



# AUASB Board Meeting Summary Paper

**AGENDA ITEM NO.** 3.1  
**Meeting Date:** 4 February 2020  
**Subject:** ED ASRS 4400 *Agreed-Upon Procedures Engagements*  
**Date Prepared:** 18 December 2019  
**Prepared By:** Rene Herman

☒ **Action Required**

☐ **For Information Purposes Only**

## Agenda Item Objectives

1. For the AUASB to consider and approve:
  - (a) The use of the term practitioner Exposure Draft 01/20 ASRS 4400 *Agreed-Upon Procedures Engagements* (ED 01/20) – refer paragraph 5 of this paper.
  - (b) Exposure Draft 01/20 ASRS 4400 *Agreed-Upon Procedures Engagements* (ED 01/20) (Agenda Item 3.1.2); and
  - (c) Explanatory Memorandum accompanying ED 01/20 (Agenda Item 3.1.1) including the questions to be asked on exposure.

## Background

1. In November 2018, the IAASB issued Exposure Draft ISRS 4400 (Revised) *Agreed-Upon Procedures Engagements*, with comments due by 15 March 2019.
2. In December 2018, the AUASB issued a Consultation Paper seeking feedback on the IAASB's Exposure Draft on ISRS 4400 and, in March 2019, the AUASB made a written submission to the IAASB in response to ED ISRS 4400.
3. This project was completed by the IAASB in December 2019 with the IAASB approving a revised ISRS 4400 at the December 2019 IAASB meeting.
4. The AUASB has been tracking the progress of the revision of ISRS 4400 in relation to the AUASB's three main areas of concern, those being: professional judgement, independence and restriction on use of report. The ATG reported back to the AUASB on these matters at the 3 December 2019 AUASB meeting (3 December 2019, Agenda Item 16.1.0). At that meeting the ATG flagged some possible questions that could be addressed to Australian stakeholders on Exposure, focusing on independence,

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

restriction on use of the AUP report and the exercise of professional judgement. Those questions have been included in the Explanatory Memorandum at Agenda Item 3.1.1.

5. ED 01/20 has been compiled based on a 'final draft' of ISRS 4400 as approved and agreed at the December 2019 IAASB meeting. This ISRS 4400 draft is still subject to numbering, referencing, formatting and final editorials before the IAASB submits this draft for PIOB approval. Accordingly, the AUASB technical team expects that there may be some numbering/referencing and minor editorial amendments that are still to be processed by the IAASB. These will all be picked up by the AUASB when the final ISRS 4400 is approved by the PIOB. The AUASB technical team is not expecting any changes in substance or content and as a consequence the AUASB technical team considers that the ED can be issued in its current form – refer paragraph 13 of the Explanatory Memorandum.

## **Matters to Consider**

### ***Part A - Specific***

6. The proposed ED 01/20 deals with the **practitioner's** responsibilities in relation to AUP engagements. The AUASB is directed to the definition of practitioner in ED 01/20, paragraph 13(h):

*Practitioner – The individual(s) conducting the engagement (usually the engagement partner or other members of the engagement team, or, as applicable, the firm). Where this ASRS expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term "engagement partner" rather than "practitioner" is used.*

The AUASB is requested to consider the use of this term in light of the extant ASRS 4400 using the term **assurance practitioner**, defined in extant ASRS 4400 as “a person or an organisation, whether in public practice, industry, commerce or the public sector, involved in the provision of assurance services.”

AUP engagements are not assurance engagements, accordingly the AUASB technical group supports the use of the term practitioner as defined in ED 01/20 paragraph 13(h).

### ***Part B – General***

7. ED 01/20 is the Australian equivalent of the IAASB's Revised ISRS 4400 as approved by the IAASB at its December 2019 IAASB meeting.
8. Explanatory Memorandum *Exposure Draft 01/20: Proposed Standard on Related Services ASRS 4400 Agreed-Upon Procedures Engagements* will accompany ED 01/20 and includes questions on exposure, specific to Australian stakeholders.
9. Compelling reasons, if any, to modify ISRS 4400 will be considered further before finalising the final ASRS 4400, and after feedback is received from Australian stakeholders.

### ***Part C – Timeline***

10. Issue ED ASRS 4400 for a 50-day comment period ending 31 March 2020.
11. Proposed disposition of comments and a working draft of the Standard to be brought to the April 2020 AUASB meeting for consideration of disposition of comments received, feeding into the final Australian standard.
12. The final proposed ASRS 4400 will be brought to the June 2020 meeting for approval to issue.

#### ***Part D – NZAuASB***

13. The NZAuASBs mandate in relation to related service standards changed late 2019. The NZAuASB plan to take an ED on ISRS 4400 to the April 2020 NZAuASB meeting. The AUASB technical team will co-ordinate and discuss the proposed revised standard with the NZAuASB technical team as this project progresses.

#### ***Part E – “Compelling Reasons” Assessment***

14. Compelling reasons will be reassessed after consideration of submissions received from Australian stakeholders, and after AUASB discussion at the 21 April 2020 AUASB meeting.

#### **AUASB Actions**

15. Read, consider and vote to issue:
  - (a) Explanatory Memorandum *Exposure Draft 01/20: Proposed Standard on Related Services ASRS 4400 Agreed-Upon Procedures Engagements*; and
  - (b) Exposure Draft 01/20 ASRS 4400 *Agreed-Upon Procedures Engagements* (ED 01/20)
16. Consider if any other questions should be included in ED 01/20.

#### **AUASB Technical Group Recommendations**

17. The AUASB approve ED 01/20 and the supporting Explanatory Memorandum for issue; with a comment period of 50 days.

#### **Material Presented**

Agenda Item 3.1	Feb20_3.1.0_BMSP_ED_ASRS4400
Agenda Item 3.1.1	Feb20_3.1.1_Explanatory Memorandum_ED0120
Agenda Item 3.1.2	Feb20_3.1.2_ED_01-20_Proposed_ASRS4400

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February 2020

# Explanatory Memorandum

## *Exposure Draft 01/20: Proposed Standard on Related Services ASRS 4400 Agreed- Upon Procedures Engagements*

Issued by the Auditing and Assurance Standards Board



Australian Government

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Auditing and Assurance Standards Board

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*Important Note and Disclaimer*

This Explanatory Memorandum is issued by the AUASB to provide information to auditors and assurance practitioners about the AUASB's implementation in Australia of the International Auditing and Assurance Standards Board's (IAASB's) revised International Standard on Related Services (ISRS) 4400 *Agreed-Upon Procedures Engagements*.

This Explanatory Memorandum does not establish or extend the requirements under an existing AUASB Standard(s) and is not intended to be a substitute for compliance with the relevant AUASB Standards with which auditors and assurance practitioners are required to comply when conducting an audit or other assurance engagement. No responsibility is taken for the results of actions or omissions to act on the basis of any information contained in this document or for any errors or omissions in it.

