



1 August 2017

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

Dear Matt,

AUASB Submission on the IAASB's Proposed International Standard on Auditing ISA 540 (Revised)
Auditing Accounting Estimates and Related Disclosures

The Australian Auditing and Assurance Standards Board (AUASB) is pleased to have the opportunity to comment on the IAASB's Proposed International Standard on Auditing ISA 540 (Revised) *Auditing Accounting Estimates and Related Disclosures* ("ISA 540").

The AUASB commends the IAASB's initiative in continuing to foster audit quality and considers the area of accounting estimates and related disclosures to be an important part of that initiative. The AUASB is supportive of the intentions behind the IAASB's proposed revisions to ISA 540 and plan to improve audit quality by keeping the auditing and quality control standards relevant in the face of continually evolving business environments and pending accounting standard changes (in particular IFRS 9, 15 and 17).

Having reviewed the proposed changes and sought feedback from a wide range of stakeholders within Australia, the AUASB raises the following key points of particular importance for the IAASB's consideration which are elaborated on further in the detailed submission:

1. Accounting estimates are an integral part of financial reporting, often accounting for a large proportion of financial statement line items. Many estimates are complex, involve a significant amount of judgement and they can include significant estimation uncertainty. In some circumstances, the estimation uncertainty can lead to a range of possible outcomes that can be many multiples of materiality. In reality, it is not possible to bring greater precision to an estimate that is inherently imprecise under the applicable financial reporting framework.
2. The introduction of the term 'low inherent risk' is problematic given the lack of definition or parameters around what constitutes a low inherent risk as well as the disconnect to ISA 315 where the risk of material misstatement is what determines the nature, extent and timing of audit effort. Accordingly, the AUASB considers that the risk of material misstatement is a current approach for driving scalability rather than a new concept of inherent risk in isolation. Furthermore, the interpretation of this standard, and which estimates are captured, may be an impediment to the clear IAASB objective of scalability. Estimates by their nature are judgemental and based on the examples presented in the standard, it is questionable as to whether all but the simplest of estimates would have an inherent risk other than low associated with it.
3. When inherent risk is not considered to be low, it is likely that some estimates will fit into all 3 categories (complexity, judgement, estimation uncertainty) which we don't believe was the intention of the revised standard. This may lead to confusion as to the extent of audit effort, may limit the exercise of professional judgement and again may be an impediment to achieving scalability.

4. While improved and additional application material and illustrative examples may be beneficial, the AUASB considers that the standard, and in particular the application material, is too verbose. The verbosity of the standard increases the risk of the standard becoming overly prescriptive and rules based leading to a diminution of auditor's professional judgement and scepticism that may result in an unintended decline in audit quality.
5. In our view, the root cause of any perceived shortcomings in the application of professional skepticism in relation to accounting estimates and related disclosures may invariably be associated with inadequate audit evidence provided to auditors by management and those charged with governance and accordingly may not necessarily be addressed solely through the revision to auditing standards. Stakeholders are concerned that greater onus is being placed on the auditor than the preparer, and the standard appears to be heading down the path of expected re-performance by auditors.

In formulating its response, the AUASB has sought input from its constituents in three principal ways. The first was from hosting a roundtable meeting with stakeholders in three of the large Australian cities - stakeholders that represent a broad range of backgrounds including assurance providers from medium and large audit firms, audit regulators, professional accounting bodies, directors, preparers and users of financial statements. The second was through an open invitation to provide comments placed on the AUASB website; and the third was by way of subsequent formal discussions by the AUASB members at recent board meetings.

The AUASB's detailed responses to the specific questions asked in the Exposure Draft accompany this letter as Attachment 1.

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

Yours sincerely,

Roger Simnett
Chair