from prior periods may no longer be relevant or reliable for the current audit. To determine whether changes have occurred that may affect the relevance or reliability of such information, the auditor may make enquiries and perform other appropriate audit procedures, such as walk-throughs of relevant systems. If the information is not reliable, the auditor may consider performing additional procedures that are appropriate in the circumstances.

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<sup>25</sup> ISA (NZ) 220, *Quality Control for an Audit of Financial Statements*, paragraph 12

*Engagement Team Discussion* (Ref: Para. 17–18)

## Why the Engagement Team Is Required to Discuss the Application of the Applicable Financial Reporting Framework and the Susceptibility of the Entity's Financial Statements to Material Misstatement

A42. The discussion among the engagement team about the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement:

- Provides an opportunity for more experienced engagement team members, including the engagement partner, to share their insights based on their knowledge of the entity. Sharing information contributes to an enhanced understanding by all engagement team members.
- Allows the engagement team members to exchange information about the business risks to which the entity is subject, how inherent risk factors may affect the susceptibility to misstatement of classes of transactions, account balances and disclosures, and about how and where the financial statements might be susceptible to material misstatement due to fraud or error.
- Assists the engagement team members to gain a better understanding of the potential for material misstatement of the financial statements in the specific areas assigned to them, and to understand how the results of the audit procedures that they perform may affect other aspects of the audit, including the decisions about the nature, timing and extent of further audit procedures. In particular, the discussion assists engagement team members in further considering contradictory information based on each member's own understanding of the nature and circumstances of the entity.
- Provides a basis upon which engagement team members communicate and share new information obtained throughout the audit that may affect the assessment of risks of material misstatement or the audit procedures performed to address these risks.

ISA (NZ) 240 requires the engagement team discussion to place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud may occur.<sup>26</sup>

A43. Professional scepticism is necessary for the critical assessment of audit evidence, and a robust and open engagement team discussion, including for recurring audits, may lead to improved identification and assessment of the risks of material misstatement. Another outcome from the discussion may be that the auditor identifies specific areas of the audit for which exercising professional scepticism may be particularly important, and may lead to the involvement of more experienced members of the engagement team who are appropriately skilled to be involved in the performance of audit procedures related to those areas.

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<sup>26</sup> ISA (NZ) 240, paragraph 16



## Scalability

- A44. When the engagement is carried out by a single individual, such as a sole practitioner (i.e., where an engagement team discussion would not be possible), consideration of the matters referred to in paragraphs A42 and A46 nonetheless may assist the auditor in identifying where there may be risks of material misstatement.
- A45. When an engagement is carried out by a large engagement team, such as for an audit of group financial statements, it is not always necessary or practical for the discussion to include all members in a single discussion (for example, in a multi-location audit), nor is it necessary for all the members of the engagement team to be informed of all the decisions reached in the discussion. The engagement partner may discuss matters with key members of the engagement team including, if considered appropriate, those with specific skills or knowledge, and those responsible for the audits of components, while delegating discussion with others, taking into account the extent of communication considered necessary throughout the engagement team. A communications plan, agreed by the engagement partner, may be useful.

## Discussion of Disclosures in the Applicable Financial Reporting Framework

- A46. As part of the discussion among the engagement team, consideration of the disclosure requirements of the applicable financial reporting framework assists in identifying early in the audit where there may be risks of material misstatement in relation to disclosures, even in circumstances where the applicable financial reporting framework only requires simplified disclosures. Matters the engagement team may discuss include:
- Changes in financial reporting requirements that may result in significant new or revised disclosures;
  - Changes in the entity's environment, financial condition or activities that may result in significant new or revised disclosures, for example, a significant business combination in the period under audit;
  - Disclosures for which obtaining sufficient appropriate audit evidence may have been difficult in the past; and
  - Disclosures about complex matters, including those involving significant management judgement as to what information to disclose.

## Considerations Specific to Public Sector Entities

- A47. As part of the discussion among the engagement team by auditors of public sector entities, consideration may also be given to any additional broader objectives, and related risks, arising from the audit mandate or obligations for public sector entities.

## Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework and the Entity's System of Internal Control (Ref: Para. 19–27)

**Appendices 1 through 6** set out further considerations relating to obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control.

### *Obtaining the Required Understanding* (Ref: Para. 19–27)

- A48. Obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control is a dynamic and iterative process of gathering, updating and analysing information and continues throughout the audit. Therefore, the auditor's expectations may change as new information is obtained.
- A49. The auditor's understanding of the entity and its environment and the applicable financial reporting framework may also assist the auditor in developing initial expectations about the classes of transactions, account balances and disclosures that may be significant classes of transactions, account balances and disclosures. These expected significant classes of transactions, account balances and disclosures form the basis for the scope of the auditor's understanding of the entity's information system.

### *Why an Understanding of the Entity and Its Environment, and the Applicable Financial Reporting Framework Is Required* (Ref: Para. 19–20)

- A50. The auditor's understanding of the entity and its environment, and the applicable financial reporting framework, assists the auditor in understanding the events and conditions that are relevant to the entity, and in identifying how inherent risk factors affect the susceptibility of assertions to misstatement in the preparation of the financial statements, in accordance with the applicable financial reporting framework, and the degree to which they do so. Such information establishes a frame of reference within which the auditor identifies and assesses risks of material misstatement. This frame of reference also assists the auditor in planning the audit and exercising professional judgement and professional scepticism throughout the audit, for example, when:
- Identifying and assessing risks of material misstatement of the financial statements in accordance with ISA (NZ) 315 (Revised) or other relevant standards (e.g., relating to risks of fraud in accordance with ISA (NZ) 240 or when identifying or assessing risks related to accounting estimates in accordance with ISA (NZ) 540 (Revised));
  - Performing procedures to help identify instances of non-compliance with laws and regulations that may have a material effect on the financial statements in accordance with ISA (NZ) 250;<sup>27</sup>

<sup>27</sup> ISA (NZ) 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraph 14

- Evaluating whether the financial statements provide adequate disclosures in accordance with ISA (NZ) 700 (Revised);<sup>28</sup>
- Determining materiality or performance materiality in accordance with ISA (NZ) 320;<sup>29</sup> or
- Considering the appropriateness of the selection and application of accounting policies, and the adequacy of financial statement disclosures.

A51. [Amended by the NZAuASB]

NZ A51. The auditor's understanding of the entity and its environment, and the applicable financial reporting framework, also informs how the auditor plans and performs further audit procedures, for example, when:

- Developing expectations for use when performing analytical procedures in accordance with ISA (NZ) 520;<sup>30</sup>
- Designing and performing further audit procedures to obtain sufficient appropriate audit evidence in accordance with ISA (NZ) 330; and
- Evaluating the sufficiency and appropriateness of audit evidence obtained (e.g., relating to assumptions or management's and, where appropriate, those charged with governance's oral and written representations).

#### Scalability

A52. The nature and extent of the required understanding is a matter of the auditor's professional judgement and varies from entity to entity based on the nature and circumstances of the entity, including:

- The size and complexity of the entity, including its IT environment;
- The auditor's previous experience with the entity;
- The nature of the entity's systems and processes, including whether they are formalised or not; and
- The nature and form of the entity's documentation.

A53. The auditor's risk assessment procedures to obtain the required understanding may be less extensive in audits of less complex entities and more extensive for entities that are more complex. The depth of the understanding that is required by the auditor is expected to be less than that possessed by management in managing the entity.

A54. Some financial reporting frameworks allow smaller entities to provide simpler and less detailed disclosures in the financial statements. However, this does not relieve the auditor of the responsibility to obtain an understanding of the entity and its environment and the applicable financial reporting framework as it applies to the entity.

<sup>28</sup> ISA (NZ) 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 13(e)

<sup>29</sup> ISA (NZ) 320, *Materiality in Planning and Performing an Audit*, paragraphs 10–11

<sup>30</sup> ISA (NZ) 520, paragraph 5

A55. The entity's use of IT and the nature and extent of changes in the IT environment may also affect the specialised skills that are needed to assist with obtaining the required understanding.

*The Entity and Its Environment* (Ref: Para. 19(a))

The Entity's Organisational Structure, Ownership and Governance, and Business Model (Ref: Para. 19(a)(i))

The entity's organisational structure and ownership

A56. An understanding of the entity's organisational structure and ownership may enable the auditor to understand such matters as:

- The complexity of the entity's structure.

**Example:**

The entity may be a single entity or the entity's structure may include subsidiaries, divisions or other components in multiple locations. Further, the legal structure may be different from the operating structure. Complex structures often introduce factors that may give rise to increased susceptibility to risks of material misstatement. Such issues may include whether goodwill, joint ventures, investments, or special-purpose entities are accounted for appropriately and whether adequate disclosure of such issues in the financial statements has been made.

- The ownership, and relationships between owners and other people or entities, including related parties. This understanding may assist in determining whether related party transactions have been appropriately identified, accounted for, and adequately disclosed in the financial statements.<sup>31</sup>
- The distinction between the owners, those charged with governance and management.

**Example:**

In less complex entities, owners of the entity may be involved in managing the entity, therefore there is little or no distinction. In contrast, such as in some listed entities, there may be a clear distinction between management, the owners of the entity, and those charged with governance.<sup>32</sup>

- The structure and complexity of the entity's IT environment.

<sup>31</sup> ISA (NZ) 550 establishes requirements and provide guidance on the auditor's considerations relevant to related parties.

<sup>32</sup> ISA (NZ) 260 (Revised), paragraphs A1 and A2, provide guidance on the identification of those charged with governance and explains that in some cases, some or all of those charged with governance may be involved in managing the entity.

**Examples:**

An entity may:

- Have multiple legacy IT systems in diverse businesses that are not well integrated resulting in a complex IT environment.
- Be using external or internal service providers for aspects of its IT environment (e.g., outsourcing the hosting of its IT environment to a third party or using a shared service centre for central management of IT processes in a group).

### Automated tools and techniques

A57. The auditor may use automated tools and techniques to understand flows of transactions and processing as part of the auditor's procedures to understand the information system. An outcome of these procedures may be that the auditor obtains information about the entity's organisational structure or those with whom the entity conducts business (e.g., vendors, customers, related parties).

### Considerations specific to public sector entities

A58. Ownership of a public sector entity may not have the same relevance as in the private sector because decisions related to the entity may be made outside of the entity as a result of political processes. Therefore, management may not have control over certain decisions that are made. Matters that may be relevant include understanding the ability of the entity to make unilateral decisions, and the ability of other public sector entities to control or influence the entity's mandate and strategic direction.

**Example:**

A public sector entity may be subject to laws or other directives from authorities that require it to obtain approval from parties external to the entity of its strategy and objectives prior to it implementing them. Therefore, matters related to understanding the legal structure of the entity may include applicable laws and regulations, and the classification of the entity (i.e., whether the entity is a ministry, department, agency or other type of entity).

### Governance

#### Why the auditor obtains an understanding of governance

A59. Understanding the entity's governance may assist the auditor with understanding the entity's ability to provide appropriate oversight of its system of internal control. However, this understanding may also provide evidence of deficiencies, which may indicate an increase in the susceptibility of the entity's financial statements to risks of material misstatement.

## Understanding the entity's governance

A60. Matters that may be relevant for the auditor to consider in obtaining an understanding of the governance of the entity include:

- Whether any or all of those charged with governance are involved in managing the entity.
- The existence (and separation) of a non-executive Board, if any, from executive management.
- Whether those charged with governance hold positions that are an integral part of the entity's legal structure, for example as directors.
- The existence of sub-groups of those charged with governance, such as an audit committee, and the responsibilities of such a group.
- The responsibilities of those charged with governance for oversight of financial reporting, including approval of the financial statements.

## The Entity's Business Model

**Appendix 1** sets out additional considerations for obtaining an understanding of the entity and its business model, as well as additional considerations for auditing special purpose entities.

## Why the auditor obtains an understanding of the entity's business model

A61. Understanding the entity's objectives, strategy and business model helps the auditor to understand the entity at a strategic level, and to understand the business risks the entity takes and faces. An understanding of the business risks that have an effect on the financial statements assists the auditor in identifying risks of material misstatement, since most business risks will eventually have financial consequences and, therefore, an effect on the financial statements.

**Examples:**

An entity's business model may rely on the use of IT in different ways:

- The entity sells shoes from a physical store, and uses an advanced stock and point of sale system to record the selling of shoes; or
- The entity sells shoes online so that all sales transactions are processed in an IT environment, including initiation of the transactions through a website.

For both of these entities the business risks arising from a significantly different business model would be substantially different, notwithstanding both entities sell shoes.

## Understanding the entity's business model

A62. Not all aspects of the business model are relevant to the auditor's understanding. Business risks are broader than the risks of material misstatement of the financial statements,

although business risks include the latter. The auditor does not have a responsibility to understand or identify all business risks because not all business risks give rise to risks of material misstatement.

A63. Business risks increasing the susceptibility to risks of material misstatement may arise from:

- Inappropriate objectives or strategies, ineffective execution of strategies, or change or complexity.
- A failure to recognise the need for change may also give rise to business risk, for example, from:
  - The development of new products or services that may fail;
  - A market which, even if successfully developed, is inadequate to support a product or service; or
  - Flaws in a product or service that may result in legal liability and reputational risk.
- Incentives and pressures on management, which may result in intentional or unintentional management bias, and therefore affect the reasonableness of significant assumptions and the expectations of management or those charged with governance.

A64. Examples of matters that the auditor may consider when obtaining an understanding of the entity's business model, objectives, strategies and related business risks that may result in a risk of material misstatement of the financial statements include:

- Industry developments, such as the lack of personnel or expertise to deal with the changes in the industry;
- New products and services that may lead to increased product liability;
- Expansion of the entity's business, and demand has not been accurately estimated;
- New accounting requirements where there has been incomplete or improper implementation;
- Regulatory requirements resulting in increased legal exposure;
- Current and prospective financing requirements, such as loss of financing due to the entity's inability to meet requirements;
- Use of IT, such as the implementation of a new IT system that will affect both operations and financial reporting; or
- The effects of implementing a strategy, particularly any effects that will lead to new accounting requirements.

A65. Ordinarily, management identifies business risks and develops approaches to address them. Such a risk assessment process is part of the entity's system of internal control and is discussed in paragraph 22, and paragraphs A109–A113.

## Considerations specific to public sector entities

A66. Entities operating in the public sector may create and deliver value in different ways to those creating wealth for owners but will still have a ‘business model’ with a specific objective. Matters public sector auditors may obtain an understanding of that are relevant to the business model of the entity, include:

- Knowledge of relevant government activities, including related programmes.
- Programme objectives and strategies, including public policy elements.

A67. For the audits of public sector entities, “management objectives” may be influenced by requirements to demonstrate public accountability and may include objectives which have their source in law, regulation or other authority.

## Industry, Regulatory and Other External Factors (Ref: Para. 19(a)(ii))

### Industry factors

A68. Relevant industry factors include industry conditions such as the competitive environment, supplier and customer relationships, and technological developments. Matters the auditor may consider include:

- The market and competition, including demand, capacity, and price competition.
- Cyclical or seasonal activity.
- Product technology relating to the entity’s products.
- Energy supply and cost.

A69. The industry in which the entity operates may give rise to specific risks of material misstatement arising from the nature of the business or the degree of regulation.

#### **Example:**

In the construction industry, long-term contracts may involve significant estimates of revenues and expenses that give rise to risks of material misstatement. In such cases, it is important that the engagement team include members with sufficient relevant knowledge and experience.<sup>33</sup>

### Regulatory factors

A70. Relevant regulatory factors include the regulatory environment. The regulatory environment encompasses, among other matters, the applicable financial reporting framework and the legal and political environment and any changes thereto. Matters the auditor may consider include:

- Regulatory framework for a regulated industry, for example, prudential requirements, including related disclosures.
- Legislation and regulation that significantly affect the entity’s operations, for example, labor laws and regulations.

<sup>33</sup> ISA (NZ) 220, paragraph 14



- Taxation legislation and regulations.
- Government policies currently affecting the conduct of the entity's business, such as monetary, including foreign exchange controls, fiscal, financial incentives (for example, government aid programmes), and tariffs or trade restriction policies.
- Environmental requirements affecting the industry and the entity's business.

A71. ISA (NZ) 250 (Revised) includes some specific requirements related to the legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates.<sup>34</sup>

#### Considerations specific to public sector entities

A72. For the audits of public sector entities, there may be particular laws or regulations that affect the entity's operations. Such elements may be an essential consideration when obtaining an understanding of the entity and its environment.

#### Other external factors

A73. Other external factors affecting the entity that the auditor may consider include the general economic conditions, interest rates and availability of financing, and inflation or currency revaluation.

#### Measures Used by Management to Assess the Entity's Financial Performance (Ref: Para. 19(a)(iii))

##### Why the auditor understands measures used by management

- A74. An understanding of the entity's measures assists the auditor in considering whether such measures, whether used externally or internally, create pressures on the entity to achieve performance targets. These pressures may motivate management to take actions that increase the susceptibility to misstatement due to management bias or fraud (e.g., to improve the business performance or to intentionally misstate the financial statements) (see ISA (NZ) 240 for requirements and guidance in relation to the risks of fraud).
- A75. Measures may also indicate to the auditor the likelihood of risks of material misstatement of related financial statement information. For example, performance measures may indicate that the entity has unusually rapid growth or profitability when compared to that of other entities in the same industry.

##### Measures used by management

- A76. Management and others ordinarily measure and review those matters they regard as important. Enquiries of management may reveal that it relies on certain key indicators, whether publicly available or not, for evaluating financial performance and taking action. In such cases, the auditor may identify relevant performance measures, whether internal or external, by considering the information that the entity uses to manage its business. If such enquiry indicates an absence of performance measurement or review, there may be an increased risk of misstatements not being detected and corrected.
- A77. Key indicators used for evaluating financial performance may include:

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<sup>34</sup> ISA (NZ) 250 (Revised), paragraph 13

- Key performance indicators (financial and non-financial) and key ratios, trends and operating statistics.
- Period-on-period financial performance analyses.
- Budgets, forecasts, variance analyses, segment information and divisional, departmental or other level performance reports.
- Employee performance measures and incentive compensation policies.
- Comparisons of an entity's performance with that of competitors.

#### Scalability (Ref: Para. 19(a)(iii))

A78. The procedures undertaken to understand the entity's measures may vary depending on the size or complexity of the entity, as well as the involvement of owners or those charged with governance in the management of the entity.

#### **Examples:**

- For some less complex entities, the terms of the entity's bank borrowings (i.e., bank covenants) may be linked to specific performance measures related to the entity's performance or financial position (e.g., a maximum working capital amount). The auditor's understanding of the performance measures used by the bank may help identify areas where there is increased susceptibility to the risk of material misstatement.
- For some entities whose nature and circumstances are more complex, such as those operating in the insurance or banking industries, performance or financial position may be measured against regulatory requirements (e.g., regulatory ratio requirements such as capital adequacy and liquidity ratios performance hurdles). The auditor's understanding of these performance measures may help identify areas where there is increased susceptibility to the risk of material misstatement.

#### Other considerations

A79. External parties may also review and analyse the entity's financial performance, in particular for entities where financial information is publicly available. The auditor may also consider publicly available information to help the auditor further understand the business or identify contradictory information such as information from:

- Analysts or credit agencies.
- News and other media, including social media.
- Taxation authorities.
- Regulators.
- Trade unions.
- Providers of finance.

Such financial information can often be obtained from the entity being audited.

A80. The measurement and review of financial performance is not the same as the monitoring of the system of internal control (discussed as a component of the system of internal control in paragraphs A114–A122), though their purposes may overlap:

- The measurement and review of performance is directed at whether business performance is meeting the objectives set by management (or third parties).
- In contrast, monitoring of the system of internal control is concerned with monitoring the effectiveness of controls including those related to management’s measurement and review of financial performance.

In some cases, however, performance indicators also provide information that enables management to identify control deficiencies.

#### Considerations specific to public sector entities

A81. In addition to considering relevant measures used by a public sector entity to assess the entity’s financial performance, auditors of public sector entities may also consider non-financial information such as achievement of public benefit outcomes (for example, the number of people assisted by a specific programme).

#### *The Applicable Financial Reporting Framework* (Ref: Para. 19(b))

#### Understanding the Applicable Financial Reporting Framework and the Entity’s Accounting Policies

A82. Matters that the auditor may consider when obtaining an understanding of the entity’s applicable financial reporting framework, and how it applies in the context of the nature and circumstances of the entity and its environment include:

- The entity’s financial reporting practices in terms of the applicable financial reporting framework, such as:
  - Accounting principles and industry-specific practices, including for industry-specific significant classes of transactions, account balances and related disclosures in the financial statements (for example, loans and investments for banks, or research and development for pharmaceuticals).
  - Revenue recognition.
  - Accounting for financial instruments, including related credit losses.
  - Foreign currency assets, liabilities and transactions.
  - Accounting for unusual or complex transactions including those in controversial or emerging areas (for example, accounting for cryptocurrency).
- An understanding of the entity’s selection and application of accounting policies, including any changes thereto as well as the reasons therefore, may encompass such matters as:
  - The methods the entity uses to recognise, measure, present and disclose significant and unusual transactions.

- The effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.
- Changes in the environment, such as changes in the applicable financial reporting framework or tax reforms that may necessitate a change in the entity's accounting policies.
- Financial reporting standards and laws and regulations that are new to the entity and when and how the entity will adopt, or comply with, such requirements.

A83. Obtaining an understanding of the entity and its environment may assist the auditor in considering where changes in the entity's financial reporting (e.g., from prior periods) may be expected.

**Example:**

If the entity has had a significant business combination during the period, the auditor would likely expect changes in classes of transactions, account balances and disclosures associated with that business combination. Alternatively, if there were no significant changes in the financial reporting framework during the period the auditor's understanding may help confirm that the understanding obtained in the prior period remains applicable.

Considerations specific to public sector entities

A84. The applicable financial reporting framework in a public sector entity is determined by the legislative and regulatory frameworks relevant to each jurisdiction or within each geographical area. Matters that may be considered in the entity's application of the applicable financial reporting requirements, and how it applies in the context of the nature and circumstances of the entity and its environment, include whether the entity applies a full accrual basis of accounting or a cash basis of accounting in accordance with as the International Public Sector Accounting Standards, or a hybrid.

How Inherent Risk Factors Affect Susceptibility of Assertions to Misstatement (Ref: Para. 19(c))

**Appendix 2** provides examples of events and conditions that may give rise to the existence of risks of material misstatement, categorised by inherent risk factor.

Why the auditor understands inherent risk factors when understanding the entity and its environment and the applicable financial reporting framework

A85. Understanding the entity and its environment, and the applicable financial reporting framework, assists the auditor in identifying events or conditions, the characteristics of which may affect the susceptibility of assertions about classes of transactions, account balances or disclosures to misstatement. These characteristics are inherent risk factors. Inherent risk factors may affect susceptibility of assertions to misstatement by influencing the likelihood of occurrence of a misstatement or the magnitude of the misstatement if it were to occur. Understanding how inherent risk factors affect the susceptibility of assertions to misstatement may assist the auditor with a preliminary understanding of the

likelihood or magnitude of misstatements, which assists the auditor in identifying risks of material misstatement at the assertion level in accordance with paragraph 28(b). Understanding the degree to which inherent risk factors affect susceptibility of assertions to misstatement also assists the auditor in assessing the likelihood and magnitude of a possible misstatement when assessing inherent risk in accordance with paragraph 31(a). Accordingly, understanding the inherent risk factors may also assist the auditor in designing and performing further audit procedures in accordance with ISA (NZ) 330.

- A86. The auditor's identification of risks of material misstatement at the assertion level and assessment of inherent risk may also be influenced by audit evidence obtained by the auditor in performing other risk assessment procedures, further audit procedures or in fulfilling other requirements in the ISAs (NZ) (see paragraphs A95, A103, A111, A121, A124 and A151).

The effect of inherent risk factors on a class of transactions, account balance or disclosure

- A87. The extent of susceptibility to misstatement of a class of transactions, account balance or disclosure arising from complexity or subjectivity is often closely related to the extent to which it is subject to change or uncertainty.

**Example:**

If the entity has an accounting estimate that is based on assumptions, the selection of which are subject to significant judgement, the measurement of the accounting estimate is likely to be affected by both subjectivity and uncertainty.

- A88. The greater the extent to which a class of transactions, account balance or disclosure is susceptible to misstatement because of complexity or subjectivity, the greater the need for the auditor to apply professional scepticism. Further, when a class of transactions, account balance or disclosure is susceptible to misstatement because of complexity, subjectivity, change or uncertainty, these inherent risk factors may create opportunity for management bias, whether unintentional or intentional, and affect susceptibility to misstatement due to management bias. The auditor's identification of risks of material misstatement, and assessment of inherent risk at the assertion level, are also affected by the interrelationships among inherent risk factors.
- A89. Events or conditions that may affect susceptibility to misstatement due to management bias may also affect susceptibility to misstatement due to other fraud risk factors. Accordingly, this may be relevant information for use in accordance with paragraph 24 of ISA (NZ) 240, which requires the auditor to evaluate whether the information obtained from the other risk assessment procedures and related activities indicates that one or more fraud risk factors are present.

*Obtaining an Understanding of the Entity's System of Internal Control (Ref: Para. 21–27)*

**Appendix 3** further describes the nature of the entity's system of internal control and inherent limitations of internal control, respectively. Appendix 3 also provides further explanation of the components of a system of internal control for the purposes of the ISAs (NZ).

- A90. The auditor's understanding of the entity's system of internal control is obtained through risk assessment procedures performed to understand and evaluate each of the components of the system of internal control as set out in paragraphs 21 to 27.
- A91. The components of the entity's system of internal control for the purpose of this ISA (NZ) may not necessarily reflect how an entity designs, implements and maintains its system of internal control, or how it may classify any particular component. Entities may use different terminology or frameworks to describe the various aspects of the system of internal control. For the purpose of an audit, auditors may also use different terminology or frameworks provided all the components described in this ISA (NZ) are addressed.

#### Scalability

- A92. The way in which the entity's system of internal control is designed, implemented and maintained varies with an entity's size and complexity. For example, less complex entities may use less structured or simpler controls (i.e., policies and procedures) to achieve their objectives.

#### Considerations Specific to Public Sector Entities

- A93. Auditors of public sector entities often have additional responsibilities with respect to internal control, for example, to report on compliance with an established code of practice or reporting on spending against budget. Auditors of public sector entities may also have responsibilities to report on compliance with law, regulation or other authority. As a result, their considerations about the system of internal control may be broader and more detailed.

#### Information Technology in the Components of the Entity's System of Internal Control

**Appendix 5** provides further guidance on understanding the entity's use of IT in the components of the system of internal control.

- A94. The overall objective and scope of an audit does not differ whether an entity operates in a mainly manual environment, a completely automated environment, or an environment involving some combination of manual and automated elements (i.e., manual and automated controls and other resources used in the entity's system of internal control).

#### Understanding the Nature of the Components of the Entity's System of Internal Control

- A95. In evaluating the effectiveness of the design of controls and whether they have been implemented (see paragraphs A175 to A181) the auditor's understanding of each of the components of the entity's system of internal control provides a preliminary understanding of how the entity identifies business risks and how it responds to them. It may also influence the auditor's identification and assessment of the risks of material misstatement in different ways (see paragraph A86). This assists the auditor in designing and performing further audit procedures, including any plans to test the operating effectiveness of controls. For example:
- The auditor's understanding of the entity's control environment, the entity's risk assessment process, and the entity's process to monitor controls components are

more likely to affect the identification and assessment of risks of material misstatement at the financial statement level.

- The auditor's understanding of the entity's information system and communication, and the entity's control activities component, are more likely to affect the identification and assessment of risks of material misstatement at the assertion level.

Control Environment, The Entity's Risk Assessment Process and the Entity's Process to Monitor the System of Internal Control (Ref: Para. 21–24)

A96. The controls in the control environment, the entity's risk assessment process and the entity's process to monitor the system of internal control are primarily indirect controls (i.e., controls that are not sufficiently precise to prevent, detect or correct misstatements at the assertion level but which support other controls and may therefore have an indirect effect on the likelihood that a misstatement will be detected or prevented on a timely basis). However, some controls within these components may also be direct controls.

Why the auditor is required to understand the control environment, the entity's risk assessment process and the entity's process to monitor the system of internal control

- A97. The control environment provides an overall foundation for the operation of the other components of the system of internal control. The control environment does not directly prevent, or detect and correct, misstatements. It may, however, influence the effectiveness of controls in the other components of the system of internal control. Similarly, the entity's risk assessment process and its process for monitoring the system of internal control are designed to operate in a manner that also supports the entire system of internal control.
- A98. Because these components are foundational to the entity's system of internal control, any deficiencies in their operation could have pervasive effects on the preparation of the financial statements. Therefore, the auditor's understanding and evaluations of these components affect the auditor's identification and assessment of risks of material misstatement at the financial statement level, and may also affect the identification and assessment of risks of material misstatement at the assertion level. Risks of material misstatement at the financial statement level affect the auditor's design of overall responses, including, as explained in ISA (NZ) 330, an influence on the nature, timing and extent of the auditor's further procedures.<sup>35</sup>

Obtaining an understanding of the control environment (Ref: Para. 21)

Scalability

- A99. The nature of the control environment in a less complex entity is likely to be different from the control environment in a more complex entity. For example, those charged with governance in less complex entities may not include an independent or outside member, and the role of governance may be undertaken directly by the owner-manager where there are no other owners. Accordingly, some considerations about the entity's control environment may be less relevant or may not be applicable.

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<sup>35</sup> ISA (NZ) 330, paragraphs A1–A3

A100. In addition, audit evidence about elements of the control environment in less complex entities may not be available in documentary form, in particular where communication between management and other personnel is informal, but the evidence may still be appropriately relevant and reliable in the circumstances.

**Examples:**

- The organisational structure in a less complex entity will likely be simpler and may include a small number of employees involved in roles related to financial reporting.
- If the role of governance is undertaken directly by the owner-manager, the auditor may determine that the independence of those charged with governance is not relevant.
- Less complex entities may not have a written code of conduct but, instead, develop a culture that emphasizes the importance of integrity and ethical behaviour through oral communication and by management example. Consequently, the attitudes, awareness and actions of management or the owner-manager are of particular importance to the auditor's understanding of a less complex entity's control environment.

Understanding the control environment (Ref: Para. 21(a))

A101. Audit evidence for the auditor's understanding of the control environment may be obtained through a combination of enquiries and other risk assessment procedures (i.e., corroborating enquiries through observation or inspection of documents).

A102. In considering the extent to which management demonstrates a commitment to integrity and ethical values, the auditor may obtain an understanding through enquiries of management and employees, and through considering information from external sources, about:

- How management communicates to employees its views on business practices and ethical behaviour; and
- Inspecting management's written code of conduct and observing whether management acts in a manner that supports that code.

Evaluating the control environment (Ref: Para. 21(b))

Why the auditor evaluates the control environment

A103. The auditor's evaluation of how the entity demonstrates behaviour consistent with the entity's commitment to integrity and ethical values; whether the control environment provides an appropriate foundation for the other components of the entity's system of internal control; and whether any identified control deficiencies undermine the other components of the system of internal control, assists the auditor in identifying potential issues in the other components of the system of internal control. This is because the control environment is foundational to the other components of the entity's system of internal control. This evaluation may also assist the auditor in understanding risks faced by the



entity and therefore in identifying and assessing the risks of material misstatement at the financial statement and assertion levels (see paragraph A86).

#### The auditor's evaluation of the control environment

A104. The auditor's evaluation of the control environment is based on the understanding obtained in accordance with paragraph 21(a).

A105. Some entities may be dominated by a single individual who may exercise a great deal of discretion. The actions and attitudes of that individual may have a pervasive effect on the culture of the entity, which in turn may have a pervasive effect on the control environment. Such an effect may be positive or negative.

**Example:**

Direct involvement by a single individual may be key to enabling the entity to meet its growth and other objectives, and can also contribute significantly to an effective system of internal control. On the other hand, such concentration of knowledge and authority can also lead to an increased susceptibility to misstatement through management override of controls.

A106. The auditor may consider how the different elements of the control environment may be influenced by the philosophy and operating style of senior management taking into account the involvement of independent members of those charged with governance.

A107. Although the control environment may provide an appropriate foundation for the system of internal control and may help reduce the risk of fraud, an appropriate control environment is not necessarily an effective deterrent to fraud.

**Example:**

Human resource policies and procedures directed toward hiring competent financial, accounting, and IT personnel may mitigate the risk of errors in processing and recording financial information. However, such policies and procedures may not mitigate the override of controls by senior management (e.g., to overstate earnings).

A108. The auditor's evaluation of the control environment as it relates to the entity's use of IT may include such matters as:

- Whether governance over IT is commensurate with the nature and complexity of the entity and its business operations enabled by IT, including the complexity or maturity of the entity's technology platform or architecture and the extent to which the entity relies on IT applications to support its financial reporting.
- The management organisational structure regarding IT and the resources allocated (for example, whether the entity has invested in an appropriate IT environment and necessary enhancements, or whether a sufficient number of appropriately skilled individuals have been employed including when the entity uses commercial software (with no or limited modifications)).

Obtaining an understanding of the entity's risk assessment process (Ref: Para. 22–23)

Understanding the entity's risk assessment process (Ref: Para. 22(a))

A109. As explained in paragraph A62, not all business risks give rise to risks of material misstatement. In understanding how management and those charged with governance have identified business risks relevant to the preparation of the financial statements, and decided about actions to address those risks, matters the auditor may consider include how management or, as appropriate, those charged with governance, has:

- Specified the entity's objectives with sufficient precision and clarity to enable the identification and assessment of the risks relating to the objectives;
- Identified the risks to achieving the entity's objectives and analysed the risks as a basis for determining how the risks should be managed; and
- Considered the potential for fraud when considering the risks to achieving the entity's objectives.<sup>36</sup>

A110. The auditor may consider the implications of such business risks for the preparation of the entity's financial statements and other aspects of its system of internal control.

Evaluating the entity's risk assessment process (Ref: Para. 22(b))

Why the auditor evaluates whether the entity's risk assessment process is appropriate

A111. The auditor's evaluation of the entity's risk assessment process may assist the auditor in understanding where the entity has identified risks that may occur, and how the entity has responded to those risks. The auditor's evaluation of how the entity identifies its business risks, and how it assesses and addresses those risks assists the auditor in understanding whether the risks faced by the entity have been identified, assessed and addressed as appropriate to the nature and complexity of the entity. This evaluation may also assist the auditor with identifying and assessing financial statement level and assertion level risks of material misstatement (see paragraph A86).

Evaluating whether the entity's risk assessment process is appropriate (Ref: Para. 22(b))

A112. The auditor's evaluation of the appropriateness of the entity's risk assessment process is based on the understanding obtained in accordance with paragraph 22(a).

Scalability

A113. Whether the entity's risk assessment process is appropriate to the entity's circumstances considering the nature and complexity of the entity is a matter of the auditor's professional judgement.

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<sup>36</sup> ISA (NZ) 240, paragraph 19

**Example:**

In some less complex entities, and particularly owner-managed entities, an appropriate risk assessment may be performed through the direct involvement of management or the owner-manager (e.g., the manager or owner-manager may routinely devote time to monitoring the activities of competitors and other developments in the market place to identify emerging business risks). The evidence of this risk assessment occurring in these types of entities is often not formally documented, but it may be evident from the discussions the auditor has with management that management are in fact performing risk assessment procedures.

Obtaining an understanding of the entity's process to monitor the entity's system of internal control (Ref: Para. 24)

## Scalability

A114. In less complex entities, and in particular owner-manager entities, the auditor's understanding of the entity's process to monitor the system of internal control is often focused on how management or the owner-manager is directly involved in operations, as there may not be any other monitoring activities.

**Example:**

Management may receive complaints from customers about inaccuracies in their monthly statement that alerts the owner-manager to issues with the timing of when customer payments are being recognised in the accounting records.

A115. For entities where there is no formal process for monitoring the system of internal control, understanding the process to monitor the system of internal control may include understanding periodic reviews of management accounting information that are designed to contribute to how the entity prevents or detects misstatements.

Understanding the entity's process to monitor the system of internal control (Ref: Para. 24(a))

A116. Matters that may be relevant for the auditor to consider when understanding how the entity monitors its system of internal control include:

- The design of the monitoring activities, for example whether it is periodic or ongoing monitoring;
- The performance and frequency of the monitoring activities;
- The evaluation of the results of the monitoring activities, on a timely basis, to determine whether the controls have been effective; and
- How identified deficiencies have been addressed through appropriate remedial actions, including timely communication of such deficiencies to those responsible for taking remedial action.

A117. The auditor may also consider how the entity's process to monitor the system of internal control addresses monitoring information processing controls that involve the use of IT. This may include, for example:

- Controls to monitor complex IT environments that:
  - Evaluate the continuing design effectiveness of information processing controls and modify them, as appropriate, for changes in conditions; or
  - Evaluate the operating effectiveness of information processing controls.
- Controls that monitor the permissions applied in automated information processing controls that enforce the segregation of duties.
- Controls that monitor how errors or control deficiencies related to the automation of financial reporting are identified and addressed.

Understanding the entity's internal audit function (Ref: Para. 24(a)(ii))

**Appendix 4** sets out further considerations for understanding the entity's internal audit function.

A118. The auditor's enquiries of appropriate individuals within the internal audit function help the auditor obtain an understanding of the nature of the internal audit function's responsibilities. If the auditor determines that the function's responsibilities are related to the entity's financial reporting, the auditor may obtain further understanding of the activities performed, or to be performed, by the internal audit function by reviewing the internal audit function's audit plan for the period, if any, and discussing that plan with the appropriate individuals within the function. This understanding, together with the information obtained from the auditor's enquiries, may also provide information that is directly relevant to the auditor's identification and assessment of the risks of material misstatement. If, based on the auditor's preliminary understanding of the internal audit function, the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed, ISA (NZ) 610 (Revised 2013)<sup>37</sup> applies.

Other sources of information used in the entity's process to monitor the system of internal control

Understanding the sources of information (Ref: Para. 24(b))

A119. Management's monitoring activities may use information in communications from external parties such as customer complaints or regulator comments that may indicate problems or highlight areas in need of improvement.

<sup>37</sup> ISA (NZ) 610 (Revised 2013), *Using the Work of Internal Auditors*

Why the auditor is required to understand the sources of information used for the entity's monitoring of the system of internal control

A120. The auditor's understanding of the sources of information used by the entity in monitoring the entity's system of internal control, including whether the information used is relevant and reliable, assists the auditor in evaluating whether the entity's process to monitor the entity's system of internal control is appropriate. If management assumes that information used for monitoring is relevant and reliable without having a basis for that assumption, errors that may exist in the information could potentially lead management to draw incorrect conclusions from its monitoring activities.

Evaluating the entity's process to monitor the system of internal control (Ref: Para 24(c))

Why the auditor evaluates whether the entity's process to monitor the system of internal control is appropriate

A121. The auditor's evaluation about how the entity undertakes ongoing and separate evaluations for monitoring the effectiveness of controls assists the auditor in understanding whether the other components of the entity's system of internal control are present and functioning, and therefore assists with understanding the other components of the entity's system of internal control. This evaluation may also assist the auditor with identifying and assessing financial statement level and assertion level risks of material misstatement (see paragraph A86).

Evaluating whether the entity's process to monitor the system of internal control is appropriate (Ref: Para. 24(c))

A122. The auditor's evaluation of the appropriateness of the entity's process to monitor the system of internal control is based on the auditor's understanding of the entity's process to monitor the system of internal control.

Information System and Communication, and Control Activities (Ref: Para. 25–26)

A123. The controls in the information system and communication, and control activities components are primarily direct controls (i.e., controls that are sufficiently precise to prevent, detect or correct misstatements at the assertion level).

Why the auditor is required to understand the information system and communication and controls in the control activities component

A124. The auditor is required to understand the entity's information system and communication because understanding the entity's policies that define the flows of transactions and other aspects of the entity's information processing activities relevant to the preparation of the financial statements, and evaluating whether the component appropriately supports the preparation of the entity's financial statements, supports the auditor's identification and assessment of risks of material misstatement at the assertion level. This understanding and evaluation may also result in the identification of risks of material misstatement at the financial statement level when the results of the auditor's procedures are inconsistent with expectations about the entity's system of internal control that may have been set based on

information obtained during the engagement acceptance or continuance process (see paragraph A86).

- A125. The auditor is required to identify specific controls in the control activities component, and evaluate the design and determine whether the controls have been implemented, as it assists the auditor's understanding about management's approach to addressing certain risks and therefore provides a basis for the design and performance of further audit procedures responsive to these risks as required by ISA (NZ) 330. The higher on the spectrum of inherent risk a risk is assessed, the more persuasive the audit evidence needs to be. Even when the auditor does not plan to test the operating effectiveness of identified controls, the auditor's understanding may still affect the design of the nature, timing and extent of substantive audit procedures that are responsive to the related risks of material misstatement.

The iterative nature of the auditor's understanding and evaluation of the information system and communication, and control activities

- A126. As explained in paragraph A49, the auditor's understanding of the entity and its environment, and the applicable financial reporting framework, may assist the auditor in developing initial expectations about the classes of transactions, account balances and disclosures that may be significant classes of transactions, account balances and disclosures. In obtaining an understanding of the information system and communication component in accordance with paragraph 25(a), the auditor may use these initial expectations for the purpose of determining the extent of understanding of the entity's information processing activities to be obtained.
- A127. The auditor's understanding of the information system includes understanding the policies that define flows of information relating to the entity's significant classes of transactions, account balances, and disclosures, and other related aspects of the entity's information processing activities. This information, and the information obtained from the auditor's evaluation of the information system may confirm or further influence the auditor's expectations about the significant classes of transactions, account balances and disclosures initially identified (see paragraph A126).
- A128. In obtaining an understanding of how information relating to significant classes of transactions, account balances and disclosures flows into, through, and out of the entity's information system, the auditor may also identify controls in the control activities component that are required to be identified in accordance with paragraph 26(a). The auditor's identification and evaluation of controls in the control activities component may first focus on controls over journal entries and controls that the auditor plans to test the operating effectiveness of in designing the nature, timing and extent of substantive procedures
- A129. The auditor's assessment of inherent risk may also influence the identification of controls in the control activities component. For example, the auditor's identification of controls relating to significant risks may only be identifiable when the auditor has assessed inherent risk at the assertion level in accordance with paragraph 31. Furthermore, controls addressing risks for which the auditor has determined that substantive procedures alone do not provide sufficient appropriate audit evidence (in accordance with paragraph 33)

may also only be identifiable once the auditor's inherent risk assessments have been undertaken.

A130. The auditor's identification and assessment of risks of material misstatement at the assertion level is influenced by both the auditor's:

- Understanding of the entity's policies for its information processing activities in the information system and communication component, and
- Identification and evaluation of controls in the control activities component.

Obtaining an understanding of the information system and communication (Ref: Para. 25)

**Appendix 3**, Paragraphs 15–19, sets out further considerations relating to the information system and communication.

Scalability

A131. The information system, and related business processes, in less complex entities are likely to be less sophisticated than in larger entities, and are likely to involve a less complex IT environment; however, the role of the information system is just as important. Less complex entities with direct management involvement may not need extensive descriptions of accounting procedures, sophisticated accounting records, or written policies. Understanding the relevant aspects of the entity's information system may therefore require less effort in an audit of a less complex entity, and may involve a greater amount of enquiry than observation or inspection of documentation. The need to obtain an understanding, however, remains important to provide a basis for the design of further audit procedures in accordance with ISA (NZ) 330 and may further assist the auditor in identifying or assessing risks of material misstatement (see paragraph A86).

Obtaining an understanding of the information system (Ref: Para. 25(a))

A132. Included within the entity's system of internal control are aspects that relate to the entity's reporting objectives, including its financial reporting objectives, but may also include aspects that relate to its operations or compliance objectives, when such aspects are relevant to financial reporting. Understanding how the entity initiates transactions and captures information as part of the auditor's understanding of the information system may include information about the entity's systems (its policies) designed to address compliance and operations objectives because such information is relevant to the preparation of the financial statements. Further, some entities may have information systems that are highly integrated such that controls may be designed in a manner to simultaneously achieve financial reporting, compliance and operational objectives, and combinations thereof.

A133. Understanding the entity's information system also includes an understanding of the resources to be used in the entity's information processing activities. Information about the human resources involved that may be relevant to understanding risks to the integrity of the information system include:

- The competence of the individuals undertaking the work;

- Whether there are adequate resources; and
- Whether there is appropriate segregation of duties.

A134. Matters the auditor may consider when understanding the policies that define the flows of information relating to the entity's significant classes of transactions, account balances, and disclosures in the information system and communication component include the nature of:

- (a) The data or information relating to transactions, other events and conditions to be processed;
- (b) The information processing to maintain the integrity of that data or information; and
- (c) The information processes, personnel and other resources used in the information processing process.

A135. Obtaining an understanding of the entity's business processes, which include how transactions are originated, assists the auditor in obtaining an understanding of the entity's information system in a manner that is appropriate to the entity's circumstances.

A136. The auditor's understanding of the information system may be obtained in various ways and may include:

- Enquiries of relevant personnel about the procedures used to initiate, record, process and report transactions or about the entity's financial reporting process;
- Inspection of policy or process manuals or other documentation of the entity's information system;
- Observation of the performance of the policies or procedures by entity's personnel; or
- Selecting transactions and tracing them through the applicable process in the information system (i.e., performing a walk-through).

#### Automated tools and techniques

A137. The auditor may also use automated techniques to obtain direct access to, or a digital download from, the databases in the entity's information system that store accounting records of transactions. By applying automated tools or techniques to this information, the auditor may confirm the understanding obtained about how transactions flow through the information system by tracing journal entries, or other digital records related to a particular transaction, or an entire population of transactions, from initiation in the accounting records through to recording in the general ledger. Analysis of complete or large sets of transactions may also result in the identification of variations from the normal, or expected, processing procedures for these transactions, which may result in the identification of risks of material misstatement.

#### Information obtained from outside of the general and subsidiary ledgers

A138. Financial statements may contain information that is obtained from outside of the general and subsidiary ledgers. Examples of such information that the auditor may consider include:



- Information obtained from lease agreements relevant to disclosures in the financial statements.
- Information disclosed in the financial statements that is produced by an entity's risk management system.
- Fair value information produced by management's experts and disclosed in the financial statements.
- Information disclosed in the financial statements that has been obtained from models, or from other calculations used to develop accounting estimates recognised or disclosed in the financial statements, including information relating to the underlying data and assumptions used in those models, such as:
  - Assumptions developed internally that may affect an asset's useful life; or
  - Data such as interest rates that are affected by factors outside the control of the entity.
- Information disclosed in the financial statements about sensitivity analyses derived from financial models that demonstrates that management has considered alternative assumptions.
- Information recognised or disclosed in the financial statements that has been obtained from an entity's tax returns and records.
- Information disclosed in the financial statements that has been obtained from analyses prepared to support management's assessment of the entity's ability to continue as a going concern, such as disclosures, if any, related to events or conditions that have been identified that may cast significant doubt on the entity's ability to continue as a going concern.<sup>38</sup>

A139. Certain amounts or disclosures in the entity's financial statements (such as disclosures about credit risk, liquidity risk, and market risk) may be based on information obtained from the entity's risk management system. However, the auditor is not required to understand all aspects of the risk management system, and uses professional judgement in determining the necessary understanding.

The entity's use of information technology in the information system

Why does the auditor understand the IT environment relevant to the information system

A140. The auditor's understanding of the information system includes the IT environment relevant to the flows of transactions and processing of information in the entity's information system because the entity's use of IT applications or other aspects in the IT environment may give rise to risks arising from the use of IT.

A141. The understanding of the entity's business model and how it integrates the use of IT may also provide useful context to the nature and extent of IT expected in the information system.

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<sup>38</sup> ISA (NZ) 570 (Revised), paragraphs 19–20

## Understanding the entity's use of IT

- A142. The auditor's understanding of the IT environment may focus on identifying, and understanding the nature and number of, the specific IT applications and other aspects of the IT environment that are relevant to the flows of transactions and processing of information in the information system. Changes in the flow of transactions, or information within the information system may result from program changes to IT applications, or direct changes to data in databases involved in processing, or storing those transactions or information.
- A143. The auditor may identify the IT applications and supporting IT infrastructure concurrently with the auditor's understanding of how information relating to significant classes of transactions, account balances and disclosures flows into, through and out the entity's information system.

## Obtaining an understanding of the entity's communication (Ref: Para. 25(b))

## Scalability

- A144. In larger, more complex entities, information the auditor may consider when understanding the entity's communication may come from policy manuals and financial reporting manuals.
- A145. In less complex entities, communication may be less structured (e.g., formal manuals may not be used) due to fewer levels of responsibility and management's greater visibility and availability. Regardless of the size of the entity, open communication channels facilitate the reporting of exceptions and acting on them.

## Evaluating whether the relevant aspects of the information system support the preparation of the entity's financial statements (Ref: Para. 25(c))

- A146. The auditor's evaluation of whether the entity's information system and communication appropriately supports the preparation of the financial statements is based on the understanding obtained in paragraphs 25(a)–(b).

## Control Activities (Ref: Para. 26)

## Controls in the control activities component

**Appendix 3**, Paragraphs 20 and 21 set out further considerations relating to control activities.

- A147. The control activities component includes controls that are designed to ensure the proper application of policies (which are also controls) in all the other components of the entity's system of internal control, and includes both direct and indirect controls.

**Example:**

The controls that an entity has established to ensure that its personnel are properly counting and recording the annual physical inventory relate directly to the risks of material misstatement relevant to the existence and completeness assertions for the inventory account balance.

A148. The auditor's identification and evaluation of controls in the control activities component is focused on information processing controls, which are controls applied during the processing of information in the entity's information system that directly address risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information). However, the auditor is not required to identify and evaluate all information processing controls related to the entity's policies that define the flows of transactions and other aspects of the entity's information processing activities for the significant classes of transactions, account balances and disclosures.

A149. There may also be direct controls that exist in the control environment, the entity's risk assessment process or the entity's process to monitor the system of internal control, which may be identified in accordance with paragraph 26. However, the more indirect the relationship between controls that support other controls and the control that is being considered, the less effective that control may be in preventing, or detecting and correcting, related misstatements.

**Example:**

A sales manager's review of a summary of sales activity for specific stores by region ordinarily is only indirectly related to the risks of material misstatement relevant to the completeness assertion for sales revenue. Accordingly, it may be less effective in addressing those risks than controls more directly related thereto, such as matching shipping documents with billing documents.

A150. Paragraph 26 also requires the auditor to identify and evaluate general IT controls for IT applications and other aspects of the IT environment that the auditor has determined to be subject to risks arising from the use of IT, because general IT controls support the continued effective functioning of information processing controls. A general IT control alone is typically not sufficient to address a risk of material misstatement at the assertion level.

A151. The controls that the auditor is required to identify and evaluate the design, and determine the implementation of, in accordance with paragraph 26 are those:

- Controls which the auditor plans to test the operating effectiveness of in determining the nature, timing and extent of substantive procedures. The evaluation of such controls provides the basis for the auditor's design of test of control procedures in accordance with ISA (NZ) 330. These controls also include controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence.
- Controls include controls that address significant risks and controls over journal entries. The auditor's identification and evaluation of such controls may also influence the auditor's understanding of the risks of material misstatement, including the identification of additional risks of material misstatement (see paragraph A95). This understanding also provides the basis for the auditor's design of the nature, timing and extent of substantive audit procedures that are responsive to the related assessed risks of material misstatement.

- Other controls that the auditor considers are appropriate to enable the auditor to meet the objectives of paragraph 13 with respect to risks at the assertion level, based on the auditor's professional judgement.

A152. Controls in the control activities component are required to be identified when such controls meet one or more of the criteria included in paragraph 26(a). However, when multiple controls each achieve the same objective, it is unnecessary to identify each of the controls related to such objective.

Types of controls in the control activities component (Ref: Para. 26)

A153. Examples of controls in the control activities component include authorisations and approvals, reconciliations, verifications (such as edit and validation checks or automated calculations), segregation of duties, and physical or logical controls, including those addressing safeguarding of assets.

A154. Controls in the control activities component may also include controls established by management that address risks of material misstatement related to disclosures not being prepared in accordance with the applicable financial reporting framework. Such controls may relate to information included in the financial statements that is obtained from outside of the general and subsidiary ledgers.

A155. Regardless of whether controls are within the IT environment or manual systems, controls may have various objectives and may be applied at various organisational and functional levels.

Scalability (Ref: Para. 26)

A156. Controls in the control activities component for less complex entities are likely to be similar to those in larger entities, but the formality with which they operate may vary. Further, in less complex entities, more controls may be directly applied by management.

**Example:**

Management's sole authority for granting credit to customers and approving significant purchases can provide strong control over important account balances and transactions.

A157. It may be less practicable to establish segregation of duties in less complex entities that have fewer employees. However, in an owner-managed entity, the owner-manager may be able to exercise more effective oversight through direct involvement than in a larger entity, which may compensate for the generally more limited opportunities for segregation of duties. Although, as also explained in ISA (NZ) 240, domination of management by a single individual can be a potential control deficiency since there is an opportunity for management override of controls.<sup>39</sup>

<sup>39</sup> ISA (NZ) 240, paragraph A28

Controls that address risks of material misstatement at the assertion level (Ref: Para. 26(a))

Controls that address risks that are determined to be a significant risk (Ref: Para. 26(a)(i))

A158. Regardless of whether the auditor plans to test the operating effectiveness of controls that address significant risks, the understanding obtained about management's approach to addressing those risks may provide a basis for the design and performance of substantive procedures responsive to significant risks as required by ISA (NZ) 330.<sup>40</sup> Although risks relating to significant non-routine or judgemental matters are often less likely to be subject to routine controls, management may have other responses intended to deal with such risks. Accordingly, the auditor's understanding of whether the entity has designed and implemented controls for significant risks arising from non-routine or judgemental matters may include whether and how management responds to the risks. Such responses may include:

- Controls, such as a review of assumptions by senior management or experts.
- Documented processes for accounting estimations.
- Approval by those charged with governance.

**Example:**

Where there are one-off events such as the receipt of a notice of a significant lawsuit, consideration of the entity's response may include such matters as whether it has been referred to appropriate experts (such as internal or external legal counsel), whether an assessment has been made of the potential effect, and how it is proposed that the circumstances are to be disclosed in the financial statements.

A159. ISA (NZ) 240<sup>41</sup> requires the auditor to understand controls related to assessed risks of material misstatement due to fraud (which are treated as significant risks), and further explains that it is important for the auditor to obtain an understanding of the controls that management has designed, implemented and maintained to prevent and detect fraud.

Controls over journal entries (Ref: Para. 26(a)(ii))

A160. Controls that address risks of material misstatement at the assertion level that are expected to be identified for all audits are controls over journal entries, because the manner in which an entity incorporates information from transaction processing into the general ledger ordinarily involves the use of journal entries, whether standard or non-standard, or automated or manual. The extent to which other controls are identified may vary based on the nature of the entity and the auditor's planned approach to further audit procedures.

<sup>40</sup> ISA (NZ) 330, paragraphe 21

<sup>41</sup> ISA (NZ) 240, paragraphes 28 and A33

**Example:**

In an audit of a less complex entity, the entity's information system may not be complex and the auditor may not plan to rely on the operating effectiveness of controls. Further, the auditor may not have identified any significant risks or any other risks of material misstatement for which it is necessary for the auditor to evaluate the design of controls and determine that they have been implemented. In such an audit, the auditor may determine that there are no identified controls other than the entity's controls over journal entries.

## Automated tools and techniques

A161. In manual general ledger systems, non-standard journal entries may be identified through inspection of ledgers, journals, and supporting documentation. When automated procedures are used to maintain the general ledger and prepare financial statements, such entries may exist only in electronic form and may therefore be more easily identified through the use of automated techniques.

**Example:**

In the audit of a less complex entity, the auditor may be able to extract a total listing of all journal entries into a simple spreadsheet. It may then be possible for the auditor to sort the journal entries by applying a variety of filters such as currency amount, name of the preparer or reviewer, journal entries that gross up the balance sheet and income statement only, or to view the listing by the date the journal entry was posted to the general ledger, to assist the auditor in designing responses to the risks identified relating to journal entries.

## Controls for which the auditor plans to test the operating effectiveness (Ref: Para. 26(a)(iii))

A162. The auditor determines whether there are any risks of material misstatement at the assertion level for which it is not possible to obtain sufficient appropriate audit evidence through substantive procedures alone. The auditor is required, in accordance with ISA (NZ) 330,<sup>42</sup> to design and perform tests of controls that address such risks of material misstatement when substantive procedures alone do not provide sufficient appropriate audit evidence at the assertion level. As a result, when such controls exist that address these risks, they are required to be identified and evaluated.

A163. In other cases, when the auditor plans to take into account the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures in accordance with ISA (NZ) 330, such controls are also required to be identified because ISA (NZ) 330<sup>43</sup> requires the auditor to design and perform tests of those controls.

**Examples:**

The auditor may plan to test the operating effectiveness of controls:

<sup>42</sup> ISA (NZ) 330, paragraph 8(b)

<sup>43</sup> ISA (NZ) 330, paragraph 8(a)

- Over routine classes of transactions because such testing may be more effective or efficient for large volumes of homogenous transactions.
- Over the completeness and accuracy of information produced by the entity (e.g., controls over the preparation of system-generated reports), to determine the reliability of that information, when the auditor intends to take into account the operating effectiveness of those controls in designing and performing further audit procedures.
- Relating to operations and compliance objectives when they relate to data the auditor evaluates or uses in applying audit procedures.

A164. The auditor's plans to test the operating effectiveness of controls may also be influenced by the identified risks of material misstatement at the financial statement level. For example, if deficiencies are identified related to the control environment, this may affect the auditor's overall expectations about the operating effectiveness of direct controls.

Other controls that the auditor considers appropriate (Ref: Para. 26(a)(iv))

A165. Other controls that the auditor may consider are appropriate to identify, and evaluate the design and determine the implementation, may include:

- Controls that address risks assessed as higher on the spectrum of inherent risk but have not been determined to be a significant risk;
- Controls related to reconciling detailed records to the general ledger; or
- Complementary user entity controls, if using a service organisation.<sup>44</sup>

Identifying IT applications and other aspects of the IT environment, risks arising from the use of IT and general IT controls (Ref: Para. 26(b)–(c))

**Appendix 5** includes example characteristics of IT applications and other aspects of the IT environment, and guidance related to those characteristics, that may be relevant in identifying IT applications and other aspects of the IT environment subject to risks arising from the use of IT.

Identifying IT applications and other aspects of the IT environment (Ref: Para. 26(b))

Why the auditor identifies risks arising from the use of IT and general IT controls related to identified IT applications and other aspects of the IT environment

A166. Understanding the risks arising from the use of IT and the general IT controls implemented by the entity to address those risks may affect:

- The auditor's decision about whether to test the operating effectiveness of controls to address risks of material misstatement at the assertion level;

<sup>44</sup> ISA (NZ) 402, *Audit Considerations Relating to an Entity Using a Service Organisation*

**Example:**

When general IT controls are not designed effectively or appropriately implemented to address risks arising from the use of IT (e.g., controls do not appropriately prevent or detect unauthorised program changes or unauthorised access to IT applications), this may affect the auditor's decision to rely on automated controls within the affected IT applications.

- The auditor's assessment of control risk at the assertion level;

**Example:**

The ongoing operating effectiveness of an information processing control may depend on certain general IT controls that prevent or detect unauthorised program changes to the IT information processing control (i.e., program change controls over the related IT application). In such circumstances, the expected operating effectiveness (or lack thereof) of the general IT control may affect the auditor's assessment of control risk (e.g., control risk may be higher when such general IT controls are expected to be ineffective or if the auditor does not plan to test the general IT controls).

- The auditor's strategy for testing information produced by the entity that is produced by or involves information from the entity's IT applications;

**Example:**

When information produced by the entity to be used as audit evidence is produced by IT applications, the auditor may determine to test controls over system-generated reports, including identification and testing of the general IT controls that address risks of inappropriate or unauthorised program changes or direct data changes to the reports.

- The auditor's assessment of inherent risk at the assertion level; or

**Example:**

When there are significant or extensive programming changes to an IT application to address new or revised reporting requirements of the applicable financial reporting framework, this may be an indicator of the complexity of the new requirements and their effect on the entity's financial statements. When such extensive programming or data changes occur, the IT application is also likely to be subject to risks arising from the use of IT.

- The design of further audit procedures.

**Example:**

If information processing controls depend on general IT controls, the auditor may determine to test the operating effectiveness of the general IT controls, which will



then require the design of tests of controls for such general IT controls. If, in the same circumstances, the auditor determines not to test the operating effectiveness of the general IT controls, or the general IT controls are expected to be ineffective, the related risks arising from the use of IT may need to be addressed through the design of substantive procedures. However, the risks arising from the use of IT may not be able to be addressed when such risks relate to risks for which substantive procedures alone do not provide sufficient appropriate audit evidence. In such circumstances, the auditor may need to consider the implications for the audit opinion.

### Identifying IT applications that are subject to risks arising from the use of IT

- A167. For the IT applications relevant to the information system, understanding the nature and complexity of the specific IT processes and general IT controls that the entity has in place may assist the auditor in determining which IT applications the entity is relying upon to accurately process and maintain the integrity of information in the entity's information system. Such IT applications may be subject to risks arising from the use of IT.
- A168. Identifying the IT applications that are subject to risks arising from the use of IT involves taking into account controls identified by the auditor because such controls may involve the use of IT or rely on IT. The auditor may focus on whether an IT application includes automated controls that management is relying on and that the auditor has identified, including controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence. The auditor may also consider how information is stored and processed in the information system relating to significant classes of transactions, account balances and disclosures and whether management is relying on general IT controls to maintain the integrity of that information.
- A169. The controls identified by the auditor may depend on system-generated reports, in which case the IT applications that produce those reports may be subject to risks arising from the use of IT. In other cases, the auditor may not plan to rely on controls over the system-generated reports and plan to directly test the inputs and outputs of such reports, in which case the auditor may not identify the related IT applications as being subject to risks arising from IT.

### Scalability

- A170. The extent of the auditor's understanding of the IT processes, including the extent to which the entity has general IT controls in place, will vary with the nature and the circumstances of the entity and its IT environment, as well as based on the nature and extent of controls identified by the auditor. The number of IT applications that are subject to risks arising from the use of IT also will vary based on these factors.

#### **Examples:**

- An entity that uses commercial software and does not have access to the source code to make any program changes is unlikely to have a process for program changes, but may have a process or procedures to configure the software (e.g., the chart of accounts, reporting parameters or thresholds). In addition, the entity

may have a process or procedures to manage access to the application (e.g., a designated individual with administrative access to the commercial software). In such circumstances, the entity is unlikely to have or need formalised general IT controls.

- In contrast, a larger entity may rely on IT to a great extent and the IT environment may involve multiple IT applications and the IT processes to manage the IT environment may be complex (e.g., a dedicated IT department exists that develops and implements program changes and manages access rights), including that the entity has implemented formalised general IT controls over its IT processes.
- When management is not relying on automated controls or general IT controls to process transactions or maintain the data, and the auditor has not identified any automated controls or other information processing controls (or any that depend on general IT controls), the auditor may plan to directly test any information produced by the entity involving IT and may not identify any IT applications that are subject to risks arising from the use of IT.
- When management relies on an IT application to process or maintain data and the volume of data is significant, and management relies upon the IT application to perform automated controls that the auditor has also identified, the IT application is likely to be subject to risks arising from the use of IT.

A171. When an entity has greater complexity in its IT environment, identifying the IT applications and other aspects of the IT environment, determining the related risks arising from the use of IT, and identifying general IT controls is likely to require the involvement of team members with specialised skills in IT. Such involvement is likely to be essential, and may need to be extensive, for complex IT environments.

Identifying other aspects of the IT environment that are subject to risks arising from the use of IT

A172. The other aspects of the IT environment that may be subject to risks arising from the use of IT include the network, operating system and databases, and, in certain circumstances, interfaces between IT applications. Other aspects of the IT environment are generally not identified when the auditor does not identify IT applications that are subject to risks arising from the use of IT. When the auditor has identified IT applications that are subject to risks arising from IT, other aspects of the IT environment (e.g., database, operating system, network) are likely to be identified because such aspects support and interact with the identified IT applications.

Identifying risks arising from the use of IT and general IT controls (Ref: Para. 26(c))

**Appendix 6** sets out considerations for understanding general IT controls.

A173. In identifying the risks arising from the use of IT, the auditor may consider the nature of the identified IT application or other aspect of the IT environment and the reasons for it being subject to risks arising from the use of IT. For some identified IT applications or other aspects of the IT environment, the auditor may identify applicable risks arising from

the use of IT that relate primarily to unauthorised access or unauthorised program changes, as well as that address risks related to inappropriate data changes (e.g., the risk of inappropriate changes to the data through direct database access or the ability to directly manipulate information).

A174. The extent and nature of the applicable risks arising from the use of IT vary depending on the nature and characteristics of the identified IT applications and other aspects of the IT environment. Applicable IT risks may result when the entity uses external or internal service providers for identified aspects of its IT environment (e.g., outsourcing the hosting of its IT environment to a third party or using a shared service center for central management of IT processes in a group). Applicable risks arising from the use of IT may also be identified related to cybersecurity. It is more likely that there will be more risks arising from the use of IT when the volume or complexity of automated application controls is higher and management is placing greater reliance on those controls for effective processing of transactions or the effective maintenance of the integrity of underlying information.

Evaluating the design, and determining implementation, of identified controls in the control activities component (Ref: Para 26(d))

A175. Evaluating the design of an identified control involves the auditor's consideration of whether the control, individually or in combination with other controls, is capable of effectively preventing, or detecting and correcting, material misstatements (i.e., the control objective).

A176. The auditor determines the implementation of an identified control by establishing that the control exists and that the entity is using it. There is little point in the auditor assessing the implementation of a control that is not designed effectively. Therefore, the auditor evaluates the design of a control first. An improperly designed control may represent a control deficiency.

A177. Risk assessment procedures to obtain audit evidence about the design and implementation of identified controls in the control activities component may include:

- Enquiring of entity personnel.
- Observing the application of specific controls.
- Inspecting documents and reports.

Enquiry alone, however, is not sufficient for such purposes.

A178. The auditor may expect, based on experience from the previous audit or based on current period risk assessment procedures, that management does not have effectively designed or implemented controls to address a significant risk. In such instances, the procedures performed to address the requirement in paragraph 26(d) may consist of determining that such controls have not been effectively designed or implemented. If the results of the procedures indicate that controls have been newly designed or implemented, the auditor is required to perform the procedures in paragraph 26(b)–(d) on the newly designed or implemented controls.

- A179. The auditor may conclude that a control, which is effectively designed and implemented, may be appropriate to test in order to take its operating effectiveness into account in designing substantive procedures. However, when a control is not designed or implemented effectively, there is no benefit in testing it. When the auditor plans to test a control, the information obtained about the extent to which the control addresses the risk(s) of material misstatement is an input to the auditor's control risk assessment at the assertion level.
- A180. Evaluating the design and determining the implementation of identified controls in the control activities component is not sufficient to test their operating effectiveness. However, for automated controls, the auditor may plan to test the operating effectiveness of automated controls by identifying and testing general IT controls that provide for the consistent operation of an automated control instead of performing tests of operating effectiveness on the automated controls directly. Obtaining audit evidence about the implementation of a manual control at a point in time does not provide audit evidence about the operating effectiveness of the control at other times during the period under audit. Tests of the operating effectiveness of controls, including tests of indirect controls, are further described in ISA (NZ) 330.<sup>45</sup>
- A181. When the auditor does not plan to test the operating effectiveness of identified controls, the auditor's understanding may still assist in the design of the nature, timing and extent of substantive audit procedures that are responsive to the related risks of material misstatement.

**Example:**

The results of these risk assessment procedures may provide a basis for the auditor's consideration of possible deviations in a population when designing audit samples.

*Control Deficiencies Within the Entity's System of Internal Control* (Ref: Para. 27)

- A182. In performing the evaluations of each of the components of the entity's system of internal control,<sup>46</sup> the auditor may determine that certain of the entity's policies in a component are not appropriate to the nature and circumstances of the entity. Such a determination may be an indicator that assists the auditor in identifying control deficiencies. If the auditor has identified one or more control deficiencies, the auditor may consider the effect of those control deficiencies on the design of further audit procedures in accordance with ISA (NZ) 330.
- A183. If the auditor has identified one or more control deficiencies, ISA (NZ) 265<sup>47</sup> requires the auditor to determine whether, individually or in combination, the deficiencies constitute a

<sup>45</sup> ISA (NZ) 330, paragraphs 8–11

<sup>46</sup> Paragraphs 21(b), 22(b), 24(c), 25(c) and 26(d)

<sup>47</sup> ISA (NZ) 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*, paragraph 8

significant deficiency. The auditor uses professional judgement in determining whether a deficiency represents a significant control deficiency.<sup>48</sup>

**Examples:**

Circumstances that may indicate a significant control deficiency exists include matters such as:

- The identification of fraud of any magnitude that involves senior management;
- Identified internal processes that are inadequate relating to the reporting and communication of deficiencies noted by internal audit;
- Previously communicated deficiencies that are not corrected by management in a timely manner;
- Failure by management to respond to significant risks, for example, by not implementing controls over significant risks; and
- The restatement of previously issued financial statements.

**Identifying and Assessing the Risks of Material Misstatement** (Ref: Para. 28–37)

*Why the Auditor Identifies and Assesses the Risks of Material Misstatement*

A184. Risks of material misstatement are identified and assessed by the auditor in order to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence. This evidence enables the auditor to express an opinion on the financial statements at an acceptably low level of audit risk.

A185. Information gathered by performing risk assessment procedures is used as audit evidence to provide the basis for the identification and assessment of the risks of material misstatement. For example, the audit evidence obtained when evaluating the design of identified controls and determining whether those controls have been implemented in the control activities component, is used as audit evidence to support the risk assessment. Such evidence also provides a basis for the auditor to design overall responses to address the assessed risks of material misstatement at the financial statement level, as well as designing and performing further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement at the assertion level, in accordance with ISA (NZ) 330.

*Identifying Risks of Material Misstatement* (Ref: Para. 28)

A186. The identification of risks of material misstatement is performed before consideration of any related controls (i.e., the inherent risk), and is based on the auditor's preliminary consideration of misstatements that have a reasonable possibility of both occurring, and being material if they were to occur.<sup>49</sup>

<sup>48</sup> ISA (NZ) 265, paragraphs A6–A7 set out indicators of significant deficiencies, and matters to be considered in determining whether a deficiency, or a combination of deficiencies, in internal control constitute a significant deficiency.

<sup>49</sup> ISA (NZ) 200, paragraph A15a

A187. Identifying the risks of material misstatement also provides the basis for the auditor's determination of relevant assertions, which assists the auditor's determination of the significant classes of transactions, account balances and disclosures.

### *Assertions*

#### Why the Auditor Uses Assertions

A188. In identifying and assessing the risks of material misstatement, the auditor uses assertions to consider the different types of potential misstatements that may occur. Assertions for which the auditor has identified related risks of material misstatement are relevant assertions.

#### The Use of Assertions

A189. In identifying and assessing the risks of material misstatement, the auditor may use the categories of assertions as described in paragraph A190(a)–(b) below or may express them differently provided all aspects described below have been covered. The auditor may choose to combine the assertions about classes of transactions and events, and related disclosures, with the assertions about account balances, and related disclosures.

A190. Assertions used by the auditor in considering the different types of potential misstatements that may occur may fall into the following categories:

- (a) Assertions about classes of transactions and events, and related disclosures, for the period under audit:
  - (i) Occurrence—transactions and events that have been recorded or disclosed have occurred, and such transactions and events pertain to the entity.
  - (ii) Completeness—all transactions and events that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
  - (iii) Accuracy—amounts and other data relating to recorded transactions and events have been recorded appropriately, and related disclosures have been appropriately measured and described.
  - (iv) Cutoff—transactions and events have been recorded in the correct accounting period.
  - (v) Classification—transactions and events have been recorded in the proper accounts.
  - (vi) Presentation—transactions and events are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.
- (b) Assertions about account balances, and related disclosures, at the period end:
  - (i) Existence—assets, liabilities and equity interests exist.

- (ii) Rights and obligations—the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
- (iii) Completeness—all assets, liabilities and equity interests that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
- (iv) Accuracy, valuation and allocation—assets, liabilities and equity interests have been included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments have been appropriately recorded, and related disclosures have been appropriately measured and described.
- (v) Classification—assets, liabilities and equity interests have been recorded in the proper accounts.
- (vi) Presentation—assets, liabilities and equity interests are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.

A191. The assertions described in paragraph A190(a)–(b) above, adapted as appropriate, may also be used by the auditor in considering the different types of misstatements that may occur in disclosures not directly related to recorded classes of transactions, events or account balances.

**Example:**

An example of such a disclosure includes where the entity may be required by the applicable financial reporting framework to describe its exposure to risks arising from financial instruments, including how the risks arise; the objectives, policies and processes for managing the risks; and the methods used to measure the risks.

### Considerations Specific to Public Sector Entities

A192. When making assertions about the financial statements of public sector entities, in addition to those assertions set out in paragraph A190(a)–(b), management may often assert that transactions and events have been carried out in accordance with law, regulation or other authority. Such assertions may fall within the scope of the financial statement audit.

### *Risks of Material Misstatement at the Financial Statement Level* (Ref: Para. 28(a) and 30)

#### Why the Auditor Identifies and Assesses Risks of Material Misstatement at the Financial Statement Level

A193. The auditor identifies risks of material misstatement at the financial statement level to determine whether the risks have a pervasive effect on the financial statements, and would therefore require an overall response in accordance with ISA (NZ) 330.<sup>50</sup>

<sup>50</sup> ISA (NZ) 330, paragraph 5

A194. In addition, risks of material misstatement at the financial statement level may also affect individual assertions, and identifying these risks may assist the auditor in assessing risks of material misstatement at the assertion level, and in designing further audit procedures to address the identified risks.

### Identifying and Assessing Risks of Material Misstatement at the Financial Statement Level

A195. Risks of material misstatement at the financial statement level refer to risks that relate pervasively to the financial statements as a whole, and potentially affect many assertions. Risks of this nature are not necessarily risks identifiable with specific assertions at the class of transactions, account balance or disclosure level (e.g., risk of management override of controls). Rather, they represent circumstances that may pervasively increase the risks of material misstatement at the assertion level. The auditor's evaluation of whether risks identified relate pervasively to the financial statements supports the auditor's assessment of the risks of material misstatement at the financial statement level. In other cases, a number of assertions may also be identified as susceptible to the risk, and may therefore affect the auditor's risk identification and assessment of risks of material misstatement at the assertion level.

**Example:**

The entity faces operating losses and liquidity issues and is reliant on funding that has not yet been secured. In such a circumstance, the auditor may determine that the going concern basis of accounting gives rise to a risk of material misstatement at the financial statement level. In this situation, the accounting framework may need to be applied using a liquidation basis, which would likely affect all assertions pervasively.

A196. The auditor's identification and assessment of risks of material misstatement at the financial statement level is influenced by the auditor's understanding of the entity's system of internal control, in particular the auditor's understanding of the control environment, the entity's risk assessment process and the entity's process to monitor the system of internal control, and:

- The outcome of the related evaluations required by paragraphs 21(b), 22(b), 24(c) and 25(c); and
- Any control deficiencies identified in accordance with paragraph 27.

In particular, risks at the financial statement level may arise from deficiencies in the control environment or from external events or conditions such as declining economic conditions.

A197. Risks of material misstatement due to fraud may be particularly relevant to the auditor's consideration of the risks of material misstatement at the financial statement level.

**Example:**

The auditor understands from enquiries of management that the entity's financial statements are to be used in discussions with lenders in order to secure further financing to maintain working capital. The auditor may therefore determine that there is a greater susceptibility to misstatement due to fraud risk factors that affect inherent risk (i.e., the



susceptibility of the financial statements to material misstatement because of the risk of fraudulent financial reporting, such as overstatement of assets and revenue and under-statement of liabilities and expenses to ensure that financing will be obtained).

A198. The auditor's understanding, including the related evaluations, of the control environment and other components of the system of internal control may raise doubts about the auditor's ability to obtain audit evidence on which to base the audit opinion or be cause for withdrawal from the engagement where withdrawal is possible under applicable law or regulation.

**Examples:**

- As a result of evaluating the entity's control environment, the auditor has concerns about the integrity of the entity's management, which may be so serious as to cause the auditor to conclude that the risk of intentional misrepresentation by management in the financial statements is such that an audit cannot be conducted.
- As a result of evaluating the entity's information system and communication, the auditor determines that significant changes in the IT environment have been poorly managed, with little oversight from management and those charged with governance. The auditor concludes that there are significant concerns about the condition and reliability of the entity's accounting records. In such circumstances, the auditor may determine that it is unlikely that sufficient appropriate audit evidence will be available to support an unmodified opinion on the financial statements.

A199. ISA (NZ) 705 (Revised)<sup>51</sup> establishes requirements and provides guidance in determining whether there is a need for the auditor to express a qualified opinion or disclaim an opinion or, as may be required in some cases, to withdraw from the engagement where withdrawal is possible under applicable law or regulation.

### Considerations Specific to Public Sector Entities

A200. For public sector entities, the identification of risks at the financial statement level may include consideration of matters related to the political climate, public interest and programme sensitivity.

### *Risks of Material Misstatement at the Assertion Level (Ref: Para. 28(b))*

**Appendix 2** sets out examples, in the context of inherent risk factors, of events or conditions that may indicate susceptibility to misstatement that may be material.

A201. Risks of material misstatements that do not relate pervasively to the financial statements are risks of material misstatement at the assertion level.

<sup>51</sup> ISA (NZ) 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

*Relevant Assertions and Significant Classes of Transactions, Account Balances and Disclosures*  
(Ref: Para. 29)

Why Relevant Assertions and Significant Classes of Transactions, Account Balances and Disclosures Are Determined

A202. Determining relevant assertions and the significant classes of transactions, account balances and disclosures provides the basis for the scope of the auditor's understanding of the entity's information system required to be obtained in accordance with paragraph 25(a). This understanding may further assist the auditor in identifying and assessing risks of material misstatement (see A86).

Automated Tools and Techniques

A203. The auditor may use automated techniques to assist in the identification of significant classes of transactions, account balances and disclosures.

**Examples:**

- An entire population of transactions may be analysed using automated tools and techniques to understand their nature, source, size and volume. By applying automated techniques, the auditor may, for example, identify that an account with a zero balance at period end was comprised of numerous offsetting transactions and journal entries occurring during the period, indicating that the account balance or class of transactions may be significant (e.g., a payroll clearing account). This same payroll clearing account may also identify expense reimbursements to management (and other employees), which could be a significant disclosure due to these payments being made to related parties.
- By analysing the flows of an entire population of revenue transactions, the auditor may more easily identify a significant class of transactions that had not previously been identified.

Disclosures that May Be Significant

A204. Significant disclosures include both quantitative and qualitative disclosures for which there is one or more relevant assertions. Examples of disclosures that have qualitative aspects and that may have relevant assertions and may therefore be considered significant by the auditor include disclosures about:

- Liquidity and debt covenants of an entity in financial distress.
- Events or circumstances that have led to the recognition of an impairment loss.
- Key sources of estimation uncertainty, including assumptions about the future.
- The nature of a change in accounting policy, and other relevant disclosures required by the applicable financial reporting framework, where, for example, new financial reporting requirements are expected to have a significant impact on the financial position and financial performance of the entity.

- Share-based payment arrangements, including information about how any amounts recognised were determined, and other relevant disclosures.
- Related parties, and related party transactions.
- Sensitivity analysis, including the effects of changes in assumptions used in the entity's valuation techniques intended to enable users to understand the underlying measurement uncertainty of a recorded or disclosed amount.

*Assessing Risks of Material Misstatement at the Assertion Level*

Assessing Inherent Risk (Ref: Para. 31–33)

Assessing the likelihood and magnitude of misstatement (Ref: Para: 31)

Why the auditor assesses likelihood and magnitude of misstatement

- A205. The auditor assesses the likelihood and magnitude of misstatement for identified risks of material misstatement because the significance of the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement were the misstatement to occur determines where on the spectrum of inherent risk the identified risk is assessed, which informs the auditor's design of further audit procedures to address the risk.
- A206. Assessing the inherent risk of identified risks of material misstatement also assists the auditor in determining significant risks. The auditor determines significant risks because specific responses to significant risks are required in accordance with ISA (NZ) 330 and other ISAs (NZ).
- A207. Inherent risk factors influence the auditor's assessment of the likelihood and magnitude of misstatement for the identified risks of material misstatement at the assertion level. The greater the degree to which a class of transactions, account balance or disclosure is susceptible to material misstatement, the higher the inherent risk assessment is likely to be. Considering the degree to which inherent risk factors affect the susceptibility of an assertion to misstatement assists the auditor in appropriately assessing inherent risk for risks of material misstatement at the assertion level and in designing a more precise response to such a risk.

Spectrum of inherent risk

- A208. In assessing inherent risk, the auditor uses professional judgement in determining the significance of the combination of the likelihood and magnitude of a misstatement.
- A209. The assessed inherent risk relating to a particular risk of material misstatement at the assertion level represents a judgement within a range, from lower to higher, on the spectrum of inherent risk. The judgement about where in the range inherent risk is assessed may vary based on the nature, size and complexity of the entity, and takes into account the assessed likelihood and magnitude of the misstatement and inherent risk factors.
- A210. In considering the likelihood of a misstatement, the auditor considers the possibility that a misstatement may occur, based on consideration of the inherent risk factors.

- A211. In considering the magnitude of a misstatement, the auditor considers the qualitative and quantitative aspects of the possible misstatement (i.e., misstatements in assertions about classes of transactions, account balances or disclosures may be judged to be material due to size, nature or circumstances).
- A212. The auditor uses the significance of the combination of the likelihood and magnitude of a possible misstatement in determining where on the spectrum of inherent risk (i.e., the range) inherent risk is assessed. The higher the combination of likelihood and magnitude, the higher the assessment of inherent risk; the lower the combination of likelihood and magnitude, the lower the assessment of inherent risk.
- A213. For a risk to be assessed as higher on the spectrum of inherent risk, it does not mean that both the magnitude and likelihood need to be assessed as high. Rather, it is the intersection of the magnitude and likelihood of the material misstatement on the spectrum of inherent risk that will determine whether the assessed inherent risk is higher or lower on the spectrum of inherent risk. A higher inherent risk assessment may also arise from different combinations of likelihood and magnitude, for example a higher inherent risk assessment could result from a lower likelihood but a very high magnitude.
- A214. In order to develop appropriate strategies for responding to risks of material misstatement, the auditor may designate risks of material misstatement within categories along the spectrum of inherent risk, based on their assessment of inherent risk. These categories may be described in different ways. Regardless of the method of categorisation used, the auditor's assessment of inherent risk is appropriate when the design and implementation of further audit procedures to address the identified risks of material misstatement at the assertion level is appropriately responsive to the assessment of inherent risk and the reasons for that assessment.

#### Pervasive Risks of Material Misstatement at the Assertion Level (Ref: Para 31(b))

- A215. In assessing the identified risks of material misstatement at the assertion level, the auditor may conclude that some risks of material misstatement relate more pervasively to the financial statements as a whole and potentially affect many assertions, in which case the auditor may update the identification of risks of material misstatement at the financial statement level.
- A216. In circumstances in which risks of material misstatement are identified as financial statement level risks due to their pervasive effect on a number of assertions, and are identifiable with specific assertions, the auditor is required to take into account those risks when assessing inherent risk for risks of material misstatement at the assertion level.

#### Considerations Specific to Public Sector Entities

- A217. In exercising professional judgement as to the assessment of the risk of material misstatement, public sector auditors may consider the complexity of the regulations and directives, and the risks of non-compliance with authorities.

## Significant Risks (Ref: Para. 32)

## Why significant risks are determined and the implications for the audit

A218. The determination of significant risks allows for the auditor to focus more attention on those risks that are on the upper end of the spectrum, through the performance of certain required responses, including:

- Controls that address significant risks are required to be identified in accordance with paragraph 26(a)(i), with a requirement to evaluate whether the control has been designed effectively and implemented in accordance with paragraph 26(d).
- ISA (NZ) 330 requires controls that address significant risks to be tested in the current period (when the auditor intends to rely on the operating effectiveness of such controls) and substantive procedures to be planned and performed that are specifically responsive to the identified significant risk.<sup>52</sup>
- ISA (NZ) 330 requires the auditor to obtain more persuasive audit evidence the higher the auditor's assessment of risk.<sup>53</sup>
- ISA (NZ) 260 (Revised) requires communicating with those charged with governance about the significant risks identified by the auditor.<sup>54</sup>
- ISA (NZ) 701 requires the auditor to take into account significant risks when determining those matters that required significant auditor attention, which are matters that may be key audit matters.<sup>55</sup>
- Timely review of audit documentation by the engagement partner at the appropriate stages during the audit allows significant matters, including significant risks, to be resolved on a timely basis to the engagement partner's satisfaction on or before the date of the auditor's report.<sup>56</sup>
- ISA (NZ) 600 requires more involvement by the group engagement partner if the significant risk relates to a component in a group audit and for the group engagement team to direct the work required at the component by the component auditor.<sup>57</sup>

## Determining significant risks

A219. In determining significant risks, the auditor may first identify those assessed risks of material misstatement that have been assessed higher on the spectrum of inherent risk to form the basis for considering which risks may be close to the upper end. Being close to the upper end of the spectrum of inherent risk will differ from entity to entity, and will not

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<sup>52</sup> ISA (NZ) 330, paragraphs 15 and 21

<sup>53</sup> ISA (NZ) 330, paragraph 7(b)

<sup>54</sup> ISA (NZ) 260 (Revised), paragraph 15

<sup>55</sup> ISA (NZ) 701, *Communicating Key Audit Matters in the Independent Auditor's Report*, paragraph 9

<sup>56</sup> ISA (NZ) 220, paragraphs 17 and A19

<sup>57</sup> ISA (NZ) 600, paragraphs 30 and 31

necessarily be the same for an entity period on period. It may depend on the nature and circumstances of the entity for which the risk is being assessed.

A220. The determination of which of the assessed risks of material misstatement are close to the upper end of the spectrum of inherent risk, and are therefore significant risks, is a matter of professional judgement, unless the risk is of a type specified to be treated as a significant risk in accordance with the requirements of another ISA (NZ). ISA (NZ) 240 provides further requirements and guidance in relation to the identification and assessment of the risks of material misstatement due to fraud.<sup>58</sup>

**Example:**

- Cash at a supermarket retailer would ordinarily be determined to be a high likelihood of possible misstatement (due to the risk of cash being misappropriated), however the magnitude would typically be very low (due to the low levels of physical cash handled in the stores). The combination of these two factors on the spectrum of inherent risk would be unlikely to result in the existence of cash being determined to be a significant risk.
- An entity is in negotiations to sell a business segment. The auditor considers the effect on goodwill impairment, and may determine there is a higher likelihood of possible misstatement and a higher magnitude due to the impact of inherent risk factors of subjectivity, uncertainty and susceptibility to management bias or other fraud risk factors. This may result in goodwill impairment being determined to be a significant risk.

A221. The auditor also takes into the account the relative effects of inherent risk factors when assessing inherent risk. The lower the effect of inherent risk factors, the lower the assessed risk is likely to be. Risks of material misstatement that may be assessed as having higher inherent risk and may therefore be determined to be a significant risk, may arise from matters such as the following:

- Transactions for which there are multiple acceptable accounting treatments such that subjectivity is involved.
- Accounting estimates that have high estimation uncertainty or complex models.
- Complexity in data collection and processing to support account balances.
- Account balances or quantitative disclosures that involve complex calculations.
- Accounting principles that may be subject to differing interpretation.
- Changes in the entity's business that involve changes in accounting, for example, mergers and acquisitions.

<sup>58</sup> ISA (NZ) 240, paragraphs 26–28

## Risks for Which Substantive Procedures Alone Do Not Provide Sufficient Appropriate Audit Evidence (Ref: Para. 33)

Why risks for which substantive procedures alone do not provide sufficient appropriate audit evidence are required to be identified

A222. Due to the nature of a risk of material misstatement, and the control activities that address that risk, in some circumstances the only way to obtain sufficient appropriate audit evidence is to test the operating effectiveness of controls. Accordingly, there is a requirement for the auditor to identify any such risks because of the implications for the design and performance of further audit procedures in accordance with ISA (NZ) 330 to address risks of material misstatement at the assertion level.

A223. Paragraph 26(a)(iii) also requires the identification of controls that address risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence because the auditor is required, in accordance with ISA (NZ) 330,<sup>59</sup> to design and perform tests of such controls.

Determining risks for which substantive procedures alone do not provide sufficient appropriate audit evidence

A224. Where routine business transactions are subject to highly automated processing with little or no manual intervention, it may not be possible to perform only substantive procedures in relation to the risk. This may be the case in circumstances where a significant amount of an entity's information is initiated, recorded, processed, or reported only in electronic form such as in an information system that involves a high degree of integration across its IT applications. In such cases:

- Audit evidence may be available only in electronic form, and its sufficiency and appropriateness usually depend on the effectiveness of controls over its accuracy and completeness.
- The potential for improper initiation or alteration of information to occur and not be detected may be greater if appropriate controls are not operating effectively.

### **Example:**

It is typically not possible to obtain sufficient appropriate audit evidence relating to revenue for a telecommunications entity based on substantive procedures alone. This is because the evidence of call or data activity does not exist in a form that is observable. Instead, substantial controls testing is typically performed to determine that the origination and completion of calls, and data activity is correctly captured (e.g., minutes of a call or volume of a download) and recorded correctly in the entity's billing system.

A225. ISA (NZ) 540 (Revised) provides further guidance related to accounting estimates about risks for which substantive procedures alone do not provide sufficient appropriate audit

<sup>59</sup> ISA (NZ) 330, paragraph 8

evidence.<sup>60</sup> In relation to accounting estimates this may not be limited to automated processing, but may also be applicable to complex models.

*Assessing Control Risk* (Ref: Para. 34)

A226. The auditor's plans to test the operating effectiveness of controls is based on the expectation that controls are operating effectively, and this will form the basis of the auditor's assessment of control risk. The initial expectation of the operating effectiveness of controls is based on the auditor's evaluation of the design, and the determination of implementation, of the identified controls in the control activities component. Once the auditor has tested the operating effectiveness of the controls in accordance with ISA (NZ) 330, the auditor will be able to confirm the initial expectation about the operating effectiveness of controls. If the controls are not operating effectively as expected, then the auditor will need to revise the control risk assessment in accordance with paragraph 37.

A227. The auditor's assessment of control risk may be performed in different ways depending on preferred audit techniques or methodologies, and may be expressed in different ways.

A228. If the auditor plans to test the operating effectiveness of controls, it may be necessary to test a combination of controls to confirm the auditor's expectation that the controls are operating effectively. The auditor may plan to test both direct and indirect controls, including general IT controls, and, if so, take into account the combined expected effect of the controls when assessing control risk. To the extent that the control to be tested does not fully address the assessed inherent risk, the auditor determines the implications on the design of further audit procedures to reduce audit risk to an acceptably low level.

A229. When the auditor plans to test the operating effectiveness of an automated control, the auditor may also plan to test the operating effectiveness of the relevant general IT controls that support the continued functioning of that automated control to address the risks arising from the use of IT, and to provide a basis for the auditor's expectation that the automated control operated effectively throughout the period. When the auditor expects related general IT controls to be ineffective, this determination may affect the auditor's assessment of control risk at the assertion level and the auditor's further audit procedures may need to include substantive procedures to address the applicable risks arising from the use of IT. Further guidance about the procedures that the auditor may perform in these circumstances is provided in ISA (NZ) 330.<sup>61</sup>

*Evaluating the Audit Evidence Obtained from the Risk Assessment Procedures* (Ref: Para 35)

**Why the Auditor Evaluates the Audit Evidence from the Risk Assessment Procedures**

A230. Audit evidence obtained from performing risk assessment procedures provides the basis for the identification and assessment of the risks of material misstatement. This provides the basis for the auditor's design of the nature, timing and extent of further audit procedures responsive to the assessed risks of material misstatement, at the assertion level,

<sup>60</sup> ISA (NZ) 540 (Revised), paragraphs A87–A89

<sup>61</sup> ISA (NZ) 330, paragraphs A29–A30



in accordance with ISA (NZ) 330. Accordingly, the audit evidence obtained from the risk assessment procedures provides a basis for the identification and assessment of risks of material misstatement whether due to fraud or error, at the financial statement and assertion levels.

### The Evaluation of the Audit Evidence

A231. Audit evidence from risk assessment procedures comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions.<sup>62</sup>

### Professional Scepticism

A232. In evaluating the audit evidence from the risk assessment procedures, the auditor considers whether sufficient understanding about the entity and its environment, the applicable financial reporting framework and the entity's system of internal control has been obtained to be able to identify the risks of material misstatement, as well as whether there is any evidence that is contradictory that may indicate a risk of material misstatement.

### *Classes of Transactions, Account Balances and Disclosures that Are Not Significant, but Which Are Material (Ref: Para. 36)*

A233. As explained in ISA (NZ) 320,<sup>63</sup> materiality and audit risk are considered when identifying and assessing the risks of material misstatement in classes of transactions, account balances and disclosures. The auditor's determination of materiality is a matter of professional judgement, and is affected by the auditor's perception of the financial information needs of users of the financial statements.<sup>64</sup> For the purpose of this ISA (NZ) and paragraph 18 of ISA (NZ) 330, classes of transactions, account balances or disclosures are material if omitting, misstating or obscuring information about them could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements as a whole.

A234. There may be classes of transactions, account balances or disclosures that are material but have not been determined to be significant classes of transactions, account balances or disclosures (i.e., there are no relevant assertions identified).

#### **Example:**

The entity may have a disclosure about executive compensation for which the auditor has not identified a risk of material misstatement. However, the auditor may determine that this disclosure is material based on the considerations in paragraph A233.

A235. Audit procedures to address classes of transactions, account balances or disclosures that are material but are not determined to be significant are addressed in ISA (NZ) 330.<sup>65</sup>

<sup>62</sup> ISA (NZ) 500, paragraph A1

<sup>63</sup> ISA (NZ) 320, paragraph A1

<sup>64</sup> ISA (NZ) 320, paragraph 4

<sup>65</sup> ISA (NZ) 330, paragraph 18

When a class of transactions, account balance or disclosure is determined to be significant as required by paragraph 29, the class of transactions, account balance or disclosure is also a material class of transactions, account balance or disclosure for the purposes of paragraph 18 of ISA (NZ) 330.

#### Revision of Risk Assessment (Ref: Para. 37)

A236. During the audit, new or other information may come to the auditor's attention that differs significantly from the information on which the risk assessment was based.

##### **Example:**

The entity's risk assessment may be based on an expectation that certain controls are operating effectively. In performing tests of those controls, the auditor may obtain audit evidence that they were not operating effectively at relevant times during the audit. Similarly, in performing substantive procedures the auditor may detect misstatements in amounts or frequency greater than is consistent with the auditor's risk assessments. In such circumstances, the risk assessment may not appropriately reflect the true circumstances of the entity and the further planned audit procedures may not be effective in detecting material misstatements. Paragraphs 16 and 17 of ISA (NZ) 330 provide further guidance about evaluating the operating effectiveness of controls.

#### Documentation (Ref: Para. 38)

A237. For recurring audits, certain documentation may be carried forward, updated as necessary to reflect changes in the entity's business or processes.

A238. ISA (NZ) 230 notes that, among other considerations, although there may be no single way in which the auditor's exercise of professional scepticism is documented, the audit documentation may nevertheless provide evidence of the auditor's exercise of professional scepticism.<sup>66</sup> For example, when the audit evidence obtained from risk assessment procedures includes evidence that both corroborates and contradicts management's assertions, the documentation may include how the auditor evaluated that evidence, including the professional judgements made in evaluating whether the audit evidence provides an appropriate basis for the auditor's identification and assessment of the risks of material misstatement. Examples of other requirements in this ISA (NZ) for which documentation may provide evidence of the exercise of professional scepticism by the auditor include:

- Paragraph 13, which requires the auditor to design and perform risk assessment procedures in a manner that is not biased towards obtaining audit evidence that may corroborate the existence of risks or towards excluding audit evidence that may contradict the existence of risks;
- Paragraph 17, which requires a discussion among key engagement team members of the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement;

<sup>66</sup> ISA (NZ) 230, paragraph A7

- Paragraphs 19(b) and 20, which require the auditor to obtain an understanding of the reasons for any changes to the entity's accounting policies and to evaluate whether the entity's accounting policies are appropriate and consistent with the applicable financial reporting framework;
- Paragraphs 21(b), 22(b), 23(b), 24(c), 25(c), 26(d) and 27, which require the auditor to evaluate, based on the required understanding obtained, whether the components of the entity's system of internal control are appropriate to the entity's circumstances considering the nature and complexity of the entity, and to determine whether one of more control deficiencies have been identified;
- Paragraph 35, which requires the auditor to take into account all audit evidence obtained from the risk assessment procedures, whether corroborative or contradictory to assertions made by management, and to evaluate whether the audit evidence obtained from the risk assessment procedures provides an appropriate basis for the identification and assessment of the risks of material misstatement; and
- Paragraph 36, which requires the auditor to evaluate, when applicable, whether the auditor's determination that there are no risks of material misstatement for a material class of transactions, account balance or disclosure remains appropriate.

### Scalability

A239. The manner in which the requirements of paragraph 38 are documented is for the auditor to determine using professional judgement.

A240. More detailed documentation, that is sufficient to enable an experienced auditor, having no previous experience with the audit, to understand the nature, timing and extent of the audit procedures performed, may be required to support the rationale for difficult judgements made.

A241. For the audits of less complex entities, the form and extent of documentation may be simple and relatively brief. The form and extent of the auditor's documentation is influenced by the nature, size and complexity of the entity and its system of internal control, availability of information from the entity and the audit methodology and technology used in the course of the audit. It is not necessary to document the entirety of the auditor's understanding of the entity and matters related to it. Key elements<sup>67</sup> of understanding documented by the auditor may include those on which the auditor based the assessment of the risks of material misstatement. However, the auditor is not required to document every inherent risk factor that was taken into account in identifying and assessing the risks of material misstatement at the assertion level.

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<sup>67</sup> ISA (NZ) 230, paragraph 8

**Example:**

In audits of less complex entities audit documentation may be incorporated in the auditor's documentation of the overall strategy and audit plan.<sup>68</sup> Similarly, for example, the results of the risk assessment may be documented separately, or may be documented as part of the auditor's documentation of further audit procedures.<sup>69</sup>

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<sup>68</sup> ISA (NZ) 300, *Planning an Audit of Financial Statements*, paragraphs 7, 9 and A11

<sup>69</sup> ISA (NZ) 330, paragraph 28

## Considerations for Understanding the Entity and its Business Model

This appendix explains the objectives and scope of the entity's business model and provides examples of matters that the auditor may consider in understanding the activities of the entity that may be included in the business model. The auditor's understanding of the entity's business model, and how it is affected by its business strategy and business objectives, may assist the auditor in identifying business risks that may have an effect on the financial statements. In addition, this may assist the auditor in identifying risks of material misstatement.

### Objectives and Scope of an Entity's Business Model

1. An entity's business model describes how an entity considers, for example its organisational structure, operations or scope of activities, business lines (including competitors and customers thereof), processes, growth opportunities, globalisation, regulatory requirements and technologies. The entity's business model describes how the entity creates, preserves and captures financial or broader value, for its stakeholders.
2. Strategies are the approaches by which management plans to achieve the entity's objectives, including how the entity plans to address the risks and opportunities that it faces. An entity's strategies are changed over time by management, to respond to changes in its objectives and in the internal and external circumstances in which it operates.
3. A description of a business model typically includes:
  - The scope of the entity's activities, and why it does them.
  - The entity's structure and scale of its operations.
  - The markets or geographical or demographic spheres, and parts of the value chain, in which it operates, how it engages with those markets or spheres (main products, customer segments and distribution methods), and the basis on which it competes.
  - The entity's business or operating processes (e.g., investment, financing and operating processes) employed in performing its activities, focusing on those parts of the business processes that are important in creating, preserving or capturing value.
  - The resources (e.g., financial, human, intellectual, environmental and technological) and other inputs and relationships (e.g., customers, competitors, suppliers and employees) that are necessary or important to its success.
  - How the entity's business model integrates the use of IT in its interactions with customers, suppliers, lenders and other stakeholders through IT interfaces and other technologies.
4. A business risk may have an immediate consequence for the risk of material misstatement for classes of transactions, account balances, and disclosures at the assertion level or the financial statement level. For example, the business risk arising from a significant fall in real estate market values may increase the risk of material misstatement associated with the valuation assertion for a lender of medium-term real estate backed loans. However, the same

risk, particularly in combination with a severe economic downturn that concurrently increases the underlying risk of lifetime credit losses on its loans, may also have a longer-term consequence. The resulting net exposure to credit losses may cast significant doubt on the entity's ability to continue as a going concern. If so, this could have implications for management's, and the auditor's, conclusion as to the appropriateness of the entity's use of the going concern basis of accounting, and determination as to whether a material uncertainty exists. Whether a business risk may result in a risk of material misstatement is, therefore, considered in light of the entity's circumstances. Examples of events and conditions that may give rise to the existence of risks of material misstatement are indicated in **Appendix 2**.

### Activities of the Entity

5. Examples of matters that the auditor may consider when obtaining an understanding of the activities of the entity (included in the entity's business model) include:
  - (a) Business operations such as:
    - Nature of revenue sources, products or services, and markets, including involvement in electronic commerce such as Internet sales and marketing activities.
    - Conduct of operations (for example, stages and methods of production, or activities exposed to environmental risks).
    - Alliances, joint ventures, and outsourcing activities.
    - Geographic dispersion and industry segmentation.
    - Location of production facilities, warehouses, and offices, and location and quantities of inventories.
    - Key customers and important suppliers of goods and services, employment arrangements (including the existence of union contracts, pension and other post-employment benefits, share option or incentive bonus arrangements, and government regulation related to employment matters).
    - Research and development activities and expenditures.
    - Transactions with related parties.
  - (b) Investments and investment activities such as:
    - Planned or recently executed acquisitions or divestitures.
    - Investments and dispositions of securities and loans.
    - Capital investment activities.
    - Investments in non-consolidated entities, including non-controlled partnerships, joint ventures and non-controlled special-purpose entities.
  - (c) Financing and financing activities such as:
    - Ownership structure of major subsidiaries and associated entities, including consolidated and non-consolidated structures.

- Debt structure and related terms, including off-balance-sheet financing arrangements and leasing arrangements.
- Beneficial owners (local, foreign, business reputation and experience) and related parties.
- Use of derivative financial instruments.

### **Nature of Special-Purpose Entities**

6. A special-purpose entity (sometimes referred to as a special-purpose vehicle) is an entity that is generally established for a narrow and well-defined purpose, such as to effect a lease or a securitisation of financial assets, or to carry out research and development activities. It may take the form of a corporation, trust, partnership or unincorporated entity. The entity on behalf of which the special-purpose entity has been created may often transfer assets to the latter (for example, as part of a derecognition transaction involving financial assets), obtain the right to use the latter's assets, or perform services for the latter, while other parties may provide the funding to the latter. As ISA (NZ) 550 indicates, in some circumstances, a special-purpose entity may be a related party of the entity.<sup>70</sup>
7. Financial reporting frameworks often specify detailed conditions that are deemed to amount to control, or circumstances under which the special-purpose entity should be considered for consolidation. The interpretation of the requirements of such frameworks often demands a detailed knowledge of the relevant agreements involving the special-purpose entity.

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<sup>70</sup> ISA (NZ) 550, paragraph A7

## Understanding Inherent Risk Factors

This appendix provides further explanation about the inherent risk factors, as well as matters that the auditor may consider in understanding and applying the inherent risk factors in identifying and assessing the risks of material misstatement at the assertion level.

### The Inherent Risk Factors

1. Inherent risk factors are characteristics of events or conditions that affect susceptibility of an assertion about a class of transactions, account balance or disclosure, to misstatement, whether due to fraud or error, and 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 other fraud risk factors<sup>71</sup> insofar as they affect inherent risk. In obtaining the understanding of the entity and its environment, and the applicable financial reporting framework and entity's accounting policies, in accordance with paragraphs 19(a)–(b), the auditor also understands how inherent risk factors affect susceptibility of assertions to misstatement in the preparation of the financial statements.
2. Inherent risk factors relating to the preparation of information required by the applicable financial reporting framework (referred to in this paragraph as “required information”) include:
  - *Complexity*—arises either from the nature of the information or in the way that the required information is prepared, including when such preparation processes are more inherently difficult to apply. For example, complexity may arise:
    - In calculating supplier rebate provisions because it may be necessary to take into account different commercial terms with many different suppliers, or many interrelated commercial terms that are all relevant in calculating the rebates due; or
    - When there are many potential data sources, with different characteristics used in making an accounting estimate, the processing of that data involves many inter-related steps, and the data is therefore inherently more difficult to identify, capture, access, understand or process.
  - *Subjectivity*—arises from inherent limitations in the ability to prepare required information in an objective manner, due to limitations in the availability of knowledge or information, such that management may need to make an election or subjective judgement about the appropriate approach to take and about the resulting information to include in the financial statements. Because of different approaches to preparing the required information, different outcomes could result from appropriately applying the requirements of the applicable financial reporting framework. As limitations in knowledge or data increase, the subjectivity in the judgements that could be made by

<sup>71</sup> ISA (NZ) 240, paragraphs A24–A27



reasonably knowledgeable and independent individuals, and the diversity in possible outcomes of those judgements will also increase.