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## **EXPLANATORY MEMORANDUM**

### ***Exposure Draft 01/20: Proposed Standard on Related Services ASRS 4400 Agreed-Upon Procedures Engagements***

#### **Purpose**

1. The aim of this Explanatory Memorandum is to:
  - a) provide stakeholders with information about Exposure Draft ED 01/20, issued in February 2020, and the Auditing and Assurance Standards Board's (AUASB) approach to implementing the International Auditing and Assurance Standards Board's (IAASB) Revised International Standard on Related Services (ISRS) 4400 *Agreed-Upon Procedures Engagements* (ISRS 4400) in Australia; and
  - b) seek stakeholder feedback on the Exposure Draft.

#### **Background**

##### **IAASB**

2. Agreed-Upon Procedures (AUP) Engagements are widely used and the superseded ISRS 4400 was developed over 20 years ago. In September 2017, the IAASB approved a project proposal to revise extant ISRS 4400 to address issues relating to AUP engagements.
3. This project was completed in December 2019 with the IAASB approving a revised ISRS 4400 at the December 2019 IAASB meeting.
4. The key changes and concepts in the revised ISRS 4400 include:
  - c) Professional judgment — new requirement and application material on the role of professional judgment in an AUP engagement.
  - d) Independence — new requirements and application material on disclosures in the AUP report relating to the practitioner's independence.
  - e) Engagement acceptance and continuance considerations — new requirements and application material addressing conditions for engagement acceptance and continuance, including guidance on what constitutes appropriate (or inappropriate) terminology to describe procedures and findings in AUP reports.
  - f) Use of a practitioner's expert — new requirements and application material to address the use of the work of a practitioner's expert in an AUP engagement, including the practitioner's responsibilities when using the work of an expert.
  - g) AUP report restrictions — clarification that the AUP report is not restricted to parties that have agreed to the procedures to be performed unless the practitioner decides to do so, and new application material on the practitioner's considerations if the practitioner wishes to place restrictions on the AUP report.
  - h) ISRS 4400 also addresses non-financial subject matters, and includes new definitions and new requirements and application material on written representations, recommendations arising from the performance of AUP engagements, and documentation, among others.



5. ISRS 4400 contains a number of paragraphs relating to quality control. The IAASB is currently undertaking a project to revise ISQC 1.<sup>1</sup> The paragraphs in ISRS 4400 relating to quality control are likely to be updated through conforming amendments arising from the finalisation of ISQM 1.

## **AUASB**

### *Feedback to IAASB*

6. In December 2018, the AUASB issued a [Consultation Paper](#) seeking feedback on the IAASB's Exposure Draft on ISRS 4400.
7. In March 2019, the AUASB made a [written submission](#) to the IAASB in response to ED ISRS 4400. In formulating its response, the AUASB sought input from its stakeholders in three principal ways. Firstly, from hosting a webinar that was attended by over 50 stakeholders representing a broad range of backgrounds, including assurance providers from a range of audit firms, professional accounting bodies, academics, those charged with governance and preparers of financial statements. Secondly, through an open invitation to provide comments on the AUASB issued Consultation Paper on this topic via the AUASB website. Finally, formal discussions and deliberations by AUASB members at AUASB meetings. The main themes expressed by the AUASB in their submission to the IAASB included:
- (a) *Independence*: The AUASB supported the proposed ED ISRS 4400 not including a precondition for the practitioner to be independent. However, where independence is required by law or regulation, the AUASB considered that there should be a requirement for the practitioner to disclose the criteria/framework used by the practitioner to assess independence. Paragraph 9(a)(ii) below describes where the IAASB settled in relation to independence in AUP engagements.
  - (b) *Restriction on use*: The AUASB considered that the use of an AUP report should be restricted to parties that have agreed to the procedures performed or have been identified as intended users in the report. Paragraph 9(b)(ii) below describes where the IAASB settled in relation to restriction of use of AUP reports.
  - (c) *Professional judgement*: The AUASB recommended that the proposed ED ISRS 4400 include a clearer requirement in relation to the exercise of professional judgement than what was put forward in the exposure draft. Paragraph 9(c)(ii) below describes where the IAASB settled in relation to the exercise of professional judgement in AUP engagements.
8. The AUASB has closely followed the activities of the IAASB in their revisions to ED ISRS 4400 and consider that the majority of feedback generated by Australian stakeholders has been addressed in the final revised ISRS 4400.

### *Main Differences between ED ASRS 4400 (based on Revised ISRS 4400) and extant ASRS 4400*

9. ED ASRS 4400 (based on the Revised ISRS 4400) largely aligns with ASRS 4400, with the main points of difference being:
- a) *Independence*
    - i. **Extant ASRS 4400** has a requirement for the practitioner to be independent **equivalent to the independence requirement applicable to 'other assurance engagements'**, unless the engaging party has explicitly agreed to modified

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<sup>1</sup> International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*

independence requirements. If modified independence is agreed, the level of independence applied is described in the AUP report.

- ii. **ED 01/20 does not require independence** for an AUP engagement and the AUP report includes one of two statements addressing circumstances when the practitioner is, or is not, required to be independent:
  - If the practitioner is not required to be independent and has not otherwise agreed in the terms of engagement to comply with independence requirements, a statement that, for the purpose of the engagement there are no independence requirements with which the practitioner is required to comply; or
  - If the practitioner is required to be independent or has agreed in the terms of engagement to comply with independence requirements, a statement that the practitioner has complied with the relevant independence requirements. The statement shall identify the relevant independence requirements.
- iii. The AUASB has specifically asked stakeholders' views on this matter – refer paragraph 18, section A, question 1 and 2 of this Explanatory Memorandum.

b) *Restriction on use*

- i. **Extant ASRS 4400 restricts the use** of an AUP report to those parties that have either agreed to the procedures to be performed or have been specifically included as users in the engagement letter. A restriction on use paragraph is required to be included in an AUP report.
- ii. **ED 01/20 does not restrict** the AUP report to parties that have agreed to the procedures to be performed, but rather the report contains a statement identifying the purpose of the report and that the report may not be suitable for another purpose.
- iii. The AUASB has specifically asked stakeholders views on this matter – refer paragraph 18, section A, question 3 and 4 of this Explanatory Memorandum.

c) *Professional Judgement*

- i. **Extant ASRS 4400** explicitly states that the assurance practitioner is **not be required**, during the course of the engagement, **to exercise professional judgement** in determining or modifying the procedures to be performed.
- ii. **ED 01/20** requires that **‘the practitioner shall exercise professional judgment** in accepting, conducting and reporting on an agreed-upon procedures engagement, taking into account the circumstances of the engagement.’

To clarify where, and how, professional judgment is exercised in an AUP engagement without implying that professional judgment is ever ‘suspended’ or ‘prohibited’, ED 01/20:

- Includes examples and subheadings in the application material to better demonstrate how professional judgment may be exercised when accepting, conducting and reporting on the AUP engagement;
- Clarifies, in the examples within the application material under ‘Conducting the engagement’ (in paragraph A15), that the practitioner is more likely to exercise professional judgment in determining an

- appropriate action or response resulting from performing the procedures, as opposed to during the performance of the specific procedures.
  - Explains in the application material (paragraph A16) the reasons why, in conducting the engagement, the need for the practitioner to exercise professional judgment when performing AUP is limited.
- iii. The AUASB has specifically asked stakeholders views on this matter – refer paragraph 18, section A, question 5 of this Explanatory Memorandum.

#### *AUASB Due Process*

10. In accordance with its mandates under section 227 of the *Australian Securities and Investments Commission Act 2001* and the Financial Reporting Council's (FRC) Strategic Direction, the AUASB's policy is to adopt the IAASB's auditing standards (ISAs), unless there are compelling reasons not to do so; and to amend the ISAs only when there are compelling reasons to do so. The AUASB's principles of convergence with the ISAs and harmonisation with the standards of the New Zealand Auditing and Assurance Standards Board (NZAuASB) can be found on the AUASB's website: [http://www.auasb.gov.au/admin/file/content102/c3/Aug14\\_IAASB-NZAuASB\\_Principles\\_of\\_Convergence\\_and\\_Harmonisation.pdf](http://www.auasb.gov.au/admin/file/content102/c3/Aug14_IAASB-NZAuASB_Principles_of_Convergence_and_Harmonisation.pdf)

While ASRS 4400 is not an Australian Auditing Standard as described in the Foreword to AUASB Pronouncements, the AUASB considers it to be in the public interest to follow the same mandate in relation to related services engagements.

11. Compelling reasons fall broadly into two categories: legal and regulatory; and principles and practices considered appropriate in maintaining or improving audit quality in Australia. Compelling reasons are further guided by the AUASB's policy of harmonisation with the standards of the NZAuASB.
12. Based on its mandate, the AUASB intend to adopt the revised ISRS 4400, relating to AUP Engagements. Prior to implementation, the AUASB is required to consult with stakeholders and, accordingly, now issues Exposure Draft ED 01/20.
13. ED 01/20 has been compiled based on a 'final draft' of ISRS 4400 as agreed at the December 2019 IAASB meeting. This ISRS 4400 draft is still subject to numbering, referencing, formatting and final editorials before the IAASB submits this draft for PIOB approval. Accordingly, the AUASB expects that there may be some numbering/referencing and minor editorial amendments that are still to be processed by the IAASB. These will all be picked up by the AUASB when the final ISRS 4400 is approved by the PIOB. The AUASB is not expecting any changes in substance or content and as a consequence considers that ED 01/20 can be issued in its current form.
14. The AUASB has historically exposed Australian versions of the finalised IAASB standard. This is the process that will be undertaken in connection with the issuance of ED 01/20. ED 01/20 is the Australian Exposure Draft of the final revised IAASB's ISRS 4400. Feedback on ED 01/20 will be used to inform the AUASB as to any requirements and guidance that may be needed in addition to, or a clarification of, the equivalent ISRS, only when there are compelling reasons to do so. At the completion of the exposure period, the AUASB will consider stakeholders' submissions and, where the AUASB determines that a compelling reason exists, amendments to the exposure draft will be made.

#### *Exposure Draft Protocols*

15. Under its convergence policies, the AUASB continues to include requirements and guidance that are in addition to, or a clarification of, the equivalent ISA (in this case ISRS) only when the compelling reason test has been met. Any such modifications will be identified in the Related

Services Engagements Standard by paragraph numbering commencing with an ‘Aus’ prefix. Any such changes do not diminish the requirements of the equivalent ISRS.

16. In addition to those changes that meet the compelling reason test, the AUASB makes format and terminology changes to comply with requirements relating primarily to legislative instruments. Such changes are machinery in nature and do not change the meaning of the equivalent ISRS.

#### *AUASB Modifications to the ISRS*

17. At this time, in line with the AUASB’s policy of convergence with the standards of the IAASB (see link at paragraph 10 above), the AUASB is not proposing any modification to ISRS 4400 (Revised). However, the AUASB has asked specific questions on exposure (refer paragraph 18 of this Explanatory Memorandum) for stakeholders’ consideration and comment. After such feedback is received, the AUASB will deliberate the need for any compelling reason amendments.

### **Request for Comments**

18. The AUASB requests comments on all matters in relation to ED 01/20, but specifically in relation to the questions below. Stakeholders may address only specific questions relevant to them or raise matters not specifically addressed by a questions.

#### **Exposure Draft Questions**

A. The AUASB is particularly interested in stakeholders views on:

*Independence (Refer paragraph 9(a) of this Explanatory Memorandum for more information):*

1. Do stakeholders support ED-ASRS 4400 not requiring independence for an AUP engagement, with the AUP report including statements addressing circumstances when the practitioner is or is not required to be independent?
2. Would stakeholders prefer a different approach be adopted in Australia equivalent to extant ASRS 4400 whereby there is an independence requirement for the practitioner equivalent to the independence requirement applicable to ‘other assurance engagements’’, unless the engaging party has explicitly agreed to modified independence requirements?

*Restriction on use (Refer paragraph 9(b) of this Explanatory Memorandum for more information).:*

3. Do stakeholders support ED-ASRS 4400 not restricting the AUP report to parties that have agreed to the procedures to be performed, but rather the report containing a statement identifying the purpose of the report and that the report may not be suitable for another purpose?
4. Would stakeholders prefer a different approach to be adopted in Australia equivalent to extant ASRS 4400 whereby the use of an AUP report is restricted to those parties that have either agreed to the procedures to be performed or have been specifically included as users in the engagement letter. Under ASRS 4400, a restriction on use paragraph is required to be included in an AUP report.

*Professional judgement (Refer paragraph 9(c) of this Explanatory Memorandum for more information):*

5. Do stakeholders support the way in which the exercise of professional judgement is dealt with in ED-ASRS 4400?

- B. The AUASB is also interested in stakeholders views on:
- (a) Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?
  - (b) Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?
  - (c) What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:
    - (i) Where those costs are likely to occur;
    - (ii) The estimated extent of costs, in percentage terms (relative to audit fee); and
    - (iii) Whether expected costs outweigh the benefits to the users of audit services?
  - (d) Are there any other significant public interest matters that stakeholders wish to raise?

### **Other Outreach Activities**

18. The AUASB intend to conduct a Webinar explaining the details of the proposed ED-ASRS 4400 in March 2020.

### **Application**

19. The revised standard will be applicable for agreed-upon procedures engagements for which the terms of engagement are agreed on or after **1 January 2022**. This application date corresponds with that of the equivalent ISRS.

#### *Early Adoption*

20. Consistent with the IAASB's policy, all AUASB Standards may be adopted early unless explicitly prohibited.

### **Comment Date**

21. ED 01/20 will be open to stakeholders for a **50 day comment period, closing 31 April 2020**.
22. At the completion of the exposure period, the AUASB will consider stakeholders' submissions and, where the AUASB determines that compelling reasons exist, amendments to the exposure draft will be made.

### **Website Resources**

23. The AUASB welcomes stakeholders input to the development of Australian Auditing Standards and regards both supportive and critical comments as essential to a balanced review of the proposed standards. Stakeholders are encouraged to access the websites of the [AUASB](#) and the [IAASB](#) to obtain further information.