- *Change*—results from events or conditions that, over time, affect the entity’s business or the economic, accounting, regulatory, industry or other aspects of the environment in which it operates, when the effects of those events or conditions are reflected in the required information. Such events or conditions may occur during, or between, financial reporting periods. For example, change may result from developments in the requirements of the applicable financial reporting framework, or in the entity and its business model, or in the environment in which the entity operates. Such change may affect management’s assumptions and judgements, including as they relate to management’s selection of accounting policies or how accounting estimates are made or related disclosures are determined.
  - *Uncertainty*—arises when the required information cannot be prepared based only on sufficiently precise and comprehensive data that is verifiable through direct observation. In these circumstances, an approach may need to be taken that applies the available knowledge to prepare the information using sufficiently precise and comprehensive observable data, to the extent available, and reasonable assumptions supported by the most appropriate available data, when it is not. Constraints on the availability of knowledge or data, which are not within the control of management (subject to cost constraints where applicable) are sources of uncertainty and their effect on the preparation of the required information cannot be eliminated. For example, estimation uncertainty arises when the required monetary amount cannot be determined with precision and the outcome of the estimate is not known before the date the financial statements are finalised.
  - *Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk*—susceptibility to management bias results from conditions that create susceptibility to intentional or unintentional failure by management to maintain neutrality in preparing the information. Management bias is often associated with certain conditions that have the potential to give rise to management not maintaining neutrality in exercising judgement (indicators of potential management bias), which could lead to a material misstatement of the information that would be fraudulent if intentional. Such indicators include incentives or pressures insofar as they affect inherent risk (for example, as a result of motivation to achieve a desired result, such as a desired profit target or capital ratio), and opportunity, not to maintain neutrality. Factors relevant to the susceptibility to misstatement due to fraud in the form of fraudulent financial reporting or misappropriation of assets are described in paragraphs A1 to A5 of ISA (NZ) 240.
3. When complexity is an inherent risk factor, there may be an inherent need for more complex processes in preparing the information, and such processes may be inherently more difficult to apply. As a result, applying them may require specialised skills or knowledge, and may require the use of a management’s expert.
  4. When management judgement is more subjective, the susceptibility to misstatement due to management bias, whether unintentional or intentional, may also increase. For example, significant management judgement may be involved in making accounting estimates that

have been identified as having high estimation uncertainty, and conclusions regarding methods, data and assumptions may reflect unintentional or intentional management bias.

### Examples of Events or Conditions that May Give Rise to the Existence of Risks of Material Misstatement

5. The following are examples of events (including transactions) and conditions that may indicate the existence of risks of material misstatement in the financial statements, at the financial statement level or the assertion level. The examples provided by inherent risk factor cover a broad range of events and conditions; however, not all events and conditions are relevant to every audit engagement and the list of examples is not necessarily complete. The events and conditions have been categorised by the inherent risk factor that may have the greatest effect in the circumstances. Importantly, due to the interrelationships among inherent risk factors, the example events and conditions also are likely to be subject to, or affected by, other inherent risk factors to varying degrees.

| Relevant Inherent Risk Factor: | Examples of Events and Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:  |
|--------------------------------|--|
| Complexity                     | <p>Regulatory:</p> <ul style="list-style-type: none"> <li>Operations that are subject to a high degree of complex regulation.</li> </ul> <p>Business model:</p> <ul style="list-style-type: none"> <li>The existence of complex alliances and joint ventures.</li> </ul> <p>Applicable financial reporting framework:</p> <ul style="list-style-type: none"> <li>Accounting measurements that involve complex processes.</li> </ul> <p>Transactions:</p> <ul style="list-style-type: none"> <li>Use of off-balance sheet finance, special-purpose entities, and other complex financing arrangements.</li> </ul> |
| Subjectivity                   | <p>Applicable financial reporting framework:</p> <ul style="list-style-type: none"> <li>A wide range of possible measurement criteria of an accounting estimate. For example, management's recognition of depreciation or construction income and expenses.</li> <li>Management's selection of a valuation technique or model for a non-current asset, such as investment properties.</li> </ul>   |
| Change                         | <p>Economic conditions:</p> <ul style="list-style-type: none"> <li>Operations in regions that are economically unstable, for example, countries with significant currency devaluation or highly inflationary economies.</li> </ul> <p>Markets:</p>   |

| Relevant<br>Inherent Risk<br>Factor: | Examples of Events and Conditions That May Indicate the Existence of<br>Risks of Material Misstatement at the Assertion Level:   |
|--------------------------------------|--|
|                                      | <ul style="list-style-type: none"> <li>• Operations exposed to volatile markets, for example, futures trading.</li> </ul> <p>Customer loss:</p> <ul style="list-style-type: none"> <li>• Going concern and liquidity issues including loss of significant customers.</li> </ul> <p>Industry model:</p> <ul style="list-style-type: none"> <li>• Changes in the industry in which the entity operates.</li> </ul> <p>Business model:</p> <ul style="list-style-type: none"> <li>• Changes in the supply chain.</li> <li>• Developing or offering new products or services, or moving into new lines of business.</li> </ul> <p>Geography:</p> <ul style="list-style-type: none"> <li>• Expanding into new locations.</li> </ul> <p>Entity structure:</p> <ul style="list-style-type: none"> <li>• Changes in the entity such as large acquisitions or reorganisations or other unusual events.</li> <li>• Entities or business segments likely to be sold.</li> </ul> <p>Human resources competence:</p> <ul style="list-style-type: none"> <li>• Changes in key personnel including departure of key executives.</li> </ul> <p>IT:</p> <ul style="list-style-type: none"> <li>• Changes in the IT environment.</li> <li>• Installation of significant new IT systems related to financial reporting.</li> </ul> <p>Applicable financial reporting framework:</p> <ul style="list-style-type: none"> <li>• Application of new accounting pronouncements.</li> </ul> <p>Capital:</p> <ul style="list-style-type: none"> <li>• New constraints on the availability of capital and credit.</li> </ul> <p>Regulatory:</p> <ul style="list-style-type: none"> <li>• Inception of investigations into the entity's operations or financial results by regulatory or government bodies.</li> <li>• Impact of new legislation related to environmental protection.</li> </ul> |

|  |  |
|--|--|
| Relevant Inherent Risk Factor:   | Examples of Events and Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:  |
| Uncertainty  | <p>Reporting:</p> <ul style="list-style-type: none"> <li>Events or transactions that involve significant measurement uncertainty, including accounting estimates, and related disclosures.</li> <li>Pending litigation and contingent liabilities, for example, sales warranties, financial guarantees and environmental remediation.</li> </ul>   |
| Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk | <p>Reporting:</p> <ul style="list-style-type: none"> <li>Opportunities for management and employees to engage in fraudulent financial reporting, including omission, or obscuring, of significant information in disclosures.</li> </ul> <p>Transactions:</p> <ul style="list-style-type: none"> <li>Significant transactions with related parties.</li> <li>Significant amount of non-routine or non-systematic transactions including intercompany transactions and large revenue transactions at period end.</li> <li>Transactions that are recorded based on management's intent, for example, debt refinancing, assets to be sold and classification of marketable securities.</li> </ul> |

*Other events or conditions that may indicate risks of material misstatement at the financial statement level:*

- Lack of personnel with appropriate accounting and financial reporting skills.
- Control deficiencies – particularly in the control environment, risk assessment process and process for monitoring, and especially those not addressed by management.
- Past misstatements, history of errors or a significant amount of adjustments at period end.

**Appendix 3**

(Ref: Para. 12(m), 21–26, A90–A181)

**Understanding the Entity’s System of Internal Control**

1. The entity’s system of internal control may be reflected in policy and procedures manuals, systems and forms, and the information embedded therein, and is effected by people. The entity’s system of internal control is implemented by management, those charged with governance, and other personnel based on the structure of the entity. The entity’s system of internal control can be applied, based on the decisions of management, those charged with governance or other personnel and in the context of legal or regulatory requirements, to the operating model of the entity, the legal entity structure, or a combination of these.
2. This appendix further explains the components of, as well as the limitations of, the entity’s system of internal control as set out in paragraphs 12(m), 21–26, and A90–A181, as they relate to a financial statement audit.
3. Included within the entity’s system of internal control are aspects that relate to the entity’s reporting objectives, including its financial reporting objectives, but it may also include aspects that relate to its operations or compliance objectives, when such aspects are relevant to financial reporting.

**Example:**

Controls over compliance with laws and regulations may be relevant to financial reporting when such controls are relevant to the entity’s preparation of disclosures of contingencies in the financial statements.

**Components of the Entity’s System of Internal Control***Control Environment*

4. The control environment includes the governance and management functions and the attitudes, awareness, and actions of those charged with governance and management concerning the entity’s system of internal control, and its importance in the entity. The control environment sets the tone of an organisation, influencing the control consciousness of its people, and provides the overall foundation for the operation of the other components of the entity’s system of internal control.
5. An entity’s control consciousness is influenced by those charged with governance, because one of their roles is to counterbalance pressures on management in relation to financial reporting that may arise from market demands or remuneration schemes. The effectiveness of the design of the control environment in relation to participation by those charged with governance is therefore influenced by such matters as:
  - Their independence from management and their ability to evaluate the actions of management.
  - Whether they understand the entity’s business transactions.

- The extent to which they evaluate whether the financial statements are prepared in accordance with the applicable financial reporting framework, including whether the financial statements include adequate disclosures.
6. The control environment encompasses the following elements:
- (a) *How management's responsibilities are carried out, such as creating and maintaining the entity's culture and demonstrating management's commitment to integrity and ethical values.* The effectiveness of controls cannot rise above the integrity and ethical values of the people who create, administer, and monitor them. Integrity and ethical behaviour are the product of the entity's ethical and behavioural standards or codes of conduct, how they are communicated (e.g., through policy statements), and how they are reinforced in practice (e.g., through management actions to eliminate or mitigate incentives or temptations that might prompt personnel to engage in dishonest, illegal, or unethical acts). The communication of entity policies on integrity and ethical values may include the communication of behavioural standards to personnel through policy statements and codes of conduct and by example.
  - (b) *When those charged with governance are separate from management, how those charged with governance demonstrate independence from management and exercise oversight of the entity's system of internal control.* An entity's control consciousness is influenced by those charged with governance. Considerations may include whether there are sufficient individuals who are independent from management and objective in their evaluations and decision-making; how those charged with governance identify and accept oversight responsibilities and whether those charged with governance retain oversight responsibility for management's design, implementation and conduct of the entity's system of internal control. The importance of the responsibilities of those charged with governance is recognised in codes of practice and other laws and regulations or guidance produced for the benefit of those charged with governance. Other responsibilities of those charged with governance include oversight of the design and effective operation of whistle blower procedures.
  - (c) *How the entity assigns authority and responsibility in pursuit of its objectives.* This may include considerations about:
    - Key areas of authority and responsibility and appropriate lines of reporting;
    - Policies relating to appropriate business practices, knowledge and experience of key personnel, and resource provided for carrying out duties; and
    - Policies and communications directed at ensuring that all personnel understand the entity's objectives, know how their individual actions interrelate and contribute to those objectives, and recognise how and for what they will be held accountable.
  - (d) *How the entity attracts, develops, and retains competent individuals in alignment with its objectives.* This includes how the entity ensures the individuals have the knowledge and skills necessary to accomplish the tasks that define the individual's job, such as:

- Standards for recruiting the most qualified individuals – with an emphasis on educational background, prior work experience, past accomplishments, and evidence of integrity and ethical behaviour.
  - Training policies that communicate prospective roles and responsibilities, including practices such as training schools and seminars that illustrate expected levels of performance and behaviour; and
  - Periodic performance appraisals driving promotions that demonstrate the entity's commitment to the advancement of qualified personnel to higher levels of responsibility.
- (e) *How the entity holds individuals accountable for their responsibilities in pursuit of the objectives of the entity's system of internal control.* This may be accomplished through, for example:
- Mechanisms to communicate and hold individuals accountable for performance of controls responsibilities and implement corrective actions as necessary;
  - Establishing performance measures, incentives and rewards for those responsible for the entity's system of internal control, including how the measures are evaluated and maintain their relevance;
  - How pressures associated with the achievement of control objectives impact the individual's responsibilities and performance measures; and
  - How the individuals are disciplined as necessary.

The appropriateness of the above matters will be different for every entity depending on its size, the complexity of its structure and the nature of its activities.

#### *The Entity's Risk Assessment Process*

7. The entity's risk assessment process is an iterative process for identifying and analysing risks to achieving the entity's objectives, and forms the basis for how management or those charged with governance determine the risks to be managed.
8. For financial reporting purposes, the entity's risk assessment process includes how management identifies business risks relevant to the preparation of financial statements in accordance with the entity's applicable financial reporting framework, estimates their significance, assesses the likelihood of their occurrence, and decides upon actions to manage them and the results thereof. For example, the entity's risk assessment process may address how the entity considers the possibility of unrecorded transactions or identifies and analyses significant estimates recorded in the financial statements.
9. Risks relevant to reliable financial reporting include external and internal events, transactions or circumstances that may occur and adversely affect an entity's ability to initiate, record, process, and report financial information consistent with the assertions of management in the financial statements. Management may initiate plans, programmes, or actions to address specific risks or it may decide to assume a risk because of cost or other considerations. Risks can arise or change due to circumstances such as the following:

- *Changes in operating environment.* Changes in the regulatory, economic or operating environment can result in changes in competitive pressures and significantly different risks.
- *New personnel.* New personnel may have a different focus on or understanding of the entity's system of internal control.
- *New or revamped information system.* Significant and rapid changes in the information system can change the risk relating to the entity's system of internal control.
- *Rapid growth.* Significant and rapid expansion of operations can strain controls and increase the risk of a breakdown in controls.
- *New technology.* Incorporating new technologies into production processes or the information system may change the risk associated with the entity's system of internal control.
- *New business models, products, or activities.* Entering into business areas or transactions with which an entity has little experience may introduce new risks associated with the entity's system of internal control.
- *Corporate restructurings.* Restructurings may be accompanied by staff reductions and changes in supervision and segregation of duties that may change the risk associated with the entity's system internal control.
- *Expanded foreign operations.* The expansion or acquisition of foreign operations carries new and often unique risks that may affect internal control, for example, additional or changed risks from foreign currency transactions.
- *New accounting pronouncements.* Adoption of new accounting principles or changing accounting principles may affect risks in preparing financial statements.
- *Use of IT.* Risks relating to:
  - Maintaining the integrity of data and information processing;
  - Risks to the entity business strategy that arise if the entity's IT strategy does not effectively supporting the entity's business strategy; or
  - Changes or interruptions in the entity's IT environment or turnover of IT personnel or when the entity does not make necessary updates to the IT environment or such updates are not timely.

#### *The Entity's Process to Monitor the System of Internal Control*

10. The entity's process to monitor the system of internal control is a continual process to evaluate the effectiveness of the entity's system of internal control, and to take necessary remedial actions on a timely basis. The entity's process to monitor the entity's system of internal control may consist of ongoing activities, separate evaluations (conducted periodically), or some combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and may include regular management and supervisory activities. The entity's process will likely vary in scope and frequency depending on the assessment of the risks by the entity.



11. The objectives and scope of internal audit functions typically include activities designed to evaluate or monitor the effectiveness of the entity's system of internal control.<sup>72</sup> The entity's process to monitor the entity's system of internal control may include activities such as management's review of whether bank reconciliations are being prepared on a timely basis, internal auditors' evaluation of sales personnel's compliance with the entity's policies on terms of sales contracts, and a legal department's oversight of compliance with the entity's ethical or business practice policies. Monitoring is done also to ensure that controls continue to operate effectively over time. For example, if the timeliness and accuracy of bank reconciliations are not monitored, personnel are likely to stop preparing them.
12. Controls related to the entity's process to monitor the entity's system of internal control, including those that monitor underlying automated controls, may be automated or manual, or a combination of both. For example, an entity may use automated monitoring controls over access to certain technology with automated reports of unusual activity to management, who manually investigate identified anomalies.
13. When distinguishing between a monitoring activity and a control related to the information system, the underlying details of the activity are considered, especially when the activity involves some level of supervisory review. Supervisory reviews are not automatically classified as monitoring activities and it may be a matter of judgement whether a review is classified as a control related to the information system or a monitoring activity. For example, the intent of a monthly completeness control would be to detect and correct errors, where a monitoring activity would ask why errors are occurring and assign management the responsibility of fixing the process to prevent future errors. In simple terms, a control related to the information system responds to a specific risk, whereas a monitoring activity assesses whether controls within each of the five components of the entity's system of internal control are operating as intended.
14. Monitoring activities may include using information from communications from external parties that may indicate problems or highlight areas in need of improvement. Customers implicitly corroborate billing data by paying their invoices or complaining about their charges. In addition, regulators may communicate with the entity concerning matters that affect the functioning of the entity's system of internal control, for example, communications concerning examinations by bank regulatory agencies. Also, management may consider in performing monitoring activities any communications relating to the entity's system of internal control from external auditors.

#### *The Information System and Communication*

15. The information system relevant to the preparation of the financial statements in consists of activities and policies, and accounting and supporting records, designed and established to:
  - Initiate, record and process entity transactions (as well as to capture, process and disclose information about events and conditions other than transactions) and to maintain accountability for the related assets, liabilities, and equity;

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<sup>72</sup> ISA (NZ) 610 (Revised) and Appendix 4 of this ISA (NZ) provides further guidance related to internal audit.

- Resolve incorrect processing of transactions, for example, automated suspense files and procedures followed to clear suspense items out on a timely basis;
  - Process and account for system overrides or bypasses to controls;
  - Incorporate information from transaction processing in the general ledger (e.g., transferring of accumulated transactions from a subsidiary ledger);
  - Capture and process information relevant to the preparation of the financial statements for events and conditions other than transactions, such as the depreciation and amortisation of assets and changes in the recoverability of assets; and
  - Ensure information required to be disclosed by the applicable financial reporting framework is accumulated, recorded, processed, summarised and appropriately reported in the financial statements.
16. An entity's business processes include the activities designed to:
- Develop, purchase, produce, sell and distribute an entity's products and services;
  - Ensure compliance with laws and regulations; and
  - Record information, including accounting and financial reporting information.
- Business processes result in the transactions that are recorded, processed and reported by the information system.
17. The quality of information affects management's ability to make appropriate decisions in managing and controlling the entity's activities and to prepare reliable financial reports.
18. Communication, which involves providing an understanding of individual roles and responsibilities pertaining to the entity's system of internal control, may take such forms as policy manuals, accounting and financial reporting manuals, and memoranda. Communication also can be made electronically, orally, and through the actions of management.
19. Communication by the entity of the financial reporting roles and responsibilities and of significant matters relating to financial reporting involves providing an understanding of individual roles and responsibilities pertaining to the entity's system of internal control relevant to financial reporting. It may include such matters as the extent to which personnel understand how their activities in the information system relate to the work of others and the means of reporting exceptions to an appropriate higher level within the entity.

### *Control Activities*

20. Controls in the control activities component are identified in accordance with paragraph 26. Such controls include information processing controls and general IT controls, both of which may be manual or automated in nature. The greater the extent of automated controls, or controls involving automated aspects, that management uses and relies on in relation to its financial reporting, the more important it may become for the entity to implement general IT controls that address the continued functioning of the automated aspects of information processing controls. Controls in the control activities component may pertain to the following:

- *Authorisation and approvals.* An authorisation affirms that a transaction is valid (i.e. it represents an actual economic event or is within an entity's policy). An authorisation typically takes the form of an approval by a higher level of management or of verification and a determination if the transaction is valid. For example, a supervisor approves an expense report after reviewing whether the expenses seem reasonable and within policy. An example of an automated approval is when an invoice unit cost is automatically compared with the related purchase order unit cost within a pre-established tolerance level. Invoices within the tolerance level are automatically approved for payment. Those invoices outside the tolerance level are flagged for additional investigation.
- *Reconciliations* – Reconciliations compare two or more data elements. If differences are identified, action is taken to bring the data into agreement. Reconciliations generally address the completeness or accuracy of processing transactions.
- *Verifications* – Verifications compare two or more items with each other or compare an item with a policy, and will likely involve a follow-up action when the two items do not match or the item is not consistent with policy. Verifications generally address the completeness, accuracy, or validity of processing transactions.
- *Physical or logical controls, including those that address security of assets against unauthorised access, acquisition, use or disposal.* Controls that encompass:
  - The physical security of assets, including adequate safeguards such as secured facilities over access to assets and records.
  - The authorisation for access to computer programs and data files (i.e., logical access).
  - The periodic counting and comparison with amounts shown on control records (for example, comparing the results of cash, security and inventory counts with accounting records).

The extent to which physical controls intended to prevent theft of assets are relevant to the reliability of financial statement preparation depends on circumstances such as when assets are highly susceptible to misappropriation.

- *Segregation of duties.* Assigning different people the responsibilities of authorising transactions, recording transactions, and maintaining custody of assets. Segregation of duties is intended to reduce the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of the person's duties.

For example, a manager authorising credit sales is not responsible for maintaining accounts receivable records or handling cash receipts. If one person is able to perform all these activities he or she could, for example, create a fictitious sale that could go undetected. Similarly, salespersons should not have the ability to modify product price files or commission rates.

Sometimes segregation is not practical, cost effective, or feasible. For example, smaller and less complex entities may lack sufficient resources to achieve ideal segregation, and the cost of hiring additional staff may be prohibitive. In these situations, management may institute alternative controls. In the example above, if the salesperson

can modify product price files, a detective control activity can be put in place to have personnel unrelated to the sales function periodically review whether and under what circumstances the salesperson changed prices.

21. Certain controls may depend on the existence of appropriate supervisory controls established by management or those charged with governance. For example, authorisation controls may be delegated under established guidelines, such as investment criteria set by those charged with governance; alternatively, non-routine transactions such as major acquisitions or divestments may require specific high-level approval, including in some cases that of shareholders.

### **Limitations of Internal Control**

22. The entity's system of internal control, no matter how effective, can provide an entity with only reasonable assurance about achieving the entity's financial reporting objectives. The likelihood of their achievement is affected by the inherent limitations of internal control. These include the realities that human judgement in decision-making can be faulty and that breakdowns in the entity's system of internal control can occur because of human error. For example, there may be an error in the design of, or in the change to, a control. Equally, the operation of a control may not be effective, such as where information produced for the purposes of the entity's system of internal control (for example, an exception report) is not effectively used because the individual responsible for reviewing the information does not understand its purpose or fails to take appropriate action.
23. Additionally, controls can be circumvented by the collusion of two or more people or inappropriate management override of controls. For example, management may enter into side agreements with customers that alter the terms and conditions of the entity's standard sales contracts, which may result in improper revenue recognition. Also, edit checks in an IT application that are designed to identify and report transactions that exceed specified credit limits may be overridden or disabled.
24. Further, in designing and implementing controls, management may make judgements on the nature and extent of the controls it chooses to implement, and the nature and extent of the risks it chooses to assume.

## Considerations for Understanding an Entity's Internal Audit Function

This appendix provides further considerations relating to understanding the entity's internal audit function when such a function exists.

### Objectives and Scope of the Internal Audit Function

1. The objectives and scope of an internal audit function, the nature of its responsibilities and its status within the organisation, including the function's authority and accountability, vary widely and depend on the size, complexity and structure of the entity and the requirements of management and, where applicable, those charged with governance. These matters may be set out in an internal audit charter or terms of reference.
2. The responsibilities of an internal audit function may include performing procedures and evaluating the results to provide assurance to management and those charged with governance regarding the design and effectiveness of risk management, the entity's system of internal control and governance processes. If so, the internal audit function may play an important role in the entity's process to monitor the entity's system of internal control. However, the responsibilities of the internal audit function may be focused on evaluating the economy, efficiency and effectiveness of operations and, if so, the work of the function may not directly relate to the entity's financial reporting.

### Enquiries of the Internal Audit Function

3. If an entity has an internal audit function, enquiries of the appropriate individuals within the function may provide information that is useful to the auditor in obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control, and in identifying and assessing risks of material misstatement at the financial statement and assertion levels. In performing its work, the internal audit function is likely to have obtained insight into the entity's operations and business risks, and may have findings based on its work, such as identified control deficiencies or risks, that may provide valuable input into the auditor's understanding of the entity and its environment, the applicable financial reporting framework, the entity's system of internal control, the auditor's risk assessments or other aspects of the audit. The auditor's enquiries are therefore made whether or not the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed.<sup>73</sup> Enquiries of particular relevance may be about matters the internal audit function has raised with those charged with governance and the outcomes of the function's own risk assessment process.
4. If, based on responses to the auditor's enquiries, it appears that there are findings that may be relevant to the entity's financial reporting and the audit of the financial statements, the auditor may consider it appropriate to read related reports of the internal audit function. Examples of reports of the internal audit function that may be relevant include the function's

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<sup>73</sup> The relevant requirements are contained in ISA (NZ) 610 (Revised 2013).

strategy and planning documents and reports that have been prepared for management or those charged with governance describing the findings of the internal audit function's examinations.

5. In addition, in accordance with ISA (NZ) 240,<sup>74</sup> if the internal audit function provides information to the auditor regarding any actual, suspected or alleged fraud, the auditor takes this into account in the auditor's identification of risk of material misstatement due to fraud.
6. Appropriate individuals within the internal audit function with whom enquiries are made are those who, in the auditor's judgement, have the appropriate knowledge, experience and authority, such as the chief internal audit executive or, depending on the circumstances, other personnel within the function. The auditor may also consider it appropriate to have periodic meetings with these individuals.

### **Consideration of the Internal Audit Function in Understanding the Control Environment**

7. In understanding the control environment, the auditor may consider how management has responded to the findings and recommendations of the internal audit function regarding identified control deficiencies relevant to the preparation of the financial statements, including whether and how such responses have been implemented, and whether they have been subsequently evaluated by the internal audit function.

### **Understanding the Role that the Internal Audit Function Plays in the Entity's Process to Monitor the System of Internal Control**

8. If the nature of the internal audit function's responsibilities and assurance activities are related to the entity's financial reporting, the auditor may also be able to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed directly by the auditor in obtaining audit evidence. Auditors may be more likely to be able to use the work of an entity's internal audit function when it appears, for example, based on experience in previous audits or the auditor's risk assessment procedures, that the entity has an internal audit function that is adequately and appropriately resourced relative to the complexity of the entity and the nature of its operations, and has a direct reporting relationship to those charged with governance.
9. If, based on the auditor's preliminary understanding of the internal audit function, the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed, ISA (NZ) 610 (Revised) applies.
10. As is further discussed in ISA (NZ) 610 (Revised), the activities of an internal audit function are distinct from other monitoring controls that may be relevant to financial reporting, such as reviews of management accounting information that are designed to contribute to how the entity prevents or detects misstatements.
11. Establishing communications with the appropriate individuals within an entity's internal audit function early in the engagement, and maintaining such communications throughout the engagement, can facilitate effective sharing of information. It creates an environment in which the auditor can be informed of significant matters that may come to the attention of

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<sup>74</sup> ISA (NZ) 240, paragraph 20

the internal audit function when such matters may affect the work of the auditor. ISA (NZ) 200 discusses the importance of the auditor planning and performing the audit with professional scepticism, including being alert to information that brings into question the reliability of documents and responses to enquiries to be used as audit evidence. Accordingly, communication with the internal audit function throughout the engagement may provide opportunities for internal auditors to bring such information to the auditor's attention. The auditor is then able to take such information into account in the auditor's identification and assessment of risks of material misstatement.

## Considerations for Understanding Information Technology (IT)

This appendix provides further matters that the auditor may consider in understanding the entity's use of IT in its system of internal control.

### Understanding the Entity's Use of Information Technology in the Components of the Entity's System of Internal Control

1. An entity's system of internal control contains manual elements and automated elements (i.e., manual and automated controls and other resources used in the entity's system of internal control). An entity's mix of manual and automated elements varies with the nature and complexity of the entity's use of IT. An entity's use of IT affects the manner in which the information relevant to the preparation of the financial statements in accordance with the applicable financial reporting framework is processed, stored and communicated, and therefore affects the manner in which the entity's system of internal control is designed and implemented. Each component of the entity's system of internal control may use some extent of IT.

Generally, IT benefits an entity's system of internal control by enabling an entity to:

- Consistently apply predefined business rules and perform complex calculations in processing large volumes of transactions or data;
  - Enhance the timeliness, availability, and accuracy of information;
  - Facilitate the additional analysis of information;
  - Enhance the ability to monitor the performance of the entity's activities and its policies and procedures;
  - Reduce the risk that controls will be circumvented; and
  - Enhance the ability to achieve effective segregation of duties by implementing security controls in IT applications, databases, and operating systems.
2. The characteristics of manual or automated elements are relevant to the auditor's identification and assessment of the risks of material misstatement, and further audit procedures based thereon. Automated controls may be more reliable than manual controls because they cannot be as easily bypassed, ignored, or overridden, and they are also less prone to simple errors and mistakes. Automated controls may be more effective than manual controls in the following circumstances:
    - High volume of recurring transactions, or in situations where errors that can be anticipated or predicted can be prevented, or detected and corrected, through automation
    - Controls where the specific ways to perform the control can be adequately designed and automated.



*Understanding the Entity's Use of Information Technology in the Information System* (Ref: Para. 25(a))

3. The entity's information system may include the use of manual and automated elements, which also affect the manner in which transactions are initiated, recorded, processed, and reported. In particular, procedures to initiate, record, process, and report transactions may be enforced through the IT applications used by the entity, and how the entity has configured those applications. In addition, records in the form of digital information may replace or supplement records in the form of paper documents.
4. In obtaining an understanding of the IT environment relevant to the flows of transactions and information processing in the information system, the auditor gathers information about the nature and characteristics of the IT applications used, as well as the supporting IT infrastructure and IT. The following table includes examples of matters that the auditor may consider in obtaining the understanding of the IT environment and includes examples of typical characteristics of IT environments based on the complexity of IT applications used in the entity's information system. However, such characteristics are directional and may differ depending on the nature of the specific IT applications in use by an entity.

|   | Examples of typical characteristics of: |  |  |
|---|---|--|--|
|   | Non-complex commercial software         | Mid-size and moderately complex commercial software or IT applications | Large or complex IT applications (e.g., ERP systems)   |
| Matters related to extent of automation and use of data:  |   |  |  |
| <ul style="list-style-type: none"> <li>The extent of automated procedures for processing, and the complexity of those procedures, including, whether there is highly automated, paperless processing</li> </ul> | N/A                                     | N/A  | Extensive and often complex automated procedures       |
| <ul style="list-style-type: none"> <li>The extent of the entity's reliance on system-generated reports in the processing of information.</li> </ul>   | Simple automated report logic           | Simple relevant automated report logic                                 | Complex automated report logic; Report-writer software |
| <ul style="list-style-type: none"> <li>How data is input (i.e., manual input, customer or vendor input, or file load).</li> </ul>   | Manual data inputs                      | Small number of data inputs or simple interfaces                       | Large number of data inputs or complex interfaces      |

|   |   |  |   |
|---|---|--|---|
| <ul style="list-style-type: none"> <li>How IT facilitates communication between applications, databases or other aspects of the IT environment, internally and externally, as appropriate, through system interfaces.</li> </ul>  | No automated interfaces (manual inputs only)  | Small number of data inputs or simple interfaces   | Large number of data inputs or complex interfaces   |
| <ul style="list-style-type: none"> <li>The volume and complexity of data in digital form being processed by the information system, including whether accounting records or other information are stored in digital form and the location of stored data.</li> </ul>    | Low volume of data or simple data that is able to be verified manually;<br>Data available locally | Low volume of data or simple data  | Large volume of data or complex data; Data warehouses; <sup>75</sup><br>Use of internal or external IT service providers (e.g., third-party storage or hosting of data) |
| Matters related to the IT applications and IT infrastructure:   |   |  |   |
| <ul style="list-style-type: none"> <li>The type of application (e.g., a commercial application with little or no customisation, or a highly-customised or highly-integrated application that may have been purchased and customised, or developed in-house).</li> </ul> | Purchased application with little or no customisation   | Purchased application or simple legacy or low-end ERP applications with little or no customisation | Custom developed applications or more complex ERPs with significant customisation   |
| <ul style="list-style-type: none"> <li>The complexity of the nature of the IT applications and the underlying IT infrastructure.</li> </ul>   | Small, simple laptop or client server-based solution  | Mature and stable mainframe, small or simple client server, software as a service cloud            | Complex mainframe, large or complex client server, web-facing,  |

<sup>75</sup> A data warehouse is generally described as a central repository of integrated data from one or more disparate sources (such as multiple databases) from which reports may be generated or that may be used by the entity for other data analysis activities. A report-writer is an IT application that is used to extract data from one or more sources (such as a data warehouse, a database or an IT application) and present the data in a specified format.

|  |  |   |  |
|--|--|---|--|
|  |  |   | infrastructure as a service cloud  |
| <ul style="list-style-type: none"> <li>Whether there is third-party hosting or outsourcing of IT.</li> </ul>   | If outsourced, competent, mature, proven provider (e.g., cloud provider)             | If outsourced, competent, mature, proven provider (e.g. cloud provider) | Competent, mature proven provider for certain applications and new or start-up provider for others |
| <ul style="list-style-type: none"> <li>Whether the entity is using emerging technologies that affect its financial reporting.</li> </ul>   | No use of emerging technologies  | Limited use of emerging technologies in some applications               | Mixed use of emerging technologies across platforms  |
| Matters related to IT processes:   |  |   |  |
| <ul style="list-style-type: none"> <li>The personnel involved in maintaining the IT environment (the number and skill level of the IT support resources that manage security and changes to the IT environment)</li> </ul>   | Few personnel with limited IT knowledge to process vendor upgrades and manage access | Limited personnel with IT skills / dedicated to IT                      | Dedicated IT departments with skilled personnel, including programming skills                      |
| <ul style="list-style-type: none"> <li>The complexity of processes to manage access rights</li> </ul>  | Single individual with administrative access manages access rights                   | Few individuals with administrative access manages access rights        | Complex processes managed by IT department for access rights                                       |
| <ul style="list-style-type: none"> <li>The complexity of the security over the IT environment, including vulnerability of the IT applications, databases, and other aspects of the IT environment to cyber risks, particularly when there are web-based transactions or transactions involving external interfaces.</li> </ul> | Simple on-premise access with no external web-facing elements;                       | Some web-based applications with primarily simple, role-based security  | Multiple platforms with web-based access and complex security models                               |

|  |  |   |   |
|--|--|---|---|
| <ul style="list-style-type: none"> <li>Whether program changes have been made to the manner in which information is processed, and the extent of such changes during the period.</li> </ul>                                  | Commercial software with no source code installed                              | Some commercial applications with no source code and other mature applications with a small number or simple changes; traditional systems development lifecycle | New or large number or complex changes, several development cycles each year                          |
| <ul style="list-style-type: none"> <li>The extent of change within the IT environment (e.g., new aspects of the IT environment or significant changes in the IT applications or the underlying IT infrastructure)</li> </ul> | Changes limited to version upgrades of commercial software                     | Changes consist of commercial software upgrades, ERP version upgrades, or legacy enhancements   | New or large number or complex changes, several development cycles each year, heavy ERP customisation |
| <ul style="list-style-type: none"> <li>Whether there was a major data conversion during the period and, if so, the nature and significance of the changes made, and how the conversion was undertaken.</li> </ul>            | Software upgrades provided by vendor. No data conversion features for upgrade. | Minor version upgrades for commercial software applications with limited data being converted   | Major version upgrade, new release, platform change   |

### *Emerging Technologies*

- Entities may use emerging technologies (e.g., blockchain, robotics or artificial intelligence) because such technologies may present specific opportunities to increase operational efficiencies or enhance financial reporting. When emerging technologies are used in the entity's information system relevant to the preparation of the financial statements, the auditor may include such technologies in the identification of IT applications and other aspects of the IT environment that are subject to risks arising from the use of IT. While emerging technologies may be seen to be more sophisticated or more complex compared to existing technologies, the auditor's responsibilities in relation to IT applications and identified general IT controls in accordance with paragraph 26(b)–(c) remain unchanged.

### *Scalability*

- Obtaining an understanding of the entity's IT environment may be more easily accomplished for a less complex entity that uses commercial software and when the entity does not have access to the source code to make any program changes. Such entities may not have dedicated IT resources but may have a person assigned in an administrator role for the purpose of

granting employee access or installing vendor-provided updates to the IT applications. Specific matters that the auditor may consider in understanding the nature of a commercial accounting software package, which may be the single IT application used by a less complex entity in its information system, may include:

- The extent to which the software is well established and has a reputation for reliability;
  - The extent to which it is possible for the entity to modify the source code of the software to include additional modules (i.e., add-ons) to the base software, or to make direct changes to data;
  - The nature and extent of modifications that have been made to the software. Although an entity may not be able to modify the source code of the software, many software packages allow for configuration (e.g., setting or amending reporting parameters). These do not usually involve modifications to source code; however, the auditor may consider the extent to which the entity is able to configure the software when considering the completeness and accuracy of information produced by the software that is used as audit evidence; and
  - The extent to which data related to the preparation of the financial statements can be directly accessed (i.e., direct access to the database without using the IT application) and the volume of data that is processed. The greater the volume of data, the more likely the entity may need controls that address maintaining the integrity of the data, which may include general IT controls over unauthorised access and changes to the data.
7. Complex IT environments may include highly-customised or highly-integrated IT applications and may therefore require more effort to understand. Financial reporting processes or IT applications may be integrated with other IT applications. Such integration may involve IT applications that are used in the entity's business operations and that provide information to the IT applications relevant to the flows of transactions and information processing in the entity's information system. In such circumstances, certain IT applications used in the entity's business operations may also be relevant to the preparation of the financial statements. Complex IT environments also may require dedicated IT departments that have structured IT processes supported by personnel that have software development and IT environment maintenance skills. In other cases, an entity may use internal or external service providers to manage certain aspects of, or IT processes within, its IT environment (e.g., third-party hosting).

#### Identifying IT Applications that are Subject to Risks Arising from the use of IT

8. Through understanding the nature and complexity of the entity's IT environment, including the nature and extent of information processing controls, the auditor may determine which IT applications the entity is relying upon to accurately process and maintain the integrity of financial information. The identification of IT applications on which the entity relies, may affect the auditor's decision to test the automated controls within such IT applications, assuming that such automated controls address identified risks of material misstatement. Conversely, if the entity is not relying on an IT application, the automated controls within such IT application are unlikely to be appropriate or sufficiently precise for purposes of

operating effectiveness tests. Automated controls that may be identified in accordance with paragraph 26(b) may include, for example, automated calculations or input, processing and output controls, such as a three-way match of a purchase order, vendor shipping document, and vendor invoice. When automated controls are identified by the auditor and the auditor determines through the understanding of the IT environment that the entity is relying on the IT application that includes those automated controls, it may be more likely for the auditor to identify the IT application as one that is subject to risks arising from the use of IT.

9. In considering whether the IT applications for which the auditor has identified automated controls are subject to risks arising from the use of IT, the auditor is likely to consider whether, and the extent to which, the entity may have access to source code that enables management to make program changes to such controls or the IT applications. The extent to which the entity makes program or configuration changes and the extent to which the IT processes over such changes are formalised may also be relevant considerations. The auditor is also likely to consider the risk of inappropriate access or changes to data.
10. System-generated reports that the auditor may intend to use as audit evidence may include, for example, a trade receivable aging report or an inventory valuation report. For such reports, the auditor may obtain audit evidence about the completeness and accuracy of the reports by substantively testing the inputs and outputs of the report. In other cases, the auditor may plan to test the operating effectiveness of the controls over the preparation and maintenance of the report, in which case the IT application from which it is produced is likely to be subject to risks arising from the use of IT. In addition to testing the completeness and accuracy of the report, the auditor may plan to test the operating effectiveness of general IT controls that address risks related to inappropriate or unauthorised program changes to, or data changes in, the report.
11. Some IT applications may include report-writing functionality within them while some entities may also utilise separate report-writing applications (i.e., report-writers). In such cases, the auditor may need to determine the sources of system-generated reports (i.e., the application that prepares the report and the data sources used by the report) to determine the IT applications subject to risks arising from the use of IT.
12. The data sources used by IT applications may be databases that, for example, can only be accessed through the IT application or by IT personnel with database administration privileges. In other cases, the data source may be a data warehouse that may itself be considered to be an IT application subject to risks arising from the use of IT.
13. The auditor may have identified a risk for which substantive procedures alone are not sufficient because of the entity's use of highly-automated and paperless processing of transactions, which may involve multiple integrated IT applications. In such circumstances, the controls identified by the auditor are likely to include automated controls. Further, the entity may be relying on general IT controls to maintain the integrity of the transactions processed and other information used in processing. In such cases, the IT applications involved in the processing and the storage of the information are likely subject to risks arising from the use of IT.

### *End-User Computing*

14. Although audit evidence may also come in the form of system-generated output that is used in a calculation performed in an end-user computing tool (e.g., spreadsheet software or simple databases), such tools are not typically identified as IT applications in the context of paragraph 26(b). Designing and implementing controls around access and change to end-user computing tools may be challenging, and such controls are rarely equivalent to, or as effective as, general IT controls. Rather, the auditor may consider a combination of information processing controls, taking into account the purpose and complexity of the end-user computing involved, such as:
- Information processing controls over the initiation and processing of the source data, including relevant automated or interface controls to the point from which the data is extracted (i.e. the data warehouse);
  - Controls to check that the logic is functioning as intended, for example, controls which ‘prove’ the extraction of data, such as reconciling the report to the data from which it was derived, comparing the individual data from the report to the source and vice versa, and controls which check the formulas or macros; or
  - Use of validation software tools, which systematically check formulas or macros, such as spreadsheet integrity tools.

### Scalability

15. The entity’s ability to maintain the integrity of information stored and processed in the information system may vary based on the complexity and volume of the related transactions and other information. The greater the complexity and volume of data that supports a significant class of transactions, account balance or disclosure, the less likely it may become for the entity to maintain integrity of that information through information processing controls alone (e.g., input and output controls or review controls). It also becomes less likely that the auditor will be able to obtain audit evidence about the completeness and accuracy of such information through substantive testing alone when such information is used as audit evidence. In some circumstances, when volume and complexity of transactions are lower, management may have an information processing control that is sufficient to verify the accuracy and completeness of the data (e.g., individual sales orders processed and billed may be reconciled to the hard copy originally entered into the IT application). When the entity relies on general IT controls to maintain the integrity of certain information used by IT applications, the auditor may determine that the IT applications that maintain that information are subject to risks arising from the use of IT.

| Example characteristics of an IT application that is likely not subject to risks arising from IT  | Example characteristics of an IT application that is likely subject to risks arising from IT   |
|---|--|
| <ul style="list-style-type: none"> <li>• Standalone applications</li> <li>• The volume of data (transactions) is not significant.</li> <li>• The application’s functionality is not complex.</li> </ul> | <ul style="list-style-type: none"> <li>• Applications are interfaced.</li> <li>• The volume of data (transactions) is significant/</li> <li>• The application’s functionality is complex as</li> </ul> |

|   |   |
|---|---|
| <ul style="list-style-type: none"> <li>• Each transaction is supported by original hard copy documentation.</li> </ul>  | <ul style="list-style-type: none"> <li>– The application automatically initiates transactions; and</li> <li>– There are a variety of complex calculations underlying automated entries.</li> </ul>  |
| <p>IT application is likely not subject to risks arising from IT because:</p> <ul style="list-style-type: none"> <li>• The volume of data is not significant and therefore management is not relying upon general IT controls to process or maintain the data.</li> <li>• Management does not rely on automated controls or other automated functionality. The auditor has not identified automated controls in accordance with paragraph 26(a).</li> <li>• Although management uses system-generated reports in their controls, they do not rely on these reports. Instead, they reconcile the reports back to the hard copy documentation and verify the calculations in the reports.</li> <li>• The auditor will directly test information produced by the entity used as audit evidence.</li> </ul> | <p>IT application is likely subject to risks arising from IT because:</p> <ul style="list-style-type: none"> <li>• Management relies on an application system to process or maintain data as the volume of data is significant.</li> <li>• Management relies upon the application system to perform certain automated controls that the auditor has also identified.</li> </ul> |

*Other Aspects of the IT Environment that Are Subject to Risks Arising from the Use of IT*

16. When the auditor identifies IT applications that are subject to risks arising from the use of IT, other aspects of the IT environment are also typically subject to risks arising from the use of IT. The IT infrastructure includes the databases, operating system, and network. Databases store the data used by IT applications and may consist of many interrelated data tables. Data in databases may also be accessed directly through database management systems by IT or other personnel with database administration privileges. The operating system is responsible for managing communications between hardware, IT applications, and other software used in the network. As such, IT applications and databases may be directly accessed through the operating system. A network is used in the IT infrastructure to transmit data and to share information, resources and services through a common communications link. The network also typically establishes a layer of logical security (enabled through the operating system) for access to the underlying resources.
17. When IT applications are identified by the auditor to be subject to risks arising from IT, the database(s) that stores the data processed by an identified IT application is typically also



identified. Similarly, because an IT application's ability to operate is often dependent on the operating system and IT applications and databases may be directly accessed from the operating system, the operating system is typically subject to risks arising from the use of IT. The network may be identified when it is a central point of access to the identified IT applications and related databases or when an IT application interacts with vendors or external parties through the internet, or when web-facing IT applications are identified by the auditor.

*Identifying Risks arising from the Use of IT and General IT Controls*

18. Examples of risks arising from the use of IT include risks related to inappropriate reliance on IT applications that are inaccurately processing data, processing inaccurate data, or both, such as
  - Unauthorised access to data that may result in destruction of data or improper changes to data, including the recording of unauthorised or non-existent transactions, or inaccurate recording of transactions. Particular risks may arise where multiple users access a common database.
  - The possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties thereby breaking down segregation of duties.
  - Unauthorised changes to data in master files.
  - Unauthorised changes to IT applications or other aspects of the IT environment.
  - Failure to make necessary changes to IT applications or other aspects of the IT environment.
  - Inappropriate manual intervention.
  - Potential loss of data or inability to access data as required.
19. The auditor's consideration of unauthorised access may include risks related to unauthorised access by internal or external parties (often referred to as cybersecurity risks). Such risks may not necessarily affect financial reporting, as an entity's IT environment may also include IT applications and related data that address operational or compliance needs. It is important to note that cyber incidents usually first occur through the perimeter and internal network layers, which tend to be further removed from the IT application, database and operating systems that affect the preparation of the financial statements. Accordingly, if information about a security breach has been identified, the auditor ordinarily considers the extent to which such a breach had the potential to affect financial reporting. If financial reporting may be affected, the auditor may decide to understand, and test the related controls to determine the possible impact or scope of potential misstatements in the financial statements or may determine that the entity has provided adequate disclosures in relation to such security breach.
20. In addition, laws and regulations that may have a direct or indirect effect on the entity's financial statements may include data protection legislation. Considering an entity's compliance with such laws or regulations, in accordance with ISA (NZ) 250 (Revised),<sup>76</sup>

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<sup>76</sup> ISA (NZ) 250 (Revised)

may involve understanding the entity's IT processes and general IT controls that the entity has implemented to address the relevant laws or regulations.

21. General IT controls are implemented to address risks arising from the use of IT. Accordingly, the auditor uses the understanding obtained about the identified IT applications and other aspects of the IT environment and the applicable risks arising from the use of IT in determining the general IT controls to identify. In some cases, an entity may use common IT processes across its IT environment or across certain IT applications, in which case common risks arising from the use of IT and common general IT controls may be identified.
22. In general, a greater number of general IT controls related to IT applications and databases are likely to be identified than for other aspects of the IT environment. This is because these aspects are the most closely concerned with the information processing and storage of information in the entity's information system. In identifying general IT controls, the auditor may consider controls over actions of both end users and of the entity's IT personnel or IT service providers.
23. Appendix 6 provides further explanation of the nature of the general IT controls typically implemented for different aspects of the IT environment. In addition, examples of general IT controls for different IT processes are provided.

## Considerations for Understanding General IT Controls

This appendix provides further matters that the auditor may consider in understanding general IT controls.

1. The nature of the general IT controls typically implemented for each of the aspects of the IT environment
  - (a) Applications

General IT controls at the IT application layer will correlate to the nature and extent of application functionality and the access paths allowed in the technology. For example, more controls will be relevant for highly-integrated IT applications with complex security options than a legacy IT application supporting a small number of account balances with access methods only through transactions.
  - (b) Database

General IT controls at the database layer typically address risks arising from the use of IT related to unauthorised updates to financial reporting information in the database through direct database access or execution of a script or program.
  - (c) Operating system

General IT controls at the operating system layer typically address risks arising from the use of IT related to administrative access, which can facilitate the override of other controls. This includes actions such as compromising other user's credentials, adding new, unauthorised users, loading malware or executing scripts or other unauthorised programs.
  - (d) Network

General IT controls at the network layer typically address risks arising from the use of IT related to network segmentation, remote access, and authentication. Network controls may be relevant when an entity has web-facing applications used in financial reporting. Network controls are also may be relevant when the entity has significant business partner relationships or third-party outsourcing, which may increase data transmissions and the need for remote access.
2. Examples of general IT controls that may exist, organised by IT process include:
  - (a) Process to manage access:
    - *Authentication*

Controls that ensure a user accessing the IT application or other aspect of the IT environment is using their own log-in credentials (i.e., the user is not using another user's credentials).

- *Authorisation*  
Controls that allow users to access the information necessary for their job responsibilities and nothing further, which facilitates appropriate segregation of duties.
  - *Provisioning*  
Controls to authorise new users and modifications to existing users' access privileges.
  - *Deprovisioning*  
Controls to remove user access upon termination or transfer.
  - *Privileged access*  
Controls over administrative or powerful users' access.
  - *User access reviews*  
Controls to recertify or evaluate user access for ongoing authorisation over time.
  - *Security configuration controls*  
Each technology generally has key configuration settings that help restrict access to the environment.
  - *Physical access*  
Controls over physical access to the data center and hardware, as such access may be used to override other controls.
- (b) Process to manage program or other changes to the IT environment
- *Change management process*  
Controls over the process to design, program, test and migrate changes to a production (i.e., end user) environment.
  - *Segregation of duties over change migration*  
Controls that segregate access to make and migrate changes to a production environment.
  - *Systems development or acquisition or implementation*  
Controls over initial IT application development or implementation (or in relation to other aspects of the IT environment).
  - *Data conversion*  
Controls over the conversion of data during development, implementation or upgrades to the IT environment.
- (c) Process to manage IT Operations
- *Job scheduling*

Controls over access to schedule and initiate jobs or programs that may affect financial reporting.

- *Job monitoring*

Controls to monitor financial reporting jobs or programs for successful execution.

- *Backup and recovery*

Controls to ensure backups of financial reporting data occur as planned and that such data is available and able to be accessed for timely recovery in the event of an outage or attack.

- *Intrusion detection*

Controls to monitor for vulnerabilities and or intrusions in the IT environment.

The table below illustrates examples of general IT controls to address examples of risks arising from the use of IT, including for different IT applications based on their nature.

| Process       | Risks  | Controls   | IT Applications   |  |  |
|---------------|--|--|---|--|--|
| IT Process    | Example Risks Arising from the Use of IT   | Example General IT Controls  | Non-complex commercial software – Applicable (yes / no) | Mid-size and moderately complex commercial software or IT applications – Applicable (yes / no) | Large or complex IT applications (e.g., ERP systems) – Applicable (yes / no) |
| Manage Access | User-access privileges: Users have access privileges beyond those necessary to perform their assigned duties, which may create improper segregation of duties. | Management approves the nature and extent of user-access privileges for new and modified user access, including standard application profiles/roles, critical financial reporting transactions, and segregation of duties. | Yes – instead of user access reviews noted below        | Yes  | Yes  |

|               |  |  |   |   |  |
|---------------|--|--|---|---|--|
|               |  | Access for terminated or transferred users is removed or modified in a timely manner.  | Yes – instead of user access reviews below                  | Yes   | Yes  |
|               |  | User access is periodically reviewed.  | Yes – instead of provisioning/Deprovisioning controls above | Yes for certain applications  | Yes  |
|               |  | Segregation of duties is monitored and conflicting access is either removed or mapped to mitigating controls, which are documented and tested.   | N/A – no system enabled segregation                         | Yes for certain applications  | Yes  |
|               |  | Privileged-level access (e.g., configuration, data and security administrators) is authorised and appropriately restricted.  | Yes – likely at IT application layer only                   | Yes at IT application and certain layers of IT environment for platform | Yes at all layers of IT environment for platform |
| Manage Access | Direct data access: Inappropriate changes are made directly to financial data through means other than application transactions. | Access to application data files or database objects/tables/data is limited to authorised personnel, based on their job responsibilities and assigned role, and such access is approved by management. | N/A   | Yes for certain applications and databases                              | Yes  |

|               |   |  |  |   |     |
|---------------|---|--|--|---|-----|
| Manage Access | System settings: Systems are not adequately configured or updated to restrict system access to properly authorised and appropriate users.   | Access is authenticated through unique user IDs and passwords or other methods as a mechanism for validating that users are authorised to gain access to the system. Password parameters meet company or industry standards (e.g., password minimum length and complexity, expiration, account lockout). | Yes – password authentication only               | Yes – mix of password and multi-factor authentication | Yes |
|               |   | The key attributes of the security configuration are appropriately implemented.  | N/A – no technical security configurations exist | Yes for certain applications and databases            | Yes |
| Manage Change | Application changes: Inappropriate changes are made to application systems or programs that contain relevant automated controls (i.e., configurable settings, automated algorithms, automated calculations, and automated | Application changes are appropriately tested and approved before being moved into the production environment.  | N/A-would verify no source code installed        | Yes for non-commercial software                       | Yes |
|               |   | Access to implement changes into the application production environment is appropriately restricted and segregated from the development environment.   | N/A  | Yes for non-commercial software                       | Yes |

|               |  |  |   |                                 |     |
|---------------|--|--|---|---------------------------------|-----|
|               | data extraction) or report logic.  |  |   |                                 |     |
| Manage Change | Database changes: Inappropriate changes are made to the database structure and relationships between the data.   | Database changes are appropriately tested and approved before being moved into the production environment.   | N/A – no database changes made at entity            | Yes for non-commercial software | Yes |
| Manage Change | System software changes: Inappropriate changes are made to system software (e.g., operating system, network, change-management software, access-control software). | System software changes are appropriately tested and approved before being moved to production.  | N/A – no system software changes are made at entity | Yes                             | Yes |
| Manage Change | Data conversion: Data converted from legacy systems or previous versions introduces data errors if the conversion  | Management approves the results of the conversion of data (e.g., balancing and reconciliation activities) from the old application system or data structure to the | N/A – Addressed through manual controls             | Yes                             | Yes |



|               |  |   |  |                      |                      |
|---------------|--|---|--|----------------------|----------------------|
|               | transfers incomplete, redundant, obsolete, or inaccurate data.   | new application system or data structure and monitors that the conversion is performed in accordance with established conversion policies and procedures.   |  |                      |                      |
| IT Operations | Network:<br>The network does not adequately prevent unauthorised users from gaining inappropriate access to information systems. | Access is authenticated through unique user IDs and passwords or other methods as a mechanism for validating that users are authorised to gain access to the system. Password parameters meet company or professional policies and standards (e.g., password minimum length and complexity, expiration, account lockout). | N/A – no separate network authentication method exists | Yes                  | Yes                  |
|               |  | Network is architected to segment web-facing applications from the internal network, where ICFR relevant applications are accessed.   | N/A – no network segmentation employed                 | Yes - with judgement | Yes - with judgement |

|               |   |  |   |                      |                      |
|---------------|---|--|---|----------------------|----------------------|
|               |   | On a periodic basis, vulnerability scans of the network perimeter are performed by the network management team, which also investigates potential vulnerabilities.                         | N/A   | Yes - with judgement | Yes - with judgement |
|               |   | On a periodic basis, alerts are generated to provide notification of threats identified by the intrusion detection systems. These threats are investigated by the network management team. | N/A   | Yes - with judgement | Yes - with judgement |
|               |   | Controls are implemented to restrict Virtual Private Network (VPN) access to authorised and appropriate users.   | N/A – no VPN                                    | Yes - with judgement | Yes - with judgement |
| IT Operations | Data backup and recovery: Financial data cannot be recovered or accessed in a timely manner when there is | Financial data is backed up on a regular basis according to an established schedule and frequency.   | N/A – relying on manual backups by finance team | Yes                  | Yes                  |

|               |   |   |                         |                              |     |
|---------------|---|---|-------------------------|------------------------------|-----|
|               | a loss of data.   |   |                         |                              |     |
| IT Operations | Job scheduling: Production systems, programs, or jobs result in inaccurate, incomplete, or unauthorised processing of data. | Only authorised users have access to update the batch jobs (including interface jobs) in the job scheduling software.   | N/A – no batch jobs     | Yes for certain applications | Yes |
|               |   | Critical systems, programs, or jobs are monitored, and processing errors are corrected to ensure successful completion. | N/A – no job monitoring | Yes for certain applications | Yes |

**ACCOMPANYING ATTACHMENT: CONFORMITY TO THE INTERNATIONAL STANDARDS ON AUDITING**

This conformity statement accompanies but is not part of ISA (NZ) 315 (Revised).

**Conformity with International Standards on Auditing**

This International Standard on Auditing (New Zealand) (ISA (NZ)) conforms to International Standard on Auditing (ISA) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*, issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this ISA (NZ) (and do not appear in the text of the equivalent ISA) are identified with the prefix “NZ”.

This ISA (NZ) incorporates terminology and definitions used in New Zealand.

Compliance with this ISA (NZ) enables compliance with ISA 315.

**Comparison with Australian Auditing Standards**

This section will be completed after the AUASB issues its revised standard.

ISA



NZ AUDITING  
AND ASSURANCE  
STANDARDS BOARD

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**INTERNATIONAL STANDARD ON AUDITING (NEW ZEALAND) 315 (Revised ~~2019~~),**

**Identifying and Assessing the Risks of Material Misstatement (ISA (NZ) 315 (Revised))**

This Standard was issued on ?? by the New Zealand Auditing and Assurance Standards Board of the External Reporting Board pursuant to section 12(b) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on ??.

An auditor that is required to apply this Standard is required to apply it for audits of financial statements for periods beginning on or after 15 December 2021. However, early adoption is permitted.

In finalising this Standard, the New Zealand Auditing and Assurance Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued as a result of International Standard on Auditing 315 being revised.

This Standard, when applied, supersedes International Standard on Auditing (New Zealand) (ISA (NZ)) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

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Appendix 6: Considerations for Understanding General IT Controls

Accompanying Attachment: Conformity to the International ~~Standard~~Standards on Auditing ~~(ISA)~~

International Standard on Auditing (New Zealand) (ISA (NZ)) 315 (Revised), "Identifying and Assessing the Risks of Material Misstatement" should be read in conjunction with ISA (NZ) 200, "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (New Zealand)."



## History of Amendments

### Table of pronouncements – ISA (NZ) 315 (Revised) *Identifying and Assessing the Risks of Material Misstatement*

This table lists the pronouncements establishing and amending ISA (NZ) 315 (Revised).

| <u>Pronouncements</u>   | <u>Date approved</u> | <u>Effective date</u>  |
|---|----------------------|--|
| <u>International Standard on Auditing (New Zealand) 315 (Revised)</u> | <u>December 2019</u> | <u>Effective for audits of financial statements for periods beginning on or after <u>15 December 2021</u>.</u> |

## Introduction

### Scope of this ISA (NZ)

1. This International Standard on Auditing (New Zealand) (ISA (NZ)) deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements

### **Key Concepts in this ISA (NZ)**

2. ISA- (NZ) 200 deals with the overall objectives of the auditor in conducting an audit of the financial statements,<sup>1</sup> including to obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level.<sup>2</sup> Audit risk is a function of the risks of material misstatement and detection risk.<sup>3</sup> ISA- (NZ) 200 explains that the risks of material misstatement may exist at two levels:<sup>4</sup> the overall financial statement level; and the assertion level for classes of transactions, account balances and disclosures.
3. ISA- (NZ) 200 requires the auditor to exercise professional ~~judgment~~judgement in planning and performing an audit, and to plan and perform an audit with professional ~~skepticism~~recognizing skepticism recognising that circumstances may exist that cause the financial statements to be materially misstated.<sup>5</sup>
4. ~~4.~~—— Risks at the financial statement level relate pervasively to the financial statements as a whole and potentially affect many assertions. Risks of material misstatement at the assertion level consist of two components, inherent and control risk:
  - Inherent risk is described as the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
  - Control risk is described as the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's system of internal control.
5. ~~5.~~—— ISA- (NZ) 200 explains that risks of material misstatement are assessed at the assertion level in order to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence.<sup>6</sup> For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk

<sup>1</sup> ISA- (NZ) 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

<sup>2</sup> ISA- (NZ) 200, paragraph 17

<sup>3</sup> ISA- (NZ) 200, paragraphs 13(c)

<sup>4</sup> ISA- (NZ) 200, paragraph A36

<sup>5</sup> ISA- (NZ) 200, paragraphs 15–16

<sup>6</sup> ISA- (NZ) 200, paragraph A43a and ISA- (NZ) 330, *The Auditor's Responses to Assessed Risks*, paragraph 6

and control risk is required by this ISA- (NZ). As explained in ISA- (NZ) 200, inherent risk is higher for some assertions and related classes of transactions, account balances and disclosures than for others. The degree to which inherent risk varies is referred to in this ISA- (NZ) as the ‘spectrum of inherent risk.’

6. 6.—— Risks of material misstatement identified and assessed by the auditor include both those due to error and those due to fraud. Although both are addressed by this ISA- (NZ), the significance of fraud is such that further requirements and guidance are included in ISA- (NZ) 240<sup>7</sup> in relation to risk assessment procedures and related activities to obtain information that is used to identify, assess and respond to the risks of material misstatement due to fraud.
7. 7.—— The auditor’s risk identification and assessment process is iterative and dynamic. The auditor’s understanding of the entity and its environment, the applicable financial reporting framework, and the entity’s system of internal control are interdependent with concepts within the requirements to identify and assess the risks of material misstatement. In obtaining the understanding required by this ISA- (NZ), initial expectations of risks may be developed, which may be further refined as the auditor progresses through the risk identification and assessment process. In addition, this ISA- (NZ) and ISA- (NZ) 330 require the auditor to revise the risk assessments, and modify further overall responses and further audit procedures, based on audit evidence obtained from performing further audit procedures in accordance with ISA- (NZ) 330, or if new information is obtained.
8. 8.—— ISA- (NZ) 330 requires the auditor to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.<sup>8</sup> ISA- (NZ) 330 further explains that the auditor’s assessment of the risks of material misstatement at the financial statement level, and the auditor’s overall responses, is affected by the auditor’s understanding of the control environment. ISA- (NZ) 330 also requires the auditor to design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level.<sup>9</sup>

## Scalability

9. 9.—— ISA- (NZ) 200 states that some ISAs (NZ) include scalability considerations which illustrate the application of the requirements to all entities regardless of whether their nature and circumstances are less complex or more complex.<sup>10</sup> This ISA- (NZ) is intended for audits of all entities, regardless of size or complexity and the application material therefore incorporates specific considerations specific to both less and more complex entities, where

<sup>7</sup> ISA- (NZ) 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*

<sup>8</sup> ISA- (NZ) 330, paragraph 5

<sup>9</sup> ISA- (NZ) 330, paragraph 6

<sup>10</sup> ISA- (NZ) 200, paragraph A65a

appropriate. While the size of an entity may be an indicator of its complexity, some smaller entities may be complex and some larger entities may be less complex.

### Effective Date

10. 40. — This ISA- (NZ) is effective for audits of financial statements for periods beginning on or after 15 December 45, 2021.

### Objective

11. 44. — The objective of the auditor is to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement.

### Definitions

12. 42. — For purposes of the ISAs, (NZ), the following terms have the meanings attributed below:

(a) (a) — *Assertions* – Representations, explicit or otherwise, with respect to the recognition, measurement, presentation and disclosure of information in the financial statements which are inherent in management representing that the financial statements are prepared in accordance with the applicable financial reporting framework. Assertions are used by the auditor to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement. (Ref: Para. A1)

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

(c) (c) — *Controls* – Policies or procedures that an entity establishes to achieve the control objectives of management or those charged with governance. In this context: (Ref: Para. A2–A5)

(i) Policies are statements of what should, or should not, be done within the entity to effect control. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions.

(ii) Procedures are actions to implement policies.

(d) (d) — *General information technology (IT) controls* – Controls over the entity's IT processes that support the continued proper operation of the IT environment, including the continued effective functioning of information processing controls and the integrity of information (i.e., the completeness, accuracy and validity of

information) in the entity's information system. Also see the definition of IT environment.

- ~~(e)~~ ~~(e)~~ *Information processing controls* – Controls relating to the processing of information in IT applications or manual information processes in the entity's information system that directly address risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information). (Ref: Para. A6)
- ~~(f)~~ ~~(f)~~ *Inherent risk factors* – Characteristics of events or conditions that affect susceptibility to misstatement, whether due to fraud or error, 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 other fraud risk factors<sup>11</sup> insofar as they affect inherent risk. (Ref: Para. A7–A8)
- ~~(g)~~ ~~(g)~~ *IT environment* – The IT applications and supporting IT infrastructure, as well as the IT processes and personnel involved in those processes, that an entity uses to support business operations and achieve business strategies. For the purposes of this ISA: (NZ):
  - ~~(i)~~ ~~(iii)~~ An IT application is a program or a set of programs that is used in the initiation, processing, recording and reporting of transactions or information. IT applications include data warehouses and report writers.
  - ~~(ii)~~ ~~(iv)~~ The IT infrastructure comprises the network, operating systems, and databases and their related hardware and software.
  - ~~(iii)~~ ~~(v)~~ The IT processes are the entity's processes to manage access to the IT environment, manage program changes or changes to the IT environment and manage IT operations.
- ~~(h)~~ ~~(h)~~ *Relevant assertions* – An assertion about a class of transactions, account balance or disclosure is relevant when it has an identified risk of material misstatement. The determination of whether an assertion is a relevant assertion is made before consideration of any related controls (i.e., the inherent risk). (Ref: Para. A9)
- ~~(i)~~ ~~(i)~~ *Risks arising from the use of IT* – Susceptibility of information processing controls to ineffective design or operation, or risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information) in the entity's information system, due to ineffective design or operation of controls in the entity's IT processes (see IT environment).

<sup>11</sup> ISA- (NZ) 240, paragraphs A24–A27

- (j) ~~(j)~~ *Risk assessment procedures* – The audit procedures designed and performed to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.
- (k) ~~(k)~~ *Significant class of transactions, account balance or disclosure* – A class of transactions, account balance or disclosure for which there is one or more relevant assertions.
- (l) ~~(l)~~ *Significant risk* – An identified risk of material misstatement: (Ref: Para. A10)
- (i) 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 inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur; or
  - (ii) That is to be treated as a significant risk in accordance with the requirements of other ISAs- (NZ).<sup>12</sup>
- (m) ~~(m)~~ *System of internal control* – The system designed, implemented and maintained by those charged with governance, management and other personnel, to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. For the purposes of the ISAs- (NZ), the system of internal control consists of five inter-related components:
- (i) Control environment;
  - (ii) The entity's risk assessment process;
  - (iii) The entity's process to monitor the system of internal control;
  - (iv) The information system and communication; and
  - (v) Control activities.

## Requirements

### Risk Assessment Procedures and Related Activities

13. ~~13.~~—The auditor shall design and perform risk assessment procedures to obtain audit evidence that provides an appropriate basis for: (Ref: Para. A11–A18)
- (a) The identification and assessment of risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels; and
  - (b) The design of further audit procedures in accordance with ISA- (NZ) 330.

<sup>12</sup> ISA- (NZ) 240, paragraph 27 and ISA- (NZ) 550, *Related Parties*, paragraph 18

The auditor shall design and perform risk assessment 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. A14)

~~14.~~ 44.—The risk assessment procedures shall include the following: (Ref: Para. A19–A21)

- (a) ~~Inquiries~~Enquiries of management and of other appropriate individuals within the entity, including individuals within the internal audit function (if the function exists). (Ref: Para. A22–A26)
- (b) Analytical procedures. (Ref: Para. A27–A31)
- (c) Observation and inspection. (Ref: Para. A32–A36)

#### *Information from Other Sources*

~~15.~~ 45.—In obtaining audit evidence in accordance with paragraph 13, the auditor shall consider information from: (Ref: Para. A37–A38)

- (a) The auditor's procedures regarding acceptance or continuance of the client relationship or the audit engagement; and
- (b) When applicable, other engagements performed by the engagement partner for the entity.

~~16.~~ 46.—When the auditor intends to use information obtained from the auditor's previous experience with the entity and from audit procedures performed in previous audits, the auditor shall evaluate whether such information remains relevant and reliable as audit evidence for the current audit. (Ref: Para. A39–A41)

#### *Engagement Team Discussion*

~~17.~~ 47.—The engagement partner and other key engagement team members shall discuss the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement. (Ref: Para. A42–A47)

~~18.~~ 48.—When there are engagement team members not involved in the engagement team discussion, the engagement partner shall determine which matters are to be communicated to those members.

### **Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework and the Entity's System of Internal Control (Ref: Para. A48–A49)**

#### *Understanding the Entity and Its Environment, and the Applicable Financial Reporting Framework (Ref: Para. A50–A55)*

~~19.~~ 49.—The auditor shall perform risk assessment procedures to obtain an understanding of:

- ~~(a)~~ (a) The following aspects of the entity and its environment:

- (i) The entity's ~~organizational~~organisational structure, ownership and governance, and its business model, including the extent to which the business model integrates the use of IT; (Ref: Para. A56–A67)
- (ii) Industry, regulatory and other external factors; (Ref: Para. A68–A73) and
- (iii) The measures used, internally and externally, to assess the entity's financial performance; (Ref: Para. A74–A81)

~~(b)~~ The applicable financial reporting framework, and the entity's accounting policies and the reasons for any changes thereto; (Ref: Para. A82–A84) and

~~(c)~~ How inherent risk factors affect susceptibility of assertions to misstatement and the degree to which they do so, in the preparation of the financial statements in accordance with the applicable financial reporting framework, based on the understanding obtained in (a) and (b). (Ref: Para. A85–A89)

~~20.~~ 20. The auditor shall evaluate whether the entity's accounting policies are appropriate and consistent with the applicable financial reporting framework.

*Understanding the Components of the Entity's System of Internal Control* (Ref: Para. A90 – A95)

Control Environment, the Entity's Risk Assessment Process and the Entity's Process to Monitor the System of Internal Control (Ref: Para. A96–A98)

Control environment

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| <p><del>21.</del> 21. The auditor shall obtain an understanding of the control environment relevant to the preparation of the financial statements, through performing risk assessment procedures, by: (Ref: Para. A99–A100)</p>   |  |
| <p>(a) Understanding the set of controls, processes and structures that address: (Ref: Para. A101–A102)</p> <ul style="list-style-type: none"> <li>(i) How management's oversight responsibilities are carried out, such as the entity's culture and management's commitment to integrity and ethical values;</li> <li>(ii) When those charged with governance are separate from management, the independence of, and oversight over the entity's system of internal control by, those charged with governance;</li> <li>(iii) The entity's assignment of authority and responsibility;</li> </ul> | <p>and</p> <p>(b) Evaluating whether: (Ref: Para. A103–A108)</p> <ul style="list-style-type: none"> <li>(i) Management, with the oversight of those charged with governance, has created and maintained a culture of honesty and ethical <del>behavior</del>behaviour;</li> <li>(ii) The control environment provides an appropriate foundation for the other components of the entity's system of internal control</li> </ul> |



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| <ul style="list-style-type: none"> <li>(iv) How the entity attracts, develops, and retains competent individuals; and</li> <li>(v) How the entity holds individuals accountable for their responsibilities in the pursuit of the objectives of the system of internal control;</li> </ul> | <p>considering the nature and complexity of the entity; and</p> <p>(iii) Control deficiencies identified in the control environment undermine the other components of the entity's system of internal control.</p> |
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#### The entity's risk assessment process

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| <p><u>22.</u> <del>22.</del> The auditor shall obtain an understanding of the entity's risk assessment process relevant to the preparation of the financial statements, through performing risk assessment procedures, by:</p>  |  |
| <p>(a) Understanding the entity's process for: (Ref: Para. A109–A110)</p> <ul style="list-style-type: none"> <li>(i) Identifying business risks relevant to financial reporting objectives; (Ref: Para. A62)</li> <li>(ii) Assessing the significance of those risks, including the likelihood of their occurrence; and</li> <li>(iii) Addressing those risks;</li> </ul> | <p>and</p> <p>(b) Evaluating whether the entity's risk assessment process is appropriate to the entity's circumstances considering the nature and complexity of the entity. (Ref: Para. A111–A113)</p> |

23. ~~23.~~ If the auditor identifies risks of material misstatement that management failed to identify, the auditor shall:

- (a) Determine whether any such risks are of a kind that the auditor expects would have been identified by the entity's risk assessment process and, if so, obtain an understanding of why the entity's risk assessment process failed to identify such risks of material misstatement; and

(b) ~~(b)~~ Consider the implications for the auditor's evaluation in paragraph 22(b).

#### The entity's process to monitor the system of internal control

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| <p><u>24.</u> <del>24.</del> The auditor shall obtain an understanding of the entity's process for monitoring the system of internal control relevant to the preparation of the financial statements, through performing risk assessment procedures, by: (Ref: Para. A114–A115)</p> |   |
| <p>(a) Understanding those aspects of the entity's process that address:</p> <ul style="list-style-type: none"> <li>(i) Ongoing and separate evaluations for monitoring the effectiveness of controls, and the identification and remediation of control</li> </ul>                 | <p>and</p> <p>(c) Evaluating whether the entity's process for monitoring the system of internal control is appropriate to the entity's circumstances considering the nature and</p> |

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| <p>deficiencies identified; (Ref: Para. A116–A117) and</p> <p>(ii) The entity’s internal audit function, if any, including its nature, responsibilities and activities; (Ref: Para. A118)</p> <p>(b) Understanding the sources of the information used in the entity’s process to monitor the system of internal control, and the basis upon which management considers the information to be sufficiently reliable for the purpose; (Ref: Para. A119–A120)</p> | <p>complexity of the entity. (Ref: Para. A121–A122)</p> |
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Information System and Communication, and Control Activities (Ref: Para. A123–A130)

The information system and communication

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| <p><u>25.</u> <del>25.</del>—The auditor shall obtain an understanding of the entity’s information system and communication relevant to the preparation of the financial statements, through performing risk assessment procedures, by: (Ref: Para. A131)</p>  |  |
| <p>(a) Understanding the entity’s information processing activities, including its data and information, the resources to be used in such activities and the policies that define, for significant classes of transactions, account balances and disclosures: (Ref: Para. A132–A143)</p> <p>(i) How information flows through the entity’s information system, including how:</p> <p>a. Transactions are initiated, and how information about them is recorded, processed, corrected as necessary, incorporated in the general ledger and reported in the financial statements; and</p> <p>b. Information about events and conditions, other than transactions, is captured, processed and disclosed in the financial statements;</p> <p>(ii) The accounting records, specific accounts in the financial statements and other supporting records relating to the flows of information in the information system;</p> | <p>and</p> <p>(c) Evaluating whether the entity’s information system and communication appropriately support the preparation of the entity’s financial statements in accordance with the applicable financial reporting framework. (Ref: Para. A146)</p> |

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| <p>(iii) The financial reporting process used to prepare the entity's financial statements, including disclosures; and</p> <p>(iv) The entity's resources, including the IT environment, relevant to (a)(i) to (a)(iii) above;</p> <p>(b) Understanding how the entity communicates significant matters that support the preparation of the financial statements and related reporting responsibilities in the information system and other components of the system of internal control: (Ref: Para. A144–A145)</p> <p>(i) Between people within the entity, including how financial reporting roles and responsibilities are communicated;</p> <p>(ii) Between management and those charged with governance; and</p> <p>(iii) With external parties, such as those with regulatory authorities;</p> |  |
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#### Control activities

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| <p><u>26.</u> <del>26.</del>—The auditor shall obtain an understanding of the control activities component, through performing risk assessment procedures, by: (Ref: Para. A147–A157)</p>   |   |
| <p>(a) Identifying controls that address risks of material misstatement at the assertion level in the control activities component as follows:</p> <p>(i) Controls that address a risk that is determined to be a significant risk; (Ref: Para. A158–A159)</p> <p>(ii) Controls over journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments; (Ref: Para. A160–A161)</p> <p>(iii) Controls for which the auditor plans to test operating effectiveness in determining the nature, timing and extent of substantive testing, which shall include controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence; and (Ref: Para. A162–A164)</p> | <p>and</p> <p>(d) For each control identified in (a) or (c)(ii): (Ref: Para. A175–A181)</p> <p>(i) Evaluating whether the control is designed effectively to address the risk of material misstatement at the assertion level, or effectively designed to support the operation of other controls; and</p> <p>(ii) Determining whether the control has been implemented by performing procedures in</p> |

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| <p>(iv) Other controls that the auditor considers are appropriate to enable the auditor to meet the objectives of paragraph 13 with respect to risks at the assertion level, based on the auditor's professional judgment; (Ref: Para. A165)</p> <p>(b) Based on controls identified in (a), identifying the IT applications and the other aspects of the entity's IT environment that are subject to risks arising from the use of IT; (Ref: Para. A166–A172)</p> <p>(c) For such IT applications and other aspects of the IT environment identified in (b), identifying: (Ref: Para. A173–A174)</p> <p>(i) The related risks arising from the use of IT; and</p> <p>(ii) The entity's general IT controls that address such risks;</p> | <p>addition to inquiry of the entity's personnel.</p> |
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#### *Control Deficiencies Within the Entity's System of Internal Control*

27. ~~27.~~—Based on the auditor's evaluation of each of the components of the entity's system of internal control, the auditor shall determine whether one or more control deficiencies have been identified. (Ref: Para. A182–A183)

### **Identifying and Assessing the Risks of Material Misstatement (Ref: Para. A184–A185)**

#### *Identifying Risks of Material Misstatement*

28. ~~28.~~—The auditor shall identify the risks of material misstatement and determine whether they exist at: (Ref: Para. A186–A192)

- (a) The financial statement level; (Ref: Para. A193–A200) or
- (b) The assertion level for classes of transactions, account balances and disclosures. (Ref: Para. A201)

29. ~~29.~~—The auditor shall determine the relevant assertions and the related significant classes of transactions, account balances and disclosures. (Ref: Para. A202–A204)

#### *Assessing Risks of Material Misstatement at the Financial Statement Level*

30. ~~30.~~—For identified risks of material misstatement at the financial statement level, the auditor shall assess the risks and: (Ref: Para. A193–A200)

- (a) Determine whether such risks affect the assessment of risks at the assertion level; and
- (b) Evaluate the nature and extent of their pervasive effect on the financial statements.

*Assessing Risks of Material Misstatement at the Assertion Level*

Assessing Inherent Risk (Ref: Para. A205–A217)

- ~~31.~~ **34.**—For identified risks of material misstatement at the assertion level, the auditor shall assess inherent risk by assessing the likelihood and magnitude of misstatement. In doing so, the auditor shall take into account how, and the degree to which:
- (a) Inherent risk factors affect the susceptibility of relevant assertions to misstatement; and
  - (b) The risks of material misstatement at the financial statement level affect the assessment of inherent risk for risks of material misstatement at the assertion level. (Ref: Para. A215–A216)
- ~~32.~~ **32.**—The auditor shall determine whether any of the assessed risks of material misstatement are significant risks. (Ref: Para. A218–A221)
- ~~33.~~ **33.**—The auditor shall determine whether substantive procedures alone cannot provide sufficient appropriate audit evidence for any of the risks of material misstatement at the assertion level. (Ref: Para. A222–A225)

Assessing Control Risk

- ~~34.~~ **34.**—If the auditor plans to test the operating effectiveness of controls, the auditor shall assess control risk. If the auditor does not plan to test the operating effectiveness of controls, the auditor's assessment of control risk shall be such that the assessment of the risk of material misstatement is the same as the assessment of inherent risk. (Ref: Para. A226–A229)

*Evaluating the Audit Evidence Obtained from the Risk Assessment Procedures*

- ~~35.~~ **35.**—The auditor shall evaluate whether the audit evidence obtained from the risk assessment procedures provides an appropriate basis for the identification and assessment of the risks of material misstatement. If not, the auditor shall perform additional risk assessment procedures until audit evidence has been obtained to provide such a basis. In identifying and assessing the risks of material misstatement, the auditor shall take into account all audit evidence obtained from the risk assessment procedures, whether corroborative or contradictory to assertions made by management. (Ref: Para. A230–A232)

*Classes of Transactions, Account Balances and Disclosures that Are Not Significant, but Which Are Material*

- ~~36.~~ **36.**—For material classes of transactions, account balances or disclosures that have not been determined to be significant classes of transactions, account balances or disclosures, the auditor shall evaluate whether the auditor's determination remains appropriate. (Ref: Para. A233–A235)

## Revision of Risk Assessment

37. 37. If the auditor obtains new information which is inconsistent with the audit evidence on which the auditor originally based the identification or assessments of the risks of material misstatement, the auditor shall revise the identification or assessment. (Ref: Para. A236)

## Documentation

38. 38. The auditor shall include in the audit documentation:<sup>13</sup> (Ref: Para. A237–A241)
- (a) The discussion among the engagement team and the significant decisions reached;
  - (b) Key elements of the auditor's understanding in accordance with paragraphs 19, 21, 22, 24 and 25; the sources of information from which the auditor's understanding was obtained; and the risk assessment procedures performed;
  - (c) The evaluation of the design of identified controls, and determination whether such controls have been implemented, in accordance with the requirements in paragraph 26; and
  - (d) The identified and assessed risks of material misstatement at the financial statement level and at the assertion level, including significant risks and risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence, and the rationale for the significant judgments made.

## Application and Other Explanatory Material

### Definitions (Ref: Para. 12)

#### Assertions (Ref: Para. 12(a))

- A1. Categories of assertions are used by auditors to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement. Examples of these categories of assertions are described in paragraph A190. The assertions differ from the written representations required by ISA (NZ) 580,<sup>14</sup> to confirm certain matters or support other audit evidence.

#### Controls (Ref: Para. 12(c))

- A2. Controls are embedded within the components of the entity's system of internal control.
- A3. Policies are implemented through the actions of personnel within the entity, or through the restraint of personnel from taking actions that would conflict with such policies.
- A4. Procedures may be mandated, through formal documentation or other communication by management or those charged with governance, or may result from behaviours.

<sup>13</sup> ISA (NZ) 230, Audit Documentation, paragraphs 8–11, and A6–A7

<sup>14</sup> ISA (NZ) 580, Written Representations

that are not mandated but are rather conditioned by the entity's culture. Procedures may be enforced through the actions permitted by the IT applications used by the entity or other aspects of the entity's IT environment.

- A5. Controls may be direct or indirect. Direct controls are controls that are precise enough to address risks of material misstatement at the assertion level. Indirect controls are controls that support direct controls.

*Information Processing Controls* (Ref: Para. 12(e))

- A6. Risks to the integrity of information arise from susceptibility to ineffective implementation of the entity's information policies, which are policies that define the information flows, records and reporting processes in the entity's information system. Information processing controls are procedures that support effective implementation of the entity's information policies. Information processing controls may be automated (i.e., embedded in IT applications) or manual (e.g., input or output controls) and may rely on other controls, including other information processing controls or general IT controls.

*Inherent Risk Factors* (Ref: Para. 12(f))

**Appendix 2** sets out further considerations relating to understanding inherent risk factors.

- A7. Inherent risk factors may be qualitative or quantitative and affect the susceptibility of assertions to misstatement. Qualitative inherent risk factors relating to the preparation of information required by the applicable financial reporting framework include:
- Complexity;
  - Subjectivity;
  - Change;
  - Uncertainty; or
  - Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk.
- A8. Other inherent risk factors, that affect susceptibility to misstatement of an assertion about a class of transactions, account balance or disclosure may include:
- The quantitative or qualitative significance of the class of transactions, account balance or disclosure; or
  - The volume or a lack of uniformity in the composition of the items to be processed through the class of transactions or account balance, or to be reflected in the disclosure.

*Relevant Assertions* (Ref: Para. 12(h))

- A9. A risk of material misstatement may relate to more than one assertion, in which case all the assertions to which such a risk relates are relevant assertions. If an assertion does not have an identified risk of material misstatement, then it is not a relevant assertion.

*Significant Risk* (Ref: Para. 12(l))

- A10. Significance can be described as the relative importance of a matter, and is judged by the auditor in the context in which the matter is being considered. For inherent risk, significance may be considered in the context of how, and the degree to which, inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur.

**Risk Assessment Procedures and Related Activities** (Ref: Para. 13–18)

- A11. The risks of material misstatement to be identified and assessed include both those due to fraud and those due to error, and both are covered by this ISA- (NZ). However, the significance of fraud is such that further requirements and guidance are included in ISA- (NZ) 240 in relation to risk assessment procedures and related activities to obtain information that is used to identify and assess the risks of material misstatement due to fraud.<sup>15</sup> In addition, the following ISAs (NZ) provide further requirements and guidance on identifying and assessing risks of material misstatement regarding specific matters or circumstances:

- ISA- (NZ) 540 (Revised)<sup>16</sup> in regard to accounting estimates;
- ISA- (NZ) 550<sup>22</sup> in regard to related party relationships and transactions;
- ISA- (NZ) 570 (Revised)<sup>17</sup> in regard to going concern; and
- ISA- (NZ) 600<sup>18</sup> in regard to group financial statements.

- A12. Professional ~~skepticism~~scepticism is necessary for the critical assessment of audit evidence gathered when performing the risk assessment procedures, and assists the auditor in remaining alert to audit evidence that is not biased towards corroborating the existence of risks or that may be contradictory to the existence of risks. Professional ~~skepticism~~scepticism is an attitude that is applied by the auditor when making professional ~~judgments~~judgements that then provides the basis for the auditor's actions. The auditor applies professional ~~judgment~~judgement in determining when the auditor has audit evidence that provides an appropriate basis for risk assessment.

<sup>15</sup> ISA- (NZ) 240, paragraphs 12–27

<sup>16</sup> ISA- (NZ) 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

<sup>17</sup> ISA- (NZ) 570 (Revised), *Going Concern*

<sup>18</sup> ISA- (NZ) 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*



A13. The application of professional ~~skepticism~~scepticism by the auditor may include:

- Questioning contradictory information and the reliability of documents;
- Considering responses to ~~inquiries~~enquiries and other information obtained from management and those charged with governance;
- Being alert to conditions that may indicate possible misstatement due to fraud or error; and
- Considering whether audit evidence obtained supports the auditor's identification and assessment of the risks of material misstatement in light of the entity's nature and circumstances.

*Why Obtaining Audit Evidence in an Unbiased Manner Is Important* (Ref: Para. 13)

A14. Designing and performing risk assessment procedures to obtain audit evidence to support the identification and assessment of the risks of material misstatement in an unbiased manner may assist the auditor in identifying potentially contradictory information, which may assist the auditor in exercising professional ~~skepticism~~scepticism in identifying and assessing the risks of material misstatement.

*Sources of Audit Evidence* (Ref: Para. 13)

A15. Designing and performing risk assessment procedures to obtain audit evidence in an unbiased manner may involve obtaining evidence from multiple sources within and outside the entity. However, the auditor is not required to perform an exhaustive search to identify all possible sources of audit evidence. In addition to information from other sources<sup>19</sup>, sources of information for risk assessment procedures may include:

- Interactions with management, those charged with governance, and other key entity personnel, such as internal auditors.
- Certain external parties such as regulators, whether obtained directly or indirectly.
- Publicly available information about the entity, for example entity-issued press releases, materials for analysts or investor group meetings, analysts' reports or information about trading activity.

Regardless of the source of information, the auditor considers the relevance and reliability of the information to be used as audit evidence in accordance with ISA- (NZ) 500.<sup>20</sup>

*Scalability* (Ref: Para. 13)

A16. The nature and extent of risk assessment procedures will vary based on the nature and circumstances of the entity (e.g., the formality of the entity's policies and procedures, and

<sup>19</sup> See paragraph A37 and A38.

<sup>20</sup> ISA- (NZ) 500, *Audit Evidence*, paragraph 7

processes and systems). The auditor uses professional ~~judgment~~judgement to determine the nature and extent of the risk assessment procedures to be performed to meet the requirements of this ISA- (NZ).

- A17. Although the extent to which an entity's policies and procedures, and processes and systems are formalized may vary, the auditor is still required to obtain the understanding in accordance with paragraphs 19, 21, 22, 24, 25 and 26.

**Examples:**

Some entities, including less complex entities, and particularly owner-managed entities, may not have established structured processes and systems (e.g., a risk assessment process or a process to monitor the system of internal control) or may have established processes or systems with limited documentation or a lack of consistency in how they are undertaken. When such systems and processes lack formality, the auditor may still be able to perform risk assessment procedures through observation and ~~inquiry~~enquiry.

Other entities, typically more complex entities, are expected to have more formalized and documented policies and procedures. The auditor may use such documentation in performing risk assessment procedures.

- A18. The nature and extent of risk assessment procedures to be performed the first time an engagement is undertaken may be more extensive than procedures for a recurring engagement. In subsequent periods, the auditor may focus on changes that have occurred since the preceding period.

*Types of Risk Assessment Procedures* (Ref: Para. 14)

- A19. ISA- (NZ) 500<sup>21</sup> explains the types of audit procedures that may be performed in obtaining audit evidence from risk assessment procedures and further audit procedures. The nature, timing and extent of the audit procedures may be affected by the fact that some of the accounting data and other evidence may only be available in electronic form or only at certain points in time.<sup>22</sup> The auditor may perform substantive procedures or tests of controls, in accordance with ISA— (NZ) 330, concurrently with risk assessment procedures, when it is efficient to do so. Audit evidence obtained that supports the identification and assessment of risks of material misstatement may also support the detection of misstatements at the assertion level or the evaluation of the operating effectiveness of controls.
- A20. Although the auditor is required to perform all the risk assessment procedures described in paragraph 14 in the course of obtaining the required understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control (see paragraphs 19–26), the auditor is not required to perform all of them

<sup>21</sup> ISA- (NZ) 500, paragraphs A14–A17 and A21–A25

<sup>22</sup> ISA- (NZ) 500, paragraph A12

for each aspect of that understanding. Other procedures may be performed when the information to be obtained may be helpful in identifying risks of material misstatement. Examples of such procedures may include making ~~inquiries~~enquiries of the entity's external legal counsel or external supervisors, or of valuation experts that the entity has used.

#### Automated Tools and Techniques (Ref: Para. 14)

- A21. Using automated tools and techniques, the auditor may perform risk assessment procedures on large volumes of data (from the general ledger, sub-ledgers or other operational data) including for analysis, recalculations, reperformance or reconciliations.

#### ~~Inquiries~~Enquiries of Management and Others within the Entity (Ref: Para. 14(a))

#### Why ~~Inquiries~~Enquiries Are Made of Management and Others Within the Entity

- A22. Information obtained by the auditor to support an appropriate basis for the identification and assessment of risks, and the design of further audit procedures, may be obtained through ~~inquiries~~enquiries of management and those responsible for financial reporting.
- A23. ~~Inquiries~~Enquiries of management and those responsible for financial reporting and of other appropriate individuals within the entity and other employees with different levels of authority may offer the auditor varying perspectives when identifying and assessing risks of material misstatement.

#### Examples:

- ~~Inquiries~~Enquiries directed towards those charged with governance may help the auditor understand the extent of oversight by those charged with governance over the preparation of the financial statements by management. ISA (NZ) 260 (Revised)<sup>23</sup> identifies the importance of effective two-way communication in assisting the auditor to obtain information from those charged with governance in this regard.
- ~~Inquiries~~Enquiries of employees responsible for initiating, processing or recording complex or unusual transactions may help the auditor to evaluate the appropriateness of the selection and application of certain accounting policies.
- ~~Inquiries~~Enquiries directed towards in-house legal counsel may provide information about such matters as litigation, compliance with laws and regulations, knowledge of fraud or suspected fraud affecting the entity, warranties, post-sales obligations, arrangements (such as joint ventures) with business partners, and the meaning of contractual terms.
- ~~Inquiries~~Enquiries directed towards marketing or sales personnel may provide information about changes in the entity's marketing strategies, sales trends, or contractual arrangements with its customers.

<sup>23</sup> ISA (NZ) 260 (Revised), *Communication with Those Charged with Governance*, paragraph 4(b)

- [InquiriesEnquiries](#) directed towards the risk management function (or [inquiriesenquiries](#) of those performing such roles) may provide information about operational and regulatory risks that may affect financial reporting.
- [InquiriesEnquiries](#) directed towards IT personnel may provide information about system changes, system or control failures, or other IT-related risks.

#### Considerations Specific to Public Sector Entities

- A24. When making [inquiriesenquiries](#) of those who may have information that is likely to assist in identifying risks of material misstatement, auditors of public sector entities may obtain information from additional sources such as from the auditors that are involved in performance or other audits related to the entity.

#### [InquiriesEnquiries](#) of the Internal Audit Function

**Appendix 4** sets out considerations for understanding an entity's internal audit function.

#### Why [inquiriesenquiries](#) are made of the internal audit function (if the function exists)

- A25. If an entity has an internal audit function, [inquiriesenquiries](#) of the appropriate individuals within the function may assist the auditor in understanding the entity and its environment, and the entity's system of internal control, in the identification and assessment of risks.

#### Considerations specific to public sector entities

- A26. Auditors of public sector entities often have additional responsibilities with regard to internal control and compliance with applicable laws and regulations. [InquiriesEnquiries](#) of appropriate individuals in the internal audit function may assist the auditors in identifying the risk of material non-compliance with applicable laws and regulations, and the risk of control deficiencies related to financial reporting.

#### *Analytical Procedures* (Ref: Para. 14(b))

#### Why Analytical Procedures Are Performed as a Risk Assessment Procedure

- A27. Analytical procedures help identify inconsistencies, unusual transactions or events, and amounts, ratios, and trends that indicate matters that may have audit implications. Unusual or unexpected relationships that are identified may assist the auditor in identifying risks of material misstatement, especially risks of material misstatement due to fraud.
- A28. Analytical procedures performed as risk assessment procedures may therefore assist in identifying and assessing the risks of material misstatement by identifying aspects of the entity of which the auditor was unaware or understanding how inherent risk factors, such as change, affect susceptibility of assertions to misstatement.

## Types of Analytical Procedures

A29. Analytical procedures performed as risk assessment procedures may:

- Include both financial and non-financial information, for example, the relationship between sales and square footage of selling space or volume of goods sold (non-financial).
- Use data aggregated at a high level. Accordingly, the results of those analytical procedures may provide a broad initial indication about the likelihood of a material misstatement.

**Example:**

In the audit of many entities, including those with less complex business models and processes, and a less complex information system, the auditor may perform a simple comparison of information, such as the change in interim or monthly account balances from balances in prior periods, to obtain an indication of potentially higher risk areas.

A30. This ISA- (NZ) deals with the auditor's use of analytical procedures as risk assessment procedures. ISA- (NZ) 520<sup>24</sup> deals with the auditor's use of analytical procedures as substantive procedures ("substantive analytical procedures") and the auditor's responsibility to perform analytical procedures near the end of the audit. Accordingly, analytical procedures performed as risk assessment procedures are not required to be performed in accordance with the requirements of ISA- (NZ) 520. However, the requirements and application material in ISA- (NZ) 520 may provide useful guidance to the auditor when performing analytical procedures as part of the risk assessment procedures.

## Automated tools and techniques

A31. Analytical procedures can be performed using a number of tools or techniques, which may be automated. Applying automated analytical procedures to the data may be referred to as data analytics.

**Example:**

The auditor may use a spreadsheet to perform a comparison of actual recorded amounts to budgeted amounts, or may perform a more advanced procedure by extracting data from the entity's information system, and further ~~analyzing~~[analysing](#) this data using ~~visualization~~[visualisation](#) techniques to identify classes of transactions, account balances or disclosures for which further specific risk assessment procedures may be warranted.

<sup>24</sup> ISA- (NZ) 520, *Analytical Procedures*

*Observation and Inspection* (Ref: Para. 14(c))

Why Observation and Inspection Are Performed as Risk Assessment Procedures

- A32. Observation and inspection may support, corroborate or contradict ~~inquiries~~enquiries of management and others, and may also provide information about the entity and its environment.

Scalability

- A33. Where policies or procedures are not documented, or the entity has less ~~formalized~~formalised controls, the auditor may still be able to obtain some audit evidence to support the identification and assessment of the risks of material misstatement through observation or inspection of the performance of the control.

**Examples:**

- The auditor may obtain an understanding of controls over an inventory count, even if they have not been documented by the entity, through direct observation.
- The auditor may be able to observe segregation of duties.
- The auditor may be able to observe passwords being entered.

Observation and Inspection as Risk Assessment Procedures

- A34. Risk assessment procedures may include observation or inspection of the following:

- The entity's operations.
- Internal documents (such as business plans and strategies), records, and internal control manuals.
- Reports prepared by management (such as quarterly management reports and interim financial statements) and those charged with governance (such as minutes of board of directors' meetings).
- The entity's premises and plant facilities.
- Information obtained from external sources such as trade and economic journals; reports by analysts, banks, or rating agencies; regulatory or financial publications; or other external documents about the entity's financial performance (such as those referred to in paragraph A79).
- The ~~behaviors~~behaviours and actions of management or those charged with governance (such as the observation of an audit committee meeting).

Automated tools and techniques

- A35. Automated tools or techniques may also be used to observe or inspect, in particular assets, for example through the use of remote observation tools (e.g., a drone).

## Considerations Specific to Public Sector Entities

A36. Risk assessment procedures performed by auditors of public sector entities may also include observation and inspection of documents prepared by management for the legislature, for example documents related to mandatory performance reporting.

## *Information from Other Sources* (Ref: Para. 15)

### Why the Auditor Considers Information from Other Sources

A37. Information obtained from other sources may be relevant to the identification and assessment of the risks of material misstatement by providing information and insights about:

- The nature of the entity and its business risks, and what may have changed from previous periods.
- The integrity and ethical values of management and those charged with governance, which may also be relevant to the auditor's understanding of the control environment.
- The applicable financial reporting framework and its application to the nature and circumstances of the entity.

### Other Relevant Sources

A38. Other relevant sources of information include:

- The auditor's procedures regarding acceptance or continuance of the client relationship or the audit engagement in accordance with ISA- (NZ) 220, including the conclusions reached thereon.<sup>25</sup>
- Other engagements performed for the entity by the engagement partner. The engagement partner may have obtained knowledge relevant to the audit, including about the entity and its environment, when performing other engagements for the entity. Such engagements may include agreed-upon procedures engagements or other audit or assurance engagements, including engagements to address incremental reporting requirements in the jurisdiction.

### Information from the Auditor's Previous Experience with the Entity and Previous Audits (Ref: Para. 16)

#### Why information from previous audits is important to the current audit

A39. The auditor's previous experience with the entity and from audit procedures performed in previous audits may provide the auditor with information that is relevant to the auditor's

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<sup>25</sup> ISA- (NZ) 220, *Quality Control for an Audit of Financial Statements*, paragraph 12



determination of the nature and extent of risk assessment procedures, and the identification and assessment of risks of material misstatement.

#### Nature of the Information from Previous Audits

A40. The auditor's previous experience with the entity and audit procedures performed in previous audits may provide the auditor with information about such matters as:

- Past misstatements and whether they were corrected on a timely basis.
- The nature of the entity and its environment, and the entity's system of internal control (including control deficiencies).
- Significant changes that the entity or its operations may have undergone since the prior financial period.
- Those particular types of transactions and other events or account balances (and related disclosures) where the auditor experienced difficulty in performing the necessary audit procedures, for example, due to their complexity.

A41. The auditor is required to determine whether information obtained from the auditor's previous experience with the entity and from audit procedures performed in previous audits remains relevant and reliable, if the auditor intends to use that information for the purposes of the current audit. If the nature or circumstances of the entity have changed, or new information has been obtained, the information from prior periods may no longer be relevant or reliable for the current audit. To determine whether changes have occurred that may affect the relevance or reliability of such information, the auditor may make [inquiriesenquiries](#) and perform other appropriate audit procedures, such as walk-throughs of relevant systems. If the information is not reliable, the auditor may consider performing additional procedures that are appropriate in the circumstances.

#### Engagement Team Discussion (Ref: Para. 17–18)

Why the Engagement Team Is Required to Discuss the Application of the Applicable Financial Reporting Framework and the Susceptibility of the Entity's Financial Statements to Material Misstatement

A42. The discussion among the engagement team about the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement:

- Provides an opportunity for more experienced engagement team members, including the engagement partner, to share their insights based on their knowledge of the entity. Sharing information contributes to an enhanced understanding by all engagement team members.
- Allows the engagement team members to exchange information about the business risks to which the entity is subject, how inherent risk factors may affect the



susceptibility to misstatement of classes of transactions, account balances and disclosures, and about how and where the financial statements might be susceptible to material misstatement due to fraud or error.

- Assists the engagement team members to gain a better understanding of the potential for material misstatement of the financial statements in the specific areas assigned to them, and to understand how the results of the audit procedures that they perform may affect other aspects of the audit, including the decisions about the nature, timing and extent of further audit procedures. In particular, the discussion assists engagement team members in further considering contradictory information based on each member's own understanding of the nature and circumstances of the entity.
- Provides a basis upon which engagement team members communicate and share new information obtained throughout the audit that may affect the assessment of risks of material misstatement or the audit procedures performed to address these risks.

ISA- (NZ) 240 requires the engagement team discussion to place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud may occur.<sup>26</sup>

- A43. Professional ~~skepticism~~scepticism is necessary for the critical assessment of audit evidence, and a robust and open engagement team discussion, including for recurring audits, may lead to improved identification and assessment of the risks of material misstatement. Another outcome from the discussion may be that the auditor identifies specific areas of the audit for which exercising professional ~~skepticism~~scepticism may be particularly important, and may lead to the involvement of more experienced members of the engagement team who are appropriately skilled to be involved in the performance of audit procedures related to those areas.

#### Scalability

- A44. When the engagement is carried out by a single individual, such as a sole practitioner (i.e., where an engagement team discussion would not be possible), consideration of the matters referred to in paragraphs A42 and A46 nonetheless may assist the auditor in identifying where there may be risks of material misstatement.
- A45. When an engagement is carried out by a large engagement team, such as for an audit of group financial statements, it is not always necessary or practical for the discussion to include all members in a single discussion (for example, in a multi-location audit), nor is it necessary for all the members of the engagement team to be informed of all the decisions reached in the discussion. The engagement partner may discuss matters with key members of the engagement team including, if considered appropriate, those with specific skills or knowledge, and those responsible for the audits of components, while delegating discussion with others, taking into account the extent of communication considered

<sup>26</sup> ISA- (NZ) 240, paragraph 16

necessary throughout the engagement team. A communications plan, agreed by the engagement partner, may be useful.

#### Discussion of Disclosures in the Applicable Financial Reporting Framework

A46. As part of the discussion among the engagement team, consideration of the disclosure requirements of the applicable financial reporting framework assists in identifying early in the audit where there may be risks of material misstatement in relation to disclosures, even in circumstances where the applicable financial reporting framework only requires simplified disclosures. Matters the engagement team may discuss include:

- Changes in financial reporting requirements that may result in significant new or revised disclosures;
- Changes in the entity's environment, financial condition or activities that may result in significant new or revised disclosures, for example, a significant business combination in the period under audit;
- Disclosures for which obtaining sufficient appropriate audit evidence may have been difficult in the past; and
- Disclosures about complex matters, including those involving significant management judgement as to what information to disclose.

#### Considerations Specific to Public Sector Entities

A47. As part of the discussion among the engagement team by auditors of public sector entities, consideration may also be given to any additional broader objectives, and related risks, arising from the audit mandate or obligations for public sector entities.

#### Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework and the Entity's System of Internal Control (Ref: Para. 19–27)

**Appendices 1 through 6** set out further considerations relating to obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control.

#### *Obtaining the Required Understanding* (Ref: Para. 19–27)

A48. Obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control is a dynamic and iterative process of gathering, updating and analyzing information and continues throughout the audit. Therefore, the auditor's expectations may change as new information is obtained.

A49. The auditor's understanding of the entity and its environment and the applicable financial reporting framework may also assist the auditor in developing initial expectations about

the classes of transactions, account balances and disclosures that may be significant classes of transactions, account balances and disclosures. These expected significant classes of transactions, account balances and disclosures form the basis for the scope of the auditor's understanding of the entity's information system.

*Why an Understanding of the Entity and Its Environment, and the Applicable Financial Reporting Framework Is Required* (Ref: Para. 19–20)

A50. The auditor's understanding of the entity and its environment, and the applicable financial reporting framework, assists the auditor in understanding the events and conditions that are relevant to the entity, and in identifying how inherent risk factors affect the susceptibility of assertions to misstatement in the preparation of the financial statements, in accordance with the applicable financial reporting framework, and the degree to which they do so. Such information establishes a frame of reference within which the auditor identifies and assesses risks of material misstatement. This frame of reference also assists the auditor in planning the audit and exercising professional ~~judgment~~judgement and professional ~~skepticism~~scepticism throughout the audit, for example, when:

- Identifying and assessing risks of material misstatement of the financial statements in accordance with ISA- (NZ) 315 (Revised) or other relevant standards (e.g., relating to risks of fraud in accordance with ISA- (NZ) 240 or when identifying or assessing risks related to accounting estimates in accordance with ISA- (NZ) 540 (Revised));
- Performing procedures to help identify instances of non-compliance with laws and regulations that may have a material effect on the financial statements in accordance with ISA- (NZ) 250;<sup>27</sup>
- Evaluating whether the financial statements provide adequate disclosures in accordance with ISA- (NZ) 700 (Revised);<sup>28</sup>
- Determining materiality or performance materiality in accordance with ISA- (NZ) 320;<sup>29</sup> or
- Considering the appropriateness of the selection and application of accounting policies, and the adequacy of financial statement disclosures.