\* \*

EXPOSURE DRAFT

**ED 01/20**

(February 2020)

# **Proposed Standard on Related Services**

## **ASRS 4400**

### ***Agreed-Upon Procedures Engagements***

Issued for Comment by the **Auditing and Assurance Standards Board**



**Australian Government**

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**Auditing and Assurance Standards Board**

## **Commenting on this Exposure Draft**

Comments on this Exposure Draft should be received by no later than 4 April 2020. Comments should be addressed to:

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

## **Formal Submissions**

Submissions should be lodged online via the “Work in Progress-Open for Comment” page of the Auditing and Assurance Standards Board (AUASB) website ([www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx](http://www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx)) as a PDF document and Word document.

A copy of all non-confidential submissions will be placed on public record on the AUASB website: [www.auasb.gov.au](http://www.auasb.gov.au)

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**Proposed Standard on Related Services ASRS 4400**  
***Agreed-Upon Procedures Engagements***

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## PREFACE

### Reasons for Issuing ED 01/20

The AUASB issues exposure draft ED 01/20 of proposed Standard on Related Services ASRS 4400 *Agreed-Upon Procedures Engagements* pursuant to the requirements of the legislative provisions explained below.

The AUASB is a non corporate Commonwealth entity of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 227B of the ASIC Act, the AUASB may formulate assurance standards for other purposes.

### Main Proposals

This proposed Standard on Related Services represents the Australian equivalent of the IAASB's revised ISRS 4400 *Agreed-Upon Procedures Engagements* and will replace the current ASRS 4400 issued by the AUASB in July 2013.

This proposed Standard on Related Services contains differences from the current ASRS 4400, which are detailed in the Explanatory Memorandum located at the front of Proposed ASRS 4400.

### Proposed Operative Date

It is intended that this proposed Standard on Related Services will be operative for agreed-upon procedures engagements for which the terms of engagement are agreed on or after 1 January 2022 (Ref: Para. A9).

### Main changes from existing ASRS 4400 *Agreed-Upon Procedures Engagements to Report Factual Findings* (July 2013)

The main differences between this proposed Standard on Related Services and the Standard on Related Services that it supersedes, ASRS 4400 *Agreed-Upon Procedures Engagements to Report Factual Findings* (July 2013), are included in the Explanatory Memorandum located in the front of the Proposed ASRS 4400.

### Request for Comments

Comments are invited on this Exposure Draft of the proposed re-issuance of ASRS 4400 *Agreed-Upon Procedures Engagements* by no later than 31 April 2020. The AUASB is seeking comments from respondents on the following questions:

**Exposure Draft Questions**

A. The AUASB is particularly interested in stakeholders views on:

*Independence (Refer paragraph 9(a) of this Explanatory Memorandum for more information):*

1. Do stakeholders support ED-ASRS 4400 not requiring independence for an AUP engagement, with the AUP report including statements addressing circumstances when the practitioner is or is not required to be independent?
2. Would stakeholders prefer a different approach be adopted in Australia equivalent to extant ASRS 4400 whereby there is an independence requirement for the practitioner equivalent to the independence requirement applicable to 'other assurance engagements', unless the engaging party has explicitly agreed to modified independence requirements?

*Restriction on use (Refer paragraph 9(b) of this Explanatory Memorandum for more information).:*

3. Do stakeholders support ED-ASRS 4400 not restricting the AUP report to parties that have agreed to the procedures to be performed, but rather the report containing a statement identifying the purpose of the report and that the report may not be suitable for another purpose?
4. Would stakeholders prefer a different approach to be adopted in Australia equivalent to extant ASRS 4400 whereby the use of an AUP report is restricted to those parties that have either agreed to the procedures to be performed or have been specifically included as users in the engagement letter. Under ASRS 4400, a restriction on use paragraph is required to be included in an AUP report.

*Professional judgement (Refer paragraph 9(c) of this Explanatory Memorandum for more information):*

5. Do stakeholders support the way in which the exercise of professional judgement is dealt with in ED-ASRS 4400?

- B. The AUASB is also interested in stakeholders views on:
1. Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?
  2. Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?
  3. What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:
    - (i) Where those costs are likely to occur;
    - (ii) The estimated extent of costs, in percentage terms (relative to audit fee); and
    - (iii) Whether expected costs outweigh the benefits to the users of audit services?
  4. Are there any other significant public interest matters that stakeholders wish to raise?

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) formulates this Standard on Related Services ASRS 4400 *Agreed-Upon Procedures Engagements* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*.

This Standard on Related Services is to be read in conjunction with ASA 100 *Preamble to AUASB Standards*, which sets out the intentions of the AUASB on how the AUASB Standards are to be understood, interpreted and applied.

## **Conformity with International Standards on Related Services**

This Standard on Related Services conforms with International Standard on Related Services ISRS 4400 issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that are expected to be added/deleted/amended to this Standard on Related Services are identified with the prefix “Aus”.

Compliance with this Standard on Related Services enables compliance with ISRS 4400.

# STANDARD ON RELATED SERVICES ASRS 4400

## *Agreed-Upon Procedures Engagements*

The grey shaded materials relate to Australian Standard on Quality Control (ASQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial information, Other Assurance Engagements and Related Services Engagements*. These grey shaded materials are subject to change to align with the revisions to the Quality Suite of Standards, currently under revision by the IAASB.

### **Introduction**

#### **Scope of this ASRS**

1. This Australian Standard on Related Services (ASRS) deals with:
  - (a) The practitioner's responsibilities when engaged to perform an agreed-upon procedures engagement; and
  - (b) The form and content of the agreed-upon procedures report.
2. This ASRS applies to the performance of agreed-upon procedures engagements on financial or non-financial subject matters. (Ref: Para. A1–A2)

#### ***Relationship with ASQC1<sup>1</sup>***

3. Quality control systems, policies and procedures are the responsibility of the firm. ASQC 1 applies to firms that perform Related Services Engagements of professional accountants in respect of a firm's agreed-upon procedures engagements. The provisions of this ASRS regarding quality control at the level of individual agreed-upon procedures engagements are premised on the basis that the firm is subject to ASQC 1 or requirements that are at least as demanding. (Ref: Para. A3–A8)

#### **The Agreed-Upon Procedures Engagement**

4. In an agreed-upon procedures engagement, the practitioner performs the procedures that have been agreed upon by the practitioner and the engaging party, where the engaging party has acknowledged that the procedures performed are appropriate for the purpose of the engagement. The practitioner communicates the agreed-upon procedures performed and the related findings in the agreed-upon procedures report. The engaging party and other intended users consider for themselves the agreed-upon procedures and findings reported by the practitioner and draw their own conclusions from the work performed by the practitioner.
5. The value of an agreed-upon procedures engagement performed in accordance with this ASRS results from:
  - (a) The practitioner's compliance with professional standards, including relevant ethical requirements; and
  - (b) Clear communication of the procedures performed and the related findings.

<sup>1</sup> Australian Standard on Quality Control ASQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial information, Other Assurance Engagements and Related Services Engagements*.

6. An agreed-upon procedures engagement is not an audit, review or other assurance engagement. An agreed-upon procedures engagement does not involve obtaining evidence for the purpose of the practitioner expressing an opinion or an assurance conclusion in any form.

#### **Authority of this ASRS**

7. This ASRS contains the objectives of the practitioner in following the ASRS, which provide the context in which the requirements of this ASRS are set. The objectives are intended to assist the practitioner in understanding what needs to be accomplished in an agreed-upon procedures engagement.
8. This ASRS contains requirements, expressed using “shall,” that are designed to enable the practitioner to meet the stated objectives.
9. In addition, this ASRS contains introductory material, definitions, and application and other explanatory material, that provide context relevant to a proper understanding of this ASRS.
10. The application and other explanatory material provides further explanation of the requirements and guidance for carrying them out. While such guidance does not in itself impose a requirement, it is relevant to the proper application of the requirements. The application and other explanatory material may also provide background information on matters addressed in this ASRS that assists in the application of the requirements.

#### **Operative Date**

11. This ASRS is effective for agreed-upon procedures engagements for which the terms of engagement are agreed on or after 1 January 2022. (Ref: Para. A9)

#### **Objectives**

12. The practitioner’s objectives in an agreed-upon procedures engagement under this ASRS are to:
- (a) Agree with the engaging party the procedures to be performed;
  - (b) Perform the agreed-upon procedures; and
  - (c) Communicate the procedures performed and the related findings in accordance with the requirements of this ASRS.

#### **Definitions**

13. For purposes of this ASRS, the following terms have the meanings attributed below:
- (a) Agreed-upon procedures – Procedures that have been agreed to by the practitioner and the engaging party (and if relevant, other parties). (Ref: Para. A10)
  - (b) Agreed-upon procedures engagement – An engagement in which a practitioner is engaged to carry out procedures to which the practitioner and the engaging party (and if relevant, other parties) have agreed and to communicate the procedures performed and the related findings in an agreed-upon procedures report. (Ref: Para. A10)
  - (c) Engagement partner – The partner or other person in the firm who is responsible for the engagement and its performance, and for the agreed-upon procedures report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.
  - (d) Engaging party – The party(ies) that engage(s) the practitioner to perform the agreed-upon procedures engagement. (Ref: Para. A11)



- (e) Engagement team – All partners and staff performing the agreed-upon procedures engagement, and any individuals engaged by the firm or a network firm who perform procedures on the engagement. This excludes a practitioner's external expert engaged by the firm or a network firm.
- (f) Findings – Findings are the factual results of agreed-upon procedures performed. Findings are capable of being objectively verified. References to findings in this ASRS exclude opinions or conclusions in any form as well as any recommendations that the practitioner may make. (Ref: Para. A12–A13)
- (g) Intended users – The individual(s) or organisation(s), or group(s) that the practitioner expects will use the agreed-upon procedures report. In some cases, there may be intended users other than those to whom the agreed-upon procedures report is addressed. (Ref: Para. A10)
- (h) Practitioner – The individual(s) conducting the engagement (usually the engagement partner or other members of the engagement team, or, as applicable, the firm). Where this ASRS expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term "engagement partner" rather than "practitioner" is used.
- (i) Practitioner's expert – An individual or organisation possessing expertise in a field other than assurance and related services, whose work in that field is used to assist the practitioner in fulfilling the practitioner's responsibilities for the agreed-upon procedures engagement. A practitioner's expert may be either a practitioner's internal expert (who is a partner or staff, including temporary staff, of the practitioner's firm or a network firm) or a practitioner's external expert.
- (j) Professional judgement - The application of relevant training, knowledge and experience, within the context provided by this ASRS and relevant ethical requirements, in making informed decisions about the courses of action that are appropriate in the circumstances of the agreed-upon procedures engagement.
- (k) Relevant ethical requirements – Ethical requirements the engagement team is subject to when undertaking agreed-upon procedures engagements. These requirements ordinarily comprise the Accounting Professional & Ethical Standards Board (APESB)'s *Code of Ethics for Professional Accountants (including Australian Independence Standards)* (APESB Code) together with national requirements that are more restrictive.
- (l) Responsible party - The party(ies) responsible for the subject matter on which the agreed-upon procedures are performed.

## **Requirements**

### **Conduct of an Agreed-Upon Procedures Engagement in Accordance with this ASRS**

- 14. The practitioner shall have an understanding of the entire text of this ASRS, including its application and other explanatory material, to understand its objectives and to apply its requirements properly.

#### *Complying with Relevant Requirements*

- 15. The practitioner shall comply with each requirement of this ASRS unless a particular requirement is not relevant to the agreed-upon procedures engagement, for example, if the circumstances addressed by the requirement do not exist in the engagement.
- 16. The practitioner shall not represent compliance with this ASRS unless the practitioner has complied with all requirements of this ASRS relevant to the agreed-upon procedures engagement.

### **Relevant Ethical Requirements**

17. The practitioner shall comply with relevant ethical requirements. (Ref: Para. A14–A20)

### **Professional Judgement**

18. The practitioner shall exercise professional judgement in accepting, conducting and reporting on an agreed-upon procedures engagement, taking into account the circumstances of the engagement. (Ref: Para. A21–A23)

### **Engagement Level Quality Control**

19. The engagement partner shall take responsibility for:
- (a) The overall quality of the agreed-upon procedures engagement including, if applicable, work performed by a practitioner's expert; and (Ref: Para. A24)
  - (b) The engagement being performed in accordance with the firm's quality control policies and procedures by:
    - (i) Following appropriate procedures regarding the acceptance and continuance of client relationships and engagements; (Ref: Para. A25)
    - (ii) Being satisfied that the engagement team, and any practitioner's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to perform the agreed-upon procedures engagement;
    - (iii) Being alert for indications of non-compliance by members of the engagement team with relevant ethical requirements, and determining the appropriate actions 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. A26)
    - (iv) Directing, supervising and performing the engagement in compliance with professional standards and applicable legal and regulatory requirements; and
    - (v) Taking responsibility for appropriate engagement documentation being maintained.
20. If the work of a practitioner's expert is to be used, the engagement partner shall be satisfied that the practitioner will be able to be involved in the work of a practitioner's expert to an extent that is sufficient to take responsibility for the findings included in the agreed-upon procedures report. (Ref: Para. A27)

### **Engagement Acceptance and Continuance**

21. Before accepting or continuing an agreed-upon procedures engagement, the practitioner shall obtain an understanding of the purpose of the engagement. The practitioner shall not accept or continue the engagement if the practitioner is aware of any facts or circumstances indicating that the procedures the practitioner is being asked to perform are inappropriate for the purpose of the agreed-upon procedures engagement: (Ref: Para. A28–A31)
22. The practitioner shall accept or continue the agreed-upon procedures engagement only when: (Ref: Para. A28–A31)
- (a) The engaging party acknowledges that the expected procedures to be performed by the practitioner are appropriate for the purpose of the engagement;

- (b) The practitioner expects to be able to obtain the information necessary to perform the agreed-upon procedures;
  - (c) The agreed-upon procedures and related findings can be described objectively, in terms that are clear, not misleading, and not subject to varying interpretations; (Ref: Para. A32-A36)
  - (d) The practitioner has no reason to believe that relevant ethical requirements will not be complied with; and
  - (e) If the practitioner is required to comply with independence requirements, the practitioner has no reason to believe that the independence requirements will not be complied with. (Ref: Para. A37-A38)
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 necessary action.