A51. [Amended by the NZAuASB]

<sup>27</sup> ISA- (NZ) 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraph 14

<sup>28</sup> ISA- (NZ) 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 13(e)

<sup>29</sup> ISA- (NZ) 320, *Materiality in Planning and Performing an Audit*, paragraphs 10–11

NZ A51. The auditor's understanding of the entity and its environment, and the applicable financial reporting framework, also informs how the auditor plans and performs further audit procedures, for example, when:

- Developing expectations for use when performing analytical procedures in accordance with ISA- (NZ) 520;<sup>30</sup>
- Designing and performing further audit procedures to obtain sufficient appropriate audit evidence in accordance with ISA- (NZ) 330; and
- Evaluating the sufficiency and appropriateness of audit evidence obtained (e.g., relating to assumptions or management's and, where appropriate, those charged with governance's oral and written representations).

#### Scalability

A52. The nature and extent of the required understanding is a matter of the auditor's professional ~~judgment~~judgement and varies from entity to entity based on the nature and circumstances of the entity, including:

- The size and complexity of the entity, including its IT environment;
- The auditor's previous experience with the entity;
- The nature of the entity's systems and processes, including whether they are ~~formalized~~formalised or not; and
- The nature and form of the entity's documentation.

A53. The auditor's risk assessment procedures to obtain the required understanding may be less extensive in audits of less complex entities and more extensive for entities that are more complex. The depth of the understanding that is required by the auditor is expected to be less than that possessed by management in managing the entity.

A54. Some financial reporting frameworks allow smaller entities to provide simpler and less detailed disclosures in the financial statements. However, this does not relieve the auditor of the responsibility to obtain an understanding of the entity and its environment and the applicable financial reporting framework as it applies to the entity.

A55. The entity's use of IT and the nature and extent of changes in the IT environment may also affect the ~~specialized~~specialised skills that are needed to assist with obtaining the required understanding.

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<sup>30</sup> ISA- (NZ) 520, paragraph 5

*The Entity and Its Environment* (Ref: Para. 19(a))

The Entity's ~~Organizational~~Organisational Structure, Ownership and Governance, and Business Model (Ref: Para. 19(a)(i))

The entity's ~~organizational~~organisational structure and ownership

A56. An understanding of the entity's ~~organizational~~organisational structure and ownership may enable the auditor to understand such matters as:

- The complexity of the entity's structure.

**Example:**

The entity may be a single entity or the entity's structure may include subsidiaries, divisions or other components in multiple locations. Further, the legal structure may be different from the operating structure. Complex structures often introduce factors that may give rise to increased susceptibility to risks of material misstatement. Such issues may include whether goodwill, joint ventures, investments, or special-purpose entities are accounted for appropriately and whether adequate disclosure of such issues in the financial statements has been made.

- The ownership, and relationships between owners and other people or entities, including related parties. This understanding may assist in determining whether related party transactions have been appropriately identified, accounted for, and adequately disclosed in the financial statements.<sup>31</sup>
- The distinction between the owners, those charged with governance and management.

**Example:**

In less complex entities, owners of the entity may be involved in managing the entity, therefore there is little or no distinction. In contrast, such as in some listed entities, there may be a clear distinction between management, the owners of the entity, and those charged with governance.<sup>32</sup>

- The structure and complexity of the entity's IT environment.

<sup>31</sup> ISA- (NZ) 550 establishes requirements and provide guidance on the auditor's considerations relevant to related parties.

<sup>32</sup> ISA- (NZ) 260 (Revised), paragraphs A1 and A2, provide guidance on the identification of those charged with governance and explains that in some cases, some or all of those charged with governance may be involved in managing the entity.

**Examples:**

An entity may:

- Have multiple legacy IT systems in diverse businesses that are not well integrated resulting in a complex IT environment.
- Be using external or internal service providers for aspects of its IT environment (e.g., outsourcing the hosting of its IT environment to a third party or using a shared service centre for central management of IT processes in a group).

### Automated tools and techniques

- A57. The auditor may use automated tools and techniques to understand flows of transactions and processing as part of the auditor's procedures to understand the information system. An outcome of these procedures may be that the auditor obtains information about the entity's ~~organizational~~ organisational structure or those with whom the entity conducts business (e.g., vendors, customers, related parties).

### Considerations specific to public sector entities

- A58. Ownership of a public sector entity may not have the same relevance as in the private sector because decisions related to the entity may be made outside of the entity as a result of political processes. Therefore, management may not have control over certain decisions that are made. Matters that may be relevant include understanding the ability of the entity to make unilateral decisions, and the ability of other public sector entities to control or influence the entity's mandate and strategic direction.

**Example:**

A public sector entity may be subject to laws or other directives from authorities that require it to obtain approval from parties external to the entity of its strategy and objectives prior to it implementing them. Therefore, matters related to understanding the legal structure of the entity may include applicable laws and regulations, and the classification of the entity (i.e., whether the entity is a ministry, department, agency or other type of entity).

### Governance

#### Why the auditor obtains an understanding of governance

- A59. Understanding the entity's governance may assist the auditor with understanding the entity's ability to provide appropriate oversight of its system of internal control. However, this understanding may also provide evidence of deficiencies, which may indicate an increase in the susceptibility of the entity's financial statements to risks of material misstatement.

## Understanding the entity's governance

A60. Matters that may be relevant for the auditor to consider in obtaining an understanding of the governance of the entity include:

- Whether any or all of those charged with governance are involved in managing the entity.
- The existence (and separation) of a non-executive Board, if any, from executive management.
- Whether those charged with governance hold positions that are an integral part of the entity's legal structure, for example as directors.
- The existence of sub-groups of those charged with governance, such as an audit committee, and the responsibilities of such a group.
- The responsibilities of those charged with governance for oversight of financial reporting, including approval of the financial statements.

## The Entity's Business Model

**Appendix 1** sets out additional considerations for obtaining an understanding of the entity and its business model, as well as additional considerations for auditing special purpose entities.

## Why the auditor obtains an understanding of the entity's business model

A61. Understanding the entity's objectives, strategy and business model helps the auditor to understand the entity at a strategic level, and to understand the business risks the entity takes and faces. An understanding of the business risks that have an effect on the financial statements assists the auditor in identifying risks of material misstatement, since most business risks will eventually have financial consequences and, therefore, an effect on the financial statements.

**Examples:**

An entity's business model may rely on the use of IT in different ways:

- The entity sells shoes from a physical store, and uses an advanced stock and point of sale system to record the selling of shoes; or
- The entity sells shoes online so that all sales transactions are processed in an IT environment, including initiation of the transactions through a website.

For both of these entities the business risks arising from a significantly different business model would be substantially different, notwithstanding both entities sell shoes.

Understanding the entity's business model

- A62. Not all aspects of the business model are relevant to the auditor's understanding. Business risks are broader than the risks of material misstatement of the financial statements, although business risks include the latter. The auditor does not have a responsibility to understand or identify all business risks because not all business risks give rise to risks of material misstatement.
- A63. Business risks increasing the susceptibility to risks of material misstatement may arise from:
- Inappropriate objectives or strategies, ineffective execution of strategies, or change or complexity.
  - A failure to ~~recognize~~recognise the need for change may also give rise to business risk, for example, from:
    - The development of new products or services that may fail;
    - A market which, even if successfully developed, is inadequate to support a product or service; or
    - Flaws in a product or service that may result in legal liability and reputational risk.
  - Incentives and pressures on management, which may result in intentional or unintentional management bias, and therefore affect the reasonableness of significant assumptions and the expectations of management or those charged with governance.
- A64. Examples of matters that the auditor may consider when obtaining an understanding of the entity's business model, objectives, strategies and related business risks that may result in a risk of material misstatement of the financial statements include:
- Industry developments, such as the lack of personnel or expertise to deal with the changes in the industry;
  - New products and services that may lead to increased product liability;
  - Expansion of the entity's business, and demand has not been accurately estimated;
  - New accounting requirements where there has been incomplete or improper implementation;
  - Regulatory requirements resulting in increased legal exposure;
  - Current and prospective financing requirements, such as loss of financing due to the entity's inability to meet requirements;
  - Use of IT, such as the implementation of a new IT system that will affect both operations and financial reporting; or



- The effects of implementing a strategy, particularly any effects that will lead to new accounting requirements.

A65. Ordinarily, management identifies business risks and develops approaches to address them. Such a risk assessment process is part of the entity's system of internal control and is discussed in paragraph 22, and paragraphs A109–A113.

#### Considerations specific to public sector entities

A66. Entities operating in the public sector may create and deliver value in different ways to those creating wealth for owners but will still have a 'business model' with a specific objective. Matters public sector auditors may obtain an understanding of that are relevant to the business model of the entity, include:

- Knowledge of relevant government activities, including related [programsprogrammes](#).
- [ProgramProgramme](#) objectives and strategies, including public policy elements.

A67. For the audits of public sector entities, "management objectives" may be influenced by requirements to demonstrate public accountability and may include objectives which have their source in law, regulation or other authority.

#### Industry, Regulatory and Other External Factors (Ref: Para. 19(a)(ii))

##### Industry factors

A68. Relevant industry factors include industry conditions such as the competitive environment, supplier and customer relationships, and technological developments. Matters the auditor may consider include:

- The market and competition, including demand, capacity, and price competition.
- Cyclical or seasonal activity.
- Product technology relating to the entity's products.
- Energy supply and cost.

A69. The industry in which the entity operates may give rise to specific risks of material misstatement arising from the nature of the business or the degree of regulation.

##### **Example:**

In the construction industry, long-term contracts may involve significant estimates of revenues and expenses that give rise to risks of material misstatement. In such cases, it is important that the engagement team include members with sufficient relevant knowledge and experience.<sup>33</sup>

<sup>33</sup> ISA- (NZ) 220, paragraph 14

## Regulatory factors

A70. Relevant regulatory factors include the regulatory environment. The regulatory environment encompasses, among other matters, the applicable financial reporting framework and the legal and political environment and any changes thereto. Matters the auditor may consider include:

- Regulatory framework for a regulated industry, for example, prudential requirements, including related disclosures.
- Legislation and regulation that significantly affect the entity's operations, for example, labor laws and regulations.
- Taxation legislation and regulations.
- Government policies currently affecting the conduct of the entity's business, such as monetary, including foreign exchange controls, fiscal, financial incentives (for example, government aid ~~programs~~programmes), and tariffs or trade restriction policies.
- Environmental requirements affecting the industry and the entity's business.

A71. ISA- (NZ) 250 (Revised) includes some specific requirements related to the legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates.<sup>34</sup>

## Considerations specific to public sector entities

A72. For the audits of public sector entities, there may be particular laws or regulations that affect the entity's operations. Such elements may be an essential consideration when obtaining an understanding of the entity and its environment.

## Other external factors

A73. Other external factors affecting the entity that the auditor may consider include the general economic conditions, interest rates and availability of financing, and inflation or currency revaluation.

## Measures Used by Management to Assess the Entity's Financial Performance (Ref: Para. 19(a)(iii))

### Why the auditor understands measures used by management

A74. An understanding of the entity's measures assists the auditor in considering whether such measures, whether used externally or internally, create pressures on the entity to achieve performance targets. These pressures may motivate management to take actions that increase the susceptibility to misstatement due to management bias or fraud (e.g., to

<sup>34</sup> ISA- (NZ) 250 (Revised), paragraph 13

improve the business performance or to intentionally misstate the financial statements) (see ISA (NZ) 240 for requirements and guidance in relation to the risks of fraud).

- A75. Measures may also indicate to the auditor the likelihood of risks of material misstatement of related financial statement information. For example, performance measures may indicate that the entity has unusually rapid growth or profitability when compared to that of other entities in the same industry.

#### Measures used by management

- A76. Management and others ordinarily measure and review those matters they regard as important. ~~Inquiries~~Enquiries of management may reveal that it relies on certain key indicators, whether publicly available or not, for evaluating financial performance and taking action. In such cases, the auditor may identify relevant performance measures, whether internal or external, by considering the information that the entity uses to manage its business. If such ~~inquiry~~enquiry indicates an absence of performance measurement or review, there may be an increased risk of misstatements not being detected and corrected.

- A77. Key indicators used for evaluating financial performance may include:

- Key performance indicators (financial and non-financial) and key ratios, trends and operating statistics.
- Period-on-period financial performance analyses.
- Budgets, forecasts, variance analyses, segment information and divisional, departmental or other level performance reports.
- Employee performance measures and incentive compensation policies.
- Comparisons of an entity's performance with that of competitors.

#### Scalability (Ref: Para. 19(a)(iii))

- A78. The procedures undertaken to understand the entity's measures may vary depending on the size or complexity of the entity, as well as the involvement of owners or those charged with governance in the management of the entity.

#### Examples:

- For some less complex entities, the terms of the entity's bank borrowings (i.e., bank covenants) may be linked to specific performance measures related to the entity's performance or financial position (e.g., a maximum working capital amount). The auditor's understanding of the performance measures used by the bank may help identify areas where there is increased susceptibility to the risk of material misstatement.
- For some entities whose nature and circumstances are more complex, such as those operating in the insurance or banking industries, performance or financial position may be

measured against regulatory requirements (e.g., regulatory ratio requirements such as capital adequacy and liquidity ratios performance hurdles). The auditor's understanding of these performance measures may help identify areas where there is increased susceptibility to the risk of material misstatement.

#### Other considerations

A79. External parties may also review and ~~analyze~~analyse the entity's financial performance, in particular for entities where financial information is publicly available. The auditor may also consider publicly available information to help the auditor further understand the business or identify contradictory information such as information from:

- Analysts or credit agencies.
- News and other media, including social media.
- Taxation authorities.
- Regulators.
- Trade unions.
- Providers of finance.

Such financial information can often be obtained from the entity being audited.

A80. The measurement and review of financial performance is not the same as the monitoring of the system of internal control (discussed as a component of the system of internal control in paragraphs A114–A122), though their purposes may overlap:

- The measurement and review of performance is directed at whether business performance is meeting the objectives set by management (or third parties).
- In contrast, monitoring of the system of internal control is concerned with monitoring the effectiveness of controls including those related to management's measurement and review of financial performance.

In some cases, however, performance indicators also provide information that enables management to identify control deficiencies.

#### Considerations specific to public sector entities

A81. In addition to considering relevant measures used by a public sector entity to assess the entity's financial performance, auditors of public sector entities may also consider non-financial information such as achievement of public benefit outcomes (for example, the number of people assisted by a specific ~~program~~programme).

*The Applicable Financial Reporting Framework* (Ref: Para. 19(b))

Understanding the Applicable Financial Reporting Framework and the Entity's Accounting Policies

A82. Matters that the auditor may consider when obtaining an understanding of the entity's applicable financial reporting framework, and how it applies in the context of the nature and circumstances of the entity and its environment include:

- The entity's financial reporting practices in terms of the applicable financial reporting framework, such as:
  - Accounting principles and industry-specific practices, including for industry-specific significant classes of transactions, account balances and related disclosures in the financial statements (for example, loans and investments for banks, or research and development for pharmaceuticals).
  - Revenue recognition.
  - Accounting for financial instruments, including related credit losses.
  - Foreign currency assets, liabilities and transactions.
  - Accounting for unusual or complex transactions including those in controversial or emerging areas (for example, accounting for cryptocurrency).
- An understanding of the entity's selection and application of accounting policies, including any changes thereto as well as the reasons therefore, may encompass such matters as:
  - The methods the entity uses to ~~recognize~~recognise, measure, present and disclose significant and unusual transactions.
  - The effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.
  - Changes in the environment, such as changes in the applicable financial reporting framework or tax reforms that may necessitate a change in the entity's accounting policies.
  - Financial reporting standards and laws and regulations that are new to the entity and when and how the entity will adopt, or comply with, such requirements.

A83. Obtaining an understanding of the entity and its environment may assist the auditor in considering where changes in the entity's financial reporting (e.g., from prior periods) may be expected.

**Example:**

If the entity has had a significant business combination during the period, the auditor would likely expect changes in classes of transactions, account balances and disclosures associated with that business combination. Alternatively, if there were no significant changes in the financial reporting framework during the period the auditor's understanding may help confirm that the understanding obtained in the prior period remains applicable.

### Considerations specific to public sector entities

- A84. The applicable financial reporting framework in a public sector entity is determined by the legislative and regulatory frameworks relevant to each jurisdiction or within each geographical area. Matters that may be considered in the entity's application of the applicable financial reporting requirements, and how it applies in the context of the nature and circumstances of the entity and its environment, include whether the entity applies a full accrual basis of accounting or a cash basis of accounting in accordance with as the International Public Sector Accounting Standards, or a hybrid.

### How Inherent Risk Factors Affect Susceptibility of Assertions to Misstatement (Ref: Para. 19(c))

**Appendix 2** provides examples of events and conditions that may give rise to the existence of risks of material misstatement, ~~categorized~~categorised by inherent risk factor.

### Why the auditor understands inherent risk factors when understanding the entity and its environment and the applicable financial reporting framework

- A85. Understanding the entity and its environment, and the applicable financial reporting framework, assists the auditor in identifying events or conditions, the characteristics of which may affect the susceptibility of assertions about classes of transactions, account balances or disclosures to misstatement. These characteristics are inherent risk factors. Inherent risk factors may affect susceptibility of assertions to misstatement by influencing the likelihood of occurrence of a misstatement or the magnitude of the misstatement if it were to occur. Understanding how inherent risk factors affect the susceptibility of assertions to misstatement may assist the auditor with a preliminary understanding of the likelihood or magnitude of misstatements, which assists the auditor in identifying risks of material misstatement at the assertion level in accordance with paragraph 28(b). Understanding the degree to which inherent risk factors affect susceptibility of assertions to misstatement also assists the auditor in assessing the likelihood and magnitude of a possible misstatement when assessing inherent risk in accordance with paragraph 31(a). Accordingly, understanding the inherent risk factors may also assist the auditor in designing and performing further audit procedures in accordance with ISA- (NZ) 330.

- A86. The auditor's identification of risks of material misstatement at the assertion level and assessment of inherent risk may also be influenced by audit evidence obtained by the auditor in performing other risk assessment procedures, further audit procedures or in fulfilling other requirements in the ISAs (NZ) (see paragraphs A95, A103, A111, A121, A124 and A151).

The effect of inherent risk factors on a class of transactions, account balance or disclosure

- A87. The extent of susceptibility to misstatement of a class of transactions, account balance or disclosure arising from complexity or subjectivity is often closely related to the extent to which it is subject to change or uncertainty.

**Example:**

If the entity has an accounting estimate that is based on assumptions, the selection of which are subject to significant ~~judgment~~ judgement, the measurement of the accounting estimate is likely to be affected by both subjectivity and uncertainty.

- A88. The greater the extent to which a class of transactions, account balance or disclosure is susceptible to misstatement because of complexity or subjectivity, the greater the need for the auditor to apply professional ~~skepticism~~ scepticism. Further, when a class of transactions, account balance or disclosure is susceptible to misstatement because of complexity, subjectivity, change or uncertainty, these inherent risk factors may create opportunity for management bias, whether unintentional or intentional, and affect susceptibility to misstatement due to management bias. The auditor's identification of risks of material misstatement, and assessment of inherent risk at the assertion level, are also affected by the interrelationships among inherent risk factors.
- A89. Events or conditions that may affect susceptibility to misstatement due to management bias may also affect susceptibility to misstatement due to other fraud risk factors. Accordingly, this may be relevant information for use in accordance with paragraph 24 of ISA- (NZ) 240, which requires the auditor to evaluate whether the information obtained from the other risk assessment procedures and related activities indicates that one or more fraud risk factors are present.

*Obtaining an Understanding of the Entity's System of Internal Control* (Ref: Para. 21–27)

**Appendix 3** further describes the nature of the entity's system of internal control and inherent limitations of internal control, respectively. Appendix 3 also provides further explanation of the components of a system of internal control for the purposes of the ISAs- (NZ).

- A90. The auditor's understanding of the entity's system of internal control is obtained through risk assessment procedures performed to understand and evaluate each of the components of the system of internal control as set out in paragraphs 21 to 27.



A91. The components of the entity's system of internal control for the purpose of this ISA- (NZ) may not necessarily reflect how an entity designs, implements and maintains its system of internal control, or how it may classify any particular component. Entities may use different terminology or frameworks to describe the various aspects of the system of internal control. For the purpose of an audit, auditors may also use different terminology or frameworks provided all the components described in this ISA- (NZ) are addressed.

#### Scalability

A92. The way in which the entity's system of internal control is designed, implemented and maintained varies with an entity's size and complexity. For example, less complex entities may use less structured or simpler controls (i.e., policies and procedures) to achieve their objectives.

#### Considerations Specific to Public Sector Entities

A93. Auditors of public sector entities often have additional responsibilities with respect to internal control, for example, to report on compliance with an established code of practice or reporting on spending against budget. Auditors of public sector entities may also have responsibilities to report on compliance with law, regulation or other authority. As a result, their considerations about the system of internal control may be broader and more detailed.

#### Information Technology in the Components of the Entity's System of Internal Control

**Appendix 5** provides further guidance on understanding the entity's use of IT in the components of the system of internal control.

A94. The overall objective and scope of an audit does not differ whether an entity operates in a mainly manual environment, a completely automated environment, or an environment involving some combination of manual and automated elements (i.e., manual and automated controls and other resources used in the entity's system of internal control).

#### Understanding the Nature of the Components of the Entity's System of Internal Control

A95. In evaluating the effectiveness of the design of controls and whether they have been implemented (see paragraphs A175 to A181) the auditor's understanding of each of the components of the entity's system of internal control provides a preliminary understanding of how the entity identifies business risks and how it responds to them. It may also influence the auditor's identification and assessment of the risks of material misstatement in different ways (see paragraph A86). This assists the auditor in designing and performing further audit procedures, including any plans to test the operating effectiveness of controls. For example:

- The auditor's understanding of the entity's control environment, the entity's risk assessment process, and the entity's process to monitor controls components are



more likely to affect the identification and assessment of risks of material misstatement at the financial statement level.

- The auditor's understanding of the entity's information system and communication, and the entity's control activities component, are more likely to affect the identification and assessment of risks of material misstatement at the assertion level.

Control Environment, The Entity's Risk Assessment Process and the Entity's Process to Monitor the System of Internal Control (Ref: Para. 21–24)

A96. The controls in the control environment, the entity's risk assessment process and the entity's process to monitor the system of internal control are primarily indirect controls (i.e., controls that are not sufficiently precise to prevent, detect or correct misstatements at the assertion level but which support other controls and may therefore have an indirect effect on the likelihood that a misstatement will be detected or prevented on a timely basis). However, some controls within these components may also be direct controls.

Why the auditor is required to understand the control environment, the entity's risk assessment process and the entity's process to monitor the system of internal control

A97. The control environment provides an overall foundation for the operation of the other components of the system of internal control. The control environment does not directly prevent, or detect and correct, misstatements. It may, however, influence the effectiveness of controls in the other components of the system of internal control. Similarly, the entity's risk assessment process and its process for monitoring the system of internal control are designed to operate in a manner that also supports the entire system of internal control.

A98. Because these components are foundational to the entity's system of internal control, any deficiencies in their operation could have pervasive effects on the preparation of the financial statements. Therefore, the auditor's understanding and evaluations of these components affect the auditor's identification and assessment of risks of material misstatement at the financial statement level, and may also affect the identification and assessment of risks of material misstatement at the assertion level. Risks of material misstatement at the financial statement level affect the auditor's design of overall responses, including, as explained in ISA- (NZ) 330, an influence on the nature, timing and extent of the auditor's further procedures.<sup>35</sup>

Obtaining an understanding of the control environment (Ref: Para. 21)

Scalability

A99. The nature of the control environment in a less complex entity is likely to be different from the control environment in a more complex entity. For example, those charged with governance in less complex entities may not include an independent or outside member,

<sup>35</sup> ISA- (NZ) 330, paragraphs A1–A3

and the role of governance may be undertaken directly by the owner-manager where there are no other owners. Accordingly, some considerations about the entity's control environment may be less relevant or may not be applicable.

A100. In addition, audit evidence about elements of the control environment in less complex entities may not be available in documentary form, in particular where communication between management and other personnel is informal, but the evidence may still be appropriately relevant and reliable in the circumstances.

**Examples:**

- The ~~organizational~~organisational structure in a less complex entity will likely be simpler and may include a small number of employees involved in roles related to financial reporting.
- If the role of governance is undertaken directly by the owner-manager, the auditor may determine that the independence of those charged with governance is not relevant.
- Less complex entities may not have a written code of conduct but, instead, develop a culture that emphasizes the importance of integrity and ethical behaviour through oral communication and by management example. Consequently, the attitudes, awareness and actions of management or the owner-manager are of particular importance to the auditor's understanding of a less complex entity's control environment.

Understanding the control environment (Ref: Para. 21(a))

A101. Audit evidence for the auditor's understanding of the control environment may be obtained through a combination of ~~inquiries~~enquiries and other risk assessment procedures (i.e., corroborating ~~inquiries~~enquiries through observation or inspection of documents).

A102. In considering the extent to which management demonstrates a commitment to integrity and ethical values, the auditor may obtain an understanding through ~~inquiries~~enquiries of management and employees, and through considering information from external sources, about:

- How management communicates to employees its views on business practices and ethical ~~behavior~~behaviour; and
- Inspecting management's written code of conduct and observing whether management acts in a manner that supports that code.

Evaluating the control environment (Ref: Para. 21(b))

Why the auditor evaluates the control environment

A103. The auditor's evaluation of how the entity demonstrates ~~behavior~~behaviour consistent with the entity's commitment to integrity and ethical values; whether the control environment provides an appropriate foundation for the other components of the entity's system of

internal control; and whether any identified control deficiencies undermine the other components of the system of internal control, assists the auditor in identifying potential issues in the other components of the system of internal control. This is because the control environment is foundational to the other components of the entity's system of internal control. This evaluation may also assist the auditor in understanding risks faced by the entity and therefore in identifying and assessing the risks of material misstatement at the financial statement and assertion levels (see paragraph A86).

#### The auditor's evaluation of the control environment

A104. The auditor's evaluation of the control environment is based on the understanding obtained in accordance with paragraph 21(a).

A105. Some entities may be dominated by a single individual who may exercise a great deal of discretion. The actions and attitudes of that individual may have a pervasive effect on the culture of the entity, which in turn may have a pervasive effect on the control environment. Such an effect may be positive or negative.

##### **Example:**

Direct involvement by a single individual may be key to enabling the entity to meet its growth and other objectives, and can also contribute significantly to an effective system of internal control. On the other hand, such concentration of knowledge and authority can also lead to an increased susceptibility to misstatement through management override of controls.

A106. The auditor may consider how the different elements of the control environment may be influenced by the philosophy and operating style of senior management taking into account the involvement of independent members of those charged with governance.

A107. Although the control environment may provide an appropriate foundation for the system of internal control and may help reduce the risk of fraud, an appropriate control environment is not necessarily an effective deterrent to fraud.

##### **Example:**

Human resource policies and procedures directed toward hiring competent financial, accounting, and IT personnel may mitigate the risk of errors in processing and recording financial information. However, such policies and procedures may not mitigate the override of controls by senior management (e.g., to overstate earnings).

A108. The auditor's evaluation of the control environment as it relates to the entity's use of IT may include such matters as:

- Whether governance over IT is commensurate with the nature and complexity of the entity and its business operations enabled by IT, including the complexity or maturity of the entity's technology platform or architecture and the extent to which the entity relies on IT applications to support its financial reporting.

- The management ~~organizational~~organisational structure regarding IT and the resources allocated (for example, whether the entity has invested in an appropriate IT environment and necessary enhancements, or whether a sufficient number of appropriately skilled individuals have been employed including when the entity uses commercial software (with no or limited modifications)).

Obtaining an understanding of the entity's risk assessment process (Ref: Para. 22–23)

Understanding the entity's risk assessment process (Ref: Para. 22(a))

A109. As explained in paragraph A62, not all business risks give rise to risks of material misstatement. In understanding how management and those charged with governance have identified business risks relevant to the preparation of the financial statements, and decided about actions to address those risks, matters the auditor may consider include how management or, as appropriate, those charged with governance, has:

- Specified the entity's objectives with sufficient precision and clarity to enable the identification and assessment of the risks relating to the objectives;
- Identified the risks to achieving the entity's objectives and ~~analyzed~~analysed the risks as a basis for determining how the risks should be managed; and
- Considered the potential for fraud when considering the risks to achieving the entity's objectives.<sup>36</sup>

A110. The auditor may consider the implications of such business risks for the preparation of the entity's financial statements and other aspects of its system of internal control.

Evaluating the entity's risk assessment process (Ref: Para. 22(b))

Why the auditor evaluates whether the entity's risk assessment process is appropriate

A111. The auditor's evaluation of the entity's risk assessment process may assist the auditor in understanding where the entity has identified risks that may occur, and how the entity has responded to those risks. The auditor's evaluation of how the entity identifies its business risks, and how it assesses and addresses those risks assists the auditor in understanding whether the risks faced by the entity have been identified, assessed and addressed as appropriate to the nature and complexity of the entity. This evaluation may also assist the auditor with identifying and assessing financial statement level and assertion level risks of material misstatement (see paragraph A86).

Evaluating whether the entity's risk assessment process is appropriate (Ref: Para. 22(b))

A112. The auditor's evaluation of the appropriateness of the entity's risk assessment process is based on the understanding obtained in accordance with paragraph 22(a).

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<sup>36</sup> ISA (NZ) 240, paragraph 19

## Scalability

A113. Whether the entity's risk assessment process is appropriate to the entity's circumstances considering the nature and complexity of the entity is a matter of the auditor's professional ~~judgment~~judgement.

**Example:**

In some less complex entities, and particularly owner-managed entities, an appropriate risk assessment may be performed through the direct involvement of management or the owner-manager (e.g., the manager or owner-manager may routinely devote time to monitoring the activities of competitors and other developments in the market place to identify emerging business risks). The evidence of this risk assessment occurring in these types of entities is often not formally documented, but it may be evident from the discussions the auditor has with management that management are in fact performing risk assessment procedures.

Obtaining an understanding of the entity's process to monitor the entity's system of internal control (Ref: Para. 24)

## Scalability

A114. In less complex entities, and in particular owner-manager entities, the auditor's understanding of the entity's process to monitor the system of internal control is often focused on how management or the owner-manager is directly involved in operations, as there may not be any other monitoring activities.

**Example:**

Management may receive complaints from customers about inaccuracies in their monthly statement that alerts the owner-manager to issues with the timing of when customer payments are being ~~recognized~~recognised in the accounting records.

A115. For entities where there is no formal process for monitoring the system of internal control, understanding the process to monitor the system of internal control may include understanding periodic reviews of management accounting information that are designed to contribute to how the entity prevents or detects misstatements.

Understanding the entity's process to monitor the system of internal control (Ref: Para. 24(a))

A116. Matters that may be relevant for the auditor to consider when understanding how the entity monitors its system of internal control include:

- The design of the monitoring activities, for example whether it is periodic or ongoing monitoring;
- The performance and frequency of the monitoring activities;

- The evaluation of the results of the monitoring activities, on a timely basis, to determine whether the controls have been effective; and
- How identified deficiencies have been addressed through appropriate remedial actions, including timely communication of such deficiencies to those responsible for taking remedial action.

A117. The auditor may also consider how the entity's process to monitor the system of internal control addresses monitoring information processing controls that involve the use of IT. This may include, for example:

- Controls to monitor complex IT environments that:
  - Evaluate the continuing design effectiveness of information processing controls and modify them, as appropriate, for changes in conditions; or
  - Evaluate the operating effectiveness of information processing controls.
- Controls that monitor the permissions applied in automated information processing controls that enforce the segregation of duties.
- Controls that monitor how errors or control deficiencies related to the automation of financial reporting are identified and addressed.

Understanding the entity's internal audit function (Ref: Para. 24(a)(ii))

**Appendix 4** sets out further considerations for understanding the entity's internal audit function.

A118. The auditor's [inquiriesenquiries](#) of appropriate individuals within the internal audit function help the auditor obtain an understanding of the nature of the internal audit function's responsibilities. If the auditor determines that the function's responsibilities are related to the entity's financial reporting, the auditor may obtain further understanding of the activities performed, or to be performed, by the internal audit function by reviewing the internal audit function's audit plan for the period, if any, and discussing that plan with the appropriate individuals within the function. This understanding, together with the information obtained from the auditor's [inquiriesenquiries](#), may also provide information that is directly relevant to the auditor's identification and assessment of the risks of material misstatement. If, based on the auditor's preliminary understanding of the internal audit function, the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed, ISA- (NZ) 610 (Revised 2013)<sup>37</sup> applies.

Other sources of information used in the entity's process to monitor the system of internal control

<sup>37</sup> ISA- (NZ) 610 (Revised 2013), *Using the Work of Internal Auditors*

Understanding the sources of information (Ref: Para. 24(b))

A119. Management's monitoring activities may use information in communications from external parties such as customer complaints or regulator comments that may indicate problems or highlight areas in need of improvement.

Why the auditor is required to understand the sources of information used for the entity's monitoring of the system of internal control

A120. The auditor's understanding of the sources of information used by the entity in monitoring the entity's system of internal control, including whether the information used is relevant and reliable, assists the auditor in evaluating whether the entity's process to monitor the entity's system of internal control is appropriate. If management assumes that information used for monitoring is relevant and reliable without having a basis for that assumption, errors that may exist in the information could potentially lead management to draw incorrect conclusions from its monitoring activities.

Evaluating the entity's process to monitor the system of internal control (Ref: Para 24(c))

Why the auditor evaluates whether the entity's process to monitor the system of internal control is appropriate

A121. The auditor's evaluation about how the entity undertakes ongoing and separate evaluations for monitoring the effectiveness of controls assists the auditor in understanding whether the other components of the entity's system of internal control are present and functioning, and therefore assists with understanding the other components of the entity's system of internal control. This evaluation may also assist the auditor with identifying and assessing financial statement level and assertion level risks of material misstatement (see paragraph A86).

Evaluating whether the entity's process to monitor the system of internal control is appropriate (Ref: Para. 24(c))

A122. The auditor's evaluation of the appropriateness of the entity's process to monitor the system of internal control is based on the auditor's understanding of the entity's process to monitor the system of internal control.

Information System and Communication, and Control Activities (Ref: Para. 25–26)

A123. The controls in the information system and communication, and control activities components are primarily direct controls (i.e., controls that are sufficiently precise to prevent, detect or correct misstatements at the assertion level).

Why the auditor Is required to understand the information system and communication and controls in the control activities component



A124. The auditor is required to understand the entity's information system and communication because understanding the entity's policies that define the flows of transactions and other aspects of the entity's information processing activities relevant to the preparation of the financial statements, and evaluating whether the component appropriately supports the preparation of the entity's financial statements, supports the auditor's identification and assessment of risks of material misstatement at the assertion level. This understanding and evaluation may also result in the identification of risks of material misstatement at the financial statement level when the results of the auditor's procedures are inconsistent with expectations about the entity's system of internal control that may have been set based on information obtained during the engagement acceptance or continuance process (see paragraph A86).

A125. The auditor is required to identify specific controls in the control activities component, and evaluate the design and determine whether the controls have been implemented, as it assists the auditor's understanding about management's approach to addressing certain risks and therefore provides a basis for the design and performance of further audit procedures responsive to these risks as required by ISA- (NZ) 330. The higher on the spectrum of inherent risk a risk is assessed, the more persuasive the audit evidence needs to be. Even when the auditor does not plan to test the operating effectiveness of identified controls, the auditor's understanding may still affect the design of the nature, timing and extent of substantive audit procedures that are responsive to the related risks of material misstatement.

The iterative nature of the auditor's understanding and evaluation of the information system and communication, and control activities

A126. As explained in paragraph A49, the auditor's understanding of the entity and its environment, and the applicable financial reporting framework, may assist the auditor in developing initial expectations about the classes of transactions, account balances and disclosures that may be significant classes of transactions, account balances and disclosures. In obtaining an understanding of the information system and communication component in accordance with paragraph 25(a), the auditor may use these initial expectations for the purpose of determining the extent of understanding of the entity's information processing activities to be obtained.

A127. The auditor's understanding of the information system includes understanding the policies that define flows of information relating to the entity's significant classes of transactions, account balances, and disclosures, and other related aspects of the entity's information processing activities. This information, and the information obtained from the auditor's evaluation of the information system may confirm or further influence the auditor's expectations about the significant classes of transactions, account balances and disclosures initially identified (see paragraph A126).

A128. In obtaining an understanding of how information relating to significant classes of transactions, account balances and disclosures flows into, through, and out of the entity's



information system, the auditor may also identify controls in the control activities component that are required to be identified in accordance with paragraph 26(a). The auditor's identification and evaluation of controls in the control activities component may first focus on controls over journal entries and controls that the auditor plans to test the operating effectiveness of in designing the nature, timing and extent of substantive procedures

A129. The auditor's assessment of inherent risk may also influence the identification of controls in the control activities component. For example, the auditor's identification of controls relating to significant risks may only be identifiable when the auditor has assessed inherent risk at the assertion level in accordance with paragraph 31. Furthermore, controls addressing risks for which the auditor has determined that substantive procedures alone do not provide sufficient appropriate audit evidence (in accordance with paragraph 33) may also only be identifiable once the auditor's inherent risk assessments have been undertaken.

A130. The auditor's identification and assessment of risks of material misstatement at the assertion level is influenced by both the auditor's:

- Understanding of the entity's policies for its information processing activities in the information system and communication component, and
- Identification and evaluation of controls in the control activities component.

~~Obtaining an understanding of the information system and communication (Ref: Para. 25)~~

Obtaining an understanding of the information system and communication (Ref: Para. 25)

**Appendix 3**, Paragraphs 15–19, sets out further considerations relating to the information system and communication.

## Scalability

A131. The information system, and related business processes, in less complex entities are likely to be less sophisticated than in larger entities, and are likely to involve a less complex IT environment; however, the role of the information system is just as important. Less complex entities with direct management involvement may not need extensive descriptions of accounting procedures, sophisticated accounting records, or written policies. Understanding the relevant aspects of the entity's information system may therefore require less effort in an audit of a less complex entity, and may involve a greater amount of inquiry than observation or inspection of documentation. The need to obtain an understanding, however, remains important to provide a basis for the design of further audit procedures in accordance with ISA (NZ) 330 and may further assist the auditor in identifying or assessing risks of material misstatement (see paragraph A86).

Obtaining an understanding of the information system (Ref: Para. 25(a))

A132. Included within the entity's system of internal control are aspects that relate to the entity's reporting objectives, including its financial reporting objectives, but may also include aspects that relate to its operations or compliance objectives, when such aspects are relevant to financial reporting. Understanding how the entity initiates transactions and captures information as part of the auditor's understanding of the information system may include information about the entity's systems (its policies) designed to address compliance and operations objectives because such information is relevant to the preparation of the financial statements. Further, some entities may have information systems that are highly integrated such that controls may be designed in a manner to simultaneously achieve financial reporting, compliance and operational objectives, and combinations thereof.

A133. Understanding the entity's information system also includes an understanding of the resources to be used in the entity's information processing activities. Information about the human resources involved that may be relevant to understanding risks to the integrity of the information system include:

- The competence of the individuals undertaking the work;
- Whether there are adequate resources; and
- Whether there is appropriate segregation of duties.

A134. Matters the auditor may consider when understanding the policies that define the flows of information relating to the entity's significant classes of transactions, account balances, and disclosures in the information system and communication component include the nature of:

- (a) The data or information relating to transactions, other events and conditions to be processed;
- (b) The information processing to maintain the integrity of that data or information; and
- (c) The information processes, personnel and other resources used in the information processing process.

A135. Obtaining an understanding of the entity's business processes, which include how transactions are originated, assists the auditor in obtaining an understanding of the entity's information system in a manner that is appropriate to the entity's circumstances.

A136. The auditor's understanding of the information system may be obtained in various ways and may include:

- ~~Inquiries~~ Enquiries of relevant personnel about the procedures used to initiate, record, process and report transactions or about the entity's financial reporting process;
- Inspection of policy or process manuals or other documentation of the entity's information system;

- Observation of the performance of the policies or procedures by entity's personnel; or
- Selecting transactions and tracing them through the applicable process in the information system (i.e., performing a walk-through).

#### Automated tools and techniques

A137. The auditor may also use automated techniques to obtain direct access to, or a digital download from, the databases in the entity's information system that store accounting records of transactions. By applying automated tools or techniques to this information, the auditor may confirm the understanding obtained about how transactions flow through the information system by tracing journal entries, or other digital records related to a particular transaction, or an entire population of transactions, from initiation in the accounting records through to recording in the general ledger. Analysis of complete or large sets of transactions may also result in the identification of variations from the normal, or expected, processing procedures for these transactions, which may result in the identification of risks of material misstatement.

#### Information obtained from outside of the general and subsidiary ledgers

A138. Financial statements may contain information that is obtained from outside of the general and subsidiary ledgers. Examples of such information that the auditor may consider include:

- Information obtained from lease agreements relevant to disclosures in the financial statements.
- Information disclosed in the financial statements that is produced by an entity's risk management system.
- Fair value information produced by management's experts and disclosed in the financial statements.
- Information disclosed in the financial statements that has been obtained from models, or from other calculations used to develop accounting estimates ~~recognized~~recognised or disclosed in the financial statements, including information relating to the underlying data and assumptions used in those models, such as:
  - Assumptions developed internally that may affect an asset's useful life; or
  - Data such as interest rates that are affected by factors outside the control of the entity.
- Information disclosed in the financial statements about sensitivity analyses derived from financial models that demonstrates that management has considered alternative assumptions.

- Information ~~recognized~~recognised or disclosed in the financial statements that has been obtained from an entity's tax returns and records.
- Information disclosed in the financial statements that has been obtained from analyses prepared to support management's assessment of the entity's ability to continue as a going concern, such as disclosures, if any, related to events or conditions that have been identified that may cast significant doubt on the entity's ability to continue as a going concern.<sup>38</sup>

A139. Certain amounts or disclosures in the entity's financial statements (such as disclosures about credit risk, liquidity risk, and market risk) may be based on information obtained from the entity's risk management system. However, the auditor is not required to understand all aspects of the risk management system, and uses professional ~~judgment~~judgement in determining the necessary understanding.

The entity's use of information technology in the information system

Why does the auditor understand the IT environment relevant to the information system

A140. The auditor's understanding of the information system includes the IT environment relevant to the flows of transactions and processing of information in the entity's information system because the entity's use of IT applications or other aspects in the IT environment may give rise to risks arising from the use of IT.

A141. The understanding of the entity's business model and how it integrates the use of IT may also provide useful context to the nature and extent of IT expected in the information system.

Understanding the entity's use of IT

A142. The auditor's understanding of the IT environment may focus on identifying, and understanding the nature and number of, the specific IT applications and other aspects of the IT environment that are relevant to the flows of transactions and processing of information in the information system. Changes in the flow of transactions, or information within the information system may result from program changes to IT applications, or direct changes to data in databases involved in processing, or storing those transactions or information.

A143. The auditor may identify the IT applications and supporting IT infrastructure concurrently with the auditor's understanding of how information relating to significant classes of transactions, account balances and disclosures flows into, through and out the entity's information system.

Obtaining an understanding of the entity's communication (Ref: Para. 25(b))

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<sup>38</sup> ISA (NZ) 570 (Revised), paragraphs 19–20

## Scalability

A144. In larger, more complex entities, information the auditor may consider when understanding the entity's communication may come from policy manuals and financial reporting manuals.

A145. In less complex entities, communication may be less structured (e.g., formal manuals may not be used) due to fewer levels of responsibility and management's greater visibility and availability. Regardless of the size of the entity, open communication channels facilitate the reporting of exceptions and acting on them.

Evaluating whether the relevant aspects of the information system support the preparation of the entity's financial statements (Ref: Para. 25(c))

A146. The auditor's evaluation of whether the entity's information system and communication appropriately supports the preparation of the financial statements is based on the understanding obtained in paragraphs 25(a)–(b).

## Control Activities (Ref: Para. 26)

### Controls in the control activities component

**Appendix 3**, Paragraphs 20 and 21 set out further considerations relating to control activities.

A147. The control activities component includes controls that are designed to ensure the proper application of policies (which are also controls) in all the other components of the entity's system of internal control, and includes both direct and indirect controls.

#### **Example:**

The controls that an entity has established to ensure that its personnel are properly counting and recording the annual physical inventory relate directly to the risks of material misstatement relevant to the existence and completeness assertions for the inventory account balance.

A148. The auditor's identification and evaluation of controls in the control activities component is focused on information processing controls, which are controls applied during the processing of information in the entity's information system that directly address risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information). However, the auditor is not required to identify and evaluate all information processing controls related to the entity's policies that define the flows of transactions and other aspects of the entity's information processing activities for the significant classes of transactions, account balances and disclosures.

A149. There may also be direct controls that exist in the control environment, the entity's risk assessment process or the entity's process to monitor the system of internal control, which may be identified in accordance with paragraph 26. However, the more indirect the

relationship between controls that support other controls and the control that is being considered, the less effective that control may be in preventing, or detecting and correcting, related misstatements.

**Example:**

A sales manager's review of a summary of sales activity for specific stores by region ordinarily is only indirectly related to the risks of material misstatement relevant to the completeness assertion for sales revenue. Accordingly, it may be less effective in addressing those risks than controls more directly related thereto, such as matching shipping documents with billing documents.

A150. Paragraph 26 also requires the auditor to identify and evaluate general IT controls for IT applications and other aspects of the IT environment that the auditor has determined to be subject to risks arising from the use of IT, because general IT controls support the continued effective functioning of information processing controls. A general IT control alone is typically not sufficient to address a risk of material misstatement at the assertion level.

A151. The controls that the auditor is required to identify and evaluate the design, and determine the implementation of, in accordance with paragraph 26 are those:

- Controls which the auditor plans to test the operating effectiveness of in determining the nature, timing and extent of substantive procedures. The evaluation of such controls provides the basis for the auditor's design of test of control procedures in accordance with ISA- (NZ) 330. These controls also include controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence.
- Controls include controls that address significant risks and controls over journal entries. The auditor's identification and evaluation of such controls may also influence the auditor's understanding of the risks of material misstatement, including the identification of additional risks of material misstatement (see paragraph A95). This understanding also provides the basis for the auditor's design of the nature, timing and extent of substantive audit procedures that are responsive to the related assessed risks of material misstatement.
- Other controls that the auditor considers are appropriate to enable the auditor to meet the objectives of paragraph 13 with respect to risks at the assertion level, based on the auditor's professional ~~judgment~~judgement.

A152. Controls in the control activities component are required to be identified when such controls meet one or more of the criteria included in paragraph 26(a). However, when multiple controls each achieve the same objective, it is unnecessary to identify each of the controls related to such objective.

Types of controls in the control activities component (Ref: Para. 26)

- A153. Examples of controls in the control activities component include ~~authorizations~~authorisations and approvals, reconciliations, verifications (such as edit and validation checks or automated calculations), segregation of duties, and physical or logical controls, including those addressing safeguarding of assets.
- A154. Controls in the control activities component may also include controls established by management that address risks of material misstatement related to disclosures not being prepared in accordance with the applicable financial reporting framework. Such controls may relate to information included in the financial statements that is obtained from outside of the general and subsidiary ledgers.
- A155. Regardless of whether controls are within the IT environment or manual systems, controls may have various objectives and may be applied at various ~~organizational~~organisational and functional levels.

Scalability (Ref: Para. 26)

- A156. Controls in the control activities component for less complex entities are likely to be similar to those in larger entities, but the formality with which they operate may vary. Further, in less complex entities, more controls may be directly applied by management.

**Example:**

Management's sole authority for granting credit to customers and approving significant purchases can provide strong control over important account balances and transactions.

- A157. It may be less practicable to establish segregation of duties in less complex entities that have fewer employees. However, in an owner-managed entity, the owner-manager may be able to exercise more effective oversight through direct involvement than in a larger entity, which may compensate for the generally more limited opportunities for segregation of duties. Although, as also explained in ISA- (NZ) 240, domination of management by a single individual can be a potential control deficiency since there is an opportunity for management override of controls.<sup>39</sup>

Controls that address risks of material misstatement at the assertion level (Ref: Para. 26(a))

Controls that address risks that are determined to be a significant risk (Ref: Para. 26(a)(i))

- A158. Regardless of whether the auditor plans to test the operating effectiveness of controls that address significant risks, the understanding obtained about management's approach to addressing those risks may provide a basis for the design and performance of substantive procedures responsive to significant risks as required by ISA- (NZ) 330.<sup>40</sup> Although risks

<sup>39</sup> ISA- (NZ) 240, paragraph A28

<sup>40</sup> ISA- (NZ) 330, ~~paragraph~~paragraphe 21



relating to significant non-routine or ~~judgmental~~judgemental matters are often less likely to be subject to routine controls, management may have other responses intended to deal with such risks. Accordingly, the auditor's understanding of whether the entity has designed and implemented controls for significant risks arising from non-routine or ~~judgmental~~judgemental matters may include whether and how management responds to the risks. Such responses may include:

- Controls, such as a review of assumptions by senior management or experts.
- Documented processes for accounting estimations.
- Approval by those charged with governance.

**Example:**

Where there are one-off events such as the receipt of a notice of a significant lawsuit, consideration of the entity's response may include such matters as whether it has been referred to appropriate experts (such as internal or external legal counsel), whether an assessment has been made of the potential effect, and how it is proposed that the circumstances are to be disclosed in the financial statements.

A159. ISA- (NZ) 240<sup>41</sup> requires the auditor to understand controls related to assessed risks of material misstatement due to fraud (which are treated as significant risks), and further explains that it is important for the auditor to obtain an understanding of the controls that management has designed, implemented and maintained to prevent and detect fraud.

Controls over journal entries (Ref: Para. 26(a)(ii))

A160. Controls that address risks of material misstatement at the assertion level that are expected to be identified for all audits are controls over journal entries, because the manner in which an entity incorporates information from transaction processing into the general ledger ordinarily involves the use of journal entries, whether standard or non-standard, or automated or manual. The extent to which other controls are identified may vary based on the nature of the entity and the auditor's planned approach to further audit procedures.

**Example:**

In an audit of a less complex entity, the entity's information system may not be complex and the auditor may not plan to rely on the operating effectiveness of controls. Further, the auditor may not have identified any significant risks or any other risks of material misstatement for which it is necessary for the auditor to evaluate the design of controls and determine that they have been implemented. In such an audit, the auditor may determine that there are no identified controls other than the entity's controls over journal entries.

<sup>41</sup> ISA- (NZ) 240, ~~paragraphs~~paragraphes 28 and A33



## Automated tools and techniques

A161. In manual general ledger systems, non-standard journal entries may be identified through inspection of ledgers, journals, and supporting documentation. When automated procedures are used to maintain the general ledger and prepare financial statements, such entries may exist only in electronic form and may therefore be more easily identified through the use of automated techniques.

**Example:**

In the audit of a less complex entity, the auditor may be able to extract a total listing of all journal entries into a simple spreadsheet. It may then be possible for the auditor to sort the journal entries by applying a variety of filters such as currency amount, name of the preparer or reviewer, journal entries that gross up the balance sheet and income statement only, or to view the listing by the date the journal entry was posted to the general ledger, to assist the auditor in designing responses to the risks identified relating to journal entries.

Controls for which the auditor plans to test the operating effectiveness (Ref: Para. 26(a)(iii))

A162. The auditor determines whether there are any risks of material misstatement at the assertion level for which it is not possible to obtain sufficient appropriate audit evidence through substantive procedures alone. The auditor is required, in accordance with ISA- (NZ) 330,<sup>42</sup> to design and perform tests of controls that address such risks of material misstatement when substantive procedures alone do not provide sufficient appropriate audit evidence at the assertion level. As a result, when such controls exist that address these risks, they are required to be identified and evaluated.

A163. In other cases, when the auditor plans to take into account the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures in accordance with ISA- (NZ) 330, such controls are also required to be identified because ISA- (NZ) 330<sup>43</sup> requires the auditor to design and perform tests of those controls.

**Examples:**

The auditor may plan to test the operating effectiveness of controls:

- Over routine classes of transactions because such testing may be more effective or efficient for large volumes of homogenous transactions.
- Over the completeness and accuracy of information produced by the entity (e.g., controls over the preparation of system-generated reports), to determine the reliability of that information, when the auditor intends to take into account the operating effectiveness of those controls in designing and performing further audit procedures.

<sup>42</sup> ISA- (NZ) 330, paragraph 8(b)

<sup>43</sup> ISA- (NZ) 330, paragraph 8(a)

- Relating to operations and compliance objectives when they relate to data the auditor evaluates or uses in applying audit procedures.

A164. The auditor's plans to test the operating effectiveness of controls may also be influenced by the identified risks of material misstatement at the financial statement level. For example, if deficiencies are identified related to the control environment, this may affect the auditor's overall expectations about the operating effectiveness of direct controls.

Other controls that the auditor considers appropriate (Ref: Para. 26(a)(iv))

A165. Other controls that the auditor may consider are appropriate to identify, and evaluate the design and determine the implementation, may include:

- Controls that address risks assessed as higher on the spectrum of inherent risk but have not been determined to be a significant risk;
- Controls related to reconciling detailed records to the general ledger; or
- Complementary user entity controls, if using a service ~~organization~~ organisation.<sup>44</sup>

Identifying IT applications and other aspects of the IT environment, risks arising from the use of IT and general IT controls (Ref: Para. 26(b)–(c))

**Appendix 5** includes example characteristics of IT applications and other aspects of the IT environment, and guidance related to those characteristics, that may be relevant in identifying IT applications and other aspects of the IT environment subject to risks arising from the use of IT.

Identifying IT applications and other aspects of the IT environment (Ref: Para. 26(b))

Why the auditor identifies risks arising from the use of IT and general IT controls related to identified IT applications and other aspects of the IT environment

A166. Understanding the risks arising from the use of IT and the general IT controls implemented by the entity to address those risks may affect:

- The auditor's decision about whether to test the operating effectiveness of controls to address risks of material misstatement at the assertion level;

<sup>44</sup> ISA- (NZ) 402, Audit Considerations Relating to an Entity Using a Service ~~Organization~~ Organisation

**Example:**

When general IT controls are not designed effectively or appropriately implemented to address risks arising from the use of IT (e.g., controls do not appropriately prevent or detect ~~unauthorized~~unauthorised program changes or ~~unauthorized~~unauthorised access to IT applications), this may affect the auditor's decision to rely on automated controls within the affected IT applications.

- The auditor's assessment of control risk at the assertion level;

**Example:**

The ongoing operating effectiveness of an information processing control may depend on certain general IT controls that prevent or detect ~~unauthorized~~unauthorised program changes to the IT information processing control (i.e., program change controls over the related IT application). In such circumstances, the expected operating effectiveness (or lack thereof) of the general IT control may affect the auditor's assessment of control risk (e.g., control risk may be higher when such general IT controls are expected to be ineffective or if the auditor does not plan to test the general IT controls).

- The auditor's strategy for testing information produced by the entity that is produced by or involves information from the entity's IT applications;

**Example:**

When information produced by the entity to be used as audit evidence is produced by IT applications, the auditor may determine to test controls over system-generated reports, including identification and testing of the general IT controls that address risks of inappropriate or ~~unauthorized~~unauthorised program changes or direct data changes to the reports.

- The auditor's assessment of inherent risk at the assertion level; or

**Example:**

When there are significant or extensive programming changes to an IT application to address new or revised reporting requirements of the applicable financial reporting framework, this may be an indicator of the complexity of the new requirements and their effect on the entity's financial statements. When such extensive programming or data changes occur, the IT application is also likely to be subject to risks arising from the use of IT.

- The design of further audit procedures.

**Example:**

If information processing controls depend on general IT controls, the auditor may determine to test the operating effectiveness of the general IT controls, which will then require the design of tests of controls for such general IT controls. If, in the same circumstances, the auditor determines not to test the operating effectiveness of the general IT controls, or the general IT controls are expected to be ineffective, the related risks arising from the use of IT may need to be addressed through the design of substantive procedures. However, the risks arising from the use of IT may not be able to be addressed when such risks relate to risks for which substantive procedures alone do not provide sufficient appropriate audit evidence. In such circumstances, the auditor may need to consider the implications for the audit opinion.

### Identifying IT applications that are subject to risks arising from the use of IT

- A167. For the IT applications relevant to the information system, understanding the nature and complexity of the specific IT processes and general IT controls that the entity has in place may assist the auditor in determining which IT applications the entity is relying upon to accurately process and maintain the integrity of information in the entity's information system. Such IT applications may be subject to risks arising from the use of IT.
- A168. Identifying the IT applications that are subject to risks arising from the use of IT involves taking into account controls identified by the auditor because such controls may involve the use of IT or rely on IT. The auditor may focus on whether an IT application includes automated controls that management is relying on and that the auditor has identified, including controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence. The auditor may also consider how information is stored and processed in the information system relating to significant classes of transactions, account balances and disclosures and whether management is relying on general IT controls to maintain the integrity of that information.
- A169. The controls identified by the auditor may depend on system-generated reports, in which case the IT applications that produce those reports may be subject to risks arising from the use of IT. In other cases, the auditor may not plan to rely on controls over the system-generated reports and plan to directly test the inputs and outputs of such reports, in which case the auditor may not identify the related IT applications as being subject to risks arising from IT.

### Scalability

- A170. The extent of the auditor's understanding of the IT processes, including the extent to which the entity has general IT controls in place, will vary with the nature and the circumstances of the entity and its IT environment, as well as based on the nature and extent of controls

identified by the auditor. The number of IT applications that are subject to risks arising from the use of IT also will vary based on these factors.

**Examples:**

- An entity that uses commercial software and does not have access to the source code to make any program changes is unlikely to have a process for program changes, but may have a process or procedures to configure the software (e.g., the chart of accounts, reporting parameters or thresholds). In addition, the entity may have a process or procedures to manage access to the application (e.g., a designated individual with administrative access to the commercial software). In such circumstances, the entity is unlikely to have or need ~~formalized~~ formalised general IT controls.
- In contrast, a larger entity may rely on IT to a great extent and the IT environment may involve multiple IT applications and the IT processes to manage the IT environment may be complex (e.g., a dedicated IT department exists that develops and implements program changes and manages access rights), including that the entity has implemented ~~formalized~~ formalised general IT controls over its IT processes.
- When management is not relying on automated controls or general IT controls to process transactions or maintain the data, and the auditor has not identified any automated controls or other information processing controls (or any that depend on general IT controls), the auditor may plan to directly test any information produced by the entity involving IT and may not identify any IT applications that are subject to risks arising from the use of IT.
- When management relies on an IT application to process or maintain data and the volume of data is significant, and management relies upon the IT application to perform automated controls that the auditor has also identified, the IT application is likely to be subject to risks arising from the use of IT.

A171. When an entity has greater complexity in its IT environment, identifying the IT applications and other aspects of the IT environment, determining the related risks arising from the use of IT, and identifying general IT controls is likely to require the involvement of team members with ~~specialized~~ specialised skills in IT. Such involvement is likely to be essential, and may need to be extensive, for complex IT environments.

Identifying other aspects of the IT environment that are subject to risks arising from the use of IT

A172. The other aspects of the IT environment that may be subject to risks arising from the use of IT include the network, operating system and databases, and, in certain circumstances, interfaces between IT applications. Other aspects of the IT environment are generally not identified when the auditor does not identify IT applications that are subject to risks arising from the use of IT. When the auditor has identified IT applications that are subject to risks arising from IT, other aspects of the IT environment (e.g., database, operating system,

network) are likely to be identified because such aspects support and interact with the identified IT applications.

Identifying risks arising from the use of IT and general IT controls (Ref: Para. 26(c))

**Appendix 6** sets out considerations for understanding general IT controls.

A173. In identifying the risks arising from the use of IT, the auditor may consider the nature of the identified IT application or other aspect of the IT environment and the reasons for it being subject to risks arising from the use of IT. For some identified IT applications or other aspects of the IT environment, the auditor may identify applicable risks arising from the use of IT that relate primarily to ~~unauthorized~~unauthorised access or ~~unauthorized~~unauthorised program changes, as well as that address risks related to inappropriate data changes (e.g., the risk of inappropriate changes to the data through direct database access or the ability to directly manipulate information).

A174. The extent and nature of the applicable risks arising from the use of IT vary depending on the nature and characteristics of the identified IT applications and other aspects of the IT environment. Applicable IT risks may result when the entity uses external or internal service providers for identified aspects of its IT environment (e.g., outsourcing the hosting of its IT environment to a third party or using a shared service center for central management of IT processes in a group). Applicable risks arising from the use of IT may also be identified related to cybersecurity. It is more likely that there will be more risks arising from the use of IT when the volume or complexity of automated application controls is higher and management is placing greater reliance on those controls for effective processing of transactions or the effective maintenance of the integrity of underlying information.

Evaluating the design, and determining implementation, of identified controls in the control activities component (Ref: Para 26(d))

A175. Evaluating the design of an identified control involves the auditor's consideration of whether the control, individually or in combination with other controls, is capable of effectively preventing, or detecting and correcting, material misstatements (i.e., the control objective).

A176. The auditor determines the implementation of an identified control by establishing that the control exists and that the entity is using it. There is little point in the auditor assessing the implementation of a control that is not designed effectively. Therefore, the auditor evaluates the design of a control first. An improperly designed control may represent a control deficiency.

A177. Risk assessment procedures to obtain audit evidence about the design and implementation of identified controls in the control activities component may include:

- ~~Inquiring~~Enquiring of entity personnel.

- Observing the application of specific controls.
- Inspecting documents and reports.

~~Inquiry~~Enquiry alone, however, is not sufficient for such purposes.

A178. The auditor may expect, based on experience from the previous audit or based on current period risk assessment procedures, that management does not have effectively designed or implemented controls to address a significant risk. In such instances, the procedures performed to address the requirement in paragraph 26(d) may consist of determining that such controls have not been effectively designed or implemented. If the results of the procedures indicate that controls have been newly designed or implemented, the auditor is required to perform the procedures in paragraph 26(b)–(d) on the newly designed or implemented controls.

A179. The auditor may conclude that a control, which is effectively designed and implemented, may be appropriate to test in order to take its operating effectiveness into account in designing substantive procedures. However, when a control is not designed or implemented effectively, there is no benefit in testing it. When the auditor plans to test a control, the information obtained about the extent to which the control addresses the risk(s) of material misstatement is an input to the auditor’s control risk assessment at the assertion level.

A180. Evaluating the design and determining the implementation of identified controls in the control activities component is not sufficient to test their operating effectiveness. However, for automated controls, the auditor may plan to test the operating effectiveness of automated controls by identifying and testing general IT controls that provide for the consistent operation of an automated control instead of performing tests of operating effectiveness on the automated controls directly. Obtaining audit evidence about the implementation of a manual control at a point in time does not provide audit evidence about the operating effectiveness of the control at other times during the period under audit. Tests of the operating effectiveness of controls, including tests of indirect controls, are further described in ISA- (NZ) 330.<sup>45</sup>

A181. When the auditor does not plan to test the operating effectiveness of identified controls, the auditor’s understanding may still assist in the design of the nature, timing and extent of substantive audit procedures that are responsive to the related risks of material misstatement.

**Example:**

The results of these risk assessment procedures may provide a basis for the auditor’s consideration of possible deviations in a population when designing audit samples.

<sup>45</sup> ISA- (NZ) 330, paragraphs 8–11



*Control Deficiencies Within the Entity's System of Internal Control* (Ref: Para. 27)

A182. In performing the evaluations of each of the components of the entity's system of internal control,<sup>46</sup> the auditor may determine that certain of the entity's policies in a component are not appropriate to the nature and circumstances of the entity. Such a determination may be an indicator that assists the auditor in identifying control deficiencies. If the auditor has identified one or more control deficiencies, the auditor may consider the effect of those control deficiencies on the design of further audit procedures in accordance with ISA- (NZ) 330.

A183. If the auditor has identified one or more control deficiencies, ISA- (NZ) 265<sup>47</sup> requires the auditor to determine whether, individually or in combination, the deficiencies constitute a significant deficiency. The auditor uses professional ~~judgment~~judgement in determining whether a deficiency represents a significant control deficiency.<sup>48</sup>

**Examples:**

Circumstances that may indicate a significant control deficiency exists include matters such as:

- The identification of fraud of any magnitude that involves senior management;
- Identified internal processes that are inadequate relating to the reporting and communication of deficiencies noted by internal audit;
- Previously communicated deficiencies that are not corrected by management in a timely manner;
- Failure by management to respond to significant risks, for example, by not implementing controls over significant risks; and
- The restatement of previously issued financial statements.

**Identifying and Assessing the Risks of Material Misstatement** (Ref: Para. 28–37)

*Why the Auditor Identifies and Assesses the Risks of Material Misstatement*

A184. Risks of material misstatement are identified and assessed by the auditor in order to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence. This evidence enables the auditor to express an opinion on the financial statements at an acceptably low level of audit risk.

<sup>46</sup> Paragraphs 21(b), 22(b), 24(c), 25(c) and 26(d)

<sup>47</sup> ISA- (NZ) 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*, paragraph 8

<sup>48</sup> ISA- (NZ) 265, paragraphs A6–A7 set out indicators of significant deficiencies, and matters to be considered in determining whether a deficiency, or a combination of deficiencies, in internal control constitute a significant deficiency.



A185. Information gathered by performing risk assessment procedures is used as audit evidence to provide the basis for the identification and assessment of the risks of material misstatement. For example, the audit evidence obtained when evaluating the design of identified controls and determining whether those controls have been implemented in the control activities component, is used as audit evidence to support the risk assessment. Such evidence also provides a basis for the auditor to design overall responses to address the assessed risks of material misstatement at the financial statement level, as well as designing and performing further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement at the assertion level, in accordance with ISA- (NZ) 330.

#### *Identifying Risks of Material Misstatement (Ref: Para. 28)*

A186. The identification of risks of material misstatement is performed before consideration of any related controls (i.e., the inherent risk), and is based on the auditor's preliminary consideration of misstatements that have a reasonable possibility of both occurring, and being material if they were to occur.<sup>49</sup>

A187. Identifying the risks of material misstatement also provides the basis for the auditor's determination of relevant assertions, which assists the auditor's determination of the significant classes of transactions, account balances and disclosures.

#### *Assertions*

##### *Why the Auditor Uses Assertions*

A188. In identifying and assessing the risks of material misstatement, the auditor uses assertions to consider the different types of potential misstatements that may occur. Assertions for which the auditor has identified related risks of material misstatement are relevant assertions.

##### *The Use of Assertions*

A189. In identifying and assessing the risks of material misstatement, the auditor may use the categories of assertions as described in paragraph A190(a)–(b) below or may express them differently provided all aspects described below have been covered. The auditor may choose to combine the assertions about classes of transactions and events, and related disclosures, with the assertions about account balances, and related disclosures.

A190. Assertions used by the auditor in considering the different types of potential misstatements that may occur may fall into the following categories:

- (a) Assertions about classes of transactions and events, and related disclosures, for the period under audit:

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<sup>49</sup> ISA- (NZ) 200, paragraph A15a

- (i) Occurrence—transactions and events that have been recorded or disclosed have occurred, and such transactions and events pertain to the entity.
  - (ii) Completeness—all transactions and events that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
  - (iii) Accuracy—amounts and other data relating to recorded transactions and events have been recorded appropriately, and related disclosures have been appropriately measured and described.
  - (iv) Cutoff—transactions and events have been recorded in the correct accounting period.
  - (v) Classification—transactions and events have been recorded in the proper accounts.
  - (vi) Presentation—transactions and events are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.
- (b) Assertions about account balances, and related disclosures, at the period end:
- (i) Existence—assets, liabilities and equity interests exist.
  - (ii) Rights and obligations—the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
  - (iii) Completeness—all assets, liabilities and equity interests that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
  - (iv) Accuracy, valuation and allocation—assets, liabilities and equity interests have been included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments have been appropriately recorded, and related disclosures have been appropriately measured and described.
  - (v) Classification—assets, liabilities and equity interests have been recorded in the proper accounts.
  - (vi) Presentation—assets, liabilities and equity interests are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.

A191. The assertions described in paragraph A190(a)–(b) above, adapted as appropriate, may also be used by the auditor in considering the different types of misstatements that may occur in disclosures not directly related to recorded classes of transactions, events or account balances.

**Example:**

An example of such a disclosure includes where the entity may be required by the applicable financial reporting framework to describe its exposure to risks arising from financial instruments, including how the risks arise; the objectives, policies and processes for managing the risks; and the methods used to measure the risks.

### Considerations Specific to Public Sector Entities

A192. When making assertions about the financial statements of public sector entities, in addition to those assertions set out in paragraph A190(a)–(b), management may often assert that transactions and events have been carried out in accordance with law, regulation or other authority. Such assertions may fall within the scope of the financial statement audit.

### *Risks of Material Misstatement at the Financial Statement Level* (Ref: Para. 28(a) and 30)

#### Why the Auditor Identifies and Assesses Risks of Material Misstatement at the Financial Statement Level

A193. The auditor identifies risks of material misstatement at the financial statement level to determine whether the risks have a pervasive effect on the financial statements, and would therefore require an overall response in accordance with ISA- (NZ) 330.<sup>50</sup>

A194. In addition, risks of material misstatement at the financial statement level may also affect individual assertions, and identifying these risks may assist the auditor in assessing risks of material misstatement at the assertion level, and in designing further audit procedures to address the identified risks.

#### Identifying and Assessing Risks of Material Misstatement at the Financial Statement Level

A195. Risks of material misstatement at the financial statement level refer to risks that relate pervasively to the financial statements as a whole, and potentially affect many assertions. Risks of this nature are not necessarily risks identifiable with specific assertions at the class of transactions, account balance or disclosure level (e.g., risk of management override of controls). Rather, they represent circumstances that may pervasively increase the risks of material misstatement at the assertion level. The auditor's evaluation of whether risks identified relate pervasively to the financial statements supports the auditor's assessment of the risks of material misstatement at the financial statement level. In other cases, a number of assertions may also be identified as susceptible to the risk, and may therefore affect the auditor's risk identification and assessment of risks of material misstatement at the assertion level.

<sup>50</sup> ISA- (NZ) 330, paragraph 5

**Example:**

The entity faces operating losses and liquidity issues and is reliant on funding that has not yet been secured. In such a circumstance, the auditor may determine that the going concern basis of accounting gives rise to a risk of material misstatement at the financial statement level. In this situation, the accounting framework may need to be applied using a liquidation basis, which would likely affect all assertions pervasively.

A196. The auditor's identification and assessment of risks of material misstatement at the financial statement level is influenced by the auditor's understanding of the entity's system of internal control, in particular the auditor's understanding of the control environment, the entity's risk assessment process and the entity's process to monitor the system of internal control, and:

- The outcome of the related evaluations required by paragraphs 21(b), 22(b), 24(c) and 25(c); and
- Any control deficiencies identified in accordance with paragraph 27.

In particular, risks at the financial statement level may arise from deficiencies in the control environment or from external events or conditions such as declining economic conditions.

A197. Risks of material misstatement due to fraud may be particularly relevant to the auditor's consideration of the risks of material misstatement at the financial statement level.

**Example:**

The auditor understands from ~~inquiries~~enquiries of management that the entity's financial statements are to be used in discussions with lenders in order to secure further financing to maintain working capital. The auditor may therefore determine that there is a greater susceptibility to misstatement due to fraud risk factors that affect inherent risk (i.e., the susceptibility of the financial statements to material misstatement because of the risk of fraudulent financial reporting, such as overstatement of assets and revenue and under-statement of liabilities and expenses to ensure that financing will be obtained).

A198. The auditor's understanding, including the related evaluations, of the control environment and other components of the system of internal control may raise doubts about the auditor's ability to obtain audit evidence on which to base the audit opinion or be cause for withdrawal from the engagement where withdrawal is possible under applicable law or regulation.

**Examples:**

- As a result of evaluating the entity's control environment, the auditor has concerns about the integrity of the entity's management, which may be so serious as to cause the auditor to conclude that the risk of intentional misrepresentation by management in the financial statements is such that an audit cannot be conducted.
- As a result of evaluating the entity's information system and communication, the auditor determines that significant changes in the IT environment have been poorly managed, with little oversight from management and those charged with governance. The auditor concludes that there are significant concerns about the condition and reliability of the entity's accounting records. In such circumstances, the auditor may determine that it is unlikely that sufficient appropriate audit evidence will be available to support an unmodified opinion on the financial statements.

A199. ISA (NZ) 705 (Revised)<sup>51</sup> establishes requirements and provides guidance in determining whether there is a need for the auditor to express a qualified opinion or disclaim an opinion or, as may be required in some cases, to withdraw from the engagement where withdrawal is possible under applicable law or regulation.

#### Considerations Specific to Public Sector Entities

A200. For public sector entities, the identification of risks at the financial statement level may include consideration of matters related to the political climate, public interest and ~~program~~ programme sensitivity.

#### *Risks of Material Misstatement at the Assertion Level (Ref: Para. 28(b))*

**Appendix 2** sets out examples, in the context of inherent risk factors, of events or conditions that may indicate susceptibility to misstatement that may be material.

A201. Risks of material misstatements that do not relate pervasively to the financial statements are risks of material misstatement at the assertion level.

#### *Relevant Assertions and Significant Classes of Transactions, Account Balances and Disclosures (Ref: Para. 29)*

#### Why Relevant Assertions and Significant Classes of Transactions, Account Balances and Disclosures Are Determined

A202. Determining relevant assertions and the significant classes of transactions, account balances and disclosures provides the basis for the scope of the auditor's understanding of the entity's information system required to be obtained in accordance with paragraph

<sup>51</sup> ISA (NZ) 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

25(a). This understanding may further assist the auditor in identifying and assessing risks of material misstatement (see A86).

#### Automated Tools and Techniques

A203. The auditor may use automated techniques to assist in the identification of significant classes of transactions, account balances and disclosures.

**Examples:**

- An entire population of transactions may be ~~analyzed~~analysed using automated tools and techniques to understand their nature, source, size and volume. By applying automated techniques, the auditor may, for example, identify that an account with a zero balance at period end was comprised of numerous offsetting transactions and journal entries occurring during the period, indicating that the account balance or class of transactions may be significant (e.g., a payroll clearing account). This same payroll clearing account may also identify expense reimbursements to management (and other employees), which could be a significant disclosure due to these payments being made to related parties.
- By ~~analyzing~~analysing the flows of an entire population of revenue transactions, the auditor may more easily identify a significant class of transactions that had not previously been identified.

#### Disclosures that May Be Significant

A204. Significant disclosures include both quantitative and qualitative disclosures for which there is one or more relevant assertions. Examples of disclosures that have qualitative aspects and that may have relevant assertions and may therefore be considered significant by the auditor include disclosures about:

- Liquidity and debt covenants of an entity in financial distress.
- Events or circumstances that have led to the recognition of an impairment loss.
- Key sources of estimation uncertainty, including assumptions about the future.
- The nature of a change in accounting policy, and other relevant disclosures required by the applicable financial reporting framework, where, for example, new financial reporting requirements are expected to have a significant impact on the financial position and financial performance of the entity.
- Share-based payment arrangements, including information about how any amounts ~~recognized~~recognised were determined, and other relevant disclosures.
- Related parties, and related party transactions.

- Sensitivity analysis, including the effects of changes in assumptions used in the entity's valuation techniques intended to enable users to understand the underlying measurement uncertainty of a recorded or disclosed amount.

*Assessing Risks of Material Misstatement at the Assertion Level*

Assessing Inherent Risk (Ref: Para. 31–33)

Assessing the likelihood and magnitude of misstatement (Ref: Para: 31)

Why the auditor assesses likelihood and magnitude of misstatement

- A205. The auditor assesses the likelihood and magnitude of misstatement for identified risks of material misstatement because the significance of the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement were the misstatement to occur determines where on the spectrum of inherent risk the identified risk is assessed, which informs the auditor's design of further audit procedures to address the risk.
- A206. Assessing the inherent risk of identified risks of material misstatement also assists the auditor in determining significant risks. The auditor determines significant risks because specific responses to significant risks are required in accordance with ISA- (NZ) 330 and other ISAs- (NZ).
- A207. Inherent risk factors influence the auditor's assessment of the likelihood and magnitude of misstatement for the identified risks of material misstatement at the assertion level. The greater the degree to which a class of transactions, account balance or disclosure is susceptible to material misstatement, the higher the inherent risk assessment is likely to be. Considering the degree to which inherent risk factors affect the susceptibility of an assertion to misstatement assists the auditor in appropriately assessing inherent risk for risks of material misstatement at the assertion level and in designing a more precise response to such a risk.

Spectrum of inherent risk

- A208. In assessing inherent risk, the auditor uses professional judgment in determining the significance of the combination of the likelihood and magnitude of a misstatement.
- A209. The assessed inherent risk relating to a particular risk of material misstatement at the assertion level represents a judgment within a range, from lower to higher, on the spectrum of inherent risk. The judgment about where in the range inherent risk is assessed may vary based on the nature, size and complexity of the entity, and takes into account the assessed likelihood and magnitude of the misstatement and inherent risk factors.
- A210. In considering the likelihood of a misstatement, the auditor considers the possibility that a misstatement may occur, based on consideration of the inherent risk factors.



- A211. In considering the magnitude of a misstatement, the auditor considers the qualitative and quantitative aspects of the possible misstatement (i.e., misstatements in assertions about classes of transactions, account balances or disclosures may be judged to be material due to size, nature or circumstances).
- A212. The auditor uses the significance of the combination of the likelihood and magnitude of a possible misstatement in determining where on the spectrum of inherent risk (i.e., the range) inherent risk is assessed. The higher the combination of likelihood and magnitude, the higher the assessment of inherent risk; the lower the combination of likelihood and magnitude, the lower the assessment of inherent risk.
- A213. For a risk to be assessed as higher on the spectrum of inherent risk, it does not mean that both the magnitude and likelihood need to be assessed as high. Rather, it is the intersection of the magnitude and likelihood of the material misstatement on the spectrum of inherent risk that will determine whether the assessed inherent risk is higher or lower on the spectrum of inherent risk. A higher inherent risk assessment may also arise from different combinations of likelihood and magnitude, for example a higher inherent risk assessment could result from a lower likelihood but a very high magnitude.
- A214. In order to develop appropriate strategies for responding to risks of material misstatement, the auditor may designate risks of material misstatement within categories along the spectrum of inherent risk, based on their assessment of inherent risk. These categories may be described in different ways. Regardless of the method of ~~categorization~~categorisation used, the auditor's assessment of inherent risk is appropriate when the design and implementation of further audit procedures to address the identified risks of material misstatement at the assertion level is appropriately responsive to the assessment of inherent risk and the reasons for that assessment.

#### Pervasive Risks of Material Misstatement at the Assertion Level (Ref: Para 31(b))

- A215. In assessing the identified risks of material misstatement at the assertion level, the auditor may conclude that some risks of material misstatement relate more pervasively to the financial statements as a whole and potentially affect many assertions, in which case the auditor may update the identification of risks of material misstatement at the financial statement level.
- A216. In circumstances in which risks of material misstatement are identified as financial statement level risks due to their pervasive effect on a number of assertions, and are identifiable with specific assertions, the auditor is required to take into account those risks when assessing inherent risk for risks of material misstatement at the assertion level.

#### Considerations Specific to Public Sector Entities

- A217. In exercising professional ~~judgment~~judgement as to the assessment of the risk of material misstatement, public sector auditors may consider the complexity of the regulations and directives, and the risks of non-compliance with authorities.



Significant Risks (Ref: Para. 32)

Why significant risks are determined and the implications for the audit

A218. The determination of significant risks allows for the auditor to focus more attention on those risks that are on the upper end of the spectrum, through the performance of certain required responses, including:

- Controls that address significant risks are required to be identified in accordance with paragraph 26(a)(i), with a requirement to evaluate whether the control has been designed effectively and implemented in accordance with paragraph 26(d).
- ISA- (NZ) 330 requires controls that address significant risks to be tested in the current period (when the auditor intends to rely on the operating effectiveness of such controls) and substantive procedures to be planned and performed that are specifically responsive to the identified significant risk.<sup>52</sup>
- ISA- (NZ) 330 requires the auditor to obtain more persuasive audit evidence the higher the auditor's assessment of risk.<sup>53</sup>
- ISA- (NZ) 260 (Revised) requires communicating with those charged with governance about the significant risks identified by the auditor.<sup>54</sup>
- ISA- (NZ) 701 requires the auditor to take into account significant risks when determining those matters that required significant auditor attention, which are matters that may be key audit matters.<sup>55</sup>
- Timely review of audit documentation by the engagement partner at the appropriate stages during the audit allows significant matters, including significant risks, to be resolved on a timely basis to the engagement partner's satisfaction on or before the date of the auditor's report.<sup>56</sup>
- ISA- (NZ) 600 requires more involvement by the group engagement partner if the significant risk relates to a component in a group audit and for the group engagement team to direct the work required at the component by the component auditor.<sup>57</sup>

Determining significant risks

A219. In determining significant risks, the auditor may first identify those assessed risks of material misstatement that have been assessed higher on the spectrum of inherent risk to form the basis for considering which risks may be close to the upper end. Being close to

<sup>52</sup> ISA- (NZ) 330, paragraphs 15 and 21

<sup>53</sup> ISA- (NZ) 330, paragraph 7(b)

<sup>54</sup> ISA- (NZ) 260 (Revised), paragraph 15

<sup>55</sup> ISA- (NZ) 701, *Communicating Key Audit Matters in the Independent Auditor's Report*, paragraph 9

<sup>56</sup> ISA- (NZ) 220, paragraphs 17 and A19

<sup>57</sup> ISA- (NZ) 600, paragraphs 30 and 31

the upper end of the spectrum of inherent risk will differ from entity to entity, and will not necessarily be the same for an entity period on period. It may depend on the nature and circumstances of the entity for which the risk is being assessed.

A220. The determination of which of the assessed risks of material misstatement are close to the upper end of the spectrum of inherent risk, and are therefore significant risks, is a matter of professional ~~judgment~~ judgement, unless the risk is of a type specified to be treated as a significant risk in accordance with the requirements of another ISA- (NZ). ISA- (NZ) 240 provides further requirements and guidance in relation to the identification and assessment of the risks of material misstatement due to fraud.<sup>58</sup>

**Example:**

- Cash at a supermarket retailer would ordinarily be determined to be a high likelihood of possible misstatement (due to the risk of cash being misappropriated), however the magnitude would typically be very low (due to the low levels of physical cash handled in the stores). The combination of these two factors on the spectrum of inherent risk would be unlikely to result in the existence of cash being determined to be a significant risk.
- An entity is in negotiations to sell a business segment. The auditor considers the effect on goodwill impairment, and may determine there is a higher likelihood of possible misstatement and a higher magnitude due to the impact of inherent risk factors of subjectivity, uncertainty and susceptibility to management bias or other fraud risk factors. This may result in goodwill impairment being determined to be a significant risk.

A221. The auditor also takes into the account the relative effects of inherent risk factors when assessing inherent risk. The lower the effect of inherent risk factors, the lower the assessed risk is likely to be. Risks of material misstatement that may be assessed as having higher inherent risk and may therefore be determined to be a significant risk, may arise from matters such as the following:

- Transactions for which there are multiple acceptable accounting treatments such that subjectivity is involved.
- Accounting estimates that have high estimation uncertainty or complex models.
- Complexity in data collection and processing to support account balances.
- Account balances or quantitative disclosures that involve complex calculations.
- Accounting principles that may be subject to differing interpretation.
- Changes in the entity's business that involve changes in accounting, for example, mergers and acquisitions.

<sup>58</sup> ISA- (NZ) 240, paragraphs 26–28

## Risks for Which Substantive Procedures Alone Do Not Provide Sufficient Appropriate Audit Evidence (Ref: Para. 33)

Why risks for which substantive procedures alone do not provide sufficient appropriate audit evidence are required to be identified

A222. Due to the nature of a risk of material misstatement, and the control activities that address that risk, in some circumstances the only way to obtain sufficient appropriate audit evidence is to test the operating effectiveness of controls. Accordingly, there is a requirement for the auditor to identify any such risks because of the implications for the design and performance of further audit procedures in accordance with ISA- (NZ) 330 to address risks of material misstatement at the assertion level.

A223. Paragraph 26(a)(iii) also requires the identification of controls that address risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence because the auditor is required, in accordance with ISA- (NZ) 330,<sup>59</sup> to design and perform tests of such controls.

## Determining risks for which substantive procedures alone do not provide sufficient appropriate audit evidence

A224. Where routine business transactions are subject to highly automated processing with little or no manual intervention, it may not be possible to perform only substantive procedures in relation to the risk. This may be the case in circumstances where a significant amount of an entity's information is initiated, recorded, processed, or reported only in electronic form such as in an information system that involves a high degree of integration across its IT applications. In such cases:

- Audit evidence may be available only in electronic form, and its sufficiency and appropriateness usually depend on the effectiveness of controls over its accuracy and completeness.
- The potential for improper initiation or alteration of information to occur and not be detected may be greater if appropriate controls are not operating effectively.

### Example:

It is typically not possible to obtain sufficient appropriate audit evidence relating to revenue for a telecommunications entity based on substantive procedures alone. This is because the evidence of call or data activity does not exist in a form that is observable. Instead, substantial controls testing is typically performed to determine that the origination and completion of calls, and data activity is correctly captured (e.g., minutes of a call or volume of a download) and recorded correctly in the entity's billing system.

<sup>59</sup> ISA- (NZ) 330, paragraph 8

A225. ISA- (NZ) 540 (Revised) provides further guidance related to accounting estimates about risks for which substantive procedures alone do not provide sufficient appropriate audit evidence.<sup>60</sup> In relation to accounting estimates this may not be limited to automated processing, but may also be applicable to complex models.

*Assessing Control Risk* (Ref: Para. 34)

A226. The auditor's plans to test the operating effectiveness of controls is based on the expectation that controls are operating effectively, and this will form the basis of the auditor's assessment of control risk. The initial expectation of the operating effectiveness of controls is based on the auditor's evaluation of the design, and the determination of implementation, of the identified controls in the control activities component. Once the auditor has tested the operating effectiveness of the controls in accordance with ISA- (NZ) 330, the auditor will be able to confirm the initial expectation about the operating effectiveness of controls. If the controls are not operating effectively as expected, then the auditor will need to revise the control risk assessment in accordance with paragraph 37.

A227. The auditor's assessment of control risk may be performed in different ways depending on preferred audit techniques or methodologies, and may be expressed in different ways.

A228. If the auditor plans to test the operating effectiveness of controls, it may be necessary to test a combination of controls to confirm the auditor's expectation that the controls are operating effectively. The auditor may plan to test both direct and indirect controls, including general IT controls, and, if so, take into account the combined expected effect of the controls when assessing control risk. To the extent that the control to be tested does not fully address the assessed inherent risk, the auditor determines the implications on the design of further audit procedures to reduce audit risk to an acceptably low level.

A229. When the auditor plans to test the operating effectiveness of an automated control, the auditor may also plan to test the operating effectiveness of the relevant general IT controls that support the continued functioning of that automated control to address the risks arising from the use of IT, and to provide a basis for the auditor's expectation that the automated control operated effectively throughout the period. When the auditor expects related general IT controls to be ineffective, this determination may affect the auditor's assessment of control risk at the assertion level and the auditor's further audit procedures may need to include substantive procedures to address the applicable risks arising from the use of IT. Further guidance about the procedures that the auditor may perform in these circumstances is provided in ISA- (NZ) 330.<sup>61</sup>

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<sup>60</sup> ISA- (NZ) 540 (Revised), paragraphs A87–A89

<sup>61</sup> ISA- (NZ) 330, paragraphs A29–A30

*Evaluating the Audit Evidence Obtained from the Risk Assessment Procedures* (Ref: Para 35)

Why the Auditor Evaluates the Audit Evidence from the Risk Assessment Procedures

A230. Audit evidence obtained from performing risk assessment procedures provides the basis for the identification and assessment of the risks of material misstatement. This provides the basis for the auditor's design of the nature, timing and extent of further audit procedures responsive to the assessed risks of material misstatement, at the assertion level, in accordance with ISA- (NZ) 330. Accordingly, the audit evidence obtained from the risk assessment procedures provides a basis for the identification and assessment of risks of material misstatement whether due to fraud or error, at the financial statement and assertion levels.

The Evaluation of the Audit Evidence

A231. Audit evidence from risk assessment procedures comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions.<sup>62</sup>

Professional ~~Skepticism~~ Scepticism

A232. In evaluating the audit evidence from the risk assessment procedures, the auditor considers whether sufficient understanding about the entity and its environment, the applicable financial reporting framework and the entity's system of internal control has been obtained to be able to identify the risks of material misstatement, as well as whether there is any evidence that is contradictory that may indicate a risk of material misstatement.

*Classes of Transactions, Account Balances and Disclosures that Are Not Significant, but Which Are Material* (Ref: Para. 36)

A233. As explained in ISA- (NZ) 320,<sup>63</sup> materiality and audit risk are considered when identifying and assessing the risks of material misstatement in classes of transactions, account balances and disclosures. The auditor's determination of materiality is a matter of professional ~~judgment~~ judgement, and is affected by the auditor's perception of the financial information needs of users of the financial statements.<sup>64</sup> For the purpose of this ISA- (NZ) and paragraph 18 of ISA- (NZ) 330, classes of transactions, account balances or disclosures are material if omitting, misstating or obscuring information about them could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements as a whole.

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<sup>62</sup> ISA- (NZ) 500, paragraph A1

<sup>63</sup> ISA- (NZ) 320, paragraph A1

<sup>64</sup> ISA- (NZ) 320, paragraph 4

A234. There may be classes of transactions, account balances or disclosures that are material but have not been determined to be significant classes of transactions, account balances or disclosures (i.e., there are no relevant assertions identified).

**Example:**

The entity may have a disclosure about executive compensation for which the auditor has not identified a risk of material misstatement. However, the auditor may determine that this disclosure is material based on the considerations in paragraph A233.

A235. Audit procedures to address classes of transactions, account balances or disclosures that are material but are not determined to be significant are addressed in ISA- (NZ) 330.<sup>65</sup> When a class of transactions, account balance or disclosure is determined to be significant as required by paragraph 29, the class of transactions, account balance or disclosure is also a material class of transactions, account balance or disclosure for the purposes of paragraph 18 of ISA- (NZ) 330.

**Revision of Risk Assessment (Ref: Para. 37)**

A236. During the audit, new or other information may come to the auditor's attention that differs significantly from the information on which the risk assessment was based.

**Example:**

The entity's risk assessment may be based on an expectation that certain controls are operating effectively. In performing tests of those controls, the auditor may obtain audit evidence that they were not operating effectively at relevant times during the audit. Similarly, in performing substantive procedures the auditor may detect misstatements in amounts or frequency greater than is consistent with the auditor's risk assessments. In such circumstances, the risk assessment may not appropriately reflect the true circumstances of the entity and the further planned audit procedures may not be effective in detecting material misstatements. Paragraphs 16 and 17 of ISA- (NZ) 330 provide further guidance about evaluating the operating effectiveness of controls.

**Documentation (Ref: Para. 38)**

A237. For recurring audits, certain documentation may be carried forward, updated as necessary to reflect changes in the entity's business or processes.

A238. ISA- (NZ) 230 notes that, among other considerations, although there may be no single way in which the auditor's exercise of professional ~~skepticism~~scepticism is documented, the audit documentation may nevertheless provide evidence of the auditor's exercise of professional ~~skepticism~~scepticism.<sup>66</sup> For example, when the audit evidence obtained from

<sup>65</sup> ISA- (NZ) 330, paragraph 18

<sup>66</sup> ISA- (NZ) 230, paragraph A7

risk assessment procedures includes evidence that both corroborates and contradicts management's assertions, the documentation may include how the auditor evaluated that evidence, including the professional ~~judgments~~judgements made in evaluating whether the audit evidence provides an appropriate basis for the auditor's identification and assessment of the risks of material misstatement. Examples of other requirements in this ISA- (NZ) for which documentation may provide evidence of the exercise of professional ~~skepticism~~scepticism by the auditor include:

- Paragraph 13, which requires the auditor to design and perform risk assessment procedures in a manner that is not biased towards obtaining audit evidence that may corroborate the existence of risks or towards excluding audit evidence that may contradict the existence of risks;
- Paragraph 17, which requires a discussion among key engagement team members of the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement;
- Paragraphs 19(b) and 20, which require the auditor to obtain an understanding of the reasons for any changes to the entity's accounting policies and to evaluate whether the entity's accounting policies are appropriate and consistent with the applicable financial reporting framework;
- Paragraphs 21(b), 22(b), 23(b), 24(c), 25(c), 26(d) and 27, which require the auditor to evaluate, based on the required understanding obtained, whether the components of the entity's system of internal control are appropriate to the entity's circumstances considering the nature and complexity of the entity, and to determine whether one of more control deficiencies have been identified;
- Paragraph 35, which requires the auditor to take into account all audit evidence obtained from the risk assessment procedures, whether corroborative or contradictory to assertions made by management, and to evaluate whether the audit evidence obtained from the risk assessment procedures provides an appropriate basis for the identification and assessment of the risks of material misstatement; and
- Paragraph 36, which requires the auditor to evaluate, when applicable, whether the auditor's determination that there are no risks of material misstatement for a material class of transactions, account balance or disclosure remains appropriate.

#### Scalability

A239. The manner in which the requirements of paragraph 38 are documented is for the auditor to determine using professional ~~judgment~~judgement.

A240. More detailed documentation, that is sufficient to enable an experienced auditor, having no previous experience with the audit, to understand the nature, timing and extent of the audit procedures performed, may be required to support the rationale for difficult ~~judgments~~judgements made.



A241. For the audits of less complex entities, the form and extent of documentation may be simple and relatively brief. The form and extent of the auditor's documentation is influenced by the nature, size and complexity of the entity and its system of internal control, availability of information from the entity and the audit methodology and technology used in the course of the audit. It is not necessary to document the entirety of the auditor's understanding of the entity and matters related to it. Key elements<sup>67</sup> of understanding documented by the auditor may include those on which the auditor based the assessment of the risks of material misstatement. However, the auditor is not required to document every inherent risk factor that was taken into account in identifying and assessing the risks of material misstatement at the assertion level.

**Example:**

In audits of less complex entities audit documentation may be incorporated in the auditor's documentation of the overall strategy and audit plan.<sup>68</sup> Similarly, for example, the results of the risk assessment may be documented separately, or may be documented as part of the auditor's documentation of further audit procedures.<sup>69</sup>

<sup>67</sup> ISA- (NZ) 230, paragraph 8

<sup>68</sup> ISA- (NZ) 300, *Planning an Audit of Financial Statements*, paragraphs 7, 9 and A11

<sup>69</sup> ISA- (NZ) 330, paragraph 28



**Appendix 1**

(Ref: Para. A61–A67)

**Considerations for Understanding the Entity and its Business Model**

This appendix explains the objectives and scope of the entity's business model and provides examples of matters that the auditor may consider in understanding the activities of the entity that may be included in the business model. The auditor's understanding of the entity's business model, and how it is affected by its business strategy and business objectives, may assist the auditor in identifying business risks that may have an effect on the financial statements. In addition, this may assist the auditor in identifying risks of material misstatement.

**Objectives and Scope of an Entity's Business Model**

1. An entity's business model describes how an entity considers, for example its ~~organizational~~organisational structure, operations or scope of activities, business lines (including competitors and customers thereof), processes, growth opportunities, ~~globalization~~globalisation, regulatory requirements and technologies. The entity's business model describes how the entity creates, preserves and captures financial or broader value, for its stakeholders.
2. Strategies are the approaches by which management plans to achieve the entity's objectives, including how the entity plans to address the risks and opportunities that it faces. An entity's strategies are changed over time by management, to respond to changes in its objectives and in the internal and external circumstances in which it operates.
3. A description of a business model typically includes:
  - The scope of the entity's activities, and why it does them.
  - The entity's structure and scale of its operations.
  - The markets or geographical or demographic spheres, and parts of the value chain, in which it operates, how it engages with those markets or spheres (main products, customer segments and distribution methods), and the basis on which it competes.
  - The entity's business or operating processes (e.g., investment, financing and operating processes) employed in performing its activities, focusing on those parts of the business processes that are important in creating, preserving or capturing value.
  - The resources (e.g., financial, human, intellectual, environmental and technological) and other inputs and relationships (e.g., customers, competitors, suppliers and employees) that are necessary or important to its success.
  - How the entity's business model integrates the use of IT in its interactions with customers, suppliers, lenders and other stakeholders through IT interfaces and other technologies.

4. A business risk may have an immediate consequence for the risk of material misstatement for classes of transactions, account balances, and disclosures at the assertion level or the financial statement level. For example, the business risk arising from a significant fall in real estate market values may increase the risk of material misstatement associated with the valuation assertion for a lender of medium-term real estate backed loans. However, the same risk, particularly in combination with a severe economic downturn that concurrently increases the underlying risk of lifetime credit losses on its loans, may also have a longer-term consequence. The resulting net exposure to credit losses may cast significant doubt on the entity's ability to continue as a going concern. If so, this could have implications for management's, and the auditor's, conclusion as to the appropriateness of the entity's use of the going concern basis of accounting, and determination as to whether a material uncertainty exists. Whether a business risk may result in a risk of material misstatement is, therefore, considered in light of the entity's circumstances. Examples of events and conditions that may give rise to the existence of risks of material misstatement are indicated in **Appendix 2**.

### Activities of the Entity

5. Examples of matters that the auditor may consider when obtaining an understanding of the activities of the entity (included in the entity's business model) include:
  - (a) Business operations such as:
    - Nature of revenue sources, products or services, and markets, including involvement in electronic commerce such as Internet sales and marketing activities.
    - Conduct of operations (for example, stages and methods of production, or activities exposed to environmental risks).
    - Alliances, joint ventures, and outsourcing activities.
    - Geographic dispersion and industry segmentation.
    - Location of production facilities, warehouses, and offices, and location and quantities of inventories.
    - Key customers and important suppliers of goods and services, employment arrangements (including the existence of union contracts, pension and other post-employment benefits, [stockshare](#) option or incentive bonus arrangements, and government regulation related to employment matters).
    - Research and development activities and expenditures.
    - Transactions with related parties.
  - (b) Investments and investment activities such as:
    - Planned or recently executed acquisitions or divestitures.
    - Investments and dispositions of securities and loans.

- Capital investment activities.
  - Investments in non-consolidated entities, including non-controlled partnerships, joint ventures and non-controlled special-purpose entities.
- (c) Financing and financing activities such as:
- Ownership structure of major subsidiaries and associated entities, including consolidated and non-consolidated structures.
  - Debt structure and related terms, including off-balance-sheet financing arrangements and leasing arrangements.
  - Beneficial owners (local, foreign, business reputation and experience) and related parties.
  - Use of derivative financial instruments.

### Nature of Special-Purpose Entities

6. A special-purpose entity (sometimes referred to as a special-purpose vehicle) is an entity that is generally established for a narrow and well-defined purpose, such as to effect a lease or a ~~securitization~~ *securitisation* of financial assets, or to carry out research and development activities. It may take the form of a corporation, trust, partnership or unincorporated entity. The entity on behalf of which the special-purpose entity has been created may often transfer assets to the latter (for example, as part of a derecognition transaction involving financial assets), obtain the right to use the latter's assets, or perform services for the latter, while other parties may provide the funding to the latter. As ISA- (NZ) 550 indicates, in some circumstances, a special-purpose entity may be a related party of the entity.<sup>70</sup>
7. Financial reporting frameworks often specify detailed conditions that are deemed to amount to control, or circumstances under which the special-purpose entity should be considered for consolidation. The interpretation of the requirements of such frameworks often demands a detailed knowledge of the relevant agreements involving the special-purpose entity.

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<sup>70</sup> ISA- (NZ) 550, paragraph A7

## Appendix 2

(Ref: Para. 12(f), 19(c), A7–A8, A85–A89)

**Understanding Inherent Risk Factors**

This appendix provides further explanation about the inherent risk factors, as well as matters that the auditor may consider in understanding and applying the inherent risk factors in identifying and assessing the risks of material misstatement at the assertion level.

**The Inherent Risk Factors**

1. Inherent risk factors are characteristics of events or conditions that affect susceptibility of an assertion about a class of transactions, account balance or disclosure, to misstatement, whether due to fraud or error, and 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 other fraud risk factors<sup>71</sup> insofar as they affect inherent risk. In obtaining the understanding of the entity and its environment, and the applicable financial reporting framework and entity's accounting policies, in accordance with paragraphs 19(a)–(b), the auditor also understands how inherent risk factors affect susceptibility of assertions to misstatement in the preparation of the financial statements.
2. Inherent risk factors relating to the preparation of information required by the applicable financial reporting framework (referred to in this paragraph as “required information”) include:
  - *Complexity*—arises either from the nature of the information or in the way that the required information is prepared, including when such preparation processes are more inherently difficult to apply. For example, complexity may arise:
    - In calculating supplier rebate provisions because it may be necessary to take into account different commercial terms with many different suppliers, or many interrelated commercial terms that are all relevant in calculating the rebates due; or
    - When there are many potential data sources, with different characteristics used in making an accounting estimate, the processing of that data involves many inter-related steps, and the data is therefore inherently more difficult to identify, capture, access, understand or process.
  - *Subjectivity*—arises from inherent limitations in the ability to prepare required information in an objective manner, due to limitations in the availability of knowledge or information, such that management may need to make an election or subjective judgment about the appropriate approach to take and about the resulting

<sup>71</sup> ISA (NZ) 240, paragraphs A24–A27

information to include in the financial statements. Because of different approaches to preparing the required information, different outcomes could result from appropriately applying the requirements of the applicable financial reporting framework. As limitations in knowledge or data increase, the subjectivity in the ~~judgments~~judgements that could be made by reasonably knowledgeable and independent individuals, and the diversity in possible outcomes of those ~~judgments~~judgements will also increase.

- *Change*—results from events or conditions that, over time, affect the entity’s business or the economic, accounting, regulatory, industry or other aspects of the environment in which it operates, when the effects of those events or conditions are reflected in the required information. Such events or conditions may occur during, or between, financial reporting periods. For example, change may result from developments in the requirements of the applicable financial reporting framework, or in the entity and its business model, or in the environment in which the entity operates. Such change may affect management’s assumptions and ~~judgments~~judgements, including as they relate to management’s selection of accounting policies or how accounting estimates are made or related disclosures are determined.
- *Uncertainty*—arises when the required information cannot be prepared based only on sufficiently precise and comprehensive data that is verifiable through direct observation. In these circumstances, an approach may need to be taken that applies the available knowledge to prepare the information using sufficiently precise and comprehensive observable data, to the extent available, and reasonable assumptions supported by the most appropriate available data, when it is not. Constraints on the availability of knowledge or data, which are not within the control of management (subject to cost constraints where applicable) are sources of uncertainty and their effect on the preparation of the required information cannot be eliminated. For example, estimation uncertainty arises when the required monetary amount cannot be determined with precision and the outcome of the estimate is not known before the date the financial statements are ~~finalized~~finalised.
- *Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk* —susceptibility to management bias results from conditions that create susceptibility to intentional or unintentional failure by management to maintain neutrality in preparing the information. Management bias is often associated with certain conditions that have the potential to give rise to management not maintaining neutrality in exercising ~~judgment~~judgement (indicators of potential management bias), which could lead to a material misstatement of the information that would be fraudulent if intentional. Such indicators include incentives or pressures insofar as they affect inherent risk (for example, as a result of motivation to achieve a desired result, such as a desired profit target or capital ratio), and opportunity, not to maintain neutrality. Factors relevant to the susceptibility to misstatement due to fraud in the form of fraudulent financial reporting or misappropriation of assets are described in paragraphs A1 to A5 of ISA- (NZ) 240.

3. When complexity is an inherent risk factor, there may be an inherent need for more complex processes in preparing the information, and such processes may be inherently more difficult to apply. As a result, applying them may require ~~specialized~~specialised skills or knowledge, and may require the use of a management's expert.
4. When management ~~judgment~~judgement is more subjective, the susceptibility to misstatement due to management bias, whether unintentional or intentional, may also increase. For example, significant management ~~judgment~~judgement may be involved in making accounting estimates that have been identified as having high estimation uncertainty, and conclusions regarding methods, data and assumptions may reflect unintentional or intentional management bias.

### Examples of Events or Conditions that May Give Rise to the Existence of Risks of Material Misstatement

5. The following are examples of events (including transactions) and conditions that may indicate the existence of risks of material misstatement in the financial statements, at the financial statement level or the assertion level. The examples provided by inherent risk factor cover a broad range of events and conditions; however, not all events and conditions are relevant to every audit engagement and the list of examples is not necessarily complete. The events and conditions have been ~~categorized~~categorised by the inherent risk factor that may have the greatest effect in the circumstances. Importantly, due to the interrelationships among inherent risk factors, the example events and conditions also are likely to be subject to, or affected by, other inherent risk factors to varying degrees.

| Relevant Inherent Risk Factor: | Examples of Events and Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:  |
|--------------------------------|--|
| Complexity                     | <p>Regulatory:</p> <ul style="list-style-type: none"> <li>Operations that are subject to a high degree of complex regulation.</li> </ul> <p>Business model:</p> <ul style="list-style-type: none"> <li>The existence of complex alliances and joint ventures.</li> </ul> <p>Applicable financial reporting framework:</p> <ul style="list-style-type: none"> <li>Accounting measurements that involve complex processes.</li> </ul> <p>Transactions:</p> <ul style="list-style-type: none"> <li>Use of off-balance sheet finance, special-purpose entities, and other complex financing arrangements.</li> </ul> |
| Subjectivity                   | Applicable financial reporting framework:  |

| Relevant Inherent Risk Factor: | Examples of Events and Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>A wide range of possible measurement criteria of an accounting estimate. For example, management's recognition of depreciation or construction income and expenses.</li> <li>Management's selection of a valuation technique or model for a non-current asset, such as investment properties.</li> </ul>  |
| Change                         | <p>Economic conditions:</p> <ul style="list-style-type: none"> <li>Operations in regions that are economically unstable, for example, countries with significant currency devaluation or highly inflationary economies.</li> </ul> <p>Markets:</p> <ul style="list-style-type: none"> <li>Operations exposed to volatile markets, for example, futures trading.</li> </ul> <p>Customer loss:</p> <ul style="list-style-type: none"> <li>Going concern and liquidity issues including loss of significant customers.</li> </ul> <p>Industry model:</p> <ul style="list-style-type: none"> <li>Changes in the industry in which the entity operates.</li> </ul> <p>Business model:</p> <ul style="list-style-type: none"> <li>Changes in the supply chain.</li> <li>Developing or offering new products or services, or moving into new lines of business.</li> </ul> <p>Geography:</p> <ul style="list-style-type: none"> <li>Expanding into new locations.</li> </ul> <p>Entity structure:</p> <ul style="list-style-type: none"> <li>Changes in the entity such as large acquisitions or <del>reorganizations</del>reorganisations or other unusual events.</li> <li>Entities or business segments likely to be sold.</li> </ul> <p>Human resources competence:</p> <ul style="list-style-type: none"> <li>Changes in key personnel including departure of key executives.</li> </ul> |

| Relevant Inherent Risk Factor:   | Examples of Events and Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:  |
|--|--|
|  | <p>IT:</p> <ul style="list-style-type: none"> <li>• Changes in the IT environment.</li> <li>• Installation of significant new IT systems related to financial reporting.</li> </ul> <p>Applicable financial reporting framework:</p> <ul style="list-style-type: none"> <li>• Application of new accounting pronouncements.</li> </ul> <p>Capital:</p> <ul style="list-style-type: none"> <li>• New constraints on the availability of capital and credit.</li> </ul> <p>Regulatory:</p> <ul style="list-style-type: none"> <li>• Inception of investigations into the entity's operations or financial results by regulatory or government bodies.</li> <li>• Impact of new legislation related to environmental protection.</li> </ul> |
| Uncertainty  | <p>Reporting:</p> <ul style="list-style-type: none"> <li>• Events or transactions that involve significant measurement uncertainty, including accounting estimates, and related disclosures.</li> <li>• Pending litigation and contingent liabilities, for example, sales warranties, financial guarantees and environmental remediation.</li> </ul>   |
| Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk | <p>Reporting:</p> <ul style="list-style-type: none"> <li>• Opportunities for management and employees to engage in fraudulent financial reporting, including omission, or obscuring, of significant information in disclosures.</li> </ul> <p>Transactions:</p> <ul style="list-style-type: none"> <li>• Significant transactions with related parties.</li> <li>• Significant amount of non-routine or non-systematic transactions including intercompany transactions and large revenue transactions at period end.</li> <li>• Transactions that are recorded based on management's intent, for example, debt refinancing, assets to be sold and classification of marketable securities.</li> </ul>                                   |



*Other events or conditions that may indicate risks of material misstatement at the financial statement level:*

- Lack of personnel with appropriate accounting and financial reporting skills.
- Control deficiencies – particularly in the control environment, risk assessment process and process for monitoring, and especially those not addressed by management.
- Past misstatements, history of errors or a significant amount of adjustments at period end.

## Appendix 3

(Ref: Para. 12(m), 21–26, A90–A181)

### Understanding the Entity's System of Internal Control

1. The entity's system of internal control may be reflected in policy and procedures manuals, systems and forms, and the information embedded therein, and is effected by people. The entity's system of internal control is implemented by management, those charged with governance, and other personnel based on the structure of the entity. The entity's system of internal control can be applied, based on the decisions of management, those charged with governance or other personnel and in the context of legal or regulatory requirements, to the operating model of the entity, the legal entity structure, or a combination of these.
2. This appendix further explains the components of, as well as the limitations of, the entity's system of internal control as set out in paragraphs 12(m), 21–26, and A90–A181, as they relate to a financial statement audit.
3. Included within the entity's system of internal control are aspects that relate to the entity's reporting objectives, including its financial reporting objectives, but it may also include aspects that relate to its operations or compliance objectives, when such aspects are relevant to financial reporting.

#### Example:

Controls over compliance with laws and regulations may be relevant to financial reporting when such controls are relevant to the entity's preparation of disclosures of contingencies in the financial statements.

### Components of the Entity's System of Internal Control

#### *Control Environment*

4. The control environment includes the governance and management functions and the attitudes, awareness, and actions of those charged with governance and management concerning the entity's system of internal control, and its importance in the entity. The control environment sets the tone of an ~~organization~~ organisation, influencing the control consciousness of its people, and provides the overall foundation for the operation of the other components of the entity's system of internal control.
5. An entity's control consciousness is influenced by those charged with governance, because one of their roles is to counterbalance pressures on management in relation to financial reporting that may arise from market demands or remuneration schemes. The effectiveness of the design of the control environment in relation to participation by those charged with governance is therefore influenced by such matters as:

- Their independence from management and their ability to evaluate the actions of management.
  - Whether they understand the entity's business transactions.
  - The extent to which they evaluate whether the financial statements are prepared in accordance with the applicable financial reporting framework, including whether the financial statements include adequate disclosures.
6. The control environment encompasses the following elements:
- (a) *How management's responsibilities are carried out, such as creating and maintaining the entity's culture and demonstrating management's commitment to integrity and ethical values.* The effectiveness of controls cannot rise above the integrity and ethical values of the people who create, administer, and monitor them. Integrity and ethical ~~behavior~~behaviour are the product of the entity's ethical and ~~behavioral~~behavioural standards or codes of conduct, how they are communicated (e.g., through policy statements), and how they are reinforced in practice (e.g., through management actions to eliminate or mitigate incentives or temptations that might prompt personnel to engage in dishonest, illegal, or unethical acts). The communication of entity policies on integrity and ethical values may include the communication of ~~behavioral~~behavioural standards to personnel through policy statements and codes of conduct and by example.
  - (b) *When those charged with governance are separate from management, how those charged with governance demonstrate independence from management and exercise oversight of the entity's system of internal control.* An entity's control consciousness is influenced by those charged with governance. Considerations may include whether there are sufficient individuals who are independent from management and objective in their evaluations and decision-making; how those charged with governance identify and accept oversight responsibilities and whether those charged with governance retain oversight responsibility for management's design, implementation and conduct of the entity's system of internal control. The importance of the responsibilities of those charged with governance is ~~recognized~~recognised in codes of practice and other laws and regulations or guidance produced for the benefit of those charged with governance. Other responsibilities of those charged with governance include oversight of the design and effective operation of whistle blower procedures.
  - (c) *How the entity assigns authority and responsibility in pursuit of its objectives.* This may include considerations about:
    - Key areas of authority and responsibility and appropriate lines of reporting;
    - Policies relating to appropriate business practices, knowledge and experience of key personnel, and resource provided for carrying out duties; and
    - Policies and communications directed at ensuring that all personnel understand the entity's objectives, know how their individual actions interrelate and

contribute to those objectives, and ~~recognize~~recognise how and for what they will be held accountable.

- (d) *How the entity attracts, develops, and retains competent individuals in alignment with its objectives.* This includes how the entity ensures the individuals have the knowledge and skills necessary to accomplish the tasks that define the individual's job, such as:
- Standards for recruiting the most qualified individuals – with an emphasis on educational background, prior work experience, past accomplishments, and evidence of integrity and ethical ~~behavior~~behaviour.
  - Training policies that communicate prospective roles and responsibilities, including practices such as training schools and seminars that illustrate expected levels of performance and ~~behavior~~behaviour; and
  - Periodic performance appraisals driving promotions that demonstrate the entity's commitment to the advancement of qualified personnel to higher levels of responsibility.
- (e) *How the entity holds individuals accountable for their responsibilities in pursuit of the objectives of the entity's system of internal control.* This may be accomplished through, for example:
- Mechanisms to communicate and hold individuals accountable for performance of controls responsibilities and implement corrective actions as necessary;
  - Establishing performance measures, incentives and rewards for those responsible for the entity's system of internal control, including how the measures are evaluated and maintain their relevance;
  - How pressures associated with the achievement of control objectives impact the individual's responsibilities and performance measures; and
  - How the individuals are disciplined as necessary.

The appropriateness of the above matters will be different for every entity depending on its size, the complexity of its structure and the nature of its activities.

#### *The Entity's Risk Assessment Process*

7. The entity's risk assessment process is an iterative process for identifying and ~~analyzing~~analysing risks to achieving the entity's objectives, and forms the basis for how management or those charged with governance determine the risks to be managed.
8. For financial reporting purposes, the entity's risk assessment process includes how management identifies business risks relevant to the preparation of financial statements in accordance with the entity's applicable financial reporting framework, estimates their significance, assesses the likelihood of their occurrence, and decides upon actions to manage them and the results thereof. For example, the entity's risk assessment process may address

how the entity considers the possibility of unrecorded transactions or identifies and analyzes significant estimates recorded in the financial statements.

9. Risks relevant to reliable financial reporting include external and internal events, transactions or circumstances that may occur and adversely affect an entity's ability to initiate, record, process, and report financial information consistent with the assertions of management in the financial statements. Management may initiate plans, programs, or actions to address specific risks or it may decide to assume a risk because of cost or other considerations. Risks can arise or change due to circumstances such as the following:
  - *Changes in operating environment.* Changes in the regulatory, economic or operating environment can result in changes in competitive pressures and significantly different risks.
  - *New personnel.* New personnel may have a different focus on or understanding of the entity's system of internal control.
  - *New or revamped information system.* Significant and rapid changes in the information system can change the risk relating to the entity's system of internal control.
  - *Rapid growth.* Significant and rapid expansion of operations can strain controls and increase the risk of a breakdown in controls.
  - *New technology.* Incorporating new technologies into production processes or the information system may change the risk associated with the entity's system of internal control.
  - *New business models, products, or activities.* Entering into business areas or transactions with which an entity has little experience may introduce new risks associated with the entity's system of internal control.
  - *Corporate restructurings.* Restructurings may be accompanied by staff reductions and changes in supervision and segregation of duties that may change the risk associated with the entity's system internal control.
  - *Expanded foreign operations.* The expansion or acquisition of foreign operations carries new and often unique risks that may affect internal control, for example, additional or changed risks from foreign currency transactions.
  - *New accounting pronouncements.* Adoption of new accounting principles or changing accounting principles may affect risks in preparing financial statements.
  - *Use of IT.* Risks relating to:
    - Maintaining the integrity of data and information processing;
    - Risks to the entity business strategy that arise if the entity's IT strategy does not effectively supporting the entity's business strategy; or

- Changes or interruptions in the entity's IT environment or turnover of IT personnel or when the entity does not make necessary updates to the IT environment or such updates are not timely.

*The Entity's Process to Monitor the System of Internal Control*

10. The entity's process to monitor the system of internal control is a continual process to evaluate the effectiveness of the entity's system of internal control, and to take necessary remedial actions on a timely basis. The entity's process to monitor the entity's system of internal control may consist of ongoing activities, separate evaluations (conducted periodically), or some combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and may include regular management and supervisory activities. The entity's process will likely vary in scope and frequency depending on the assessment of the risks by the entity.
11. The objectives and scope of internal audit functions typically include activities designed to evaluate or monitor the effectiveness of the entity's system of internal control.<sup>72</sup> The entity's process to monitor the entity's system of internal control may include activities such as management's review of whether bank reconciliations are being prepared on a timely basis, internal auditors' evaluation of sales personnel's compliance with the entity's policies on terms of sales contracts, and a legal department's oversight of compliance with the entity's ethical or business practice policies. Monitoring is done also to ensure that controls continue to operate effectively over time. For example, if the timeliness and accuracy of bank reconciliations are not monitored, personnel are likely to stop preparing them.
12. Controls related to the entity's process to monitor the entity's system of internal control, including those that monitor underlying automated controls, may be automated or manual, or a combination of both. For example, an entity may use automated monitoring controls over access to certain technology with automated reports of unusual activity to management, who manually investigate identified anomalies.
13. When distinguishing between a monitoring activity and a control related to the information system, the underlying details of the activity are considered, especially when the activity involves some level of supervisory review. Supervisory reviews are not automatically classified as monitoring activities and it may be a matter of ~~judgment~~ judgement whether a review is classified as a control related to the information system or a monitoring activity. For example, the intent of a monthly completeness control would be to detect and correct errors, where a monitoring activity would ask why errors are occurring and assign management the responsibility of fixing the process to prevent future errors. In simple terms, a control related to the information system responds to a specific risk, whereas a monitoring activity assesses whether controls within each of the five components of the entity's system of internal control are operating as intended.

<sup>72</sup> ISA- (NZ) 610 (Revised 2013) and Appendix 4 of this ISA- (NZ) provides further guidance related to internal audit.

14. Monitoring activities may include using information from communications from external parties that may indicate problems or highlight areas in need of improvement. Customers implicitly corroborate billing data by paying their invoices or complaining about their charges. In addition, regulators may communicate with the entity concerning matters that affect the functioning of the entity's system of internal control, for example, communications concerning examinations by bank regulatory agencies. Also, management may consider in performing monitoring activities any communications relating to the entity's system of internal control from external auditors.

#### *The Information System and Communication*

15. The information system relevant to the preparation of the financial statements in consists of activities and policies, and accounting and supporting records, designed and established to:
  - Initiate, record and process entity transactions (as well as to capture, process and disclose information about events and conditions other than transactions) and to maintain accountability for the related assets, liabilities, and equity;
  - Resolve incorrect processing of transactions, for example, automated suspense files and procedures followed to clear suspense items out on a timely basis;
  - Process and account for system overrides or bypasses to controls;
  - Incorporate information from transaction processing in the general ledger (e.g., transferring of accumulated transactions from a subsidiary ledger);
  - Capture and process information relevant to the preparation of the financial statements for events and conditions other than transactions, such as the depreciation and ~~amortization~~ amortisation of assets and changes in the recoverability of assets; and
  - Ensure information required to be disclosed by the applicable financial reporting framework is accumulated, recorded, processed, ~~summarized~~ summarised and appropriately reported in the financial statements.
16. An entity's business processes include the activities designed to:
  - Develop, purchase, produce, sell and distribute an entity's products and services;
  - Ensure compliance with laws and regulations; and
  - Record information, including accounting and financial reporting information.

Business processes result in the transactions that are recorded, processed and reported by the information system.

17. The quality of information affects management's ability to make appropriate decisions in managing and controlling the entity's activities and to prepare reliable financial reports.
18. Communication, which involves providing an understanding of individual roles and responsibilities pertaining to the entity's system of internal control, may take such forms as



policy manuals, accounting and financial reporting manuals, and memoranda. Communication also can be made electronically, orally, and through the actions of management.

19. Communication by the entity of the financial reporting roles and responsibilities and of significant matters relating to financial reporting involves providing an understanding of individual roles and responsibilities pertaining to the entity's system of internal control relevant to financial reporting. It may include such matters as the extent to which personnel understand how their activities in the information system relate to the work of others and the means of reporting exceptions to an appropriate higher level within the entity.

#### *Control Activities*

20. Controls in the control activities component are identified in accordance with paragraph 26. Such controls include information processing controls and general IT controls, both of which may be manual or automated in nature. The greater the extent of automated controls, or controls involving automated aspects, that management uses and relies on in relation to its financial reporting, the more important it may become for the entity to implement general IT controls that address the continued functioning of the automated aspects of information processing controls. Controls in the control activities component may pertain to the following:

- ~~Authorization~~*Authorisation* and approvals. An ~~authorization~~*authorisation* affirms that a transaction is valid (i.e. it represents an actual economic event or is within an entity's policy). An ~~authorization~~*authorisation* typically takes the form of an approval by a higher level of management or of verification and a determination if the transaction is valid. For example, a supervisor approves an expense report after reviewing whether the expenses seem reasonable and within policy. An example of an automated approval is when an invoice unit cost is automatically compared with the related purchase order unit cost within a pre-established tolerance level. Invoices within the tolerance level are automatically approved for payment. Those invoices outside the tolerance level are flagged for additional investigation.
- *Reconciliations* – Reconciliations compare two or more data elements. If differences are identified, action is taken to bring the data into agreement. Reconciliations generally address the completeness or accuracy of processing transactions.
- *Verifications* – Verifications compare two or more items with each other or compare an item with a policy, and will likely involve a follow-up action when the two items do not match or the item is not consistent with policy. Verifications generally address the completeness, accuracy, or validity of processing transactions.
- *Physical or logical controls, including those that address security of assets against ~~unauthorized~~*unauthorised* access, acquisition, use or disposal.* Controls that encompass:



- The physical security of assets, including adequate safeguards such as secured facilities over access to assets and records.
- The ~~authorization~~authorisation for access to computer programs and data files (i.e., logical access).
- The periodic counting and comparison with amounts shown on control records (for example, comparing the results of cash, security and inventory counts with accounting records).

The extent to which physical controls intended to prevent theft of assets are relevant to the reliability of financial statement preparation depends on circumstances such as when assets are highly susceptible to misappropriation.

- *Segregation of duties.* Assigning different people the responsibilities of ~~authorizing~~authorising transactions, recording transactions, and maintaining custody of assets. Segregation of duties is intended to reduce the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of the person's duties.

For example, a manager ~~authorizing~~authorising credit sales is not responsible for maintaining accounts receivable records or handling cash receipts. If one person is able to perform all these activities he or she could, for example, create a fictitious sale that could go undetected. Similarly, salespersons should not have the ability to modify product price files or commission rates.

Sometimes segregation is not practical, cost effective, or feasible. For example, smaller and less complex entities may lack sufficient resources to achieve ideal segregation, and the cost of hiring additional staff may be prohibitive. In these situations, management may institute alternative controls. In the example above, if the salesperson can modify product price files, a detective control activity can be put in place to have personnel unrelated to the sales function periodically review whether and under what circumstances the salesperson changed prices.

21. Certain controls may depend on the existence of appropriate supervisory controls established by management or those charged with governance. For example, ~~authorization~~authorisation controls may be delegated under established guidelines, such as investment criteria set by those charged with governance; alternatively, non-routine transactions such as major acquisitions or divestments may require specific high-level approval, including in some cases that of shareholders.

### Limitations of Internal Control

22. The entity's system of internal control, no matter how effective, can provide an entity with only reasonable assurance about achieving the entity's financial reporting objectives. The likelihood of their achievement is affected by the inherent limitations of internal control. These include the realities that human ~~judgment~~judgement in decision-making can be faulty

and that breakdowns in the entity's system of internal control can occur because of human error. For example, there may be an error in the design of, or in the change to, a control. Equally, the operation of a control may not be effective, such as where information produced for the purposes of the entity's system of internal control (for example, an exception report) is not effectively used because the individual responsible for reviewing the information does not understand its purpose or fails to take appropriate action.

23. Additionally, controls can be circumvented by the collusion of two or more people or inappropriate management override of controls. For example, management may enter into side agreements with customers that alter the terms and conditions of the entity's standard sales contracts, which may result in improper revenue recognition. Also, edit checks in an IT application that are designed to identify and report transactions that exceed specified credit limits may be overridden or disabled.
24. Further, in designing and implementing controls, management may make ~~judgments~~judgements on the nature and extent of the controls it chooses to implement, and the nature and extent of the risks it chooses to assume.

## Considerations for Understanding an Entity's Internal Audit Function

This appendix provides further considerations relating to understanding the entity's internal audit function when such a function exists.

### Objectives and Scope of the Internal Audit Function

1. The objectives and scope of an internal audit function, the nature of its responsibilities and its status within the ~~organization~~organisation, including the function's authority and accountability, vary widely and depend on the size, complexity and structure of the entity and the requirements of management and, where applicable, those charged with governance. These matters may be set out in an internal audit charter or terms of reference.
2. The responsibilities of an internal audit function may include performing procedures and evaluating the results to provide assurance to management and those charged with governance regarding the design and effectiveness of risk management, the entity's system of internal control and governance processes. If so, the internal audit function may play an important role in the entity's process to monitor the entity's system of internal control. However, the responsibilities of the internal audit function may be focused on evaluating the economy, efficiency and effectiveness of operations and, if so, the work of the function may not directly relate to the entity's financial reporting.

### ~~Inquiries~~Enquiries of the Internal Audit Function

3. If an entity has an internal audit function, ~~inquiries~~enquiries of the appropriate individuals within the function may provide information that is useful to the auditor in obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control, and in identifying and assessing risks of material misstatement at the financial statement and assertion levels. In performing its work, the internal audit function is likely to have obtained insight into the entity's operations and business risks, and may have findings based on its work, such as identified control deficiencies or risks, that may provide valuable input into the auditor's understanding of the entity and its environment, the applicable financial reporting framework, the entity's system of internal control, the auditor's risk assessments or other aspects of the audit. The auditor's ~~inquiries~~enquiries are therefore made whether or not the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed.<sup>73</sup> ~~inquiries~~Enquiries of particular relevance may be about matters the internal audit function has raised with those charged with governance and the outcomes of the function's own risk assessment process.

<sup>73</sup> The relevant requirements are contained in ISA- (NZ) 610 (Revised 2013).

4. If, based on responses to the auditor's ~~inquiries~~~~enquiries~~, it appears that there are findings that may be relevant to the entity's financial reporting and the audit of the financial statements, the auditor may consider it appropriate to read related reports of the internal audit function. Examples of reports of the internal audit function that may be relevant include the function's strategy and planning documents and reports that have been prepared for management or those charged with governance describing the findings of the internal audit function's examinations.
5. In addition, in accordance with ISA- (NZ) 240,<sup>74</sup> if the internal audit function provides information to the auditor regarding any actual, suspected or alleged fraud, the auditor takes this into account in the auditor's identification of risk of material misstatement due to fraud.
6. Appropriate individuals within the internal audit function with whom ~~inquiries~~~~enquiries~~ are made are those who, in the auditor's ~~judgment~~~~judgement~~, have the appropriate knowledge, experience and authority, such as the chief internal audit executive or, depending on the circumstances, other personnel within the function. The auditor may also consider it appropriate to have periodic meetings with these individuals.

### **Consideration of the Internal Audit Function in Understanding the Control Environment**

7. In understanding the control environment, the auditor may consider how management has responded to the findings and recommendations of the internal audit function regarding identified control deficiencies relevant to the preparation of the financial statements, including whether and how such responses have been implemented, and whether they have been subsequently evaluated by the internal audit function.

### **Understanding the Role that the Internal Audit Function Plays in the Entity's Process to Monitor the System of Internal Control**

8. If the nature of the internal audit function's responsibilities and assurance activities are related to the entity's financial reporting, the auditor may also be able to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed directly by the auditor in obtaining audit evidence. Auditors may be more likely to be able to use the work of an entity's internal audit function when it appears, for example, based on experience in previous audits or the auditor's risk assessment procedures, that the entity has an internal audit function that is adequately and appropriately resourced relative to the complexity of the entity and the nature of its operations, and has a direct reporting relationship to those charged with governance.
9. If, based on the auditor's preliminary understanding of the internal audit function, the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed, ISA- (NZ) 610 (Revised ~~2013~~) applies.

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<sup>74</sup> ISA- (NZ) 240, paragraph 20

10. As is further discussed in ISA- (NZ) 610 (Revised ~~2013~~), the activities of an internal audit function are distinct from other monitoring controls that may be relevant to financial reporting, such as reviews of management accounting information that are designed to contribute to how the entity prevents or detects misstatements.
11. Establishing communications with the appropriate individuals within an entity's internal audit function early in the engagement, and maintaining such communications throughout the engagement, can facilitate effective sharing of information. It creates an environment in which the auditor can be informed of significant matters that may come to the attention of the internal audit function when such matters may affect the work of the auditor. ISA- (NZ) 200 discusses the importance of the auditor planning and performing the audit with professional ~~skepticism~~scepticism, including being alert to information that brings into question the reliability of documents and responses to ~~inquiries~~enquiries to be used as audit evidence. Accordingly, communication with the internal audit function throughout the engagement may provide opportunities for internal auditors to bring such information to the auditor's attention. The auditor is then able to take such information into account in the auditor's identification and assessment of risks of material misstatement.

**Appendix 5**

(Ref: Para. 25(a), 26(b)–(c), A94, A166–A172)

**Considerations for Understanding Information Technology (IT)**

This appendix provides further matters that the auditor may consider in understanding the entity's use of IT in its system of internal control.

**Understanding the Entity's Use of Information Technology in the Components of the Entity's System of Internal Control**

1. An entity's system of internal control contains manual elements and automated elements (i.e., manual and automated controls and other resources used in the entity's system of internal control). An entity's mix of manual and automated elements varies with the nature and complexity of the entity's use of IT. An entity's use of IT affects the manner in which the information relevant to the preparation of the financial statements in accordance with the applicable financial reporting framework is processed, stored and communicated, and therefore affects the manner in which the entity's system of internal control is designed and implemented. Each component of the entity's system of internal control may use some extent of IT.

Generally, IT benefits an entity's system of internal control by enabling an entity to:

- Consistently apply predefined business rules and perform complex calculations in processing large volumes of transactions or data;
  - Enhance the timeliness, availability, and accuracy of information;
  - Facilitate the additional analysis of information;
  - Enhance the ability to monitor the performance of the entity's activities and its policies and procedures;
  - Reduce the risk that controls will be circumvented; and
  - Enhance the ability to achieve effective segregation of duties by implementing security controls in IT applications, databases, and operating systems.
2. The characteristics of manual or automated elements are relevant to the auditor's identification and assessment of the risks of material misstatement, and further audit procedures based thereon. Automated controls may be more reliable than manual controls because they cannot be as easily bypassed, ignored, or overridden, and they are also less prone to simple errors and mistakes. Automated controls may be more effective than manual controls in the following circumstances:
    - High volume of recurring transactions, or in situations where errors that can be anticipated or predicted can be prevented, or detected and corrected, through automation

- Controls where the specific ways to perform the control can be adequately designed and automated.

*Understanding the Entity's Use of Information Technology in the Information System* (Ref: Para. 25(a))

- The entity's information system may include the use of manual and automated elements, which also affect the manner in which transactions are initiated, recorded, processed, and reported. In particular, procedures to initiate, record, process, and report transactions may be enforced through the IT applications used by the entity, and how the entity has configured those applications. In addition, records in the form of digital information may replace or supplement records in the form of paper documents.
- In obtaining an understanding of the IT environment relevant to the flows of transactions and information processing in the information system, the auditor gathers information about the nature and characteristics of the IT applications used, as well as the supporting IT infrastructure and IT. The following table includes examples of matters that the auditor may consider in obtaining the understanding of the IT environment and includes examples of typical characteristics of IT environments based on the complexity of IT applications used in the entity's information system. However, such characteristics are directional and may differ depending on the nature of the specific IT applications in use by an entity.

|   | Examples of typical characteristics of: |  |  |
|---|---|--|--|
|   | Non-complex commercial software         | Mid-size and moderately complex commercial software or IT applications | Large or complex applications or systems             |
| Matters related to extent of automation and use of data:  |   |  |  |
| <ul style="list-style-type: none"> <li>The extent of automated procedures for processing, and the complexity of those procedures, including, whether there is highly automated, paperless processing</li> </ul> | N/A                                     | N/A  | Extensive and complex automated procedures           |
| <ul style="list-style-type: none"> <li>The extent of the entity's reliance on system-generated reports in the processing of information.</li> </ul>   | Simple automated report logic           | Simple relevant automated report logic                                 | Complex automated report logic; Reliance on software |

|   |   |   |  |
|---|---|---|--|
| <ul style="list-style-type: none"> <li>How data is input (i.e., manual input, customer or vendor input, or file load).</li> </ul>   | Manual data inputs  | Small number of data inputs or simple interfaces  | Large number of data inputs or complex interfaces  |
| <ul style="list-style-type: none"> <li>How IT facilitates communication between applications, databases or other aspects of the IT environment, internally and externally, as appropriate, through system interfaces.</li> </ul>                                      | No automated interfaces (manual inputs only)  | Small number of data inputs or simple interfaces  | Large number of data inputs or complex interfaces  |
| <ul style="list-style-type: none"> <li>The volume and complexity of data in digital form being processed by the information system, including whether accounting records or other information are stored in digital form and the location of stored data.</li> </ul>  | Low volume of data or simple data that is able to be verified manually;<br>Data available locally | Low volume of data or simple data   | Large volume of data or complex data; data stored in data warehouses, internal or external, or service providers; third-party service providers hosting or processing data |
| Matters related to the IT applications and IT infrastructure:   |   |   |  |
| <ul style="list-style-type: none"> <li>The type of application (e.g., a commercial application with little or no <del>customization</del>customisation, or a highly-customizedcustomised or highly-integrated application that may have been purchased and</li> </ul> | Purchased application with little or no <del>customization</del> customisation                    | Purchased application or simple legacy or low-end ERP applications with little or no <del>customization</del> customisation | Custom developed applications; complex ERP applications with significant <del>customization</del> customisation  |

<sup>75</sup> A data warehouse is generally described as a central repository of integrated data from one or more disparate sources (such as multiple databases) from which reports may be generated or that may be used by the entity for other data analysis activities. A report-writer is an IT application that is used to extract data from one or more sources (such as a data warehouse, a database or an IT application) and present the data in a specified format.



|  |  |   |   |
|--|--|---|---|
| customized or developed in-house).   |  |   |   |
| <ul style="list-style-type: none"> <li>The complexity of the nature of the IT applications and the underlying IT infrastructure.</li> </ul>  | Small, simple laptop or client server-based solution                                 | Mature and stable mainframe, small or simple client server, software as a service cloud | Complex mainframe, large or complex client server, web-based applications, infrastructure cloud     |
| <ul style="list-style-type: none"> <li>Whether there is third-party hosting or outsourcing of IT.</li> </ul>   | If outsourced, competent, mature, proven provider (e.g., cloud provider)             | If outsourced, competent, mature, proven provider (e.g. cloud provider)                 | Competent, mature, proven provider for certain applications, new or start-up for other applications |
| <ul style="list-style-type: none"> <li>Whether the entity is using emerging technologies that affect its financial reporting.</li> </ul>   | No use of emerging technologies  | Limited use of emerging technologies in some applications                               | Mixed use of emerging technologies in some applications   |
| Matters related to IT processes:   |  |   |   |
| <ul style="list-style-type: none"> <li>The personnel involved in maintaining the IT environment (the number and skill level of the IT support resources that manage security and changes to the IT environment)</li> </ul>   | Few personnel with limited IT knowledge to process vendor upgrades and manage access | Limited personnel with IT skills / dedicated to IT                                      | Dedicated IT personnel with skilled personnel including professional skills                         |
| <ul style="list-style-type: none"> <li>The complexity of processes to manage access rights</li> </ul>  | Single individual with administrative access manages access rights                   | Few individuals with administrative access manages access rights                        | Complex processes managed by multiple individuals in department with access rights                  |
| <ul style="list-style-type: none"> <li>The complexity of the security over the IT environment, including vulnerability of the IT applications, databases, and other aspects of the IT environment to cyber risks, particularly when there are web-based</li> </ul> | Simple on-premise access with no external web-facing elements;                       | Some web-based applications with primarily simple, role-based security                  | Multiple platforms, web-based applications with complex security                                    |

|  |  |   |   |
|--|--|---|---|
| transactions or transactions involving external interfaces.  |  |   |   |
| <ul style="list-style-type: none"> <li>Whether program changes have been made to the manner in which information is processed, and the extent of such changes during the period.</li> </ul>                                  | Commercial software with no source code installed                              | Some commercial applications with no source code and other mature applications with a small number or simple changes; traditional systems development lifecycle | New or large complex change, development over a year                      |
| <ul style="list-style-type: none"> <li>The extent of change within the IT environment (e.g., new aspects of the IT environment or significant changes in the IT applications or the underlying IT infrastructure)</li> </ul> | Changes limited to version upgrades of commercial software                     | Changes consist of commercial software upgrades, ERP version upgrades, or legacy enhancements   | New or large complex change, development over a year, heavy customization |
| <ul style="list-style-type: none"> <li>Whether there was a major data conversion during the period and, if so, the nature and significance of the changes made, and how the conversion was undertaken.</li> </ul>            | Software upgrades provided by vendor. No data conversion features for upgrade. | Minor version upgrades for commercial software applications with limited data being converted   | Major version new release, change   |

### *Emerging Technologies*

- Entities may use emerging technologies (e.g., blockchain, robotics or artificial intelligence) because such technologies may present specific opportunities to increase operational efficiencies or enhance financial reporting. When emerging technologies are used in the entity's information system relevant to the preparation of the financial statements, the auditor may include such technologies in the identification of IT applications and other aspects of the IT environment that are subject to risks arising from the use of IT. While emerging technologies may be seen to be more sophisticated or more complex compared to existing

technologies, the auditor's responsibilities in relation to IT applications and identified general IT controls in accordance with paragraph 26(b)–(c) remain unchanged.

### *Scalability*

6. Obtaining an understanding of the entity's IT environment may be more easily accomplished for a less complex entity that uses commercial software and when the entity does not have access to the source code to make any program changes. Such entities may not have dedicated IT resources but may have a person assigned in an administrator role for the purpose of granting employee access or installing vendor-provided updates to the IT applications. Specific matters that the auditor may consider in understanding the nature of a commercial accounting software package, which may be the single IT application used by a less complex entity in its information system, may include:
  - The extent to which the software is well established and has a reputation for reliability;
  - The extent to which it is possible for the entity to modify the source code of the software to include additional modules (i.e., add-ons) to the base software, or to make direct changes to data;
  - The nature and extent of modifications that have been made to the software. Although an entity may not be able to modify the source code of the software, many software packages allow for configuration (e.g., setting or amending reporting parameters). These do not usually involve modifications to source code; however, the auditor may consider the extent to which the entity is able to configure the software when considering the completeness and accuracy of information produced by the software that is used as audit evidence; and
  - The extent to which data related to the preparation of the financial statements can be directly accessed (i.e., direct access to the database without using the IT application) and the volume of data that is processed. The greater the volume of data, the more likely the entity may need controls that address maintaining the integrity of the data, which may include general IT controls over ~~unauthorized~~unauthorised access and changes to the data.
7. Complex IT environments may include highly-~~customized~~customised or highly-integrated IT applications and may therefore require more effort to understand. Financial reporting processes or IT applications may be integrated with other IT applications. Such integration may involve IT applications that are used in the entity's business operations and that provide information to the IT applications relevant to the flows of transactions and information processing in the entity's information system. In such circumstances, certain IT applications used in the entity's business operations may also be relevant to the preparation of the financial statements. Complex IT environments also may require dedicated IT departments that have structured IT processes supported by personnel that have software development and IT environment maintenance skills. In other cases, an entity may use internal or external

service providers to manage certain aspects of, or IT processes within, its IT environment (e.g., third-party hosting).

#### Identifying IT Applications that are Subject to Risks Arising from the use of IT

8. Through understanding the nature and complexity of the entity's IT environment, including the nature and extent of information processing controls, the auditor may determine which IT applications the entity is relying upon to accurately process and maintain the integrity of financial information. The identification of IT applications on which the entity relies, may affect the auditor's decision to test the automated controls within such IT applications, assuming that such automated controls address identified risks of material misstatement. Conversely, if the entity is not relying on an IT application, the automated controls within such IT application are unlikely to be appropriate or sufficiently precise for purposes of operating effectiveness tests. Automated controls that may be identified in accordance with paragraph 26(b) may include, for example, automated calculations or input, processing and output controls, such as a three-way match of a purchase order, vendor shipping document, and vendor invoice. When automated controls are identified by the auditor and the auditor determines through the understanding of the IT environment that the entity is relying on the IT application that includes those automated controls, it may be more likely for the auditor to identify the IT application as one that is subject to risks arising from the use of IT.
9. In considering whether the IT applications for which the auditor has identified automated controls are subject to risks arising from the use of IT, the auditor is likely to consider whether, and the extent to which, the entity may have access to source code that enables management to make program changes to such controls or the IT applications. The extent to which the entity makes program or configuration changes and the extent to which the IT processes over such changes are ~~formalized~~formalised may also be relevant considerations. The auditor is also likely to consider the risk of inappropriate access or changes to data.
10. System-generated reports that the auditor may intend to use as audit evidence may include, for example, a trade receivable aging report or an inventory valuation report. For such reports, the auditor may obtain audit evidence about the completeness and accuracy of the reports by substantively testing the inputs and outputs of the report. In other cases, the auditor may plan to test the operating effectiveness of the controls over the preparation and maintenance of the report, in which case the IT application from which it is produced is likely to be subject to risks arising from the use of IT. In addition to testing the completeness and accuracy of the report, the auditor may plan to test the operating effectiveness of general IT controls that address risks related to inappropriate or ~~unauthorized~~unauthorised program changes to, or data changes in, the report.
11. Some IT applications may include report-writing functionality within them while some entities may also ~~utilize~~utilise separate report-writing applications (i.e., report-writers). In such cases, the auditor may need to determine the sources of system-generated reports (i.e., the application that prepares the report and the data sources used by the report) to determine the IT applications subject to risks arising from the use of IT.

12. The data sources used by IT applications may be databases that, for example, can only be accessed through the IT application or by IT personnel with database administration privileges. In other cases, the data source may be a data warehouse that may itself be considered to be an IT application subject to risks arising from the use of IT.
13. The auditor may have identified a risk for which substantive procedures alone are not sufficient because of the entity's use of highly-automated and paperless processing of transactions, which may involve multiple integrated IT applications. In such circumstances, the controls identified by the auditor are likely to include automated controls. Further, the entity may be relying on general IT controls to maintain the integrity of the transactions processed and other information used in processing. In such cases, the IT applications involved in the processing and the storage of the information are likely subject to risks arising from the use of IT.

#### *End-User Computing*

14. Although audit evidence may also come in the form of system-generated output that is used in a calculation performed in an end-user computing tool (e.g., spreadsheet software or simple databases), such tools are not typically identified as IT applications in the context of paragraph 26(b). Designing and implementing controls around access and change to end-user computing tools may be challenging, and such controls are rarely equivalent to, or as effective as, general IT controls. Rather, the auditor may consider a combination of information processing controls, taking into account the purpose and complexity of the end-user computing involved, such as:
  - Information processing controls over the initiation and processing of the source data, including relevant automated or interface controls to the point from which the data is extracted (i.e. the data warehouse);
  - Controls to check that the logic is functioning as intended, for example, controls which 'prove' the extraction of data, such as reconciling the report to the data from which it was derived, comparing the individual data from the report to the source and vice versa, and controls which check the formulas or macros; or
  - Use of validation software tools, which systematically check formulas or macros, such as spreadsheet integrity tools.

#### **Scalability**

15. The entity's ability to maintain the integrity of information stored and processed in the information system may vary based on the complexity and volume of the related transactions and other information. The greater the complexity and volume of data that supports a significant class of transactions, account balance or disclosure, the less likely it may become for the entity to maintain integrity of that information through information processing controls alone (e.g., input and output controls or review controls). It also becomes less likely that the auditor will be able to obtain audit evidence about the completeness and accuracy of

such information through substantive testing alone when such information is used as audit evidence. In some circumstances, when volume and complexity of transactions are lower, management may have an information processing control that is sufficient to verify the accuracy and completeness of the data (e.g., individual sales orders processed and billed may be reconciled to the hard copy originally entered into the IT application). When the entity relies on general IT controls to maintain the integrity of certain information used by IT applications, the auditor may determine that the IT applications that maintain that information are subject to risks arising from the use of IT.

| Example characteristics of an IT application that is likely not subject to risks arising from IT   | Example characteristics of an IT application that is likely subject to risks arising from IT  |
|--|---|
| <ul style="list-style-type: none"> <li>• Standalone applications</li> <li>• The volume of data (transactions) is not significant.</li> <li>• The application's functionality is not complex.</li> <li>• Each transaction is supported by original hard copy documentation.</li> </ul>  | <ul style="list-style-type: none"> <li>• Applications are interfaced.</li> <li>• The volume of data (transactions) is significant/</li> <li>• The application's functionality is complex as <ul style="list-style-type: none"> <li>– The application automatically initiates transactions; and</li> <li>–</li> <li>– There are a variety of complex calculations underlying automated entries.</li> </ul> </li> </ul> |
| <p>IT application is likely not subject to risks arising from IT because:</p> <ul style="list-style-type: none"> <li>• The volume of data is not significant and therefore management is not relying upon general IT controls to process or maintain the data.</li> <li>• Management does not rely on automated controls or other automated functionality. The auditor has not identified automated controls in accordance with paragraph 26(a).</li> <li>• Although management uses system-generated reports in their controls, they do not rely on these reports. Instead, they reconcile the reports back to the</li> </ul> | <p>IT application is likely subject to risks arising from IT because:</p> <ul style="list-style-type: none"> <li>• Management relies on an application system to process or maintain data as the volume of data is significant.</li> <li>• Management relies upon the application system to perform certain automated controls that the auditor has also identified.</li> </ul>                                       |

|  |  |
|--|--|
| <p>hard copy documentation and verify the calculations in the reports.</p> <ul style="list-style-type: none"> <li>• The auditor will directly test information produced by the entity used as audit evidence.</li> </ul> |  |
|--|--|

*Other Aspects of the IT Environment that Are Subject to Risks Arising from the Use of IT*

16. When the auditor identifies IT applications that are subject to risks arising from the use of IT, other aspects of the IT environment are also typically subject to risks arising from the use of IT. The IT infrastructure includes the databases, operating system, and network. Databases store the data used by IT applications and may consist of many interrelated data tables. Data in databases may also be accessed directly through database management systems by IT or other personnel with database administration privileges. The operating system is responsible for managing communications between hardware, IT applications, and other software used in the network. As such, IT applications and databases may be directly accessed through the operating system. A network is used in the IT infrastructure to transmit data and to share information, resources and services through a common communications link. The network also typically establishes a layer of logical security (enabled through the operating system) for access to the underlying resources.
17. When IT applications are identified by the auditor to be subject to risks arising from IT, the database(s) that stores the data processed by an identified IT application is typically also identified. Similarly, because an IT application's ability to operate is often dependent on the operating system and IT applications and databases may be directly accessed from the operating system, the operating system is typically subject to risks arising from the use of IT. The network may be identified when it is a central point of access to the identified IT applications and related databases or when an IT application interacts with vendors or external parties through the internet, or when web-facing IT applications are identified by the auditor.

*Identifying Risks arising from the Use of IT and General IT Controls*

18. Examples of risks arising from the use of IT include risks related to inappropriate reliance on IT applications that are inaccurately processing data, processing inaccurate data, or both, such as
  - ~~Unauthorized~~Unauthorised access to data that may result in destruction of data or improper changes to data, including the recording of ~~unauthorized~~unauthorised or non-existent transactions, or inaccurate recording of transactions. Particular risks may arise where multiple users access a common database.
  - The possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties thereby breaking down segregation of duties.



- ~~Unauthorized~~Unauthorised changes to data in master files.
  - ~~Unauthorized~~Unauthorised changes to IT applications or other aspects of the IT environment.
  - Failure to make necessary changes to IT applications or other aspects of the IT environment.
  - Inappropriate manual intervention.
  - Potential loss of data or inability to access data as required.
19. The auditor's consideration of ~~unauthorized~~unauthorised access may include risks related to ~~unauthorized~~unauthorised access by internal or external parties (often referred to as cybersecurity risks). Such risks may not necessarily affect financial reporting, as an entity's IT environment may also include IT applications and related data that address operational or compliance needs. It is important to note that cyber incidents usually first occur through the perimeter and internal network layers, which tend to be further removed from the IT application, database and operating systems that affect the preparation of the financial statements. Accordingly, if information about a security breach has been identified, the auditor ordinarily considers the extent to which such a breach had the potential to affects financial reporting. If financial reporting may be affected, the auditor may decide to understand, and test the related controls to determine the possible impact or scope of potential misstatements in the financial statements or may determine that the entity has provided adequate disclosures in relation to such security breach.
20. In addition, laws and regulations that may have a direct or indirect effect on the entity's financial statements may include data protection legislation. Considering an entity's compliance with such laws or regulations, in accordance with ISA- (NZ) 250 (Revised),<sup>76</sup> may involve understanding the entity's IT processes and general IT controls that the entity has implemented to address the relevant laws or regulations.
21. General IT controls are implemented to address risks arising from the use of IT. Accordingly, the auditor uses the understanding obtained about the identified IT applications and other aspects of the IT environment and the applicable risks arising from the use of IT in determining the general IT controls to identify. In some cases, an entity may use common IT processes across its IT environment or across certain IT applications, in which case common risks arising from the use of IT and common general IT controls may be identified.
22. In general, a greater number of general IT controls related to IT applications and databases are likely to be identified than for other aspects of the IT environment. This is because these aspects are the most closely concerned with the information processing and storage of information in the entity's information system. In identifying general IT controls, the auditor

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<sup>76</sup> ISA- (NZ) 250 (Revised)



may consider controls over actions of both end users and of the entity's IT personnel or IT service providers.

23. Appendix 6 provides further explanation of the nature of the general IT controls typically implemented for different aspects of the IT environment. In addition, examples of general IT controls for different IT processes are provided.

## Appendix 6

(Ref: Para. 25(c)(ii), A173–A174)

**Considerations for Understanding General IT Controls**

This appendix provides further matters that the auditor may consider in understanding general IT controls.

1. The nature of the general IT controls typically implemented for each of the aspects of the IT environment

- (a) Applications

General IT controls at the IT application layer will correlate to the nature and extent of application functionality and the access paths allowed in the technology. For example, more controls will be relevant for highly-integrated IT applications with complex security options than a legacy IT application supporting a small number of account balances with access methods only through transactions.

- (b) Database

General IT controls at the database layer typically address risks arising from the use of IT related to ~~unauthorized~~unauthorised updates to financial reporting information in the database through direct database access or execution of a script or program.

- (c) Operating system

General IT controls at the operating system layer typically address risks arising from the use of IT related to administrative access, which can facilitate the override of other controls. This includes actions such as compromising other user's credentials, adding new, ~~unauthorized~~unauthorised users, loading malware or executing scripts or other ~~unauthorized~~unauthorised programs.

- (d) Network

General IT controls at the network layer typically address risks arising from the use of IT related to network segmentation, remote access, and authentication. Network controls may be relevant when an entity has web-facing applications used in financial reporting. Network controls are also may be relevant when the entity has significant business partner relationships or third-party outsourcing, which may increase data transmissions and the need for remote access.

2. Examples of general IT controls that may exist, ~~organized~~organised by IT process include:

- (a) Process to manage access:

- Authentication

Controls that ensure a user accessing the IT application or other aspect of the IT environment is using their own log-in credentials (i.e., the user is not using another user's credentials).

○ ~~Authorization~~

○ Authorisation

Controls that allow users to access the information necessary for their job responsibilities and nothing further, which facilitates appropriate segregation of duties.

○ *Provisioning*

Controls to ~~authorize~~authorise new users and modifications to existing users' access privileges.

○ *Deprovisioning*

Controls to remove user access upon termination or transfer.

○ *Privileged access*

Controls over administrative or powerful users' access.

○ *User access reviews*

Controls to recertify or evaluate user access for ongoing ~~authorization~~authorisation over time.

○ *Security configuration controls*

Each technology generally has key configuration settings that help restrict access to the environment.

○ *Physical access*

Controls over physical access to the data center and hardware, as such access may be used to override other controls.

(b) Process to manage program or other changes to the IT environment

○ *Change management process*

Controls over the process to design, program, test and migrate changes to a production (i.e., end user) environment.

○ *Segregation of duties over change migration*

Controls that segregate access to make and migrate changes to a production environment.

○ *Systems development or acquisition or implementation*

Controls over initial IT application development or implementation (or in relation to other aspects of the IT environment).

- *Data conversion*

Controls over the conversion of data during development, implementation or upgrades to the IT environment.

(c) Process to manage IT Operations

- *Job scheduling*

Controls over access to schedule and initiate jobs or programs that may affect financial reporting.

- *Job monitoring*

Controls to monitor financial reporting jobs or programs for successful execution.

- *Backup and recovery*

Controls to ensure backups of financial reporting data occur as planned and that such data is available and able to be accessed for timely recovery in the event of an outage or attack.

- *Intrusion detection*

Controls to monitor for vulnerabilities and or intrusions in the IT environment.

The table below illustrates examples of general IT controls to address examples of risks arising from the use of IT, including for different IT applications based on their nature.

| Process       | Risks  | Controls   | IT Applications   |  |  |
|---------------|--|--|---|--|--|
| IT Process    | Example Risks Arising from the Use of IT                                       | Example General IT Controls                              | Non-complex commercial software – Applicable (yes / no) | Mid-size and moderately complex commercial software or IT applications – Applicable (yes / no) | Large or complex IT applications (e.g., ERP systems) – Applicable (yes / no) |
| Manage Access | User-access privileges: Users have access privileges beyond those necessary to | Management approves the nature and extent of user-access | Yes – instead of user access reviews                    | Yes  | Yes  |

|  |   |   |   |                              |     |
|--|---|---|---|------------------------------|-----|
|  | perform their assigned duties, which may create improper segregation of duties. | privileges for new and modified user access, including standard application profiles/roles, critical financial reporting transactions, and segregation of duties. | noted below   |                              |     |
|  |   | Access for terminated or transferred users is removed or modified in a timely manner.   | Yes – instead of user access reviews below                      | Yes                          | Yes |
|  |   | User access is periodically reviewed.   | Yes – instead of provisioning/<br>Deprovisioning controls above | Yes for certain applications | Yes |
|  |   | Segregation of duties is monitored and conflicting access is either removed or mapped to mitigating controls, which are   | N/A – no system enabled segregation                             | Yes for certain applications | Yes |

|               |  |   |   |   |  |
|---------------|--|---|---|---|--|
|               |  | documented and tested.  |   |   |  |
|               |  | Privileged-level access (e.g., configuration, data and security administrators) is <del>authorized</del> <u>authorised</u> and appropriately restricted.  | Yes – likely at IT application layer only | Yes at IT application and certain layers of IT environment for platform | Yes at all layers of IT environment for platform |
| Manage Access | Direct data access: Inappropriate changes are made directly to financial data through means other than application transactions.                                       | Access to application data files or database objects/tables/data is limited to <del>authorized</del> <u>authorised</u> personnel, based on their job responsibilities and assigned role, and such access is approved by management. | N/A                                       | Yes for certain applications and databases                              | Yes  |
| Manage Access | System settings: Systems are not adequately configured or updated to restrict system access to properly <del>authorized</del> <u>authorised</u> and appropriate users. | Access is authenticated through unique user IDs and passwords or other methods as a mechanism for validating that users are <del>authorized</del> <u>authorised</u> to gain   | Yes – password authentication only        | Yes – mix of password and multi-factor authentication                   | Yes  |

|               |   |  |  |  |     |
|---------------|---|--|--|--|-----|
|               |   | access to the system.<br>Password parameters meet company or industry standards (e.g., password minimum length and complexity, expiration, account lockout). |  |  |     |
|               |   | The key attributes of the security configuration are appropriately implemented.  | N/A – no technical security configurations exist | Yes for certain applications and databases | Yes |
| Manage Change | Application changes:<br>Inappropriate changes are made to application systems or programs that contain relevant automated controls (i.e., configurable settings, automated algorithms, automated calculations, and automated extraction) or report logic. | Application changes are appropriately tested and approved before being moved into the production environment.  | N/A-would verify no source code installed        | Yes for non-commercial software            | Yes |
|               |   | Access to implement changes into the application production environment is appropriately restricted and segregated from the                                  | N/A  | Yes for non-commercial software            | Yes |

|               |  |   |   |                                 |     |
|---------------|--|---|---|---------------------------------|-----|
|               |  | development environment.  |   |                                 |     |
| Manage Change | Database changes: Inappropriate changes are made to the database structure and relationships between the data.   | Database changes are appropriately tested and approved before being moved into the production environment.  | N/A – no database changes made at entity            | Yes for non-commercial software | Yes |
| Manage Change | System software changes: Inappropriate changes are made to system software (e.g., operating system, network, change-management software, access-control software).               | System software changes are appropriately tested and approved before being moved to production.   | N/A – no system software changes are made at entity | Yes                             | Yes |
| Manage Change | Data conversion: Data converted from legacy systems or previous versions introduces data errors if the conversion transfers incomplete, redundant, obsolete, or inaccurate data. | Management approves the results of the conversion of data (e.g., balancing and reconciliation activities) from the old application system or data structure to the new application system or data structure and monitors that | N/A – Addressed through manual controls             | Yes                             | Yes |



|               |   |   |  |                     |                     |
|---------------|---|---|--|---------------------|---------------------|
|               |   | the conversion is performed in accordance with established conversion policies and procedures.  |  |                     |                     |
| IT Operations | Network: The network does not adequately prevent unauthorized users from gaining inappropriate access to information systems. | Access is authenticated through unique user IDs and passwords or other methods as a mechanism for validating that users are authorized to gain access to the system. Password parameters meet company or professional policies and standards (e.g., password minimum length and complexity, expiration, account lockout). | N/A – no separate network authentication method exists | Yes                 | Yes                 |
|               |   | Network is architected to segment web-facing applications from the internal   | N/A – no network segmentation employed                 | Yes - with judgment | Yes - with judgment |

|  |  |  |              |                                     |                                     |
|--|--|--|--------------|-------------------------------------|-------------------------------------|
|  |  | network, where ICFR relevant applications are accessed.  |              |                                     |                                     |
|  |  | On a periodic basis, vulnerability scans of the network perimeter are performed by the network management team, which also investigates potential vulnerabilities.                         | N/A          | Yes - with <a href="#">judgment</a> | Yes - with <a href="#">judgment</a> |
|  |  | On a periodic basis, alerts are generated to provide notification of threats identified by the intrusion detection systems. These threats are investigated by the network management team. | N/A          | Yes - with <a href="#">judgment</a> | Yes - with <a href="#">judgment</a> |
|  |  | Controls are implemented to restrict Virtual Private Network (VPN) access to <a href="#">authorized</a>  | N/A – no VPN | Yes - with <a href="#">judgment</a> | Yes - with <a href="#">judgment</a> |

|               |   |   |   |                              |     |
|---------------|---|---|---|------------------------------|-----|
|               |   | <u>orised</u> and appropriate users.  |   |                              |     |
| IT Operations | Data backup and recovery: Financial data cannot be recovered or accessed in a timely manner when there is a loss of data.                       | Financial data is backed up on a regular basis according to an established schedule and frequency.                                      | N/A – relying on manual backups by finance team | Yes                          | Yes |
| IT Operations | Job scheduling: Production systems, programs, or jobs result in inaccurate, incomplete, or <u>unauthorizedunauth orised</u> processing of data. | Only <u>authorizedautho rised</u> users have access to update the batch jobs (including interface jobs) in the job scheduling software. | N/A – no batch jobs                             | Yes for certain applications | Yes |
|               |   | Critical systems, programs, or jobs are monitored, and processing errors are corrected to ensure successful completion.                 | N/A – no job monitoring                         | Yes for certain applications | Yes |

**ACCOMPANYING ATTACHMENT: CONFORMITY TO THE INTERNATIONAL STANDARDS ON AUDITING**

This conformity statement accompanies but is not part of ISA (NZ) 315 (Revised).

**Conformity with International Standards on Auditing**

This International Standard on Auditing (New Zealand) (ISA (NZ)) conforms to International Standard on Auditing (ISA) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*, issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this ISA (NZ) (and do not appear in the text of the equivalent ISA) are identified with the prefix “NZ”.

This ISA (NZ) incorporates terminology and definitions used in New Zealand.

Compliance with this ISA (NZ) enables compliance with ISA 315.

**Comparison with Australian Auditing Standards**

This section will be completed after the AUASB issues its revised standard.

## Memorandum

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**Date:** 13 December 2019

**To:** Michele Embling, Chair XRB Board

**From:** Robert Buchanan, Chairman NZAuASB

**Subject:** Certificate Signing Memo: International Standard on Auditing (New Zealand) ISA (NZ) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement and Conforming and Consequential Amendments Arising from ISA (NZ) 315 (Revised)*

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### Introduction

1. In accordance with the protocols established by the XRB Board, the NZAuASB seeks your approval to issue International Standard on Auditing (New Zealand) (ISA (NZ)) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement and Conforming and Consequential Amendments Arising from ISA (NZ) 315 (Revised)*.

### Background

#### International process

2. The IAASB's Post-Implementation Review of the Clarified International Standards on Auditing<sup>1</sup>, completed in 2013, identified the following issues in relation to the ISA 315 (Revised):
  - Inconsistencies in the number and nature of significant risks being identified;
  - The nature and extent of work to be performed on internal control relevant to the audit, including information technology controls, in particular where information technology systems are complex or the auditor does not intend to rely on controls as part of the audit;
  - Practically identifying risks of material misstatements at the assertion level; and
  - Documentation of risk assessment procedures in identifying and assessing the risk of material misstatement.

In addition, it has been identified from the ISA Implementation Monitoring project and by others, including respondents to the IAASB's Stakeholder Survey on its future strategy and work plan, and NSS, that the requirements and guidance in ISA 315 (Revised) has not

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<sup>1</sup> <https://www.iaasb.org/projects/isa-implementation-monitoring>

been updated for evolving environmental influences (such as changing internal control frameworks and more advanced technology systems being utilized).

3. Consequently, the IAASB consultations in developing its Strategy for 2015-2019<sup>2</sup> and related Work Plan for 2015-2016<sup>3</sup> indicated a need for the International Auditing and Assurance Standards Board (IAASB) to take action to address issues relevant to the application of ISA 315 (Revised).
4. 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 project proposal<sup>4</sup> was presented and approved in the IAASB's September 2016 meeting.
5. The IAASB issued for public comments its exposure draft (ED) of proposed ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*, in July 2018 with comments due on 2 November 2018.
6. The ED required a more robust risk assessment process and intended to achieve the following objectives:
  - Emphasise the complexity and iterative nature of the standard
  - Improve scalability of the standard
  - Modernising and updating the ISA for an evolving business environment
  - Better explain how automated tools and techniques may be used in risk assessment process
  - To provide 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
  - How fraud is considered as part of the risk assessment process
7. The IAASB received seventy-two responses to ED-315 from a broad range of stakeholders. An overarching theme throughout the responses related to the complexity of the proposals, as well as the scalability and proportionality of the proposed standard. There were also many comments related to individual aspects of the proposals, some

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2 [http://www.ifac.org/system/files/publications/files/IAASB-Strategy-2015-2019\\_0.pdf](http://www.ifac.org/system/files/publications/files/IAASB-Strategy-2015-2019_0.pdf)

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

4 [http://www.iaasb.org/system/files/meetings/files/20160912-IAASB\\_CAG\\_Agenda\\_Item\\_D-ISA-315-Revised\\_Cover-final.pdf](http://www.iaasb.org/system/files/meetings/files/20160912-IAASB_CAG_Agenda_Item_D-ISA-315-Revised_Cover-final.pdf)

supporting the specific changes that had been proposed, while other comments highlighted concerns or disagreement.

8. In response to the comments received from all respondents, significant amendments to the ED and related conforming amendments were made. Appendix A includes detailed of changes made. The IAASB determined that the changes to the ED did not meet the requirements for re-exposure.
9. In its September 2019 meeting, the IAASB approved the revisions to ISA 315 (Revised), as well as the related conforming amendments. The revised ISA will be effective for audits of financial statements for periods beginning on or after December 15, 2021. Once the Public Interest Oversight Board's (PIOB) confirmation that due process was followed is received, the IAASB will formally release the standard.

#### **Domestic process and harmonisation with Australia**

10. The NZAuASB sought feedback from constituents on the IAASB's ED through round table discussions held on 6 September 2018 in Auckland and 30 August 2018 in Wellington. Participants at the combined round table discussions represented the following: OAG, CAANZ, FMA, PWC, EY, KPMG, Grant Thornton, Staples Rodway and RSM. No formal submission was received.
11. On 16 August 2018, the NZAuASB jointly hosted a 90-minute webinar with the Australian Auditing and Assurance Standards Board in relation to ED-315. 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.
12. The NZAuASB's submission to the IAASB was prepared based on feedback received from the round table discussions and the Board at its September 2018 meeting.
13. The NZAuASB did not identify any compelling reason amendments, except for one amendment carried forward from the Extant standard<sup>5</sup>, to include in ISA (NZ) 315 (Revised). The usual New Zealand terminology and spelling changes were made to the international standard.

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<sup>5</sup> NZ A1.1 was amended by the NZAuASB to be consistent with changes made by the NZAuASB within ISA (NZ) 580, Written Representations. To remain consistent with the changes previously made in New Zealand to ISA (NZ) 580, the NZAuASB included a reference to management and where relevant those charged with governance when obtaining written representations (paragraph A51 of ISA (NZ) 315).

### **Due process**

14. The due process followed by the NZAuASB complied with the due process requirements established by the XRB Board and in the NZAuASB's view meets the requirements of section 12(b) of the Financial Reporting Act 2013.

### **Consistency with XRB Financial Reporting Strategy**

15. The adoption of International Standard on Auditing (New Zealand) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement and Conforming and Consequential Amendments Arising from ISA (NZ) 315 (Revised)* is consistent with one of the key strategic objectives set by the XRB Board for the NZAuASB to adopt international auditing and assurance standards, as applying in New Zealand unless there are compelling reasons not to.

### **Other matters**

16. There are no other matters relating to the issue of this standard that the NZAuASB considers to be pertinent or that should be drawn to your attention.

### **Recommendation**

17. The NZAuASB recommends that you sign the attached certificate of determination on behalf of the XRB Board.

### **Attachments**

International Standard on Auditing (New Zealand) ISA (NZ) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*

*Conforming and Consequential Amendments Arising from ISA (NZ) 315 (Revised)*

Appendix A: IAASB's significant amendments to the ED

Robert Buchanan

Chair NZAuASB



## NZAuASB Board Meeting Summary Paper

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**AGENDA ITEM NO.** 5.1

**Meeting date:** 5 December 2019

**Subject:** Follow up joint report with the FMA on auditor reporting

**Date:** 20 November 2019

**Prepared by:** Misha Pieters

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☒ **Action Required**

☐ **For Information Purposes Only**

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### Agenda Item Objectives

For the Board to:

- Receive an update on the project to develop a second joint report with the FMA on auditor reporting.
- Based on the update, provide comments to assist in developing the content of the report.

### Background

1. At the October meeting, the Board provided feedback on a project plan and AGREED to target users (investors), preferably by way of interviews or discussions, to obtain views about whether or not the revised auditor's report met the objectives of the IAASB's auditor reporting project.
2. This outreach would be beneficial for building relationships with the users, a key stakeholder group. In addition, feedback will be useful to inform the IAASB's post implementation review of the revised auditor's report.
3. The FMA is responsible to analyse data from the auditors' reports of the following entities:
  - All NZX listed entities for the year-end 30 September 2018 until 30th of June 2019.
  - All registered Banks and Insurance companies' year-ends 31 December 2018 until 30th of September 2019.
  - A couple of industries that have entities with higher public accountability such as Kiwisaver; funds; forestry and Property schemes to understand if there is any theme coming from those reports (approx. 10 for each).
  - 20 large FMC reporting entities with higher public accountability.
4. The XRB is responsible for engaging with stakeholders and developing content to include in the report based on this outreach.
5. We aim to issue the report at the end of February 2020.

### **Update**

6. We have planned two roundtable discussions, one with shareholder association members and a separate discussion with major institutional investors and share brokers. These discussions will occur on November 26<sup>th</sup>. At this stage the expected attendance is low therefore we are likely to obtain views from only a few investors. We have encouraged targeted investors to provide their comments via email if unable to attend the discussions, however, many have indicated that they will not be commenting.
7. We plan to explore the following matters:
  - How often do you refer to the auditor's KAMs?
  - Do you have examples of particularly useful auditor's reports?
  - Has the reporting of KAMs improved the communicative value of the auditor's report?
  - What more could be done to enhance communication and build trust in the audit?
8. We will provide a verbal update of the progress made by the FMA in their analysis work and about the key messages we heard from investors during our outreach at the December meeting.

### **Material Presented**

Agenda item 5.1

Board Meeting Summary Paper

## NZAuASB Board Meeting Summary Paper

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**AGENDA ITEM NO.** 6.1

**Meeting date:** 5 December 2019

**Subject:** ED NZ SRE 2410

**Date:** 22 November 2019

**Prepared by:** Misha Pieters

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☒ **Action Required**

☐ **For Information Purposes Only**

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### Agenda Item Objectives

To:

- Receive an update on the joint sub-committee's discussions on going concern matters;
- Consider other matters raised by the submissions.

### Update on going concern

1. At the October meeting, the Board considered the various views received in respect of the description of the auditor's responsibilities related to going concern.
2. The indicative preference of the NZAuASB after the October discussions was to remain silent in the interim review report on the auditor's responsibilities related to going concern. It was acknowledged however that the AUASB had not yet discussed the remain silent option and that further collaboration and discussion was needed, in recognition of a strong message for the two Boards to align.
3. The NZAuASB recognised concerns that the word "conclude" may be misunderstood as providing positive assurance. While still of the view that "concluding" is technically correct, the NZAuASB recognised that this approach may have unintended consequences. The NZAuASB also recognised concerns that listing procedures is not the same as describing the responsibility (i.e., is incomplete). The Board agreed that neither option identified in the invitation to comment was a workable way forward.
4. The Board reflected on feedback received that highlighted a need to clarify the auditor's responsibilities within the standard. While it was agreed that clarifying these issues is beyond the scope of the current project, it was acknowledged that this lack of clarity is contributing to the difficulty in agreeing the words. To appropriately deal with the issue of the auditor's responsibilities related to going concern, a separate project may need to be agreed to. In the interim, remaining silent may be the most appropriate way forward, within the scope of the current project.

5. As agreed by both Boards, a joint sub-committee was formed and met to discuss a preferred direction of travel in November.
6. The NZAuASB members expressed a preference for the remain silent option. The AUASB members, having been updated on the NZAuASB's discussion, acknowledged that remaining silent may be a way forward, given the constraints of the current project and the technical nature of the matters that contribute to the difficulty of expressing these responsibilities in a way that does not add to the expectation gap. The AUASB members however expressed a desire to further explore words, and one suggestion made during the call was that the need for detailed wording in the report template could be overcome by reference to wording on a website (similar to the option allowed under the auditor reporting model). The AUASB members will be exploring that option further with the staff of both boards. In doing so, it may be necessary to seek consensus on what is the responsibility, as opposed to the procedure, before determining how to describe that responsibility in the report. Should the suggested approach not succeed, and the subcommittee decide on the option of remaining silent, it may be possible to develop a FAQ or Basis for Conclusion as to why the report is silent.
7. Staff and the joint sub-committee members will continue to work together to find a way forward.

#### **Other matters to address**

8. Both Boards received various feedback on matters other than going concern. These fall into the following categories:
  - Non-compliance with laws and regulations – some stakeholders have requested that additional requirements and references be added into the revised standard.
  - Other information – two stakeholders have queried whether the standard should require a separate section on other information.
  - Respondents have queried whether additional requirements related to “adequate disclosures” from ISA 570 should be added. In addition, we want to confirm the logic of the requirements if it is unclear whether the auditor is required to conclude on going concern.
  - Matters arising which are considered to be outside the scope of this project – we seek confirmation, on an exception basis, as to whether of these matters are beyond the scope and therefore no further action has been taken
  - Areas where there are existing differences between NZ SRE 2410 and ASRE 2410. We are not recommending revisiting existing differences and again seek feedback from the NZAuASB on an exception basis as to whether further changes are needed.
  - Editorial – comments and actions are included in a mark up of the standard. We suggest that the Board provide feedback on these and any other editorial type amendments on an exception basis.
9. These issues are explored in more detail in the issues paper in agenda item 6.2 and in the mark-up of the draft revised standard at agenda item 6.3. We also seek feedback on the inclusion of hyperlinks in the final standard to enhance navigation.

#### **Material Presented**

|                 |  |
|-----------------|--|
| Agenda item 6.1 | Board Meeting Summary Paper                    |
| Agenda item 6.2 | Issues paper                                   |
| Agenda item 6.3 | Mark up from the exposure draft of NZ SRE 2410 |

## **NZ SRE 2410 issues paper**

### **Enhancing the usability of the assurance standards**

1. We are exploring new ideas to enhance the navigation and interaction within the standards. We may be able to achieve some “easy wins” within the current functions of Microsoft word and PDF documents.
2. As a first step towards exploring new features, we suggest adding hyperlinks within NZ 2410. If this is successful and is useful to those who access the standards, these simple techniques could be extended to other assurance standards. Given that this is a New Zealand domestic standard (rather than based on an international equivalent) this may be a good test pilot. We will continue to explore other ideas with other standard setters who are similarly looking at innovative ways to enhance interaction with the standards.
3. We have added hyperlinks within the menu and between cross references between requirements and application material. Using Alt +Left Arrow you are able to navigate back to where you came from. A similar technique can be used for defined terms.
4. In investigating this option for defined terms, we identified that the term “interim financial statements” is only used in the illustrations. We wonder if the term “interim financial statements” is the appropriate term to use throughout the requirements that refer to “financial statements”. This may however be beyond the scope of this project. At this stage we have not hyperlinked defined terms to the definition section.

**5. Does the Board have any comments on adding hyperlinks within NZ SRE 2410?**

### **Non-compliance with laws and regulations (NOCLAR)**

6. Two (EY and CAANZ) out of three responses to the NZAuASB agreed with the proposals related to conforming amendments to reflect the new NOCLAR ethical framework.
7. One submission to the NZAuASB from CPA recommended that more is required in NZ SRE 2410 to more fully reflect the revised NOCLAR framework.

“However, we consider that the applicable requirements of the PES 1 (Revised), with respect to NOCLAR, need to be more fully addressed in the revised standard.

Whilst additional requirements for NOCLAR are included in paragraph 31 of the ED, we consider that the following amendments are also needed:

- a) Inclusion of the following requirements under the heading “Enquiries, Analytical and Other Review Procedures”:
  - (i.) the auditor to enquire about whether the entity is aware of any NOCLAR (See ISA (NZ) 250 (revised) paragraph 15), and
  - (ii.) if the auditor becomes aware of an instance of, or suspects, NOCLAR, to obtain an understanding of the nature of the act and the circumstances in which it has occurred, as well as further information to evaluate the possible effect on the financial statements (See ISA (NZ) 250 (revised) paragraph 19).

- b) Amendment of paragraph 31 to better reflect the communications the auditor would need to undertake under PES 1. In particular, rather than requesting “management’s assessment of the effect on the financial statements” (subparagraph 31(b)), we consider there should be a requirement to address the circumstance where management or those charged with governance (TCWG) may be involved in the NOCLAR and consider the need for the auditor to obtain legal advice. (See ISA (NZ) 250 (revised), paragraphs 25).

We support reference to (NZ) 250 (revised) as a source of guidance.”

8. KPMG in Australia noted that 2410 does not appear to cover the extent of the auditor’s obligations covered by ASA 250 or the Code of Ethics, including communication with respect to groups and documentation requirements.

We note that ISA (NZ) 250<sup>1</sup> includes an introductory paragraph to remind (not require) that the auditor may have additional responsibilities in law, regulation or ethical requirements dealing with specific communications with management, those charged with governance or other auditors (e.g. in a group audit situation) and documentation.

In addition, ISA (NZ) 250 includes detailed documentation requirements specific to NOCLAR.

9. GT also commented to the AUASB that 2410 did not appear to address paragraphs 23-25 of ASA 250. These paragraphs deal in detail with communicating and reporting NOCLAR with those charged with governance.
10. Five areas were suggested for consideration, all with reference to ISA (NZ) 250<sup>2</sup>:
- a. To remind the auditor that they may have other ethical responsibilities related to NOCLAR;
  - b. To more fully address the enquiries that are required to be made;
  - c. To more fully address what the auditor is required to do when they become aware of NOCLAR under the heading “enquiries, analytical and other review procedures”; and
  - d. To better reflect the communications that the auditor would need to undertake; and
  - e. To include more explicit documentation requirements related to NOCLAR.
11. ISA (NZ) 250 is an entire standard dedicated to the topic of consideration of laws and regulations. Prior to updating ISA (NZ) 250 for conforming amendments as a result of the new ethical framework, ISA (NZ) 250 included more detailed requirements than NZ SRE 2410 did.
12. The objective in this project was to update NZ SRE 2410 for conforming amendments to be consistent with the new NOCLAR terminology and ensure that there is no inconsistency with the new NOCLAR framework. In developing the proposals to NZ SRE 2410, we considered both ISA (NZ) 250 (Revised) and ISRE (NZ) 2400 (Revised)<sup>3</sup>. We are mindful that the ethical requirements are the same in New Zealand, regardless of whether this is a review or an audit. (This is not the case in Australia or internationally as the NZAuASB agreed to align the framework when finalising PES 1.)
13. It may not be necessary to add additional bulk to NZ SRE 2410, given that the ethical requirements are already covered in both the Code of Ethics and ISA (NZ) 250. If, however the NZAuASB agrees to add additional material on NOCLAR into NZ SRE 2410, we have the following suggestions based on the CPA submission:

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<sup>1</sup> ISA (NZ) 250 Consideration of Laws and Regulations in an Audit of Financial Statements

<sup>2</sup> ISA (NZ) 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

<sup>3</sup> ISRE (NZ) 2400 (Revised), *Review of Historical Financial Statements Performed by an Assurance Practitioner who is Not the Auditor of the Entity*

- a. We do not recommend including a reminder about other ethical requirements in NZ SRE 2410. This would seem out of content in NZ SRE 2410 whereas it is appropriate for a whole standard on the topic of laws and regulations. No such conforming amendment was made to ISRE 2400 by the IAASB.

**Does the Board wish to include a reminder from ISA 250?**

- b. If the Board considers it necessary to be specific about NOCLAR enquiries, (Illustrated below paragraph 21 in agenda item 6.3) we suggest using the language from ISRE 2400 (Revised) to describe the enquiries that shall be made. This language is clearer as to what NOCLAR the enquiries relate to rather than cross referencing to ISA 250 in the requirement.

**Does the Board wish to add a requirement here? If so, comment is sought on the drafting.**

- c. ED NZ SRE 2410 already addressed what the auditor is required to do when they become aware of NOCLAR and required communications under a separate heading “communication” in paragraph 31. This uses the existing structure of 2410. We consider we would be replicating the response to NOCLAR if this was also addressed in the section on “Enquiries, analytical procedures and other review procedures”. The drafting of paragraph 31 aligns with the drafting of ISRE (NZ) 2400 so we consider that the communication section is sufficiently clear.

**Does the Board agree that no further action is required?**

- d. We do not consider that including specific documentation requirements on NOCLAR is appropriate in the context of the high-level documentation requirements in extant NZ SRE 2410. No NOCLAR documentation requirements are included within ISRE 2400. The [Code of Ethics](#) covers the documentation requirements.

**Does the Board wish to include additional documentation requirements?**

## **Other information**

14. Two out of three submissions that commented on the question related to “Other Information” considered that an “Other Information” section would be useful for users. This is not a matter that we explored with users. CAANZ agreed with the proposals not to require the inclusion of a section on “Other Information” based on the rationale in the ITC.

“We are not convinced that there is a compelling argument to not require a section on Other Information in the interim review report. As most interim reports would be published by entities with commentary and other information attached, it would be useful for the user to understand the context of our responsibilities in relation to Other Information in the interim report. However, we agree that it is a pragmatic solution to consider this potential improvement at a later date.” (EY)

“As interim financial statements will typically be published in conjunction with other information, such as the directors’ report, we suggest that it would aid transparency to include a section on other information, when applicable, to clarify what the auditor did in relation to that other information.” (CPA)

15. The rationale for excluding the section on Other Information as articulated in the ITC is as follows:

“The NZAuASB is not proposing to include a section on “Other Information” for interim review engagements. There is less “other information” reported at the interim stage and therefore

there is no need to place additional reporting requirements on the auditor at the interim stage. This may be re-considered after a post implementation review of the reporting requirements has been completed by the IAASB.”

16. **Does the Board agree that inclusion of an “Other Information” section would aid transparency and clarify what the auditor did in relation to Other Information? If so, is this something that should be addressed in finalising NZ SRE 2410 (Revised)?**

**Modified Conclusion: “appropriate disclosures” and appropriateness of going concern**

17. Extant NZ SRE 2410 addresses the following two scenarios related to going concern and significant uncertainties:
- 41. If adequate disclosure is made in the financial statements, the auditor shall add an emphasis of matter paragraph to the review report to highlight a material uncertainty relating to an event or condition that casts significant doubt on the entity’s ability to continue as a going concern.
  - 42. If a material uncertainty that casts significant doubt on the entity’s ability to continue as a going concern is not adequately disclosed in the financial statements, the auditor shall express a qualified or adverse conclusion, as appropriate. The report shall include specific reference to the fact that there is such a material uncertainty.
18. The exposure draft proposed that more detail be included in the report in these scenarios, consistent with ISA (NZ) 570 (Revised).
- 49. If adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified conclusion and the auditor’s report shall include a separate section under the heading “Material Uncertainty Related to Going Concern” to the review report to highlight a material uncertainty relating to an event or condition that casts significant doubt on the entity’s ability to continue as a going concern. This section shall:
    - a. Draw attention to the note(s) in the financial statements that discloses the matter; and
    - b. State that the events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity’s ability to continue as a going concern and that the auditor’s conclusion is not modified in respect of the matter.
  - 50. If a material uncertainty that casts significant doubt on the entity’s ability to continue as a going concern is not adequately disclosed in the financial statements, the auditor shall:
    - a. Express a qualified or adverse conclusion, as appropriate; and
    - b. In the Basis for Qualified or Adverse Conclusion section of the review report, state that a material uncertainty exists that may cast significant doubt on the entity’s ability to continue as a going concern and that the financial statements do not adequately disclose this matter.
19. CAANZ commented that:
- “It is not clear what “adequate disclosure” would be in an interim financial report when there is a material uncertainty relating to an event or condition that casts significant doubt on the entity’s ability to continue as a going concern. In contrast, paragraph 19 of ISA (NZ) 570



prescribes four specific disclosure requirements for annual financial statements that are subject to audit:

- The principle events or conditions that may cast doubt on the entity's ability to continue as a going concern;
- Management's plans for dealing with these events or conditions;
- That there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern; and
- That, therefore, the entity may be unable to realise its assets and discharge its liabilities in the normal course of business."

20. The comment that the auditing standards are "prescribing" the necessary disclosures rather than the accounting standards is something that we can raise with the NZASB at the joint meeting of the Boards in February 2020.
21. A lack of clarity around "adequate disclosure" may already be an issue with the extant standard. However additional detail has been introduced in the exposure draft as highlighted above in proposed paragraph 50.
22. **The question arises as to whether the board wishes to add more clarity into the standard in response to the feedback received? Possible wording from ISA (NZ) 570 (Revised) paragraph is illustrated above paragraph 49 in agenda item 6.3.**
23. The ED proposed to include the additional scenario where the use of the going concern basis of accounting is inappropriate. The ED then covered all possibilities on the spectrum as dealt with in ISA (NZ) 570 (Revised). This was not covered in the extant standard. We note that ISA (NZ) 570 is explicitly requiring the auditor to conclude on the appropriateness of management's use of the going concern basis of accounting.

*Use of going concern basis of accounting is inappropriate*

51. If the financial statements have been prepared using the going concern basis of accounting but, in the auditor's judgement, management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, the auditor shall express an adverse conclusion.
24. Given concerns expressed by some stakeholders about the auditor's responsibilities related to going concern (i.e. some stakeholder views that the auditor is not required to conclude on the appropriateness of the use of the going concern basis as part of the interim review), we wonder if it is appropriate to include paragraph 51, without clarifying the required procedures. We are still of the view that this is implicit and therefore are comfortable with retaining the proposed requirement. We do consider that the required procedures addressing going concern matters would benefit from additional clarification but acknowledge that may be beyond the scope of the project.

- |   |
|---|
| 25. <b>We seek confirmation from the Board that it is appropriate to include paragraph 51 in the final standard without clarifying the required procedures.</b> |
|---|

**Outside the scope of the project**

26. We consider the following matters identified by stakeholders are outside the scope of this limited revision to NZ SRE 2410.

**27. We seek confirmation from the board, that no further action is required:**

- a) CPA recommended that the auditor of the entity be defined to clarify that it means the auditor of the entity's annual financial statements.
- b) In outreach in New Zealand and in submissions received by the AUASB, practitioners have queried what the auditor is required to do in the year they are first appointed as the auditor (i.e. have not actually audited the annual financial statements yet). We consider that this is an existing gap in NZ SRE 2410, and would require clarification or addition of the procedures to be performed, which the AUASB and NZAuASB have agreed are out of scope.
- c) Additional suggestions for using "plain English" in the review report, which may not be consistent with the international requirements or changes made by the NZAuASB in the auditor's report.
- d) KPMG Australia encouraged the AUASB to consistently make the relevant reporting changes to the full suite of review standards. No similar suggestions were received in New Zealand. We consider that this is beyond the scope of the current project and that no further action is taken ahead of the IAASB post implementation review.

28. Whilst strictly outside the scope of the limited scope project, stakeholders have raised possible matters that may improve the quality of the standard.

**29. The board is asked whether this change can be made regardless even though they may strictly be out of scope:**

- a) Deloitte have queried the words "financial statement components" in paragraph A12. Possible clarification is illustrated in agenda item 6.3.

**Areas of differences with ASRE 2410**

30. Extant NZ SRE 2410 and ASRE 2410 have existing differences:

- a. NZ SRE 2410 already explicitly deals with compliance frameworks. The AUASB has received feedback on whether to add this to the Australian standard. We consider this feedback is outside the scope of the New Zealand project. It is not something we asked the New Zealand stakeholders to comment on.
- b. There are existing differences in the references to management and those charged with governance (TCWG). In New Zealand, specific reference is made to TCWG in the engagement letter, written representations and in the responsibilities in the report. In Australia, some stakeholders raised concern that these words are used inconsistently. This matter is beyond the scope of the New Zealand project. CAANZ noted inconsistency between para 36(a) and 12(a) and suggested edits to paragraph A2. The Board is asked to consider these comments in the mark-up of the ED.
- c. CPA commented that there is an additional statement in ED NZ SRE 2410 "as to the existence of any relationship (other than that of auditor) which the auditor has with, or any interests which the auditor has in, the entity or any of its subsidiaries". This is an existing difference that has been added to the ISAs (NZ) and to the review standards. This matter is beyond the scope of the New Zealand project.
- d. Bradbury suggested deleting the words "on behalf of the entity" from the interim review report. These words have been added throughout the ISAs (NZ) and the review standards

to better reflect the legal position in New Zealand. This matter is beyond the scope of the New Zealand project.

**31. The Board is asked to comment on an exception basis if you wish to address any of these existing differences.**

**Editorial comments**

32. Various editorial comments have been captured in agenda item 6.3. Where changes have been illustrated, we recommend that these changes be accepted. Where we do not recommend making the change or seek further confirmation, we have added a comment.

**33. We ask that the Board provide feedback on these edits on an exception basis.**

EXPOSURE DRAFT NZAuASB 2018-2



NZ AUDITING  
AND ASSURANCE  
STANDARDS BOARD

## **NEW ZEALAND STANDARD ON REVIEW ENGAGEMENTS 2410 (Revised)**

### **Review of Financial Statements Performed by the Independent Auditor of the Entity (NZ SRE 2410 (Revised))**

This Standard was issued on xxx by the New Zealand Auditing and Assurance Standards Board of the External Reporting Board pursuant to section 12(b) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on 6 December 2018.

An auditor that is required to apply this Standard is required to apply it for audits of financial statements for periods beginning on or after xxx. However, early adoption is permitted.

In finalising this Standard, the New Zealand Auditing and Assurance Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued to promote consistency in practice and with the form and content of the auditor's report prepared in accordance with ISA (NZ) 700 (Revised) .

This Standard, when applied, supersedes New Zealand Standard on Review Engagements 2410, *Review of Financial Statements Performed by the Independent Auditor of the Entity*.

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ISBN xxx

**Commented [MP1]:** Is this now considered to be developed jointly?

**NEW ZEALAND STANDARD ON REVIEW ENGAGEMENTS 2410 (Revised)****REVIEW OF FINANCIAL STATEMENTS PERFORMED BY THE INDEPENDENT AUDITOR OF THE  
ENTITY***Issued by the New Zealand Auditing and Assurance Standards Board***~~PROPOSED AMENDMENTS TO NZ SRE 2410~~***This exposure draft uses underlines and strike through to indicate proposed changes to NZ SRE 2410***CONTENTS**

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## NZ SRE 2410 (Revised)

### Operative Date

1. This New Zealand Standard on Review Engagements (NZ SRE) 2410 is effective for reviews of financial statements for periods beginning on or after 1 January 2020, with early adoption permitted.
2. This NZ SRE 2410 supersedes Review Standard 1 issued by the External Reporting Board in July 2011.

**Commented [MP2]:** Can we leave this or does delay mean we have to delay

**Commented [MP3]:** Suggest we supersede extant 2410 – nature of changes are pervasive, so reissue revised standard rather than an amending standard that will need to be compiled?

### Introduction

#### Scope of this NZ SRE 2410

3. This NZ SRE 2410 deals with the auditor's responsibilities when an auditor undertakes an engagement to review the financial statements of an audit client, and on the form and content of the auditor's review report. The term "auditor" is used throughout this NZ SRE 2410, not because the auditor is performing an audit function but because the scope of this NZ SRE 2410 is limited to a review performed by the independent auditor of the financial statements of the entity.
4. This NZ SRE 2410 is directed towards a review of financial statements by an entity's auditor. This NZ SRE 2410 is to be applied, adapted as necessary, when an entity's auditor undertakes an engagement to review historical financial information other than financial statements of an audit client.

### Objective

5. The objective of the auditor is to plan and perform the review to enable the auditor to express a conclusion whether, on the basis of the review, anything has come to the auditor's attention that causes the auditor to believe that the financial statement, or complete set of financial statements, is (are) not prepared, in all material respects, in accordance with the applicable financial reporting framework. (Ref: Para. A1-A3)

### Definitions

6. For the purposes of this NZ SRE 2410, the following terms have the meanings attributed below:
  - (a) **Interim financial statements** means financial statements that are prepared in accordance with an applicable financial reporting framework for a period that is shorter than the entity's financial year.
  - (b) **Financial statements** means a structured representation of historical financial information, including disclosures, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The term "financial statements" ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement. Disclosures comprise explanatory or descriptive information, set out as required, expressly permitted or otherwise allowed by the applicable financial reporting framework, on the face of the financial statement, or in the notes, or incorporated therein by cross-reference.

**Commented [MP4]:** CPA submission to NZAuASB  
We recommend that:

- "auditor of the entity" is defined to clarify that it means the auditor of the entity's annual financial statements.

This may be beyond the scope of the project. Is there a compelling reason to define a term not defined in ISRE 2410?

**Commented [MP5]:** The term "interim financial statements" is only used in the illustrative reports. Had thought to link defined terms to the defined term but the standard actually refers to "financial statements". 2410 does not have defined terms so this is something we have introduced in the clarified text.

Shall we use this term in the standard rather than just financial statements?  
While financial statements is also defined, is this rather



#### **ED-NZ SRE 2410 (Revised)**

- (c) An applicable financial reporting framework means the financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

The term “fair presentation framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

- (a) acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
- (b) acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.

## **Requirements**

### **Performing a Review**

7. The auditor who is engaged to perform a review of financial statements shall perform the review in accordance with this NZ SRE 2410. (Ref: Para. A4)

### **General Principles of a Review of Financial Statements**

- 8. The auditor shall comply with relevant ethical requirements relating to the audit of the annual financial statements of the entity. (Ref: Para. A5)
- 9. The auditor shall implement quality control procedures that are applicable to the individual engagement. (Ref: Para. A6)
- 10. The auditor shall comply with the engagement quality control requirements of ISA (NZ) 220<sup>1</sup> when performing a review engagement in accordance with this NZ SRE 2410.
- 11. The auditor shall plan and perform the review by exercising professional judgement and with an attitude of professional scepticism, recognising that circumstances may exist that cause the financial statements to require a material adjustment for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework. (Ref: Para. A7)

### **Agreeing the Terms of the Engagement (Ref: Para. A8, A55 and A57)**

#### *Preconditions for a Review*

12. The auditor shall, prior to agreeing the terms of the engagement, determine whether the financial reporting framework is acceptable and obtain agreement from those charged with governance, that they acknowledge and understand their responsibility:

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<sup>1</sup> ISA (NZ) 220, Quality Control for an Audit of Financial Statements.

#### ED-NZ SRE 2410 (Revised)

- (a) For the preparation ~~and fair presentation~~ of the financial statements including where relevant their fair presentation;
- (b) For such internal controls as management and those charged with governance deem necessary to enable the preparation of the financial statements that are free from material misstatement; and
- (c) To provide the auditor with:
- access to information relevant to the preparation of the financial statements;
  - additional information that the auditor may request for the purposes of the review engagement; and
  - unrestricted access to persons from whom the auditor determines it necessary to obtain evidence.

**Commented [MP6]:** Submission feedback (Deloitte) Inconsistent with A8 – also a compliance framework will not result in fair presentation.

Also comment from CAANZ to the NZAuASB that 12(a) is inconsistent with 36(a)

#### *Agreement on Review Engagement Terms*

13. The auditor shall agree the terms of the engagement with those charged with governance, which shall be recorded in writing by the auditor and forwarded to the entity. When the review engagement is undertaken pursuant to legislation, the minimum applicable terms are those contained in the legislation.

**Commented [MP7]:** AUASB received feedback to review the use of management and TCWG for inconsistency. In New Zealand we have specific references when TCWG is used. This may not be consistent with Australia.

In New Zealand, NZ para change to require TCWG to agree the terms of the engagement. TCWG used consistently with ISA (NZ) 210.

#### **Procedures for a Review of Financial Statements**

##### **Understanding the Entity and its Environment, Including its Internal Control**

14. The auditor shall obtain an understanding of the entity and its environment, including its internal control, as it relates to the preparation of both the annual and interim or other financial statements, sufficient to plan and conduct the engagement so as to be able to:
- (a) Identify the types of potential material misstatements and consider the likelihood of their occurrence; and
- (b) Select the enquiries, analytical and other review procedures that will provide the auditor with a basis for reporting whether anything has come to the auditor's attention that causes the auditor to believe that the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework. (Ref: Para. A9-A12)
15. In order to plan and conduct a review of financial statements, a recently appointed auditor, who has not yet performed an audit of the annual financial statements in accordance with International Standards on Auditing (New Zealand), shall obtain an understanding of the entity and its environment, including its internal control, as it relates to the preparation of both the annual and interim or other financial statements. (Ref: Para. A13)

##### **Materiality** (Ref: Para. A14-A18)

16. The auditor shall consider materiality, using professional judgement, when:
- (a) Determining the nature, timing and extent of review procedures; and
- (b) Evaluating the effect of misstatements.

**Enquiries, Analytical and Other Review Procedures**

17. The auditor shall make enquiries, primarily of persons responsible for financial and accounting matters, and perform analytical and other review procedures to enable the auditor to conclude whether, on the basis of the procedures performed, anything has come to the auditor's attention that causes the auditor to believe that the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework. (Ref: Para. A19-A23)
18. The auditor shall obtain evidence that the financial statements agree or reconcile with the underlying accounting records. (Ref: Para. A24)
19. The auditor shall enquire whether management has identified all events up to the date of the review report that may require adjustment to or disclosure in the financial statements. (Ref: Para. A25)
20. The auditor shall enquire whether those charged with governance have changed their assessment of the entity's ability to continue as a going concern. When, as the result of this enquiry or other review procedures, the auditor becomes aware of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, the auditor shall:
  - (a) Enquire of those charged with governance as to their plans for future actions based on their going concern assessment, the feasibility of these plans, and whether they believe that the outcome of these plans will improve the situation; and
  - (b) Consider the adequacy of the disclosure about such matters in the financial statements. (Ref: Para. A26)
21. When a matter comes to the auditor's attention that leads the auditor to question whether a material adjustment should be made for the financial statements to be prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor shall make additional enquiries or perform other procedures to enable the auditor to express a conclusion in the review report. (Ref: Para. A27)

The auditor shall enquire of management and, where appropriate, those charged with governance, as to the existence of any actual or suspected non-compliance with provisions of laws and regulations that are generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements.

**Comparatives – First Financial Statements** (Ref: Para. A28-A31)

- ~~21.~~22. When comparative information is included for the first time in the financial statements, an auditor shall perform similar procedures on the comparative information as applied to the current period financial statements.

**Evaluation of Misstatements** (Ref: Para. A32-A34)

- ~~22.~~23. The auditor shall evaluate, individually and in the aggregate, whether uncorrected misstatements that have come to the auditor's attention are material to the financial statements.

**Written Representations**

- ~~23.~~24. The auditor shall endeavour to obtain written representations from those charged with governance, that:

**Commented [MP8]:** ISA (NZ) 570 refers to management's assessment. (In NZ standards changed references from management to TCWG in three aspects: engagement letter, written representations and report. Australian submissions suggest a need for further consistency or review of how these terms have been interchanged.

**Commented [MP9]:** Consider the need to include an additional requirement re NOCLAR. CPA Australia suggested: The auditor shall enquire about whether the entity is aware of any NOCLAR (see ISA (NZ) 250 (Revised) para 15; and IF the auditor becomes aware of an instance of, or suspects, NOCLAR, to obtain an understanding of the nature of the act and the circumstances in which it has occurred, as well as further information to evaluate the possible effect on the financial statements.

If more is to be added, suggest the enquiry from 2400 may be more appropriate for a review. Does the board wish to add an additional requirement? Is so, thoughts on approach and drafting. Para 31 covers what the auditor should do if they consider there are indicators of NOCLAR.

**Commented [MP10]:** Consistent with NZ Approach in ISA (NZ) 580

#### **ED-NZ SRE 2410 (Revised)**

- (a) They acknowledge their responsibility for the design and implementation of internal control to prevent and detect fraud and error;
- (b) The financial statements are prepared and presented in accordance with the applicable financial reporting framework;
- (c) They believe the effect of those uncorrected misstatements aggregated by the auditor during the review are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. A summary of such items is included in or attached to the written representations;
- (d) They have disclosed to the auditor all significant facts relating to any frauds or suspected frauds known to them that may have affected the entity;
- (e) They have disclosed to the auditor the results of their assessment of the risk that the financial statements may be materially misstated as a result of fraud;
- (f) They have disclosed to the auditor all ~~identified~~ known actual or suspected non-compliance with laws and regulations, the effects of which are to be considered when preparing the financial statements; and
- (g) They have disclosed to the auditor all significant events that have occurred subsequent to the balance sheet date and through to the date of the review report that may require adjustment to or disclosure in the financial statements.
- (h) They have disclosed to the auditor all information relevant to the use of the going concern basis of accounting. (Ref: Para. A35)

~~24-25.~~ If those charged with governance refuse to provide a written representation that the auditor considers necessary, this constitutes a limitation on the scope of the auditor's work and the auditor shall express a qualified conclusion or a disclaimer of conclusion, as appropriate.

#### **Auditor's Responsibility for Other Information**

~~25-26.~~ The auditor shall read the other information that accompanies the financial statements to consider whether there ~~is~~ are any material inconsistencies with the financial statements. (Ref: Para. A36)

~~26-27.~~ If a matter comes to the auditor's attention that causes the auditor to believe that the other information appears to include a material misstatement of fact, the auditor shall discuss the matter with the entity's management, and where appropriate, those charged with governance. (Ref: Para. A37)

#### **Communication**

~~27-28.~~ When, as a result of performing a review of the financial statements, a matter comes to the auditor's attention that causes the auditor to believe that it is necessary to make a material adjustment to the financial statements for them to be prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor shall communicate this matter as soon as practicable to the appropriate level of management.

~~28-29.~~ When, in the auditor's judgement, management does not respond appropriately within a reasonable period of time, the auditor shall inform those charged with governance. (Ref: Para. A38)

**Commented [MP11]:** KPMG submission to AUASB suggest change identified to known – ISA 250 refers to known and ISRE 2400 refers to known actual . Suggest use known actual.

**Commented [MP12]:** Suggestion by EY in New Zealand submission

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~~29,30.~~ When, in the auditor's judgement, those charged with governance do not respond appropriately within a reasonable period of time, the auditor shall consider:

- (a) Whether to modify the review report; or
- (b) The possibility of withdrawing from the engagement; and
- (c) The possibility of resigning from the appointment to audit the annual financial statements. (Ref: Para. A58)

~~30,31.~~ When, as a result of performing the review of the financial statements, a matter comes to the auditor's attention that indicates the existence of fraud or non-compliance with laws and regulations, or suspected fraud or non-compliance with laws and regulations, has occurred in the entity, the auditor shall:

- (a) Communicate the matter, unless prohibited by law or regulation, as soon as practicable with those charged with governance;
- (b) Request management's assessment of the effect(s), if any, on the financial statements;
- (c) Consider the effect on the auditor's conclusion and the review report; and
- (d) Determine whether law, regulation or relevant ethical requirements:
  - (i) Require the auditor to report to an appropriate authority outside the entity.
  - (ii) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances. (Ref: Para. A39-A40)

~~31,32.~~ The auditor shall communicate relevant matters of governance interest arising from the review of the financial statements to those charged with governance. (Ref: Para. A41 and A59)

## Reporting the Nature, Extent and Results of the Review of Financial Statements

~~32,33.~~ The auditor shall issue a written report that contains the following:

- (a) An appropriate title clearly identifying it as a review report of the independent auditor of the entity.
- (b) An addressee, as required by the circumstances of the engagement.

~~33,34.~~ The first section of the auditor's review report shall include the auditor's conclusion, and shall have the heading "Conclusion". The Conclusion section of the report shall:

- (a) Identify the entity whose financial statements have been reviewed;
- (b) State that the financial statements have been reviewed;
- (c) Identify the title of each statement comprising the financial statements;
- (d) Refer to the notes, including the summary of significant accounting policies; and
- (e) Specify the date of, or period covered by, each financial statement comprising the financial statements; and
- (f) Include a conclusion:
  - (i) When expressing an unmodified conclusion on financial statements prepared in accordance with a fair presentation framework, the report shall

**Commented [MP13]:** Deloitte comment - The remaining reference is only to guidance specifically for public sector auditors. Is this a problem?

**Commented [MP14]:** Deloitte suggested remove "has occurred in the entity" but this has been retained in ISRE 2400.

**Commented [MP15]:** CPA Australia suggested amending para 31 to better reflect the communications the auditor would need to undertake under PES 1 i.e. rather than requesting managements assessment, there should be a requirement to address the circumstance where management and tcwg may be involved in the NOCLAR and consider the need for the auditor to obtain legal advice.

**Commented [MP16]:** Do not call it auditor's review report here as duplication with the independent auditor of the entity.

**Commented [MP17]:** Deloitte AUASB submission – be consistent. Do we need to state this each time in the requirement on reporting?

**Commented [MP18]:** KPMG submission to AUASB – inconsistent with ASA 700, but this is consistent with ISA (NZ) so not an issue in NZ.

**Commented [MP19]:** Deloitte submission – I suggest we go back to what we had in the original NZ ED – as a separate paragraph.

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include a conclusion as to whether anything has come to the auditor's attention that causes the auditor to believe that the financial statements do not present fairly, in all material respects, or if applicable are not true and fair, in accordance with the applicable financial reporting framework (including a reference to the jurisdiction or country of origin of the financial reporting framework when New Zealand is not the origin of the financial reporting framework used).

- (ii) When expressing an unmodified conclusion on financial statements prepared in accordance with a compliance framework, the report shall include a conclusion as to whether anything has come to the auditor's attention that causes the auditor to believe that the financial statements have ~~statements have~~ not been prepared, in all material respects, in accordance with the applicable financial reporting framework (including a reference to the jurisdiction or country of origin of the financial reporting framework when New Zealand is not the origin of the financial reporting framework used). (Ref: Para. A43)

~~34.35.~~ The auditor's review report shall include a section, directly following the Conclusion section, with the heading "Basis for Conclusion", that:

- (a) States that the review of the financial statements was conducted in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*;
- (b) Refers to the section of the auditor's review report that describes the auditor's responsibilities under NZ SRE 2410;
- (c) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements in New Zealand relating to the audit of the annual financial statements, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements.
- (d) Includes a statement as to the existence of any relationship (other than that of auditor) which the auditor has with, or any interests which the auditor has in, the entity or any of its subsidiaries.

~~35.36.~~ The auditor's review report shall include a section with a heading "Responsibilities of Those Charged with Governance for the Financial Statements." This section of the report shall describe the responsibilities of those charged with governance for:

- (a) The preparation of the financial statements in accordance with the applicable financial reporting framework, and for such internal control as those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
- (b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern.

~~36.37.~~ When the financial statements are prepared in accordance with a fair presentation framework, the description of responsibilities for the financial statements in the auditor's review report shall refer to the "preparation and fair presentation of these

**Commented [MP20]:** EY submission to NZAuASB:  
•In paragraph 34 f(i) we think the following highlighted wording is missing "When expressing an unmodified conclusion on financial statements prepared in accordance with a fair presentation framework, the report shall include a conclusion as to whether anything has come to the auditor's attention that causes the auditor to believe that the financial statements do not present fairly, in all material respects, the financial position of the entity and of its financial performance and its cash flows or if applicable are not true and fair, in accordance with the applicable financial reporting framework (including a reference to the jurisdiction or country of origin of the financial reporting framework when New Zealand is not the origin of the financial reporting framework used)."  
Staff suggest no change – from ISA 700

**Commented [MP21]:** EY submission to NZAuASB.

**Commented [MP22]:** KPMG comment to AUASB suggest keeping independent in title. NZ SRE had not proposed to remove so no issue in NZ standard

**Commented [MP23]:** This aligns to 700 now get consistent in the reports.

**Commented [MP24]:** Consistent with ISAs (NZ) this refers to responsibilities of TCWG

**Commented [MP25]:** This lead in differs from Australia not sure we can be consistent as we have a different approach to amending for TCWG.

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financial statements” or “the preparation of financial statements that give a true and fair view” as appropriate.

~~37.~~38. The auditor’s review report shall include a section with the heading “Auditor’s Responsibilities for the Review of the Financial Statements.” This section of the auditor’s review report shall:

- (a) State that the auditor is responsible for expressing a conclusion on the financial statements based on the review.
- (b) State that a review consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.
- (c) State that based on the review procedures performed, the auditor concludes on whether anything has come to the auditor’s attention that causes the auditor to believe that the use of the going concern basis of accounting by those charged with governance is not appropriate and whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern. If a matter comes to the attention of the auditor that causes the auditor to believe that a material uncertainty related to going concern exists, the auditor is required to draw attention in the review report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify the conclusion. The auditor’s conclusions are based on the procedures performed up to the date of the review report. However, future events or conditions may cause the entity to cease to continue as a going concern.
- (d) State that a review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently does not enable the auditor to obtain assurance that the auditor would become aware of all significant matters that might be identified in an audit, and that accordingly no audit opinion is expressed.

~~38.~~39. The name of the engagement partner shall be included in the auditor’s review report on financial statements of FMC reporting entities considered to have a higher level of public accountability unless, in rare circumstances, such disclosure is reasonably expected to lead to a significant personal security threat.

~~39.~~40. The auditor’s review report shall include:

- (a) The date the auditor signs the report.
- (b) The location in the country or jurisdiction where the auditor practices.
- (c) The auditor’s signature. (Ref: Para. A42)

**Departure from the Applicable Financial Reporting Framework**

~~40.~~41. The auditor shall express a qualified or adverse conclusion when a matter has come to the auditor’s attention that causes the auditor to believe that a material adjustment should be made to the financial statements for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework. The auditor shall amend the heading “Basis for Conclusion” to “Basis for Qualified Conclusion” or “Basis for Adverse Conclusion” in the report, that describes the nature of the departure and, if practicable, states the effects on the financial statements. If the effects or possible effects are incapable of being measured reliably, a statement to that effect and

**Commented [MP26]:** NZAuASB have a different approach to Australia – did not include Modified Conclusion section as this is repetitive, therefore Deloitte suggestions not relevant.

**Commented [MP27]:** Leave as is? Deloitte suggest it should be state not states?

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the reasons therefore shall be included in the Basis for Conclusion section. The conclusion paragraph shall be headed “Qualified Conclusion” or “Adverse Conclusion”, whichever is relevant. (Ref: Para. A44–A45)

**Commented [MP28]:** ED NZ SRE differed from ED ASRE 2410 – Deloitte suggestion not relevant in NZ. Re reference to modification paragraph

~~41.~~~~42.~~ When the effect of the departure is so material and pervasive to the financial statements that the auditor concludes a qualified conclusion is not adequate to disclose the misleading or incomplete nature of the financial statements, the auditor shall express an adverse conclusion. (Ref: Para. A46)

#### **Limitation on Scope**

~~42.~~~~43.~~ When the auditor is unable to complete the review, the auditor shall communicate, in writing, to the appropriate level of management and to those charged with governance the reason why the review cannot be completed, and consider whether it is appropriate to issue a review report. (Ref: Para. A47)

#### **Limitation on Scope Imposed by Management**

~~43.~~~~44.~~ Unless required by law or regulation, an auditor shall not accept an engagement to review the financial statements when management has imposed a limitation on the scope of the auditor’s review. (Ref: Para. A48 and ~~A57~~)

**Commented [MP29]:** Is this A58?

~~44.~~~~45.~~ If, after accepting the engagement, management imposes a limitation on the scope of the review, the auditor shall request management to remove the limitation. If management refuses the auditor’s request to remove the limitation, the auditor shall communicate, in writing, to the appropriate level of management and those charged with governance, the reason(s) why the review cannot be completed. (Ref: Para. A49)

~~45.~~~~46.~~ If management and, where appropriate, those charged with governance, refuses the auditor’s request to remove a limitation that has been imposed on the scope of the review, but there is a legal or regulatory requirement for the auditor to issue a report, the auditor shall issue a disclaimer of conclusion or qualified conclusion report, as appropriate, containing the reason(s) why the review cannot be completed. (Ref: Para. A50)

~~46.~~~~47.~~ When the auditor disclaims a conclusion on the financial statements, the auditor shall amend the description of the auditor’s responsibilities required by paragraph 38 to include only:

- (a) A statement that the auditor’s responsibility is to conduct the review of the entity’s financial statements in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*;
- (b) A statement that, however, because of the matter(s) described in the Basis for Disclaimer of Conclusion section, the auditor was not able to obtain sufficient evidence to provide a basis for a review conclusion on the financial statements; and
- (c) The statement about auditor independence and other ethical responsibilities required by paragraphs 35(c) and (d).