#### **Agreeing the Terms of the Engagement**

24. The practitioner shall agree the terms of the agreed-upon procedures engagement with the engaging party and record the agreed terms of engagement in an engagement letter or other suitable form of written agreement. These terms shall include the following: (Ref: Para. A39-A40)
- (a) Identification of the subject matter(s) on which the agreed-upon procedures will be performed;
  - (b) The purpose of the engagement and the intended users of the agreed-upon procedures report as identified by the engaging party;
  - (c) If applicable, the responsible party as identified by the engaging party, and a statement that the agreed-upon procedures engagement is performed on the basis that the responsible party is responsible for the subject matter on which the agreed-upon procedures are performed;
  - (d) Acknowledgement of the relevant ethical requirements with which the practitioner will comply in conducting the agreed-upon procedures engagement;
  - (e) A statement as to whether the practitioner is required to comply with independence requirements and, if so, the relevant independence requirements; (Ref: Para. A37-A38)
  - (f) The nature of the agreed-upon procedures engagement, including statements that:
    - (i) An agreed-upon procedures engagement involves the practitioner performing the procedures agreed with the engaging party (and if relevant, other parties), and reporting the findings; (Ref: Para. A10)
    - (ii) Findings are the factual results of the agreed-upon procedures performed; and
    - (iii) An agreed-upon procedures engagement is not an assurance engagement and accordingly, the practitioner does not express an opinion or an assurance conclusion;
  - (g) Acknowledgement by the engaging party (and if relevant, other parties) that the agreed-upon procedures are appropriate for the purpose of the engagement; (Ref: Para. A10)
  - (h) Identification of the addressee of the agreed-upon procedures report;

- (i) The nature, timing and extent of the procedures to be performed, described in terms that are clear, not misleading and not subject to varying interpretations; and (Ref: Para. A41-A42)
  - (j) Reference to the expected form and content of the agreed-upon procedures report.
25. If the agreed-upon procedures are modified during the course of the engagement, the practitioner shall agree amended terms of engagement with the engaging party that reflect the modified procedures. (Ref: Para. A43)

#### *Recurring Agreed-Upon Procedures Engagements*

26. On recurring agreed-upon procedures engagements, the practitioner shall evaluate whether circumstances, including changes in the engagement acceptance considerations, require the terms of the engagement to be revised and whether there is a need to remind the engaging party of the existing terms of engagement. (Ref: Para. A44)

#### **Performing the Agreed-Upon Procedures**

27. The practitioner shall perform the procedures as agreed upon in the terms of the engagement.
28. The practitioner shall consider whether to request written representations. (Ref: Para. A45)

#### **Using the Work of a Practitioner's Expert**

29. If the practitioner uses the work of a practitioner's expert, the practitioner shall: (Ref: Para. A46–A47, A50)
- (a) Evaluate the competence, capabilities and objectivity of the practitioner's expert;
  - (b) Agree with the practitioner's expert on the nature, scope and objectives of that expert's work; (Ref: Para. A48-A49);
  - (c) Determine whether the nature, timing and extent of the work performed by the practitioner's expert is consistent with the work agreed with the expert; and
  - (d) Determine whether the findings adequately describe the results of the work performed, taking into account the work performed by the practitioner's expert.

#### **The Agreed-Upon Procedures Report**

30. The agreed-upon procedures report shall be in writing and shall include: (Ref: Para. A51)
- (a) A title that clearly indicates that the report is an agreed-upon procedures report;
  - (b) An addressee as set forth in the terms of the engagement;
  - (c) Identification of the subject matter on which the agreed-upon procedures are performed; (Ref: Para. A52)
  - (d) Identification of the purpose of the agreed-upon procedures report and a statement that the agreed-upon procedures report may not be suitable for another purpose; (Ref: Para. A53-A54)
  - (e) A description of an agreed-upon procedures engagement stating that:
    - (i) An agreed-upon procedures engagement involves the practitioner performing the procedures that have been agreed with the engaging party (and if relevant, other parties), and reporting the findings; (Ref: Para. A10)

- (ii) Findings are the factual results of the agreed-upon procedures performed;
  - (iii) The engaging party (and if relevant, other parties) has acknowledged that the agreed-upon procedures are appropriate for the purpose of the engagement; and (Ref: Para. A10)
  - (f) If applicable, the responsible party as identified by the engaging party, and a statement that the responsible party is responsible for the subject matter on which the agreed-upon procedures are performed;
  - (g) A statement that the engagement was performed in accordance with ASRS 4400;
  - (h) A statement that the practitioner makes no representation regarding the appropriateness of the agreed-upon procedures;
  - (i) A statement that the agreed-upon procedures engagement is not an assurance engagement and accordingly, the practitioner does not express an opinion or an assurance conclusion;
  - (j) A statement that, had the practitioner performed additional procedures, other matters might have come to the practitioner's attention that would have been reported;
  - (k) A statement that the practitioner complies with the ethical requirements of the APESB Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding;
  - (l) With respect to independence:
    - (i) If the practitioner is not required to be independent and has not otherwise agreed in the terms of engagement to comply with independence requirements, a statement that, for the purpose of the engagement, there are no independence requirements with which the practitioner is required to comply; or
    - (ii) If the practitioner is required to be independent or has agreed in the terms of engagement to comply with independence requirements, a statement that the practitioner has complied with the relevant independence requirements. The statement shall identify the relevant independence requirements;
  - (m) A statement that the firm of which the practitioner is a member applies ASQC 1, or other professional requirements, or requirements in law or regulation, that are at least as demanding as ASQC 1. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements in law or regulation, applied that are at least as demanding as ASQC 1;
  - (n) A description of the procedures performed detailing the nature and extent, and if applicable, the timing, of each procedure as agreed in the terms of the engagement; (Ref: Para. A55-A57)
  - (o) The findings from each procedure performed, including details on exceptions found; (Ref: Para. A55-A56)
  - (p) The practitioner's signature;
  - (q) The date of the agreed-upon procedures report; and
  - (r) The location in the jurisdiction where the practitioner practices.
31. If the practitioner refers to the work performed by a practitioner's expert in the agreed-upon procedures report, the wording of the report shall not imply that the practitioner's

responsibility for performing the procedures and reporting the findings is reduced because of the involvement of an expert. (Ref: Para. A58)

32. If the practitioner provides a summary of findings in the agreed-upon procedures report in addition to the description of findings as required by paragraph 30(o):
- (a) The summary of findings shall be described in a manner that is objective, in terms that are clear, not misleading, and not subject to varying interpretations; and
  - (b) The agreed-upon procedures report shall include a statement indicating that reading the summary is not a substitute for reading the complete report.
33. The practitioner shall date the agreed-upon procedures report no earlier than the date on which the practitioner completed the agreed-upon procedures and determined the findings in accordance with this ASRS.

**Undertaking an Agreed-Upon Procedures Engagement Together with another Engagement**

34. The agreed-upon procedures report shall be clearly distinguished from reports on other engagements. (Ref: Para. A59)

**Documentation**

35. The practitioner shall include in the engagement documentation: (Ref: Para. A60)
- (a) The written terms of engagement and, if applicable, the agreement of the engaging party as to modifications to the procedures;
  - (b) The nature, timing and extent of the agreed-upon procedures performed; and
  - (c) The findings resulting from the agreed-upon procedures performed.

\* \* \*

## **Application and Other Explanatory Material**

### **Scope of this ASRS** (Ref: Para. 2)

- A1. Reference to “subject matters” in this ASRS encompasses anything on which agreed-upon procedures are performed, including information, documents, measurements or compliance with laws and regulations, as relevant.
- A2. Examples of financial and non-financial subject matters on which an agreed-upon procedures engagement may be performed include:
- Financial subject matters relating to:
    - The entity’s financial report or specific classes of transactions, account balances or disclosures within the financial report.
    - Eligibility of expenditures claimed from a funding program.
    - Revenues for determining royalties, rent or franchise fees based on a percentage of revenues.
    - Capital adequacy ratios for regulatory authorities.
  - Non-financial subject matters relating to:
    - Numbers of passengers reported to a civil aviation authority.
    - Observation of destruction of fake or defective goods reported to a regulatory authority.
    - Data generating processes for lottery draws reported to a regulatory authority.
    - Volume of greenhouse gas emissions reported to a regulatory authority.

The above list is not exhaustive. Additional types of subject matters may arise as external reporting demands evolve.

### ***Relationship with ASQC 1*** (Ref: Para. 3)

- A3. ASQC 1 deals with the firm’s responsibilities to establish and maintain its system of quality control for related services engagements, including agreed-upon procedures engagements. Those responsibilities are directed at establishing:
- The firm’s quality control system; and
  - The firm’s related policies designed to achieve the objective of the quality control system and its procedures to implement and monitor compliance with those policies.
- A4. Under ASQC 1, the firm has an obligation to establish and maintain a system of quality control to provide it with reasonable assurance that:
- (a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and

(b) Reports issued by the firm or engagement partners are appropriate in the circumstances.<sup>2</sup>

A5. A jurisdiction that has not adopted ASQC 1 in relation to agreed-upon procedures engagements may set out requirements for quality control in firms performing such engagements. The provisions of this ASRS regarding quality control at the engagement level are premised on the basis that quality control requirements adopted are at least as demanding as those of ASQC 1. This is achieved when those requirements impose obligations on the firm to achieve the aims of the requirements of ASQC 1, including an obligation to establish a system of quality control that includes policies and procedures that address each of the following elements:

- Leadership responsibilities for quality within the firm;
- Relevant ethical requirements;
- Acceptance and continuance of client relationships and specific engagements;
- Human resources;
- Engagement performance; and
- Monitoring.

A6. 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.

A7. 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:

- Competence of personnel through their recruitment and formal training.
- Maintenance of client relationships through acceptance and continuance systems.
- Adherence to legal and regulatory requirements through the monitoring process.

In considering deficiencies identified in the firm's system of quality control that may affect the agreed-upon procedures engagement, the engagement partner may consider measures taken by the firm to rectify the situation that the engagement partner considers are sufficient in the context of that agreed-upon procedures engagement.

A8. A deficiency in the firm's system of quality control does not necessarily indicate that an agreed-upon procedures engagement was not performed in accordance with professional standards and applicable legal and regulatory requirements, or that the agreed-upon procedures report was not appropriate.

**Effective Date** (Ref: Para. 11)

A9. For terms of engagement covering multiple years, practitioners may wish to update the terms of engagement so that the agreed-upon procedures engagements will be conducted in accordance with this ASRS on or after the effective date.

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<sup>2</sup> ASQC 1, paragraph 11



## **Definitions**

*Engaging Party and Other Intended Users* (Ref: Para. 13(a), 13(b), 13(d), 13(g), 24 (f)(i), 24(g) 30(e)(i), 30(e)(iii))

- A10. In some circumstances, the procedures may be agreed with intended users in addition to the engaging party. Intended users other than the engaging party may also acknowledge the appropriateness of the procedures.
- A11. The engaging party may be, under different circumstances, the responsible party, a regulator or other intended user. References to the engaging party in this ASRS include multiple engaging parties when relevant.

*Findings* (Ref: Para. 13(f))

- A12. Findings are capable of being objectively verified, which means that different practitioners performing the same procedures are expected to arrive at equivalent results. Findings exclude the expression of an opinion or a conclusion as well as any recommendations that the practitioner may make.
- A13. Practitioners may use the term “factual findings” in place of “findings”, for example, in cases when the practitioner is concerned that the term “findings” may be misunderstood. This may be the case in jurisdictions or languages where the term “findings” may be understood as including results that are not factual.

## **Relevant Ethical Requirements** (Ref: Para. 17)

*Objectivity and Independence*

- A14. A practitioner performing an agreed-upon procedures engagement is required to comply with relevant ethical requirements. Relevant ethical requirements ordinarily comprise the APESB Code, together with national requirements that are more restrictive. The APESB Code requires practitioners to comply with fundamental principles including objectivity, which requires practitioners not to compromise their professional or business judgement because of bias, conflict of interest or the undue influence of others. Accordingly, relevant ethical requirements to which the practitioner is subject would, at a minimum, require the practitioner to be objective when performing an agreed-upon procedures engagement.
- A15. The APESB Code does not contain independence requirements for agreed-upon procedures engagements. However, national ethical codes, laws or regulations, other professional requirements, or conditions of a contract, program, or arrangement relating to the subject matter for the agreed-upon procedures engagement may specify requirements pertaining to independence.

*Non-Compliance with Laws and Regulations*<sup>3</sup>

- A16. Law, regulation or relevant ethical requirements may:
- (a) Require the practitioner to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.
  - (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.<sup>4</sup>

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<sup>3</sup> Relevant ethical requirements may indicate that non-compliance with laws and regulations includes fraud. See, for example, 360.5A2 of the APESB Code

<sup>4</sup> See, for example, paragraphs R360.36 to 360.36A3 of the APESB Code.

- A17. 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:
- (a) Law, regulation or relevant ethical requirements require the practitioner to report;
  - (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
  - (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so.
- A18. The practitioner is not expected to have a level of understanding of laws and regulations beyond that necessary to be able to perform the agreed-upon procedures engagement. However, law, regulation or relevant ethical requirements may expect the practitioner to apply knowledge, professional judgement 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.
- A19. 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>5</sup>
- A20. 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>6</sup>

**Professional Judgement** (Ref: Para. 18)

- A21. Professional judgement is exercised in applying the requirements of this ASRS and relevant ethical requirements, and in making informed decisions about courses of action throughout the agreed-upon procedures engagement, as appropriate.
- A22. In accepting, conducting and reporting on an agreed-upon procedures engagement, professional judgement is exercised, for example, in:
- Accepting the engagement
- Discussing and agreeing with the engaging party (and if relevant, other parties) the nature, timing and extent of the procedures to be performed (taking into account the purpose of the engagement).
  - Determining whether engagement acceptance and continuance conditions have been met.
  - Determining the resources necessary to carry out the procedures as agreed in the terms of the engagement, including the need to involve a practitioner's expert.

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<sup>5</sup> See, for example, paragraphs R114.1, 114.1A1 and R360.37 of the APESB Code.