#### **Other Limitations on Scope Not Imposed by Management**

~~47.~~~~48.~~ The auditor shall express a qualified conclusion when, in rare circumstances, there is a limitation on the scope of the auditor’s work that is confined to one or more specific matters, which while material, is not in the auditor’s judgement pervasive to the



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financial statements, and when the auditor concludes that an unqualified conclusion cannot be expressed. A qualified conclusion shall be expressed as being “except for” the effects of the matter to which the qualification relates. The conclusion paragraph shall be headed “Qualified Conclusion”. (Ref: Para. A51-A52)

### Going Concern and a Material Uncertainty Exists (Ref: Para. A53-A54A54)

*Use of going concern basis of accounting is appropriate but a material uncertainty exists*

If a material uncertainty exists, the auditor shall determine whether the financial statements:

- (a) Adequately disclose the principal events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern and management’s plans to deal with these events or conditions; and
- (b) Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern and, therefore, that it may be unable to realise its assets and discharge its liabilities in the normal course of business.

~~48-49.~~ If adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified conclusion and the auditor’s report shall include a separate section under the heading “Material Uncertainty Related to Going Concern” to the review report to highlight a material uncertainty relating to an event or condition that casts significant doubt on the entity’s ability to continue as a going concern. This section shall:

- (a) Draw attention to the note(s) in the financial statements that discloses the matter; and
- (b) State that the events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity’s ability to continue as a going concern and that the auditor’s conclusion is not modified in respect of the matter.

~~49-50.~~ If a material uncertainty that casts significant doubt on the entity’s ability to continue as a going concern is not adequately disclosed in the financial statements, the auditor shall:

- (a) Express a qualified or adverse conclusion, as appropriate; and
- (b) In the Basis for Qualified or Adverse Conclusion section of the review report, state that a material uncertainty exists that may cast significant doubt on the entity’s ability to continue as a going concern and that the financial statements do not adequately disclose this matter.

*Use of going concern basis of accounting is inappropriate*

~~50-51.~~ If the financial statements have been prepared using the going concern basis of accounting but, in the auditor’s judgement, management’s use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, the auditor shall express an adverse conclusion.

### Emphasis of Matter Paragraphs

~~51-52.~~ The auditor shall consider ~~adding including~~ an emphasis of matter paragraph to draw users’ attention to a matter presented or disclosed in the financial statements that, in the

**Commented [MP30]:** Deloitte suggestion to rename “Material Uncertainty Exists Related to Going Concern”?

Deloitte suggest stipulating the order within the review report. I did not think that 700 stipulated the order, 570 already provides some illustrations so why include more here?

Possible inconsistency introduced by this section. 570 describes what a MU is and requires the auditor to conclude whether a MU exists. (Must gather evidence to determine whether there is a MU. It then goes on to deal with the reporting implications. The ED just deals with the reporting implications (but does not explicitly require the auditor to conclude whether there is a MU or not – how does the auditor meet the reporting obligations if they do not conclude whether use of GC is appropriate or whether there is a MU or not?)

**Commented [MP31]:** Is this not requiring the auditor to conclude whether a MU exists?

**Commented [MP32]:** CAANZ comment - it is not clear what “adequate disclosure” would be in an interim financial report when there is a material uncertainty relating to an event or condition that casts significant doubt. ISA (NZ) 570 prescribes four specific disclosure requirements for financial statements.

Board is asked to comment on whether to add more here?

**Commented [MP33]:** EY submission to NZAuASB

**Commented [MP34]:** Deloitte suggestion

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auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements.

~~52.53.~~ When the auditor includes an Emphasis of Matter paragraph in the auditor's review report, the auditor shall:

- (a) Include the paragraph within a separate section of the auditor's review report with an appropriate heading that includes the term "Emphasis of Matter";
- (b) Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph shall refer only to information presented or disclosed in the financial statements; and
- (c) Indicate that the auditor's conclusion is not modified in respect of the matter emphasized.

### Other Matter Paragraph

~~53.54.~~ The auditor shall consider ~~adding including~~ an Other Matter paragraph in the review report to communicate a matter other than those that are presented or disclosed in the financial statements, that in the auditor's judgement is relevant to users' understanding of the review, the auditor's responsibilities, or the review report, if not prohibited by law or regulation. When including an Other Matter paragraph in the review report, the auditor shall include a separate section with the heading "Other Matter", or other appropriate heading.

**Commented [MP35]:** Deloitte suggestion

### Documentation (Ref: Para. A60)

~~54.55.~~ The auditor shall prepare review documentation that is sufficient and appropriate to provide a basis for the auditor's conclusion, and to provide evidence that the review was performed in accordance with this NZ SRE 2410 and applicable legal and regulatory requirements.

\* \* \*

**Commented [MP36]:** KPMG Australia queried the need to detail possible documentation of NOCLAR from ASA 250. We note that ISRE 2400, that has been updated for NOCLAR, does not deal with NOCLAR in the documentation section. 2410 documentation requirement seem very basic when compared to 2400 but this is a matter that may be beyond the scope of the project. We consider that adding NOCLAR in here would be unusual given the high level nature of the requirement.

### Application and Other Explanatory Material

#### Objective (Ref: Para. 5)

- A1. Under paragraph 14, the auditor needs to make enquiries, and perform analytical and other review procedures in order to reduce to a limited level the risk of expressing an inappropriate conclusion when the financial statements are materially misstated.
- A2. The objective of a review of the financial statements differs significantly from that of an audit conducted in accordance with International Standards on Auditing (New Zealand). A review of the financial statements does not provide a basis for expressing an opinion whether the financial statements give a true and fair view, or are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.
- A3. A review, in contrast to an audit, is not designed to obtain reasonable assurance that the financial statements are free from material misstatement. A review consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review may bring significant

**Commented [MP37]:** Should this be 17?

**Commented [MP38]:** CAANZ comment on compliance frameworks. "If NZ SRE 2410 is to also include reference to compliance frameworks This was added in the Aus ED but has been addressed previously in the NZ standard. Do you wish to amend references for compliance frameworks? This may be beyond the scope of the project? Does the NZAuASB wish to reconsider its approach to compliance frameworks?"

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matters affecting the financial statements to the auditor's attention, but it does not provide all of the evidence that would be required in an audit.

### **Performing a Review (Ref: Para 7)**

- A4. Through performing the audit of the annual financial statements, the auditor obtains an understanding of the entity and its environment, including its internal control. When the auditor is engaged to review the financial statements, under paragraph 14, the auditor needs to update this understanding through enquiries made in the course of the review, to assist the auditor in focusing the enquiries to be made and the analytical and other review procedures to be applied. An assurance practitioner who is engaged to perform a review of the financial statements, and who is not the auditor of the entity, does not perform the review in accordance with NZ SRE 2410\*, as the assurance practitioner ordinarily does not have the same understanding of the entity and its environment, including its internal control, as the auditor of the entity. Although other International Standards on Auditing (New Zealand) do not apply to review engagements, they include guidance which may be helpful to auditors performing reviews covered by this NZ SRE 2410.

### **General Principles of a Review of Financial Statements**

- A5. Relevant ethical requirements<sup>2</sup> govern the auditor's professional responsibilities in the following areas: independence, integrity, objectivity, professional competence and due care, confidentiality, professional behaviour, and technical standards. (Ref: Para. 8)
- A6. The elements of quality control that are relevant to an individual engagement include leadership responsibilities for quality on the engagement, ethical requirements, acceptance and continuance of client relationships and specific engagements, assignment of engagement teams, engagement performance, and monitoring. (Ref: Para. 9)
- A7. An attitude of professional scepticism denotes that the auditor makes a critical assessment, with a questioning mind, of the validity of evidence obtained and is alert to evidence that contradicts or brings into question the reliability of documents or representations by those charged with governance of the entity. ISA (NZ) 200 includes guidance which may be helpful.\* (Ref: Para. 11)

### **Agreeing the Terms of the Engagement**

- A8. Written agreement of the terms of the engagement helps to avoid misunderstandings regarding the nature of the engagement and, in particular, the objective and scope of the review, the responsibilities of those charged with governance, the extent of the auditor's responsibilities, the assurance obtained, and the nature and form of the report. The communication ordinarily covers the following matters:
- (a) the objective of a review of the financial statements;
  - (b) the scope of the review;

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\* See ISRE (NZ) 2400 *Engagements to Review Historical Financial Statements*.

<sup>2</sup> Professional and Ethical Standard 1—~~(Revised)~~, *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand).

\* ISA (NZ) 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing* (New Zealand).

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- (c) the responsibilities of those charged with governance for:
  - (i) the preparation of the financial statements in accordance with the applicable financial reporting framework including where relevant their fair presentation;
  - (ii) establishing and maintaining effective internal control relevant to the preparation of the financial statements; and
  - (iii) making all financial records and related information available to the auditor;
- (d) agreement from those charged with governance:
  - (i) to provide written representations to the auditor to confirm representations made orally during the review, as well as representations that are implicit in the entity's records; and
  - (ii) that where any document containing the financial statements indicates that the financial statements have been reviewed by the entity's auditor, the review report also will be included in the document; and
- (e) the anticipated form and content of the report to be issued, including the identity of the addressee of the report.

An illustrative engagement letter is set out in Appendix 1. The terms of engagement to review the financial statements can also be combined with the terms of engagement to audit the annual financial statements. ISA (NZ) 210 includes guidance which may be helpful.\* (Ref: Para. 12)

#### Procedures for a Review of the Financial Statements

##### Understanding the Entity and its Environment, Including its Internal Control

- A9. Under ISA (NZ) 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, the auditor who has audited the entity's financial statements for one or more annual periods has obtained an understanding of the entity and its environment, including its internal control, as it relates to the preparation of the annual financial statements, that was sufficient to conduct the audit. In planning a review of the financial statements, the auditor needs to update this understanding. The auditor also needs to obtain a sufficient understanding of internal control as it relates to the preparation of the financial statements subject to review, as it may differ from internal control as it relates to the preparation of the annual financial statements. (Ref: Para. 14)
- A10. The auditor needs to use the understanding of the entity and its environment, including its internal control, to determine the enquiries to be made and the analytical and other review procedures to be applied, and to identify the particular events, transactions or assertions to which enquiries may be directed or analytical or other review procedures applied. (Ref: Para. 14)
- A11. The procedures performed by the auditor to update the understanding of the entity and its environment, including its internal control, ordinarily include the following:
- (a) reading the documentation, to the extent necessary, of the preceding year's audit, reviews of prior period(s) of the current year, and corresponding period(s)

**Commented [MP39]:** Will need a conforming amendment in NZ for new standard

\* ISA (NZ) 210 *Agreeing the Terms of Audit Engagements*.

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of the prior year, to enable the auditor to identify matters that may affect the current-period financial statements;

- (b) considering any significant risks, including the risk of management override of controls, that were identified in the audit of the prior year's financial statements;
- (c) reading the most recent annual and comparable prior period financial statements;
- (d) considering materiality with reference to the applicable financial reporting framework as it relates to the financial statements, to assist in determining the nature and extent of the procedures to be performed and evaluating the effect of misstatements;
- (e) considering the nature of any corrected material misstatements and any identified uncorrected immaterial misstatements in the prior year's financial statements;
- (f) considering significant financial accounting and reporting matters that may be of continuing significance, such as material weaknesses in internal control;
- (g) considering the results of any audit procedures performed with respect to the current year's financial statements;
- (h) considering the results of any internal audit performed and the subsequent actions taken by management;
- (i) enquiring of management about the results of management's assessment of the risk that the financial statements may be materially misstated as a result of fraud;
- (j) enquiring of management about the effect of changes in the entity's business activities;
- (k) enquiring of management about any significant changes in internal control and the potential effect of any such changes on the preparation of the financial statements; and
- (l) enquiring of management of the process by which the financial statements have been prepared and the reliability of the underlying accounting records to which the financial statements are agreed or reconciled. (Ref: Para. 14)

A12. The auditor needs to determine the nature of the review procedures, if any, to be performed for components and, where applicable, communicate these matters to other auditors involved in the review. Factors considered ordinarily include the materiality of, and risk of misstatement in, the financial statement information of the components, and the auditor's understanding of the extent to which internal control over the preparation of such financial statements is centralised or decentralised. (Ref: Para. 14)

A13. Obtaining an understanding of the entity and its environment enables the auditor to focus the enquiries made, and the analytical and other review procedures applied in performing a review of the financial statements in accordance with this NZ SRE 2410. As part of obtaining this understanding, ordinarily the auditor makes enquiries of the predecessor auditor and, where practicable, reviews the predecessor auditor's documentation for the preceding annual audit and for any prior periods in the current year that have been reviewed by the predecessor auditor. In doing so, ordinarily the auditor considers the nature of any corrected misstatements, and any uncorrected misstatements aggregated by the auditor, any significant risks, including the risk of management override of controls, and significant accounting and any reporting matters

**Commented [MP40]:** Deloitte consider this is unclear – not used in 600. Suggest financial information of the component. Strictly not within scope but we have made other improvements that are not within scope when developing the ED using the logic if it is blatantly wrong then let's fix it.

**Commented [MP41]:** Suggest information

that may be of continuing significance, such as material weaknesses in internal control.  
(Ref: Para. 15)

**Materiality (Ref: Para. 16)**

- A14. The auditor needs to use professional judgement and consider qualitative and quantitative factors in determining materiality.
- A15. Ordinarily, the auditor's consideration of materiality for a review of the financial statements is based on the period financial data and accordingly, materiality based on interim period financial data may be less than materiality for annual financial data. If the entity's business is subject to cyclical variations or if the financial results for the current period show an exceptional decrease or increase compared to prior periods and expected results for the current year, the auditor may, for example, conclude that materiality is more appropriately determined using a normalised figure for the period.
- A16. The auditor's consideration of materiality, in evaluating the effects of misstatements, is a matter of professional judgement and is affected by the auditor's perception of the financial information needs of users of the financial statements.
- A17. If the applicable financial reporting framework contains a definition of materiality, it will ordinarily provide a frame of reference to the auditor when determining materiality for planning and performing the review.
- A18. The auditor needs, when relevant, to consider materiality from the perspective of both the entity and the consolidated entity.

**Enquiries, Analytical and Other Review Procedures**

- A19. A review ordinarily does not require tests of the accounting records through inspection, observation or confirmation. Procedures for performing a review of the financial statements ordinarily are limited to making enquiries, primarily of persons responsible for financial and accounting matters and applying analytical and other review procedures, rather than corroborating information obtained concerning matters relating to the financial statements. The auditor's understanding of the entity and its environment, including its internal control, the results of the risk assessments relating to the preceding audit and the auditor's consideration of materiality as it relates to the financial statements, affects the nature and extent of the enquiries made, and analytical and other review procedures applied. (Ref: Para. 17)
- A20. The auditor ordinarily performs the following procedures:
  - (a) Reading the minutes of the meetings of shareholders, those charged with governance and other appropriate committees to identify matters that may affect the financial statements, and enquiring about matters dealt with at meetings for which minutes are not available that may affect the financial statements.
  - (b) Considering the effect, if any, of matters giving rise to a modification of the audit or review report, accounting adjustments or unadjusted misstatements, at the time of the previous audit or reviews.
  - (c) Communicating, where appropriate, with other auditors who are performing a review of the financial statements of the entity's significant components.
  - (d) Enquiring of members of management responsible for financial and accounting matters, and others as appropriate, about the following:

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- (i) whether the financial statements have been prepared and presented in accordance with the applicable financial reporting framework;
  - (ii) whether there have been any changes in accounting principles or in the methods of applying them;
  - (iii) whether any new transactions have necessitated the application of a new accounting principle;
  - (iv) whether the financial statements contain any known uncorrected misstatements;
  - (v) unusual or complex situations that may have affected the financial statements, such as a business combination or disposal of a segment of the business;
  - (vi) significant assumptions that are relevant to the fair value measurement or disclosures and management's intention and ability to carry out specific courses of action on behalf of the entity;
  - (vii) whether related party transactions have been appropriately accounted for and disclosed in the financial statements;
  - (viii) significant changes in commitments and contractual obligations;
  - (ix) significant changes in contingent assets and contingent liabilities including litigation or claims;
  - (x) compliance with debt covenants;
  - (xi) matters about which questions have arisen in the course of applying the review procedures;
  - (xii) significant transactions occurring in the last several days of the period or the first several days of the next period;
  - (xiii) knowledge of any fraud or suspected fraud affecting the entity involving:
    - management;
    - employees who have significant roles in internal control; or
    - others where the fraud could have a material effect on the financial statements; and
  - (xiv) knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial information communicated by employees, former employees, analysts, regulators or others; and
  - (xv) knowledge of any actual or suspected non-compliance with laws and regulations that could have a material effect on the financial statements. If the auditor becomes aware of any actual or suspected non-compliance with laws and regulations ISA (NZ) 250 *Consideration of Laws and Regulations in an Audit of Financial Statements* provides guidance.
- (e) Applying analytical procedures to the financial statements designed to identify relationships and individual items that appear to be unusual and that may reflect a material misstatement in the financial statements. Analytical procedures may include ratio analysis and statistical techniques such as trend analysis or regression analysis and may be performed manually or with the use of computer-

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assisted auditing techniques. Appendix 2 to this NZ SRE 2410 contains examples of analytical procedures the auditor may consider when performing a review of the financial statements.

- (f) Reading the financial statements and considering whether anything has come to the auditor's attention that causes the auditor to believe that the financial statements are not in accordance with the applicable financial reporting framework. (Ref: Para. 17)

A21. The auditor may perform many of the review procedures before or simultaneously with the entity's preparation of the financial statements. For example, it may be practicable to update the understanding of the entity and its environment, including its internal control, and begin reading applicable minutes before the end of the period. Performing some of the review procedures earlier in the period also permits early identification and consideration of significant accounting matters affecting the financial statements. (Ref: Para. 17)

A22. The auditor performing a review of the financial statements is also the auditor of the annual financial statements of the entity. For convenience and efficiency, the auditor may decide to perform certain audit procedures concurrently with the review of the financial statements. For example, information gained from reading the minutes of meetings of the board of directors in connection with the review of the financial statements may also be used for the annual audit. The auditor may decide also to perform, at the time of the review, auditing procedures that would need to be performed for the purpose of the audit of the annual financial statements, for example, performing auditing procedures on:

- (a) significant or unusual transactions that occurred during the period, such as business combinations, restructurings, or significant revenue transactions, or
- (b) opening balances (when applicable). (Ref: Para. 17)

A23. A review of financial statements ordinarily does not require corroborating the enquiries about litigation or claims. It is, therefore, ordinarily not necessary to send an enquiry letter to the entity's lawyer. Direct communication with the entity's lawyer with respect to litigation or claims, or alternative procedures, may, however, be appropriate if a matter comes to the auditor's attention that causes the auditor to question whether the financial statements are in accordance with the applicable financial reporting framework. (Ref: Para. 17)

A24. The auditor may obtain evidence that the financial statements agree or reconcile with the underlying accounting records by tracing the financial statements to:

- (a) the accounting records, such as the general ledger, or a consolidating schedule that agrees or reconciles with the accounting records; and
- (b) other supporting data in the entity's records as necessary. (Ref: Para. 18)

A25. The auditor need not perform procedures to identify events occurring after the date of the review report. (Ref: Para. 19)

A26. Events or conditions which may cast significant doubt on the entity's ability to continue as a going concern may have existed at the date of the annual financial statements, or may be identified as a result of enquiries of management or in the course of performing other review procedures. When such events or conditions come to the auditor's attention, the auditor needs to enquire of those charged with governance as to their



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plans for future action, such as their plans to liquidate assets, borrow money or restructure debt, reduce or delay expenditures, or increase capital. The auditor needs to enquire also as to the feasibility of the plans of those charged with governance and whether they believe that the outcome of these plans will improve the situation. Ordinarily, the auditor considers, based on procedures performed, whether it is necessary to corroborate the feasibility of the plans of those charged with governance and whether the outcome of these plans will improve the situation. (Ref: Para. 20)

- A27. For example, if the auditor's review procedures lead the auditor to question whether a significant sales transaction is recorded in accordance with the applicable financial reporting framework, the auditor performs additional procedures sufficient to resolve the auditor's questions, such as discussing the terms of the transaction with senior marketing and accounting personnel or reading the sales contract. (Ref: Para. 21)

#### **Comparatives – First Financial Statements (Ref: Para. 22)**

- A28. When comparative information is included in the first financial statements and the auditor is unable to obtain sufficient appropriate review evidence to achieve the review objective, a limitation on the scope of the review exists and the auditor needs to modify the review report. Ordinarily, a restriction on the scope of the auditor's work will result in a qualified ("except for") conclusion. In such cases, ordinarily an auditor encourages clear disclosure in the financial statements, that the auditor has been unable to review the comparatives. An example of a modified review report is included in Appendix 3. ISA (NZ) 510<sup>3</sup> includes illustrative examples that may be useful in circumstances when the comparative information has not been audited or reviewed.

**Commented [MP42]:** Deleted this example based on AUASB decision to remove, so suggest move ref to 510 that was included in A44 here rather – this was what it intended to replace.

- A29. When comparative information is included in the first financial statements and the auditor believes a material adjustment should be made to the financial statements, under paragraph 41, the auditor needs to modify the review report.
- A30. When an entity has come into existence only within the first financial reporting period, comparative information will not be provided in the first financial statements and no modified review report is required.
- A31. New Zealand Equivalent to International Accounting Standard 1 *Presentation of Financial Statements* provides requirements and explanatory guidance relating to comparative information included in financial statements prepared in accordance with New Zealand Accounting Standards. New Zealand Equivalent to International Financial Reporting Standards 1 *First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards* provides requirements and guidance relating to comparative information when an entity adopts New Zealand Equivalents to International Financial Reporting Standards for the first time.

#### **Evaluation of Misstatements (Ref: Para. 23)**

- A32. A review of the financial statements, in contrast to an audit engagement, is not designed to obtain reasonable assurance that the financial statements are free from material misstatement. However, misstatements which come to the auditor's attention, including inadequate disclosures, need to be evaluated individually and in the aggregate to determine whether a material adjustment is required to be made to the financial

<sup>3</sup> ISA (NZ) 510 Initial Audit Engagements - Opening Balances

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statements for them to be prepared, in all material respects, in accordance with the applicable financial reporting framework.

A33. The auditor needs to exercise professional judgement in evaluating the materiality of any misstatements that the entity has not corrected. Ordinarily, the auditor considers matters such as the nature, cause and amount of the misstatements, whether the misstatements originated in the preceding year or current year, and the potential effect of the misstatements on future interim or annual periods.

A34. The auditor may designate an amount below which misstatements need not be aggregated, because the auditor expects that the aggregation of such amounts clearly would not have a material effect on the financial statements. In so doing, under paragraph 16, the auditor needs to consider the fact that the determination of materiality involves quantitative as well as qualitative considerations and that misstatements of a relatively small amount could nevertheless have a material effect on the financial statements.

#### Written Representations

A35. The auditor needs to endeavour to obtain additional representations as are appropriate to matters specific to the entity's business or industry. An illustrative representation letter is set out in Appendix 1. (Ref: Para. 24)

#### Auditor's Responsibility for Other Information

A36. ~~An Auditor~~ conducting a review engagement under this review standard ~~are is not~~ required to comply with ISA (NZ) 720 (Revised)<sup>4</sup>, however ISA (NZ) 720 (Revised) includes guidance which may be useful. ISA (NZ) 720 (Revised) requires ~~an auditor~~ to read the other information that accompanies the financial statements to consider whether there is a material inconsistency with the financial statements. If the auditor identifies a material inconsistency, the auditor needs to consider whether the financial statements or the other information needs to be amended. If an amendment is necessary in the financial statements and those charged with governance refuse to make the amendment, the auditor needs to consider the implications for the review report. If an amendment is necessary in the other information and those charged with governance refuse to make the amendment, the auditor may consider including an Other Information paragraph in the review report and ~~describes~~ the material misstatement. For example, those charged with governance may present alternative measures of earnings that more positively portray financial performance than the financial statements, and such alternative measures are given excessive prominence, or are not clearly defined, or not clearly reconciled to the financial statements such that they are confusing and potentially misleading. (Ref: Para. 26)

A37. While reading the other information for the purpose of identifying material inconsistencies, an apparent material misstatement of fact may come to the auditor's attention (that is, information, not related to matters appearing in the financial statements, that is incorrectly stated or presented). When discussing the matter with the entity's management, ordinarily the auditor considers the validity of the other information and management's responses to the auditor's enquiries, whether valid differences of judgement or opinion exist and whether to request management to

**Commented [MP43]:** Suggested by Deloitte

**Commented [MP44]:** Deloitte suggest describe? Or is it describing? The auditor may consider ...and describing the material misstatement

<sup>4</sup> ISA (NZ) 720 (Revised) *The Auditor's Responsibilities Relating to Other Information*

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consult with a qualified third party to resolve the apparent misstatement of fact. If an amendment is necessary to correct a material misstatement of fact and management refuses to make the amendment, ordinarily the auditor considers taking further action as appropriate, such as notifying those charged with governance and, if necessary, considering the implications for the review report. ISA (NZ) 720 (Revised) includes guidance which may be helpful. (Ref: Para. 27)

### **Communication**

- A38. Communications with management and/or those charged with governance are made as soon as practicable, either orally or in writing. The auditor's decision whether to communicate orally or in writing ordinarily is affected by factors such as the nature, sensitivity and significance of the matter to be communicated and the timing of the communications. If the information is communicated orally, under paragraph 545, the auditor needs to document the communication. (Ref: Para. 29, 31)
- A39. The determination of which level of management may also be informed is affected by the likelihood of collusion or the involvement of a member of management. (Ref: Para. 31)
- A40. Law or regulation may restrict the auditor's communication of certain matters with management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report identified or suspected non-compliance with laws and regulation to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the auditor may be complex and the auditor may consider it appropriate to obtain legal advice. ISA (NZ) 250 (Revised) includes guidance which may be helpful.<sup>5</sup> (Ref: Para 31)
- A41. As a result of performing a review of financial statements, the auditor may become aware of matters that in the opinion of the auditor are both important and relevant to those charged with governance in overseeing the financial reporting and disclosure process. (Ref: Para. 32)

### **Reporting the Nature, Extent and Results of the Review of Financial Statements (Ref: Para. 33-51)**

- A42. Appendix 3 contains illustrations of the auditor's review reports incorporating the elements in paragraphs 33 to 51. With the exception of the Conclusion and Basis for Conclusion sections, this review standard does not establish requirements for ordering the elements of the auditor's review report. However, this review standard requires the use of specific headings, which are intended to assist in making reports more consistent and recognisable.
- A43. Paragraph 34(f)(i) includes the conclusion required for review of financial statements prepared under a fair presentation framework and a compliance framework. In some cases, law or regulation governing the review of financial statements may prescribe wording for the auditor's conclusion that is different from the wording described in paragraph 34(f). Although the auditor may be obliged to use the prescribed wording,

**Commented [MP45]:** Deloitte suggestion – should link to documentation section. Not hyperlinked as cannot get back.

**Commented [MP46]:** Suggest add by Deloitte

<sup>5</sup> ISA (NZ) 250 (Revised) *Consideration of Laws and Regulations in an Audit of Financial Statements*.

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the auditor's responsibilities as described in this NZ SRE 2410 for coming to the conclusion remain the same. ISA (NZ) 700 (Revised) includes guidance which may be helpful.<sup>6</sup> Illustrative auditor's review reports are set out in Appendix 3.

**Commented [MP47]:** Is this superfluous as this is stated in first sentence of A42?

### Departure from the Applicable Financial Reporting Framework (Ref: Para. 41–42)

- A44. ISA (NZ) 705<sup>7</sup> and ISRE (NZ) 2400<sup>8</sup> includes guidance that may be useful when issuing a modified conclusion. ~~ISA (NZ) 510<sup>9</sup> includes illustrative examples that may be useful in circumstances when the comparative information has not been audited or reviewed.~~
- A45. If matters have come to the auditor's attention that cause the auditor to believe that the financial statements are or may be materially affected by a departure from the applicable financial reporting framework, and those charged with governance do not correct the financial statements, the auditor needs to modify the review report. If the information that the auditor believes is necessary for adequate disclosure is not included in the financial statements, the auditor needs to modify the review report and, if practicable, include the necessary information in the review report. Illustrative auditor's review reports with a qualified conclusion are set out in Appendix 3.
- A46. Departures from the applicable financial reporting framework, may result in an adverse conclusion. An illustrative auditor's review report with an adverse conclusion is set out in Appendix 3.

### Limitation on Scope (Ref: Para. 43)

- A47. Ordinarily, a limitation on scope prevents the auditor from completing the review.

### Limitation on Scope Imposed by Management

- A48. The auditor needs to refuse to accept an engagement to review financial statements if the auditor's preliminary knowledge of the engagement circumstances indicates that the auditor would be unable to complete the review because there will be a limitation on the scope of the auditor's review imposed by management of the entity. (Ref: Para. 44)
- A49. If, after accepting the engagement, management imposes a limitation on the scope of the review, the auditor needs to request the removal of that limitation. If management refuses to do so, the auditor is unable to complete the review and express a conclusion. In such cases, the auditor needs to communicate, in writing, to the appropriate level of management and those charged with governance, the reason(s) why the review cannot be completed. Nevertheless, if a matter comes to the auditor's attention that causes the auditor to believe that a material adjustment to the financial statements is necessary for the financial statements to be prepared, in all material respects, in accordance with the applicable financial reporting framework, under paragraphs 28, 29 and 31, the auditor needs to communicate such matters to the appropriate level of management and, where appropriate, those charged with governance. (Ref: Para. 45)
- A50. The auditor needs to consider the legal and regulatory requirements, including whether there is a legal requirement for the auditor to issue a report. If there is such a

<sup>6</sup> ISA (NZ) 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*.

<sup>7</sup> ISA (NZ) 705 (Revised) *Modifications to the Opinion in the Independent Auditor's Report*

<sup>8</sup> ISRE (NZ) 2400 *Review of Historical Financial Statements Performed by an Assurance Practitioner*

<sup>9</sup> ~~ISA (NZ) 510 *Initial Audit Engagements – Opening Balances*~~

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requirement, the auditor needs to disclaim a conclusion and provide in the review report the reason why the review cannot be completed. However, if a matter comes to the auditor's attention that causes the auditor to believe that a material adjustment to the financial statements is necessary for the financial statements to be prepared, in all material respects, in accordance with the applicable financial reporting framework the auditor needs to communicate such a matter in the report. (Ref: Para. 46)

### Other Limitations on Scope Not Imposed by Management (Ref: Para. 48)

A51. A limitation on scope may occur due to circumstances other than a limitation on scope imposed by management or those charged with governance. In such circumstances, the auditor is ordinarily unable to complete the review and express a conclusion, and is guided by paragraphs 48 and 51. There may be, however, some rare circumstances where the limitation on the scope of the auditor's work is clearly confined to one or more specific matters that, while material, are not in the auditor's judgement pervasive to the financial statements. In such circumstances, the auditor needs to modify the auditor's review report by indicating that, except for the effects of the matter which is described in the Basis for Qualified Conclusion paragraph section of the auditor's review report, the review was conducted in accordance with this NZ SRE 2410, and by qualifying the conclusion. Illustrative auditor's review reports with a qualified conclusion are set out in Appendix 3.

**Commented [MP48]:** Deloitte submission suggestion.

A52. The auditor may have expressed a qualified opinion on the audit of the latest annual financial statements because of a limitation on the scope of that audit. The auditor needs to consider whether that limitation on scope still exists and, if so, the implications for the review report.

### Going Concern and a Material Uncertainty Exists (Ref: Para. 49-51)

A53. The auditor may have alerted users to the existence of a material uncertainty relating to an event or condition that casts significant doubt on the entity's ability to continue as a going concern by adding an emphasis of matter paragraph a separate section under the heading "Material Uncertainty Related to Going Concern" to a prior audit or review report. If the material uncertainty still exists and adequate disclosure is made in the financial statements, the auditor needs to continue to alert users by adding a separate section under the heading "Material Uncertainty Related to Going Concern" paragraph to highlight the continued material uncertainty.

**Commented [MP49]:** KPMG suggests adding an EOM or MURGC to a prior...

The new audit report with the updated heading has been in effect for a while now, while the previous year EOM may have been in the review report this will not be the case for the audit and only occurs in the transition to the new heading, streamline by updating it once otherwise it may be confusing going forward.

**Commented [MP50]:** New language is a section not a paragraph – check consistency throughout. Suggest this change to make language consistent with para 49

A54. If, as a result of enquiries or other review procedures, a material uncertainty relating to an event or condition comes to the auditor's attention that casts significant doubt on the entity's ability to continue as a going concern, and adequate disclosure is made in the financial statements, the auditor alerts users to the existence of a material uncertainty related to going concern in a separate section. ISA (NZ) 570 (Revised) *Going Concern* provides information that the auditor may find helpful in considering going concern in the context of the review engagement.

**Commented [MP51]:** CPA recommends reference is made as guidance when reviewing management's assessment of the entity's ability to continue as a going concern.

Is this sufficient here?

### Other Considerations

A55. The terms of the engagement include agreement by those charged with governance that, where any document containing the financial statements indicates that the financial statements have been reviewed by the entity's auditor, the review report will be also included in the document. If those charged with governance have not included the review report in the document, ordinarily the auditor considers seeking legal advice to

assist in determining the appropriate course of action in the circumstances. (Ref: Para. 12)

- A56. If the auditor has issued a modified review report and those charged with governance issue the financial statements without including the modified review report in the document containing the financial statements, ordinarily the auditor considers seeking legal advice to assist in determining the appropriate course of action in the circumstances, and the possibility of resigning from the appointment to audit the annual financial statements.

#### *Considerations Specific to Public Sector Entities*

- A57. The auditor needs to communicate the terms of engagement to the entity subject to the review. When communicating the terms of engagement, an engagement letter helps to avoid misunderstandings regarding the nature of the engagement and, in particular, the objective and scope of the review, the responsibilities of those charged with governance, the extent of the auditor's responsibilities, the assurance obtained, and the nature and form of the report. Law or regulation governing review engagements in the public sector ordinarily mandates the appointment of the auditor. Nevertheless, an engagement letter setting out the matters referred to in paragraph A8 may be useful to both the public sector auditor and the entity subject to the review. Public sector auditors, therefore, consider communicating the terms of a review engagement by way of an engagement letter<sup>10</sup>. (Ref: Para. 12)

Commented [MP52]: Suggest we delete this footnote

- A58. In the public sector, the auditor's statutory audit obligation may extend to other work, such as a review of interim financial information. Where this is the case, the public sector auditor cannot avoid such an obligation and, consequently, may not be in a position not to accept, or to withdraw from a review engagement. The public sector auditor also may not be in the position to resign from the appointment to audit the annual financial statements. (Ref: Para. 30(b)-30(c))

- A59. The auditor needs to communicate to those charged with governance and consider the implications for the review when a matter comes to the auditor's attention that causes the auditor to believe in the existence of fraud or actual or suspected non-compliance by the entity with laws and regulations. In the public sector, the auditor may be subject to statutory or other regulatory requirements to report such a matter to regulatory or other public authorities. (Ref: Para. 32)

Commented [MP53]: Consider adding actual or suspected

#### **Documentation** (Ref: Para. 55)

- A60. The auditor needs to prepare documentation that enables an experienced auditor having no previous connection with the engagement to understand the nature, timing and extent of the enquiries made and analytical and other review procedures applied, information obtained, and any significant matters considered during the performance of the review, including the disposition of such matters.

<sup>10</sup> Paragraphs A57-A59 are a reproduction of the AUASB's standard. The External Reporting Board does not have the statutory mandate to formulate auditing and assurance standards for public sector entities, and does not intend this guidance to have mandatory effect. New Zealand amendments have been made to align the text with the New Zealand legal position.

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### Appendix 1

(Ref: Para. A8)

#### Example of an Engagement Letter For A Review of Financial Statements

The following letter is to be used as a guide in conjunction with the requirements outlined in paragraph 12-13 of this NZ SRE 2410 and will need to be adapted according to individual requirements and circumstances.

To [those charged with governance:<sup>11</sup>]

You have requested that we review the interim financial statements of [name of entity], which comprises the statement of financial position as at 31 December 20XX, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the six-month period ended on that date, and notes comprising significant accounting policies and other explanatory information. We are pleased to confirm our acceptance and our understanding of the terms and objectives of our engagement by means of this letter.

Our review will be conducted in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*, issued by the New Zealand Auditing and Assurance Standards Board, with the objective of providing us with a basis for reporting whether anything has come to our attention that causes us to believe that the interim financial statements are not prepared, in all material respects, in accordance with the [indicate applicable financial reporting framework, including a reference to the jurisdiction or country of origin of the financial reporting when New Zealand is not the origin of the financial reporting framework]. Such a review consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures and does not, ordinarily, require corroboration of the information obtained. The scope of a review of the financial statements is substantially less than the scope of an audit conducted in accordance with International Standards on Auditing (New Zealand) whose objective is the expression of an opinion regarding the financial statements and consequently does not enable us to obtain assurance that we might identify in an audit. Accordingly, we shall express no such opinion. NZ SRE 2410 requires us to also comply with the ethical requirements relevant to the audit of the annual financial statements of the entity.

We expect to report on the interim financial statements as follows:

[Include text of sample review report - see Appendix 3 as appropriate.]

The directors [those charged with governance<sup>12</sup>] of the [type of entity] are responsible for the preparation of the interim financial statements in accordance with generally accepted accounting practice in New Zealand and that gives a true and fair view of the matters to which they relate and for such internal control as the directors [those charged with governance] determine is necessary to enable the preparation of the interim financial statements that are free from material misstatement, whether due to fraud or error. As part of our review, we shall request written representations from those charged with governance concerning assertions made in connection with the review. We shall also request that where any document containing the interim financial statements indicates that the interim financial statements have been reviewed, our review report will also be included in the document.

<sup>11</sup> Insert the appropriate term, such as "Directors" or "Board of Management".

<sup>12</sup> Insert the appropriate term, such as "Directors or Board of Management".

The directors [those charged with governance] of the [entity] acknowledge and understand they have responsibility to provide us with:

- i. access to information relevant to the preparation of the financial statements;
- ii. additional information that we may request for the purposes of the review engagement; and
- iii. unrestricted access to persons from whom we determine it is necessary to obtain evidence.

A review of the interim financial statements does not provide assurance that we shall become aware of all significant matters that might be identified in an audit. Further, our engagement cannot be relied upon to disclose whether fraud or errors, or illegal acts exist. However, we shall inform you of any material matters that come to our attention.

### **Fees**

[Insert additional information here regarding fee arrangements and billings, as appropriate.]

We look forward to full co-operation with your staff and we trust that they will make available to us whatever records, documentation and other information are requested in connection with our review.

[This letter will be effective for future years unless it is terminated, amended or superseded.<sup>13</sup>]

Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the arrangements for our review of the interim financial statements.

Yours faithfully,

(signed)

.....

Name and Title

Date

Acknowledged on behalf of [entity] by

(signed)

.....

Name and Title

Date

---

<sup>13</sup> Use if applicable.



### Example of a Representation Letter

The following letter is not intended to be a standard letter. It is to be used as a guide only and will need to be adapted according to individual requirements and circumstances.

Representations by those charged with governance will vary from one entity to another and from one period to the next. Representation letters are ordinarily useful where evidence, other than that obtained by enquiry, may not be reasonably expected to be available or when those charged with governance have made oral representations which the auditor wishes to confirm in writing.

[Entity Letterhead]

[Addressee – Auditor]

[Date]

This representation letter is provided in connection with your review of the interim financial statements of [name of entity] for the [period] ended [date], for the purpose of you expressing a conclusion as to whether anything has come to your attention that causes you to believe that the interim financial statements are not, in all material respects, presented fairly in accordance with [applicable financial reporting framework<sup>14</sup>].

We acknowledge our responsibility for ensuring that the interim financial statements are in accordance with [applicable financial reporting framework].

We confirm that the interim financial statements are prepared and presented fairly in accordance with [applicable financial reporting framework] and are free of material misstatements, including omissions].

We confirm, to the best of our knowledge and belief, the following representations made to you during your review.

[Include representations required by this NZ SRE 2410 (paragraph 24) and those relevant to the entity. Such representations may include the following examples.]

1. We have made available to you:
  - (a) all financial records and related data, other information, explanations and assistance necessary for the conduct of the review; and
  - (b) minutes of all meetings of [shareholders, directors, committees of directors, Boards of Management].
2. We have disclosed to you the results of our assessment of the risk that the [interim financial statements] may be materially misstated as a result of fraud.
3. There:
  - (a) has been no fraud or suspected fraud, error or non-compliance with laws and regulations involving management or employees who have a significant role in the internal control structure;
  - (b) has been no fraud or suspected fraud, error or non-compliance with laws and regulations that could have a material effect on the financial statements; and

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<sup>14</sup> Specify the applicable financial reporting framework requirements.

- (c) have been no communications from regulatory agencies concerning non-compliance with, or deficiencies in, financial reporting practices that could have a material effect on the financial statements.
- 4. We are responsible for an adequate internal control structure to prevent and detect fraud and error and to facilitate the preparation of reliable financial statements. We confirm that adequate accounting records have been maintained and that all material transactions have been recorded properly in the accounting records underlying the financial statements.
- 5. We have no plans or intentions that may affect materially the carrying values, or classification, of assets and liabilities.
- 6. We have considered the requirements of New Zealand Equivalents to International Accounting Standard 36 Impairment of Assets, when assessing the impairment of assets and in ensuring that no assets are stated in excess of their recoverable amount.
- 7. We believe the effects of uncorrected misstatements summarised in the accompanying schedule are immaterial, both individually and in the aggregate, to the [interim] financial statements taken as a whole.
- 8. The following have been recorded and/or disclosed properly in the [interim] financial statements:
  - (a) related party transactions and related amounts receivable or payable, including sales, purchases, loans, transfers, leasing arrangements and guarantees (written or oral);
  - (b) share options, warrants, conversions or other requirements;
  - (c) arrangements involving restrictions on cash balances, compensating balances and line-of-credit or similar arrangements;
  - (d) agreements to repurchase assets previously sold;
  - (e) material liabilities or contingent liabilities or assets including those arising under derivative financial instruments;
  - (f) all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements in accordance with the applicable financial reporting framework.
- 9. We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
- 10. The entity has satisfactory title to all assets, and there are no liens or encumbrances on such assets that have not been disclosed nor has any asset been pledged as collateral. Allowances for depreciation have been adjusted for all important items of property, plant and equipment that have been abandoned or are otherwise unusable.
- 11. The entity has complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of non-compliance.
- 12. There were no material commitments for construction or acquisition of property, plant and equipment or to acquire other non-current assets, such as investments or intangibles, other than those disclosed in the financial statements.

13. We have no plans to abandon lines of product or other plans or intentions that will result in any excess or obsolete inventory, and no inventory is stated at an amount in excess of net realisable value.
14. No events have occurred subsequent to the balance sheet date through to the date of this letter that would require adjustment to, or disclosure in, the [interim financial statements].

We understand that your examination was made in accordance with NZ SRE 2410 and was, therefore, designed primarily for the purpose of expressing a conclusion on the interim financial statements of [the entity], and that your procedures were limited to those which you considered necessary for that purpose.

Yours faithfully

[Name of signing officer and title]

Notes:

*[The above example representation letter may need to be amended in certain circumstances. The following illustrate some of those situations.]*

(a) Exceptions

Where matters are disclosed in the financial statements, the associated representation needs to be amended, for example:

- If a subsequent event has been disclosed, Item 14 (above) could be modified to read:  
“Except as discussed in Note X to the financial statements, no events have occurred .....”
- If the entity has plans that impact the carrying values of assets and liabilities, Item 5 (above) could be modified to read:  
“The entity has no plans or intentions that may materially affect the carrying value or classification of assets and liabilities, except for our plan to dispose of segment X, as disclosed in note Y in the financial statements, which is discussed in the minutes of the meeting of the governing body<sup>15</sup> held on [date]”.

(b) Other Required Information

Certain entities may be required to include other information in the interim financial statements, for example, performance indicators for government entities. In addition to identifying this information and the applicable financial reporting framework in paragraphs 1 and 2 of the example representation letter, an additional paragraph similar to the following may be appropriate:

“The disclosures of key performance indicators have been prepared and presented in conformity with [relevant statutory requirements] and we consider the indicators reported to be relevant to the stated objectives of the [entity]”.

(c) Opinions and Representation in the Notes to the Financial Statements

Where the notes to the interim financial statements include opinions and representations by those charged with governance, such matters may be addressed in the representation

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<sup>15</sup> Insert the appropriate term, such as “Directors or Board of Management”.

letter. For example, notes relating to the anticipated outcome of litigation, the intent and ability to hold long-term securities to maturity and plans necessary to support the going concern basis.

(d) Environmental Matters

In situations where there are environmental matters that may, but probably will not, require an outflow of resources, this may be reflected in an addition to Item 9 (above), for example:

“However, the [entity] has received an abatement notice from a local authority or an enforcement order from the Environmental Court that may result in clean up or other costs for the [name] waste disposal site. This matter has been disclosed in Note A in the financial statements and we believe that the disclosure and estimated contingent loss is reasonable based on available information.”

(e) Compliance

If, as part of the review, the auditor is required also to report on the entity’s compliance with laws and regulations, a representation may be appropriate acknowledging that those charged with governance are responsible for the entity’s compliance with applicable laws and regulations and that the requirements have been met. For example, the following paragraph may be added:

“The financial records of the [company, registered scheme or disclosing entity] have been kept so as to be sufficient to enable financial statements to be prepared and reviewed, and other records and registers required by the [applicable legislation] have been kept properly and are up-to-date.”

(f) Other Matters

Additional representations that may be appropriate in specific situations may include the following:

- Justification for a change in accounting policy.
- The work of a management expert has been used.
- Arrangements for controlling the dissemination of the financial statements and review report on the Internet.

## Appendix 2

(Ref: Para. A20)

**Commented [MP54]:** Deloitte suggestion for AUASB to expand Appendix 2 for NOCLAR. NZ SRE appendix 2 differs from AUASB in that it only deals with ARP, AUASB is detailed procedures more generally. Don't suggest we update this.

### Analytical Procedures the Auditor May Consider When Performing a Review of Financial Statements

The analytical procedures carried out in a review of the financial statements are determined by the auditor's judgement. The procedures listed below are for illustrative purposes only. It is not intended that all the procedures suggested apply to every review engagement. This Appendix is not intended to serve as a programme or checklist in the conduct of a review.

Examples of analytical procedures the auditor may consider when performing a review of the financial statements include the following:

- Comparing the financial statements with the financial statements of the immediately preceding period, with the financial statements of the corresponding period of the preceding financial year, with the financial statements that was expected by management for the current period, and with the most recent audited annual financial statements.
- Comparing the current financial statements with anticipated results, such as budgets or forecasts. For example, comparing sources of revenue and the cost of sales in the current financial statements with corresponding information in:
  - (a) budgets, including expected gross margin(s); and
  - (b) financial information for prior periods.
- Comparing the current financial statements with relevant non-financial information.
- Comparing the recorded amounts, or ratios developed from recorded amounts, to expectations developed by the auditor. The auditor develops such expectations by identifying and applying relationships that reasonably are expected to exist based on the auditor's understanding of the entity and of the industry in which the entity operates.
- Comparing ratios and indicators for the current period with those of entities in the same industry.
- Comparing relationships among elements in the current financial statements with corresponding relationships in the financial statements of prior periods, for example, expense by type as a percentage of sales, assets by type as a percentage of total assets, and percentage of change in sales to percentage of change in receivables.
- Comparing disaggregated data. The following are examples of how data may be disaggregated:
  - (a) by period, for example, revenue or expense items disaggregated into quarterly, monthly, or weekly amounts;
  - (b) by product line or source of revenue;
  - (c) by location, for example by component;
  - (d) by attributes of the transaction, for example, revenue generated by designers, architects, or craftsmen; and
  - (e) by several attributes of the transaction, for example, sales by product and month.

### Appendix 3

(Ref: Para. A42)

#### Illustrations of Review Reports—Unmodified and Modified Conclusions

Example of an Unmodified Auditor's Review Report on Financial Statements

Example of an Auditor's Review Report with a Qualified Conclusion (Except For) for a Departure from the Applicable Financial Reporting Framework

Example of an Auditor's Review Report with a Qualified Conclusion for a Limitation On Scope Not Imposed by Management

Example of an Auditor's Review Report with an Adverse Conclusion for a Departure from the Applicable Financial Reporting Framework

## Example of an Unmodified Auditor's Review Report on Financial Statements

For purposes of this illustrative report, it is assumed that the auditor has reviewed the interim financial statements of a FMC reporting entity considered to have higher level of public accountability.

### INDEPENDENT AUDITOR'S REVIEW REPORT

To [Appropriate Addressee]

#### Report on the Review of the [appropriate title for the Financial Statements] Financial Statements<sup>16</sup>

##### Conclusion

We have reviewed the accompanying [period] financial statements of [name of entity], which comprise the statement of financial position as at [date], and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the [period] ended on that date, and a summary of significant accounting policies and other explanatory information.

Based on our review, which is not an audit, nothing has come to our attention that causes us to believe that these accompanying [period] financial statements of [name of entity] do not present fairly, in all material respects, [or "give a true and fair view of"<sup>17</sup>] the financial position of the [entity] as at [date], and of its financial performance and its cash flows for the [period] ended on that date, in accordance with [applicable financial reporting framework]<sup>18</sup>.

or

Based on our review, which is not an audit, nothing has come to our attention that causes us to believe that these accompanying [period] financial statements of [name of entity] are not prepared, in all material respects, in accordance with [applicable financial reporting framework]<sup>19</sup>.

##### Basis for Conclusion

We conducted our review in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*. Our responsibilities are further described in the *Auditor's Responsibilities for the Review of the Financial Statements* section of our report. We are independent of the [entity] in accordance with the relevant ethical requirements in New Zealand relating to the audit of the annual financial statements, and we have fulfilled our other ethical responsibilities in accordance with these ethical requirements relevant to the audit of the annual financial statements. Other than in our capacity as assurance practitioner we have no relationship with, or interests in, [name of entity].

[Title of those charged with governance] Responsibility for the [period] Financial Statements

The [title of those charged with governance] of the [type of entity] are responsible, on behalf of the [entity], for the preparation [and fair presentation] of the [period] financial statements in accordance with the [applicable financial reporting framework] and for such internal control as the directors [those charged with governance] determine is necessary to enable the

**Commented [MP55]:** Bradbury submission to NZAuASB suggest simplification of the language in the report.

**Commented [MP56]:** KPMG submission to AUASB suggests including footnote consistent with illustrative examples in ISA (NZ) 700

**Commented [MP57]:** KPMG submission – notes that the word accompanying in ISA 700 is in the opinion paragraph. Recommend aligning.

**Commented [MP58]:** KPMG submission to AUASB – not in requirements. Also not consistent with ISRE 2400 so recommend delete. Also suggested by Bradbury.

**Commented [MP59]:** Bradbury suggests deleting "Further" ?

**Commented [MP60]:** Streamline and make consistent with para 35© and consistent through all illustrations.

**Commented [MP61]:** Bradbury suggest separating these sentences.

**Commented [MP62]:** Bradbury suggests deleting these words using Plain English. This was added by the NZAuASB throughout the NZ standards.

**Commented [MP63]:** Suggested by Bradbury

<sup>16</sup> The sub-title "Report on the Review of the [Financial Statements]" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

<sup>17</sup> ISA (NZ) 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*, contains information on the wording of reports that may be helpful.

<sup>18</sup> This conclusion is appropriate where a fair presentation framework has been used.

<sup>19</sup> This conclusion is appropriate where a compliance framework has been used.

preparation *[and fair presentation]* of the [period] financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, [those charged with governance] are responsible on behalf of the entity for assessing the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless [those charged with governance] either intend to liquidate the entity or to cease operations, or have no realistic alternative but to do so.

#### *Auditor's Responsibilities for the Review of the Financial Statements*

Our responsibility is to express a conclusion on the [period] financial statements based on our review. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the [period] financial statements, taken as a whole, are not prepared in all material respects, in accordance with the [applicable financial reporting framework].

A review of [period] financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. We perform procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently does not enable us to obtain assurance that we might identify in an audit. Accordingly, we do not express an audit opinion on those [period] financial statements.

Based on the review procedures performed, we conclude whether anything has come to our attention that causes us to believe that the use of the going concern basis of accounting by [those charged with governance] is not appropriate and whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If a matter comes to our attention that causes us to believe that a material uncertainty related to going concern exists, we are required to draw attention in our review report to the related disclosures in the [period] financial statements or, if such disclosures are inadequate, to modify our conclusion. Our conclusions are based on the procedures performed up to the date of the review report. However, future events or conditions may cause the entity to cease to continue as a going concern.

#### **Report on Other Legal and Regulatory Requirements**

[Form and content of this section of the review report will vary depending on the nature of the auditor's other reporting responsibilities.]

The engagement partner on the review resulting in this independent auditor's review report is [name].

[Auditor's signature]<sup>20</sup>

[Date of the review report]<sup>21</sup>

[Auditor's address]

<sup>20</sup> The auditor's review report is required to be signed in one or more of the name of the audit firm, the name of the audit company or the personal name of the auditor, as appropriate.

<sup>21</sup> The date of the auditor's review report is the date the auditor signs the report.

**Commented [MP64]:** Bradbury suggests deleting. Added by NZAuASB throughout NZ standards.

**Commented [MP65]:** Bradbury suggests "and make appropriate disclosures"

**Commented [MP66]:** Bradbury suggests using bullet points here to use plain English.  
The firms will use discretion in formatting when preparing their own reports but could improve the illustrations? This is not done in ISRE (NZ) 2400.

**Commented [MP67]:** Bradbury suggests deleting



## Example of an Auditor's Review Report with a Qualified Conclusion (Except For) For a Departure From the Applicable Financial Reporting Framework

### INDEPENDENT AUDITOR'S REVIEW REPORT

[Appropriate Addressee]

#### Report on the Review of [appropriate title for the financial statements]<sup>22</sup> ~~Financial Statements~~

##### *Qualified Conclusion*

We have reviewed the ~~accompanying~~ [period] financial statements of [name of entity], which comprise the statement of financial position as at [date], and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the [period] ended on that date, and a summary of significant accounting policies and other explanatory information.

Based on our review, ~~which is not an audit~~, with the exception of the matter described in the *Basis for Qualified Conclusion* section of our report, nothing has come to our attention that causes us to believe that these ~~accompanying~~ [period] financial statements of [name of entity] do not present fairly, in all material respects, [or "give a true and fair view of"<sup>23</sup>] the financial position of the [entity] as at [date], and of its financial performance and its cash flows for the [period] period ended on that date, in accordance with [applicable financial reporting framework].<sup>24</sup>

or

Based on our review, ~~which is not an audit~~, with the exception of the matter described in the *Basis for Qualified Conclusion* section of our report, nothing has come to our attention that causes us to believe that these ~~accompanying~~ [period] financial statements of [name of entity] are not prepared, in all material respects, in accordance with [applicable financial reporting framework].<sup>25</sup>

##### *Basis for Qualified Conclusion*

Based on information provided to us by management, [name of entity] has excluded from property and long-term debt certain lease obligations that we believe should be capitalised to conform with [indicate applicable financial reporting framework]. This information indicates that if these lease obligations were capitalised at 31 December 20XX, property would be increased by \$\_\_\_\_\_, long-term debt by \$\_\_\_\_\_, and net income and earnings per share would be increased (decreased) by \$\_\_\_\_\_ and \$\_\_\_\_\_ respectively for the [period] ended on that date.

We conducted our review in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*. Our responsibilities are further described in the *Auditor's Responsibilities for the Review of the Financial Statements* section of our report. We are independent of the [entity] ~~Company~~ in accordance with the relevant ethical requirements in New Zealand relating to the audit of the annual financial statements. ~~As the~~

<sup>22</sup> The sub-title "Report on the Review of the [Financial Statements]" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

<sup>23</sup> ISA (NZ) 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*, contains information on the wording of reports that may be helpful.

<sup>24</sup> This conclusion is appropriate where a fair presentation framework has been used.

<sup>25</sup> This conclusion is appropriate where a compliance framework has been used.

~~auditor of [name of entity], NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements, and we have fulfilled our other ethical responsibilities in accordance with these ethical requirements. Other than in our capacity as assurance practitioner we have no relationship with, or interests in, [name of entity].~~

**Commented [MP68]:** Inconsistent with requirements and reports above. Delete extra wording for consistency.

*[Title of those charged with governance] Responsibility for the [period] Financial Statements*

The [title of those charged with governance] of the [type of entity] are responsible, on behalf of the entity, for the preparation *[and fair presentation]* of the [period] financial statements in accordance with the [applicable financial reporting framework] and for such internal control as the directors [those charged with governance] determine is necessary to enable the preparation *[and fair presentation]* of the [period] financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, [those charged with governance] are responsible on behalf of the entity for assessing the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless [those charged with governance] either intend to liquidate the entity or to cease operations, or have no realistic alternative but to do so.

*Auditor's Responsibilities for the Review of the Financial Statements*

Our responsibility is to express a conclusion on the [period] financial statements based on our review. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the [period] financial statements are not prepared, in all material respects, in accordance with the [applicable financial reporting framework].

A review of [period] financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. We perform procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently does not enable us to obtain assurance that we might identify in an audit. Accordingly, we do not express an audit opinion on those [period] financial statements.

Based on the review procedures performed, we conclude whether anything has come to our attention that causes us to believe that the use of the going concern basis of accounting by [those charged with governance] is not appropriate and whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If a matter comes to our attention that causes us to believe that a material uncertainty related to going concern exists, we are required to draw attention in our review report to the related disclosures in the [period] financial statements or, if such disclosures are inadequate, to modify our conclusion. Our conclusions are based on the procedures performed up to the date of the review report. However, future events or conditions may cause the entity to cease to continue as a going concern.

**Report on Other Legal and Regulatory Requirements**

[Form and content of this section of the review report will vary depending on the nature of the auditor's other reporting responsibilities].

The engagement partner on the review resulting in this independent auditor's review report is [name].

[Auditor's signature]<sup>26</sup>

[Date of the review report]<sup>27</sup>

[Auditor's address]

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<sup>26</sup> The auditor's review report is required to be signed in one or more of the name of the audit firm, the name of the audit company or the personal name of the auditor, as appropriate.

<sup>27</sup> The date of the auditor's review report is the date the auditor signs the report.

**Example of an Auditor's Review Report with a Qualified Conclusion For a Limitation of Scope Not Imposed by Management or Those Charged with Governance**

**INDEPENDENT AUDITOR'S REVIEW REPORT**

To [Appropriate Addressee]

**Report on the Review of [appropriate title for the financial statements]<sup>28</sup> ~~Financial Statements~~**

*Qualified Conclusion*

We have reviewed the ~~accompanying~~ [period] financial statements of [name of entity], which comprises the statement of financial position as at [date], and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the [period] ended on that date, and a summary of significant accounting policies and other explanatory information.

Except for the adjustments to the [period] financial statements that we might have become aware of had it not been for the situation described above, based on our review nothing has come to our attention that causes us to believe that ~~these accompanying~~ [period] financial statements of [name of entity] does not present fairly, in all material respects, [or "give a true and fair view of"<sup>29</sup>] the financial position of the [entity] as at [date], and of its financial performance and its cash flows for the [period] period ended on that date, in accordance with [applicable financial reporting framework].<sup>30</sup>

or

*Except for the adjustments to the [period] financial statements that we might have become aware of had it not been for the situation described above, based on our review, nothing has come to our attention that causes us to believe that ~~these accompanying~~ [period] financial statements of [name of entity] are not prepared, in all material respects, in accordance with [applicable financial reporting framework]*<sup>31</sup>.

*Basis for Qualified Conclusion*

As a result of a fire in a branch office on [date] that destroyed its accounts receivable records, we were unable to complete our review of accounts receivable totalling \$\_\_\_\_\_ included in the [period] financial statements. The [entity] is in the process of reconstructing these records and is uncertain as to whether these records will support the amount shown above and the related allowance for uncollectible accounts. Had we been able to complete our review of accounts receivable, matters might have come to our attention indicating that adjustments might be necessary to the [period] financial statements.

We conducted our review in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*. Our responsibilities are further described in the *Auditor's Responsibilities for the Review of the Financial Statements* section of our report. We are independent of the [entity] ~~Company~~ in accordance with the relevant ethical requirements in New Zealand ~~relating to the audit of the annual financial statements.~~ ~~As the~~

<sup>28</sup> The sub-title "Report on the Review of the [Financial Statements]" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

<sup>29</sup> ISA (NZ) 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*, contains information on the wording of reports that may be helpful.

<sup>30</sup> This conclusion is appropriate where a fair presentation framework has been used.

<sup>31</sup> This conclusion is appropriate where a compliance framework has been used.

~~auditor of [name of entity], NZ SRE 2410 requires that and we fulfilled our other ethical responsibilities in accordance with these ethical requirements relevant to the audit of the annual financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements.~~ Other than in our capacity as assurance practitioner we have no relationship with, or interests in, [name of entity]. *[Title of those charged with governance] Responsibility for the [period] Financial Statements*

The [title of those charged with governance] of the [type of entity] are responsible, on behalf of the entity, for the preparation *[and fair presentation]* of the [period] financial statements in accordance with the [applicable financial reporting framework] and for such internal control as the directors [those charged with governance] determine is necessary to enable the preparation *[and fair presentation]* of the [period] financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, [those charged with governance] are responsible on behalf of the entity for assessing the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless [those charged with governance] either intend to liquidate the entity or to cease operations, or have no realistic alternative but to do so.

#### *Auditor's Responsibilities for the Review of the Financial Statements*

Our responsibility is to express a conclusion on the [period] financial statements based on our review. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the [period] financial statements, taken as a whole, are not prepared, in all material respects, in accordance with the [applicable financial reporting framework].

A review of [period] financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently does not enable us to obtain assurance that we might identify in an audit. Accordingly, we do not express an audit opinion on those [period] financial statements.

Based on the review procedures performed, we conclude whether anything has come to our attention that causes us to believe that the use of the going concern basis of accounting by [those charged with governance] is not appropriate and whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If a matter comes to our attention that causes us to believe that a material uncertainty related to going concern exists, we are required to draw attention in our review report to the related disclosures in the [period] financial statements or, if such disclosures are inadequate, to modify our conclusion. Our conclusions are based on the procedures performed up to the date of the review report. However, future events or conditions may cause the entity to cease to continue as a going concern.

#### **Report on Other Legal and Regulatory Requirements**

[Form and content of this section of the review report will vary depending on the nature of the auditor's other reporting responsibilities.]

The engagement partner on the review resulting in this independent auditor's review report is [name].

[Auditor's signature<sup>32</sup>]

[Date of the review report]<sup>33</sup>

[Auditor's address]

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<sup>32</sup> The auditor's review report is required to be signed in one or more of the name of the audit firm, the name of the audit company or the personal name of the auditor, as appropriate.

<sup>33</sup> The date of the auditor's review report is the date the auditor signs the report. |

## Example of an Auditor's Review Report With an Adverse Conclusion For a Departure From the Applicable Financial Reporting Framework

### INDEPENDENT AUDITOR'S REVIEW REPORT

To [Appropriate Addressee]

#### Report on the Review of [appropriate title for the financial statements]<sup>34</sup> ~~Financial Statements~~

##### *Adverse Conclusion*

We have reviewed the ~~accompanying~~ [period] financial statements of [name of entity], which comprise statement of financial position as at [date], and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the [period] ended on that date, and summary of significant accounting policies and other explanatory information.

Based on our review, ~~which is not an audit~~, because of the significance of the matter described in the *Basis for Adverse Conclusion* section of our report, the ~~accompanying~~ [period] financial statements of [name of entity] do not present fairly, in all material respects, [or "give a true and fair view of<sup>35</sup>"] the financial position of the [entity] as at [date], and of its financial performance and its cash flows for the [period] period ended on that date, in accordance with [applicable financial reporting framework].<sup>36</sup>

or

Based on our review, ~~which is not an audit~~, because of the significance of the matter described in the *Basis for Adverse Conclusion* section of our report, the ~~accompanying~~ [period] financial statements of [name of entity] are not prepared, in all material respects, in accordance with [applicable financial reporting framework]<sup>37</sup>.

##### *Basis for Adverse Conclusion*

As explained in Note X, commencing this period, [title of those charged with governance] of the [entity] ceased to consolidate the financial statements of its subsidiary companies since [title of those charged with governance] considers consolidation to be inappropriate because of the existence of new substantial non-controlling interests. This is not in accordance with [applicable financial reporting framework]. Had consolidated financial statements been prepared, virtually every account in the financial statements would have been materially different. The effects on the financial statements of the failure to consolidate have not been determined.

We conducted our review in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*. Our responsibilities are further described in the *Auditor's Responsibilities for the Review of the Financial Statements* section of our report. We are independent of the ~~Company~~ [entity] in accordance with the relevant ethical requirements in New Zealand ~~relating to the audit of the annual financial statements~~. ~~As the auditor of [name of entity], NZ SRE 2410 requires that we comply with the ethical~~

<sup>34</sup> The sub-title "Report on the Review of the [Financial Statements]" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

<sup>35</sup> ISA (NZ) 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*, contains information on the wording of reports that may be helpful.

<sup>36</sup> This conclusion is appropriate where a fair presentation framework has been used.

<sup>37</sup> This conclusion is appropriate where a compliance framework has been used.

~~requirements relevant to the audit of the annual financial statements~~, and we have fulfilled our other ethical responsibilities in accordance with these requirements. Other than in our capacity as assurance practitioner we have no relationship with, or interests in, [name of entity].

*[Title of those charged with governance] Responsibility for the [period] Financial Statements*

The [title of those charged with governance] of the [type of entity] are responsible, on behalf of the entity, for the preparation *[and fair presentation]* of the [period] financial statements in accordance with the [applicable financial reporting framework] and for such internal control as the directors [those charged with governance] determine is necessary to enable the preparation *[and fair presentation]* of the [period] financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, [those charged with governance] are responsible on behalf of the entity for assessing the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless [those charged with governance] either intend to liquidate the entity or to cease operations, or have no realistic alternative but to do so.

*Auditor's Responsibilities for the Review of the Financial Statements*

Our responsibility is to express a conclusion on the [period] financial statements based on our review. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the [period] financial statements are not prepared, in all material respects, in accordance with the [applicable financial reporting framework].

A review of [period] financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. We perform procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently does not enable us to obtain assurance that we might identify in an audit. Accordingly, we do not express an audit opinion on those [period] financial statements.

Based on the review procedures performed, we conclude whether anything has come to our attention that causes us to believe that the use of the going concern basis of accounting by [those charged with governance] is not appropriate and whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If a matter comes to our attention that causes us to believe that a material uncertainty related to going concern exists, we are required to draw attention in our review report to the related disclosures in the [period] financial statements or, if such disclosures are inadequate, to modify our conclusion. Our conclusions are based on the procedures performed up to the date of the review report. However, future events or conditions may cause the entity to cease to continue as a going concern.

**Report on Other Legal and Regulatory Requirements**

[Form and content of this section of the review report will vary depending on the nature of the auditor's other reporting responsibilities.]

The engagement partner on the review resulting in this independent auditor's review report is [name].



[Auditor's signature<sup>38</sup>]

[Date of the review report]<sup>39</sup>

[Auditor's address]

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<sup>38</sup> The auditor's review report is required to be signed in one or more of the name of the audit firm, the name of the audit company or the personal name of the auditor, as appropriate.

<sup>39</sup> The date of the auditor's review report is the date the auditor signs the report.

## NZAuASB Board Meeting Summary Paper

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**AGENDA ITEM NO.** 7.1  
**Meeting date:** 5 December 2019  
**Subject:** Audit/review alternative for small charities  
**Date:** 21 November 2019  
**Prepared by:** Peyman Momenan

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|---|--|
| <input type="checkbox"/> <b>Action Required</b> | <input checked="" type="checkbox"/> <b>For Information Purposes Only</b> |
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### Agenda Item Objectives

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

- NOTE the update on the progress of the audit/review alternative for small charities project.

### Background

1. In February 2019, the NZAuASB considered the recommendation from the working group on a possible approach for an alternative engagement (other than an audit or review) for small not-for-profits.
2. The working group's recommendation was to investigate using the Independent Examination (IE) regime in the UK as a guiding model to develop the engagement, by engaging with relevant stakeholders and considering the results of the NZAuASB's previous research on user needs of small New Zealand charities.
3. The Board noted its support for the recommended approach and provided the following feedback.
  - It needs to be very clear that the alternative engagement is not an audit or a review and to be very specific on independence.
  - The competency and objectivity of the person undertaking the engagement are fundamental aspects of this project. Specifically, if volunteers are expected to undertake the engagement.
  - There is a need to work closely with other interested parties, in particular the Charities Services and CAANZ and CPA Australia.
4. The working group held its second meeting on 20 November 2019 to explore the next steps of the project. The working group recommendations, discussions as well the expected next steps of the project are included in the Agenda item 7.2

**Action**

5. For the Board to NOTE the update on the direction and progress of the project.

**Material Presented**

|                 |   |
|-----------------|---|
| Agenda item 7.1 | Board Meeting Summary Paper                     |
| Agenda item 7.2 | The minutes of the working group second meeting |

### **Summary of Recommendations:**

On 20 November 2019, the Working Group held its second meeting to explore the next steps of the project.

A Summary of the Working Group recommendations is as follows.

- Continue the user need focus to better tailor an (Independent Examiners) IE like product for small NZ charities.
- Engage and involve the Charities Services and ensure their expectations and needs are clearly understood and incorporated into the alternative product.
- Further explore the feasibility and appeal of a modular product that addresses elements of matters not included in the charity's performance report.
- Keep an eye on any feedback from the UK on the IE regime.
- Engage with professional bodies (CA ANZ and CPA Australia) as they have plans relevant to this project.

### **Minutes of the Working Group discussions:**

The Working Group considered the staff memo highlighting the need to tailor the product to NZ users needs to ensure that the assurance needs of NZ stakeholders are best served. A better alignment of the scope of the project to those needs may entail a slightly different focus than the procedures included in the IE regime. For example, earlier XRB research showed that philanthropic funding organisation and government agencies are interested in whether a charity has the essential record keeping and financial control procedures in place to ensure that financial affairs are conducted honestly and effectively (financial management fitness).

The Working Group supported the staff recommendation that from the perspective of usefulness to stakeholders, the subject matter of the alternative engagement should include financial management fitness.

The core elements of financial management fitness may include:

- 1) Financial record keeping (including bookkeeping) systems.
- 2) Internal controls over financial affairs (with strong emphasis over prevention of fraud)
- 3) Reporting (including annual financial and performance reports)

The Working Group agreed that if practical, it may be beneficial to include specific procedures to address the core elements of financial management fitness.

The Working Group supported the focus on user needs however they noted that charities and other small not for profit entities have a wide range of stakeholders with different information needs and areas of interest. Volunteers and members information and assurance needs may be different to of the regulator (Charities Services) and philanthropic funding organisations. The Working Group discussed this point and concluded to start with a focus on the regulator (Charities Services) and then the philanthropic funding organisations. The Working Group requested staff to devise a plan to engage with these key stakeholders to ensure that their information needs are understood and appropriately reflected in the alternative product being developed.

The Working Group also noted that the IE regime is being reviewed by the UK Charities Regulator following a study published in August 2019 by the Charity Commission finding that only around half of charity accounts reviewed met the regulator's external scrutiny benchmark. This follows reviews of the quality of charity accounts which show that auditors and independent examiners are failing to identify significant failings in charity accounts. The study found that accounts reviewed by an auditor met the benchmark more frequently than those reviewed by an independent examiner. Although qualified examiners performed better, only 44% of accounts submitted by qualified examiners met the

## Agenda item 7.2

benchmark. Just 18% of unqualified examiners met the benchmark. The Working Group recommended the staff to keep an eye on the review, the lessons learned from the UK.

The Working Group supported the notion of an alternative product encompassing areas other than the charities performance report. They recommend staff to continue exploring a modular approach while working closely with key stakeholders.

The Working Group also noted that the professional bodies in Australia are exploring whether there is a need to create a new category of accredited assurance practitioners to address needs of smaller entities, including small charities. The working group asked the staff to gain a better understanding of the situation by engaging with the professional bodies as well as colleagues in the AUASB.

### **Project's next step:**

- To agree a plan with the AUASB staff to ensure that we are working together and helping each other for a better outcome in December 2019.
- Engage with Charities Services in February 2020 to understand their needs, views and ideas.
- Engage with professional bodies in relation to relevant activities to the project.

The staff will report to the working group on the project progress in March 2019.

## NZAuASB Board Meeting Summary Paper

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**AGENDA ITEM NO.** 8.1

**Meeting date:** 5 December 2019

**Subject:** IESBA – Non- Assurance Services and Fees

**Date:** 18 November 2019

**Prepared By:** Sharon Walker

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☒ **Action Required**

☐ **For Information Purposes Only**

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### Agenda Item Objectives

1. To provide an update to the Board on the IESBA's Non- Assurance Services and Fees projects, and to obtain preliminary feedback on the proposals.

### Background

2. Due to the late availability of papers for the IESBA December 2019 meeting, the issues papers presented at agenda items 8.2 and 8.3 are based on the proposals discussed by the IESBA at its September 2019 meeting.

#### *A: Non-Assurance Services*

3. The objective of the IESBA's non-assurance services (NAS) project is to ensure that all the NAS provisions in the IESBA Code are robust and of high quality for global application, thereby increase confidence in the independence of audit firms.
4. The NAS project proposes revisions to Section 600, *Provision of Non-assurance Services to an Audit Client*, and related conforming amendments, including to Section 950, *Provision of Non-assurance Services to Assurance Clients Other than Audit and Review Engagements*.
5. Some of the key matters the IESBA is considering include:
  - Prohibition on firms and network firms from providing a NAS that will create a self-review threat to an audit client that is a public interest entity (PIE).
  - How and when the IESBA Code should be revised to reflect new and emerging NAS that firms are providing as a result of advances in technology.
  - The extent to which the following prohibitions that apply to audit clients that are PIEs, irrespective of materiality, should be extended to audit clients that are not PIEs:
    - Tax planning and tax advisory when the effectiveness of the tax advice is dependent on a particular accounting treatment or presentation.

- Tax services that involve assisting in the resolution of tax disputes when the services involve acting as an advocate for the client before a public tribunal or court.
  - Providing corporate finance services to an audit client when the effectiveness of such advice depends on a particular accounting treatment or presentation.
  - Proposals to enhance transparency about auditor independence through improved firm communications with those charged with governance about NAS-related matters, including a proposed requirement for the firm to obtain the concurrence of those charged with governance to provide a non-assurance service to a PIE audit client.
6. At its December 2019 meeting, the IESBA will consider the proposals with a view to approving an exposure draft.

#### *B: Fees*

7. The objective of the IESBA's Fees project is to review the provisions in the IESBA Code pertaining to fee-related matters. The project is responsive to a public interest need for the IESBA to deal with fee-related matters, including those that impact or are perceived to impact auditor independence.
8. The project was informed by extensive fact finding, which included research performed by an academic and a global stakeholder survey on the topic of fees. The results of this fact-finding is summarized in a final report which can be accessed [here](#).
9. The scope of the project encompasses the following specific areas:
- A review of the provisions with respect to the level of audit fees for individual audit engagements, including the role of professional accountants in business in approving the level of audit fees;
  - A review of the provisions pertaining to fee dependency at a firm, office and partner level for all clients, including considering the introduction of a specific threshold for audit clients that are not PIEs; and
  - A review of the safeguards in the Code pertaining to the scope of the project.
10. A joint working group comprising representatives of the IAASB and IESBA has been established to facilitate the timely coordination of overlapping topics arising from the Fees Project, including considerations relating to public disclosure of fee-related information in the auditor's report.
11. The IESBA is expected to approve an exposure draft at its December 2019 meeting.

#### **Reference Materials**

12. Articles of interest on these topics are included in as supplementary materials. We thank Craig Fisher for bringing these articles to our attention.

#### **Recommendation**

13. We recommend that the Board note and provide preliminary feedback on the proposed changes to the non-assurance services and fees provisions in the IESBA Code.

**Material Presented**

Agenda item 8.1

Agenda item 8.2

Agenda item 8.3

Board Meeting Summary Paper

Issues Paper – Non- Assurance Services

Issues Paper – Fees



## Non-assurance Services

### Key Issues for consideration

1. Section 600<sup>1</sup> of the IESBA Code sets out requirements and application material relevant to applying the conceptual framework to identify, evaluate and address threats to independence when providing non-assurance services to audit clients.
  - A. *Distinction for PIEs and non-PIEs*
2. The proposals to section 600 reflect the IESBA task force's view that concerns about a firm's independence are heightened in the case of public interest entities (PIEs), and that the use of the reasonable and informed third party test is especially important when deciding whether to provide a non-assurance service (NAS) to an audit client that is a PIE.
3. Most of the task force's proposals apply only to audit clients that are PIEs. Paragraph 600.10 A1 includes new application material which the task force believes provides a useful explanation of the reasons for having difference NAS provisions in the Code for audit clients that are PIEs and those that are not PIEs.
4. New guidance is added to the Code, which states,
 

“Concerns about a firm's independence are heightened in the case of audits of public interest entities. Therefore, as required in identifying, evaluating and addressing threats to independence, the use of the reasonable and informed third party test is especially important when deciding whether to provide a non-assurance service to a public interest entity.” [610.10 A1]

#### **Matters for Board consideration**

- Does the Board agree that the provisions in the Code pertaining to non-assurance services should distinguish between PIEs and non-PIEs?
- Does the Board agree with the proposed wording to explain the different approaches in the Code for audit clients that are PIEs and those that are non-PIEs?

### B. *Self-review Threat Prohibition for PIEs*

5. Proposed new application material describes the NAS specific self-review threat as follows,
 

“A self-review threat is created when a firm or a network firm provides a non-assurance service to an audit client and there is a possibility that the firm will not appropriately evaluate the results of a judgement made or an activity performed by another individual within the firm or network firm as part of that service and on which the audit team will rely when forming a judgement as part of an audit.”  
[600.14 A1]
6. A new requirement is established to prohibit firms and network firms from providing NAS to audit clients that are PIEs when the provision of such NAS will create a self-review threat. The task force view is that, in the case of audit clients that are PIEs, self-review threats cannot be eliminated, and safeguards are not capable of being applied to reduce the self-review threat to an acceptable level. New application material has been added to help firms

<sup>1</sup> Section 600, *Provision of Non-Assurance Services to an Audit Client*

and network firms determine whether a NAS creates a self-review threat. [R600.15 – R600.15 A2]

7. This new requirement applies only to audit clients that are PIEs. For audit clients that are not PIEs, the firm applies the conceptual framework.

**Matters for Board consideration**

- Does the guidance clearly describe the NAS specific review threat?
- Does the Board agree that the prohibition on providing NAS to PIEs is limited only to those services that create a self-review threat? Other types of threats would be addressed under the conceptual framework.
- Does the Board agree that the prohibition on providing NAS that create a self-review threat should apply only to PIEs?
- Should the IESBA proceed to finalise this as a requirement, is there a compelling reason for a change to PES-1 to prohibit non-assurance services to audit clients, similarly to the decision the Auditor-General has taken for public sector audit entities?

*C. Communication with Those Charged with Governance Regarding Non-Assurance Services*

8. A new requirement and guidance have been established to enhance the communication with those charged with governance about NAS. For audit clients that are PIEs, before accepting an engagement to provide a NAS to an audit client, the firm will be required to provide those charged with governance of the PIE information about:
  - a. The nature and scope of the service to be provided;
  - b. Any threats to independence that might be created by the provision of such service;
  - c. The firm's evaluation of whether any threats identified are at an acceptable level;
  - d. Actions that the firm or network firm intends to take to address any threats that are not at an acceptable level; and
  - e. If actions are proposed to address such threats, why the threats would be eliminated or reduced to an acceptable level. [R600.18]
9. Provision of a NAS to an audit client that is a PIE is prohibited unless those charged with governance agree to the provision of that service and with the firm's conclusion that any threats to independence have been eliminated or reduced to an acceptable level.

**Matters for Board consideration**

- Does the Board agree with the enhanced communication requirements?

*D. Summary of Other Proposed Changes:*

*D.1 Multiple NAS provided to the same audit client*

10. The application material in the extant Code relating to the combined effect of threats created by providing multiple NAS to the same client is elevated to a requirement. New application material is added. [R600.12-600.12 A1]
11. *Non-assurance services provisions in laws or regulations*
12. Guidance is added to remind the firm that where laws or regulations relating to the provision of NAS differ from or go beyond the Code, the firm must comply with the more stringent provisions, unless required by law or regulation to provide a non-assurance service. [606.6 A1]

#### *D.2 Addressing Threats*

13. New application material with examples of actions that might be safeguards to address threats to independence created by providing a NAS to an audit client has been added. In addition, the application material relating to addressing threats has been refined and more closely aligned with section 120 (conceptual framework). [600.13 A1-600.13 A3]

#### *D.3 Providing Advice and Recommendations*

14. Guidance on providing advice and recommendations has been redrafted to better explain the interaction between the existing prohibition relating to assuming a management responsibility for an audit client and providing advice and recommendations to assist management and to clarify whether the self-review threat prohibition would apply in circumstances when firms provide advice and recommendations to audit clients that are PIEs during a NAS engagement.
15. The view held by some members of the IESBA is that providing advice and recommendations generally does not create self-review threats if management accepts responsibility for implementing that advice. This is consistent with the position in the extant Code.

#### *D.4 Prohibition for Assuming Management Responsibility and Related Provisions*

16. The overarching requirement that prohibits firms and network firms from assuming management responsibility for audit clients and related provisions are repositioned in Section 400, *Applying the Conceptual Framework to Independence for Audit and Review Engagements*. The task force view is that the placement in section 400 makes the prohibition more prominent in the Code and is clearer because of its close proximity to the requirement for the firm to be independent. Additionally, the move emphasises the fact that firms and network firms are prohibited from assuming a management responsibility for audit clients more broadly and not only when they provide a NAS.

#### *D.5 Accounting and Bookkeeping Services*

17. The prohibition on providing accounting and bookkeeping services to audit clients that are PIEs have been strengthened with the withdrawal of the exemption for the provision of accounting and bookkeeping services of a routine and mechanical nature:
  - for divisions or related entities of audit clients that are PIEs; or
  - for NAS that are collectively immaterial to the financial statements of the division or related entity.

#### *D.6 Valuation Services*

18. The prohibition for audit clients that are PIEs is strengthened with the withdrawal of the qualifier, i.e., material effect, individually or in the aggregate, on the financial statements on which the firm will express an opinion. The revised prohibition applies to the provision of a valuation service that will create a self-review threat in relation to the audit of the financial statements on which the firm will express an opinion.

*D.7 Tax Services*

19. The tax subsection of the Code is unique in that it includes general provisions that apply to all tax services and more specific provisions that apply to certain tax service areas.
20. A new requirement applicable to all audit clients prohibits the provision of a tax service if the service relates to marketing, planning or opining in favour of the tax treatment for a transaction unless that treatment is more likely than not to be allowable under applicable tax laws and regulations. [R604.4]
21. Prohibitions for audit clients that are PIEs are strengthened by the withdrawal of the reference to materiality. These prohibitions relate to:
- Preparation of tax calculations of current and deferred tax liabilities [R604.10]
  - Provision of tax advisory and tax planning services if the provision of such services will create a self-review threat (new) [R604.15]
  - Provision of assistance in the resolution of tax disputes if the services involve acting as an advocate before a tribunal or court [R604.26]
22. Application material with examples of safeguards that might address self-review threats for audit clients that are PIEs are also withdrawn.

*D8. Internal Audit Services*

23. A new requirement prohibiting the provision of internal audit services to an audit client that is a PIE if the provision of such services will create a self-review threat has been introduced. The list of prohibited internal audit services in the extant Code has been revised to be application material. The materiality/significant qualifier has been withdrawn. [R605.6]

*D9. Information Technology Systems*

24. This subsection has been revised leveraging the recently released AICPA Interpretation, [Information System Services](#).
25. With respect to audit clients that are PIEs, a new self-review threat prohibition applies for the provision of IT systems services. The materiality/significant qualifier has been withdrawn.

*D10. Litigation Support Services*

26. A new self-review threat prohibition has been introduced for litigation support services for audit clients that are PIEs. The materiality/significant qualifier has been withdrawn. [R607.6]
27. Application material with examples of safeguards that might address self-review threats for audit clients is applicable now only to audit clients that are not PIEs.

*D11. Legal Services*

28. A new self-review threat provision has been introduced for legal services for audit clients that are PIEs. In addition, the firm or network firm is prohibited from acting in an advocacy role for an audit client that is a PIE in resolving a dispute or litigation before a tribunal or court. [R608.6 and R608.9]
29. The extant provision prohibiting a partner or employee of the firm or a network firm from serving as General Counsel for legal affairs for an audit client has been retained. [R608.7]

*D12. Corporate Finance and Transaction Services*

30. For all audit clients, the materiality/significant qualifier has been withdrawn in relation to the provision of corporate finance and transaction-related advice, thereby strengthening the prohibition.
31. For audit clients that are PIEs, a prohibition on providing corporate finance services that create a self-review threat has been introduced.
32. Application material with examples of safeguards that might address self-review threats is not applicable only to audit clients that are non-PIEs.

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| <b>Matters for Board consideration</b> |
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| <ul style="list-style-type: none"><li>• Does the Board have any comments regarding the other proposed changes?</li></ul> |
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## Fees

### Key Issues for consideration

1. The IESBA proposes to amend Section 410<sup>1</sup> of the IESBA Code along with conforming changes and consequential amendments to other sections of Part 4A and Part 4B (the International Independence standards). This issues paper focuses on the significant proposed changes to be made to Section 410.
  - A. *Level of Audit Fees*
    2. The task force has proposed a requirement that prior to signing the audit report, the engagement partner be satisfied that the level of audit fee did not compromise the firm's independence and hence its ability to perform the audit in compliance with the fundamental principles. The task force view is that, irrespective of the facts and circumstances that determine the level of audit fee, the fee quoted or charged should allow the firm to perform the audit in accordance with professional standards. This overarching principle to be applied when determining the level of audit fees is in line with proposed ISQM 1 and ISA 220, and the task force recommends including a reference to these standards in section 410. [R410.4]
    3. A further requirement is added that the firm shall be satisfied that the provision, or possible provision, of services other than audit to an audit client does not influence the level of audit fees. Fees for an audit engagement should stand alone and should not be considered as part of a spectrum of total fees and provision of other services which could result in changes to the level of audit fees. [R410.6] Guidance indicates that a firm agreeing to provide audit services at a lower fee as an incentive for the supply of services other than audit creates an intimidation threat and may create a self-interest threat.
    4. New application material is added to describe the threats created when firms agree to lower audit fees in order to be engaged for provision of other services with the audit client.
    5. The intent of this new requirement and application material is to require that the firm not low-ball audit fees in anticipation of the supply of other services.

6. Does the Board agree that the Code should address the level of the audit fee as a standalone matter, and that it should include provisions to address threats created by fees paid for the provision of services other than audit to the audit client?

### B. *Total Fees – Relative Size*

7. The task force has proposed a similar model for firms addressing the threats to the fundamental principles for non-PIE audit clients as for the Code's existing fee-dependency model for PIE audit clients, but allowing greater latitude in the thresholds and safeguards proposed.
  - (i) *Audit Clients that are not PIEs*
8. When total fees from an audit client that is not a PIE represent more than 30% of the total fees of the firm for five consecutive years, the firm is required to determine whether either

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<sup>1</sup> Section 410, *Fees*

of the following actions might be a safeguard to address the threat created by the total fees received by the firm from the client, and if so, apply it:

- (a) Prior to the audit opinion being issued on the fifth year's financial statements, a professional accountant who is not a member of the firm expressing the opinion on the financial statements or a professional body, performs an engagement quality review of that engagement ("pre-issuance review") or
  - (b) After the audit opinion on the fifth year's financial statements has been issued, and before issuance of the opinion on the sixth year's financial statements, a professional accountant who is not a member of the firm expressing the opinion on the financial statements or a professional body, performs an engagement quality review of that engagement ("post issuance review").
9. If the fees from the audit client continue to exceed 30%, the firm is required to determine whether either the pre-issuance or post issuance review described in the preceding paragraph to the relevant year's engagement might be a safeguard to address the threat.
- (ii) Audit Clients that are PIEs*
10. For audit clients that are public interest entities, where total fees from the client and its related entities are expected to represent more than 15% of total fees received by the firm for two consecutive years, the firm is required to determine whether a pre-issuance review (as described above) is a safeguard to address the threat.
11. If the fees received from the audit client continue to exceed 15% of total fees received by the firm for five consecutive years, the firm is required to cease to be the auditor of the public interest entity after the audit report for the fifth year is issued [R410.18] unless there are (i) compelling reasons, having regard to the public interest, for the firm not to cease to be the auditor and (ii) a review, equivalent to an engagement quality review, is performed by a professional body or a professional accountant who is not a member of the firm. [R410.19]
12. Requirements and application material regarding communication of fee dependency to those charged with governance after the first year and public disclosure after the second year have been moved to a new subsection on transparency.

- 13. Does the Board agree that in the case of fee dependency, the Code should have different approaches for PIE and non-PIE audit clients, allowing greater flexibility in the approach for non-PIE audit clients?
- 14. Does the Board agree with the proposed thresholds – 15% for audit clients that are PIEs and 30% for audit clients that are not PIEs?
- 15. Does the Board agree that excessive fee dependency on an audit client that is a PIE should not be permitted to continue indefinitely unless, exceptionally, it can be shown to be in the public interest to do so?

*C. Transparency of Information Regarding Fees for Audit Clients that are PIEs*

Threats to independence, particularly independence in appearance, are generally greater for public interest entities. Accordingly, new requirements have been added for disclosure of fee related information to both those charged with governance and to stakeholders more generally for audit clients that are public interest entities.

*(i) Communication About Fee-related Information with Those Charged With Governance*

16. The task force considers that the communication related to the level of fees should go beyond a factual statement about the level of audit and other fees and that the communication should apply to all public interest entities (PIEs). ISA 260 sets out requirements for auditor communication with those charged with governance regarding independence, however that requirement applies only to listed entities<sup>2</sup>.
17. The task force's aim is to create a more meaningful basis for auditor communication with those charged with governance than is currently required, involving communication of relevant facts and circumstances related to fees that would allow those charged with governance to be better informed about the level of fees quoted or charged. This information would help those charged with governance assess whether auditors have performed the audit in accordance with professional standards.
18. The proposed requirement is for the firm to communicate timely to those charged with governance of an audit client that is a public interest entity regarding:
  - (a) The amount of the fee for the audit of the financial statements and the factors or other relevant information that the firm took into account in determining it;
  - (b) Any fees for the audit of special purpose financial statements and review engagements; and
  - (c) How the firm complied with the requirement that the firm be satisfied, prior to the engagement partner signing the audit report, that the level of fee did not compromise the firm's independence and hence its ability to perform the audit in compliance with the fundamental principles, including in accordance with professional standards. (see paragraph 2 of this paper). [R410.23]
19. In addition, the firm is required to communicate timely with those charged with governance of an audit client that is a public interest entity regarding the fees charged during the period covered by the financial statements for the provision by the firm or a network firm of

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<sup>2</sup> ISA 260 (Revised), paragraph 17, In the case of listed entities, the auditor shall communicate with those charged with governance:

- (a) A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and
  - i. All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgement, may reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor; and
  - ii. The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level [410.25]



services other than audit to the audited entity (which for this purpose shall include only related entities over which the audited entity has direct or indirect control). [R410.24]

20. If the firm determines that there is a self-interest or intimidation threat to independence created by the proportion of fees charged for the provision of fees other than audit relative to the audit fee, the firm is required to communicate with those charged with governance of an audit client that is a public interest entity:

- (a) Whether the threats created by the provision of such services are at an acceptable level and
- (b) The safeguards that the firm has taken or intends to take to reduce such threats to an acceptable level. [R410.25]

21. Where there is fee dependency, i.e., total fees from an audit client that is a PIE represent or are likely to represent more than 15% of the total fees received by the firm, the firm is required to communicate with those charged with governance regarding:

- (a) That fact and whether the situation is likely to continue (extant requirement)
- (b) The safeguards applied to address the threats created, including where relevant the use of a pre-issuance review (similar to extant requirement)
- (c) Any proposal to continue as auditor under R410.19 (new – refer to paragraph 11 above)

*(ii) Public Disclosure of Fee-related Information*

22. Some jurisdictions have laws and regulations requiring public disclosure of fee-related information. The primary source of this information should be the client's financial statements. Nevertheless, recognizing the stakeholders' interests in having access to fee-related information, as a key element in forming an opinion on the firm's independence, the task force considers there is a strong case for firms to carry the responsibility of having such information properly disclosed where this information is not available from the client's financial statements.
23. The task force's proposals take into account current national rules and regulations, but also establish a responsibility for firms to publicly disclose fee related information in circumstances when national laws and regulations do not address the public disclosure of fee related information. To provide the same level of accessibility to this information, the task force proposes the audit report, as a common platform, for the location of this disclosure, when required.
24. The firm shall be satisfied that the following information is publicly disclosed in a timely manner, providing appropriate accessibility:
  - (a) The amount of the fee for the audit of the financial statements;
  - (b) The amount of fees charged during the period covered by the financial statements for the provision by the firm or a network firm of services to the audit client (which, for this purpose shall include only related entities over which the audit client has director or indirect control) other than as disclosed under (a); and

- (c) If applicable, the fact that the total fees received by the firm from the audit client and its related entities represent, or are likely to represent, more than 15% of the total fees received by the firm for two consecutive years, and the year that this situation first arose.

The requirements in subparagraphs (a) to (c) above shall be met by compliance with laws and regulations which substantively satisfy the corresponding requirements.

[R410.27]

- 25. While the drafting does not specifically state, this requirement is intended to apply to public interest entities only.

- 26. Does the Board agree that transparency is an appropriate tool to mitigate threats created by fees paid to an audit client that is a PIE and that the Code should include provisions to promote such disclosure?
  - 27. What is the Board's view about the proposed split of disclosure of fees, i.e. to disclose audit fees and other fees? Would it be more appropriate to require the disclosure of audit fees, other assurance fees and non-assurance fees, or at a minimum, assurance fees and non-assurance fees? Independence issues are linked to the provision of non-assurance fees, so would it be more beneficial to the user to know that split?

## NZAuASB Board Meeting Summary Paper

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| AGENDA ITEM NO. | 10.1   |
| Meeting date:   | 5 December 2019  |
| Subject:        | Conforming Amendments to IAASB International Standards |
| Date:           | 18 November 2019                                       |
| Prepared By:    | Sharon Walker  |

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### Agenda Item Objectives

1. To approve the draft submission to the IAASB on its Exposure Draft: Proposed Amendments to the IAASB's International Standards, *Conforming Amendments to the IAASB International Standards as a Result of the Revised IESBA Code*, subject to comments received from stakeholders.
2. To update the Board on the proposed amendments to domestic standards as a result of the revised Professional and Ethical Standard 1<sup>1</sup>.

### Background

3. The IAASB has issued for public comment the above referenced exposure draft which proposes amendments to certain of the IAASB's International Standards<sup>2</sup> in response to the revised IESBA Code<sup>3</sup>.
4. A project to update the IAASB's International Standards is necessary to address inconsistencies between the International Standards and the revised IESBA Code. The purpose of making the revisions is solely to align the extant wording with the revised IESBA Code and not to re-evaluate or discuss the merits of each reference,

<sup>1</sup> Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand)

<sup>2</sup> The IAASB's International Standards comprise the International Standards on Auditing (ISAs), International Standards on Review Engagements (ISREs), International Standards on Assurance Engagements (ISAEs), International Standards on Related Services (ISRSs), and International Standards on Quality Control (ISQCs)

<sup>3</sup> International Ethics Standards Board for Accountants' (IESBA) *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code)

thus ensuring that the International Standards can continue to be applied effectively together with the revised IESBA Code.

5. The amendments are editorial in nature and generally involve little or no judgement in preparing them as there are no, or very limited options for amending the wording.
6. The proposed amendments to the IAASB's International Standards can be characterised into the following categories:
  - Category 1: proposed amendments to reflect structural changes to, and the applicability of the IESBA Code.
  - Category 2: proposed amendments to the framework for addressing threats to compliance with the fundamental principles to the IESBA Code.
  - Category 3: updates to the title of the IESBA Code.
  - Category 4: proposed amendments to align with terminology used in the IESBA Code.
7. Given the limited nature of the amendments proposed and because the conforming amendments do not create any new obligations, the IAASB is proposing that the conforming amendments become effective approximately 90 days after the approval of due process by the Public Interest Oversight Board.
8. A draft response to the ED is at agenda item 10.2. The Board is asked to consider and approve the draft submission subject to stakeholder feedback. Submissions to the IAASB are due on 10 January 2020. We have requested feedback on the submissions to be received by the XRB by Friday, 20 December 2019.

#### **NZ Domestic Exposure Draft**

9. The Board considered and approved proposed changes to the NZ specific paragraphs and domestic standards at its October 2019 meeting. These included the proposed change to the way the relevant ethical standards are referred to in the auditor's report and updates to references to Professional and Ethical Standard 1. The intent of the Board was that the proposed domestic changes should be exposed concurrent with the IAASB's exposure draft.
10. Following the October NZAuASB meeting, the Chair and senior staff had discussions with representatives of CAANZ, which included ethics related matters and how to incorporate Part B of the NZICA Code into an eCode for New Zealand. The possibility of combining the respective Codes and issuing a joint eCode was raised for further follow-up.
11. The Chief Executive and senior staff had a follow up discussion regarding the mandate of the NZAuASB and whether Part B of the IESBA Code, as it relates to assurance practitioners, could be incorporated into PES 1. Current thinking is that inclusion of Part B of the IESBA Code, as it relates to assurance practitioners, does fit within the mandate of the NZAuASB, and that it is appropriate to include it

within PES 1. Accordingly, in the new year, we propose to amend PES 1 to incorporate Part B.

12. The proposed amendment to ISA (NZ) 700 the Board previously approved relates to how we refer to relevant ethical standards in the auditor's report. Our initial thinking was because Part 2 of the IESBA Code was excluded from PES 1, we were unable to assert compliance with the IESBA Code. Given our current thinking that it is appropriate to include Part B of the IESBA Code in PES 1, the amendment to ISA (NZ) 700 and consequential amendments to the illustrative auditor's reports in other ISAs (NZ) would no longer be appropriate.
13. We recognise that until Part 2 is incorporated into PES 1 and becomes effective, the previously approved proposed amendment to ISA (NZ) 700 is more technically correct. However, we believe that making an amendment and withdrawing it in a short space of time will be confusing for both preparers and users of the report.
14. An amended ITC and ED is presented at agenda item 8.4, removing the previously proposed changes to ISA (NZ) 700 and consequential changes to the illustrative reports in the auditing and assurance standards for the Board's consideration.

#### **Recommendation**

15. We recommend that the Board
  - APPROVE the draft submission to the IAASB in response to the Exposure Draft: Proposed Amendments to the IAASB's International Standards, *Conforming Amendments to the IAASB International Standards as a Result of the Revised IESBA Code*, subject to comments received from stakeholders.
  - CONSIDER and APPROVE the proposed changes to the New Zealand exposure draft.

#### **Material Presented**

|                  |  |
|------------------|--|
| Agenda item 10.1 | Board Meeting Summary Paper                    |
| Agenda item 10.2 | Draft Submission – IAASB conforming amendments |
| Agenda item 10.3 | IAASB ED: IESBA Conforming Amendments          |
| Agenda item 10.4 | New Zealand ITC and ED                         |



NZ AUDITING  
AND ASSURANCE  
STANDARDS BOARD

10 January 2020

Willie Botha  
Technical Director  
International Auditing and Assurance Standards Board  
529 Fifth Avenue  
New York, NY 10017  
USA

Dear Willie,

**IAASB Exposure Draft –Proposed Amendments to the IAASB’s International Standards, *Conforming Amendments to the IAASB International Standards as a Result of the Revised IESBA Code***

Thank you for the opportunity to comment on the above referenced exposure draft. We submit the feedback from the New Zealand Auditing and Assurance Standards Board (NZAuASB) to the specific questions raised in the explanatory memorandum in the attachment.

The External Reporting Board (XRB) is a Crown Entity responsible for developing and issuing accounting and auditing and assurance standards in New Zealand. The XRB’s outcome goal is to contribute to the creation of dynamic and trusted markets through the establishment of an accounting and assurance framework that engenders confidence in New Zealand financial reporting, assists entities to compete internationally and enhances entities’ accountability to stakeholders. The NZAuASB has been delegated responsibility by the XRB for developing and issuing auditing and assurance standards.

The NZAuASB supports the IAASB’s proposals to amend the International Standards as a result of the revised IESBA Code.

Should you have any queries concerning our submission please contact either myself at the address details provided below or Sylvia van Dyk ([sylvia.vandyk@xrb.govt.nz](mailto:sylvia.vandyk@xrb.govt.nz)).

Yours sincerely,

**Robert Buchanan**  
**Chairman**  
Email: [robert@buchananlaw.co.nz](mailto:robert@buchananlaw.co.nz)

## **Submission of the New Zealand Auditing and Assurance Standards Board**

### ***IAASB Exposure Draft – Conforming Amendments to the IAASB’s International Standards***

#### **I Schedule of Responses to the IAASB’s Specific Questions**

- 1. Do you believe the proposed limited amendments are sufficient to resolve actual or perceived inconsistencies between the IAASB’s International Standards and the changes made by the IESBA in issuing the revised Code?**

**Response:**

The NZAuASB believes the proposed limited amendments are sufficient to resolve actual or perceived inconsistencies between the IAASB’s International Standards and the changes made by the IESBA in issuing the revised Code. The NZAuASB supports the approach taken by the IAASB to align the extant wording with the revised Code and not to re-consider the objectives, requirements and application material of the International Standards.

**Do you believe the at the proposed effective date of approximately 90 days after the approval of due process by the Public Interest Oversight Board is appropriate?**

**Response:**

The NZAuASB is fully supportive of the proposed effective date of approximately 90 days after the approval of the due process by the Public Interest Oversight Board. Given the limited nature of the conforming amendments, to align the IAASB’s International Standards with the revised IESBA Code and not to create any new obligations, the NZAuASB believes the proposed effective date allows sufficient time for implementation. Further, the NZAuASB believes it is in the public interest that the amendments become effective on a timely basis, given the revised provisions in the IESBA Code became effective in June 2019.

**Exposure Draft  
November 2019**

*Comments due: January 10, 2020*

*Proposed Amendments to the IAASB's  
International Standards*

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# Conforming Amendments to the IAASB International Standards as a Result of the Revised IESBA Code



International Auditing  
and Assurance  
Standards Board



## About the IAASB

This Exposure Draft was developed and approved by the International Auditing and Assurance Standards Board (IAASB).

The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

The IAASB develops auditing and assurance standards and guidance for use by all professional accountants under a shared standard-setting process involving the Public Interest Oversight Board, which oversees the activities of the IAASB, and the IAASB Consultative Advisory Group, which provides public interest input into the development of the standards and guidance. The structures and processes that support the operations of the IAASB are facilitated by the International Federation of Accountants (IFAC).

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## REQUEST FOR COMMENTS

This Exposure Draft, proposed *Conforming Amendments to the IAASB International Standards as a Result of the Revised IESBA Code*, was developed and approved by the International Auditing and Assurance Standards Board® (IAASB®).

The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form. **Comments are requested by January 10, 2020.**

Respondents are asked to submit their comments electronically through the IAASB website, using the “[Submit a Comment](#)” link. Please submit comments in both a PDF and Word file. First-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website.

This publication may be downloaded from the IAASB website: [www.iaasb.org](http://www.iaasb.org). The approved text is published in the English language.

# EXPLANATORY MEMORANDUM

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## Section 1 Introduction

1. This memorandum provides background to, and an explanation of, the International Auditing and Assurance Standards Board's (IAASB's) proposed amendments to certain of its International Standards<sup>1</sup> in response to the revised IESBA Code<sup>2</sup>. The IAASB approved the proposed amendments to the following International Standards on November 7, 2019 for exposure:
- ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*;
  - ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*;
  - ISA 220, *Quality Control for an Audit of Financial Statements*;
  - ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*;
  - ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*;
  - ISA 260 (Revised), *Communication with Those Charged with Governance*;
  - ISA 600, *Special Considerations – Audits of Group Financial Statements (Including the Work of the Component Auditors)*;
  - ISA 610 (Revised 2013), *Using the Work of Internal Auditors*;
  - ISA 620, *Using the Work of an Auditor's Expert*;
  - ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*;
  - ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*;
  - ISA 800 (Revised), *Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*;
  - ISA 805 (Revised), *Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of Financial Statement*;
  - ISA 810 (Revised), *Engagements to Report on Summary Financial Statements*;
  - IAPN 1000, *Special Considerations in Auditing Financial Instruments*;
  - ISRE 2400 (Revised), *Engagements to Review Historical Financial Statements*;
  - ISAE 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*;
  - ISAE 3402, *Assurance Reports on Controls at a Service Organization*;
  - ISAE 3410, *Assurance Engagements on Greenhouse Gas Statements*;

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<sup>1</sup> The IAASB's International Standards comprise the International Standards on Auditing (ISAs), International Standards on Review Engagements (ISREs), International Standards on Assurance Engagements (ISAEs), International Standards on Related Services (ISRSs), and International Standards on Quality Control (ISQCs)

<sup>2</sup> International Ethics Standards Board for Accountants' (IESBA) *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code)

- ISAE 3420, *Assurance Engagements to Report on the Compilation of Pro Forma Financial Information included in a Prospectus*;
  - ISRS 4400, *Engagements to Perform Agreed-Upon Procedures Regarding Financial Information (Previously ISA 920)*; and
  - ISRS 4410 (Revised), *Compilation Engagements*.
2. Amendments are also proposed to the *International Framework for Assurance Engagements*.

## Section 2 Background

### Implications of the Revised IESBA Code

3. The IAASB's International Standards (the International Standards) refer to the IESBA Code in various ways, ranging from simple references to the title of the IESBA Code to detailed references to specific paragraphs in the IESBA Code as it existed before April 2018.
4. The revised IESBA Code was effective from June 15, 2019. The IESBA's Basis for Conclusions, [\*Improving the Structure of the Code of Ethics for Professional Accountants\*](#), indicates that the IESBA was careful to not inadvertently change the meaning of the IESBA Code or weaken it.
5. A project to update the IAASB Handbook (the Handbook) for the revised IESBA Code is necessary to address inconsistencies between the International Standards in the Handbook and the revised IESBA Code. The purpose of making the revisions is solely to align the extant wording with the revised IESBA Code and not to reevaluate or discuss the merits of each reference, thus ensuring that the International Standards can continue to be applied effectively together with the revised IESBA Code.
6. The IAASB believes it would not be effective to make the changes on a piecemeal basis (i.e., wait until substantive changes are made to each standard to update references to the revised IESBA Code), as some of the affected standards may not be updated on a timely basis.

### Public Interest Issues Addressed by this Project

7. The IAASB believes that it is in the public interest that its International Standards and the IESBA Code be able to operate in concert and without confusion due to the many jurisdictions that utilize both. It is also important that the IAASB's International Standards acknowledge and do not potentially undermine the enhancements that are made to the IESBA Code—either through being inconsistent or through failing to draw appropriate attention to the revised requirements in the IESBA Code. Equally, it would not be in the public interest for practitioners to be placed in a situation where the IESBA Code required one approach but the IAASB's International Standards, either in the requirements or the application material, did not support or recognize that approach.

## Section 3 Guide for Respondents

The IAASB welcomes comments on all matters addressed in this exposure draft (ED), but especially those identified in the *Request for Comments* section. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this ED (especially those calling for change in current practice), it will be helpful for the IAASB to be made aware of this view as this cannot always be inferred when not stated.

## Section 4 Significant Matters

8. The ED includes those amendments that the IAASB has determined would be necessary to resolve actual or perceived inconsistencies between the IAASB's International Standards and the changes made by IESBA in issuing the revised IESBA Code. All the changes are relatively minor or editorial in nature, or are changes only to reflect existing obligations under the revised IESBA Code.
9. These amendments are limited, as developing them does not involve re-consideration of the objectives, requirements and application material of the International Standards, in their own right. The amendments generally involve little or no judgment in preparing them as there are no, or very limited, options for amending the wording.
10. Broadly, the proposed amendments to the IAASB's International Standards can be characterized into a small number of categories. The categories are:
  - a) Category 1: Proposed amendments to reflect structural changes to, and the applicability of, the IESBA Code. An example of these changes is replacing terms such as "Parts A and B of the [Code]" with "the provisions of the [Code]." This change is necessary as the IESBA Code is intended to be read holistically, rather than linking directly to only certain sections.
  - b) Category 2: Proposed amendments to the framework for addressing threats to compliance with the fundamental principles to the IESBA Code. An example of these changes is in the ISA 620,<sup>3</sup> Paragraph A18, where it is proposed to replace the phrase "*Safeguards may eliminate or reduce such threats, and may be created by external structures (for example, the auditor's expert's profession, legislation or regulation),*" with the phrase "*Such threats may be addressed by eliminating the circumstances that create the threat, applying safeguards or by the auditor's expert's work environment (for example, quality control policies and procedures).*" This change is necessary because, under the previous Code, safeguards include actions or measures that eliminate or reduce the threats to an acceptable level whereas under the revised IESBA Code, safeguards are measures that are applied to reduce the threats, while measures to eliminate threats are separate from safeguards.
  - c) Category 3: Updates to the title of the IESBA Code. The full title of the IESBA Code is now "*International Code of Ethics for Professional Accountants (including International Independence Standards).*"

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<sup>3</sup> ISA 620, *Using the Work of an Auditor's Expert*

- d) Category 4: Proposed amendments to align with terminology used in the IESBA Code. An example of these changes is the amendments to the definition of “independence,” which is needed to align with the revised definition in the IESBA Code.
11. A tabular presentation format has been used to show the extant IAASB Handbook text, relevant notes on the revisions to the IESBA Code, the proposed change to the IAASB Handbook text, and the category of the change.

#### *Effective Date*

12. Given the limited nature of the amendments proposed and because the conforming amendments do not create any new obligations, the IAASB is proposing that the conforming amendments become effective approximately 90 days after the approval of the due process by the Public Interest Oversight Board. Such timeframe is considered necessary to allow jurisdictions sufficient time for translation of the final text of the International Standards, for national adoption processes to occur, and for practitioners to update templates and associated internal materials. The IAASB considered whether a longer effective date would be in the public interest, but concluded that it would prolong the non-alignment between the IAASB International Standards and the revised IESBA Code, would delay the production of the IAASB Handbook, and that a longer effective date is unnecessary due to the limited nature of the conforming amendments. The IAASB is seeking comments on the effective date of the conforming amendments.

## **Section 5 Request for Comments**

13. While the IAASB welcomes comments on all matters addressed in this ED, the IAASB is specifically seeking comments on the following matters:
- 1) Whether respondents believe the proposed limited amendments are sufficient to resolve actual or perceived inconsistencies between the IAASB's International Standards and the changes made by IESBA in issuing the revised IESBA Code.
  - 2) Whether respondents believe that the proposed effective date of approximately 90 days after the approval of the due process by the Public Interest Oversight Board is appropriate.

## EXPOSURE DRAFT: PROPOSED CHANGES TO THE IAASB STANDARDS AS A RESULT OF THE REVISED IESBA CODE<sup>4</sup>

| IAASB Standards |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-----------------|---|---|---|--------------------|
| Standard        | Extant Paragraphs   |   | Proposed Change   | Category of change |
| Glossary        | <p><i>Independence</i><sup>16</sup>—Comprises:</p> <p>(a) Independence of mind—the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.</p> <p>(b) Independence in appearance—the avoidance of facts and circumstances that are so significant a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised.</p> <p><small>16 As defined in the IESBA Code of Ethics for Professional Accountants</small></p> | <ul style="list-style-type: none"> <li>The definition of “independence in appearance” has been amended (see paragraph 120.12 A1)</li> </ul> | <p><i>Independence</i><sup>16</sup>—Comprises:</p> <p>(a) Independence of mind—the state of mind that permits the <u>expression</u> <del>provision</del> of an opinion without being affected by influences that compromise professional judgment, <u>thereby</u> allowing an individual to act with integrity, and exercise objectivity and professional skepticism.</p> <p>(b) Independence in appearance—the avoidance of facts and circumstances that are so significant <u>that</u> a reasonable and informed third party, <del>having knowledge of all relevant information, including any safeguards applied,</del> would <u>be likely to reasonably conclude that</u> a firm's or a <del>member of the an audit or assurance team's</del> <u>member's</u> integrity, objectivity or professional skepticism <del>has</del> been compromised.</p> <p><small>16 As defined in the IESBA Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code)</small></p> | 4                  |
| Glossary        | <p><i>Network</i>—A larger structure:</p>   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>   | N/A   | N/A                |

<sup>4</sup> The comparison is based on the 2018 Handbooks published by IAASB and IESBA



| IAASB Standards  |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|--|--|---|---|--------------------|
| Standard   | Extant Paragraphs  |   | Proposed Change                         | Category of change |
| (Refer also to standards that contain this definition)             | <p>(a) That is aimed at cooperation, and</p> <p>(b) That is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.</p>  |   |   |                    |
| Glossary<br>(Refer also to standards that contain this definition) | Network firm—A firm or entity that belongs to a network.   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>   | N/A                                     | N/A                |
| Glossary<br>(Refer also to standards that contain this definition) | <p>Non-compliance (in the context of ISA 250<sup>17</sup>)—Acts of omission or commission, intentional or unintentional, committed by the entity, or by those charged with governance, by management or by other individuals working for or under the direction of the entity, which are contrary to the prevailing laws or regulations. Non-compliance does not include personal misconduct unrelated to the business activities of the entity.</p> <p>17 ISA 250 (Revised), <i>Consideration of Laws and Regulations in an Audit of Financial Statements</i></p> | <ul style="list-style-type: none"> <li>No changes identified (note that the ISA includes an additional clarification on personal misconduct that was intentionally included in the definition)</li> </ul> | N/A                                     | N/A                |

| IAASB Standards  |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--|--|--|--|--------------------|
| Standard   | Extant Paragraphs  |  | Proposed Change  | Category of change |
| Glossary<br>(Refer also to standards that contain this definition) | <p>Professional accountant<sup>19</sup>—An individual who is a member of an IFAC member body.</p> <p>19 As defined in the IESBA <i>Code of Ethics for Professional Accountants</i></p>   | <ul style="list-style-type: none"> <li>Update footnote for title of Code</li> </ul>    | 19 As defined in the IESBA <del><i>Code of Ethics for Professional Accountants</i></del> | 3                  |
| Glossary<br>(Refer also to standards that contain this definition) | <p>Professional accountant in public practice<sup>20</sup>—A professional accountant, irrespective of functional classification (for example, audit, tax or consulting) in a firm that provides professional services. This term is also used to refer to a firm of professional accountants in public practice.</p> <p>20 As defined in the IESBA <i>Code of Ethics for Professional Accountants</i></p>  | <ul style="list-style-type: none"> <li>Update footnote for title of Code</li> </ul>    | 20 As defined in the IESBA <del><i>Code of Ethics for Professional Accountants</i></del> | 3                  |
| Glossary<br>(Refer also to standards that contain this definition) | <p><i>Professional judgment</i>—The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.</p> <p><i>Professional judgment (in the context of ISAE 3000 (Revised))</i>—The application of relevant training, knowledge and experience, within the context provided by assurance and ethical standards, in making informed decisions about the courses of</p> | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul> | N/A  | N/A                |

| IAASB Standards  |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|--|---|--|---|--------------------|
| Standard   | Extant Paragraphs   |  | Proposed Change   | Category of change |
|  | <p>action that are appropriate in the circumstances of the engagement.</p> <p><i>Professional judgment (in the context of ISRE 2400 (Revised))</i>—The application of relevant training, knowledge and experience, within the context provided by assurance, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the review engagement.</p>   |  |   |                    |
| Glossary<br>(Refer also to standards that contain this definition) | <p><i>Relevant ethical requirements</i>—Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) together with national requirements that are more restrictive. In the context of ISRE 2400 (Revised), relevant ethical requirements are defined as the ethical requirements the engagement team is subject to when undertaking review engagements. These requirements ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code),</p> | <ul style="list-style-type: none"> <li>• Update to the title of the Code</li> <li>• Parts A, B and C have been renamed and there are now International Independence Standards (Parts 4A and 4B)</li> </ul> | <p><i>Relevant ethical requirements (in the context of ISQC 1)</i>—Ethical requirements to which the engagement team and engagement quality control reviewer are subject <u>when undertaking audits or reviews of financial statements, or other assurance or related services engagements</u>, which ordinarily comprise <u>the provisions of the Parts A and B of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i></u> (IESBA Code) together with national requirements that are more restrictive.</p> <p><i>Relevant ethical requirements (in the context of the ISAs)</i>—Ethical requirements to which the engagement team and engagement quality control reviewer are subject when undertaking</p> | 1 & 3              |

| IAASB Standards |  | Notes in Relation to the 2018 IESBA Code | Proposed Changes to the IAASB Standards  |                    |
|-----------------|--|--|--|--------------------|
| Standard        | Extant Paragraphs  |  | Proposed Change  | Category of change |
|                 | <p>together with national requirements that are more restrictive. In the context of ISRS 4410 (Revised), relevant ethical requirements are defined as the ethical requirements the engagement team is subject to when undertaking compilation engagements. These requirements ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) (excluding Section 290, <i>Independence—Audit and Review Engagements</i>, and Section 291, <i>Independence—Other Assurance Engagements</i> in Part B), together with national requirements that are more restrictive.</p> |  | <p><u>an audit engagement, which ordinarily comprise the provisions of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants</i> (including <i>International Independence Standards</i>) (IESBA Code) related to an audit of financial statements, together with national requirements that are more restrictive.</u></p> <p><u><i>Relevant ethical requirements (in the context of ISRE 2400 (Revised))</i></u>, <del>relevant ethical requirements are defined as the e</del>Ethical requirements <u>to which</u> the engagement team is subject <del>to</del>—when undertaking <u>a</u> review engagements, <u>which</u>. These requirements ordinarily comprise <u>the provisions of Parts A and B of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants</i> (including <i>International Independence Standards</i>) (IESBA Code) related to a review of financial statements,</u> together with national requirements that are more restrictive.</p> <p><u><i>Relevant ethical requirements (in the context of ISRS 4410 (Revised))</i></u>, <del>relevant ethical requirements are defined as the e</del>Ethical requirements <u>to which</u> the engagement team is subject <del>to</del>—when undertaking <u>a</u> compilation engagements, <u>which</u> These requirements ordinarily comprise <u>Parts A and B of the</u></p> |                    |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|--|---|--|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                         |  |   | <u>provisions of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) (excluding Section 290, <i>Independence—Audit and Review Engagements</i>, and Section 291, <i>Independence—Other Assurance Engagements</i> in Part B)</u> related to compilation engagements, together with national requirements that are more restrictive.   |                    |
| ISQC 1<br>Paragraph 12q | Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) together with national requirements that are more restrictive. | <ul style="list-style-type: none"> <li>Refer comments above regarding proposed changes</li> </ul> | Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject <u>when undertaking audits or reviews of financial statements, or other assurance or related services engagements</u> , which ordinarily comprise <del>Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code)</del> <u>the provisions of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code)</u> , together with national requirements that are more restrictive. | 1 & 3              |
| ISQC 1<br>Paragraph 20  | The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm and its  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                           | N/A  | N/A                |

| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------|--|---|---|--------------------|
| Standard               | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                        | personnel comply with relevant ethical requirements. (Ref: Para. A7–A10)   |   |   |                    |
| ISQC 1<br>Paragraph 21 | <p>The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including network firm personnel) maintain independence where required by relevant ethical requirements. Such policies and procedures shall enable the firm to: (Ref: Para. A10)</p> <p>(a) Communicate its independence requirements to its personnel and, where applicable, others subject to them; and</p> <p>(b) Identify and evaluate circumstances and relationships that create threats to independence, and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement, where withdrawal is possible under applicable law or regulation.</p> | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how identified threats are addressed. Notably, under the extant Code, safeguards include actions or measures that eliminate or reduce the threats to an acceptable level. Under the revised Code, safeguards are measures that are applied to reduce the threats, while measures to eliminate threats</li> </ul> | <p>...</p> <p>(b) <del>Identify and evaluate circumstances and relationships that create threats to independence, evaluate whether the identified threats are at an acceptable level, and address them by and to take appropriate action to eliminating the circumstances that create the threat, applying safeguards, or withdrawing from the engagement, safeguards, or, if considered appropriate, to withdraw from the engagement,</del> where withdrawal is possible under applicable law or regulation.</p> | 2                  |

| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|------------------------|--|--|--|--------------------|
| Standard               | Extant Paragraphs  |  | Proposed Change  | Category of change |
|                        |  | <p>are separate from safeguards</p> <ul style="list-style-type: none"> <li>Paragraph 400.6, R400.11 and R400.12 of the IESBA Code</li> </ul>   |  |                    |
| ISQC 1<br>Paragraph 22 | <p>Such policies and procedures shall require: (Ref: Para. A10)</p> <p>(a) Engagement partners to provide the firm with relevant information about client engagements, including the scope of services, to enable the firm to evaluate the overall impact, if any, on independence requirements;</p> <p>(b) Personnel to promptly notify the firm of circumstances and relationships that create a threat to independence so that appropriate action can be taken; and</p> <p>(c) The accumulation and communication of relevant information to appropriate personnel so that:</p> <p>(i) The firm and its personnel can readily determine whether they satisfy independence requirements;</p> | <ul style="list-style-type: none"> <li>The revised Code describes threats to compliance differently</li> <li>Part (c) - the revised Code refers to addressing threats, i.e., not appropriate action</li> </ul> | <p>Such policies and procedures shall require: (Ref: Para. A10)</p> <p>(a) Engagement partners to provide the firm with relevant information about client engagements, including the scope of services, to enable the firm to evaluate the overall impact, if any, on independence requirements;</p> <p>(b) Personnel to promptly notify the firm of <del>circumstances and relationships that create a threats</del> to <u>compliance with independence requirements</u> so that <u>the firm can evaluate whether such threats are at an acceptable level and if not, address them by eliminating the circumstances that create the threat, applying safeguards, or withdrawing from the engagement, where withdrawal is possible under applicable law or regulation appropriate action can be taken</u>; and</p> | 2                  |

| IAASB Standards        |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards  |                    |
|------------------------|---|---|--|--------------------|
| Standard               | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                        | <p>(ii) The firm can maintain and update its records relating to independence; and</p> <p>(iii) The firm can take appropriate action regarding identified threats to independence that are not at an acceptable level.</p>  |   | <p>(c) The accumulation and communication of relevant information to appropriate personnel so that:</p> <p>(i) The firm and its personnel can readily determine whether they satisfy independence requirements;</p> <p>(ii) The firm can maintain and update its records relating to independence; and</p> <p>(iii) The firm can take appropriate action regarding identified threats to independence that are not at an acceptable level.</p> |                    |
| ISQC 1<br>Paragraph 23 | <p>The firm shall establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements, and to enable it to take appropriate actions to resolve such situations. The policies and procedures shall include requirements for: (Ref: Para. A10)</p> <p>(a) Personnel to promptly notify the firm of independence breaches of which they become aware;</p> <p>(b) The firm to promptly communicate identified breaches of these policies and procedures to:</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A  | N/A                |



| IAASB Standards        |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|------------------------|---|---|--|--------------------|
| Standard               | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                        | <p>(i) The engagement partner who, with the firm, needs to address the breach; and</p> <p>(ii) Other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action; and</p> <p>(c) Prompt communication to the firm, if necessary, by the engagement partner and the other individuals referred to in subparagraph 23(b)(ii) of the actions taken to resolve the matter, so that the firm can determine whether it should take further action.</p> |   |  |                    |
| ISQC 1<br>Paragraph 24 | At least annually, the firm shall obtain written confirmation of compliance with its policies and procedures on independence from all firm personnel required to be independent by relevant ethical requirements. (Ref: Para. A10–A11)  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>   | N/A  | N/A                |
| ISQC 1<br>Paragraph 25 | <p>The firm shall establish policies and procedures: (Ref: Para. A10)</p> <p>(a) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable</p>   | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the</li> </ul> | <p>The firm shall establish policies and procedures: (Ref: Para. A10)</p> <p>(a) <u>Eliminating the threat or</u> <del>Setting out criteria for applying determining the need for safeguards to reduce the threat of the</del></p> | 2                  |

| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------|--|---|---|--------------------|
| Standard               | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                        | <p>level when using the same senior personnel on an assurance engagement over a long period of time; and</p> <p>(b) Requiring, for audits of financial statements of listed entities, the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements. (Ref: Para. A12–A17)</p>  | <p>extant Code, in particular in relation to how identified threats are addressed</p> | <p><u>long association with an entity to an acceptable level</u>, <del>the familiarity threat to an acceptable level</del> when using the same senior personnel on an assurance engagement over a long period of time; and</p> <p>(b) Requiring, for audits of financial statements of listed entities, the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements. (Ref: Para. A12–A17)</p> |                    |
| ISQC 1<br>Paragraph 27 | <p>Such policies and procedures shall require:</p> <p>(a) The firm to obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. (Ref: Para. A21, A23)</p> <p>(b) If a potential conflict of interest is identified in accepting an engagement from a new or an</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>               | N/A   | N/A                |

| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code                               | Proposed Changes to the IAASB Standards |                    |
|------------------------|--|--|---|--------------------|
| Standard               | Extant Paragraphs  |  | Proposed Change                         | Category of change |
|                        | <p>existing client, the firm to determine whether it is appropriate to accept the engagement.</p> <p>(c) If issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, the firm to document how the issues were resolved.</p>   |  |   |                    |
| ISQC 1<br>Paragraph 28 | <p>The firm shall establish policies and procedures on continuing an engagement and the client relationship, addressing the circumstances where the firm obtains information that would have caused it to decline the engagement had that information been available earlier. Such policies and procedures shall include consideration of:</p> <p>(a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and</p> <p>(b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship. (Ref: Para. A22–A23)</p> | <ul style="list-style-type: none"> <li>No change identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|------------------------|--|--|--|--------------------|
| Standard               | Extant Paragraphs  |  | Proposed Change  | Category of change |
| ISQC 1<br>Paragraph 38 | <p>For audits of financial statements of listed entities, the firm shall establish policies and procedures to require the engagement quality control review to also include consideration of the following:</p> <p>(a) The engagement team's evaluation of the firm's independence in relation to the specific engagement;</p> <p>(b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and</p> <p>(c) Whether documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A45–A46)</p> | <ul style="list-style-type: none"> <li>N/A</li> </ul>  | N/A  | N/A                |
| ISQC 1<br>Paragraph A7 | <p>The IESBA Code establishes the fundamental principles of professional ethics, which include:</p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p>   | <ul style="list-style-type: none"> <li>Aligning with terminology used in the Code</li> </ul> | <p>The IESBA Code establishes the fundamental principles of <del>professional</del>—ethics, which <del>include</del><u>are</u>:</p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> | 4                  |

| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------|--|---|---|--------------------|
| Standard               | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                        | (d) Confidentiality; and<br>(e) Professional behavior.   |   | (e) Professional behavior.<br><u>The fundamental principles of ethics establish the standard of behavior expected of a professional accountant.</u>   |                    |
| ISQC 1<br>Paragraph A8 | Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations. It provides examples of safeguards that may be appropriate to address threats to compliance with the fundamental principles and also provides examples of situations where safeguards are not available to address the threats. | <ul style="list-style-type: none"> <li>Aligning with terminology used in the Code</li> <li>Reflecting the structural changes to the Code</li> </ul> | <p><del>Part B of is to be applied in specific situations. It provides examples of safeguards that may be appropriate to address threats to compliance with the fundamental principles and also provides examples of situations where safeguards are not available to address the threats.</del></p> <p><u>The IESBA Code provides a conceptual framework that professional accountants are to apply in order to identify, evaluate and address threats to compliance with the fundamental principles. In the case of audits, reviews and other assurance engagements, the IESBA Code sets out <i>International Independence Standards</i>, which apply the conceptual framework of identifying, evaluating and addressing threats to the fundamental principles and compliance with independence requirements.</u></p> | 1, 2 & 4           |
| ISQC 1<br>Paragraph A9 | <p>The fundamental principles are reinforced in particular by:</p> <ul style="list-style-type: none"> <li>The leadership of the firm;</li> </ul>   | <ul style="list-style-type: none"> <li>The Code refers to “breaches” of the Code. “Non-</li> </ul>  | <p>The fundamental principles are reinforced in particular by:</p> <ul style="list-style-type: none"> <li>The leadership of the firm;</li> </ul>  | 4                  |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code                               | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|---|--|--|--------------------|
| Standard                | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                         | <ul style="list-style-type: none"> <li>Education and training;</li> <li>Monitoring; and</li> <li>A process for dealing with non-compliance.</li> </ul>  | compliance” is used to refer to laws and regulations                   | <ul style="list-style-type: none"> <li>Education and training;</li> <li>Monitoring; and</li> <li>A process for dealing with <u>breaches</u><del>non-compliance</del>.</li> </ul> |                    |
| ISQC 1<br>Paragraph A10 | <p>The definitions of “firm,” network” or “network firm” in relevant ethical requirements may differ from those set out in this ISQC. For example, the IESBA Code defines the “firm” as:</p> <p>(a) A sole practitioner, partnership or corporation of professional accountants;</p> <p>(b) An entity that controls such parties through ownership, management or other means; and</p> <p>(c) An entity controlled by such parties through ownership, management or other means.</p> <p>The IESBA Code also provides guidance in relation to the terms “network” and “network firm.”</p> <p>In complying with the requirements in paragraphs 20–25, the definitions used in the relevant ethical requirements apply in so</p> | <ul style="list-style-type: none"> <li>No change identified</li> </ul> | N/A  | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|--|---|--|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                         | far as is necessary to interpret those ethical requirements.   |   |  |                    |
| ISQC 1<br>Paragraph A11 | Written confirmation may be in paper or electronic form. By obtaining confirmation and taking appropriate action on information indicating non-compliance, the firm demonstrates the importance that it attaches to independence and makes the issue current for, and visible to, its personnel. | <ul style="list-style-type: none"> <li>Aligning with terminology used by the IESBA Code</li> </ul>  | Written confirmation may be in paper or electronic form. By obtaining confirmation and taking appropriate action on information indicating <u>a breach</u> <del>non-compliance</del> , the firm demonstrates the importance that it attaches to independence and makes the issue current for, and visible to, its personnel.   | 4                  |
| ISQC 1<br>Paragraph A12 | <p>Familiarity Threat (Ref: Para. 25)</p> <p>The IESBA Code discusses the familiarity threat that may be created by using the same senior personnel on an assurance engagement over a long period of time and the safeguards that might be appropriate to address such threats.</p>              | <ul style="list-style-type: none"> <li>Section 540 and 940 of the Code have been updated</li> </ul> | <p><u>Long Association with an Entity Familiarity Threat</u> (Ref: Para. 25)</p> <p>The IESBA Code discusses the <del>familiarity</del> threats that may be created <u>as a result of an individual's long association with:</u></p> <ul style="list-style-type: none"> <li><u>The entity and its operations;</u></li> <li><u>The entity's senior management; or</u></li> <li><u>The underlying subject matter and subject matter information of the assurance engagement.</u></li> </ul> <p><del>by using the same senior personnel on an assurance engagement over a long period of time and the safeguards that might be appropriate to address such threats.</del></p> | 2                  |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|--|--|--|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change  | Category of change |
| ISQC 1<br>Paragraph A13 | <p>Determining appropriate criteria to address familiarity threat may include matters such as:</p> <ul style="list-style-type: none"> <li>The nature of the engagement, including the extent to which it involves a matter of public interest; and</li> <li>The length of service of the senior personnel on the engagement.</li> </ul> <p>Examples of safeguards include rotating the senior personnel or requiring an engagement quality control review.</p> | <ul style="list-style-type: none"> <li>Section 540 and 940 of the Code have been recently updated</li> </ul> | <p>The IESBA Code includes examples of factors <u>that are relevant to evaluating the level of a threat that may arise when an individual is involved in an assurance engagement over a long period of time. The IESBA Code also provides examples of actions:</u></p> <ul style="list-style-type: none"> <li><u>Eliminating the threats, by rotating the individual off the engagement team; or</u></li> <li><u>Applying safeguards to reduce the threats to an acceptable level.</u></li> </ul> <p><del>Determining appropriate criteria to address familiarity threat may include matters such as:</del></p> <ul style="list-style-type: none"> <li><del>The nature of the engagement, including the extent to which it involves a matter of public interest; and</del></li> <li><del>The length of service of the senior personnel on the engagement.</del></li> </ul> <p><del>Examples of safeguards include rotating the senior personnel or requiring an engagement quality control review.</del></p> | 2                  |
| ISQC 1<br>Paragraph A14 | <p>The IESBA Code recognizes that the familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these audits, the IESBA Code requires the rotation of the key audit partner<sup>4</sup> after a pre-defined period, normally no more than seven years, and provides</p>   | <ul style="list-style-type: none"> <li>Section 540 and 940 of the Code have been updated</li> </ul>          | <p><u>The IESBA Code requires the rotation of the engagement partner, the engagement quality control reviewer, and other key audit partners<sup>4</sup> in respect of certain engagements. The IESBA Code recognizes that the familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these</u></p>   | 2                  |



| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|-------------------------|--|--|---|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                         | <p>related standards and guidance. National requirements may establish shorter rotation periods.</p> <p>4 As defined in the IESBA Code</p>   |  | <p><del>audits, the IESBA Code requires the rotation of the key audit partner<sup>4</sup> after a pre-defined period, normally no more than seven years, and provides related standards and guidance. National requirements may establish shorter rotation periods.</del></p> <p>4 As defined in the IESBA Code</p> |                    |
| ISQC 1<br>Paragraph A15 | Statutory measures may provide safeguards for the independence of public sector auditors. However, threats to independence may still exist regardless of any statutory measures designed to protect it. Therefore, in establishing the policies and procedures required by paragraphs 20–25, the public sector auditor may have regard to the public sector mandate and address any threats to independence in that context. | <ul style="list-style-type: none"> <li>No change identified</li> </ul>   | N/A   | N/A                |
| ISQC 1<br>Paragraph A18 | Consideration of whether the firm has the competence, capabilities, and resources to undertake a new engagement from a new or an existing client involves reviewing the specific requirements of the engagement and the existing partner and staff profiles at all relevant levels, and including whether:   | <ul style="list-style-type: none"> <li>Paragraphs 320.3 A4 and 320.3 A5 explain factors that may be relevant in evaluating a threat and</li> </ul> | N/A   | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|---|---|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                         | <ul style="list-style-type: none"> <li>Firm personnel have knowledge of relevant industries or subject matters;</li> <li>Firm personnel have experience with relevant regulatory or reporting requirements, or the ability to gain the necessary skills and knowledge effectively;</li> <li>The firm has sufficient personnel with the necessary competence and capabilities;</li> <li>Experts are available, if needed;</li> <li>Individuals meeting the criteria and eligibility requirements to perform engagement quality control review are available, where applicable; and</li> <li>The firm is able to complete the engagement within the reporting deadline.</li> </ul> | possible safeguards   |   |                    |
| ISQC 1<br>Paragraph A19 | <p>With regard to the integrity of a client, matters to consider include, for example:</p> <ul style="list-style-type: none"> <li>The identity and business reputation of the client's principal owners, key management, and those charged with its governance.</li> <li>The nature of the client's operations, including its business practices.</li> </ul>   | <ul style="list-style-type: none"> <li>No similar guidance or requirements exist in the Code</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|--|---|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change                         | Category of change |
|                         | <ul style="list-style-type: none"> <li>Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment.</li> <li>Whether the client is aggressively concerned with maintaining the firm's fees as low as possible.</li> <li>Indications of an inappropriate limitation in the scope of work.</li> <li>Indications that the client might be involved in money laundering or other criminal activities.</li> <li>The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.</li> <li>The identity and business reputation of related parties.</li> </ul> <p>The extent of knowledge a firm will have regarding the integrity of a client will generally grow within the context of an ongoing relationship with that client.</p> |  |   |                    |
| ISQC 1<br>Paragraph A20 | Sources of information on such matters obtained by the firm may include the following:   | <ul style="list-style-type: none"> <li>Paragraph R320.8 requires the firm to make</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|---|---|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                         | <ul style="list-style-type: none"> <li>Communications with existing or previous providers of professional accountancy services to the client in accordance with relevant ethical requirements, and discussions with other third parties.</li> <li>Inquiry of other firm personnel or third parties such as bankers, legal counsel and industry peers.</li> <li>Background searches of relevant databases.</li> </ul> | enquiries of an existing or predecessor accountant when accepting an engagement, in the case of an audit or review. For other engagement types, this is optional as explained in paragraph 320.4 A4. This is broadly covered in the first bullet although it is noted that in ISA 220 this was more specifically explained as part of the conforming amendments in the NOCLAR project |   |                    |
| ISQC 1<br>Paragraph A21 | Deciding whether to continue a client relationship includes consideration of significant matters that have arisen during the current or previous engagements, and  | <ul style="list-style-type: none"> <li>No change identified (see</li> </ul>   | N/A                                     | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code                               | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|--|---|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change                         | Category of change |
|                         | their implications for continuing the relationship. For example, a client may have started to expand its business operations into an area where the firm does not possess the necessary expertise.   | paragraph R320.9)  |   |                    |
| ISQC 1<br>Paragraph A22 | <p>Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship address issues that include the following:</p> <ul style="list-style-type: none"> <li>Discussing with the appropriate level of the client's management and those charged with its governance the appropriate action that the firm might take based on the relevant facts and circumstances.</li> <li>If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client's management and those charged with its governance withdrawal from the engagement or from both the engagement and the client relationship, and the reasons for the withdrawal.</li> <li>Considering whether there is a professional, legal or regulatory requirement for the firm to remain in place, or for the firm to report the</li> </ul> | <ul style="list-style-type: none"> <li>No change identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|-------------------------|---|---|---|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                         | <p>withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities.</p> <ul style="list-style-type: none"> <li>Documenting significant matters, consultations, conclusions and the basis for the conclusions.</li> </ul>   |   |   |                    |
| ISQC 1<br>Paragraph A25 | <p>Competence can be developed through a variety of methods, including the following:</p> <ul style="list-style-type: none"> <li>Professional education.</li> <li>Continuing professional development, including training.</li> <li>Work experience.</li> <li>Coaching by more experienced staff, for example, other members of the engagement team.</li> <li>Independence education for personnel who are required to be independent.</li> </ul> | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |
| ISQC 1<br>Paragraph A51 | <p>In the public sector, a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General) may act in a role equivalent to that of engagement partner with overall responsibility for public sector</p>  | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code                                    | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|---|---|--|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                         | audits. In such circumstances, where applicable, the selection of the engagement quality control reviewer includes consideration of the need for independence from the audited entity and the ability of the engagement quality control reviewer to provide an objective evaluation.  |   |  |                    |
| ISQC 1<br>Paragraph A56 | <p>Relevant ethical requirements establish an obligation for the firm's personnel to observe at all times the confidentiality of information contained in engagement documentation, unless specific client authority has been given to disclose information, or there are responsibilities under law, regulation or relevant ethical requirements to do so.<sup>5</sup> Specific laws or regulations may impose additional obligations on the firm's personnel to maintain client confidentiality, particularly where data of a personal nature are concerned</p> <p><sup>5</sup> See, for example, Section 140.7 and Section 225.35 of the IESBA Code.</p> | <ul style="list-style-type: none"> <li>Update footnote reference</li> </ul> | <p>Relevant ethical requirements establish an obligation for the firm's personnel to observe at all times the confidentiality of information contained in engagement documentation, unless specific client authority has been given to disclose information, or there are responsibilities under law, regulation or relevant ethical requirements to do so.<sup>5</sup> Specific laws or regulations may impose additional obligations on the firm's personnel to maintain client confidentiality, particularly where data of a personal nature are concerned.</p> <p><sup>5</sup> See, for example, <u>paragraphs R114.1, 114.1 A1 and R360.26</u> <del>Section 140.7 and Section 225.35</del> of the IESBA Code.</p> | 1                  |
| ISQC 1<br>Paragraph A63 | Unless otherwise specified by law or regulation, engagement documentation is the property of the firm. The firm may, at its discretion, make portions of, or extracts from, engagement documentation available to   | <ul style="list-style-type: none"> <li>N/A</li> </ul>                       | N/A  | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code                | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|---|---|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                         | clients, provided such disclosure does not undermine the validity of the work performed, or, in the case of assurance engagements, the independence of the firm or its personnel.  |   |   |                    |
| ISQC 1<br>Paragraph A65 | <p>Ongoing consideration and evaluation of the system of quality control include matters such as the following:</p> <ul style="list-style-type: none"> <li>• Analysis of: <ul style="list-style-type: none"> <li>◦ New developments in professional standards and applicable legal and regulatory requirements, and how they are reflected in the firm's policies and procedures where appropriate;</li> <li>◦ Written confirmation of compliance with policies and procedures on independence;</li> <li>◦ Continuing professional development, including training; and</li> <li>◦ Decisions related to acceptance and continuance of client relationships and specific engagements.</li> </ul> </li> </ul> <p>...</p> | <ul style="list-style-type: none"> <li>• N/A</li> </ul> | N/A                                     | N/A                |



| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|-------------------------|---|---|---|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change                         | Category of change |
| ISQC 1<br>Paragraph A73 | <p>The form and content of documentation evidencing the operation of each of the elements of the system of quality control is a matter of judgment and depends on a number of factors, including the following:</p> <ul style="list-style-type: none"> <li>The size of the firm and the number of offices.</li> <li>The nature and complexity of the firm's practice and organization.</li> </ul> <p>For example, large firms may use electronic databases to document matters such as independence confirmations, performance evaluations and the results of monitoring inspections.</p> | <ul style="list-style-type: none"> <li>N/A</li> </ul>                   | N/A                                     | N/A                |
| ISA 200<br>Paragraph 14 | <p>The auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. (Ref: Para. A16–A19)</p>   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 200<br>Paragraph A5 | <p>The applicable financial reporting framework often encompasses financial reporting standards established by an authorized or recognized standards setting organization, or legislative or regulatory requirements. In some cases, the financial reporting framework may encompass both financial reporting standards established by an</p>   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards |   | Notes in Relation to the 2018 IESBA Code | Proposed Changes to the IAASB Standards |                    |
|-----------------|---|--|---|--------------------|
| Standard        | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                 | <p>authorized or recognized standards setting organization and legislative or regulatory requirements. Other sources may provide direction on the application of the applicable financial reporting framework. In some cases, the applicable financial reporting framework may encompass such other sources, or may even consist only of such sources. Such other sources may include:</p> <ul style="list-style-type: none"> <li>• The legal and ethical environment, including statutes, regulations, court decisions, and professional ethical obligations in relation to accounting matters;</li> <li>• Published accounting interpretations of varying authority issued by standards setting, professional or regulatory organizations;</li> <li>• Published views of varying authority on emerging accounting issues issued by standards setting, professional or regulatory organizations;</li> <li>• General and industry practices widely recognized and prevalent; and</li> <li>• Accounting literature.</li> </ul> |  |   |                    |

| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|---|--|--|--------------------|
| Standard                 | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                          | Where conflicts exist between the financial reporting framework and the sources from which direction on its application may be obtained, or among the sources that encompass the financial reporting framework, the source with the highest authority prevails.   |  |  |                    |
| ISA 200<br>Paragraph A16 | The auditor is subject to relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. Relevant ethical requirements ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) related to an audit of financial statements together with national requirements that are more restrictive. | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>Remove references to the parts so that Code is referenced holistically</li> </ul>        | The auditor is subject to relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. Relevant ethical requirements ordinarily comprise <u>the provisions</u> <del>Parts A and B</del> of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) related to an audit of financial statements, together with national requirements that are more restrictive. | 1 & 3              |
| ISA 200<br>Paragraph A17 | Part A of the IESBA Code establishes the fundamental principles of professional ethics relevant to the auditor when conducting an audit of financial statements and provides a conceptual framework for applying those principles. The fundamental principles with which the auditor is required to comply by the IESBA Code are:<br><br>(a) Integrity;   | <ul style="list-style-type: none"> <li>Aligning with terminology used in the Code and to reflect the structural changes to the Code (also refer comments in</li> </ul> | <del>Part A of the</del> IESBA Code establishes the fundamental principles of ethics, <u>which are</u> <del>and provides a conceptual framework for applying those principles. The fundamental principles with which the auditor is required to comply by the IESBA Code are:</del><br><br>(a) Integrity;<br>(b) Objectivity;  | 1 & 4              |

| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|---|--|--|--------------------|
| Standard                 | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                          | <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> <p>(e) Professional behavior.</p> <p>Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations.</p>  | paragraph A7 of ISQC 1)  | <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> <p>(e) Professional behavior.</p> <p><del>Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations.</del> <u>The fundamental principles of ethics establish the standard of behavior expected of a professional accountant.</u></p> <p><u>The IESBA Code provides a conceptual framework that professional accountants are to apply in order to identify, evaluate and address threats to compliance with the fundamental principles. In the case of audits, reviews and other assurance engagements, the IESBA Code sets out <i>International Independence Standards</i>, which apply the conceptual framework of identifying, evaluating and addressing threats to the fundamental principles and compliance with independence requirements.</u></p> |                    |
| ISA 200<br>Paragraph A18 | In the case of an audit engagement it is in the public interest and, therefore, required by the IESBA Code, that the auditor be independent of the entity subject to the audit. The IESBA Code describes independence as comprising both independence of mind and independence in appearance. The auditor's independence from the entity safeguards the auditor's | <ul style="list-style-type: none"> <li>No changes identified (see paragraph 400.1, 400.5)</li> </ul> | N/A  | N/A                |

| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|---|---|--|--------------------|
| Standard                 | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                          | ability to form an audit opinion without being affected by influences that might compromise that opinion. Independence enhances the auditor's ability to act with integrity, to be objective and to maintain an attitude of professional skepticism.  |   |  |                    |
| ISA 200<br>Paragraph A19 | International Standard on Quality Control (ISQC) 1, or national requirements that are at least as demanding, deal with the firm's responsibilities to establish and maintain its system of quality control for audit engagements. ISQC 1 sets out the responsibilities of the firm for establishing policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements, including those pertaining to independence. ISA 220 sets out the engagement partner's responsibilities with respect to relevant ethical requirements. These include remaining alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team, determining the appropriate action if matters come to the engagement partner's attention that indicate that members of the engagement team have not complied with relevant | <ul style="list-style-type: none"> <li>The Code refers to breaches, rather than non-compliance</li> </ul> | International Standard on Quality Control (ISQC) 1, or national requirements that are at least as demanding, deal with the firm's responsibilities to establish and maintain its system of quality control for audit engagements. ISQC 1 sets out the responsibilities of the firm for establishing policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements, including those pertaining to independence. ISA 220 sets out the engagement partner's responsibilities with respect to relevant ethical requirements. These include remaining alert, through observation and making inquiries as necessary, for evidence of <del>non-compliance with</del> <u>breaches of</u> relevant ethical requirements by members of the engagement team, determining the appropriate action if matters come to the engagement partner's attention that indicate that members of the engagement team have <del>not complied with</del> <u>breached</u> relevant ethical requirements, and forming a conclusion on compliance with independence requirements that apply to the | 4                  |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|--|---|--|--------------------|
| Standard                 | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                          | ethical requirements, and forming a conclusion on compliance with independence requirements that apply to the audit engagement. ISA 220 recognizes that the engagement team is entitled to rely on a firm's system of quality control in meeting its responsibilities with respect to quality control procedures applicable to the individual audit engagement, unless information provided by the firm or other parties suggests otherwise. |   | audit engagement. ISA 220 recognizes that the engagement team is entitled to rely on a firm's system of quality control in meeting its responsibilities with respect to quality control procedures applicable to the individual audit engagement, unless information provided by the firm or other parties suggests otherwise. |                    |
| ISA 200<br>Paragraph A25 | Professional judgment is essential to the proper conduct of an audit. This is because interpretation of relevant ethical requirements and the ISAs and the informed decisions required throughout the audit cannot be made without the application of relevant knowledge and experience to the facts and circumstances. Professional judgment is necessary in particular regarding decisions about:<br><br>...                               | <ul style="list-style-type: none"> <li>Paragraphs 120.5 A1 to 120.5 A4 explains the exercise of professional judgment in the context of the Code. This is new application material from the extant Code. It explains how the professional accountant applies professional judgment. No</li> </ul> | N/A  | N/A                |

| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|--------------------------|---|--|---|--------------------|
| Standard                 | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                          |   | conforming changes are needed because the Code explanation of professional judgment relates to the application of the Code |   |                    |
| ISA 200<br>Paragraph A26 | The distinguishing feature of the professional judgment expected of an auditor is that it is exercised by an auditor whose training, knowledge and experience have assisted in developing the necessary competencies to achieve reasonable judgments.   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>  | N/A                                     | N/A                |
| ISA 210<br>Paragraph A1  | Assurance engagements, which include audit engagements, may only be accepted when the practitioner considers that relevant ethical requirements such as independence and professional competence will be satisfied, and when the engagement exhibits certain characteristics. <sup>7</sup> The auditor's responsibilities in respect of ethical requirements in the context of the acceptance of an audit engagement and in so far as they are within the control of the auditor are dealt with in ISA 220. <sup>8</sup> This ISA | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>  | N/A                                     | N/A                |

| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code                                  | Proposed Changes to the IAASB Standards |                    |
|--------------------------|---|---|---|--------------------|
| Standard                 | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                          | <p>deals with those matters (or preconditions) that are within the control of the entity and upon which it is necessary for the auditor and the entity's management to agree.</p> <p><sup>7</sup> International Framework for Assurance Engagements, paragraph 17</p> <p><sup>8</sup> ISA 220, paragraphs 9–11</p>  |   |   |                    |
| ISA 210<br>Paragraph A26 | <p>When relevant, the following points could also be made in the audit engagement letter:</p> <ul style="list-style-type: none"> <li>• Arrangements concerning the involvement of other auditors and experts in some aspects of the audit.</li> <li>• Arrangements concerning the involvement of internal auditors and other staff of the entity.</li> <li>• Arrangements to be made with the predecessor auditor, if any, in the case of an initial audit.</li> <li>• A reference to, and description of, the auditor's responsibilities under law, regulation or relevant ethical requirements that address reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.</li> </ul> | <ul style="list-style-type: none"> <li>• No changes identified</li> </ul> | N/A                                     | N/A                |



| IAASB Standards        |  | Notes in Relation to the 2018 IESBA Code                               | Proposed Changes to the IAASB Standards |                    |
|------------------------|--|--|---|--------------------|
| Standard               | Extant Paragraphs  |  | Proposed Change                         | Category of change |
|                        | <ul style="list-style-type: none"> <li>Any restriction of the auditor's liability when such possibility exists.</li> <li>A reference to any further agreements between the auditor and the entity.</li> <li>Any obligations to provide audit working papers to other parties.</li> </ul> <p>An example of an audit engagement letter is set out in Appendix 1.</p>             |  |   |                    |
| ISA 210<br>Appendix 1  | <p>Example of an Audit Engagement Letter [...]</p> <p>[The responsibilities of the auditor]</p> <p>We will conduct our audit in accordance with ISAs. Those standards require that we comply with ethical requirements. As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:</p> | <ul style="list-style-type: none"> <li>No change identified</li> </ul> | N/A                                     | N/A                |
| ISA 220<br>Paragraph 3 | <p>Within the context of the firm's system of quality control, engagement teams have a responsibility to implement quality control procedures that are applicable to the audit engagement and provide the firm with relevant information to enable the</p>   | <ul style="list-style-type: none"> <li>N/A</li> </ul>                  | N/A                                     | N/A                |

| IAASB Standards           |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|---------------------------|--|--|---|--------------------|
| Standard                  | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                           | functioning of that part of the firm's system of quality control relating to independence.   |  |   |                    |
| ISA 220<br>Paragraph 7(n) | <p>For purposes of the ISAs, the following terms have the meanings attributed below:</p> <p>...</p> <p>(n) Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) related to an audit of financial statements together with national requirements that are more restrictive.</p> <p>...</p> | <ul style="list-style-type: none"> <li>Update title and references to the Code</li> <li>Parts A, B and C have been renamed and there are now International Independence Standards (Parts 4A and 4B)</li> </ul> | <p>For purposes of the ISAs, the following terms have the meanings attributed below:</p> <p>...</p> <p>Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject <u>when undertaking an audit engagement</u>, which ordinarily comprise <u>the provisions of Parts A and B</u> of the International Ethics Standards Board for Accountants' <u>International Code of Ethics for Professional Accountants (including International Independence Standards)</u> (IESBA Code) related to an audit of financial statements, together with national requirements that are more restrictive.</p> <p>...</p> | 1 & 3              |
| ISA 220<br>Paragraph 9    | Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. (Ref: Para. A4–A5)   | <ul style="list-style-type: none"> <li>The Code refers to breaches, rather than non-compliance. Perhaps this is a better phrase, also given the more recent</li> </ul>   | Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of <u>breaches of non-compliance with</u> relevant ethical requirements by members of the engagement team. (Ref: Para. A4–A5)   | 4                  |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|-------------------------|--|--|---|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                         |  | introduction of non-compliance in the Code that has another meaning  |   |                    |
| ISA 220<br>Paragraph 10 | If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)   | <ul style="list-style-type: none"> <li>The Code refers to breaches, rather than non-compliance</li> </ul>  | If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have <del>not complied with</del> <u>breached</u> relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)   | 4                  |
| ISA 220<br>Paragraph 11 | <p>The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall: (Ref: Para. A5)</p> <p>(a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence;</p> <p>(b) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether</p> | <ul style="list-style-type: none"> <li>The revised Code describes threats to compliance differently</li> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how identified threats are addressed</li> </ul> | <p>The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall: (Ref: Para. A5)</p> <p>(a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate <del>circumstances and relationships that create</del> threats to independence;</p> <p>(b) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement; <del>and</del></p> | 2 & 4              |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|---|--|--|--------------------|
| Standard                | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                         | <p>they create a threat to independence for the audit engagement; and</p> <p>(c) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is possible under applicable law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action. (Ref: Para. A6–A7)</p> |  | <p>(c) <u>Evaluate whether the identified threats are at an acceptable level; and</u></p> <p>(d) <u>Take appropriate action to address the threats by eliminating the circumstances that create the threats, applying safeguards, or withdrawing—</u><del>Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw</del> from the engagement, where withdrawal is possible under applicable law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action. (Ref: Para. A6–A7)</p> |                    |
| ISA 220<br>Paragraph 12 | The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate. (Ref: Para. A8-A10)   | <ul style="list-style-type: none"> <li>No change identified (see Section 320)</li> </ul>     | N/A  | N/A                |
| ISA 220<br>Paragraph 13 | If the engagement partner obtains information that would have caused the firm to decline the audit engagement had that information been available earlier, the engagement partner shall communicate that information promptly to the firm, so that  | <ul style="list-style-type: none"> <li>No change identified (see paragraph 320.9)</li> </ul> | N/A  | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code                               | Proposed Changes to the IAASB Standards |                    |
|-------------------------|---|--|---|--------------------|
| Standard                | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                         | the firm and the engagement partner can take the necessary action. (Ref: Para. A9)  |  |   |                    |
| ISA 220<br>Paragraph 21 | <p>For audits of financial statements of listed entities, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following:</p> <p>(a) The engagement team's evaluation of the firm's independence in relation to the audit engagement;</p> <p>(b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and</p> <p>(c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A29–A32)</p> | <ul style="list-style-type: none"> <li>N/A</li> </ul>                  | N/A                                     | N/A                |
| ISA 220<br>Paragraph 24 | <p>The auditor shall include in the audit documentation:<sup>5</sup></p> <p>(a) Issues identified with respect to compliance with relevant ethical</p>  | <ul style="list-style-type: none"> <li>No change identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|---|---|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                         | <p>requirements and how they were resolved.</p> <p>(b) Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the firm that support these conclusions.</p> <p>(c) Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements.</p> <p>(d) The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement.<br/>(Ref: Para. A37)</p> <p>5 ISA 230, <i>Audit Documentation</i>, paragraphs 8-11, and A6</p> |   |   |                    |
| ISA 220<br>Paragraph A2 | <p>Unless information provided by the firm or other parties suggest otherwise, the engagement team may rely on the firm's system of quality control in relation to, for example:</p> <ul style="list-style-type: none"> <li>Competence of personnel through their recruitment and formal training.</li> <li>Independence through the accumulation and communication of relevant independence information.</li> </ul>   | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-------------------------|---|---|---|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                         | <ul style="list-style-type: none"> <li>Maintenance of client relationships through acceptance and continuance systems.</li> <li>Adherence to applicable legal and regulatory requirements through the monitoring process.</li> </ul>  |   |   |                    |
| ISA 220<br>Paragraph A4 | <p>The IESBA Code establishes the fundamental principles of professional ethics, which include:</p> <ul style="list-style-type: none"> <li>(a) Integrity;</li> <li>(b) Objectivity;</li> <li>(c) Professional competence and due care;</li> <li>(d) Confidentiality; and</li> <li>(e) Professional behavior.</li> </ul> | <ul style="list-style-type: none"> <li>Refer to comments in paragraph A7 of ISQC 1</li> </ul> | <p>The IESBA Code establishes the fundamental principles of <del>professional</del> ethics which <del>include</del> are:</p> <ul style="list-style-type: none"> <li>(a) Integrity;</li> <li>(b) Objectivity;</li> <li>(c) Professional competence and due care;</li> <li>(d) Confidentiality; and</li> <li>(e) Professional behavior.</li> </ul> <p><u>The fundamental principles of ethics establish the standard of behavior expected of a professional accountant.</u></p> | 4                  |
| ISA 220<br>Paragraph A5 | <p>The definitions of “firm,” “network” or “network firm” in relevant ethical requirements may differ from those set out in this ISA. For example, the IESBA Code defines the “firm” as:</p>  | <ul style="list-style-type: none"> <li>No change identified</li> </ul>                        | N/A   | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|-------------------------|--|--|---|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                         | <p>(a) A sole practitioner, partnership or corporation of professional accountants;</p> <p>(b) An entity that controls such parties through ownership, management or other means; and</p> <p>(c) An entity controlled by such parties through ownership, management or other means.</p> <p>The IESBA Code also provides guidance in relation to the terms “network” and “network firm.”</p> <p>In complying with the requirements in paragraphs 9–11, the definitions used in the relevant ethical requirements apply in so far as is necessary to interpret those ethical requirements.</p> |  |   |                    |
| ISA 220<br>Paragraph A6 | The engagement partner may identify a threat to independence regarding the audit engagement that safeguards may not be able to eliminate or reduce to an acceptable level. In that case, as required by paragraph 11(c), the engagement partner reports to the relevant person(s) within the firm to determine appropriate action, which may include eliminating the activity or interest that creates the threat, or withdrawing from   | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how identified threats are addressed</li> </ul> | The engagement partner may identify a threat to independence regarding the audit engagement that safeguards may not be able to <del>eliminate or</del> reduce to an acceptable level. In that case, as required by paragraph 11(c), the engagement partner reports to the relevant person(s) within the firm to determine <u>the</u> appropriate action, which may include eliminating the <u>circumstance that is creating activity or interest that creates the</u> threat, or withdrawing from the audit | 2                  |



| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards                                      |                    |
|-------------------------|---|---|--|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                         | the audit engagement, where withdrawal is possible under applicable law or regulation.  |   | engagement, where withdrawal is possible under applicable law or regulation. |                    |
| ISA 220<br>Paragraph A7 | Statutory measures may provide safeguards for the independence of public sector auditors. However, public sector auditors or audit firms carrying out public sector audits on behalf of the statutory auditor may, depending on the terms of the mandate in a particular jurisdiction, need to adapt their approach in order to promote compliance with the spirit of paragraph 11. This may include, where the public sector auditor's mandate does not permit withdrawal from the engagement, disclosure through a public report, of circumstances that have arisen that would, if they were in the private sector, lead the auditor to withdraw. | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                   | N/A  | N/A                |
| ISA 220<br>Paragraph A8 | ISQC 1 requires the firm to obtain information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. Information such as the following assists the engagement partner in   | <ul style="list-style-type: none"> <li>No changes identified (see Section 320)</li> </ul> | N/A  | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|---|---|--|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                         | <p>determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate:</p> <ul style="list-style-type: none"> <li>• The integrity of the principal owners, key management and those charged with governance of the entity;</li> <li>• Whether the engagement team is competent to perform the audit engagement and has the necessary capabilities, including time and resources;</li> <li>• Whether the firm and the engagement team can comply with relevant ethical requirements; and</li> <li>• Significant matters that have arisen during the current or previous audit engagement, and their implications for continuing the relationship.</li> </ul> |   |  |                    |
| ISA 220<br>Paragraph A9 | Law, regulation, or relevant ethical requirements <sup>7</sup> may require the auditor to request, prior to accepting the engagement, the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor's judgment, the auditor needs to be aware of before deciding whether to accept the engagement. In some circumstances,  | <ul style="list-style-type: none"> <li>• Update footnote paragraph references</li> <li>• No other changes identified</li> </ul> | <p>7 See, for example, <u>paragraph R320.8</u> <del>Sections 240.14</del> of the IESBA Code.</p> <p>8 See, for example, <u>paragraph R360.22</u> <del>Sections 225.34</del> of the IESBA Code.</p> | 1                  |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|--------------------------|--|---|---|--------------------|
| Standard                 | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                          | <p>the predecessor auditor may be required, on request by the proposed successor auditor, to provide information regarding identified or suspected non-compliance with laws and regulations to the proposed successor auditor. For example, where the predecessor auditor has withdrawn from the engagement as a result of identified or suspected non-compliance with laws and regulations, the IESBA Code requires that the predecessor auditor, on request by a proposed successor auditor, provides all such facts and other information concerning such non-compliance that, in the predecessor auditor's opinion, the proposed successor auditor needs to be aware of before deciding whether to accept the audit appointment.<sup>8</sup></p> <p>7 See, for example, Sections 210.14 of the IESBA Code.</p> <p>8 See, for example, Sections 225.31 of the IESBA Code.</p> |   |   |                    |
| ISA 220<br>Paragraph A32 | In the public sector, a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General), may act in a role equivalent to that of engagement partner with overall responsibility for public sector audits. In such circumstances, where  | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards        |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|------------------------|---|---|---|--------------------|
| Standard               | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                        | applicable, the selection of the engagement quality control reviewer includes consideration of the need for independence from the audited entity and the ability of the engagement quality control reviewer to provide an objective evaluation.   |   |   |                    |
| ISA 240<br>Paragraph 9 | <p>The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, including fraud, which may differ from or go beyond this and other ISAs, such as: (Ref: Para. A6)</p> <p>(a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance, assessing the appropriateness of their response to non-compliance and determining whether further action is needed;</p> <p>(b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of group financial statements); and</p> | <ul style="list-style-type: none"> <li>No changes identified – see section 360</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|-------------------------|---|--|--|--------------------|
| Standard                | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                         | <p>(c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.</p> <p>Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other ISAs (e.g., regarding the integrity of management or, where appropriate, those charged with governance).</p>                         |  |  |                    |
| ISA 240<br>Paragraph 44 | <p>If the auditor has identified or suspects a fraud, the auditor shall determine whether law, regulation or relevant ethical requirements: (Ref: Para. A67–A69)</p> <p>(a) Require the auditor to report to an appropriate authority outside the entity.</p> <p>(b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.</p> | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.21, 360.21 A1, 360.25 A1–R360.26</li> </ul> | N/A  | N/A                |
| ISA 240<br>Paragraph A6 | <p>Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the <i>Code of Ethics for Professional Accountants</i> issued</p>   | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>No other changes identified – see</li> </ul>     | <p>Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the <u>International Ethics Standards Board for Accountants' International Code of</u></p> | 1 & 3              |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards   |                    |
|--------------------------|--|---|---|--------------------|
| Standard                 | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                          | <p>by the International Ethics Standards Board for Accountants (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements.<sup>15</sup></p> <p>15 See, for example, Sections 225.21–225.22 of the IESBA Code.</p> | paragraph R360.10–R360.28   | <p><i>Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements.<sup>15</sup></p> <p>15 See, for example, <u>paragraphs R360.16–360.18 A1</u> <del>Sections 225.21–225.22</del> of the IESBA Code.</p> |                    |
| ISA 240<br>Paragraph A57 | The auditor has professional and legal responsibilities in such circumstances and these responsibilities may vary by country. In some countries, for example, the auditor may be entitled to, or required to, make a statement or report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities. Given the exceptional nature of the circumstances and the need to consider the legal requirements, the auditor may consider it appropriate to seek legal advice when deciding whether to withdraw from an   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A   | N/A                |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|--------------------------|--|---|---|--------------------|
| Standard                 | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                          | <p>engagement and in determining an appropriate course of action, including the possibility of reporting to shareholders, regulators or others.<sup>24</sup></p> <p>24 The IESBA Code provides guidance on communications with an auditor replacing the existing auditor.</p>  |   |   |                    |
| ISA 240<br>Paragraph A67 | <p>ISA 250 (Revised)<sup>27</sup> provides further guidance with respect to the auditor's determination of whether reporting identified or suspected non-compliance with laws or regulations to an appropriate authority outside the entity is required or appropriate in the circumstances, including consideration of the auditor's duty of confidentiality.</p> <p>27 ISA 250 (Revised), <i>Consideration of Laws and Regulations in an Audit of Financial Statements</i>, paragraphs A28-A34</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 240<br>Paragraph A68 | <p>The determination required by paragraph 44 may involve complex considerations and professional judgments. Accordingly, the auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The</p>  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                  |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|----------------------------------|---|--|---|--------------------|
| Standard                         | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                                  | auditor may also consider obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular course of action.  |  |   |                    |
| ISA 250 (Revised)<br>Paragraph 3 | It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements.  | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.8 A1</li> </ul> | N/A                                     | N/A                |
| ISA 250 (Revised)<br>Paragraph 6 | <p>This ISA distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows: (Ref: Para. A6, A12–A13)</p> <p>(a) The provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements such as tax and pension laws and regulations (see paragraph 14) (Ref: Para. A12);</p> <p>(b) Other laws and regulations that do not have a direct effect on the</p> | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.3</li> </ul>    | N/A                                     | N/A                |



| IAASB Standards                     |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|-------------------------------------|---|---|---|--------------------|
| Standard                            | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                                     | determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (e.g., compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations therefore have a material effect on the financial statements (see paragraph 15) (Ref: Para. A13). |   |   |                    |
| ISA 250<br>(Revised)<br>Paragraph 9 | <p>The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond this ISA, such as: (Ref: Para. A8)</p> <p>(a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance, assessing the appropriateness of</p>   | <ul style="list-style-type: none"> <li>No changes identified – see section 360</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                   |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|-----------------------------------|--|---|---|--------------------|
| Standard                          | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                   | <p>their response to non-compliance and determining whether further action is needed;</p> <p>(b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of group financial statements); and</p> <p>(c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.</p> <p>Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other ISAs (e.g., regarding the integrity of management or, where appropriate, those charged with governance).</p> |   |   |                    |
| ISA 250 (Revised)<br>Paragraph 12 | <p>For the purposes of this ISA, the following term has the meaning attributed below:</p> <p>Non-compliance – Acts of omission or commission, intentional or unintentional, committed by the entity, or by those charged with governance, by management or by other individuals working for or under the direction of the entity, which are contrary to the prevailing laws or regulations. Non-</p>   | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.5 A1 and 360.7 A3</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|---|--|---|--------------------|
| Standard                             | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                                      | compliance does not include personal misconduct unrelated to the business activities of the entity. (Ref: Para. A9–A10)   |  |   |                    |
| ISA 250<br>(Revised)<br>Paragraph 29 | <p>If the auditor has identified or suspects non-compliance with laws and regulations, the auditor shall determine whether law, regulation or relevant ethical requirements: (Ref: Para. A28–A34)</p> <p>(a) Require the auditor to report to an appropriate authority outside the entity.</p> <p>(b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.</p>  | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.21, 360.21 A1, 360.25 A1–R360.26</li> </ul> | N/A                                     | N/A                |
| ISA 250<br>(Revised)<br>Paragraph A6 | <p>The nature and circumstances of the entity may impact whether relevant laws and regulations are within the categories of laws and regulations described in paragraphs 6(a) or 6(b). Examples of laws and regulations that may be included in the categories described in paragraph 6 include those that deal with:</p> <ul style="list-style-type: none"> <li>Fraud, corruption and bribery.</li> <li>Money laundering, terrorist financing and proceeds of crime.</li> <li>Securities markets and trading.</li> </ul> | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.5 A2</li> </ul>                               | N/A                                     | N/A                |

| IAASB Standards                |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------|--|---|---|--------------------|
| Standard                       | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                | <ul style="list-style-type: none"> <li>Banking and other financial products and services.</li> <li>Data protection.</li> <li>Tax and pension liabilities and payments.</li> <li>Environmental protection.</li> <li>Public health and safety.</li> </ul>  |   |   |                    |
| ISA 250 (Revised) Paragraph A8 | Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements. <sup>11</sup> | <ul style="list-style-type: none"> <li>Update title and references to the Code</li> <li>No other change identified – see paragraph R360.10–R360.28</li> </ul> | Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the <del>Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards)</del> (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes | 1 & 3              |

| IAASB Standards                 |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------|---|--|--|--------------------|
| Standard                        | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                                 | 11 See, for example, Sections 225.21–225.22 of the IESBA Code.  |  | other than the audit of the group financial statements. <sup>11</sup><br><br>11 See, for example, <u>paragraphs R360.16–360.18 A1</u> <del>Sections 225.21–225.22</del> of the IESBA Code. |                    |
| ISA 250 (Revised) Paragraph A9  | Acts of non-compliance with laws and regulations include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, by management or by other individuals working for or under the direction of the entity.   | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.5 A1</li> </ul>               | N/A  | N/A                |
| ISA 250 (Revised) Paragraph A10 | Non-compliance also includes personal misconduct related to the business activities of the entity, for example, in circumstances where an individual in a key management position, in a personal capacity, has accepted a bribe from a supplier of the entity and in return secures the appointment of the supplier to provide services or contracts to the entity. | <ul style="list-style-type: none"> <li>No changes identified (no corresponding paragraph)</li> </ul>           | N/A  | N/A                |
| ISA 250 (Revised) Paragraph A25 | In certain circumstances, the auditor may consider withdrawing from the engagement, where permitted by law or regulation, for example when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances or the identified or suspected non-compliance                                    | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs 360.20 A1 – 360.21 A2</li> </ul> | N/A  | N/A                |

| IAASB Standards                    |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|------------------------------------|---|---|---|--------------------|
| Standard                           | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                                    | <p>raises questions regarding the integrity of management or those charged with governance, even when the non-compliance is not material to the financial statements. The auditor may consider it appropriate to obtain legal advice to determine whether withdrawal from the engagement is appropriate. When the auditor determines that withdrawing from the engagement would be appropriate, doing so would not be a substitute for complying with other responsibilities under law, regulation or relevant ethical requirements to respond to identified or suspected non-compliance. Furthermore, paragraph A9 of ISA 220<sup>14</sup> indicates that some ethical requirements may require the predecessor auditor, upon request by the proposed successor auditor, to provide information regarding non-compliance with laws and regulations to the successor auditor.</p> <p>14 ISA 220, Quality Control for an Audit of Financial Statements</p> |   |   |                    |
| ISA 250 (Revised)<br>Paragraph A29 | In some jurisdictions, the auditor may be required by law, regulation or relevant ethical requirements to report identified or suspected non-compliance with laws and regulations to an appropriate authority   | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.6</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|------------------------------------|--|---|--|--------------------|
| Standard                           | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                                    | outside the entity. For example, in some jurisdictions, statutory requirements exist for the auditor of a financial institution to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to a supervisory authority. Also, misstatements may arise from non-compliance with laws or regulations and, in some jurisdictions, the auditor may be required to report misstatements to an appropriate authority in cases where management or those charged with governance fail to take corrective action.   |   |  |                    |
| ISA 250 (Revised)<br>Paragraph A30 | In other cases, the relevant ethical requirements may require the auditor to determine whether reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the IESBA Code requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed, which may include reporting to an appropriate authority outside the entity. <sup>17</sup> The IESBA Code explains that such reporting would not be considered a breach | <ul style="list-style-type: none"> <li>• Update footnote references</li> <li>• No other changes identified – see paragraphs 360.21 A1, 360.25 A1–360.227, R114.1, R115.1 A 1 and R360.26</li> </ul> | <p>17 See, for example, <u>paragraphs 360.21 A1 and 360.25 A1–R360.27</u> <del>Section 225.29 and Sections 225.33–225.36</del> of the IESBA Code.</p> <p>18 See, for example, <u>paragraphs R114.1– R114.1 A1 and R360.26</u> <del>Section 140.7 and Section 225.35</del> of the IESBA Code.</p> | 1                  |

| IAASB Standards                 |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|---------------------------------|--|---|---|--------------------|
| Standard                        | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                 | <p>of the duty of confidentiality under the IESBA Code.<sup>18</sup></p> <p>17 See, for example, Section 225.29 and Sections 225.33–225.36 of the IESBA Code.</p> <p>18 See, for example, Section 140.7 and Section 225.35 of the IESBA Code.</p>  |   |   |                    |
| ISA 250 (Revised) Paragraph A32 | In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the auditor's duty of confidentiality under law, regulation or relevant ethical requirements.   | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.6 and 360.25 A1</li> </ul> | N/A                                     | N/A                |
| ISA 250 (Revised) Paragraph A33 | The determination required by paragraph 29 may involve complex considerations and professional judgments. Accordingly the auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The auditor may also consider obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular course of action. | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.24 A1</li> </ul>             | N/A                                     | N/A                |



| IAASB Standards                       |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------------|--|--|--|--------------------|
| Standard                              | Extant Paragraphs  |  | Proposed Change  | Category of change |
| ISA 250<br>(Revised)<br>Paragraph A36 | <p>Law, regulation or relevant ethical requirements may also set out additional documentation requirements regarding identified or suspected non-compliance with laws and regulations.<sup>19</sup></p> <p>19 See, for example, Section 225.37 of the IESBA Code.</p>  | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>No other changes identified – see paragraph R360.28</li> </ul> | 19 See, for example, <del>Section 225.37</del> <u>paragraph R360.28</u> of the IESBA Code. | 1                  |
| ISA 260<br>(Revised)<br>Paragraph 4   | <p>This ISA focuses primarily on communications from the auditor to those charged with governance. Nevertheless, effective two-way communication is important in assisting:</p> <p>(a) The auditor and those charged with governance in understanding matters related to the audit in context, and in developing a constructive working relationship. This relationship is developed while maintaining the auditor's independence and objectivity;</p> <p>(b) The auditor in obtaining from those charged with governance information relevant to the audit. For example, those charged with governance may assist the auditor in understanding the entity and its environment, in identifying appropriate sources of audit evidence, and in providing</p> | <ul style="list-style-type: none"> <li>N/A</li> </ul>  | N/A  | N/A                |

| IAASB Standards                   |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|-----------------------------------|--|---|---|--------------------|
| Standard                          | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                   | <p>information about specific transactions or events; and</p> <p>(c) Those charged with governance in fulfilling their responsibility to oversee the financial reporting process, thereby reducing the risks of material misstatement of the financial statements.</p> |   |   |                    |
| ISA 260 (Revised)<br>Paragraph 11 | The auditor shall determine the appropriate person(s) within the entity's governance structure with whom to communicate. (Ref: Para. A1–A4)  | <ul style="list-style-type: none"> <li>Similar requirements exist in the Code regarding communication with those charged with governance in paragraph R300.9 – R300.10 A1. These are substantially similar to the ISA.</li> </ul> | N/A                                     | N/A                |
| ISA 260 (Revised)<br>Paragraph 12 | If the auditor communicates with a subgroup of those charged with governance, for example, an audit committee, or an individual, the auditor shall determine whether the auditor also needs to communicate with the governing body. (Ref: Para. A5–A7)                 | <ul style="list-style-type: none"> <li>Similar requirements exist in the Code regarding communication with those charged with</li> </ul>  | N/A                                     | N/A                |

| IAASB Standards                   |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-----------------------------------|---|---|---|--------------------|
| Standard                          | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                                   |   | governance in paragraph R300.9 – R300.10 A1. These are substantially similar to the ISA.  |   |                    |
| ISA 260 (Revised)<br>Paragraph 13 | In some cases, all of those charged with governance are involved in managing the entity, for example, a small business where a single owner manages the entity and no one else has a governance role. In these cases, if matters required by this ISA are communicated with person(s) with management responsibilities, and those person(s) also have governance responsibilities, the matters need not be communicated again with those same person(s) in their governance role. These matters are noted in paragraph 16(c). The auditor shall nonetheless be satisfied that communication with person(s) with management responsibilities adequately informs all of those with whom the auditor would otherwise communicate in their governance capacity. (Ref: Para. A8) | <ul style="list-style-type: none"> <li>Similar requirements exist in the Code regarding communication with those charged with governance in paragraph R300.9 – R300.10 A1. These are substantially similar to the ISA.</li> </ul> | N/A   | N/A                |
| ISA 260 (Revised)<br>Paragraph 17 | In the case of listed entities, the auditor shall communicate with those charged with governance:   | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been</li> </ul>  | In the case of listed entities, the auditor shall communicate with those charged with governance: | 2                  |

| IAASB Standards |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-----------------|--|---|--|--------------------|
| Standard        | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                 | <p>(a) A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and</p> <p>(i) All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, may reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor; and</p> | <p>amended from the extant Code, in particular in relation to how identified threats are addressed.</p> | <p>(a) A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and</p> <p>(i) All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor; and</p> <p>(ii) <u>In respect of threats to independence that are not at an acceptable level, the actions taken to address the threat, including actions that were taken to eliminate such threats, or any</u> <del>The</del> related safeguards that have been applied to <del>eliminate identified</del> reduce <del>them</del> <u>the threats</u> to an acceptable level. (Ref: Para. A29–A32)</p> |                    |

| IAASB Standards                 |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|---------------------------------|--|---|---|--------------------|
| Standard                        | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                 | (ii) The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level. (Ref: Para. A29–A32)   |   |   |                    |
| ISA 260 (Revised) Paragraph 20  | The auditor shall communicate in writing with those charged with governance regarding auditor independence when required by paragraph 17.  | <ul style="list-style-type: none"> <li>N/A</li> </ul>   | N/A   | N/A                |
| ISA 260 (Revised) Paragraph A29 | <p>The auditor is required to comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements.<sup>24</sup></p> <p><sup>24</sup> ISA 200, <i>Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing</i>, paragraph 14</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>   | N/A   | N/A                |
| ISA 260 (Revised) Paragraph A30 | <p>The relationships and other matters, and safeguards to be communicated, vary with the circumstances of the engagement, but generally address:</p> <p>(a) Threats to independence, which may be categorized as: self-interest threats, self-review threats, advocacy threats, familiarity threats, and intimidation threats; and</p>                                       | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how</li> </ul> | <p>The <u>communication about</u> relationships and other matters, and <u>how threats to independence that are not at an acceptable level have been addressed</u> <del>safeguards to be communicated</del>, <del>varies</del> with the circumstances of the engagement <u>and generally addresses the threats to independence, safeguards to reduce the threats, and measures to eliminate threats.</u> <del>but generally address:</del></p> | 2                  |

| IAASB Standards                    |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|------------------------------------|---|--|---|--------------------|
| Standard                           | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                                    | (b) Safeguards created by the profession, legislation or regulation, safeguards within the entity, and safeguards within the firm's own systems and procedures  | <p>identified threats are addressed.</p> <ul style="list-style-type: none"> <li>Unlike the previous Code (300.13), the new Code does not refer to safeguards created by the profession etc. (see paragraphs R120.10 – 120.10 A2).</li> </ul> | <p><del>(a) Threats to independence, which may be categorized as: self-interest threats, self-review threats, advocacy threats, familiarity threats, and intimidation threats; and</del></p> <p><del>(b) Safeguards created by the profession, legislation or regulation, safeguards within the entity, and safeguards within the firm's own systems and procedures</del></p>   |                    |
| ISA 260 (Revised)<br>Paragraph A31 | <p>Relevant ethical requirements or law or regulation may also specify particular communications to those charged with governance in circumstances where breaches of independence requirements have been identified. For example, the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) requires the auditor to communicate with those charged with governance in writing about any breach and the action the firm has taken or proposes to take.<sup>25</sup></p> <p><sup>25</sup> See Section 290.39–49 of the IESBA Code, which addresses breaches of independence.</p> | <ul style="list-style-type: none"> <li>Update title and references to the Code</li> </ul>  | <p>Relevant ethical requirements or law or regulation may also specify particular communications to those charged with governance in circumstances where breaches of independence requirements have been identified. For example, the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) requires the auditor to communicate with those charged with governance in writing about any breach and the action the firm has taken or proposes to take.<sup>25</sup></p> | 1 & 3              |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------------|---|---|--|--------------------|
| Standard                              | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                                       |   |   | 25 See, for example, paragraphs R400.81, R400.82 and R400.84 <del>Section 290.39–49</del> of the IESBA Code, which addresses breaches of independence. |                    |
| ISA 260<br>(Revised)<br>Paragraph A32 | The communication requirements relating to auditor independence that apply in the case of listed entities may also be appropriate in the case of some other entities, including those that may be of significant public interest, for example, because they have a large number and wide range of stakeholders and considering the nature and size of the business. Examples of such entities may include financial institutions (such as banks, insurance companies, and pension funds), and other entities such as charities. On the other hand, there may be situations where communications regarding independence may not be relevant, for example, where all of those charged with governance have been informed of relevant facts through their management activities. This is particularly likely where the entity is owner-managed, and the auditor's firm and network firms have little involvement with the entity beyond a financial statement audit. | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A  | N/A                |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|---------------------------------------|---|--|---|--------------------|
| Standard                              | Extant Paragraphs   |  | Proposed Change   | Category of change |
| ISA 260<br>(Revised)<br>Paragraph A49 | <p>Timely communication throughout the audit contributes to the achievement of robust two-way dialogue between those charged with governance and the auditor. However, the appropriate timing for communications will vary with the circumstances of the engagement. Relevant circumstances include the significance and nature of the matter, and the action expected to be taken by those charged with governance. For example:</p> <p>...</p> <ul style="list-style-type: none"> <li>Communications regarding independence may be appropriate whenever significant judgments are made about threats to independence and related safeguards, for example, when accepting an engagement to provide non-audit services, and at a concluding discussion.</li> </ul> <p>...</p> | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how identified threats are addressed</li> </ul> | <p>Timely communication throughout the audit contributes to the achievement of robust two-way dialogue between those charged with governance and the auditor. However, the appropriate timing for communications will vary with the circumstances of the engagement. Relevant circumstances include the significance and nature of the matter, and the action expected to be taken by those charged with governance. For example:</p> <p>...</p> <ul style="list-style-type: none"> <li>Communications regarding independence may be appropriate whenever significant judgments are made about threats to independence and <u>how threats to independence that are not at an acceptable level will be addressed</u> <del>related safeguards</del>, for example, when accepting an engagement to provide non-audit services, and at a concluding discussion.</li> </ul> <p>...</p> | 2                  |
| ISA 300<br>Paragraph 6                | <p>The auditor shall undertake the following activities at the beginning of the current audit engagement:</p> <p>(a) Performing procedures required by ISA 220 regarding the continuance of</p>   | <ul style="list-style-type: none"> <li>N/A</li> </ul>  | N/A   | N/A                |



| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|-------------------------|---|--|---|--------------------|
| Standard                | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                         | <p>the client relationship and the specific audit engagement;<sup>1</sup></p> <p>(b) Evaluating compliance with relevant ethical requirements, including independence, in accordance with ISA 220,<sup>2</sup> and</p> <p>(c) Establishing an understanding of the terms of the engagement, as required by ISA 210.<sup>3</sup> (Ref: Para. A5–A7)</p> <p><sup>1</sup> ISA 220, <i>Quality Control for an Audit of Financial Statements</i>, paragraphs 12–13</p> <p><sup>2</sup> ISA 220, paragraphs 9–11</p> <p><sup>3</sup> ISA 220, <i>Quality Control for an Audit of Financial Statements</i>, paragraphs 12–13</p> |  |   |                    |
| ISA 300<br>Paragraph 13 | <p>The auditor shall undertake the following activities prior to starting an initial audit:</p> <p>(a) Performing procedures required by ISA 220 regarding the acceptance of the client relationship and the specific audit engagement; and</p> <p>(b) Communicating with the predecessor auditor, where there has been a change of auditors, in compliance with relevant ethical requirements. (Ref: Para. A22)</p>  | <ul style="list-style-type: none"> <li>No changes identified – see paragraph R320.8</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|---|---|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change                         | Category of change |
| ISA 300<br>Paragraph A6 | <p>Performing these preliminary engagement activities enables the auditor to plan an audit engagement for which, for example:</p> <ul style="list-style-type: none"> <li>The auditor maintains the necessary independence and ability to perform the engagement.</li> <li>There are no issues with management integrity that may affect the auditor's willingness to continue the engagement.</li> <li>There is no misunderstanding with the client as to the terms of the engagement.</li> </ul>  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 300<br>Paragraph A7 | <p>The auditor's consideration of client continuance and relevant ethical requirements, including independence, occurs throughout the audit engagement as conditions and changes in circumstances occur. Performing initial procedures on both client continuance and evaluation of relevant ethical requirements (including independence) at the beginning of the current audit engagement means that they are completed prior to the performance of other significant activities for the current audit engagement. For continuing audit engagements, such initial procedures often</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|--------------------------|--|---|---|--------------------|
| Standard                 | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                          | occur shortly after (or in connection with) the completion of the previous audit.  |   |   |                    |
| ISA 510<br>Paragraph A5  | Relevant ethical and professional requirements guide the current auditor's communications with the predecessor auditor.  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 550<br>Paragraph A32 | <p>Examples of substantive audit procedures that the auditor may perform when the auditor has assessed a significant risk that management has not appropriately accounted for or disclosed specific related party transactions in accordance with the applicable financial reporting framework (whether due to fraud or error) include:</p> <ul style="list-style-type: none"> <li>Confirming or discussing specific aspects of the transactions with intermediaries such as banks, law firms, guarantors, or agents, where practicable and not prohibited by law, regulation or ethical rules.</li> </ul> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 550<br>Paragraph A36 | <p>Examples of substantive audit procedures that the auditor may perform relating to newly identified related parties or significant related party transactions include:</p> <ul style="list-style-type: none"> <li>Making inquiries regarding the nature of the entity's relationships with the newly identified related parties, including (where appropriate and not prohibited by law, regulation or ethical rules) inquiring of</li> </ul>  | <ul style="list-style-type: none"> <li>No change identified</li> </ul>  | N/A                                     | N/A                |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|-------------------------|--|---|---|--------------------|
| Standard                | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                         | parties outside the entity who are presumed to have significant knowledge of the entity and its business, such as legal counsel, principal agents, major representatives, consultants, guarantors, or other close business partners.   |   |   |                    |
| ISA 600<br>Paragraph 19 | <p>If the group engagement team plans to request a component auditor to perform work on the financial information of a component, the group engagement team shall obtain an understanding of the following: (Ref: Para. A32–A35)</p> <p>(a) Whether the component auditor understands and will comply with the ethical requirements that are relevant to the group audit and, in particular, is independent. (Ref: Para. A37)</p> <p>...</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 600<br>Paragraph 20 | <p>If a component auditor does not meet the independence requirements that are relevant to the group audit, or the group engagement team has serious concerns about the other matters listed in paragraph 19(a)–(c), the group engagement team shall obtain sufficient appropriate audit evidence relating to the financial information of the component without requesting that component auditor to perform work on the</p>                | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards         |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|-------------------------|---|---|---|--------------------|
| Standard                | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                         | financial information of that component.<br>(Ref: Para. A39–A41)  |   |   |                    |
| ISA 600<br>Paragraph 40 | <p>The group engagement team shall communicate its requirements to the component auditor on a timely basis. This communication shall set out the work to be performed, the use to be made of that work, and the form and content of the component auditor's communication with the group engagement team. It shall also include the following: (Ref: Para. A57, A58, A60)</p> <p>...</p> <p>(b) The ethical requirements that are relevant to the group audit and, in particular, the independence requirements.</p> <p>...</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|--------------------------|---|---|---|--------------------|
| Standard                 | Extant Paragraphs   |   | Proposed Change                         | Category of change |
| ISA 600<br>Paragraph 41  | <p>The group engagement team shall request the component auditor to communicate matters relevant to the group engagement team's conclusion with regard to the group audit. Such communication shall include: (Ref: Para. A60)</p> <p>(a) Whether the component auditor has complied with ethical requirements that are relevant to the group audit, including independence and professional competence;</p> <p>...</p>  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISA 600<br>Paragraph A37 | <p>When performing work on the financial information of a component for a group audit, the component auditor is subject to ethical requirements that are relevant to the group audit. Such requirements may be different or in addition to those applying to the component auditor when performing a statutory audit in the component auditor's jurisdiction. The group engagement team therefore obtains an understanding whether the component auditor understands and will comply with the ethical requirements that are relevant to the group audit, sufficient to fulfill the component auditor's responsibilities in the group audit.</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code                                   | Proposed Changes to the IAASB Standards   |                    |
|--------------------------|--|--|---|--------------------|
| Standard                 | Extant Paragraphs  |  | Proposed Change   | Category of change |
| ISA 600<br>Paragraph A39 | The group engagement team cannot overcome the fact that a component auditor is not independent by being involved in the work of the component auditor or by performing additional risk assessment or further audit procedures on the financial information of the component.   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>    | N/A   | N/A                |
| ISA 600<br>Appendix I    | <ul style="list-style-type: none"> <li>The International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants comprises all of the relevant ethical requirements that apply to the audit.</li> </ul> <p>We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the <i>Auditor's Responsibilities for the Audit of the Consolidated Financial Statements</i> section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.</p> | <ul style="list-style-type: none"> <li>Update title of the Code</li> </ul> | <p><b>For purposes of this illustrative auditor's report, the following circumstances are assumed:</b></p> <p>...</p> <ul style="list-style-type: none"> <li>The International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) comprises all of the relevant ethical requirements that apply to the audit.</li> </ul> <p>...</p> <p>...</p> <p>We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the <i>Auditor's Responsibilities for the Audit of the Consolidated Financial Statements</i> section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for</p> | 3                  |

| IAASB Standards                            |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--|--|--|--|--------------------|
| Standard                                   | Extant Paragraphs  |  | Proposed Change  | Category of change |
|  |  |  | Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion. |                    |
| ISA 600<br>Appendix 4                      | 1. We have an understanding of [indicate relevant ethical requirements] that is sufficient to fulfill our responsibilities in the audit of the group financial statements, and will comply therewith. In particular, and with respect to [name of parent] and the other components in the group, we are independent within the meaning of [indicate relevant ethical requirements] and comply with the applicable requirements of [refer to rules] promulgated by [name of regulatory agency]. | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                      | N/A  | N/A                |
| ISA 610<br>(Revised 2013)<br>Paragraph A14 | In addition, the IESBA Code <sup>17</sup> states that a self-review threat is created when the external auditor accepts an engagement to provide internal audit services to an audit client, and the results of those services will be used in conducting the audit. This is because of the possibility that the engagement team will use the results of the internal audit service without properly   | <ul style="list-style-type: none"> <li>Update to title and references to the Code</li> </ul> | <p>17 The International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code), paragraph 605.4 A3-Section 290.194</p> <p>18 IESBA Code, paragraphs <del>R605.1-R605.5</del>-Section <del>290.190-290.195</del></p>  | 1 & 3              |



| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|--------------------------|---|---|---|--------------------|
| Standard                 | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                          | <p>evaluating those results or without exercising the same level of professional skepticism as would be exercised when the internal audit work is performed by individuals who are not members of the firm. The IESBA Code<sup>18</sup> discusses the prohibitions that apply in certain circumstances and the safeguards that can be applied to reduce the threats to an acceptable level in other circumstances.</p> <p>17 The International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code), Section 290.194</p> <p>18 IESBA Code, Section 290.190–290.195</p> |   |   |                    |
| ISA 620<br>Paragraph 9   | <p><b>The Competence, Capabilities and Objectivity of the Auditor's Expert</b></p> <p>The auditor shall evaluate whether the auditor's expert has the necessary competence, capabilities and objectivity for the auditor's purposes. In the case of an auditor's external expert, the evaluation of objectivity shall include inquiry regarding interests and relationships that may create a threat to that expert's objectivity. (Ref: Para. A14–A20)</p>   | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |
| ISA 620<br>Paragraph A12 | <p>An auditor's external expert is not a member of the engagement team and is not subject to quality control policies and procedures in</p>   | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|--|---|--|--------------------|
| Standard                 | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                          | <p>accordance with ISQC 1.<sup>11</sup> In some jurisdictions, however, law or regulation may require that an auditor's external expert be treated as a member of the engagement team, and may therefore be subject to relevant ethical requirements, including those pertaining to independence, and other professional requirements, as determined by that law or regulation.</p> <p><sup>11</sup> ISQC 1, paragraph 12(f)</p>                 |   |  |                    |
| ISA 620<br>Paragraph A16 | Matters relevant to evaluating the competence, capabilities and objectivity of the auditor'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. | <ul style="list-style-type: none"> <li>N/A</li> </ul>   | N/A  | N/A                |
| ISA 620<br>Paragraph A18 | 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 eliminate or reduce such threats, and may be created by external structures (for   | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in</li> </ul> | A broad range of circumstances may threaten objectivity, for example, self-interest threats, advocacy threats, familiarity threats, self-review threats, and intimidation threats. <del>Safeguards may eliminate or reduce such threats, and may be created by external structures (for example, the auditor's expert's profession, legislation or</del> | 2                  |

| IAASB Standards          |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|--|--|--|--------------------|
| Standard                 | Extant Paragraphs  |  | Proposed Change  | Category of change |
|                          | example, the auditor's expert's profession, legislation or regulation), or by the auditor's expert's work environment (for example, quality control policies and procedures). There may also be safeguards specific to the audit engagement.   | <p>relation to how identified threats are addressed</p> <ul style="list-style-type: none"> <li>Section 100.13 of the old Code referred to "(a) Safeguards created by the profession, legislation or regulation; and</li> <li>"Safeguards in the work environment." The revised Code does not discuss safeguards created by the profession</li> </ul> | <del>regulation),</del> Such threats may be addressed by <u>eliminating the circumstances that create the threats, applying safeguards,</u> or by the auditor's expert's work environment (for example, quality control policies and procedures). There may also be safeguards specific to the audit engagement.   |                    |
| ISA 620<br>Paragraph A19 | The evaluation of the significance of threats to objectivity and of whether there is a need for safeguards may depend upon the role of the auditor's expert and the significance of the expert's work in the context of the audit. There may be some circumstances in which safeguards cannot reduce threats to an acceptable level, for example, if a proposed auditor's expert is an individual who has played a significant role in preparing the | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how identified threats are addressed</li> </ul>   | The evaluation of <u>whether the threats to objectivity are at an acceptable level</u> <del>the significance of threats to objectivity and of whether there is a need for safeguards</del> may depend upon the role of the auditor's expert and the significance of the expert's work in the context of the audit. There may be some circumstances in which safeguards cannot reduce threats to an acceptable level, for example, if a proposed auditor's expert is an | 2                  |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------------------|--|---|--|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                                      | information that is being audited, that is, if the auditor's expert is a management's expert.  |   | individual who has played a significant role in preparing the information that is being audited, that is, if the auditor's expert is a management's expert.  |                    |
| ISA 620<br>Paragraph A31             | It is necessary for the confidentiality provisions of relevant ethical requirements that apply to the auditor also to apply to the auditor's expert. Additional requirements may be imposed by law or regulation. The entity may also have requested that specific confidentiality provisions be agreed with auditor's external experts.   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>           | N/A  | N/A                |
| ISA 700<br>(Revised)<br>Paragraph 28 | <p>The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that: (Ref: Para. A32)</p> <p>...</p> <p>(c) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall identify the jurisdiction of origin of the relevant ethical requirements or refer to the International Ethics Standards Board</p> | <ul style="list-style-type: none"> <li>Update to the title of the Code</li> </ul> | <p>The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that: (Ref: Para. A32)</p> <p>...</p> <p>(c) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall identify the jurisdiction of origin of the relevant ethical requirements or refer to the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence</i></p> | 3                  |

| IAASB Standards                   |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-----------------------------------|---|---|--|--------------------|
| Standard                          | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                                   | for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code); and (Ref: Para. A34–A39)<br>...   |   | <u>Standards</u> ) (IESBA Code); and (Ref: Para. A34–A39)<br>...   |                    |
| ISA 700 (Revised)<br>Paragraph 40 | The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report also shall: (Ref: Para. A50)<br>...<br>(b) For audits of financial statements of listed entities, state that the auditor provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements regarding independence and communicates with them all relationships and other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, related safeguards; and<br>... | <ul style="list-style-type: none"> <li>Change to reflect wording of the Code (threats)</li> </ul> | The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report also shall: (Ref: Para. A50)<br>...<br>(b) For audits of financial statements of listed entities, state that the auditor provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements regarding independence and communicates with them all relationships and other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, <u>related safeguards how threats have been eliminated or safeguards applied</u> ; and<br>... | 2                  |
| ISA 700 (Revised)<br>Paragraph 50 | If the auditor is required by law or regulation of a specific jurisdiction to use a specific layout, or wording of the auditor's report, the auditor's report shall refer to International Standards on Auditing only if the auditor's  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                           | N/A  | N/A                |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|------------------------------------|--|--|---|--------------------|
| Standard                           | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                                    | <p>report includes, at a minimum, each of the following elements: (Ref: Para. A70–A71)</p> <p>...</p> <p>(d) A statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall identify the jurisdiction of origin of the relevant ethical requirements or refer to the IESBA Code.</p> <p>...</p>   |  |   |                    |
| ISA 700 (Revised)<br>Paragraph A34 | <p>The identification of the jurisdiction of origin of relevant ethical requirements increases transparency about those requirements relating to the particular audit engagement. ISA 200 explains that relevant ethical requirements ordinarily comprise Parts A and B of the IESBA Code related to an audit of financial statements together with national requirements that are more restrictive. When the relevant ethical requirements include those of the IESBA Code, the statement may also make reference to the IESBA Code. If the IESBA</p> | <ul style="list-style-type: none"> <li>Alignment with ISA 200 – refer ISA 200 for explanation</li> </ul> | <p>The identification of the jurisdiction of origin of relevant ethical requirements increases transparency about those requirements relating to the particular audit engagement. ISA 200 explains that relevant ethical requirements ordinarily comprise <u>the provisions of Parts A and B</u> of the IESBA Code related to an audit of financial statements, together with national requirements that are more restrictive. When the relevant ethical requirements include those of the IESBA Code, the statement may also make reference to the IESBA Code. If the IESBA Code constitutes all of the ethical requirements</p> | 1                  |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|---------------------------------------|---|---|---|--------------------|
| Standard                              | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                                       | Code constitutes all of the ethical requirements relevant to the audit, the statement need not identify a jurisdiction of origin.   |   | relevant to the audit, the statement need not identify a jurisdiction of origin.  |                    |
| ISA 700<br>(Revised)<br>Paragraph A39 | The ISAs do not establish specific independence or ethical requirements for auditors, including component auditors, and thus do not extend, or otherwise override, the independence requirements of the IESBA Code or other ethical requirements to which the group engagement team is subject, nor do the ISAs require that the component auditor in all cases to be subject to the same specific independence requirements that are applicable to the group engagement team. As a result, relevant ethical requirements, including those pertaining to independence, in a group audit situation may be complex. ISA 600 provides guidance for auditors in performing work on the financial information of a component for a group audit, including those situations where the component auditor does not meet the independence requirements that are relevant to the group audit. | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>           | N/A   | N/A                |
| ISA 700<br>(Revised)                  | The relevant ethical requirements that apply to the audit comprise the International Ethics Standards Board for Accountants'  | <ul style="list-style-type: none"> <li>Update to the title of the Code</li> </ul> | The relevant ethical requirements that apply to the audit comprise the International Ethics Standards Board for Accountants' <i>International</i> | 3                  |

| IAASB Standards  |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--|---|---|--|--------------------|
| Standard   | Extant Paragraphs   |   | Proposed Change  | Category of change |
| Appendix (various)   | <i>Code of Ethics for Professional Accountants</i> together with the ethical requirements relating to the audit in the jurisdiction, and the auditor refers to both.  |   | <i>Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code), together with the ethical requirements relating to the audit in the jurisdiction, and the auditor refers to both.  |                    |
| ISA 700 (Revised)<br>Appendix (various)<br>*** Various illustrative reports in the other standards require the same update | We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the <i>Auditor's Responsibilities for the Audit of the Financial Statements</i> section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in <i>[jurisdiction]</i> , and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. | <ul style="list-style-type: none"> <li>Update to the title of the Code</li> </ul>                 | We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the <i>Auditor's Responsibilities for the Audit of the Financial Statements</i> section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in <i>[jurisdiction]</i> , and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. | 3                  |
| ISA 700 (Revised)<br>Appendix (various)  | We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships  | <ul style="list-style-type: none"> <li>Change to reflect wording of the Code (threats)</li> </ul> | We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may  | 2                  |



| IAASB Standards   |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards   |                    |
|---|---|---|---|--------------------|
| Standard  | Extant Paragraphs   |   | Proposed Change   | Category of change |
| *** Various illustrative reports in the other standards require the same update | and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.   |   | reasonably be thought to bear on our independence, and where applicable, <del>related safeguards</del> <u>how threats have been eliminated or safeguards applied.</u> |                    |
| ISA 701<br>Paragraph A55  | It may also be necessary for the auditor to consider the implications of communicating about a matter determined to be a key audit matter in light of relevant ethical requirements. In addition, the auditor may be required by law or regulation to communicate with applicable regulatory, enforcement or supervisory authorities in relation to the matter, regardless of whether the matter is communicated in the auditor's report. Such communication may also be useful to inform the auditor's consideration of the adverse consequences that may arise from communicating about the matter. | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A   | N/A                |
| ISA 706<br>Paragraph A15  | The content of an Other Matter paragraph reflects clearly that such other matter is not required to be presented and disclosed in the financial statements. An Other Matter paragraph does not include information that the auditor is prohibited from providing by law, regulation or other professional standards, for example, ethical standards   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A   | N/A                |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------------------|--|---|---|--------------------|
| Standard                           | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                    | relating to confidentiality of information. An Other Matter paragraph also does not include information that is required to be provided by management.   |   |   |                    |
| ISA 720 (Revised)<br>Paragraph 4   | <p>This ISA may also assist the auditor in complying with relevant ethical requirements<sup>2</sup> that require the auditor to avoid being knowingly associated with information that the auditor believes contains a materially false or misleading statement, statements or information furnished recklessly, or omits or obscures information required to be included where such omission or obscurity would be misleading.</p> <p><sup>2</sup> International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code), paragraph 110.2</p> | <ul style="list-style-type: none"> <li>Update to the title and references to the Code</li> <li>Corresponding material in the IESBA Code has not changed in substance</li> </ul> | 2 International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code), paragraph R111.2 440-2. | 1 & 3              |
| ISA 720 (Revised)<br>Paragraph A38 | Remaining alert for other indications that the other information not related to the financial statements or the auditor's knowledge obtained in the audit appears to be materially misstated assists the auditor in complying with relevant ethical requirements that require the auditor to avoid being knowingly associated with other information that the auditor believes contains a materially false or misleading statement, a statement furnished  | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>Corresponding material in the IESBA Code has not changed in substance</li> </ul>                  | 12 IESBA Code, paragraph R111.2440-2  | 1                  |

| IAASB Standards                   |   | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|-----------------------------------|---|---|---|--------------------|
| Standard                          | Extant Paragraphs   |   | Proposed Change                         | Category of change |
|                                   | <p>recklessly, or omits or obscures necessary information such that the other information is misleading.<sup>12</sup></p> <p>Remaining alert for other indications that the other information appears to be materially misstated could potentially result in the auditor identifying such matters as:</p> <ul style="list-style-type: none"> <li>Differences between the other information and the general knowledge, apart from the knowledge obtained in the audit, of the engagement team member reading the other information that lead the auditor to believe that the other information appears to be materially misstated; or</li> <li>An internal inconsistency in the other information that leads the auditor to believe that the other information appears to be materially misstated.</li> </ul> <p><sup>12</sup> IESBA Code, paragraph 110.2</p> |   |   |                    |
| ISA 800 (Revised)<br>Paragraph A9 | ISA 200 requires the auditor to comply with (a) relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements, and (b) all ISAs relevant to the audit. It also requires the auditor to comply with each requirement of an ISA unless, in the   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------------------|--|---|--|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                                      | circumstances of the audit, the entire ISA is not relevant or the requirement is not relevant because it is conditional and the condition does not exist. In exceptional circumstances, the auditor may judge it necessary to depart from a relevant requirement in an ISA by performing alternative audit procedures to achieve the aim of that requirement.  |   |  |                    |
| ISA 800<br>Illustration 3            | We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.   | <ul style="list-style-type: none"> <li>Change to reflect wording of the Code (threats)</li> </ul> | We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, <u>how threats have been eliminated or safeguards applied.</u> <del>related safeguards.</del> | 2                  |
| ISA 805<br>(Revised)<br>Paragraph A5 | ISA 200 requires the auditor to comply with (a) relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements, and (b) all ISAs relevant to the audit. It also requires the auditor to comply with each requirement of an ISA unless, in the circumstances of the audit, the entire ISA is not relevant or the requirement is not relevant because it is conditional and the condition does not exist. In exceptional | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                           | N/A  | N/A                |

| IAASB Standards                       |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------------|--|---|--|--------------------|
| Standard                              | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                                       | circumstances, the auditor may judge it necessary to depart from a relevant requirement in an ISA by performing alternative audit procedures to achieve the aim of that requirement. <sup>19</sup>   |   |  |                    |
| ISA 805<br>Illustration 3             | We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.   | <ul style="list-style-type: none"> <li>Change to reflect wording of the Code (threats)</li> </ul>   | We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, <u>how threats have been eliminated or safeguards applied.</u> <del>related safeguards.</del> | 2                  |
| ISA 810<br>(Revised)<br>Paragraph A13 | In reading the information included in a document containing the summary financial statements and the auditor's report thereon, the auditor may become aware that such information is misleading and may need to take appropriate action. Relevant ethical requirements <sup>14</sup> require the auditor to avoid being knowingly associated with information that the auditor believes contains a materially false or misleading statement, statements or information furnished recklessly, or omits or obscures information required to be included where such omission or obscurity would be misleading. | <ul style="list-style-type: none"> <li>Update to the title and references to the Code</li> <li>Corresponding material in the IESBA Code has not changed in substance</li> </ul> | 14 International Ethics Standards Board for Accountants' <u>International Code of Ethics for Professional Accountants (including International Independence Standards)</u> -(IESBA Code), paragraph <u>R111.2-440-2</u> .  | 1 & 3              |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|------------------------------------|--|--|--|--------------------|
| Standard                           | Extant Paragraphs  |  | Proposed Change  | Category of change |
|                                    | 14 International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), paragraph 110.2   |  |  |                    |
| ISA 810 (Revised)<br>Paragraph A17 | A title indicating the report is the report of an independent auditor, for example, "Report of the Independent Auditor," affirms that the auditor has met all of the relevant ethical requirements regarding independence. This distinguishes the report of the independent auditor from reports issued by others.   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                          | N/A  | N/A                |
| IAPN 1000<br>Paragraph 78          | A key consideration in audits involving financial instruments, particularly complex financial instruments, is the competence of the auditor. ISA 220 <sup>15</sup> requires the engagement partner to be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements and to enable an auditor's report that is appropriate in the circumstances to be issued. Further, relevant ethical requirements <sup>16</sup> require the auditor to determine whether acceptance of the engagement would create any threats to compliance with the fundamental principles, including the professional competence and | <ul style="list-style-type: none"> <li>Update to the title and references to the Code</li> </ul> | <p>15 ISA 220, paragraph 14</p> <p>16 <u>International Code of Ethics for Professional Accountants (including International Independence Standards)</u> (IESBA Code) paragraphs 320.1–320.10 A1.</p> | 1 & 3              |

| IAASB Standards                     |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-------------------------------------|---|---|---|--------------------|
| Standard                            | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                                     | <p>due care. Paragraph 79 below provides examples of the types of matters that may be relevant to the auditor's considerations in the context of financial instruments.</p> <p>15 ISA 220, paragraph 14</p> <p>16 IESBA Code of Ethics for Professional Accountants paragraphs 210.1 and 210.6</p>  |   |   |                    |
| ISRE 2400 (Revised) Paragraph 17(h) | <i>Professional judgment</i> —The application of relevant training, knowledge and experience, within the context provided by assurance, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the review engagement.  | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul>  | N/A   | N/A                |
| ISRE 2400 (Revised) Paragraph 17(i) | <i>Relevant ethical requirements</i> —Ethical requirements the engagement team is subject to when undertaking review engagements. These requirements ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code), together with national requirements that are more restrictive. | <ul style="list-style-type: none"> <li>Refer explanation under the Glossary for the changes (including editorial changes and alignment with the title of the revised IESBA Code)</li> </ul> | Relevant ethical requirements – Ethical requirements <u>to which</u> the engagement team is subject <del>to</del> —when undertaking review engagements. <del>These requirements which</del> ordinarily comprise <u>the provisions of Parts A and B of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants</i> (including <i>International Independence Standards</i>) (IESBA Code)</u> related to a review of financial statements, together with national requirements that are more restrictive. | 1 & 3              |

| IAASB Standards                     |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|-------------------------------------|---|--|---|--------------------|
| Standard                            | Extant Paragraphs   |  | Proposed Change                         | Category of change |
| ISRE 2400 (Revised)<br>Paragraph 21 | The practitioner shall comply with relevant ethical requirements, including those pertaining to independence. (Ref: Para. A15–A16)  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                  | N/A                                     | N/A                |
| ISRE 2400 (Revised)<br>Paragraph 25 | <p>The engagement partner shall take responsibility for: (Ref: Para. A27–A30)</p> <p>...</p> <p>(d) The engagement being performed in accordance with the firm's quality control policies, including the following:</p> <p>(i) Being satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and engagements have been followed, and that conclusions reached are appropriate, including considering whether there is information that would lead the engagement partner to conclude that management lacks integrity; (Ref: Para. A32–A33)</p> | <ul style="list-style-type: none"> <li>No change identified (see section 320)</li> </ul> | N/A                                     | N/A                |
| ISRE 2400 (Revised)<br>Paragraph 26 | If the engagement partner obtains information that would have caused the firm to decline the engagement had that information been available earlier, the  | <ul style="list-style-type: none"> <li>No change identified (see</li> </ul>              | N/A                                     | N/A                |



| IAASB Standards                     |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-------------------------------------|--|---|---|--------------------|
| Standard                            | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                     | engagement partner shall communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action.   | paragraph R320.9)   |   |                    |
| ISRE 2400 (Revised)<br>Paragraph 27 | Throughout the engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. | <ul style="list-style-type: none"> <li>The Code refers to breaches, rather than non-compliance</li> </ul> | Throughout the engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of <del>non-compliance with breaches of</del> relevant ethical requirements by members of the engagement team. If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have <del>not complied with breached</del> relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. | 4                  |
| ISRE 2400 (Revised)<br>Paragraph 29 | Unless required by law or regulation, the practitioner shall not accept a review engagement if: (Ref: Para. A34–A35)<br>...<br>(b) The practitioner has reason to believe that relevant ethical requirements, including independence, will not be satisfied;   | <ul style="list-style-type: none"> <li>No changes identified (see paragraph R320.9)</li> </ul>            | N/A   | N/A                |

| IAASB Standards                     |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|-------------------------------------|--|--|---|--------------------|
| Standard                            | Extant Paragraphs  |  | Proposed Change                         | Category of change |
|                                     | <p>...</p> <p>(d) The practitioner has cause to doubt management's integrity such that it is likely to affect proper performance of the review; or (Ref: Para. A37(b))</p> <p>...</p>  |  |   |                    |
| ISRE 2400 (Revised)<br>Paragraph 52 | <p>When there is an indication that fraud or non-compliance with laws and regulations, or suspected fraud or non-compliance with laws and regulations, has occurred in the entity, the practitioner shall:</p> <p>...</p> <p>(d) Determine whether law, regulation or relevant ethical requirements: (Ref: Para. A94–A98)</p> <p>(i) Require the practitioner to report to an appropriate authority outside the entity.</p> <p>(ii) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.</p> | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.36–360.36 A3</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--------------------------------------|--|--|--|--------------------|
| Standard                             | Extant Paragraphs  |  | Proposed Change  | Category of change |
| ISRE 2400 (Revised)<br>Paragraph 86  | <p>The practitioner's report for the review engagement shall be in writing, and shall contain the following elements: (Ref: Para. A124–A127, A148, A150)</p> <p>...</p> <p>(j) A reference to the practitioner's obligation under this ISRE to comply with relevant ethical requirements;</p> <p>...</p>   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                        | N/A  | N/A                |
| ISRE 2400 (Revised)<br>Paragraph A15 | <p>Part A of the IESBA Code establishes the fundamental principles of professional ethics practitioners must comply with, and provides a conceptual framework for applying those principles. The fundamental principles are:</p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> <p>(e) Professional behavior.</p> <p>Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations. In complying with the IESBA Code, threats to the practitioner's compliance with relevant ethical</p> | <ul style="list-style-type: none"> <li>Refer paragraph A7 of ISQC 1 for explanation</li> </ul> | <p><del>Part A of the IESBA Code establishes the fundamental principles of ethics, which are that practitioners must comply with, and provides a conceptual framework for applying those principles. The fundamental principles are:</del></p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> <p>(e) Professional behavior.</p> <p><del>Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations. In complying with the IESBA Code, threats to the practitioner's compliance with</del></p> | 1                  |

| IAASB Standards                      |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|---|--|---|--------------------|
| Standard                             | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                                      | requirements are required to be identified and appropriately addressed.   |  | <p><del>relevant ethical requirements are required to be identified and appropriately addressed.</del></p> <p><u>The IESBA Code provides a conceptual framework that professional accountants are to apply in order to identify, evaluate and address threats to compliance with the fundamental principles. In the case of audits, reviews and other assurance engagements, the IESBA Code sets out <i>International Independence Standards</i>, which apply the conceptual framework of identifying, evaluating and addressing threats to the fundamental principles and compliance with independence requirements.</u></p> |                    |
| ISRE 2400 (Revised)<br>Paragraph A16 | In the case of an engagement to review financial statements, the IESBA Code requires that the practitioner be independent of the entity whose financial statements are reviewed. The IESBA Code describes independence as comprising both independence of mind and independence in appearance. The practitioner's independence safeguards the practitioner's ability to form a conclusion without being affected by influences that might otherwise compromise that conclusion. Independence enhances the practitioner's ability to act with integrity, to be objective and to maintain an attitude of professional skepticism. | <ul style="list-style-type: none"> <li>No changes identified (see paragraph 400.1, 400.5)</li> </ul> | N/A   | N/A                |

| IAASB Standards                      |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|---|--|---|--------------------|
| Standard                             | Extant Paragraphs   |  | Proposed Change                         | Category of change |
| ISRE 2400 (Revised)<br>Paragraph A21 | Professional judgment is essential to the proper conduct of a review engagement. This is because interpretation of relevant ethical requirements and the requirements of this ISRE, and the need for informed decisions throughout the performance of a review engagement, require the application of relevant knowledge and experience to the facts and circumstances of the engagement. Professional judgment is necessary, in particular: ...  | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul> | N/A                                     | N/A                |
| ISRE 2400 (Revised)<br>Paragraph A22 | The distinguishing feature of the professional judgment expected of the practitioner is that it is exercised by a practitioner whose training, knowledge and experience, including in the use of assurance skills and techniques, have assisted in developing the necessary competencies to achieve reasonable judgments. Consultation on difficult or contentious matters during the course of the engagement, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm, assists the practitioner in making informed and reasonable judgments. | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change                         | Category of change |
| ISRE 2400 (Revised)<br>Paragraph A27 | Within the context of the firm's system of quality control, engagement teams have a responsibility to implement quality control procedures applicable to the engagement, and provide the firm with relevant information to enable the functioning of that part of the firm's system of quality control relating to independence.   | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |
| ISRE 2400 (Revised)<br>Paragraph A29 | <p>Unless information provided by the firm or other parties suggests otherwise, the engagement team is entitled to rely on the firm's system of quality control. For example, the engagement team may rely on the firm's system of quality control in relation to:</p> <ul style="list-style-type: none"> <li>Competence of personnel through their recruitment and formal training.</li> <li>Independence through the accumulation and communication of relevant independence information.</li> <li>Maintenance of client relationships through acceptance and continuance systems.</li> <li>Adherence to regulatory and legal requirements through the monitoring process.</li> </ul> <p>In considering deficiencies identified in the firm's system of quality control that</p> | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|---|--|---|--------------------|
| Standard                             | Extant Paragraphs   |  | Proposed Change                         | Category of change |
|                                      | may affect the review engagement, the engagement partner may consider measures taken by the firm to rectify those deficiencies.   |  |   |                    |
| ISRE 2400 (Revised)<br>Paragraph A32 | <p>ISQC 1 requires the firm to obtain information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. Information that assists the engagement partner in determining whether acceptance and continuance of client relationships and review engagements are appropriate may include information concerning:</p> <ul style="list-style-type: none"> <li>• The integrity of the principal owners, key management and those charged with governance; and</li> <li>• Significant matters that have arisen during the current or a previous review engagement, and their implications for continuing the relationship.</li> </ul> | <ul style="list-style-type: none"> <li>• No change identified – see section 320</li> </ul> | N/A                                     | N/A                |
| ISRE 2400 (Revised)<br>Paragraph A34 | The practitioner's consideration of engagement continuance, and relevant ethical requirements, including  | <ul style="list-style-type: none"> <li>• No change identified – see section 320</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|--|--|---|--------------------|
| Standard                             | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                                      | independence, occurs throughout the engagement, as conditions and changes in circumstances occur. Performing initial procedures on engagement continuance and evaluation of relevant ethical requirements (including independence) at the beginning of an engagement informs the practitioner's decisions and actions prior to the performance of other significant activities for the engagement.   |  |   |                    |
| ISRE 2400 (Revised)<br>Paragraph A88 | <p>The practitioner may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, including fraud, which may differ from or go beyond this ISRE, such as:</p> <p>(a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance and considering whether further action is needed;</p> <p>(b) Communicating identified or suspected non-compliance with laws and</p> | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>No other changes identified – see paragraphs R360.29–R360.40 A1</li> </ul> | 11 See, for example, <del>Sections 225.44–225.48</del> paragraphs <u>R360.29–360.40 A1</u> of the IESBA Code. | 1                  |



| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|--|--|---|--------------------|
| Standard                             | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                                      | <p>regulations to an auditor, for example a group engagement partner;<sup>11</sup> and</p> <p>(c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.</p> <p>Complying with any additional responsibilities may provide further information that is relevant to the practitioner's work in accordance with this ISRE (e.g., regarding the integrity of management or, where appropriate, those charged with governance).</p> <p>11 See, for example, Sections 225.44–225.48 of the IESBA Code.</p>  |  |   |                    |
| ISRE 2400 (Revised)<br>Paragraph A95 | <p>In some cases, the relevant ethical requirements may require the practitioner to report or to consider whether reporting identified or suspected fraud or non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the IESBA Code requires the practitioner to take steps to respond to identified or suspected non-compliance with laws and regulations, and consider whether further action is needed, which may include reporting to an appropriate authority outside the entity.<sup>12</sup> The IESBA Code explains that</p> | <ul style="list-style-type: none"> <li>• Update references to the Code</li> <li>• No other changes identified – see section R360.29–R360.38</li> </ul> | <p>12 See, for example, <u>paragraphs R360.36–360.36</u> <del>A3</del> <del>Section 225.51 to 225.52</del> of the IESBA Code.</p> <p>13 See, for example, <del>Section 140.7</del> <u>paragraphs R114.1.114.1 A1 and R360.37</u> <del>and Section 225.53</del> of the IESBA Code.</p> | 1                  |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                      | <p>such reporting would not be considered a breach of the duty of confidentiality under the IESBA Code.<sup>13</sup></p> <p>12 See, for example, Section 225.51 to 225.52 of the IESBA Code.</p> <p>13 See, for example, Section 140.7 and Section 225.53 of the IESBA Code.</p>   |   |   |                    |
| ISRE 2400 (Revised)<br>Paragraph A97 | In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation or relevant ethical requirements.  | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.6 and 360.36 A3</li> </ul> | N/A                                     | N/A                |
| ISRE 2400 (Revised)<br>Paragraph A98 | The determination required by paragraph 52(d) may involve complex considerations and professional judgments. Accordingly, the practitioner may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The practitioner may also consider obtaining legal advice to understand the | <ul style="list-style-type: none"> <li>No changes identified – see paragraph 360.39 A1</li> </ul>             | N/A                                     | N/A                |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code                                | Proposed Changes to the IAASB Standards |                    |
|------------------------------------|--|---|---|--------------------|
| Standard                           | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                    | practitioner's options and the professional or legal implications of taking any particular course of action.   |   |   |                    |
| ISRE 2400 (Revised) Paragraph A125 | A title indicating the report is the report of an independent practitioner, for example, "Independent Practitioner's Review Report," affirms that the practitioner has met all of the relevant ethical requirements regarding independence and, therefore, distinguishes the independent practitioner's report from reports issued by others.  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul> | N/A                                     | N/A                |
| ISRE 2400 (Revised) Appendix 1     | We will conduct our review in accordance with International Standard on Review Engagements (ISRE) 2400 (Revised), Engagements to Review Historical Financial Statements. ISRE 2400 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. ISRE 2400 (Revised) also requires us to comply with relevant ethical requirements. | <ul style="list-style-type: none"> <li>N/A</li> </ul>                   | N/A                                     | N/A                |

| IAASB Standards                   |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|-----------------------------------|---|--|---|--------------------|
| Standard                          | Extant Paragraphs   |  | Proposed Change                         | Category of change |
| ISRE 2400 (Revised)<br>Appendix 2 | Our responsibility is to express a conclusion on the accompanying financial statements. We conducted our review in accordance with International Standard on Review Engagements (ISRE) 2400 (Revised), <i>Engagements to Review Historical Financial Statements</i> . ISRE 2400 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements. | <ul style="list-style-type: none"> <li>N/A</li> </ul>  | N/A                                     | N/A                |
| ISRE 2410<br>Paragraph 4          | <b>The auditor should comply with the ethical requirements relevant to the audit of the annual financial statements of the entity.</b> These ethical requirements govern the auditor's professional responsibilities in the following areas: independence, integrity, objectivity, professional competence and due care, confidentiality, professional behavior, and technical standards.   | <ul style="list-style-type: none"> <li>The fundamental principles highlighted are not the same as the Code, paragraph 110.1 A1</li> <li>General updates to this standard are needed to reference relevant ethical requirements in the same manner</li> </ul> | N/A                                     | N/A                |

| IAASB Standards |                   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|-----------------|-------------------|---|---|--------------------|
| Standard        | Extant Paragraphs |   | Proposed Change                         | Category of change |
|                 |                   | <p>as the other standards</p> <ul style="list-style-type: none"> <li>• However, given that this standard has not been updated for conforming amendments in relation to other recent projects of the IAASB, it is proposed that no changes are made as it may give the appearance that the standard is up to date</li> </ul> |   |                    |

| IAASB Standards                    |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|------------------------------------|---|---|--|--------------------|
| Standard                           | Extant Paragraphs   |   | Proposed Change  | Category of change |
| ISAE 3000 (Revised)<br>Paragraph 3 | <p>This ISAE is premised on the basis that:</p> <p>(a) The members of the engagement team and the engagement quality control reviewer (for those engagements where one has been appointed) are subject to Parts A and B of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants (IESBA Code) related to assurance engagements, or other professional requirements, or requirements in law or regulation, that are at least as demanding; and (Ref: Para. A30–A34)</p> <p>...</p> | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>See explanation in the glossary for basis for more general references to the Code. However, in context of ISAE 3000, is this appropriate, given we are more specific about the relevant ethical requirements because the standard may be used by non-accountants</li> </ul> | <p>This ISAE is premised on the basis that:</p> <p>(a) The members of the engagement team and the engagement quality control reviewer (for those engagements where one has been appointed) are subject to <u>the provisions—Parts A and B of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants</i> (including <i>International Independence Standards</i>) issued by the International Ethics Standards Board for Accountants</u> (IESBA Code) related to assurance engagements, or other professional requirements, or requirements in law or regulation, that are at least as demanding; and (Ref: Para. A30–A34)</p> | 1 & 3              |

| IAASB Standards                     |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards |                    |
|-------------------------------------|--|--|---|--------------------|
| Standard                            | Extant Paragraphs  |  | Proposed Change                         | Category of change |
| ISAE 3000 (Revised) Paragraph 4     | Quality control within firms that perform assurance engagements, and compliance with ethical principles, including independence requirements, are widely recognized as being in the public interest and an integral part of high-quality assurance engagements. Professional accountants in public practice will be familiar with such requirements. If a competent practitioner other than a professional accountant in public practice chooses to represent compliance with this or other ISAE, it is important to recognize that this ISAE includes requirements that reflect the premise in the preceding paragraph. | <ul style="list-style-type: none"> <li>N/A</li> </ul>                                  | N/A                                     | N/A                |
| ISAE 3000 (Revised) Paragraph 12(t) | Professional judgment—The application of relevant training, knowledge and experience, within the context provided by assurance and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the engagement.  | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                     |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-------------------------------------|---|---|---|--------------------|
| Standard                            | Extant Paragraphs   |   | Proposed Change   | Category of change |
| ISAE 3000 (Revised)<br>Paragraph 20 | The practitioner shall comply with Parts A and B of the IESBA Code related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. (Ref: Para. A30–A34, A60)  | <ul style="list-style-type: none"> <li>Refer explanation above under paragraph 3</li> </ul> | The practitioner shall comply with <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. (Ref: Para. A30–A34, A60) | 1                  |
| ISAE 3000 (Revised)<br>Paragraph 21 | The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and assurance engagements have been followed by the firm, and shall determine that conclusions reached in this regard are appropriate.   | <ul style="list-style-type: none"> <li>No changes identified – see section 320</li> </ul>   | N/A   | N/A                |
| ISAE 3000 (Revised)<br>Paragraph 22 | <p>The practitioner shall accept or continue an assurance engagement only when: (Ref: Para. A30–A34)</p> <p>(a) The practitioner has no reason to believe that relevant ethical requirements, including independence, will not be satisfied;</p> <p>(b) The practitioner is satisfied that those persons who are to perform the engagement collectively have the appropriate competence and capabilities (see also paragraph 32); and</p> | <ul style="list-style-type: none"> <li>No changes identified – see section 320</li> </ul>   | N/A   | N/A                |



| IAASB Standards                  |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|----------------------------------|---|---|--|--------------------|
| Standard                         | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                                  | ...   |   |  |                    |
| ISAE 3000 (Revised) Paragraph 23 | If the engagement partner obtains information that would have caused the firm to decline the engagement had that information been available earlier, the engagement partner shall communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action.   | <ul style="list-style-type: none"> <li>No changes identified (see paragraph R320.9)</li> </ul>  | N/A  | N/A                |
| ISAE 3000 (Revised) Paragraph 33 | <p>The engagement partner shall take responsibility for the overall quality on the engagement. This includes responsibility for:</p> <p>(a) Appropriate procedures being performed regarding the acceptance and continuance of client relationships and engagements;</p>  | <ul style="list-style-type: none"> <li>No changes identified – see section 320</li> </ul>   | N/A  | N/A                |
| ISAE 3000 (Revised) Paragraph 34 | Throughout the engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the | <ul style="list-style-type: none"> <li>The Code refers to breaches, rather than non-compliance</li> <li>Paragraph R100.4 states "take whatever actions might be available, as soon as possible, to</li> </ul> | Throughout the engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of <u>breaches of</u> <del>non-compliance with</del> relevant ethical requirements by members of the engagement team. If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have <u>breached</u> <del>not complied with</del> relevant | 4                  |

| IAASB Standards                        |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--|--|--|--|--------------------|
| Standard                               | Extant Paragraphs  |  | Proposed Change  | Category of change |
|  | engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action.   | address the consequences of the breach satisfactorily"   | ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action.   |                    |
| ISAE 3000 (Revised)<br>Paragraph 69(j) | <p>The assurance report shall include, at a minimum, the following basic elements:</p> <p>...</p> <p>A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements. (Ref: Para. A172)</p> <p>...</p> | <ul style="list-style-type: none"> <li>Refer explanation above under paragraph 3</li> </ul>    | <p>The assurance report shall include, at a minimum, the following basic elements:</p> <p>...</p> <p>A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as the <u>provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements. (Ref: Para. A172)</p> <p>...</p> | 1                  |
| ISAE 3000 (Revised)<br>Paragraph A30   | Part A of the IESBA Code establishes the following fundamental principles with which the practitioner is required to comply:   | <ul style="list-style-type: none"> <li>Refer paragraph A7 of ISQC 1 for explanation</li> </ul> | <del>Part A of t</del> The IESBA Code establishes the following-fundamental principles <u>of ethics, which</u>   | 1                  |

| IAASB Standards                      |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|---|--|---|--------------------|
| Standard                             | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                                      | (a) Integrity;<br>(b) Objectivity;<br>(c) Professional competence and due care;<br>(d) Confidentiality; and<br>(e) Professional behavior.   |  | <del>are with which the practitioner is required to comply:</del><br>(a) Integrity;<br>(b) Objectivity;<br>(c) Professional competence and due care;<br>(d) Confidentiality; and<br>(e) Professional behavior.  |                    |
| ISAE 3000 (Revised)<br>Paragraph A31 | Part A of the IESBA Code also provides a conceptual framework for professional accountants to apply to:<br>(a) Identify threats to compliance with the fundamental principles. Threats fall into one or more of the following categories:<br>(i) Self-interest;<br>(ii) Self-review;<br>(iii) Advocacy;<br>(iv) Familiarity; and<br>(v) Intimidation;<br>(b) Evaluate the significance of the threats identified; and<br>(c) Apply safeguards, when necessary, to eliminate the threats or reduce | <ul style="list-style-type: none"> <li>In ISQC 1 and ISRE 2400 this has been explained more generally. However, ISAE 3000 contains more detail to explain the Code as this was the Board's decision at the time</li> </ul> | <u>The IESBA Code provides a conceptual framework that professional accountants are to apply in order to identify, evaluate and address threats to compliance with the fundamental principles. In the case of audits, reviews and other assurance engagements, the IESBA Code sets out <i>International Independence Standards</i>, which apply the conceptual framework of identifying, evaluating and addressing threats to the fundamental principles and compliance with independence requirements.</u><br><del>Part A of the IESBA Code also provides a conceptual framework for professional accountants to apply to. This includes:</del><br>(a) Identifying threats to compliance with the fundamental principles. Threats fall into one or more of the following categories: | 1 & 2              |

| IAASB Standards |   | Notes in Relation to the 2018 IESBA Code | Proposed Changes to the IAASB Standards   |                    |
|-----------------|---|--|---|--------------------|
| Standard        | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                 | <p>them to an acceptable level. Safeguards are necessary when the professional accountant determines that the threats are not at a level at which a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances available to the professional accountant at that time, that compliance with the fundamental principles is not compromised.</p> |  | <p>(i) Self-interest;</p> <p>(ii) Self-review;</p> <p>(iii) Advocacy;</p> <p>(iv) Familiarity; and</p> <p>(v) Intimidation;</p> <p>(b) Evaluating <u>whether the significance of the threats identified are at an acceptable level</u>; and</p> <p>(c) <u>If the identified threats to compliance with the fundamental principles are not at an acceptable level, addressing them by eliminating the circumstances that create the threats, applying safeguards, or withdrawing from the engagement, where withdrawal is possible under applicable law or regulation.</u></p> <p><del>(c) Apply safeguards, when necessary, to eliminate the threats or reduce them to an acceptable level. Safeguards are necessary when the professional accountant determines that the threats are not at a level at which a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances available to the professional accountant at that time, that compliance with the fundamental principles is not compromised.</del></p> |                    |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|--------------------------------------|--|--|--|--------------------|
| Standard                             | Extant Paragraphs  |  | Proposed Change  | Category of change |
| ISAE 3000 (Revised)<br>Paragraph A32 | <p>Part B of the IESBA Code describes how the conceptual framework in Part A applies in certain situations to professional accountants in public practice, including:</p> <ul style="list-style-type: none"> <li>Professional appointment;</li> <li>Conflicts of interest;</li> <li>Second opinions;</li> <li>Fees and other types of remuneration;</li> <li>Marketing professional services;</li> <li>Gifts and hospitality;</li> <li>Custody of client assets;</li> <li>Objectivity; and</li> <li>Independence.</li> </ul> | <ul style="list-style-type: none"> <li>ISAE 3000 contains more detail than the other standards to explain the Code as this was the Board's decision at the time</li> </ul> | <p><del>Part B of the IESBA Code sets out requirements and application material on various topics describes how the conceptual framework in Part A applies in certain situations to professional accountants in public practice, including:</del></p> <ul style="list-style-type: none"> <li><del>Professional appointment;</del></li> <li>Conflicts of interest;</li> <li><del>Professional appointment;</del></li> <li>Second opinions;</li> <li>Fees and other types of remuneration;</li> <li><del>Marketing professional services;</del></li> <li><u>Inducements, including gifts and hospitality;</u></li> <li>Custody of client assets;</li> <li><u>Responding to non-compliance with laws and regulations;</u></li> <li><del>Objectivity; and</del></li> <li><del>Independence.</del></li> </ul> | 1 & 4              |
| ISAE 3000 (Revised)<br>Paragraph A33 | <p>The IESBA Code defines independence as comprising both independence of mind and independence in appearance. Independence safeguards the ability to form an assurance conclusion without being</p>   | <ul style="list-style-type: none"> <li>ISAE 3000 contains more detail than the other standards to explain the Code</li> </ul>  | <p>The IESBA Code <u>also includes the <i>International Independence Standards</i>, which contain requirements and application material addressing the independence of professional accountants.</u> The IESBA Code defines</p>  | 1 & 4              |

| IAASB Standards |  | Notes in Relation to the 2018 IESBA Code     | Proposed Changes to the IAASB Standards   |                    |
|-----------------|--|--|---|--------------------|
| Standard        | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                 | <p>affected by influences that might compromise that conclusion. Independence enhances the ability to act with integrity, to be objective and to maintain an attitude of professional skepticism. Matters addressed in the IESBA Code with respect to independence include:</p> <ul style="list-style-type: none"> <li>• Financial interests;</li> <li>• Loans and guarantees;</li> <li>• Business relationships;</li> <li>• Family and personal relationships;</li> <li>• Employment with assurance clients;</li> <li>• Recent service with an assurance client;</li> <li>• Serving as a director or officer of an assurance client;</li> <li>• Long association of senior personnel with assurance clients;</li> <li>• Provision of non-assurance services to assurance clients;</li> <li>• Fees (relative size, overdue, and contingent fees);</li> <li>• Gifts and hospitality; and</li> <li>• Actual or threatened litigation.</li> </ul> | as this was the Board's decision at the time | <p>independence as comprising both independence of mind and independence in appearance. Independence safeguards the ability to form an assurance conclusion without being affected by influences that might compromise that conclusion. Independence enhances the ability to act with integrity, to be objective and to maintain an attitude of professional skepticism. Matters addressed in the <i>International Independence Standards</i> in the IESBA Code <del>with respect to independence</del> include, <u>for example</u>:</p> <ul style="list-style-type: none"> <li>• <u>Fees</u>;</li> <li>• <u>Gifts and hospitality</u>;</li> <li>• <u>Actual or threatened litigation</u>;</li> <li>• Financial interests;</li> <li>• Loans and guarantees;</li> <li>• Business relationships;</li> <li>• Family and personal relationships;</li> <li>• <del>Employment with assurance clients</del>;</li> <li>• Recent service with an assurance client;</li> <li>• Serving as a director or officer of an assurance client;</li> <li>• <u>Employment with an assurance client</u>;</li> </ul> |                    |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                      |  |   | <ul style="list-style-type: none"> <li>Long association of <del>senior</del> personnel with <u>an</u> assurance clients;</li> <li>Provision of non-assurance services to <u>an</u> assurance clients; <u>and</u></li> <li><u>Reports that include a restriction on use and distribution.</u></li> <li><del>Fees (relative size, overdue, and contingent fees);</del></li> <li><del>Gifts and hospitality; and</del></li> <li><del>Actual or threatened litigation.</del></li> </ul> |                    |
| ISAE 3000 (Revised)<br>Paragraph A34 | Professional requirements, or requirements imposed by law or regulation, are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements when they address all the matters referred to in paragraphs A30–A33 and impose obligations that achieve the aims of the requirements set out in Parts A and B of the IESBA Code related to assurance engagements. | <ul style="list-style-type: none"> <li>To reflect the structural changes to the code</li> </ul> | Professional requirements, or requirements imposed by law or regulation, are at least as demanding as <u>the provisions of</u> <del>Parts A and B of</del> the IESBA Code related to assurance engagements when they address all the matters referred to in paragraphs A30–A33 and impose obligations that achieve the aims of the requirements set out in <del>Parts A and B of</del> the IESBA Code related to <u>such</u> engagements.   | 1                  |
| ISAE 3000 (Revised)<br>Paragraph A60 | This ISAE has been written in the context of a range of measures taken to ensure the quality of assurance engagements undertaken by professional accountants in public practice, such as those taken by IFAC member bodies in accordance with  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                         | N/A   | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                      | <p>IFAC's Member Body Compliance Program and Statements of Membership Obligations. Such measures include:</p> <ul style="list-style-type: none"> <li>Competency requirements, such as education and experience benchmarks for entry to membership, and ongoing continuing professional development as well as life-long learning requirements.</li> <li>Quality control policies and procedures implemented across the firm. ISQC 1 applies to all firms of professional accountants in respect of assurance and related services engagements.</li> <li>A comprehensive Code of Ethics, including detailed independence requirements, founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.</li> </ul> |   |   |                    |
| ISAE 3000 (Revised)<br>Paragraph A61 | ISQC 1 deals with the firm's responsibilities to establish and maintain its system of quality control for assurance engagements. It sets out the responsibilities of the firm for establishing policies and procedures designed to provide it with reasonable  | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |



| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                      | <p>assurance that the firm and its personnel comply with relevant ethical requirements, including those pertaining to independence. Compliance with ISQC 1 requires, among other things, that the firm establish and maintain a system of quality control that includes policies and procedures addressing each of the following elements, and that it documents its policies and procedures and communicates them to the firm's personnel:</p> <p>...</p>   |   |   |                    |
| ISAE 3000 (Revised)<br>Paragraph A65 | <p>Unless information provided by the firm or other parties suggests otherwise, the engagement team is entitled to rely on the firm's system of quality control. For example, the engagement team may rely on the firm's system of quality control in relation to:</p> <p>(a) Competence of personnel through their recruitment and formal training.</p> <p>(b) Independence through the accumulation and communication of relevant independence information.</p> <p>(c) Maintenance of client relationships through acceptance and continuance systems.</p> | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                      | <p>(d) Adherence to regulatory and legal requirements through the monitoring process.</p> <p>In considering deficiencies identified in the firm's system of quality control that may affect the assurance engagement, the engagement partner may consider measures taken by the firm to rectify those deficiencies.</p>  |   |   |                    |
| ISAE 3000 (Revised)<br>Paragraph A68 | <p>The IESBA Code requires the professional accountant in public practice to agree to provide only those services that the professional accountant in public practice is competent to perform.<sup>4</sup> The practitioner has sole responsibility for the assurance conclusion expressed, and that responsibility is not reduced by the practitioner's use of the work of a practitioner's expert. Nonetheless, if the practitioner using the work of a practitioner's expert, having followed this ISAE, concludes that the work of that expert is adequate for the practitioner's purposes, the practitioner may accept that expert's findings or conclusions in the expert's field as appropriate evidence.</p> <p><sup>4</sup> IESBA Code, paragraph 210.6</p> | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>Requirement in paragraph 210.6 of the Code changed to application material</li> </ul> | <p>The IESBA Code <u>provides guidance on the self-interest threat to compliance with the principle of professional competence and due care that is created if the engagement team does not possess, or cannot acquire, the competencies to perform the professional services</u> <del>requires the professional accountant in public practice to agree to provide only those services that the professional accountant in public practice is competent to perform.</del><sup>4</sup> The practitioner has sole responsibility for the assurance conclusion expressed, and that responsibility is not reduced by the practitioner's use of the work of a practitioner's expert. Nonetheless, if the practitioner using the work of a practitioner's expert, having followed this ISAE, concludes that the work of that expert is adequate for the practitioner's purposes, the practitioner may accept that expert's findings or conclusions in the expert's field as appropriate evidence.</p> | 1                  |

| IAASB Standards                      |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards           |                    |
|--------------------------------------|---|--|---|--------------------|
| Standard                             | Extant Paragraphs   |  | Proposed Change                                   | Category of change |
|                                      |   |  | 4 IESBA Code, paragraph <del>320.3 A3-240.6</del> |                    |
| ISAE 3000 (Revised)<br>Paragraph A75 | Other matters that may be considered in an engagement quality control review include:<br><br>(a) The engagement team's evaluation of the firm's independence in relation to the engagement;<br><br>(b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and<br><br>(c) Whether engagement documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                | N/A   | N/A                |
| ISAE 3000 (Revised)<br>Paragraph A81 | Professional judgment is essential to the proper conduct of an assurance engagement. This is because interpretation of relevant ethical requirements and relevant ISAE and the informed decisions required throughout the engagement cannot be made without the application of relevant training, knowledge, and experience to the facts and circumstances.   | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul> | N/A   | N/A                |

| IAASB Standards                       |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------------|--|--|--|--------------------|
| Standard                              | Extant Paragraphs  |  | Proposed Change  | Category of change |
|                                       | Professional judgment is necessary in particular regarding decisions about:  |  |  |                    |
| ISAE 3000 (Revised)<br>Paragraph A82  | The distinguishing feature of the professional judgment expected of a practitioner whose training, knowledge and experience have assisted in developing the necessary competencies to achieve reasonable judgments.  | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul> | N/A  | N/A                |
| ISAE 3000 (Revised)<br>Paragraph A102 | <p>The practitioner may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond the practitioner's responsibilities under this ISAE, such as:</p> <p>(a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance and considering whether further action is needed;</p> <p>(b) Communicating identified or suspected non-compliance with laws and regulations to an auditor;<sup>7</sup> and</p> | <ul style="list-style-type: none"> <li>Update reference to the Code</li> </ul>         | 7 See, for example, <del>Sections 225.44–225.48</del> paragraphs <u>R360.31–360.35 A1</u> of the IESBA Code. | 1                  |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code              | Proposed Changes to the IAASB Standards |                    |
|------------------------------------|--|---|---|--------------------|
| Standard                           | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                    | <p>(c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.</p> <p>Complying with any additional responsibilities may provide further information that is relevant to the practitioner's work in accordance with this and any other ISAE (e.g., regarding the integrity of the responsible party or those charged with governance). Paragraphs A194–A198 further address the practitioner's responsibilities under law, regulation or relevant ethical requirements regarding communicating and reporting identified or suspected non-compliance with laws and regulations.</p> <p>7 See, for example, Sections 225.44–225.48 of the IESBA Code.</p> |   |   |                    |
| ISAE 3000 (Revised) Paragraph A124 | <p>Engagement teams are entitled to rely on the firm's system of quality control, unless information provided by the firm or other parties suggests otherwise. The extent of that reliance will vary with the circumstances, and may affect the nature, timing and extent of the practitioner's procedures with respect to such matters as:</p> <p>...</p>   | <ul style="list-style-type: none"> <li>N/A</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                    |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------------------|---|---|---|--------------------|
| Standard                           | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                                    | <ul style="list-style-type: none"> <li>The practitioner's evaluation of the objectivity of the practitioner's expert. Practitioner's internal experts are subject to relevant ethical requirements, including those pertaining to independence.</li> </ul> <p>...</p>   |   |   |                    |
| ISAE 3000 (Revised) Paragraph A128 | The evaluation of the significance of threats to objectivity and of whether there is a need for safeguards may depend upon the role of the practitioner's expert and the significance of the expert's work in the context of the engagement. There may be some circumstances in which safeguards cannot reduce threats to an acceptable level, for example, if a proposed practitioner's expert is an individual who has played a significant role in preparing the subject matter information. | <ul style="list-style-type: none"> <li>Under the extant Code, safeguards include actions or measures that eliminate or reduce the threats to an acceptable level. Under the revised Code, safeguards are measures that are applied to reduce the threats, while measures to eliminate threats are separate</li> </ul> | The evaluation of <u>whether the threats to objectivity are at an acceptable level</u> <del>the significance of threats to objectivity and of whether there is a need for safeguards</del> may depend upon the role of the practitioner's expert and the significance of the expert's work in the context of the engagement. There may be some circumstances in which safeguards cannot reduce threats to an acceptable level, for example, if a proposed practitioner's expert is an individual who has played a significant role in preparing the subject matter information. | 2                  |
| ISAE 3000 (Revised) Paragraph A173 | <p>The following is an illustration of a statement in the assurance report regarding compliance with ethical requirements:</p> <p>We have complied with the independence and other ethical requirements of the <i>Code</i></p>  | <ul style="list-style-type: none"> <li>Update to the title of the IESBA Code</li> </ul>   | <p>The following is an illustration of a statement in the assurance report regarding compliance with ethical requirements:</p> <p>We have complied with the independence and other ethical requirements of the <u>International</u></p>   | 3                  |

| IAASB Standards                    |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------------------|--|---|---|--------------------|
| Standard                           | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                                    | <i>of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.   |   | <u>Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards)</u> issued by the <del>International Ethics Standards Board for Accountants (IESBA Code)</del> , which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior. |                    |
| ISAE 3000 (Revised) Paragraph A194 | Relevant ethical requirements may include a requirement to report identified or suspected non-compliance with laws and regulations to an appropriate level of management or those charged with governance. In some jurisdictions, law or regulation may restrict the practitioner's communication of certain matters with the responsible party, management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the practitioner is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the practitioner may | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.6 and 360.36 A3</li> </ul> | N/A   | N/A                |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------------|---|--|--|--------------------|
| Standard                              | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                                       | be complex and the practitioner may consider it appropriate to obtain legal advice.   |  |  |                    |
| ISAE 3000 (Revised)<br>Paragraph A195 | <p>Law, regulation or relevant ethical requirements may:</p> <p>(a) Require the practitioner to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.</p> <p>(b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.<sup>8</sup></p> <p><sup>8</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.</p> | <ul style="list-style-type: none"> <li>Update footnote</li> <li>No other change identified – see paragraphs R360.36–360.36 A3</li> </ul> | <p>8 See, for example, <u>paragraphs R360.36 - 360.37</u> <del>Section 225.51 to 225.52</del> of the IESBA Code.</p> | 1                  |
| ISAE 3000 (Revised)<br>Paragraph A196 | <p>Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:</p> <p>(a) Law, regulation or relevant ethical requirements require the practitioner to report;</p> <p>(b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected</p>   | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.36–360.36 A3</li> </ul>                               | N/A  | N/A                |



| IAASB Standards                       |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|---------------------------------------|--|---|---|--------------------|
| Standard                              | Extant Paragraphs  |   | Proposed Change                         | Category of change |
|                                       | <p>non-compliance in accordance with relevant ethical requirements; or</p> <p>(c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so.</p>   |   |   |                    |
| ISAE 3000 (Revised)<br>Paragraph A197 | <p>The reporting of identified or suspected non-compliance with laws and regulations in accordance with law, regulation or relevant ethical requirements may include non-compliance with laws and regulations that the practitioner comes across or is made aware of when performing the engagement but which may not affect the subject matter information. Under this ISAE, the practitioner is not expected to have a level of understanding of laws and regulations beyond those affecting the subject matter information. However, law, regulation or relevant ethical requirements may expect the practitioner to apply knowledge, professional judgment and expertise in responding to such non-compliance. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.</p> | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.29 A1</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|---------------------------------------|---|--|---|--------------------|
| Standard                              | Extant Paragraphs   |  | Proposed Change   | Category of change |
| ISAE 3000 (Revised)<br>Paragraph A198 | <p>In some circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation, or relevant ethical requirements. In other cases, reporting identified or suspected non-compliance to an appropriate authority outside the entity would not be considered a breach of the duty of confidentiality under the relevant ethical requirements.<sup>9</sup></p> <p><sup>9</sup> See, for example, Section 140.7 and Section 225.53 of the IESBA Code.</p> | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>No other changes identified – see paragraphs R360.6 and 360.36 A3</li> </ul> | <p>9 See, for example, <u>paragraphs R114.1, 114.1A1 and R360.37</u> <del>Section 140.7 and Section 225.53</del> of the IESBA Code.</p> | 1                  |
| ISAE 3000 (Revised)<br>Paragraph A199 | <p>The practitioner may consider consulting internally (e.g., within the firm or network firm), obtaining legal advice to understand the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulations or would breach the duty of confidentiality).<sup>10</sup></p> <p><sup>10</sup> See, for example, Section 225.55 of the IESBA Code.</p>   | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>No other changes identified – see paragraph 360.39 A1</li> </ul>             | <p>10 See, for example, <u>paragraph 360.39 A1</u> <del>Section 225.55</del> of the IESBA Code</p>                                      | 1                  |

| IAASB Standards                       |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|---------------------------------------|--|---|--|--------------------|
| Standard                              | Extant Paragraphs  |   | Proposed Change  | Category of change |
| ISAE 3000 (Revised)<br>Paragraph A204 | <p>Documentation may include a record of, for example:</p> <ul style="list-style-type: none"> <li>Issues identified with respect to compliance with relevant ethical requirements and how they were resolved.</li> <li>Conclusions on compliance with independence requirements that apply to the engagement, and any relevant discussions with the firm that support these conclusions.</li> <li>Conclusions reached regarding the acceptance and continuance of client relationships and assurance engagements.</li> <li>The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the engagement.</li> </ul> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>             | N/A  | N/A                |
| ISAE 3402<br>Paragraph 6              | Compliance with ISAE 3000 (Revised) requires, among other things, compliance with Parts A and B of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants (IESBA Code) related to assurance engagements, or other professional requirements, or requirements  | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | Compliance with ISAE 3000 (Revised) requires, among other things, compliance with <u>the provisions <del>Parts A and B</del> of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> issued by the International Ethics Standards Board for</u> | 1 & 3              |

| IAASB Standards              |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------------|---|---|---|--------------------|
| Standard                     | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                              | <p>imposed by law and regulation, that are at least as demanding.<sup>5</sup> It also requires the engagement partner to be a member of a firm that applies ISQC 1,<sup>6</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1.</p> <p>5 ISAE 3000 (Revised), paragraphs 3(a), 20 and 24</p> <p>6 ISAE 3000 (Revised), paragraphs 3(b) and 31 (a). International Standard of Quality Control (ISQC) 1, <i>Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements</i>.</p> |   | <p><del>Accountants</del>-(IESBA Code) related to assurance engagements, or other professional requirements, or requirements imposed by law and regulation, that are at least as demanding.<sup>5</sup> It also requires the engagement partner to be a member of a firm that applies ISQC 1,<sup>6</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1.</p> <p>5 ISAE 3000 (Revised), paragraphs 3(a), 20 and 24</p> <p>6 ISAE 3000 (Revised), paragraphs 3(b) and 31 (a). International Standard of Quality Control (ISQC) 1, <i>Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements</i>.</p> |                    |
| ISAE 3402<br>Paragraph 11    | The service auditor shall comply with Parts A and B of the IESBA Code relating to assurance engagements or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. (Ref: Para. A5)   | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | The service auditor shall comply with <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code relating to assurance engagements or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. (Ref: Para. A5)  | 1                  |
| ISAE 3402<br>Paragraph 53(i) | <p>The service auditor's assurance report shall include, at a minimum, the following basic elements (Ref: Para. A47):</p> <p>A statement that the practitioner complies with the independence and other ethical</p>   | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of  | 1                  |

| IAASB Standards            |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|----------------------------|--|---|--|--------------------|
| Standard                   | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                            | requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least demanding as Parts A and B of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements. |   | the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements.  |                    |
| ISAE 3402<br>Paragraph A5  | The service auditor is subject to relevant independence requirements, which ordinarily comprise Parts A and B of the IESBA Code together with national requirements that are more restrictive. In performing an engagement in accordance with this ISAE, the IESBA Code does not require the service auditor to be independent from each user entity.  | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul>   | The service auditor is subject to relevant independence requirements, which ordinarily comprise <u>the International Independence Standards</u> <del>Parts A and B</del> of the IESBA Code together with national requirements that are more restrictive. In performing an engagement in accordance with this ISAE, the IESBA Code does not require the service auditor to be independent from each user entity. | 1                  |
| ISAE 3402<br>Paragraph A44 | <p>The IESBA Code requires that a service auditor not be associated with information where the service auditor believes that the information:</p> <p>(a) Contains a materially false or misleading statement;</p>  | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>Aligning with terminology used by the Code</li> </ul> | <p>The IESBA Code requires that a service auditor not be associated with information where the service auditor believes that the information:</p> <p>(a) Contains a materially false or misleading statement;</p> <p>(b) Contains statements or information <u>provided</u> <del>furnished</del> recklessly; or</p>  | 1 & 4              |

| IAASB Standards            |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|----------------------------|--|---|---|--------------------|
| Standard                   | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                            | <p>(b) Contains statements or information furnished recklessly; or</p> <p>(c) Omits or obscures information required to be included where such omission or obscurity would be misleading.<sup>14</sup></p> <p>If other information included in a document containing the service organization's description of its system and the service auditor's assurance report contains future-oriented information such as recovery or contingency plans, or plans for modifications to the system that will address deviations identified in the service auditor's assurance report, or claims of a promotional nature that cannot be reasonably substantiated, the service auditor may request that information be removed or restated.</p> <p>14 IESBA Code, paragraph 110.2</p> |   | <p>(c) Omits or obscures <u>required</u> information <del>required to be included</del> where such omission or obscurity would be misleading.<sup>14</sup></p> <p>If other information included in a document containing the service organization's description of its system and the service auditor's assurance report contains future-oriented information such as recovery or contingency plans, or plans for modifications to the system that will address deviations identified in the service auditor's assurance report, or claims of a promotional nature that cannot be reasonably substantiated, the service auditor may request that information be removed or restated.</p> <p>14 IESBA Code paragraph, <u>R111.2410.2</u></p> |                    |
| ISAE 3402<br>Paragraph A53 | <p>Appropriate actions to respond to the circumstances identified in paragraph 56, unless prohibited by law or regulation, may include:</p> <ul style="list-style-type: none"> <li>Obtaining legal advice about the consequences of different courses of action.</li> </ul>  | <ul style="list-style-type: none"> <li>Update footnote reference – the paragraph references need to be expanded from extant to cover the communication</li> </ul> | <p>36 See, for example, <u>paragraphs R360.29 to R360.340</u> <del>A1Section 225.44 to 225.48</del> of the IESBA Code.</p>  | 1                  |

| IAASB Standards         |  | Notes in Relation to the 2018 IESBA Code                                       | Proposed Changes to the IAASB Standards   |                    |
|-------------------------|--|--|---|--------------------|
| Standard                | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                         | <ul style="list-style-type: none"> <li>Communicating with those charged with governance of the service organization.</li> <li>Determining whether to communicate with third parties (e.g., law, regulation or relevant ethical requirements may require the service auditor to report to an appropriate authority outside the entity or the external auditor of the service organization,<sup>36</sup> or establish responsibilities under which such reporting may be appropriate in the circumstances).</li> <li>Modifying the service auditor's opinion, or adding an Other Matter paragraph.</li> <li>Withdrawing from the engagement.</li> </ul> <p><sup>36</sup> See, for example, Section 225.44 to 225.48 of the IESBA Code.</p> | requirements in the Code   |   |                    |
| ISAE 3402<br>Appendix 2 | We have complied with the independence and other ethical requirements of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional   | <ul style="list-style-type: none"> <li>Update reference to the Code</li> </ul> | We have complied with the independence and other ethical requirements of the <u>International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants</i></u> <del>issued by the International Ethics Standards Board for Accountants</del> <u>(including <i>International Independence Standards</i>) (IESBA Code)</u> , which is founded on fundamental principles of integrity, objectivity, professional | 3                  |

| IAASB Standards           |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|---------------------------|--|---|---|--------------------|
| Standard                  | Extant Paragraphs  |   | Proposed Change   | Category of change |
|                           | behavior.  |   | competence and due care, confidentiality and professional behavior.   |                    |
| ISAE 3410<br>Paragraph 10 | Compliance with ISAE 3000 (Revised) requires, among other things, compliance with Parts A and B of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants (IESBA Code) related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. It also requires the engagement partner to be a member of a firm that applies ISQC 1, or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1. (Ref: Para. A5–A6) | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | Compliance with ISAE 3000 (Revised) requires, among other things, compliance with <u>the provisions</u> <del>Parts A and B</del> of the International Ethics Standards Board for Accountants' <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> <del>issued by the International Ethics Standards Board for Accountants</del> (IESBA Code) related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. It also requires the engagement partner to be a member of a firm that applies ISQC 1, or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1. (Ref: Para. A5–A6) | 1 & 3              |
| ISAE 3410<br>Paragraph 67 | <p>The practitioner shall include in the engagement documentation:</p> <p>(a) Issues identified with respect to compliance with relevant ethical requirements and how they were resolved;</p> <p>(b) Conclusions on compliance with independence requirements that apply to the engagement, and any</p>  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>             | N/A   | N/A                |



| IAASB Standards              |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|------------------------------|---|---|---|--------------------|
| Standard                     | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                              | <p>relevant discussions with the firm that support these conclusions;</p> <p>(c) Conclusions reached regarding the acceptance and continuance of client relationships and assurance engagements; and</p> <p>(d) The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the engagement.</p>  |   |   |                    |
| ISAE 3410<br>Paragraph 76(j) | <p>The assurance report shall include, at a minimum, the following basic elements: (Ref. Para. A134)</p> <p>...</p> <p>A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements.</p> | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | <p>The assurance report shall include, at a minimum, the following basic elements: (Ref. Para. A134)</p> <p>...</p> <p>A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements.</p> | 1                  |

| IAASB Standards           |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|---------------------------|--|---|---|--------------------|
| Standard                  | Extant Paragraphs  |   | Proposed Change   | Category of change |
| ISAE 3410<br>Paragraph A5 | <p>The IESBA Code adopts a threats and safeguards approach to independence. Compliance with the fundamental principles may potentially be threatened by a broad range of circumstances. Many threats fall into the following categories:</p> <ul style="list-style-type: none"> <li>• Self-interest, for example, undue dependence on total fees from the entity.</li> <li>• Self-review, for example, performing another service for the entity that directly affects the GHG statement, such as involvement in the quantification of the entity's emissions.</li> <li>• Advocacy, for example, acting as an advocate on behalf of the entity with respect to the interpretation of the applicable criteria.</li> <li>• Familiarity, for example, a member of the engagement team having a long association, or close or immediate family relationship, with an employee of the entity who is in a position to exert direct and significant influence over the preparation of the GHG statement.</li> <li>• Intimidation, for example, being</li> </ul> | <ul style="list-style-type: none"> <li>• Describing the Code as a threats and safeguards approach appears inaccurate</li> </ul> | <p>The IESBA Code <del>adopts</del> <u>requires application of a conceptual framework to identify, evaluate and address threats to the fundamental principles and a safeguards approach to independence.</u> Compliance with the fundamental principles may potentially be threatened by a broad range of circumstances. Many threats fall into the following categories:</p> <ul style="list-style-type: none"> <li>• Self-interest, for example, undue dependence on total fees from the entity.</li> <li>• Self-review, for example, performing another service for the entity that directly affects the GHG statement, such as involvement in the quantification of the entity's emissions.</li> <li>• Advocacy, for example, acting as an advocate on behalf of the entity with respect to the interpretation of the applicable criteria.</li> <li>• Familiarity, for example, a member of the engagement team having a long association, or close or immediate family relationship, with an employee of the entity who is in a position to exert direct and significant influence over the preparation of the GHG statement.</li> <li>• Intimidation, for example, being pressured to reduce inappropriately the extent of</li> </ul> | 2                  |

| IAASB Standards             |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|-----------------------------|---|--|---|--------------------|
| Standard                    | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                             | pressured to reduce inappropriately the extent of work performed in order to lower fees, or being threatened with withdrawal of the practitioner's registration by a registering authority that is associated with the entity's industry group.   |  | work performed in order to lower fees, or being threatened with withdrawal of the practitioner's registration by a registering authority that is associated with the entity's industry group.   |                    |
| ISAE 3410<br>Paragraph A6   | Safeguards created by the profession, law or regulation, or safeguards in the work environment, may eliminate or reduce such threats to an acceptable level.  | <ul style="list-style-type: none"> <li>Paragraph R120.6, R120.7 and R120.10 have been amended from the extant Code, in particular in relation to how identified threats are addressed</li> </ul> | <del>Safeguards created by the profession, law or regulation, or safeguards in the work environment, may eliminate or reduce such threats to an acceptable level.</del> <u>In cases when identified threats are not at an acceptable level, the IESBA Code requires that the threats be addressed by eliminating the circumstances that create the threats, applying safeguards, or withdrawing from the engagement, where withdrawal is possible under applicable law or regulation.</u> | 2                  |
| ISAE 3410<br>Paragraph A114 | <p>Relevant matters that the engagement team may request another practitioner to communicate include:</p> <ul style="list-style-type: none"> <li>Whether the other practitioner has complied with ethical requirements that are relevant to the group engagement, including independence and professional competence.</li> <li>...</li> </ul> | <ul style="list-style-type: none"> <li>N/A</li> </ul>  | N/A   | N/A                |

| IAASB Standards             |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-----------------------------|--|---|--|--------------------|
| Standard                    | Extant Paragraphs  |   | Proposed Change  | Category of change |
| ISAE 3410<br>Paragraph A123 | If the engagement does not include assurance on comparative information, the requirement to perform procedures in the circumstances addressed by paragraph 63(a) is to satisfy the practitioner's ethical obligation to not knowingly be associated with materially false or misleading information.   | <ul style="list-style-type: none"> <li>N/A</li> </ul>                               | N/A  | N/A                |
| ISAE 3410<br>Paragraph A130 | <p>Other matters that may be considered in an engagement quality control review include:</p> <ul style="list-style-type: none"> <li>The engagement team's evaluation of the firm's independence in relation to the engagement.</li> </ul> <p>...</p>   | <ul style="list-style-type: none"> <li>N/A</li> </ul>                               | N/A  | N/A                |
| ISAE 3410<br>Appendix 2     | We have complied with the independence and other ethical requirements of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior. | <ul style="list-style-type: none"> <li>Update reference to the Code</li> </ul>      | We have complied with the independence and other ethical requirements of the <u>International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards)</u> (IESBA Code) issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior. | 3                  |
| ISAE 3420<br>Paragraph 8    | Compliance with ISAE 3000 (Revised) requires, among other things, compliance   | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | Compliance with ISAE 3000 (Revised) requires, among other things, compliance with <u>the</u>   | 1 & 3              |

| IAASB Standards           |   | Notes in Relation to the 2018 IESBA Code                           | Proposed Changes to the IAASB Standards  |                    |
|---------------------------|---|--|--|--------------------|
| Standard                  | Extant Paragraphs   |  | Proposed Change  | Category of change |
|                           | <p>with Parts A and B of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants (IESBA Code) related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding.<sup>3</sup> It also requires the engagement partner to be a member of a firm that applies ISQC 1,<sup>4</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1.</p> <p>3 ISAE 3000 (Revised), paragraphs 3(a), 20 and 24</p> <p>4 ISAE 3000 (Revised), paragraphs 3(b) and 31 (a). International Standard of Quality Control (ISQC) 1, <i>Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements</i>.</p> |  | <p><del>provisions Parts A and B of the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants</del> (IESBA Code) related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding.<sup>3</sup> It also requires the engagement partner to be a member of a firm that applies ISQC 1,<sup>4</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1.</p> <p>3 ISAE 3000 (Revised), paragraphs 3(a), 20 and 24</p> <p>4 ISAE 3000 (Revised), paragraphs 3(b) and 31 (a). International Standard of Quality Control (ISQC) 1, <i>Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements</i>.</p> |                    |
| ISAE 3420<br>Paragraph 13 | Before agreeing to accept an engagement to report on whether pro forma financial information included in a prospectus has been compiled, in all material respects, on the basis of the applicable criteria, the practitioner shall:   | No changes that affect this application material – see section 320 | N/A  | N/A                |

| IAASB Standards              |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|------------------------------|--|---|--|--------------------|
| Standard                     | Extant Paragraphs  |   | Proposed Change  | Category of change |
|                              | <p>(a) Determine that those persons who are to perform the engagement collectively have the appropriate competence and capabilities; (Ref: Para. A10)</p> <p>...</p>   |   |  |                    |
| ISAE 3420<br>Paragraph 35(h) | <p>The practitioner's report shall include, at a minimum, the following basic elements: (Ref: Para. A51)</p> <p>...</p> <p>A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law and regulation, applied that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements.</p> | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | <p>The practitioner's report shall include, at a minimum, the following basic elements: (Ref: Para. A51)</p> <p>...</p> <p>A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law and regulation, applied that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements.</p> | 1                  |
| ISAE 3420<br>Paragraph A10   | <p>The IESBA Code requires the practitioner to maintain appropriate professional knowledge and skill, including an</p>   | <ul style="list-style-type: none"> <li>Update footnote reference</li> </ul>         | <p>The IESBA Code requires the practitioner to <u>comply with the principle of professional competence and due care by attaining and</u></p>   | 1 & 4              |

| IAASB Standards |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|-----------------|---|---|--|--------------------|
| Standard        | Extant Paragraphs   |   | Proposed Change  | Category of change |
|                 | <p>awareness and understanding of relevant technical, professional and business developments, in order to provide competent professional service.<sup>7</sup> In the context of this requirement of the IESBA Code, relevant capabilities and competence to perform the engagement also include matters such as the following:</p> <ul style="list-style-type: none"> <li>• Knowledge and experience of the industry in which the entity operates;</li> <li>• An understanding of the relevant securities laws and regulations and related developments;</li> <li>• An understanding of the listing requirements of the relevant securities exchange and of capital market transactions such as mergers, acquisitions and securities offerings;</li> <li>• Familiarity with the process of preparing a prospectus and listing securities on the securities exchange; and</li> <li>• Knowledge of the financial reporting frameworks used in the preparation of the sources from which the unadjusted financial information and, if applicable, the acquiree's financial information have been extracted.</li> </ul> | <ul style="list-style-type: none"> <li>• Paragraph R113.1 – 113.1A2 of the IESBA Code now include these requirements, but seem to have been slightly amended</li> </ul> | <p>maintaining <del>appropriate</del> professional knowledge and skill, <del>including an awareness and understanding of relevant technical, professional and business developments</del>, in order to provide competent professional service, <u>based on current technical and professional standards and relevant legislation and to act diligently in accordance with such professional standards and legislation.</u><sup>7</sup> In the context of this requirement of the IESBA Code, <del>relevant capabilities and professional</del> competence to perform the engagement <del>also may</del> include matters such as the following:</p> <p>....</p> <p>7 IESBA Code, paragraphs <del>R113.1 430.1–430.3</del></p> |                    |

| IAASB Standards            |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|----------------------------|---|--|---|--------------------|
| Standard                   | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                            | 7 IESBA Code, paragraphs 130.1–130.3  |  |   |                    |
| ISAE 3420<br>Paragraph A41 | <p>The IESBA Code requires that a practitioner not knowingly be associated with reports, returns, communications or other information that the practitioner believes:<sup>9</sup></p> <p>(a) Contain a materially false or misleading statement;</p> <p>(b) Contain statements or information furnished recklessly; or</p> <p>(c) Omit or obscure information required to be included where such omission or obscurity would be misleading.</p> <p>9 IESBA Code, paragraph 110.2</p>  | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>Minor changes to wording of the requirement in the Code</li> </ul> | <p>The IESBA Code requires that a practitioner not knowingly be associated with reports, returns, communications or other information that the practitioner believes:<sup>9</sup></p> <p>(a) Contain a materially false or misleading statement;</p> <p>(b) Contain statements or information <del>furnished</del><u>provided</u> recklessly; or</p> <p>(c) Omit or obscure <u>required</u> information <del>required to be included</del> where such omission or obscurity would be misleading.</p> <p>9 IESBA Code, paragraph <del>R111.2</del><u>110.2</u></p> | 1 & 4              |
| ISAE 3420<br>Paragraph A51 | <p>A title indicating that the report is the report of an independent practitioner, for example, “Independent Practitioner’s Assurance Report on the Compilation of Pro Forma Financial Information Included in a Prospectus,” affirms that the practitioner has met all of the relevant ethical requirements regarding independence as required by ISAE 3000 (Revised).<sup>10</sup> This distinguishes the report of the independent practitioner from reports issued by others.</p> <p><sup>10</sup> ISAE 3000 (Revised), paragraph 20</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>  | N/A   | N/A                |



| IAASB Standards          |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------|---|---|--|--------------------|
| Standard                 | Extant Paragraphs   |   | Proposed Change  | Category of change |
| ISAE 3420<br>Appendix    | We have complied with the independence and other ethical requirement of the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.   | <ul style="list-style-type: none"> <li>Update reference to the Code</li> </ul>  | We have complied with the independence and other ethical requirement of the <u>International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards)</u> issued by the <del>International Ethics Standards Board for Accountants (IESBA Code)</del> , which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.  | 3                  |
| ISRS 4400<br>Paragraph 7 | <p>The auditor should comply with the <b><i>Code of Ethics for Professional Accountants</i></b> issued by the <b>International Ethics Standards Board for Accountants (IESBA Code)</b>. Ethical principles governing the auditor's professional responsibilities for this type of engagement are:</p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality;</p> <p>(e) Professional behavior; and</p> <p>(f) Technical standards.</p> <p>Independence is not a requirement for</p> | <ul style="list-style-type: none"> <li>Update references to the Code</li> <li>The references to the fundamental principles are outdated – see paragraph 110.1 A1</li> </ul> | <p>The auditor should comply with the <u><b>International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards)</b></u> <del>issued by the International Ethics Standards Board for Accountants (IESBA Code)</del>. Ethical principles governing the auditor's professional responsibilities for this type of engagement are:</p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; <u>and</u></p> <p>(e) Professional behavior; <del>and</del></p> <p>(f) <del>Technical standards.</del></p> | 1 & 3              |

| IAASB Standards                     |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|-------------------------------------|---|---|---|--------------------|
| Standard                            | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                                     | agreed-upon procedures engagements; however, the terms or objectives of an engagement or national standards may require the auditor to comply with the independence requirements of the IESBA Code. Where the auditor is not independent, a statement to that effect would be made in the report of factual findings.   |   | Independence is not a requirement for agreed-upon procedures engagements; however, the terms or objectives of an engagement or national standards may require the auditor to comply with the <u>International Independence Standards</u> in independence requirements of the IESBA Code. Where the auditor is not independent, a statement to that effect would be made in the report of factual findings.  |                    |
| ISRS 4410 (Revised) Paragraph 17(g) | <i>Relevant ethical requirements</i> – Ethical requirements the engagement team is subject to when undertaking compilation engagements. These requirements ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code) (excluding Section 290, <i>Independence—Audit and Review Engagements</i> , and Section 291, <i>Independence—Other Assurance Engagements</i> in Part B), together with national requirements that are more restrictive. (Ref: Para. A21) | <ul style="list-style-type: none"> <li>Refer to glossary for explanation</li> </ul> | Relevant ethical requirements – Ethical requirements <u>to which</u> the engagement team is subject <del>to</del> when undertaking <u>a</u> compilation engagements, <u>which</u> <del>These</del> requirements ordinarily comprise <del>Parts A and B of the</del> International Ethics Standards Board for Accountants' <u>International</u> <i>Code of Ethics for Professional Accountants</i> <u>(including International Independence Standards)</u> (IESBA Code) <del>(excluding Section 290, Independence—Audit and Review Engagements, and Section 291, Independence—Other Assurance Engagements in Part B)</del> , together with national requirements that are more restrictive. (Ref: Para. A21) | 1 & 3              |
| ISRS 4410 (Revised) Paragraph 21    | The practitioner shall comply with relevant ethical requirements. (Ref: Para. A19–A21e)   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>             | N/A   | N/A                |

| IAASB Standards                        |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|--|--|---|---|--------------------|
| Standard                               | Extant Paragraphs  |   | Proposed Change   | Category of change |
| ISRS 4410 (Revised)<br>Paragraph 23(b) | <p>The engagement partner shall take responsibility for:</p> <p>...</p> <p>(b) The engagement being performed in accordance with the firm's quality control policies and procedures, by: (Ref: Para. A25)</p> <p>(i) Following appropriate procedures regarding the acceptance and continuance of client relationships and engagements; (Ref: Para. A26)</p> <p>....</p> <p>(iii) Being alert for indications of non-compliance by members of the engagement team with relevant ethical requirements, and determining the appropriate action if matters come to the engagement partner's attention indicating that members of the engagement team have not complied with relevant ethical requirements; (Ref: Para. A27)</p> | <ul style="list-style-type: none"> <li>The Code refers to breaches, rather than non-compliance</li> </ul> | <p>The engagement partner shall take responsibility for:</p> <p>...</p> <p>(b) The engagement being performed in accordance with the firm's quality control policies and procedures, by: (Ref: Para. A25)</p> <p>(i) Following appropriate procedures regarding the acceptance and continuance of client relationships and engagements; (Ref: Para. A26)</p> <p>....</p> <p>(iii) Being alert for indications of <u>breaches of relevant ethical requirements</u> <del>non-compliance</del> by members of the engagement team <del>with relevant ethical requirements</del>, and determining the appropriate action if matters come to the engagement partner's attention indicating that members of the engagement team have not complied with relevant ethical requirements; (Ref: Para. A27)</p> | 4                  |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------------------|--|---|--|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change  | Category of change |
| ISRS 4410 (Revised)<br>Paragraph 40  | <p>The practitioner's report issued for the compilation engagement shall be in writing, and shall include the following elements: (Ref: Para. A56–A57, A63)</p> <p>...</p> <p>(g) A description of the practitioner's responsibilities in compiling the financial information, including that the engagement was performed in accordance with this ISRS, and that the practitioner has complied with relevant ethical requirements;</p> <p>...</p> | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>                           | N/A  | N/A                |
| ISRS 4410 (Revised)<br>Paragraph A19 | <p>Part A of the IESBA Code establishes the fundamental principles of professional ethics that practitioners must comply with, and provides a conceptual framework for applying those principles. The fundamental principles are:</p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> <p>(e) Professional behavior.</p>   | <ul style="list-style-type: none"> <li>Refer to paragraph A7 of ISQC 1 for explanation</li> </ul> | <p><del>Part A of the</del> The IESBA Code establishes the fundamental principles of professional ethics <del>that practitioners must comply with, which are and provides a conceptual framework for applying those principles. The fundamental principles are:</del></p> <p>(a) Integrity;</p> <p>(b) Objectivity;</p> <p>(c) Professional competence and due care;</p> <p>(d) Confidentiality; and</p> <p>(e) Professional behavior.</p> | 4                  |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|--------------------------------------|--|--|---|--------------------|
| Standard                             | Extant Paragraphs  |  | Proposed Change   | Category of change |
|                                      | Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations. In complying with the IESBA Code, threats to the practitioner's compliance with relevant ethical requirements are required to be identified and appropriately addressed.  |  | <p><del>Part B of the IESBA Code illustrates how the conceptual framework is to be applied in specific situations. In complying with the IESBA Code, threats to the practitioner's compliance with relevant ethical requirements are required to be identified and</del></p> <p><u>The IESBA Code provides a conceptual framework that professional accountants are to apply in order to identify, evaluate and address threats to compliance with the fundamental principles. In the case of audits, reviews and other assurance engagements, the IESBA Code sets out <i>International Independence Standards</i>, which apply the conceptual framework of identifying, evaluating and addressing threats to the fundamental principles and compliance with independence requirements.</u></p> |                    |
| ISRS 4410 (Revised)<br>Paragraph A20 | <p>Under the IESBA Code,<sup>5</sup> in applying the principle of integrity, a professional accountant is required to not knowingly be associated with reports, returns, communications or other information where the professional accountant believes that the information:</p> <p>(a) Contains a materially false or misleading statement;</p> <p>(b) Contains statements or information furnished recklessly; or</p> | <ul style="list-style-type: none"> <li>Update footnote reference to paragraph R111.2</li> <li>Minor changes to wording of the requirement in the Code</li> </ul> | <p>Under the IESBA Code,<sup>5</sup> in applying the principle of integrity, a professional accountant is required to not knowingly be associated with reports, returns, communications or other information where the professional accountant believes that the information:</p> <p>(a) Contains a materially false or misleading statement;</p> <p>(b) Contain statements or information <del>furnished</del><u>provided</u> recklessly; or</p> <p>(c) Omit or obscure <u>required</u> information</p>  | 1 & 4              |

| IAASB Standards                   |   | Notes in Relation to the 2018 IESBA Code                                       | Proposed Changes to the IAASB Standards   |                    |
|-----------------------------------|---|--|---|--------------------|
| Standard                          | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                                   | <p>(c) Omits or obscures information required to be included where such omission or obscurity would be misleading.</p> <p>When a professional accountant becomes aware that the accountant has been associated with such information, the accountant is required by the IESBA Code to take steps to be disassociated from that information.</p> <p>5 IESBA Code Part A, paragraph 110.2</p> |  | <p><del>required to be included</del> where such omission or obscurity would be misleading.</p> <p>When a professional accountant becomes aware that the accountant has been associated with such information, the accountant is required by the IESBA Code to take steps to be disassociated from that information.</p> <p>5 IESBA Code <del>Part A</del>, paragraph <del>R111.2440.2</del></p>  |                    |
| ISRS 4410 (Revised) Paragraph A21 | <p>Notwithstanding that Section 290, <i>Independence—Audit and Review Engagements</i> and Section 291, <i>Independence—Other Assurance Engagements</i> in Part B of the IESBA Code do not apply to compilation engagements, national ethical codes or laws or regulations may specify requirements or disclosure rules pertaining to independence.</p>                                      | <ul style="list-style-type: none"> <li>Update reference to the Code</li> </ul> | <p>Notwithstanding that the <i>International Independence Standards</i> Section 290, <del><i>Independence—Audit and Review Engagements</i></del> and Section 291, <del><i>Independence—Other Assurance Engagements</i></del> in <del>Part B</del> of the IESBA Code do not apply to compilation engagements, national ethical codes or laws or regulations may specify requirements or disclosure rules pertaining to independence.</p> | 1                  |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|---------------------------------------|---|---|---|--------------------|
| Standard                              | Extant Paragraphs   |   | Proposed Change   | Category of change |
| ISRS 4410 (Revised)<br>Paragraph A22  | <p>Law, regulation or relevant ethical requirements may:</p> <p>(a) Require the practitioner to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.</p> <p>(b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.<sup>37</sup></p> <p><sup>37</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.</p>       | <ul style="list-style-type: none"> <li>Update footnote</li> <li>No changes identified – see paragraphs R360.36–360.36 A3</li> </ul> | <p>37 See, for example, <u>paragraphs R360.36 and R360.37</u></p> <p><del>Section 225.51 to 225.52</del> of the IESBA Code.</p> | 1                  |
| ISRS 4410 (Revised)<br>Paragraph A21b | <p>Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:</p> <p>(a) Law, regulation or relevant ethical requirements require the practitioner to report;</p> <p>(b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements; or</p> | No changes identified – see paragraphs R360.36–360.36 A3  | N/A   | N/A                |

| IAASB Standards                       |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|---------------------------------------|---|---|---|--------------------|
| Standard                              | Extant Paragraphs   |   | Proposed Change   | Category of change |
|                                       | (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so.  |   |   |                    |
| ISRS 4410 (Revised)<br>Paragraph A21c | Under paragraph 28 of this ISRS, the practitioner is not expected to have a level of understanding of laws and regulations beyond that necessary to be able to perform the compilation engagement. However, law, regulation or relevant ethical requirements may expect the practitioner to apply knowledge, professional judgment and expertise in responding to identified or suspected non-compliance. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body. | <ul style="list-style-type: none"> <li>No changes identified – see paragraphs R360.29 A1</li> </ul>   | N/A   | N/A                |
| ISRS 4410 (Revised)<br>Paragraph A25  | In some circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation or relevant ethical requirements. In other cases, reporting identified or suspected non-compliance to an appropriate authority outside the entity would not be considered a breach of the duty of confidentiality under the relevant ethical requirements. <sup>38</sup>                                 | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>No other changes identified – see paragraph R360.6 and 360.36 A3</li> </ul> | 38 See, for example, <u>paragraphs R114.1, 114.1A1 and R360.37</u> <del>Section 140.7 and Section 225.53</del> of the IESBA Code. | 1                  |



| IAASB Standards                    |   | Notes in Relation to the 2018 IESBA Code   | Proposed Changes to the IAASB Standards   |                    |
|------------------------------------|---|--|---|--------------------|
| Standard                           | Extant Paragraphs   |  | Proposed Change   | Category of change |
|                                    | 38 See, for example, Section 140.7 and Section 225.53 of the IESBA Code.  |  |   |                    |
| ISRS 4410 (Revised) Paragraph A21e | <p>The practitioner may consider consulting internally (e.g., within the firm or network firm), obtaining legal advice to understand the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulations or would breach the duty of confidentiality).<sup>39</sup></p> <p>39 See, for example, Section 225.55 of the IESBA Code.</p>  | <ul style="list-style-type: none"> <li>Update footnote reference</li> <li>No other changes identified – see paragraph 360.39 A1</li> </ul> | 39 See, for example, <u>paragraph 360.39 A1</u> <del>Section 225.55</del> of the IESBA Code | 1                  |
| ISRS 4410 (Revised) Paragraph A22  | Professional judgment is essential to the proper conduct of a compilation engagement. This is because interpretation of relevant ethical requirements and the requirements of this ISRS, and the need for informed decisions throughout the performance of a compilation engagement, require the application of relevant knowledge and experience to the facts and circumstances of the engagement. Professional judgment is necessary, in particular, when the engagement involves assisting management of the entity regarding decisions about: | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul>   | N/A   | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards |                    |
|--------------------------------------|--|---|---|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change                         | Category of change |
| ISRS 4410 (Revised)<br>Paragraph A23 | Professional judgment involves the application of relevant training, knowledge and experience, within the context provided by this ISRS and accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the compilation engagement.  | <ul style="list-style-type: none"> <li>See comment on ISA 200 Paragraph A25</li> </ul>    | N/A                                     | N/A                |
| ISRS 4410 (Revised)<br>Paragraph A26 | ISQC 1 requires the firm to obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. Information that assists the engagement partner in determining whether acceptance or continuance of client relationships and compilation engagements is appropriate may include information concerning the integrity of the principal owners, key management and those charged with governance. If the engagement partner has cause to doubt management's integrity to a degree that is likely to affect proper performance of the engagement, it may not be appropriate to accept the engagement. | <ul style="list-style-type: none"> <li>No changes identified – see section 320</li> </ul> | N/A                                     | N/A                |

| IAASB Standards                      |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--------------------------------------|--|---|--|--------------------|
| Standard                             | Extant Paragraphs  |   | Proposed Change  | Category of change |
| ISRS 4410 (Revised)<br>Paragraph A27 | ISQC 1 sets out the responsibilities of the firm for establishing policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements. This ISRS sets out the engagement partner's responsibilities with respect to the engagement team's compliance with relevant ethical requirements.  | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>         | N/A  | N/A                |
| ISRS 4410 (Revised)<br>Appendix 1    | We will perform the compilation engagement in accordance with the International Standard on Related Services (ISRS) 4410 (Revised), <i>Compilation Engagements</i> . ISRS 4410 (Revised) requires that, in undertaking this engagement, we comply with relevant ethical requirements, including principles of integrity, objectivity, professional competence and due care. For that purpose, we are required to comply with the International Ethics Standards Board for Professional Accountants' <i>Code of Ethics for Professional Accountants</i> (IESBA Code). | <ul style="list-style-type: none"> <li>Update to title of IESBA Code</li> </ul> | We will perform the compilation engagement in accordance with the International Standard on Related Services (ISRS) 4410 (Revised), <i>Compilation Engagements</i> . ISRS 4410 (Revised) requires that, in undertaking this engagement, we comply with relevant ethical requirements, including principles of integrity, objectivity, professional competence and due care. For that purpose, we are required to comply with the International Ethics Standards Board for Professional Accountants' <u><i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i></u> (IESBA Code). | 3                  |

| IAASB Standards  |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--|--|---|--|--------------------|
| Standard   | Extant Paragraphs  |   | Proposed Change  | Category of change |
| ISRS 4410 (Revised)<br>Appendix 2                                | We have applied our expertise in accounting and financial reporting to assist you in the preparation and presentation of these financial statements on the basis of accounting described in Note X to the financial statements. We have complied with relevant ethical requirements, including principles of integrity, objectivity, professional competence and due care.   | <ul style="list-style-type: none"> <li>No changes identified</li> </ul>           | N/A  | N/A                |
| International Framework for Assurance Engagements<br>Paragraph 2 | This Framework is not a Standard and, accordingly, does not establish any requirements (or basic principles or essential procedures) for the performance of audits, reviews, or other assurance engagements. <sup>8</sup> An assurance report cannot, therefore, claim that an engagement has been conducted in accordance with this Framework, but rather should refer to relevant Assurance Standards. Assurance Standards contain objectives, requirements, application and other explanatory material, introductory material and definitions that are consistent with this Framework, and are to be applied in audit, review, and other assurance engagements. Appendix 1 illustrates the ambit of pronouncements issued by the International Auditing and Assurance Standards Board (IAASB) and their | <ul style="list-style-type: none"> <li>Update to the title of the Code</li> </ul> | This Framework is not a Standard and, accordingly, does not establish any requirements (or basic principles or essential procedures) for the performance of audits, reviews, or other assurance engagements. <sup>8</sup> An assurance report cannot, therefore, claim that an engagement has been conducted in accordance with this Framework, but rather should refer to relevant Assurance Standards. Assurance Standards contain objectives, requirements, application and other explanatory material, introductory material and definitions that are consistent with this Framework, and are to be applied in audit, review, and other assurance engagements. Appendix 1 illustrates the ambit of pronouncements issued by the International Auditing and Assurance Standards Board (IAASB) and their relationship to each other and to the International Ethics Standards Board for Accountants' <i>International Code of Ethics for</i> | 3                  |

| IAASB Standards   |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|---|--|---|--|--------------------|
| Standard  | Extant Paragraphs  |   | Proposed Change  | Category of change |
|   | <p>relationship to each other and to the <i>Code of Ethics for Professional Accountants</i> issued by the International Ethics Standards Board for Accountants (IESBA Code).</p> <p><sup>8</sup> See the <i>Preface to the International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements</i>.</p>   |   | <p><i>Professional Accountants</i> <u>_____</u> <i>(including International Independence Standards)</i> issued by the <del>International Ethics Standards Board for Accountants</del> (IESBA Code).</p> <p><sup>8</sup> See the <i>Preface to the International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements</i>.</p>  |                    |
| International Framework for Assurance Engagements Paragraph 5 | <p><b>Ethical Principles and Quality Control Standards</b></p> <p>Quality control within firms that perform assurance engagements, and compliance with ethical principles, including independence requirements, are widely recognized as being in the public interest and an integral part of high-quality assurance engagements. Such engagements are performed in accordance with Assurance Standards, which are premised on the basis that:</p> <p>(a) The members of the engagement team and the engagement quality control reviewer (for those engagements where one has been appointed) are subject to Parts A and B of the IESBA Code related to assurance engagements, other professional requirements, or requirements in law or regulation, that are at least demanding; and</p> | <ul style="list-style-type: none"> <li>Reflecting the structural changes to the Code</li> </ul> | <p><b>Ethical Principles and Quality Control Standards</b></p> <p>Quality control within firms that perform assurance engagements, and compliance with ethical principles, including independence requirements, are widely recognized as being in the public interest and an integral part of high-quality assurance engagements. Such engagements are performed in accordance with Assurance Standards, which are premised on the basis that:</p> <p>a) The members of the engagement team and the engagement quality control reviewer (for those engagements where one has been appointed) are subject to <u>the provisions</u> <del>Parts A and B</del> of the IESBA Code related to assurance engagements, other professional requirements, or requirements in law or regulation, that are at least demanding; and</p> | 1                  |

| IAASB Standards  |   | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards   |                    |
|--|---|---|---|--------------------|
| Standard   | Extant Paragraphs   |   | Proposed Change   | Category of change |
|  | (b) ...   |   | b) ...  |                    |
| International Framework for Assurance Engagements<br>Paragraph 6 | <p>The IESBA Code</p> <p>Part A of the IESBA Code establishes the following fundamental principles with which the practitioner is required to comply:</p> <ul style="list-style-type: none"> <li>(a) Integrity;</li> <li>(b) Objectivity;</li> <li>(c) Professional competence and due care;</li> <li>(d) Confidentiality; and</li> <li>(e) Professional behavior.</li> </ul> | <ul style="list-style-type: none"> <li>• Reflecting the structural changes to the Code</li> </ul>   | <p>The IESBA Code</p> <p><del>Part A of t</del><u>Part A of the IESBA Code establishes the following fundamental principles of ethics, which are with which the practitioner is required to comply:</u></p> <ul style="list-style-type: none"> <li>(a) Integrity;</li> <li>(b) Objectivity;</li> <li>(c) Professional competence and due care;</li> <li>(d) Confidentiality; and</li> <li>(e) Professional behavior.</li> </ul>   | 1                  |
| International Framework for Assurance Engagements<br>Paragraph 7 | <p>Part A also provides a conceptual framework for professional accountants to apply to identify threats to compliance with the fundamental principles, evaluate the significance of the threats identified, and apply safeguards, when necessary, to eliminate the threats or reduce them to an acceptable level.</p>  | <ul style="list-style-type: none"> <li>• Reflecting the structural changes to the Code</li> <li>• Aligning with terminology used in the Code</li> </ul> | <p><u>The IESBA Code provides a conceptual framework that professional accountants are to apply in order to identify, evaluate and address threats to compliance with the fundamental principles.</u></p> <p><del>Part A also provides a conceptual framework for professional accountants to apply to identify threats to compliance with the fundamental principles, evaluate the significance of the threats identified, and apply safeguards, when necessary, to eliminate the threats or reduce them to an acceptable level.</del></p> | 1, 2 & 4           |

| IAASB Standards  |  | Notes in Relation to the 2018 IESBA Code  | Proposed Changes to the IAASB Standards  |                    |
|--|--|---|--|--------------------|
| Standard   | Extant Paragraphs  |   | Proposed Change  | Category of change |
| International Framework for Assurance Engagements<br>Paragraph 8 | Part B of the IESBA Code describes how the conceptual framework in Part A applies in certain situations to professional accountants in public practice, including independence. The IESBA Code defines independence as comprising both independence of mind and independence in appearance. Independence safeguards the ability to form an assurance conclusion without being affected by influences that might compromise that conclusion. Independence enhances the ability to act with integrity, to be objective and to maintain an attitude of professional skepticism. | <ul style="list-style-type: none"> <li>Reflecting the structural changes to the Code</li> </ul> | <del>Part B of t</del> The IESBA Code <u>sets out requirements and application material on various topics</u> <del>describes how the conceptual framework in Part A applies in certain situations to professional accountants in public practice, including independence.</del> The IESBA Code defines independence as comprising both independence of mind and independence in appearance. Independence safeguards the ability to form an assurance conclusion without being affected by influences that might compromise that conclusion. Independence enhances the ability to act with integrity, to be objective and to maintain an attitude of professional skepticism. | 1                  |

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## **EXPOSURE DRAFT**

# **NEW ZEALAND SPECIFIC AMENDMENTS TO AUDITING AND ASSURANCE STANDARDS: IMPLICATIONS OF THE REVISED PROFESSIONAL AND ETHICAL STANDARD 1 ON THE NZAuASB's STANDARDS**

**ED NZAuASB 2019-3**

**Invitation to Comment**

November 2019

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New Zealand  
<http://www.xrb.govt.nz>

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# Information for Respondents

## Invitation to Comment

The New Zealand Auditing and Assurance Standards Board (NZAuASB)<sup>1</sup> is seeking comments on the specific matters raised in this Invitation to Comment. We will consider all comments before finalising *New Zealand Specific Amendments to the Auditing and Assurance Standards: Implications of the Revised Professional and Ethical Standard 1 on the NZAuASB's Standards*.

If you want to comment, please supplement your opinions with detailed comments, whether supportive or critical of the proposals, as both supportive and critical comments are essential to a balanced view.

Comments are most useful if they indicate the specific paragraph to which they relate, contain a clear rationale and, where applicable, provide a suggestion for an alternative. Feel free to provide comments only for those questions or issues that are relevant to you.

Comments should be submitted electronically using our 'Open for comment' page at

[\[insert link\]](#)

The closing date for submissions is [\[date\]](#)

## Publication of Submissions, the Official Information Act and the Privacy Act

We intend publishing all submissions on the XRB website ([xrb.govt.nz](http://xrb.govt.nz)), unless the submission may be defamatory. If you have any objection to publication of your submission, we will not publish it on the internet. However, it will remain subject to the Official Information Act 1982 and may, therefore, be released in part or full. The Privacy Act 1993 also applies.

If you have an objection to the release of any information contained in your submission, we would appreciate you identifying the parts of your submission be withheld, and the grounds under the Official Information Act 1982 for doing so (e.g. that it would be likely to unfairly prejudice the commercial position of the person providing the information).

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<sup>1</sup> The NZAuASB is a sub-Board of the External Reporting Board and is responsible for setting auditing and assurance standards.

## List of Abbreviations

The following abbreviations are used in this Invitation to Comment.

|           |  |
|-----------|--|
| ED        | Exposure Draft                                       |
| IAASB     | International Auditing and Assurance Standards Board |
| IESBA     | International Ethics Standards Board for Accountants |
| ISAs      | International Standards on Auditing                  |
| ISAs (NZ) | International Standards on Auditing (New Zealand)    |
| ITC       | Invitation to comment                                |
| NZAuASB   | New Zealand Auditing and Assurance Standards Board   |
| PES       | Professional and Ethical Standard                    |
| XRB       | External Reporting Board                             |

## Summary of Questions for Respondents

1. Do you agree with the proposed amendments to the auditing and assurance standards to align with the revised Professional and Ethical Standard 1?
2. Do you have any other comments on ED NZAuASB 2019-2 *New Zealand Specific Amendments to the Auditing and Assurance Standards: Implications of the Revised Professional and Ethical Standard 1 on the NZAuASB's Standards* (please be specific)?
3. Do you ~~believe that the proposed effective date of approximately 90 days after approval of the final standard is appropriate? agree that a lengthy transition period is not required given the limited nature of the proposed changes?~~ If not, please explain why not.

# 1. Introduction

## 1.1 Purpose of this Invitation to Comment

1. The purpose of this Invitation to Comment is to seek feedback on the proposed amendments to standards issued by the NZAuASB.

## 1.2 Background

2. In December 2018, the NZAuASB issued a revised code of ethics, Professional and Ethical Standard (PES) 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*, based on the International Ethics Standards Board for Accountants' (IESBA), *International Code of Ethics for Professional Accountants (including International Independence Standards)*.
3. The International Auditing and Assurance Standards Board (IAASB) has proposed amendments to its auditing, assurance and related services standards to address inconsistencies between the extant international standards and the revised IESBA Code.
4. This Invitation to Comment and Exposure Draft proposes amendments to the auditing and assurance standards, including Professional and Ethical Standard 3 (Amended)<sup>2</sup> issued by the NZAuASB that are not otherwise captured by the amendments proposed by the IAASB. This includes amendments to New Zealand specific paragraphs within ISAs (NZ), ISAEs (NZ) and ISREs (NZ) and to domestic standards.
5. The New Zealand exposure draft should be considered in conjunction with the IAASB's Exposure Draft, [\*Proposed Conforming Amendments to the IAASB's International Standards\*](#). The ~~New Zealand~~ exposure draft does not mark up the changes to the international standards, as made by the IAASB. These are explained in the IAASB's explanatory memorandum. Stakeholders are advised to read this Invitation to Comment and the attached exposure draft together with the IAASB explanatory memorandum and exposure draft to fully understand the impact of the changes.

## 1.3 Reasons for Issuing this Exposure Draft

6. This exposure draft considers the implications of the revised PES 1 on the NZAuASB's auditing and assurance standards, including Professional and Ethical Standard 3 (Amended). The amendments affect numerous standards issued by the NZAuASB as identified in the Exposure Draft.

## 1.4 Timeline and Next Steps

7. Submissions on ED 2019-3 are due by [date]. Information on how to make submissions is provided on page 4 of this Invitation to Comment.

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<sup>2</sup> Professional and Ethical Standard 3 (Amended), *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements*

8. The NZAuASB will consider the submissions received immediately after the consultation period ends. Subject to the content of that feedback, the NZAuASB expects to issue the *Standard New Zealand Specific Amendments to the Auditing and Assurance Standards: Implications of the revised Professional and Ethical Standard 1 on the NZAuASB's Standards* in early 2020.
9. Given the limited nature of the amendments proposed and because the conforming amendments do not create any new obligations, the NZAuASB is proposing that the conforming amendments become effective approximately 90 days after approval of the final standard. The NZAuASB is seeking comments on the effective date of the conforming amendments.~~The effective date for the final conforming amendments is a matter for the NZAuASB to determine. However, it is anticipated that, given the limited nature of the amendments proposed, the amendments can go into effect almost immediately.~~



## 2. Overview of Exposure Draft *New Zealand Specific Amendments to the Auditing and Assurance Standards: Implications of the Revised Professional and Ethical Standard 1 on the NZAuASB's Standards*

### 2.1 Matters Addressed in this Exposure Draft

10. The exposure draft considers the implications of the revised Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*, on standards issued by the NZAuASB.
11. The purpose of making the revisions is solely to align the extant wording with the revised PES 1 and not to re-evaluate or discuss the merits of each reference, thus ensuring that the auditing and assurance standards can continue to be applied effectively together with the revised PES 1.
12. The IAASB has proposed amendments to its auditing, assurance and related services standards to address inconsistencies between the extant international standards and the revised *International Code of Ethics for Professional Accountants (including International Independence Standards)* issued by the IESBA.

### ~~2.2 Proposed Amendments to ISA (NZ) 700 (Revised)~~

- ~~13. The NZAuASB proposes to amend the independence statement in the "basis for opinion" paragraph in the auditor's report by replacing the reference to Professional and Ethical Standard 1 with a reference to the ethical requirements that are relevant to the audit of financial statements in New Zealand.~~
- ~~14. As part of the restructure and revision of the IESBA Code, the applicability of Part 2, *Professional Accountants in Business*, was clarified and enhanced to apply also to professional accountants in public practice. This increased emphasis on the applicability of Part 2 to professional accountants in public practice raises the question as to whether an assurance practitioner can assert compliance with the ethical requirements that are at least as stringent as the IESBA Code if Professional and Ethical Standard 1 does not incorporate these provisions.~~
- ~~15. As the NZAuASB's mandate relates to professional and ethical standard for assurance practitioners, to address the applicability issue, PES 1 states, "When dealing with an ethics issue, the assurance practitioner shall consider the context in which the issue has arisen or might arise. Where an individual who is an assurance practitioner is performing assurance services pursuant to the assurance practitioner's relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with any other ethical standards that apply to these circumstances."<sup>3</sup> [emphasis added]~~

<sup>3</sup>-Professional and Ethical Standard 1, paragraphs NZ-R120.4.1 and NZ-R300.5

~~16. Given the reference in PES 1 to “any other ethical standards”, the NZAuASB is of the view that a generic reference to ethical requirements relevant to the audit financial Statements is appropriate. Accordingly, the requirement to refer to Professional and Ethical Standard 1 in the auditor’s report is amended. The proposed wording references ethical standards that are relevant to an audit of financial statements in New Zealand.~~

### Questions for Respondents

1. Do you agree with the proposed amendments to the auditing and assurance standards to align with the revised Professional and Ethical Standard 1?
2. Do you have any other comments on ED 2019-2, *New Zealand Specific Amendments to the Auditing and Assurance Standards: Implications of the Revised Professional and Ethical Standard 1 on the NZAuASB’s Standards* (please be specific)?

### 2.32 Effective Date

~~17.13. Given the limited nature of the amendments proposed and because the conforming amendments do not create any new obligations, the NZAuASB is proposing that the conforming amendments become effective approximately 90 days after approval of the final standard. The NZAuASB does not consider that a lengthy transition period is required given the extent of the change is limited in nature.~~

### Questions for Respondents

3. Do you believe that the proposed effective date of approximately 90 days after approval of the final standard is appropriate? ~~agree that a lengthy transition period is not required given the limited nature of the proposed changes?~~ If not, please explain why not.

## **EXPOSURE DRAFT NZAuASB 2019-3**

### **New Zealand Specific Amendments to the Auditing and Assurance Standards: *Implications of the Revised Professional and Ethical Standard 1 on the NZAuASB's Standards***

#### **CONTENTS**

##### **A: INTRODUCTION**

##### **B: PROPOSED AMENDMENTS TO NZ SPECIFIC PARAGRAPHS**

##### **C: PROPOSED AMENDMENTS TO DOMESTIC STANDARDS**

##### **D: EFFECTIVE DATE**

## **A: INTRODUCTION**

This document sets out proposed amendments to the auditing and assurance standards, including professional and ethical standards arising from the issuance of Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand)

Amended paragraphs are shown with new text underlined and deleted text struck through.

The footnote numbers within these amendments do not align with the ISAs (NZ) and other pronouncements that are amended, and reference should be made to those ISAs (NZ) and other pronouncements.

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## B: Proposed Amendments to NZ specific paragraphs

### B.1 Professional and Ethical Standard 3 (Amended) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements*

Amend paragraphs NZ12.9 and NZA14.1 to replace reference to Professional and Ethical Standard 1 (Revised) with Professional and Ethical Standard 1. Footnote references to PES 1 are updated. A new footnote is added following the first reference to PES 1 to add its title.

- NZ12.9 Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Professional and Ethical Standard 1<sup>4</sup> ~~(Revised)~~, and other applicable law or regulation.
- NZA14.1 Professional and Ethical Standard 1 ~~(Revised)~~ recognises that the familiarity threat is particularly relevant in the context of financial statement audits of public interest entities. For these audits, Professional and Ethical Standard 1 ~~(Revised)~~ requires the rotation of the key audit partner<sup>5</sup> after a pre-defined period, normally no more than seven years, and provides related standards and guidance<sup>6</sup>.

### B.2 ISA (NZ) 210 *Agreeing the Terms of Audit Engagements*

Amend paragraph NZ21.1 and related footnote to reflect the new title of Professional and Ethical Standard 1.

- NZ21.1 Professional and Ethical Standard 1 ~~(Revised)~~,<sup>7</sup> requires assurance practitioners to comply with Auditing Standards; therefore auditors shall not sign an audit report that does not conform to the requirements of this ISA (NZ). In the extremely rare situation described in paragraph 21, the auditor shall attach a separate report that conforms to the requirements of this ISA (NZ).

### B.3 ISA (NZ) 700 ~~(Revised)~~ *Forming an Opinion and Reporting on Financial Statements*

~~In paragraphs NZ28(c) and NZ50(e)(1) the reference to Professional and Ethical Standard 1 (Revised) is replaced with a reference to “ethical requirements that are relevant to the audit of financial statements in New Zealand”. This change is necessary to reflect the structural changes~~

<sup>4</sup> Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*

<sup>5</sup> Professional and Ethical Standard 1 ~~(Revised)~~, Definitions:

<sup>6</sup> ~~Paragraph 290.151 of Professional and Ethical Standard 1, section 540, *Long Association of Personnel (including Partner Rotation) with an Audit or Review Client* – (Revised)~~

<sup>7</sup> Professional and Ethical Standard 1 ~~(Revised)~~, *“International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand) (Compiled)”*.

to Professional and Ethical Standard 1 and the revised applicability of Professional and Ethical Standard 1. The illustrative reports are also amended accordingly.

### **Basis for Opinion**

28. ~~The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that: (Ref: Para. A32)~~
- ~~(a) States that the audit was conducted in accordance with International Standards on Auditing (New Zealand); (Ref: Para. A33)~~
  - ~~(b) Refers to the section of the auditor's report that describes the auditor's responsibilities under the ISAs (NZ);~~
  - ~~(c) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall identify the jurisdiction of origin of the relevant ethical requirements or refer to the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code); and (Ref: Para. A34–A39)~~
- ~~NZ28(c) In New Zealand, the statement required by paragraph 28(c) shall refer to ethical requirements that are relevant to the audit of financial statements in New Zealand. Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board. Professional and Ethical Standard 1 (Revised) is at least as restrictive as Parts A and B of the IESBA Code related to an audit of financial statements.~~
- ~~(d) States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.~~

### ***Auditor's Report Prescribed by Law or Regulation***

50. ~~If the auditor is required by law or regulation of a specific jurisdiction to use a specific layout, or wording of the auditor's report, the auditor's report shall refer to International Standards on Auditing (New Zealand) only if the auditor's report includes, at a minimum, each of the following elements: (Ref: Para. A70–A71)~~
- ~~(a) A title.~~
  - ~~(b) An addressee, as required by the circumstances of the engagement.~~
  - ~~(c) An Opinion section containing an expression of opinion on the financial statements and a reference to the applicable financial reporting framework used to prepare the financial statements (including identifying the jurisdiction of origin of the financial reporting framework that is not International Financial Reporting Standards or International Public Sector Accounting Standards, see paragraph 26).~~
- ~~NZ50(e)(1) The opinion paragraph shall identify the applicable financial reporting requirements issued by the New Zealand Accounting Standards Board used to prepare the financial statements.~~

- (d) ~~An identification of the entity's financial statements that have been audited.~~
- (e) ~~A statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall identify the jurisdiction of origin of the relevant ethical requirements or refer to the IESBA Code.~~
- NZ50(e)(1) ~~In New Zealand, the independence statement shall refer to ethical requirements that are relevant to the audit of financial statements in New Zealand. Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board.~~
- (f) ~~Where applicable, a section that addresses, and is not inconsistent with, the reporting requirements in paragraph 22 of ISA (NZ) 570 (Revised).~~
- (g) ~~Where applicable, a Basis for Qualified (or Adverse) Opinion section that addresses, and is not inconsistent with, the reporting requirements in paragraph 23 of ISA (NZ) 570 (Revised).~~
- (h) ~~Where applicable, a section that includes the information required by ISA (NZ) 701, or additional information about the audit that is prescribed by law or regulation and that addresses, and is not inconsistent with, the reporting requirements in that ISA (NZ).<sup>8</sup> (Ref: Para. A72–A73)~~
- (i) ~~Where applicable, a section that addresses the reporting requirements in paragraph 24 of ISA (NZ) 720 (Revised)<sup>9</sup>.~~
- (j) ~~[Amended by the NZAuASB].~~
- NZ50(j)(1) ~~A description of the responsibilities of those charged with governance for the preparation of the financial statements that addresses, and is not inconsistent with, the requirements in paragraphs 33–36.~~
- (k) ~~A reference to International Standards on Auditing (New Zealand) and the law or regulation, and a description of the auditor's responsibilities for an audit of the financial statements that addresses, and is not inconsistent with, the requirements in paragraphs 37–40. (Ref: Para. A54–A55)~~
- (l) ~~[Amended by the NZAuASB].~~
- NZ50(l)(1) ~~For audits of complete sets of general purpose financial statements of FMC reporting entities considered to have a higher level of public accountability, the name of the engagement partner unless, in rare circumstances, such disclosure is reasonably expected to lead to a significant personal security threat.~~
- (m) ~~The auditor's signature.~~
- (n) ~~The auditor's address.~~
- (o) ~~The date of the auditor's report.~~

<sup>8</sup>—ISA (NZ) 701, paragraphs 11–16

<sup>9</sup>—ISA (NZ) 720 (Revised), paragraph 24.

...

~~[NZ] Illustration 1 — Auditor's Report on Financial Statements of a FMC Reporting Entity Considered to have a Higher Level of Public Accountability Prepared in Accordance with a Fair Presentation Framework (for example NZ IFRS)~~

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- ~~Audit of a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances<sup>10</sup>. comprises all of the relevant ethical requirements that apply to the audit. The auditor has also chosen to refer to the International Ethics Standards Board for Accountants *International Code of Ethics for Professional Accountants (including International Independence Standards)*.~~
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~The auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information.~~
- ~~In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.~~

**INDEPENDENT AUDITOR'S REPORT**

...

**Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in

<sup>10</sup> ~~For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*~~



~~accordance with the ethical requirements that are relevant to our audit of financial Statements in New Zealand Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the Company.~~

~~...~~

[NZ] Illustration 2— Auditor’s Report on Consolidated Financial Statements of a FMC Reporting Entity Considered to have a Higher Level of Public Accountability Prepared in Accordance with a Fair Presentation Framework (for example, NZ IFRS)

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- ~~Audit of a complete set of consolidated financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is a group audit of an entity with subsidiaries (i.e., ISA (NZ) 600 applies).~~
- ~~The consolidated financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the consolidated financial statements in ISA (NZ) 210.~~
- ~~The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>11</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~The auditor has obtained all of the other information prior to the date of the auditor’s report and has not identified a material misstatement of the other information.~~
- ~~In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law.~~

## **INDEPENDENT AUDITOR’S REPORT**

...

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial Statements in New Zealand Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit

<sup>11</sup> ~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

~~evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company or any of its subsidiaries.~~

~~...~~

DRAFT

~~[NZ] Illustration 3— Auditor’s Report on Financial Statements of a Public Benefit Entity that is not a FMC Reporting Entity Considered to have a Higher Level of Public Accountability Prepared in Accordance with a Fair Presentation Framework (for example, Public Benefit Entity Standards)~~

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- ~~• Audit of a complete set of financial statements of a public benefit entity that is not a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~• The financial statements are prepared by management of the entity in accordance with Public Benefit Entity Standards<sup>12</sup> (a general purpose framework).~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~• The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>13</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701.~~
- ~~• The auditor has obtained all of the other information prior to the date of the auditor’s report and has not identified a material misstatement of the other information.~~
- ~~• The auditor has no other reporting responsibilities required under local law.~~

<sup>12</sup> ~~The use of Public Benefit Entity Standards is used for the purposes of illustration. The appropriate financial reporting standards to be applied by an entity will be determined by the tier structure established in XRB A1 *Application of the Accounting Standards Framework*. The Auditor’s Report would identify one of the following:~~

- ~~• New Zealand equivalents to International Financial Reporting Standards. (This may also include compliance with International Financial Reporting Standards)~~
- ~~• New Zealand equivalents to International Financial Reporting Standards Reduced Disclosure Regime~~
- ~~• Public Benefit Entity Standards~~
- ~~• Public Benefit Entity Standards Reduced Disclosure Regime~~
- ~~• Public Benefit Entity Simple Format Reporting—Accrual (Public Sector)~~
- ~~• Public Benefit Entity Simple Format Reporting—Accrual (Not For Profit).~~

<sup>13</sup> ~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

- ~~The auditor elects to refer to the description of the auditor's responsibility included on the website of the XRB.~~

## INDEPENDENT AUDITOR'S REPORT

...

### **Basis for Opinion**

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the [entity] in accordance with the ethical requirements that are relevant to our audit of financial Statements in New Zealand Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the [entity].~~

[NZ] Illustration 4— Auditor’s Report on Financial Statements of an Entity Other than a FMC Reporting Entity Considered to have a Higher Level of Public Accountability Prepared in Accordance with a General Purpose Compliance Framework

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- ~~Audit of a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability required by law or regulation. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~The financial statements are prepared by management of the entity in accordance with the Financial Reporting Framework (XYZ Law) of Jurisdiction X (that is, a financial reporting framework, encompassing law or regulation, designed to meet the common financial information needs of a wide range of users, but which is not a fair presentation framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>14</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701.~~
- ~~The auditor has obtained all of the other information prior to the date of the auditor’s report and has not identified a material misstatement of the other information.~~
- ~~The auditor has no other reporting responsibilities required under local law.~~

## INDEPENDENT AUDITOR’S REPORT

...

### Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of financial Statements in New Zealand Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other

<sup>14</sup>— For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*

responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company.

#### **B.4 ISA (NZ) 705 *Modifications to the Opinion in the Independent Auditor's Report***

Amend illustrative reports [NZ] Illustration 1 through [NZ] Illustration 5 to reflect changes to the wording in the auditor's report as required by ISA (NZ) 700 (Revised).

#### **Appendix**

(Ref: Para. A17 A18, A25)

#### **Illustrations of Auditor's Reports with Modifications to the Opinion**

- ~~[NZ] Illustration 1: An auditor's report containing a qualified opinion due to a material misstatement of the financial statements.~~
- ~~[NZ] Illustration 2: An auditor's report containing an adverse opinion due to a material misstatement of the consolidated financial statements.~~
- ~~[NZ] Illustration 3: An auditor's report containing a qualified opinion due to the auditor's inability to obtain sufficient appropriate audit evidence regarding a foreign associate.~~
- ~~[NZ] Illustration 4: An auditor's report containing a disclaimer of opinion due to the auditor's inability to obtain sufficient appropriate audit evidence about a single element of the consolidated financial statements.~~
- ~~[NZ] Illustration 5: An auditor's report containing a disclaimer of opinion due to the auditor's inability to obtain sufficient appropriate audit evidence about multiple elements of the financial statements.~~

### ~~[NZ] Illustration 1—Qualified Opinion due to a Material Misstatement of the Financial Statements~~

~~For purposes of this illustrative auditor’s report, the following circumstances are assumed:~~

- ~~• Audit of a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600<sup>15</sup> does not apply).~~
- ~~• The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.<sup>16</sup>~~
- ~~• Inventories are misstated. The misstatement is deemed to be material but not pervasive to the financial statements (i.e., a qualified opinion is appropriate).~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>17</sup>, comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~• The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the qualified opinion on the consolidated financial statements also affects the other information.~~
- ~~• In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.~~

## **~~INDEPENDENT AUDITOR’S REPORT~~**

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

### **~~Report on the Audit of the Financial Statements<sup>18</sup>~~**

#### **~~Qualified Opinion~~**

~~We have audited the financial statements of ABC Company (the Company), which comprise the~~

<sup>15</sup>—ISA (NZ) 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

<sup>16</sup>—ISA (NZ) 210, *Agreeing the Terms of Audit Engagements*

<sup>17</sup>—For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*

<sup>18</sup>—The sub title “Report on the Audit of the Financial Statements” is unnecessary in circumstances when the second sub title “Report on Other Legal and Regulatory Requirements” is not applicable.



statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion* section of our report, the accompanying financial statements present fairly, in all material respects, (or *give a true and fair view of*) the financial position of the Company as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).

### **Basis for Qualified Opinion**

The Company's inventories are carried in the statement of financial position at xxx. Management has not stated the inventories at the lower of cost and net realisable value but has stated them solely at cost, which constitutes a departure from NZ IFRS. The Company's records indicate that, had management stated the inventories at the lower of cost and net realisable value, an amount of xxx would have been required to write the inventories down to their net realisable value. Accordingly, cost of sales would have been increased by xxx, and income tax, net income and shareholders' equity would have been reduced by xxx, xxx and xxx, respectively.

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

...

## [NZ] Illustration 2—Adverse Opinion due to a Material Misstatement of the Consolidated Financial Statements

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- ~~Audit of a complete set of consolidated financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is a group audit of an entity with subsidiaries (i.e., ISA (NZ) 600 applies).~~
- ~~The consolidated financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the consolidated financial statements in ISA (NZ) 210.~~
- ~~The consolidated financial statements are materially misstated due to the non-consolidation of a subsidiary. The material misstatement is deemed to be pervasive to the consolidated financial statements. The effects of the misstatement on the consolidated financial statements have not been determined because it was not practicable to do so (i.e., an adverse opinion is appropriate).~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>19</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~ISA (NZ) 701 applies; however, the auditor has determined that there are no key audit matters other than the matter described in the Basis for Adverse Opinion section.~~
- ~~The auditor has obtained all of the other information prior to the date of the auditor's report and the matter giving rise to the adverse opinion on the consolidated financial statements also affects the other information.~~
- ~~In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law.~~

## **INDEPENDENT AUDITOR'S REPORT**

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

### **Report on the Audit of the Consolidated Financial Statements<sup>20</sup>**

<sup>19</sup> For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

<sup>20</sup> The sub title "Report on the Audit of the Consolidated Financial Statements" is unnecessary in circumstances when the second sub title "Report on Other Legal and Regulatory Requirements" is not applicable.

## **Adverse Opinion**

~~We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.~~

~~In our opinion, because of the significance of the matter discussed in the *Basis for Adverse Opinion* section of our report, the accompanying consolidated financial statements do not present fairly (or *do not give a true and fair view of*) the consolidated financial position of the Group as at December 31, 20X1, and (of) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).~~

## **Basis for Adverse Opinion**

~~As explained in Note X, the Group has not consolidated subsidiary XYZ Company that the Group acquired during 20X1 because it has not yet been able to determine the fair values of certain of the subsidiary's material assets and liabilities at the acquisition date. This investment is therefore accounted for on a cost basis. Under NZ IFRS, the Company should have consolidated this subsidiary and accounted for the acquisition based on provisional amounts. Had XYZ Company been consolidated, many elements in the accompanying consolidated financial statements would have been materially affected. The effects on the consolidated financial statements of the failure to consolidate have not been determined.~~

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the group financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our adverse opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company or any of its subsidiaries.~~

~~...~~

### [NZ] Illustration 3—Qualified Opinion due to the Auditor’s Inability to Obtain Sufficient Audit Evidence Regarding a Foreign Associate

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- ~~Audit of a complete set of consolidated financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is a group audit of an entity with subsidiaries (i.e., ISA (NZ) 600 applies).~~
- ~~The consolidated financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the consolidated financial statements in ISA (NZ) 210.~~
- ~~The auditor was unable to obtain sufficient appropriate audit evidence regarding an investment in a foreign associate. The possible effects of the inability to obtain sufficient appropriate audit evidence are deemed to be material but not pervasive to the consolidated financial statements (i.e., a qualified opinion is appropriate).~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards (New Zealand))* and any other ethical provisions that apply to these circumstances.<sup>21</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the qualified opinion on the consolidated financial statements also affects the other information.~~
- ~~In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law.~~

## **INDEPENDENT AUDITOR’S REPORT**

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

### **Report on the Audit of the Consolidated Financial Statements<sup>22</sup>**

#### **Qualified Opinion**

<sup>21</sup> ~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

<sup>22</sup> ~~The sub title “Report on the Audit of the Consolidated Financial Statements” is unnecessary in circumstances when the second sub title “Report on Other Legal and Regulatory Requirements” is not applicable.~~

~~We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.~~

~~In our opinion, except for the possible effects of the matter described in the *Basis for Qualified Opinion* section of our report, the accompanying consolidated financial statements present fairly, in all material respects, (or give a true and fair view of) the financial position of the Group as at December 31, 20X1, and (of) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).~~

### **Basis for Qualified Opinion**

~~The Group's investment in XYZ Company, a foreign associate acquired during the year and accounted for by the equity method, is carried at xxx on the consolidated statement of financial position as at December 31, 20X1, and ABC's share of XYZ's net income of xxx is included in ABC's income for the year then ended. We were unable to obtain sufficient appropriate audit evidence about the carrying amount of ABC's investment in XYZ as at December 31, 20X1 and ABC's share of XYZ's net income for the year because we were denied access to the financial information, management, and the auditors of XYZ. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.~~

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the group financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company or any of its subsidiaries.~~

~~---~~

#### [NZ] Illustration 4 — Disclaimer of Opinion due to the Auditor's Inability to Obtain Sufficient Appropriate Audit Evidence about a Single Element of the Consolidated Financial Statements

For purposes of this illustrative auditor's report, the following circumstances are assumed:

Audit of a complete set of consolidated financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is a group audit of an entity with subsidiaries (i.e., ISA (NZ) 600 applies).

The consolidated financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).

The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the consolidated financial statements in ISA (NZ) 210.

~~The auditor was unable to obtain sufficient appropriate audit evidence about a single element of the consolidated financial statements. That is, the auditor was also unable to obtain audit evidence about the financial information of a joint venture investment that represents over 90% of the entity's net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the consolidated financial statements (i.e., a disclaimer of opinion is appropriate).~~

~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand) and any other ethical provisions that apply to these circumstances.<sup>23</sup> comprises all of the relevant ethical requirements that apply to the audit.~~

~~A more limited description of the auditor's responsibilities section is required.~~

~~In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law.~~

## **~~INDEPENDENT AUDITOR'S REPORT~~**

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

### **~~Report on the Audit of the Consolidated Financial Statements<sup>24</sup>~~**

#### **~~Disclaimer of Opinion~~**

~~We were engaged to audit the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.~~

~~We do not express an opinion on the accompanying consolidated financial statements of the Group. Because of the significance of the matter described in the *Basis for Disclaimer of Opinion* section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these consolidated financial statements.~~

#### **~~Basis for Disclaimer of Opinion~~**

~~The Group's investment in its joint venture XYZ Company is carried at xxx on the Group's consolidated statement of financial position, which represents over 90% of the Group's net assets as at December 31, 20X1. We were not allowed access to the management and the auditors of XYZ Company, including XYZ Company's auditors' audit documentation. As a result, we were unable to determine whether any adjustments were necessary in respect of the Group's proportional share of XYZ Company's assets that it controls jointly, its proportional share of XYZ Company's liabilities for which it is jointly responsible,~~

<sup>23</sup>—For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

<sup>24</sup>—The sub title "Report on the Audit of the Consolidated Financial Statements" is unnecessary in circumstances when the second sub title "Report on Other Legal and Regulatory Requirements" is not applicable.



its proportional share of XYZ's income and expenses for the year, and the elements making up the consolidated statement of changes in equity and the consolidated cash flow statement.

### **Directors' Responsibilities for the Consolidated Financial Statements<sup>25</sup>**

~~[Reporting in accordance with ISA (NZ) 700 (Revised)—see Illustration 2 in ISA (NZ) 700 (Revised).]~~

### **Auditor's Responsibilities for the Audit of the Consolidated Financial Statements**

Our responsibility is to conduct an audit of the Group's consolidated financial statements in accordance with International Standards on Auditing (New Zealand) and to issue an auditor's report. However, because of the matter described in the *Basis for Disclaimer of Opinion* section of our report, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these consolidated financial statements.

We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company or any of its subsidiaries.

### **Report on Other Legal and Regulatory Requirements**

~~[Reporting in accordance with ISA (NZ) 700 (Revised)—see Illustration 2 in ISA (NZ) 700 (Revised).]~~

~~[Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate]~~

~~[Auditor Address]~~

~~[Date]~~

#### ~~[NZ] Illustration 5—Disclaimer of Opinion due to the Auditor's Inability to Obtain Sufficient Appropriate Audit Evidence about Multiple Elements of the Financial Statements~~

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- ~~Audit of a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600, does not apply).~~
- ~~The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~The auditor was unable to obtain sufficient appropriate audit evidence about multiple elements of the financial statements, that is, the auditor was also unable to obtain audit~~

<sup>25</sup> ~~Or other terms that are appropriate in the context of the legal framework of the entity~~

evidence about the entity's inventories and accounts receivable. The possible effects of this inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements.

- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand) and any other ethical provisions that apply to these circumstances.<sup>26</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~A more limited description of the auditor's responsibilities section is required.~~
- ~~In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.~~

## **INDEPENDENT AUDITOR'S REPORT**

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

### **Report on the Audit of the Financial Statements<sup>27</sup>**

#### **Disclaimer of Opinion**

We were engaged to audit the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

We do not express an opinion on the accompanying financial statements of the Company. Because of the significance of the matters described in the *Basis for Disclaimer of Opinion* section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

#### **Basis for Disclaimer of Opinion**

We were not appointed as auditors of the Company until after December 31, 20X1 and thus did not observe the counting of physical inventories at the beginning and end of the year. We were unable to satisfy ourselves by alternative means concerning the inventory quantities held at December 31, 20X0 and 20X1, which are stated in the statements of financial position at xxx and xxx, respectively. In addition, the introduction of a new computerised accounts receivable system in September 20X1 resulted in numerous errors in accounts receivable. As of the date of our report, management was still in the process of rectifying the system deficiencies and correcting the errors. We were unable to confirm or verify by alternative means accounts receivable included in the statement of financial position at a total amount of xxx as at December 31, 20X1. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of

<sup>26</sup> — For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

<sup>27</sup> — The sub title "Report on the Audit of the Financial Statements" is unnecessary in circumstances when the second sub title "Report on Other Legal and Regulatory Requirements" is not applicable.



~~recorded or unrecorded inventories and accounts receivable, and the elements making up the statement of comprehensive income, statement of changes in equity and statement of cash flows.~~

### **Directors' Responsibilities for the Financial Statements<sup>28</sup>**

~~[Reporting in accordance with ISA (NZ) 700 (Revised) — see Illustration 1 in ISA (NZ) 700 (Revised).]~~

### **Auditor's Responsibilities for the Audit of the Financial Statements**

~~Our responsibility is to conduct an audit of the Company's financial statements in accordance with International Standards on Auditing (New Zealand) and to issue an auditor's report. However, because of the matters described in the *Basis for Disclaimer of Opinion* section of our report, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.~~

~~We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the Company.~~

### **Report on Other Legal and Regulatory Requirements**

~~[Reporting in accordance with ISA (NZ) 700 (Revised) — see Illustration 1 in ISA (NZ) 700 (Revised).]~~

~~[Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate]~~

~~[Auditor Address]~~

~~[Date]~~

## **B.5 ISA (NZ) 720 The Auditor's Responsibilities Relating to Other Information**

~~Amend Appendix 2, [NZ] Illustration 1 through [NZ] Illustration 7 to reflect changes to the wording in the auditor's report as required by ISA (NZ) 700 (Revised).~~

### **Appendix 2**

(Ref: Para. 21–22, A53)

### **Illustrations of Auditor's Reports Relating to Other Information**

- ~~• [NZ] Illustration 1: An auditor's report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an unmodified opinion when the auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information.~~

<sup>28</sup>—Or other terms that are appropriate in the context of the legal framework of the entity

- ~~[NZ] Illustration 2: An auditor's report of a FMC reporting entity considered to have a higher level of public accountability containing an unmodified opinion when the auditor has obtained part of the other information prior to the date of the auditor's report, has not identified a material misstatement of the other information, and expects to obtain other information after the date of the auditor's report.~~
- ~~[NZ] Illustration 3: An auditor's report of an entity other than a FMC reporting entity considered to have a higher level of public accountability containing an unmodified opinion when the auditor has obtained part of the other information prior to the date of the auditor's report, has not identified a material misstatement of the other information, and expects to obtain other information after the date of the auditor's report.~~
- ~~[NZ] Illustration 4: An auditor's report of a FMC reporting entity considered to have a higher level of public accountability containing an unmodified opinion when the auditor has obtained no other information prior to the date of the auditor's report but expects to obtain other information after the date of the auditor's report.~~
- ~~[NZ] Illustration 5: An auditor's report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an unmodified opinion when the auditor has obtained all of the other information prior to the date of the auditor's report and has concluded that a material misstatement of the other information exists.~~
- ~~[NZ] Illustration 6: An auditor's report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing a qualified opinion when the auditor has obtained all of the other information prior to the date of the auditor's report and there is a limitation of scope with respect to a material item in the consolidated financial statements which also affects the other information.~~
- ~~[NZ] Illustration 7: An auditor's report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an adverse opinion when the auditor has obtained all of the other information prior to the date of the auditor's report and the adverse opinion on the consolidated financial statements also affects the other information.~~

~~[NZ] Illustration 1 — An auditor's report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an unmodified opinion when the auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information.~~

~~For purposes of this illustrative auditor's report, the following circumstances are assumed:~~

- ~~Audit of a complete set of financial statements of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600<sup>29</sup> does not apply).~~
- ~~The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~

<sup>29</sup>—ISA (NZ) 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

- ~~The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.~~<sup>30</sup>
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~<sup>31</sup>
- ~~Key audit matters have been communicated in accordance with ISA (NZ) 701.~~<sup>32</sup>
- ~~The auditor has obtained all of the other information prior to the date of the auditor’s report and has not identified a material misstatement of the other information.~~
- ~~In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.~~

## **~~INDEPENDENT AUDITOR’S REPORT~~**

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

### **~~Report on the Audit of the Financial Statements~~**<sup>33</sup>

#### **~~Opinion~~**

~~We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.~~

~~In our opinion, the accompanying financial statements present fairly, in all material respects, (or *give a true and fair view of*) the financial position of the Company as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).~~

#### **~~Basis for Opinion~~**

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that~~

<sup>30</sup> ~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

<sup>31</sup> ~~ISA (NZ) 570 (Revised), *Going Concern*~~

<sup>32</sup> ~~ISA (NZ) 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*. The Key Audit Matters section is required for FMC reporting entities considered to have a higher level of public accountability only.~~

<sup>33</sup> ~~The sub title “Report on the Audit of the Financial Statements” is unnecessary in circumstances when the second sub title “Report on Other Legal and Regulatory Requirements” is not applicable.~~

~~the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.  
Other than in our capacity as auditor we have no relationship with, or interests in, the Company.  
...~~

DRAFT

~~[NZ] Illustration 2 — An auditor’s report of a FMC reporting entity considered to have a higher level of public accountability containing an unmodified opinion when the auditor has obtained part of the other information prior to the date of the auditor’s report, has not identified a material misstatement of the other information, and expects to obtain other information after the date of the auditor’s report.~~

~~For purposes of this illustrative auditor’s report, the following circumstances are assumed:~~

- ~~• — Audit of a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~• — The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~• — The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~• — The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~• — The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>34</sup>~~
- ~~• — Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• — Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~• — The auditor has obtained part of the other information prior to the date of the auditor’s report, has not identified a material misstatement of the other information, and expects to obtain other information after the date of the auditor’s report.~~
- ~~• — In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.~~

## ~~INDEPENDENT AUDITOR’S REPORT~~

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

### ~~Report on the Audit of the Financial Statements<sup>35</sup>~~

#### ~~Opinion~~

~~We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.~~

~~In our opinion, the accompanying financial statements present fairly, in all material respects, (or give a~~

<sup>34</sup> — ~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

<sup>35</sup> — ~~The sub title “Report on the Audit of the Financial Statements” is unnecessary in circumstances when the second sub title “Report on Other Legal and Regulatory Requirements” is not applicable.~~

*true and fair view of* the financial position of the Company as at December 31, 20X1, and *(of)* its financial performance and its cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

[NZ] Illustration 3—An auditor's report of an entity other than a FMC reporting entity considered to have a higher level of public accountability containing an unmodified opinion when the auditor has obtained part of the other information prior to the date of the auditor's report, has not identified a material misstatement of the other information, and expects to obtain other information after the date of the auditor's report.

For purposes of this illustrative auditor's report, the following circumstances are assumed:

Audit of a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).

The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).

The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.

The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.

The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>36</sup>

Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).

<sup>36</sup>—For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

~~The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701.~~

~~The auditor has obtained part of the other information prior to the date of the auditor's report, has not identified a material misstatement of the other information, and expects to obtain other information after the date of the auditor's report.~~

~~The auditor has no other reporting responsibilities required under law or regulation.~~

## **INDEPENDENT AUDITOR'S REPORT**

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

### **Opinion**

~~We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.~~

~~In our opinion, the accompanying financial statements present fairly, in all material respects, (or *give a true and fair view of*) the financial position of the Company as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ-IFRS).~~

### **Basis for Opinion**

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners*, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the Company.~~

~~...~~



~~[NZ] Illustration 4—An auditor’s report of a FMC reporting entity considered to have a higher level of public accountability containing an unmodified opinion when the auditor has obtained no other information prior to the date of the auditor’s report but expects to obtain other information after the date of the auditor’s report.~~

~~For purposes of this illustrative auditor’s report, the following circumstances are assumed:~~

- ~~• Audit of a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~• The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~• The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>37</sup>.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~• The auditor has obtained no other information prior to the date of the auditor’s report but expects to obtain other information after the date of the auditor’s report.~~
- ~~• In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under local law.~~

## **INDEPENDENT AUDITOR’S REPORT**

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

### **Report on the Audit of the Financial Statements<sup>38</sup>**

#### **Opinion**

~~We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.~~

~~In our opinion, the accompanying financial statements present fairly, in all material respects, (or give a true and fair view of) the financial position of the Company as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with New Zealand~~

<sup>37</sup>—~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

<sup>38</sup>—~~The sub title “Report on the Audit of the Financial Statements” is unnecessary in circumstances when the second sub title “Report on Other Legal and Regulatory Requirements” is not applicable.~~



equivalents to International Financial Reporting Standards (NZ-IFRS).

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners*, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

~~[NZ] Illustration 5—An auditor’s report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an unmodified opinion when the auditor has obtained all of the other information prior to the date of the auditor’s report and has concluded that a material misstatement of the other information exists.~~

~~For purposes of this illustrative auditor’s report, the following circumstances are assumed:~~

- ~~• Audit of a complete set of financial statements of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, using a fair presentation framework. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~• The financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~• The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards (New Zealand))* and any other ethical provisions that apply to these circumstances.<sup>39</sup>.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~• The auditor has obtained all of the other information prior to the date of the auditor’s report and has concluded that a material misstatement of the other information exists~~
- ~~• The auditor has no other reporting responsibilities required under law or regulation.~~

## **INDEPENDENT AUDITOR’S REPORT**

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

### **Opinion**

We have audited the financial statements of ABC Company (the Company), which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, (or *give a true and fair view of*) the financial position of the Company as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).

<sup>39</sup>—~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

...

~~[NZ] Illustration 6—An auditor’s report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an qualified opinion when the auditor has obtained all of the other information prior to the date of the auditor’s report and there is a limitation of scope with respect to a material item in the consolidated financial statements which also affects the other information.~~

~~For purposes of this illustrative auditor’s report, the following circumstances are assumed:~~

- ~~• Audit of a complete set of consolidated financial statements of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, using a fair presentation framework. The audit is a group audit (i.e., ISA (NZ) 600 applies).~~
- ~~• The consolidated financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the consolidated financial statements in ISA (NZ) 210.~~
- ~~• The auditor was unable to obtain sufficient appropriate audit evidence regarding an investment in a foreign associate. The possible effects of the inability to obtain sufficient appropriate audit evidence are deemed to be material but not pervasive to the consolidated financial statements (i.e., a qualified opinion is appropriate).~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>40</sup>.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~• The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the qualified opinion on the consolidated financial statements also affects the other information.~~
- ~~• The auditor has no other reporting responsibilities required under law or regulation.~~

## **INDEPENDENT AUDITOR’S REPORT**

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

### **Qualified Opinion**

~~We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.~~

<sup>40</sup> ~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

In our opinion, except for the possible effects of the matter described in the *Basis for Qualified Opinion* section of our report, the accompanying consolidated financial statements present fairly, in all material respects, (or *give a true and fair view of*) the financial position of the Group as at December 31, 20X1, and (of) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ-IFRS).

#### **Basis for Qualified Opinion**

The Group's investment in XYZ Company, a foreign associate acquired during the year and accounted for by the equity method, is carried at xxx on the consolidated statement of financial position as at December 31, 20X1, and ABC's share of XYZ's net income of xxx is included in ABC's income for the year then ended. We were unable to obtain sufficient appropriate audit evidence about the carrying amount of ABC's investment in XYZ as at December 31, 20X1 and ABC's share of XYZ's net income for the year because we were denied access to the financial information, management, and the auditors of XYZ. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the group financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company or any of its subsidiaries.

...

~~[NZ] Illustration 7—An auditor’s report of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, containing an adverse opinion when the auditor has obtained all of the other information prior to the date of the auditor’s report and the adverse opinion on the consolidated financial statements also affects the other information.~~

~~For purposes of this illustrative auditor’s report, the following circumstances are assumed:~~

- ~~• Audit of a complete set of consolidated financial statements of any entity, whether a FMC reporting entity considered to have a higher level of public accountability or not, using a fair presentation framework. The audit is a group audit (i.e., ISA (NZ) 600 applies).~~
- ~~• The consolidated financial statements are prepared by management of the entity in accordance with NZ IFRS (a general purpose framework).~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the consolidated financial statements in ISA (NZ) 210.~~
- ~~• The consolidated financial statements are materially misstated due to the non-consolidation of a subsidiary. The material misstatement is deemed to be pervasive to the consolidated financial statements. The effects of the misstatement on the consolidated financial statements have not been determined because it was not practicable to do so (i.e., an adverse opinion is appropriate).~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>41</sup>.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• Key audit matters have been communicated in accordance with ISA (NZ) 701.~~
- ~~• The auditor has obtained all of the other information prior to the date of the auditor’s report and the matter giving rise to the adverse opinion on the consolidated financial statements also affects the other information.~~
- ~~• The auditor has no other reporting responsibilities required under law or regulation.~~

## **INDEPENDENT AUDITOR’S REPORT**

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

### **Adverse Opinion**

~~We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.~~

<sup>41</sup>—~~For example, the New Zealand Institute of Chartered Accountants “Code of Ethics” including Part 2, *Members in Business*~~

In our opinion, because of the significance of the matter discussed in the *Basis for Adverse Opinion* section of our report, the accompanying consolidated financial statements do not present fairly (or do not give a true and fair view of) the consolidated financial position of the Group as at December 31, 20X1, and (of) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).

### **Basis for Adverse Opinion**

As explained in Note X, the Group has not consolidated subsidiary XYZ Company that the Group acquired during 20X1 because it has not yet been able to determine the fair values of certain of the subsidiary's material assets and liabilities at the acquisition date. This investment is therefore accounted for on a cost basis. Under NZ IFRS, the Group should have consolidated this subsidiary and accounted for the acquisition based on provisional amounts. Had XYZ Company been consolidated, many elements in the accompanying consolidated financial statements would have been materially affected. The effects on the consolidated financial statements of the failure to consolidate have not been determined.

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in New Zealand[jurisdiction], and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our adverse opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company or any of its subsidiaries.

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## **~~B.6 ISA (NZ) 800 Special Considerations—Audits of Financial Statements Prepared Accordance with Special Purpose Frameworks~~**

Amend Appendix 1, [NZ] Illustration 1 through [NZ] Illustration 3 to reflect changes to the wording in the auditor's report as required by ISA (NZ) 700 (Revised).

**Appendix 1**  
(Ref: Para. A14)

### **~~Illustrations of Independent Auditor's Reports on Special Purpose Financial Statements~~**

- ~~• [NZ] Illustration 1: An auditor's report on a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with the financial reporting provisions of a contract (for purposes of this illustration, a compliance framework).~~
- ~~• [NZ] Illustration 2: An auditor's report on a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with the tax basis of accounting (for purposes of this illustration, a compliance framework).~~
- ~~• [NZ] Illustration 3: An auditor's report on a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with the financial reporting provisions established by a regulator (for purposes of this illustration, a fair presentation framework).~~



[NZ] Illustration 1: An auditor's report on a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with the financial reporting provisions of a contract (for purposes of this illustration, a compliance framework).

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- The financial statements have been prepared by management of the entity in accordance with the financial reporting provisions of a contract (that is, a special purpose framework). Management does not have a choice of financial reporting frameworks.
- The applicable financial reporting framework is a compliance framework.
- An auditor's report on the complete set of general purpose financial statements was not issued.
- The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.
- The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.
- The relevant ethical requirements that apply to the audit comprise of Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>42</sup> issued by the New Zealand Auditing and Assurance Standards Board.
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).
- Distribution and use of the auditor's report are restricted.
- The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701.
- The auditor has determined that there is no other information (i.e., the requirements of ISA (NZ) 720 (Revised) do not apply).
- The auditor has no other reporting responsibilities required under local law or regulation.

## INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

### Opinion

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

In our opinion, the accompanying financial statements of the Company for the year ended December 31, 20X1 are prepared, in all material respects, in accordance with the financial reporting provisions of Section Z of the contract dated January 1, 20X1 between the Company and

<sup>42</sup> For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

DEF Company (“the contract”). [Opinion section positioned first as required in ISA (NZ) 700 (Revised)]

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. [The first and last sentences in this section used to be in the Auditor’s Responsibility section. Also, the Basis for Opinion section is positioned immediately after the Opinion section as required in ISA (NZ) 700 (Revised).]

Other than in our capacity as auditor we have no relationship with, or interests in, the Company.

...

~~[NZ] Illustration 2: An auditor's report on a complete set of financial statements of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with the tax basis of accounting in New Zealand (for purposes of this illustration, a compliance framework).~~

~~For purposes of this illustrative auditor's report, the following circumstances are assumed:~~

- ~~• Audit of a complete set of financial statements that have been prepared by management of a partnership in accordance with the tax basis of accounting in New Zealand (that is, a special purpose framework) to assist the partners in preparing their individual income tax returns. Management does not have a choice of financial reporting frameworks.~~
- ~~• The applicable financial reporting framework is a compliance framework.~~
- ~~• The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.~~
- ~~• The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.~~
- ~~• The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>43</sup>.~~
- ~~• Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~• Distribution of the auditor's report is restricted.~~
- ~~• The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701.~~
- ~~• The auditor has determined that there is no other information (i.e., the requirements of ISA (NZ) 720 (Revised) do not apply).~~
- ~~• The auditor has no other reporting responsibilities required under local law or regulation.~~

## **INDEPENDENT AUDITOR'S REPORT**

~~[Appropriate Addressee]~~

### **Opinion**

~~We have audited the financial statements of ABC Partnership (the Partnership), which comprise the balance sheet as at December 31, 20X1 and the income statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.~~

~~In our opinion, the accompanying financial statements of the Partnership for the year ended December 31, 20X1 are prepared, in all material respects, in accordance with [describe the~~

<sup>43</sup> ~~For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*~~

*applicable income tax law*] of New Zealand. [Opinion section positioned first as required in ISA (NZ) 700 (Revised)]

### **Basis for Opinion**

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Partnership in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. [The first and last sentences in this section used to be in the Auditor's Responsibility section. Also, the Basis for Opinion section is positioned immediately after the Opinion section as required in ISA (NZ) 700 (Revised).]~~

Other than in our capacity as auditor we have no relationship with, or interests in, the Partnership.

...

[NZ] Illustration 3: An auditor's report on a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with the financial reporting provisions established by a regulator (for purposes of this illustration, a fair presentation framework).

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- Audit of a complete set of financial statements of a FMC reporting entity considered to have a higher level of public accountability that have been prepared by management of the entity in accordance with the financial reporting provisions established by a regulator (that is, a special purpose framework) to meet the requirements of that regulator. Management does not have a choice of financial reporting frameworks.
- The applicable financial reporting framework is a fair presentation framework.
- The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.
- The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.
- The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>44</sup>
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised). The disclosure of the material uncertainty in the financial statements is adequate.
- Distribution or use of the auditor's report is not restricted.
- The auditor is required by the regulator to communicate key audit matters in accordance with ISA (NZ) 701.
- The auditor has determined that there is no other information (i.e., the requirements of ISA (NZ) 720 (Revised) do not apply).
- The auditor has no other reporting responsibilities required under local law or regulation.

## **INDEPENDENT AUDITOR'S REPORT**

To the Shareholders of ABC Company [or Appropriate Addressee]

### **Opinion**

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

In our opinion, the accompanying financial statements present fairly, in all material respects, (or give a true and fair view of) the financial position of the Company as at December 31, 20X1, and

<sup>44</sup> For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

~~(of) its financial performance and its cash flows for the year then ended in accordance with the financial reporting provisions of Section Y of Regulation Z. [Opinion section positioned first as required in ISA (NZ) 700 (Revised)]~~

### **~~Basis for Opinion~~**

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. [The first and last sentences in this section used to be in the Auditor's Responsibility section. Also, the Basis for Opinion section is positioned immediately after the Opinion section as required in ISA (NZ) 700 (Revised).]~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the Company.~~

~~...~~

## **~~B.7 ISA (NZ) 805 Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement~~**

~~Amend Appendix 2, [NZ] Illustration 1 through [NZ] Illustration 3 to reflect to reflect changes to the wording in the auditor's report as required by ISA (NZ) 700 (Revised).~~

### **~~Appendix 2 (Ref: Para. A16)~~**

## **~~Illustrations of Independent Auditor's Reports on a Single Financial Statement and on a Specific Element of a Financial Statement~~**

- ~~• [NZ] Illustration 1: An auditor's report on a single financial statement of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with a general purpose framework (for purposes of this illustration, a fair presentation framework).~~
- ~~• [NZ] Illustration 2: An auditor's report on a single financial statement of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with a special purpose framework (for purposes of this illustration, a fair presentation framework).~~
- ~~• [NZ] Illustration 3: An auditor's report on a specific element of a financial statement of a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with a special purpose framework (for purposes of this illustration, a compliance framework).~~

[NZ] Illustration 1: An auditor's report on a single financial statement of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with a general purpose framework (for purposes of this illustration, a fair presentation framework)

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- Audit of a balance sheet (that is, a single financial statement) of an entity other than a FMC reporting entity considered to have a higher level of public accountability.
- The balance sheet has been prepared by management of the entity in accordance with the requirements of the applicable financial reporting framework issued by the New Zealand Accounting Standards Board relevant to preparing a balance sheet.
- The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.
- The applicable financial reporting framework is a fair presentation framework designed to meet the common financial information needs of a wide range of users.
- The auditor has determined that it is appropriate to use the phrase "presents fairly, in all material respects," in the auditor's opinion.
- The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand) and any other ethical provisions that apply to these circumstances.<sup>45</sup>
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised). The disclosure of the material uncertainty in the single financial statement is adequate.
- The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701 in the context of the audit of the balance sheet.
- The auditor has determined that there is no other information (i.e., the requirements of ISA (NZ) 720 (Revised) do not apply).
- The auditor has no other reporting responsibilities required under local law or regulation.

## INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

### Opinion

We have audited the balance sheet of ABC Company (the Company) as at December 31, 20X1 and notes to the financial statement, including a summary of significant accounting policies (together "the financial statement").

In our opinion, the accompanying financial statement presents fairly, in all material respects, the financial position of the Company as at December 31, 20X1 in accordance with those requirements of the [applicable financial reporting framework issued by the New Zealand

<sup>45</sup> For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*



Accounting Standards Board] relevant to preparing such a financial statement. [Opinion section positioned first as required in ISA (NZ) 700 (Revised)]

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statement* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. [The first and last sentences in this section used to be in the Auditor's Responsibility section. Also, the Basis for Opinion section is positioned immediately after the Opinion section as required in ISA (NZ) 700 (Revised).]

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company.

...

[NZ] Illustration 2: An auditor's report on a single financial statement of an entity other than a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with a special purpose framework.

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- Audit of a statement of cash receipts and disbursements (that is, a single financial statement) of an entity other than a FMC reporting entity considered to have a higher level of public accountability.
- An auditor's report on the complete set of financial statements was not issued.
- The financial statement has been prepared by management of the entity in accordance with the cash receipts and disbursements basis of accounting to respond to a request for cash flow information received from a creditor. Management has a choice of financial reporting frameworks.
- The applicable financial reporting framework is a fair presentation framework designed to meet the financial information needs of specific users.<sup>46</sup>
- The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.
- The auditor has determined that it is appropriate to use the phrase "presents fairly, in all material respects," in the auditor's opinion.
- The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>47</sup> comprises all of the relevant ethical requirements that apply to the audit.
- Distribution or use of the auditor's report is not restricted.
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).
- The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701 in the context of the audit of the statement of cash receipts and disbursements.
- The auditor has determined that there is no other information (i.e., the requirements of ISA (NZ) 720 (Revised) do not apply).
- The auditor has no other reporting responsibilities required under local law or regulation.

## INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

### Opinion

<sup>46</sup> ISA (NZ) 800 (Revised) contains requirements and guidance on the form and content of financial statements prepared in accordance with a special purpose framework.

<sup>47</sup> For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*

We have audited the statement of cash receipts and disbursements of ABC Company (the Company) for the year ended December 31, 20X1 and notes to the statement of cash receipts and disbursements, including a summary of significant accounting policies (together “the financial statement”).

In our opinion, the accompanying financial statement presents fairly, in all material respects, the cash receipts and disbursements of the Company for the year ended December 31, 20X1 in accordance with the cash receipts and disbursements basis of accounting described in Note X. [Opinion section positioned first as required in ISA (NZ) 700 (Revised)]

### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statement* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. [The first and last sentences in this section used to be in the Auditor’s Responsibility section. Also, the Basis for Opinion section is positioned immediately after the Opinion section as required in ISA (NZ) 700 (Revised).]

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Company.

[NZ] Illustration 3: An auditor’s report on a specific element of a financial statement of a FMC reporting entity considered to have a higher level of public accountability prepared in accordance with a special purpose framework.

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

Audit of an accounts receivable schedule (that is, element, account or item of a financial statement).

The financial information has been prepared by management of the entity in accordance with the financial reporting provisions established by a regulator to meet the requirements of that regulator. Management does not have a choice of financial reporting frameworks.

The applicable financial reporting framework is a compliance framework designed to meet the financial information needs of specific users.<sup>48</sup>

The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the financial statements in ISA (NZ) 210.

The auditor has concluded an unmodified (i.e., “clean”) opinion is appropriate based on the audit evidence obtained.

<sup>48</sup> ISA (NZ) 800 (Revised) contains requirements and guidance on the form and content of financial statements prepared in accordance with a special purpose framework.

~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>49</sup> comprises all of the relevant ethical requirements that apply to the audit.~~

~~Distribution of the auditor's report is restricted.~~

~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~

~~The auditor is not required, and has otherwise not decided to communicate key audit matters in accordance with ISA (NZ) 701 in the context of the audit of the accounts receivable schedule.~~

~~The auditor has determined that there is no other information (i.e., the requirements of ISA (NZ) 720 (Revised) do not apply).~~

~~The auditor has no other reporting responsibilities required under local law or regulation.~~

## INDEPENDENT AUDITOR'S REPORT

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

### Opinion

~~We have audited the accounts receivable schedule of ABC Company (the Company) as at December 31, 20X1 ("the schedule").~~

~~In our opinion, the financial information in the schedule of the Company as at December 31, 20X1 is prepared, in all material respects, in accordance with [describe the financial reporting provisions established by the regulator]. [Opinion section positioned first as required ISA (NZ) 700 (Revised)]~~

### Basis for Opinion

~~We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Schedule* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial Statements in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. [The first and last sentences in this section used to be in the Auditor's Responsibility section. Also, the Basis for Opinion section is positioned immediately after opinion section as required in ISA (NZ) 700 (Revised).]~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the Company.~~

~~...~~

<sup>49</sup> ~~For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*~~

## C: Proposed Amendments to domestic standards

### C.1: External Reporting Board Standard Au1 *Application of Auditing and Assurance Standards*

Amend Appendix 1 to update the title of PES 1.

## Appendix 1

### Professional and Ethical Standards

*This appendix is an integral part of the Standard.*

This appendix lists the Professional and Ethical Standards to be applied in preparing for and conducting all assurance engagements.

- |                              |  |
|------------------------------|--|
| PES 1 ( <del>Revised</del> ) | <u>International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)</u> |
| PES 3 (Amended)              | Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements             |

### C.2 New Zealand Auditing Standard 1 *The Audit of Service Performance Information*

Add a footnote to paragraph A18(a) to include the title of Professional and Ethical Standard 1. ~~The illustrative auditor's reports in Appendix 6 and Appendix 7 are amended to reflect changes to the wording in the auditor's report as required by ISA (NZ) 700 (Revised).~~

- A18 The service performance information may include information upon which another practitioner may have expressed an opinion. The auditor may decide to use the evidence on which that other practitioner's opinion is based to provide evidence regarding the service performance information included in the general purpose financial report. The work of another practitioner may be used in relation to service performance information that falls outside the boundary of the reporting entity. Such practitioners are not part of the engagement team. Relevant considerations when the engagement team plans to use the work of another auditor may include:
- (a) Whether the auditor understands and complies with the requirements of Professional and Ethical Standard 1<sup>50</sup>.
  - (b) The other practitioner's professional competence.
  - (c) The extent of the engagement teams' involvement in the work of the other practitioner.

<sup>50</sup> Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*

**Illustrative Auditor's Report Including Service Performance Information**

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- ~~Audit of a general purpose financial report/performance report of a public benefit entity that is not a FMC reporting entity considered to have a higher level of public accountability using a fair presentation framework<sup>51</sup>. The audit is not a group audit (i.e., ISA (NZ) 600 does not apply).~~
- ~~The general purpose financial report/performance report is prepared by management of the entity in accordance with a general purpose framework.~~
- ~~The terms of the audit engagement reflect the description of the responsibilities of those charged with governance for the general purpose financial report/performance report in ISA (NZ) 210.~~
- ~~The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.~~
- ~~The relevant ethical requirements that apply to the audit comprise Professional and Ethical Standard 1 (Revised) *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* and any other ethical provisions that apply to these circumstances.<sup>52</sup> comprises all of the relevant ethical requirements that apply to the audit.~~
- ~~Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA (NZ) 570 (Revised).~~
- ~~The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA (NZ) 701.~~
- ~~The auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information.~~
- ~~The auditor has no other reporting responsibilities required under local law.~~

**INDEPENDENT AUDITOR'S REPORT**

To Appropriate Addressee

**Opinion**

We have audited the *[general purpose financial report/performance report]* of ABC *[entity]*, which comprise the financial statements on pages *x to xx*, the *[service performance information/statement*

<sup>51</sup>—The general purpose financial report may be referred to as a performance report and include entity information, according to the requirements of the applicable financial reporting framework.

<sup>52</sup>—For example, the New Zealand Institute of Chartered Accountants "Code of Ethics" including Part 2, *Members in Business*



~~of service performance] on pages x to xx [and the entity information on page x]. The complete set of financial statements comprise the statement of financial position as at December 31, 20X1, the [statement of financial performance/statement of comprehensive revenue and expense, statement of changes in net assets/equity], statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.~~

~~In our opinion the accompanying [general purpose financial report/performance report] presents fairly, in all material respects, (or gives a true and fair view of):~~

- ~~• [the entity information as at December 31, 20X1];~~
- ~~• the financial position of the [entity] as at December 31, 20X1, and (of) its financial performance, and its cash flows for the year then ended; and~~
- ~~• the service performance for the year ended December 31, 20X1 in accordance with the entity's service performance criteria~~

~~in accordance with [Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)] issued by the New Zealand Accounting Standards Board.~~

~~[For a long form report, include a separate section, under an appropriate heading, for example:~~

- ~~• Underlying facts and information about the entity's process to select what service performance to report on (e.g., the maturity of the entity's process compared to others in the industry).~~
- ~~• The source of the service performance criteria, and whether they are externally established. (e.g., established in section xxx of applicable legislation or externally established performance frameworks).~~
- ~~• Any significant interpretations made in selecting or applying the entity's service performance criteria in the circumstances.~~
- ~~• Whether there have been any changes in the service performance criteria (e.g., changes in the performance measures used).~~
- ~~• Findings or recommendations for improvements to the service performance information.~~
- ~~• Any other matters the auditor considers necessary to assist intended users in making decisions based on the service performance information.]~~

### **Basis for Opinion**

~~We conducted our audit of the [financial statements] in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and the audit of the service performance information in accordance with the ISAs and New Zealand Auditing Standard (NZ AS) 1 *The Audit of Service Performance Information* (NZ). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the [General Purpose Financial Report/Performance Report]* section of our report. We are independent of the [entity] in accordance with the ethical requirements that are relevant to our audit of the [general purpose financial report/performance report/financial statements] in New Zealand, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the [entity].~~

~~...~~

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**Illustrations of Auditor's Reports with Modifications to the Opinion with Respect to the Service Performance Information**

- Illustration 1: An auditor's report containing an unmodified opinion on the financial statements and a qualified opinion due to a material misstatement of the service performance information.
- Illustration 2: An auditor's report containing an unmodified opinion on the financial statements and an adverse opinion due to a material misstatement of the service performance information.
- Illustration 3: An auditor's report containing an unmodified opinion on the financial statements and a qualified opinion due to the auditor's inability to obtain sufficient appropriate audit evidence about a single element of the service performance information.
- Illustration 4: An auditor's report containing a qualified opinion on both the financial statements and the service performance information due to the auditor's inability to obtain sufficient appropriate audit evidence about a single element of the financial statements.

Illustration 1: An auditor's report containing an unmodified opinion on the financial statements and a qualified opinion due to a material misstatement of the service performance information

## **INDEPENDENT AUDITOR'S REPORT**

To [Appropriate Addressee]

### **Opinions**

We have audited the ~~[general purpose financial report/performance report]~~ of ABC [entity], which comprise the financial statements on pages ~~x to xx~~, the ~~[service performance information/statement of service performance]~~ on pages ~~x to xx~~ ~~[and the entity information on page x]~~. The complete set of financial statements comprise the statement of financial position as at December 31, 20X1, the ~~[statement of financial performance/statement of comprehensive revenue and expense, statement of changes in net assets/equity]~~, statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

#### *Opinion on the [Entity Information and] Financial Statements*

In our opinion, the accompanying ~~[general purpose financial report/performance report]~~ presents fairly, in all material respects, (or gives a true and fair view of) the ~~[entity information and the]~~ financial position of the [entity] as at December 31, 20X1, and (of) its, financial performance and its cash flows for the year then ended in accordance with ~~[Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)]~~ issued by the New Zealand Accounting Standards Board.

#### *Qualified Opinion on the Service Performance Information*

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion on the Service Performance Information* section of our report the accompanying ~~[general purpose financial report/performance report]~~ presents fairly, in all material respects (or gives a true and fair view of) the service performance of the [entity] for the year ended December 31, 20X1 in accordance with the entity's service performance criteria and with ~~[Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)]~~ issued by the New Zealand Accounting Standards Board.

### **Basis for Qualified Opinion on the Service Performance Information**

~~[As reported in the service performance information on page xx, the entity has identified its service performance as [describe improvements reported or description of the difference that the entity has made] and measured this performance by [list performance measures and/or descriptions reported] to report its service performance. The entity has not been able to provide evidence of its role in those particular improvements and therefore should not have reported this improvement.]~~

We conducted our audit of the ~~[financial statements]~~ in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and the audit of the service performance information in accordance with the ISAs (NZ) and New Zealand Auditing Standard 1 *The Audit of Service Performance Information*. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the [General Purpose Financial Report/Performance Report]* section of our report. We are independent of the [entity] in accordance with the ethical requirements that

~~are relevant to our audit of the [General Purpose Financial Report/Performance Report] in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the [entity].~~

~~...~~

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Illustration 2: An auditor's report containing an unmodified opinion on the financial statements and an adverse opinion due to a material misstatement of the service performance information

## **INDEPENDENT AUDITOR'S REPORT**

To [Appropriate Addressee]

### **Opinions**

We have audited the ~~[general purpose financial report/performance report]~~ of ABC [entity], which comprise the financial statements on pages *x to xx*, the ~~[service performance information/statement of service performance]~~ on pages *x to xx* ~~[and the entity information on page *x*]~~. The complete set of financial statements comprise the statement of financial position as at December 31, 20X1, the ~~[statement of financial performance/statement of comprehensive revenue and expense, statement of changes in net assets/equity]~~, statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

#### *Opinion on the [Entity Information and] Financial Statements*

In our opinion, the accompanying ~~[general purpose financial report/performance report]~~ presents fairly, in all material respects, (or *gives a true and fair view of*) the ~~[entity information and the]~~ financial position of the [entity] as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with ~~[Public Benefit Entity Standards Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)]~~ issued by the New Zealand Accounting Standards Board.

#### *Adverse Opinion on the Service Performance Information*

In our opinion, because of the significance of the matter discussed in the *Basis for Adverse Opinion on the Service Performance Information* section of our report the accompanying ~~[general purpose financial report/performance report]~~ does not present fairly (or *does not give a true and fair view of*) the service performance of the [entity] ~~[on pages *x to xx*]~~ for the year ended December 31, 20X1 in accordance with the entity's service performance criteria and with ~~[Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)]~~ issued by the New Zealand Accounting Standards Board.

### **Basis for Adverse Opinion on the Service Performance Information**

~~[As reported in the service performance information on pages ..., the entity has identified its service performance to include [list appropriate goods and services] and measured and evaluated this performance with reference to [describe performance measures and/or descriptions reported] to report its service performance. We do not consider that these performance measures will enable a meaningful assessment of the service performance of the entity for the year ended December 31, 20X1 to be made. Had the entity identified more meaningful performance measures, the service performance information would have been materially affected, reporting performance measures including xxx and linking to its responsibility for yyyy.]~~

We conducted our audit of the ~~[financial statements]~~ in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and the audit of the service performance information in accordance with the ISAs (NZ) and New Zealand Auditing Standard 1 *The Audit of Service Performance Information*. Our responsibilities under those standards are further described in the

*Auditor's Responsibilities for the Audit of the [General Purpose Financial Report/Performance Report]* section of our report. We are independent of the [entity] in accordance with the ethical requirements that are relevant to our audit of the [General Purpose Financial Report/Performance Report] in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, the [entity].

...

Illustration 3: An auditor's report containing an unmodified opinion on the financial statements and a qualified opinion due to the auditor's inability to obtain sufficient appropriate audit evidence about a single element of the service performance information

## **INDEPENDENT AUDITOR'S REPORT**

To [Appropriate Addressee]

### **Opinions**

We have audited the ~~[general purpose financial report/performance report]~~ of ABC [entity], which comprise the financial statements on pages *x to xx*, the ~~[service performance information/statement of service performance]~~ on pages *x to xx* ~~[and the entity information on page *x*]~~. The complete set of financial statements comprise the statement of financial position as at December 31, 20X1, the ~~[statement of financial performance/statement of comprehensive revenue and expense, statement of changes in net assets/equity]~~, statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

#### *Opinion on the [Entity Information and] Financial Statements*

In our opinion, the accompanying ~~[general purpose financial report/performance report]~~ presents fairly, in all material respects, ~~(or gives a true and fair view of)~~ the ~~[entity information and the]~~ financial position of the [entity] as at December 31, 20X1, and ~~(of)~~ its financial performance and its cash flows for the year then ended in accordance with ~~[Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)]~~ issued by the New Zealand Accounting Standards Board.

#### *Qualified Opinion on the Service Performance Information*

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion on the Service Performance Information* section of our report the accompanying ~~[general purpose financial report/performance report]~~ presents fairly, in all material respects ~~(or gives a true and fair view of)~~ the service performance of the [entity] for the year ended December 31, 20X1 in accordance with the entity's service performance criteria and with ~~[Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)]~~ issued by the New Zealand Accounting Standards Board.

### **Basis for Qualified Opinion on the Service Performance Information**

~~[Some significant performance measures of the entity, rely on information from third parties, such as (give examples). The entity's control over much of this information is limited, and there are no practical audit procedures to determine the effect of this limited control. For example, [describe performance measure and explain where information comes from that we are unable to independently test.]]~~

We conducted our audit of the ~~[financial statements]~~ in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and the audit of the service performance information in accordance with the ISAs (NZ) and New Zealand Auditing Standard 1 *The Audit of Service Performance Information*. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the [General Purpose Financial Report/Performance Report]* section of our report. We are independent of the [entity] in accordance with the ethical requirements that

~~are relevant to our audit of the [General Purpose Financial Report/Performance Report] in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the [entity].~~

~~...~~

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Illustration 4: Qualified opinion on both the financial statements and the service performance information due to the auditor's inability to obtain sufficient appropriate audit evidence about a single element of the financial statements

## **INDEPENDENT AUDITOR'S REPORT**

To [Appropriate Addressee]

### **Qualified Opinion on the [General Purpose Financial Report/Performance Report/**

We have audited the [general purpose financial report/performance report] of ABC [entity], which comprise the financial statements on pages *x to xx*, the [service performance information/statement of service performance] on pages *x to xx* [and the entity information on page *x*]. The complete set of financial statements comprise the statement of financial position as at December 31, 20X1, the [statement of financial performance/statement of comprehensive revenue and expense, statement of changes in net assets/equity], statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion* section of our report the accompanying [general purpose financial report/performance report] presents fairly, in all material respects (or *gives a true and fair view of*):

- [the entity information as at December 31, 20X1];
- the financial position of the [entity] as at December 31, 20X1, and (of) its financial performance, and its cash flows for the year then ended; and
- the service performance for the year ended December 31, 20X1 in accordance with the entity's service performance criteria

in accordance with [Public Benefit Entity Standards/*Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)*] issued by the New Zealand Accounting Standards Board.

### **Basis for Qualified Opinion**

[As outlined on page *xx* of the [general purpose financial report/performance report], [entity] has not applied the requirements of the [Public Benefit Entity Standards/*Public Benefit Entity Simple Format Reporting—Accrual (Not for profit)*] to its grant expenditure. We have been unable to obtain sufficient audit evidence to quantify the effects of this limitation. As a result of this matter, we were unable to quantify the adjustments that are necessary in respect of grant expenditure in the [statement of comprehensive revenue and expenses]; assets, liabilities and equity in the statement of financial position, [total comprehensive revenue and expense] and opening and closing equity in the [statement of changes in equity] and grants expense reported in the [service performance information/statement of service performance].]

We conducted our audit of the [financial statements] in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and the audit of the service performance information in accordance with the ISAs (NZ) and New Zealand Auditing Standard 1 *The Audit of Service Performance Information*. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the [General Purpose Financial Report/Performance Report]* section of our report. We are independent of the [entity] in accordance with the ethical requirements that



~~are relevant to our audit of the [General Purpose Financial Report/Performance Report] in New Zealand, Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

~~Other than in our capacity as auditor we have no relationship with, or interests in, the [entity].~~

~~...~~

### C.3 SAE 3100 Assurance Engagements on Compliance

Amend paragraphs 9, 19, 46, A19 and A65 to reflect the new title of PES 1. The footnote in paragraph A65 is amended with the new section reference.

9. Compliance with ISAE (NZ) 3000 (Revised) requires, among other things, that the assurance practitioner comply with Professional and Ethical Standard 1 ~~(Revised)~~<sup>53</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding related to assurance engagements<sup>54</sup>. It also requires the lead assurance practitioner<sup>55</sup> to be a member of a firm that applies Professional and Ethical Standard 3 (Amended)<sup>56</sup> or requirements in law or regulation, that are at least as demanding related to assurance engagements.
19. As required by ISAE (NZ) 3000 (Revised), the assurance practitioner shall comply with Professional and Ethical Standard 1 ~~(Revised)~~<sup>57</sup>, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. (Ref: Para. A6)
46. If the assurance practitioner becomes aware of information concerning an instance of non-compliance or suspected non-compliance with respect to laws and regulations, the assurance practitioner shall comply with Professional and Ethical Standard 1 ~~(Revised)~~, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding. (Ref. Para. A65)
- A19. Where relevant, the terms of the engagement could also include a reference to, and description of, the auditor's responsibility in accordance with:
- Professional and Ethical Standard 1 ~~(Revised)~~; and/or
  - applicable law or regulation, and

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<sup>53</sup> Professional and Ethical Standard 1 ~~(Revised)~~ *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*.

<sup>54</sup> See ISAE (NZ) 3000 (Revised), paragraphs 3(a) and 20.

<sup>55</sup> The term "lead assurance practitioner" is referred to in Professional and Ethical Standard 1 ~~(Revised)~~ and Professional and Ethical Standard 3 (Amended) as the "engagement partner".

<sup>56</sup> See ISAE (NZ) 3000 (Revised), paragraphs 3(b) and 31(a).

<sup>57</sup> See ISAE (NZ) 3000 (Revised), paragraph 20.

- obligations to report identified or suspected matters of non-compliance with laws and regulations to an appropriate authority outside the entity is required or appropriate in the circumstances.

A65. Professional and Ethical Standard 1 ~~(Revised)~~<sup>58</sup>, sets out the approach to be taken by an assurance practitioner who encounters or is made aware of matter(s) of non-compliance or suspected matter(s) of non-compliance with laws or regulations.<sup>59</sup> In these circumstances, the assurance practitioner shall consider the appropriate response to the identified matter(s) of non-compliance with laws and regulations in accordance with Professional and Ethical Standard 1 ~~(Revised)~~.

#### **C.4 SAE 3150 Assurance Engagements on Controls**

Amend paragraphs 9, 19, and A124, to update the title of PES 1. In addition, the footnote to paragraph 19 is replaced with a reference to the applicable requirement in ISAE (NZ) 3000 ~~(Revised)~~.

~~Paragraph 88(1) and the illustrative assurance practitioner's reports in Appendix 8 are amended consistent with the changes to the wording in the auditor's report as required by ISA (NZ) 700 ~~(Revised)~~.~~

9. Compliance with ISAE (NZ) 3000 ~~(Revised)~~ requires, among other things, that the assurance practitioner complies with Professional and Ethical Standard 1 ~~(Revised)~~<sup>59</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding related to assurance engagements<sup>60</sup>. It also requires the lead assurance practitioner<sup>61</sup> to be a member of a firm that applies Professional and Ethical Standard 3 (Amended) or requirements in law or regulation, that are at least as demanding related to assurance engagements.<sup>62</sup>
19. As required by ISAE (NZ) 3000 ~~(Revised)~~, the assurance practitioner shall comply with Professional and Ethical Standard 1 ~~(Revised)~~<sup>63</sup> or other professional requirements, or requirements in law or regulation, that are at least as demanding related to assurance engagements. (Ref: Para. A10)

~~88(1) — a statement that the assurance practitioner complies with the independence and other~~

<sup>58</sup> See Professional and Ethical Standard 1 ~~(Revised)~~, Section 225360, *Responding to Non-Compliance with Laws and Regulations*

<sup>59</sup> Professional and Ethical Standard 1 ~~(Revised)~~, International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)

<sup>60</sup> ISAE (NZ) 3000 ~~(Revised)~~, paragraphs 3(a) and 20:

<sup>61</sup> The term “lead assurance practitioner” is referred to in Professional and Ethical Standard 1 ~~(Revised)~~ and Professional and Ethical Standard 3 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements* (Amended) as the “engagement partner”.

<sup>62</sup> ISAE (NZ) 3000 ~~(Revised)~~, paragraphs 3(b) and 31(a):

<sup>63</sup> ~~Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners. See ISAE (NZ) 3000 (Revised), paragraph 20~~

~~relevant ethical requirements related to assurance engagements; of Professional and Ethical Standard 1 (Revised), or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as Professional and Ethical Standard 1 (Revised);~~

A124. Professional and Ethical Standard 1—~~(Revised)~~ or other professional requirements, or requirements in law or regulation, that are at least as demanding require that an assurance practitioner not be associated with information where the assurance practitioner believes that the information:

- (a) contains a materially false or misleading statement;
- (b) contains statements or information furnished recklessly; or
- (c) omits or obscures information required to be included where such omission or obscurity would be misleading.

## **Appendix 8**

(Ref: Para. A139)

### **EXAMPLE ASSURANCE REPORTS ON CONTROLS**

~~Example 1: Limited Assurance Report on Design and Description of the Entity's Controls as at a Specified Date~~

~~Example 2: Reasonable Assurance Report on the Design, Description and Operating Effectiveness of the Entity's Controls throughout the Period~~

~~Example 3: Reasonable Assurance Report on the Design and Implementation of the Entity's Controls as at a Specified Date~~

~~Example 4: Reasonable Assurance Report on the Design and Operating Effectiveness of the Entity's Controls throughout the Period~~

~~The following examples of reports are for guidance only and are not intended to be exhaustive or applicable to all situations. They can be applied to both attestation and direct engagements. These examples are short form reports but may be converted to long form reports by inclusion of additional information as indicated.~~

## **Example 1: Limited Assurance Report on Design and Description of the Entity's Controls as at a Specified Date**

### **Independent Assurance Practitioner's Report**

*[Appropriate Addressee]*

#### *Scope*

We have undertaken a limited assurance engagement on the design of controls within ABC's *[type or name of]* system (the controls), comprising *[identify system by distinguishing features, boundaries and control components]*<sup>64</sup>; as at *[date]* relevant to *[[list overall objectives]/* the following control objectives: *[list or reference specific control objectives]*<sup>65</sup>*]* and ABC's description of its *[type or name of]* system at pages *[bb-cc]* (the description)<sup>66</sup>. The scope of our limited assurance engagement does not include whether the controls were implemented as designed or operated effectively.

#### *ABC's Responsibilities*

ABC is responsible for:

- (a) — the *[functions or services]* within the *[type/name of]* system;
- (b) — identifying the control objectives;
- (c) — identifying the risks that threaten achievement of the control objectives;
- (d) — designing controls to mitigate those risks, so that those risks will not prevent achievement of the identified control objectives; and
- (e) — preparing the description<sup>67</sup> *[and Statement]* at page *[aa]*, including the completeness, accuracy and method of presentation of the description *[and Statement]*.

#### *Our Independence and Quality Control*

We have complied with the relevant ethical requirements relating to assurance engagements, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* or other professional requirements, or requirements in law or regulation, that are at least as demanding, which include independence and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

In accordance with Professional and Ethical Standard 3 (Amended) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements* or other professional requirements, or requirements in law or regulation, that are at least as demanding, *[name of firm]* maintains a comprehensive system of quality control including documented policies

<sup>64</sup>—Identify system by function or service provided and entity, facility or location. If the scope of the engagement is restricted to certain control components, identify those components. Components may include: the control environment, risk assessment, control activities, information and communication or monitoring activities, or equivalent components defined by control framework applied.

<sup>65</sup>—Control objectives are listed if they are not detailed in the entity's description

<sup>66</sup>—If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

<sup>67</sup>—Insert for attestation engagements if a responsible party's or evaluator's Statement is provided to users.

and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

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## **~~Example 2: Reasonable Assurance Report on the Design, Description, and Operating Effectiveness of the Entity's Controls throughout the Period Independent Assurance Practitioner's Report~~**

~~[Appropriate Addressee]~~

### *~~Scope~~*

~~We have undertaken a reasonable assurance engagement on the design of controls within ABC's [type/name of] system (the controls), comprising [identify system by distinguishing features, boundaries and control components]<sup>68</sup>, throughout the period [date] to [date] relevant to [[list overall control objectives]/ the following control objectives: [list or reference the control objectives]], ABC's description of its [type or name of] system at pages [bb-cc] (the description)<sup>69</sup>, and the operating effectiveness of those controls.~~

### *~~ABC's Responsibilities~~*

~~ABC is responsible for:~~

- ~~(a) — the [functions or services] within the [type/name of] system;~~
- ~~(b) — identifying the control objectives;~~
- ~~(c) — identifying the risks that threaten achievement of the control objectives;~~
- ~~(d) — designing controls to mitigate those risks, so that those risks will not prevent achievement of the identified control objectives;~~
- ~~(e) — preparing the description [and Statement]<sup>70</sup> at page [aa], including the completeness, accuracy and method of presentation of the description [and Statement]<sup>71</sup>; and~~
- ~~(f) — operating those controls effectively as designed throughout the period.~~

### *~~Our Independence and Quality Control~~*

~~We have complied with relevant ethical requirements relating to assurance engagements, the Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* or other professional ethical requirements, or requirements in law or regulation, that are at least as demanding, which include independence and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.~~

~~In accordance with Professional and Ethical Standard 3 (Amended) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements* or other professional requirements, or requirements in law or regulation, that are at least as demanding,~~

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<sup>68</sup> \_\_ Identify the system by function or service provided and entity, facility or location. If the scope of the engagement is restricted to certain control components, identify those components. Components may include: the control environment, risk assessment, control activities, information and communication or monitoring activities, or equivalent components defined by control framework applied.

<sup>69</sup> \_\_ If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

<sup>70</sup> \_\_ Insert for attestation engagements if the responsible party's or evaluator's Statement is provided to users.

<sup>71</sup> \_\_ Insert for attestation engagements if the opinion is phrased in terms of the Statement.

~~[name of firm] maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.~~

~~...~~

DRAFT

### **Example 3: Reasonable Assurance Report on the Design and Implementation of the Entity's Controls as at a Specified Date**

#### **Independent Assurance Practitioner's Report**

*[Appropriate Addressee]*

##### *Scope*

We have undertaken a reasonable assurance engagement on the design and implementation of controls within ABC's *[type/name of]* system (the controls), comprising *[identify system by distinguishing features, boundaries and control components<sup>72</sup>]* as at *[date]* relevant to *[[list overall objectives]/ the following control objectives: [List or reference the control objectives<sup>73</sup>]]*

##### *ABC's Responsibilities*

ABC is responsible for:

- (a) — the *[functions or services]* within the *[type/name of]* system;
- (b) — identifying the control objectives;
- (c) — identifying the risks that threaten achievement of the control objectives;
- (d) — designing and implementing controls to mitigate those risks, so that those risks will not prevent achievement of the identified control objectives;
- (e) — implementing the controls as designed; and
- (f) — *[preparing the accompanying Statement at page [aa], including the completeness, accuracy and method of presentation of the Statement.]<sup>74</sup>*

##### *Our Independence and Quality Control*

We have complied with relevant ethical requirements relating to assurance engagements, the Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* or other professional ethical requirements, which include independence and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

In accordance with Professional and Ethical Auditing Standard 3 (Amended) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements* or other professional requirements, or requirements in law or regulation, that are at least as demanding, *[name of firm]* maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

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72—Identify the system by function or service provided and entity, facility or location. If the scope of the engagement is restricted to certain control components, identify those components. Components may include: the control environment, risk assessment, control activities, information and communication or monitoring activities, or equivalent components defined by control framework applied.

73— Either list overall control objectives or list specified control objectives depending on scope of engagement.

74— Insert for attestation engagements if the responsible party's or evaluator's Statement is provided to users.



...

#### **Example 4: Reasonable Assurance Report on the Design and Operating Effectiveness of the Entity's Controls throughout the Period**

##### **Independent Assurance Practitioner's Report**

*[Appropriate Addressee]*

##### *Scope*

We have undertaken a reasonable assurance engagement on the design and the operating effectiveness of controls within ABC's *[type/name of]* system (the controls), comprising *[identify system by distinguishing features, boundaries and control components<sup>75</sup>]*, throughout the period *[date]* to *[date]* relevant to *[[list overall objectives]/ the following control objectives: [List or reference the control objectives<sup>76</sup>]]*

##### *ABC's Responsibilities*

ABC is responsible for:

- (a) the *[functions or services]* within the *[type/name of]* system;
- (b) identifying the control objectives;
- (c) identifying the risks that threaten achievement of the control objectives;
- (d) designing controls to mitigate those risks, so that those risks will not prevent achievement of the identified control objectives;
- (e) operating effectively the controls as designed throughout the period; and
- (f) *[preparing the accompanying Statement at page [aa], including the completeness, accuracy and method of presentation of the Statement.<sup>77</sup>]*

##### *Our Independence and Quality Control*

We have complied with relevant ethical requirements relating to assurance engagements, Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* or other professional ethical requirements, or requirements in law or regulation, that are at least as demanding, which include independence and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

In accordance with Professional and Ethical Auditing Standard 3 (Amended) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements* or other professional requirements, or requirements in law or regulation, that are at least as demanding, *[name of firm]* maintains a comprehensive system of quality control including

<sup>75</sup> Identify the system by function or service provided and entity, facility or location. If the scope of the engagement is restricted to certain control components, identify those components. Components may include: the control environment, risk assessment, control activities, information and communication or monitoring activities, or equivalent components defined by control framework applied.

<sup>76</sup> Either list overall control objectives or list specified control objectives depending on scope of engagement.

<sup>77</sup> Insert for attestation engagements if the responsible party's or evaluator's Statement is provided to users.

~~documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.~~

## **C.5 ISRE (NZ) 2400 Assurance Engagements on Controls**

Amend paragraph NZA95.1 to reflect the new title of PES 1. In the footnotes, paragraph references to PES 1 have been updated. New text is underlined and deleted text is struck through.

NZA95.1 In some cases the relevant ethical requirements may require the assurance practitioner to report or to consider whether reporting identified or suspected fraud or non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, Professional and Ethical Standard 1 ~~(Revised)~~ requires the assurance practitioner to take steps to respond to identified or suspected non-compliance with laws and regulations, and determine whether further action is needed, which may include reporting to an appropriate authority outside the entity.<sup>78</sup> Professional and Ethical Standard 1 ~~(Revised)~~ explains that such reporting would not be considered a breach of the duty of confidentiality under Professional and Ethical Standard 1 ~~(Revised)~~.<sup>79</sup>

## **D. Effective Date**

Given the limited nature of the amendments proposed and because the conforming amendments do not create any new obligations, the NZAuASB is proposing that the conforming amendments become effective approximately 90 days after approval of the final standard. ~~The effective date for the final conforming amendments is a matter for the NZAuASB to determine. However, it is anticipated that, given the limited nature of the amendments proposed, the amendments can go into effect almost immediately.~~

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<sup>78</sup> See, for example, paragraph 360.21 A1 ~~Section 225.29~~ of Professional and Ethical Standard 1 ~~(Revised)~~

<sup>79</sup> See, for example, Section paragraphs R114.1(d) and R360.26-40.7 ~~and Section 225.35~~ of Professional and Ethical Standard 1 ~~(Revised)~~.

## NZAuASB Board Meeting Summary Paper

**AGENDA ITEM NO.** 11.1

**Meeting date:** 5 December 2019

**Subject:** Modified audit reports

**Date:** 22 November 2019

**Prepared by:** Peyman Momenan

|                          |                        |                                     |                                      |
|--------------------------|------------------------|-------------------------------------|--------------------------------------|
| <input type="checkbox"/> | <b>Action Required</b> | <input checked="" type="checkbox"/> | <b>For Information Purposes Only</b> |
|--------------------------|------------------------|-------------------------------------|--------------------------------------|

### Objective

For the Board to note the summary of modified auditor reports received by the XRB between 1 June 2019 and 22 November 2019.

### Introduction

1. In September 2016, the XRB approved a policy for dealing with modified audit reports received under the Companies Act 1993 and the Financial Markets Conduct Act 2013. The policy requires the NZAuASB to consider implications for the relevant standards by ensuring that the modified audit opinions do not raise any issue about the appropriateness, applicability, clarity and/or completeness of the relevant standards.
2. In December 2016, the policy was supplemented by an operating procedure (OP) document including specific actions that the XRB and its boards (including the NZAuASB) need to take to operationalise the policy. The OP requires the NZAuASB staff to review the received modified audit reports in order to:
  - Categories of modified audit opinions that affect auditing & assurance standards
  - Identify trends, if any
  - Refer any strategy-related issues to the XRB Board staff team, as appropriate
  - Make appropriate recommendation to NZAuASB, as necessary
3. The OP requires staff to report to the NZAuASB at least every 6 months on matters including:
  - the number of audit reports received
  - the types of modified audit opinions
  - the nature/subject matter of the modified opinions
  - whether the modified audit opinions have implications for any XRB standards and/or XRB strategy/standards frameworks
  - any emerging trends.

4. The Board had previously seen the summary of modified audit reports up to end of May 2019 at the June 2019 meeting. This report is a catch up for the modified audit reports received since. This report is the second report under the XRB modified auditor report policy.
5. For the past two years we have reported the modified audit reports at the Board's July and December meetings. The timing of the distribution of Board meeting papers and the timing of Board meetings has resulted in the cut-off dates for the periods being reported on being during the month. We are proposing to change the dates of reporting to the full six-monthly periods of 1 January to 30 June and 1 July to 31 December. To align with these new dates the modified audit reports will be reported to the Board at its September and February meetings each year. We will implement these new reporting dates from September 2020. The staff of the NZASB will also be proposing these new dates to the NZASB. The timing of reporting to the XRB Board will also change from its December meeting to its March meeting. This new timing of reporting also works better for the XRB Board because the modified audit reports received for the year would have been considered by both the NZASB and the NZAuASB at their February meetings.

### **Matters to consider**

6. We have prepared a summary of the reasons for the qualifications by modification type with a view to consider if there are any implications for the XRB standards. A summary of the reasons for the modified audit reports received from 1 June 2019 to 22 November 2019 is attached at agenda item.
7. We have not identified any implications for the auditing and assurance standards and have no recommendations for further action required by the NZAuASB. It is worth mentioning that the accounting staff have also not identified any implications for the accounting standards when they presented their analysis to NZASB in December 2019. The overall conclusions are due to be presented to the XRB Board in March 2020.

### **Recommendations**

8. It is recommended that the Board **NOTE** the contents of this report.

### **Material Presented**

|                  |                             |
|------------------|-----------------------------|
| Agenda item 11.1 | Board Meeting Summary Paper |
| Agenda item 11.2 | Summary of modifications    |

**Modified Auditor Reports received by the XRB between 1/06/2019 and 22/11/2019****A) Modified Auditor Reports**

| Modification in relation to                           | Adverse Opinion                               | Disclaimer of Opinion                                  | Qualified Opinion                             |  | Grand Total                                   |  |
|---|---|--|---|--|---|--|
|   | Financial statements are materially misstated | Unable to obtain sufficient appropriate audit evidence | Financial statements are materially misstated | Unable to obtain sufficient appropriate audit evidence | Financial statements are materially misstated | Unable to obtain sufficient appropriate audit evidence |
| Accounting records for property, plant and equipment  |   |  |   | 1  |   | 1  |
| Appropriateness of using the Going Concern assumption |   | 1  |   |  |   | 1  |
| Audit Procedures                                      |   |  |   | 1  |   | 1  |
| Impairment test of PPE                                |   | 1  |   |  |   | 1  |
| Revenue from Contracts with Customers                 |   |  | 2   |  | 2   |  |
| Valuation of Investment in associated entities        |   |  |   | 1  |   | 1  |
| <b>Total</b>  | <b>0</b>                                      | <b>2</b>   | <b>2</b>                                      | <b>3</b>   | <b>2</b>                                      | <b>5</b>   |

During this period, we also received one auditor report that was not a modified report. It was for a licensed insurer who were required by the RBNZ to adjust and resubmit its solvency tests for year ended 31 March 2019. This report is included in our internal database but is NOT included in the above table.

## Modified Auditor Reports received by the XRB between 1/06/2019 and 22/11/2019

| ID number <sup>1</sup><br>Nature of industry<br>Balance date<br>Audit report date                       | Type of modified audit opinion   | Accounting standard(s) affected  | Proposed action  |
|---|--|--|--|
| 185<br>Manufacturer and wholesaler of plastic containers and coat hangers<br>31 Dec 2018<br>28 May 2019 | Qualified opinion<br>Unable to obtain sufficient appropriate audit evidence to support the carrying value of inventories because the auditor was unable to observe the counting of the inventories.<br>Unable to obtain sufficient appropriate audit evidence to support the goodwill arising from an acquisition. | NZ IFRS 3 <i>Business Combinations</i><br>NZ IAS 2 <i>Inventories</i><br>NZ IAS 38 <i>Intangible Assets</i>            | Nil.<br>We did not identify any issues with the Auditing Standards standards.<br><br>NZASB did not identify any issues with the Accounting Standards |
| 186<br>Provider of cloud based software<br>31 Mar 2016<br>4 Jun 2019                                    | Disclaimer of opinion<br>Unable to obtain sufficient appropriate audit evidence to support the going concern assumption.   | NZ IAS 1 <i>Presentation of Financial Statements</i>   | Nil.<br>We did not identify any issues with the Auditing Standards.<br><br>NZASB did not identify any issues with the Accounting Standards           |
| 187<br>Manufacturer of fine fish oil<br>31 Mar 2019<br>24 Jun 2019                                      | Disclaimer of opinion<br>Unable to obtain sufficient appropriate audit evidence to support the assumptions in assessing the recoverable value and the impairment expense of property, plant and equipment and inventory for the current and prior period.  | NZ IAS 2 <i>Inventories</i><br>NZ IAS 16 <i>Property, Plant and Equipment</i><br>NZ IAS 36 <i>Impairment of Assets</i> | Nil.<br>We did not identify any issues with the Auditing Standards.<br><br>NZASB did not identify any issues with the Accounting Standards           |
| 188<br>Services and technologies to food processors and retailers<br>31 Mar 2019<br>10 Sep 2019         | Qualified opinion<br>The entity's interpretation of NZ IFRS 15 has resulted in material misstatements of retained earnings for the opening balance of the comparatives and current period's contract asset and revenue.  | NZ IFRS 15 <i>Revenue from Contracts with Customers</i>  | Nil.<br>We did not identify any issues with the Auditing Standards.<br><br>NZASB did not identify any issues with the Accounting Standards           |
| 189<br>Out of home media<br>31 Dec 2018<br>6 Nov 2019   | Qualified opinion<br>Unable to obtain sufficient appropriate audit evidence to support the accuracy of the cost and related accumulated depreciation of plant and equipment.   | NZ IAS 16 <i>Property, Plant and Equipment</i>   | Nil.<br>We did not identify any issues with the Auditing Standards.<br><br>NZASB did not identify any issues with the Accounting Standards           |
| 190<br>Solution provider for accounting software<br>31 Mar 2019<br>19 Aug 2019                          | Qualified opinion<br>Unable to obtain sufficient appropriate audit evidence to support the carrying values of the following.   | NZ IFRS 9 <i>Financial Instruments</i><br>NZ IAS 28 <i>Investments in Associate and Joint Venture</i>                  | Nil.<br>We did not identify any  |

<sup>1</sup> From internal database.

## Modified Auditor Reports received by the XRB between 1/06/2019 and 22/11/2019

| ID number <sup>1</sup><br>Nature of industry<br>Balance date<br>Audit report date | Type of modified audit opinion   | Accounting standard(s)<br>affected                      | Proposed action   |
|---|--|---|---|
|   | <ul style="list-style-type: none"> <li>Investment in associate.</li> <li>Loan to the associate.</li> <li>Share of the associate's net loss.</li> <li>Investment in joint venture.</li> <li>Loan to the joint venture.</li> <li>Impairment expense of the investment in joint venture.</li> <li>Share of the joint venture's net loss.</li> </ul> |   | <p>issues with the Auditing Standards.</p> <p>NZASB did not identify any issues with the Accounting Standards</p>                                     |
| 191<br>Insurer<br>31 March 2019<br>23 Sep 2019                                    | N/A (No modification)<br>'RBNZ requested the company to adjust and resubmit its solvency tests for year ended 31 March 2019  | NA  | <p>Nil.</p> <p>We did not identify any issues with the Auditing Standards.</p> <p>NZASB did not identify any issues with the Accounting Standards</p> |
| 192<br>Packaging machinery<br>31 Dec 2018<br>23 Sep 2019                          | <p>Qualified opinion</p> <p>The entity has not recognised revenue in accordance with NZ IFRS 15. Revenue has been recognised at a point in time rather than over time and the bill and hold requirements have not been considered.</p>   | NZ IFRS 15 <i>Revenue from Contracts with Customers</i> | <p>Nil.</p> <p>We did not identify any issues with the Auditing Standards.</p> <p>NZASB did not identify any issues with the Accounting Standards</p> |



NZ AUDITING  
AND ASSURANCE  
STANDARDS BOARD

**DATE:** 22 November 2019

**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 second half of October and November 2019.

### **International Federation of Accountants (IFAC)**

1. There have been no significant developments related to audit and assurance to report in the period.

### **International Auditing and Assurance Standards Board (IAASB)**

1. The IAASB Ongoing projects (refer to appendix 1)

### **International Ethics Standards Board for Accountants (IESBA)**

1. There have been no significant developments related to audit and assurance to report in the period.

### **Accountancy Europe (AE) (former FEE)**

1. *This article has been published by [Audit Analytics](#). It is about the second annual survey we performed on the auditor's reporting of key audit matters (KAMs) in the [European banking sector](#) since KAMs became required by EU law and international standards in 2017.*  
One of the main goals of the survey is to benchmark and compare the data from the banking sector, year-over-year. The survey, which highlights over 60 banks that own the vast majority of assets in the European banking sector, focuses on the average number and main topics of KAMs that were reported during the year. More specifically, it takes a deeper dive into the reasons for communicating KAMs and some of the challenges that arise during this process.  
In addition, the survey looks at the clarity and presentation of the KAM disclosures. In a year-over-year analysis of the 62 audit reports within the sector, there was a slight decrease in the average number of KAMs per report between 2017 and 2018, from 4.4 to 4.2, respectively.  
These averages are much higher in comparison to the average number of KAMs across all industries. As cited in the survey, [Audit Analytics](#) found an average of 2.7 KAMs in 2018 for all industries; excluding the banking sector resulted in an average of 2.6 KAMs per audit report.  
Please read the full article [here](#).
1. AE [issued its response](#) to IESBA Exposure Draft, Proposed Revisions to the Code to Promote the Role and Mindset. The Revised Code became applicable in June 2019 and AE believe that



further changes should be limited to the cases where the need is significant. AE also note that IESBA should be cautious when adding new terms to the Code as they may not always provide more clarity.

#### **Public Interest Oversight Board of IFAC (IPIOB)**

1. There have been no significant developments related to audit and assurance to report in the period.

#### **International Integrated Reporting Council (IIRC)**

1. There have been no significant developments related to audit and assurance to report in the period.

#### **Global Reporting Initiative (GRI)**

1. There have been no significant developments related to audit and assurance to report in the period.

#### **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. There have been no significant developments related to audit and assurance to report in the period.

#### **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. The AUASB provided a Submission to the Parliamentary inquiry into regulation of auditing in Australia on 25<sup>th</sup> of October 2019.

The AUASB supports all activities that promote continuous improvement in audit quality, transparency and professional conduct across the auditing profession. In its submission the AUASB emphasised its support of evidence-informed, best practice initiatives aimed at improving the quality of audit and financial reporting in Australia, and that improving audit quality requires interaction between, and action by, all key parties / stakeholders in the financial reporting supply chain. [Link to submission](#)

## **United Kingdom**

#### **FRC**

1. Audit quality is still not consistently reaching the necessary high standards expected, according to the Financial Reporting Council's (FRC) [Developments in Audit](#) report, particularly when challenging management and performing routine procedures such as revenue recognition. High quality audit is essential to ensure confidence in financial reporting by UK companies.

The FRC is working with audit firms to ensure quality improves and will hold firms to account where remedial action is not taken to an appropriate level or on a sufficiently timely basis.

AQR inspection reports show that auditors continue to struggle most with challenging management sufficiently, especially in more judgemental areas, such as long-term contracts, goodwill impairment or the valuation of financial instruments. The inherent uncertainty and high potential financial impact of these issues mean the importance of robust, specific and independent challenge is vital.

Other shortcomings were identified in more routine audit procedures - notably in relation to revenue recognition, which is typically a key metric considered by users of financial statements.

2. The largest accountancy firms have increased their share of the UK audit market with 100% of FTSE 100 companies now audited by the Big Four\*, according to new research from the Financial Reporting Council (FRC).

The latest edition of [\*Key Facts and Trends in the Accountancy Profession\*](#) published today reveals the Big Four increased their combined 'total fee income' by 4.7% to £10.95 billion and 'audit fee income' by 1.7% to £2.1 billion. By contrast, total fee income at non-big four public interest entity audit firms fell by 8.1% and 'audit fee income' fell by 6.3% (compared to a 3% increase in 2016/17).

The average audit fee income in 2018 for all firms with public interest entity clients per responsible individual was £1.46 million, an increase of £0.16 million (12.3%) from 2017.

The number of audit firms registered to carry out statutory audit work in the UK and the Republic of Ireland (ROI) fell by 4.7% in 2017/18, down from 5,660 to 5,394 audit firms. This is in part due to a decline in both the number of sole practitioner audit firms (down from 2,733 to 2,558) and firms with 2 - 6 Principals (down from 2,618 to 2,534).

Meanwhile membership of the accountancy bodies continues to grow. The seven bodies overseen by the FRC have over 365,000 members in the UK and the ROI and almost 550,000 members worldwide. The average annual growth in the UK and the ROI between 2014 to 2018 was 2.2% and 3.1% worldwide.

There are over 164,000 accounting students in the UK and the ROI and nearly 600,000 worldwide. Student numbers in the UK and the ROI increased by 0.2% and by 1.5% worldwide from 2017 to 2018, indicating accountancy remains a popular profession and the UK a centre of excellence.

A link to the research can be viewed [here](#).

3. Companies are falling short of investors' expectations for clearer reporting on climate-related issues according to a new report [\*Climate-related corporate reporting\*](#) from the FRC Financial Reporting Lab (the Lab).

As economies increasingly transition towards low carbon and climate resilient futures, the Lab's report highlights the gap between current reporting and investor expectations and calls on companies to bridge this gap.

It provides practical guidance about where companies can improve their reporting. The report also outlines what investors want to understand, questions companies should ask themselves, recommended disclosures, and a range of examples of the developing practice of climate-related reporting.

While reporting on climate change is an evolving practice, expectations are changing rapidly. The Lab recommends companies use the Task Force on Climate-related Financial Disclosures (TCFD) framework to report on climate-related issues, as this was well supported by participants, and the UK Government expects all listed companies and large asset owners to disclose in line with the TCFD recommendations by 2022.

Earlier this year, the FRC published a statement outlining the responsibility of Boards of UK companies to consider their impact on the environment and the likely consequences of long-term

business decisions. Boards should, therefore, address and where relevant, report on the effects of climate change.

### **Institute of Chartered Accountants in England and Wales**

1. What is assurance? How does it work and why might it be useful to users of non-financial information? This 'Buyers Guide to Assurance on non-financial information', written collaboratively between ICAEW's Audit and Assurance Faculty and the World Business Council for Sustainable Development, addresses these questions to bring much needed clarity on what is often perceived as a confusing topic. (See Appendix 2 for a copy of the guide).

### **The Charity Commission**

1. There have been no significant developments related to audit and assurance to report in the period.

### **Association of Chartered Certified Accountants (ACCA)**

1. There have been no significant developments related to audit and assurance to report in the period.

### **Other news from the UK**

1. Changes designed to shake up UK auditing after accounting scandals are driving an increasing number of large listed companies to approach firms outside the Big Four.

The UK government is weighing proposals from the competition watchdog that would force all large listed businesses to appoint one of the Big Four — Deloitte, EY, KPMG and PwC — and a challenger firm to conduct joint audits.

As a result, smaller accounting firms are reporting a wave of audit inquiries from large companies. (read the rest of the article [here](#))

2. Due to be re-launched as the Audit, Reporting and Governance Authority (ARGA) after a string of audit failures and lack of adequate oversight of the major audit firms, the FRC is reported to be looking for wider powers to curb the audit market by setting fixed audit fees for listed audits, according to reports in the Sunday Times. (read the rest of the article [here](#))
3. Simon Dingemans, the recently appointed chair of the Financial Reporting Council (FRC), has backed reforms to split the big six firms. (read the rest of the article [here](#))

## **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. The AICPA has issued a new Technical Question and Answer (TQA) to provide nonauthoritative guidance on implementing the AICPA Auditing Standards Board's new standard on auditor reporting. Discussion in [TQA 8100.04](#) addresses the circumstance in which a continuing auditor is engaged to perform an audit of comparative financial statements in the first year of implementation of

Statement on Auditing Standards No. 134, *Auditor Reporting and Amendments, Including Amendments Addressing Disclosures in the Audit of Financial Statements*.

**Center for Audit Quality (CAQ) - (affiliated with AICPA)**

1. Although growth has been steady in the amount of information provided in audit committee disclosures, significant opportunities continue to exist to enhance transparency in this area, according to [the 2019 edition of the Audit Committee Transparency Barometer](#). A report issued jointly by the CAQ and Audit Analytics, the Barometer tracks S&P Composite 1500 proxy disclosures to gauge transparency around audit committee oversight of the external auditor and other key financial reporting topics.

In addition to presenting statistics on disclosure trends, the Barometer offers disclosure examples to illustrate how audit committees are enhancing information for investors and others.

**Other news from US:**

1. The demand for sustainability assurance is likely to grow in the coming years, according to a new survey conducted by The Conference Board.

Thirty-seven of the 57 large U.S. and European companies participating in the survey said they obtain assurance on at least some of their publicly reported sustainability information. Seventy percent of the companies that obtain this assurance said they expect that the need for sustainability assurance will increase over the next five years.

In addition, four respondents said they plan to begin obtaining assurance on their sustainability information within the next three years, and 10 more respondents said they will consider obtaining assurance during that time frame. Twelve respondents who already obtain assurance said they plan to expand the scope of sustainability information subject to assurance. More than three-fourths (77%) of the respondents to the survey were from U.S. companies. (More details [here](#))

2. The number of companies across the world who issue some form of sustainability report continues to increase. However, even as organizations place more emphasis on improving reporting quality related to the environmental and social impact of their business activities, little is known about whether assurance for these reports improves the quality, and whether accounting firm assurers improve that quality to a greater extent than nonaccounting firm assurers. "With investor attention on such information higher than ever, corporate sustainability reporting is ripe for the next phase of its evolution," said a 2018 report posted on the Harvard Law School Forum on Corporate Governance and Financial Regulation.

This article provides a summary of insights on these issues based on an academic study we recently published in the *Journal of Accounting and Public Policy* ("Corporate Social Responsibility Assurance and Reporting Quality: Evidence From Restatements"). (read the rest of the article [here](#)).

## Canada

**Canadian Auditing and Assurance Standards Board (AASB)**

1. There have been no significant developments related to audit and assurance to report in the period.

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**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   |
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| <p><b>Quality Control</b></p> <p><b>No Update for the period</b></p> | <p><b>Objective of the Project:</b> 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><b>Background and current status:</b> 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 <a href="#">project proposals for quality control</a> that were presented at the September 2016 IAASB meeting.</p> <p>The IAASB considered the Quality Control Other Working Group's (QCOWG) <a href="#">proposals</a> in respect of:</p> <ul style="list-style-type: none"> <li>• Setting the objective of an engagement quality control (EQC) Revising the definition of an EQC review;</li> <li>• Determining the scope of the engagements subject to an EQC review; and</li> <li>• The execution of an EQC review.</li> </ul> <p>At its March 2017 meeting, the IAASB discussed matters to do with the <a href="#">eligibility</a> of the engagement quality control reviewer.</p> <p><b>QC-Firm Level</b></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"> <li>• 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</li> </ul> |

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|  | <ul style="list-style-type: none"> <li>• the proposals in relation to other engagements for which the firm determines that an EQC review is required (see here for details)</li> <li>• 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</li> <li>• 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</li> <li>• the proposed requirements and application material in relation to the eligibility of the EQC reviewer.</li> </ul> <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>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 Board discussed the exposure draft (ED) of proposed ISQC 1 (Revised)1 and was supportive of the direction that the Quality Control Task Force was taking the standard, noting the improvement in the readability and understandability overall. The Board encouraged the Quality Control Task Force to consider whether there are further opportunities to address scalability, including further refinement and simplification of the standard, where possible. The Board also discussed changing the title of the standard</p> <p>In finalizing the ED in December 2018, the Board discussed the definition of deficiencies and bringing more emphasis to positive findings from the firm’s monitoring activities and how they may be used in the system of quality management. The Board also discussed the requirement for the firm to establish additional quality objectives beyond those required by the standard and further clarifying the identification and assessment of quality risks. In addition, the Board suggested further simplification of the requirement addressing communication with external parties, although in general agreed to retain an explicit reference to transparency reports in the requirement. The Board also discussed network requirements or network services, and</p> |
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|  | <p>adjusted the requirement to clearly reflect the expectations of the firm regarding the effect of network requirements or network services on the firm's system of quality management.</p> <p>The Board supported the Quality Control Task Force's recommendations regarding matters to be addressed in the Explanatory Memorandum, including the proposed questions.</p> <p>In September 2019, the Board discussed the comment letters received on certain areas of the Exposure Draft (ED) of ISQM 1 (ED-ISQM 1)<sup>3</sup> relating to the quality management approach, implementation challenges, the components and structure of the standard and the firm's risk assessment process. The Board concurred that four significant themes had emerged from the comments: scalability; prescriptiveness; addressing firms who do not perform audit or assurance engagements; and challenges with implementation. The Board, in general, supported proposals to address the structure of the standard and clarify the nature of the components and how they interrelate. The Board also supported addressing the granularity of the quality objectives, introducing quality risk considerations, and refining the required responses. The Board agreed with the ISQM 1 Task Force's proposals to simplify the firm's risk assessment process, including addressing concerns about the threshold for the identification of quality risks. The Board did not support the proposal to develop a separate standard for quality management for related services engagements and encouraged exploration of other ways to address scalability concerns. The ISQM 1 Task Force will take these comments into account in preparing revised drafting and issues for discussion at the December 2019 IAASB meeting.</p> <p><b>Quality Control – Engagement Level</b></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>The Board discussed a draft ED of proposed ISA 220 (Revised)<sup>2</sup> and was supportive of the proposed changes. The discussions focused on whether changes were needed to the objective of the standard and the wording of the requirement regarding the engagement partner being "sufficiently and appropriately involved." The Task Force plans on presenting the ED of proposed ISA 220 (Revised) for approval by the Board at the December 2018 meeting.</p> <p>In December 2018 the Board supported the requirement for the firm to establish policies or procedures addressing limitations on the engagement partner moving into the role of engagement quality reviewer, including the reference to a cooling-off period in the application material. The Board agreed that stakeholder views were needed relating to the objectivity of the engagement quality reviewer and a cooling-off period and supported the</p> |
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|  | <p>ISQM 2 Task Force's recommendation for including specific questions in the Explanatory Memorandum on this matter to be developed in coordination with the IESBA. The Board also clarified the requirement for notifications by the engagement quality reviewer to the engagement partner and, when applicable, individual(s) within the firm, as well as the documentation requirements.</p> <p>The Board discussed the requirements that address firm policies or procedures, the role of the engagement partner vis-à-vis other members of the engagement team and the difference between the usages of the phrases "the auditor shall determine" and "the auditor shall be satisfied." The board also discussed how best to clarify the requirement addressing communications from the firm about the firm's monitoring and remediation process.</p> <p>In September 2019, the Board discussed the comment letters received to ED-ISA 2205 and the ISA 220 Task Force's proposals for addressing the key issues respondents raised. The Board supported the fundamental principle that the engagement partner has overall responsibility for managing and achieving quality and being sufficiently and appropriately involved in the engagement. The Board also supported clarifying the requirement addressing circumstances when the engagement partner assigns procedures or tasks to other engagement team members, the principles underpinning the proposed engagement team definition and proposals to address scalability of the requirements to audits of larger or more complex entities. The ISA 220 Task Force will take these comments into account in preparing revised drafting and issues for discussion at the December 2019 IAASB meeting.</p>  |
| <p><b>Group Audits– ISA 600</b></p> <p><b>No Update for the period</b></p> | <p><b>Objective of the project:</b> 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><b>Background and current status:</b> 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, <a href="#">presented the results</a> 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</p> |

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|  | <p>requirements in those standards provide appropriate connection points between those projects and ISA 600.<sup>4</sup> 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>In March 2019, the Board was updated on the work performed by the Group Audit Task Force since the start of the project to revise ISA 600<sup>1</sup> and was asked for its views on issues related to scoping a group audit, the definitions, and the linkages with other ISAs. The Board continued to support developing a risk-based approach for scoping a group audit and generally supported the Group Audit Task Force's approach on the definitions and the issues that were presented in relation to the responsibilities of the group engagement partner, acceptance and continuance, understanding the group and its components, understanding the component auditor, identifying and assessing the risks of material misstatement and responding to assessed risks, the consolidation process, communication between the group auditor and component auditors, and evaluating the audit evidence obtained. These and other issues need to be further developed in the context of the risk-based approach and changes made to other of the IAASB's International Standards. The Group Audit Task Force will continue to work on the issues related to scoping a group audit, the definitions and other issues identified in the <a href="#">Invitation to Comment</a>, and will present it for further discussion at the June 2019 IAASB meeting.</p> <p>In June 2019, the Board was updated on the ISA 6003 Task Force's progress since the March 2019 meeting and discussed the public interest issues that the ISA 600 Task Force identified, the ISA 600 Task Force's proposals with respect to the risk-based approach to scoping a group audit, and the special considerations related to auditing a group. The Board also discussed indicative drafting related to the risk-based approach to scoping a group audit and the special considerations related to proposed ISA 220 (Revised).<sup>4</sup> Generally, the Board was supportive of the approach taken but had suggestions on the way forward and the indicative drafting. The ISA 600 Task Force will take these comments into account and will present further drafting at the September 2019 meeting. The ISA 600 Task Force will also continue its outreach to key stakeholders and coordinate with IESBA and other IAASB Task Forces as needed.</p> <p>In September 2019, the Board was updated on the work of the ISA 600 Task Force since the June 2019 meeting, including the outreach performed and the feedback received from the IAASB's Consultative Advisory Group. The Board discussed, among other matters, the updated public interest issues, a draft of a significant part of the standard and the ISA 600 Task Force's</p> |
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<sup>1</sup> International Standard on Auditing (ISA) 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

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|  | <p>proposals with respect to the scope and structure of the standard, materiality considerations in a group audit and a proposed stand-back requirement. The ISA 600 Task Force will take these comments into account in preparing revised drafting and issues for discussion at the December 2019 IAASB meeting</p>  |
| <p><b>Professional Scepticism</b></p> <p><b>No Update for the period</b></p> | <p><b>Objective of the project:</b> To make recommendations on how to more effectively respond to issues related to professional scepticism.</p> <p><b>Background and current status:</b> 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, <a href="#">presented the results</a> 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 <a href="#">here</a>.</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</p> |

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|   | <p>Professional Skepticism Subgroup will liaise as needed with the Professional Skepticism Joint Working Group.</p> <p>In September 2018 meeting, The Board received an update on the activities of the IAASB's Professional Skepticism Subgroup (Subgroup) since March 2018. The Chair of the Subgroup also presented the Board with a draft publication that seeks to highlight the IAASB's efforts to appropriately reflect professional scepticism into the IAASB standards as well as other relevant news and information on professional skepticism, including collaboration with the International Ethics Standards Board for Accountants (IESBA) and International Accounting Education Standards Board (IAESB). The Board supported the issuance of the publication and future publications of this nature.</p>   |
| <p><b>Accounting Estimates (ISA 540) and Special Audit Considerations Relevant to Financial Institutions (No Update for the period)</b></p> | <p><b>Objective of the project:</b> The objective of the financial institutions project is to:</p> <ul style="list-style-type: none"> <li>A. Clarify and enhance the relationship between the banking supervisors and the bank's external auditors;</li> <li>B. Consider and address issues of particular significance in audits of financial institutions; and</li> <li>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</li> </ul> <p><b>Background and current status:</b> 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 clear er 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. <a href="#">The board reviewed the draft in its June 2016 meeting.</a></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</p> |

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|  | <p>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)<sup>1</sup> 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><b>Data Analytics</b></p> <p><b>No Update for the period</b></p>                            | <p><b>Objective of the project:</b> The objective of the Data Analytics Working Group (WG) is to:</p> <p>A) Explore emerging developments in audit data analytics; and</p> <p>B) Explore how the IAASB most effectively can respond via International Standards or non-authoritative guidance (including Staff publications) and in what timeframe.</p> <p><b>Background and current status:</b> 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 <a href="#">update</a> 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><b>Emerging External Reporting</b></p> <p><b>Update for the period</b></p> <p><b>No</b></p> | <p><b>Objective of the project:</b> The objective of the Integrated Reporting Working Group (IRWG) is to:</p> <p>A) Explore emerging developments in integrated reporting and other emerging developments in external reporting;</p> <p>B) Gather further information on the demand for assurance, the scope of the assurance engagement and the key assurance issues; and</p>  |

C) Explore how the IAASB most effectively can respond via International Standards or non-authoritative guidance (including Staff publications) and in what timeframe.

**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.

The Discussion Paper was issued in August 2016.

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.

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).

In its September 2018 meeting, the EER Task Force presented the remaining Phase 1 'issues' that were not presented in June alongside a first draft of the Phase 1 guidance. The Board noted the need for the guidance to demonstrate its full alignment with the requirements of ISAE 3000 (Revised), 5 and for the EER Task Force to provide further explanations about any guidance that goes beyond the requirements and application material in ISAE 3000 (Revised). The EER Task Force expects to receive further input from stakeholders during its forthcoming series of discussion events and will present a revised draft of the guidance to the IAASB in December 2018.

In December 2018 The EER Task Force presented an updated version of the Phase 1 draft guidance, which reflects changes to address feedback received from the IAASB at the September 2018 IAASB meeting, and from other stakeholders, including in relation to a 'materiality process' and assertions as they relate to the characteristics of suitable criteria. The Board noted that the draft guidance had significantly improved since discussions at the September 2018 meeting, but that further work on the drafting is enquired. The Board will discuss a further version on a teleconference in January 2019 before the draft guidance is published for public comment.



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|   | <p>In March 2019, the Board approved for public comment Phase 1 of the draft guidance in January 2019. At its March 2019 meeting, the Board discussed several challenges related to Phase 2 of the guidance. The challenges include: determining the scope of an EER assurance engagement; communicating effectively in the assurance report; exercising professional skepticism and professional judgment; obtaining the competence necessary to perform the engagement; and obtaining evidence in respect of narrative and future-oriented information. The Board's deliberations of the challenges concerned were facilitated through breakout sessions, after which each breakout group reported back to the Board in a plenary session. The EER Task Force will consider the inputs that were received in progressing the development of Phase 2 of the guidance for further discussion at the June 2019 IAASB meeting.</p> <p>In June 2019, the Board was updated on the work of the EER Task Force on the challenges allocated to Phase 2 of the project. These challenges include: determining the scope of an EER assurance engagement; obtaining evidence in respect of narrative and future-oriented information; exercising professional skepticism and professional judgment; obtaining the competence necessary to perform the engagement; and communicating effectively in the assurance report. The Board discussed views on the EER Task Force's initial proposals to address each of these challenges in the Phase 2 guidance. The EER Task Force will consider the inputs received from the Board, together with responses to the Phase 1 EER Consultation Paper in so far as they impact the Phase 2 guidance, in developing the draft Phase 2 guidance, which will be presented for discussion at the September 2019 IAASB meeting.</p> <p>In September 2019, the Board received an overview of the comment letters received on the EER Assurance Consultation Paper. The Board discussed respondents' comments on the Consultation Paper, that included the draft Phase 1 guidance, and the EER Task Force's proposals for addressing the comments. The Board also discussed the initial drafting of the Phase 2 guidance developed to date by the EER Task Force. A revised draft of the combined Phase 1 and Phase 2 guidance will be presented to the Board, for approval of an exposure draft at the December 2019 IAASB meeting.</p> |
| <p><b>Agreed-Up<br/>Procedures</b></p> <p><b>No Update for the<br/>period</b></p> | <p><b>The objective of the project is to:</b></p> <p>A) Revise International Standard on Related Services (ISRS) 4400, Engagements to Perform Agreed-Up 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><b>Background and current status:</b> 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'</p>   |

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|   | <p>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, <a href="#"><i>Exploring the Growing Demand for Agreed-Upon Procedures Engagements and Other Services and the Implications for the IAASB's Standards</i></a>, 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 <b>approved</b> 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>In its September 2018 meeting, The Board approved the ED of ISRS 4400 (Revised)<sup>3</sup> for public exposure. In finalizing the ED, the Board agreed that independence is not required for an AUP engagement and that the AUP report would include statements addressing circumstances when the practitioner is (or is not) required to be independent, and whether the practitioner is (or is not) independent. The ED will be issued in early November with a 120 day comment period.</p> <p>In June 2019 the Board received an overview of the responses to proposed ISRS 4400 (Revised)<sup>2</sup> (ED–4400). The Board discussed, among other matters, respondents' comments on the application of professional judgment when performing procedures, the independence disclosure requirements, and the effective date.</p> <p>The Board also acknowledged areas of broad support, including not including a precondition for the practitioner to be independent, using the term “findings” and requiring an explanation of this term in the engagement letter and the AUP report, not requiring or prohibiting a reference to the practitioner's expert in the AUP report, and not requiring a restriction on use or distribution of the AUP report. The AUP Task Force will deliberate the Board's input and will present the first read of the post-exposure ISRS 4400 (Revised) to the Board in the second half of 2019.</p> |
| <p><b>ISA 315 (Revised)</b><br/><b>No Update for the period</b></p> | <p><b>The tentative objectives of the projects at this stage are:</b></p> <ul style="list-style-type: none"> <li>A) to address the issues that have been identified by the ISA Implementation Monitoring project.</li> <li>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).</li> <li>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</li> </ul>  |



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|  | <p>at its September 2016 meeting to commence standard-setting activities. The <a href="#">project proposal</a> 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 <a href="#">March meeting papers</a>.</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)<sup>2</sup>. 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>The ED was issued in July 2018 for public consultation.</p> <p>In March 2019 The Board discussed the ISA 315 Task Force's initial proposals to address specific responses to the proposed ISA 315 (Revised)<sup>2</sup> (<a href="#">ED-315</a>), in particular, the broad concerns in relation to the length and complexity of the standard. In doing so, the Board considered alternative approaches about how</p> |
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<sup>2</sup> Proposed ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*

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|  | <p>to present the requirements for the auditor's understanding of the entity's system of internal control.</p> <p>The Board agreed to move forward by presenting the requirements at a broader, higher level (i.e., in a more direct way in terms of focusing on the 'what' that is required from the auditor), while maintaining the robustness of the current standard. Accordingly, all of the requirements will be reconsidered, the criteria or matters that are definitional will be relocated to definitions, and the 'why' and 'how' will be further explicitly considered as to where it is appropriate to be moved to. The Board acknowledged that scalability was likely best addressed in the application material.</p> <p>The Board's discussions also focused on proposed changes to address specific issues within the section on understanding the entity's system of internal control, in particular, in relation to clarifications on controls relevant to the audit, the information system and control activities components, and the various evaluations required within this section of the standard.</p> <p>Aspects of ED-315 and related feedback that have not been addressed during this meeting will be presented at the June 2019 IAASB meeting. The ISA 315 Task Force will continue to progress the proposed changes to ED-315 with a targeted approval of the final standard at the September 2019 IAASB meeting.</p> <p>In June 2019, the Board discussed a full version of the standard reflecting the new drafting approach that was broadly supported with the Board at its March 2019 meeting. The Board broadly supported specific aspects of this approach, in particular the enhanced flow and understandability of the requirements, as well as the separate presentation or signposting of examples and scalability paragraphs in the application material.</p> <p>Notwithstanding broad support for the overall approach, concern was expressed about the change to move certain material (primarily criteria or terms previously included in requirements relating to the understanding of the system of internal control) to definitions. It was also highlighted that this could cause challenges in navigating the standard. The Board was presented with a revised approach to drafting the requirements for the understanding of the system of internal control, which reconnected the definitions, and the Board broadly supported moving forward.</p> <p>Specific other areas discussed and agreed include revisions to the definitions of significant risk and the inherent risk factors, specifically in relation to how fraud is presented within the inherent risk factors. Conforming amendments arising from the proposed changes to the standard will be discussed at an IAASB teleconference in August 2019 and a final draft of the proposed standard will be presented to the IAASB for approval at its September 2019 meeting.</p> <p>In September 2019, the Board approved the revisions to ISA 315 (Revised),<sup>1</sup> as well as the related conforming amendments. The revised ISA will be effective for audits of financial statements for periods beginning on or after December 15, 2021. Once the Public Interest Oversight Board's (PIOB) confirmation that due process was followed is received, the Board will formally release the standard. In finalizing ISA 315 (Revised), the Board continued to</p> |
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|  | <p>focus on the understandability and complexity of the ISA, as well as the iterative nature of the standard. The Board continued to discuss the threshold for identifying risks of material misstatement and agreed the supporting guidance for this as a conforming amendment to ISA 200.2 The Board also recognized that support is critical when initially applying the changes to ISA 315 (Revised) and will further consider the most appropriate actions in providing this initial support. The Board also acknowledged the need to monitor implementation challenges as they arise.</p>  |
| <p><b>Less Complex Entities</b></p> <p><b>No Update for the period</b></p> | <p>In March 2019 the Board discussed a proposed Discussion Paper (DP), <i>Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Implementing the ISAs</i>. The discussion highlighted the shift in focus on complexity of the entity rather than its size in driving the ongoing discussions and activities to address issues and challenges in audits of less complex entities (LCEs). The Board was supportive of the DP's overall direction, noting the importance of the project and the need for action by the IAASB and others.</p> <p>The Board liked the simple, clear way the DP had been presented and noted it was appropriate for its key target audience (i.e., auditors of LCEs). The Board made suggestions for improvements, particularly with respect to the issues and challenges, the possible actions presented within the DP and the questions to be posed to respondents in order to obtain relevant and useful feedback. Proposed changes to the DP will be presented in a Board call on April 10<sup>th</sup>, with the final DP targeted to be published for public consultation before the end of April 2019.</p> |
| <p><b>Audit Evidence has</b></p> <p><b>No Update for the period</b></p>    | <p>The Board discussed the analysis undertaken by the Audit Evidence Working Group of the issues across the ISAs related to audit evidence and the use of technology more broadly, and the possible actions to address the issues. The Board concurred that guidance should be developed on the effect of technology when applying certain aspects of the ISAs, and that this should be actioned expeditiously.</p> <p>The Board also indicated that more extensive information gathering and research need to be undertaken to understand the issues related to audit evidence, so that the Board is fully informed of the issues in determining the need for revisions to ISA 5005 and possibly other related standards.</p> <p>In September 2019, the Board was provided with an overview of the development of the Audit Evidence Workstream Plan. The Audit Evidence Working Group will accordingly undertake further information gathering and research, and develop recommendations for possible further actions to be presented to the Board in the first half of 2020.</p>  |

## Agenda Item 12.2



NZ AUDITING  
AND ASSURANCE  
STANDARDS BOARD

**DATE:** 22 November 2019

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

**FROM:** Peyman Momenan

**SUBJECT:** Domestic Update

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### **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 October to November 2019.

### **Financial Markets Authority (FMA)**

1. Audit quality has broadly improved again but auditors continue to apply standards inconsistently, the FMA's annual [Audit Quality Report 2019](#) has found.

The annual review is part of a three-year monitoring cycle of licensed auditors. Each of the audit firms reviewed for this report have been reviewed previously and the FMA found most auditors had made improvements.( read the rest of the article [here](#))

### **The New Zealand Institute of Chartered Accountants**

1. On 1 August 2019 the Senate referred an inquiry into the regulation of auditing in Australia to the Parliamentary Joint Committee on Corporations and Financial Services for report by 1 March 2020.

CA ANZ welcomes the inquiry as an opportunity for Australia to join the global discussion on the purpose of audit so we can continually evolve to meet modern stakeholder expectations. The CA ANZ submission to the inquiry can be accessed from [here](#).

2. For the first time, CA ANZ, with the help of the Center for Audit Quality in the United States, has commissioned research into the attitudes of New Zealand retail investors to discover who they trust, what keeps them up at night and how they view New Zealand's capital markets and companies.

[The survey](#) captured the views of just over 500 retail investors in New Zealand. The results show that they have healthy levels of confidence in New Zealand capital

markets and listed companies but are less confident in global capital markets due to concerns about global political uncertainty.

Ninety percent of retail investors have some level of confidence in the audited financial reports produced by New Zealand public companies. This confidence is driven by the trust that the investors have in independent auditors—the most trusted group for these investors—and other stakeholders in the markets such as regulators, audit committees and analysts.

**CPA Australia**

1. No update for the period.

**The Institute of Directors (IoD)**

1. No update for the period.