<sup>6</sup> See, for example, paragraph 360.39 A1 of the APESB Code.

- Determining appropriate actions if the practitioner becomes aware of facts or circumstances suggesting that the procedures to which the practitioner is being asked to agree are inappropriate for the purpose of the agreed-upon procedures engagement.

**Conducting the engagement**

- Determining appropriate actions or responses if, when performing the agreed-upon procedures, the practitioner becomes aware of:
  - Matters that may indicate fraud or an instance of non-compliance or suspected non-compliance with laws or regulations.
  - Other matters that cast doubt on the integrity of the information relevant to the agreed-upon procedures engagement or that indicate that the information may be misleading.
  - Procedures that cannot be performed as agreed.

**Reporting on the engagement**

- Describing the findings in an objective manner and in sufficient detail, including when exceptions are found.

A23. In conducting the agreed-upon procedures engagement, the need for the practitioner to exercise professional judgement when performing the agreed-upon procedures is limited for reasons including:

- An agreed-upon procedures engagement involves the performance of procedures that have been agreed upon by the practitioner and the engaging party, where the engaging party has acknowledged that the procedures performed are appropriate for the purpose of the engagement.
- The agreed-upon procedures and the findings that result from performing those procedures are capable of being described objectively, in terms that are clear, not misleading, and not subject to varying interpretations.
- The findings are capable of being objectively verified, which means that different practitioners performing the same procedures are expected to arrive at equivalent results.

**Engagement Level Quality Control** (Ref: Para. 19)

A24. The actions of the engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on each engagement, emphasise the importance to achieving the quality of the engagement of:

- (a) Performing work that complies with professional standards and regulatory and legal requirements;
- (b) Complying with the firm's quality control policies and procedures as applicable; and
- (c) Issuing the practitioner's report for the engagement in accordance with this ASRS.

A25. ASQC1 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 agreed-upon procedures 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.

- A26. ASQC1 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 ASRS sets out the engagement partner's responsibilities with respect to the engagement team's compliance with relevant ethical requirements.
- A27. If the practitioner is unable to meet the requirement in paragraph 20, it may be appropriate for the practitioner to agree with the engaging party to limit the scope of the agreed-upon procedures engagement to procedures for which the practitioner can appropriately take responsibility. The engaging party may separately engage an expert to perform the other procedures.

**Engagement Acceptance and Continuance** (Ref: Para. 21–23)

- A28. In obtaining an understanding of the purpose of the agreed-upon procedures engagement, the practitioner may become aware of indications that the procedures the practitioner is asked to perform are inappropriate for the purpose of the agreed-upon procedures engagement. For example, the practitioner may be aware of facts or circumstances that indicate:
- The procedures are selected in a manner intended to bias the intended users' decision-making.
  - The subject matter on which the agreed-upon procedures are performed is unreliable.
  - An assurance engagement or advisory service may better serve the needs of the engaging party or other intended users.
- A29. Other actions that may satisfy the practitioner that the conditions in paragraphs 21 and 22 are met include:
- Comparing the procedures to be performed with written requirements set out, for example, in law or regulation, or in a contractual agreement (sometimes referred to as the "Terms of Reference"), where appropriate.
  - Requesting the engaging party to:
    - Distribute a copy of the anticipated procedures and the form and content of the agreed-upon procedures report as set out in the terms of engagement to the intended user(s).
    - Obtain acknowledgement from the intended user(s) of the procedures to be performed.
    - Discuss the procedures to be performed with appropriate representatives of the intended user(s).
  - Reading correspondence between the engaging party and other intended user(s) if the engaging party is not the only intended user.
- A30. If the conditions in paragraphs 21-22 are not met, it is unlikely that an agreed-upon procedures engagement is able to meet the needs of the engaging party or other intended users. In such circumstances, the practitioner may suggest other services, such as an assurance engagement, that may be more appropriate.
- A31. All the conditions in paragraphs 21 to 22 also apply to procedures that have been added or modified during the course of the engagement.

*Descriptions of Agreed-Upon Procedures and Findings* (Ref: Para. 22 (c))

- A32. The procedures to be performed during the agreed-upon procedures engagement may be prescribed by law or regulation. In some circumstances, law or regulation may also prescribe the way the procedures or findings are to be described in the agreed-upon procedures report. As set out in paragraph 22(c), a condition of accepting an agreed-upon procedures engagement is that the practitioner has determined that the agreed-upon procedures and findings can be described objectively, in terms that are clear, not misleading, and not subject to varying interpretations.
- A33. Agreed-upon procedures are described objectively, in terms that are clear, not misleading, and not subject to varying interpretations. This means that they are described at a level of specificity sufficient for an intended user to understand the nature and extent and if applicable, the timing, of the procedures performed. It is important to recognise that any term could potentially be used in an unclear or misleading manner, depending on context or the absence thereof. Assuming that the terms are appropriate in the context in which they are used, examples of descriptions of actions that may be acceptable include:
- Confirm.
  - Compare.
  - Agree.
  - Trace.
  - Inspect.
  - Enquire.
  - Recalculate.
  - Observe.
- A34. Terms that may be unclear, misleading, or subject to varying interpretations depending on the context in which they are used, may include, for example:
- Terms that are associated with assurance under the AUASB's Standards such as "present fairly" or "true and fair," "audit," "review," "assurance," "opinion," or "conclusion."
  - Terms that imply expression of an assurance opinion or conclusion such as "we certify," "we verify," "we have ascertained" or "we have ensured" with regard to the findings.
  - Unclear or vague phrases such as "we obtained all the explanations and performed such procedures as we considered necessary."
  - Terms that are subject to varying interpretations such as "material" or "significant."
  - Imprecise descriptions of procedures such as "discuss," "evaluate," "test," "analyse" or "examine" without specifying the nature and extent, and if applicable, the timing, of the procedures to be performed. For example, using the word "discuss" may be imprecise without specifying with whom the discussion is held or the specific questions asked.
  - Terms that suggest that the findings do not reflect factual results such as "in our view," "from our perspective" or "we take the position that."

- A35. For example, a procedure such as “review cost allocations to determine if they are reasonable” is unlikely to meet the condition for terms to be clear, not misleading, or not subject to varying interpretations because:
- The term “review” may be misinterpreted by some users to mean that the cost allocation was the subject of a limited assurance engagement even though no such assurance is intended by the procedure.
  - The term “reasonable” is subject to varying interpretations as to what constitutes “reasonable.”
- A36. In circumstances when law or regulation specifies a procedure or describes a procedure using terms that are unclear, misleading, or subject to varying interpretations, the practitioner may satisfy the condition in paragraph 24(d) by, for example, requesting the engaging party to:
- Modify the procedure or the description of the procedure so that it is no longer unclear, misleading, or subject to varying interpretations.
  - If a term that is unclear, misleading or subject to varying interpretations cannot be amended, for example because of law or regulation, include a definition of the term in the agreed-upon procedures report.

*Compliance with Independence Requirements* (Ref: Para. 22(e), 24(e))

- A37. Paragraph 22(e) applies when the practitioner is required to comply with independence requirements for reasons such as those set out in paragraph A15. Paragraph 22(e) also applies when the practitioner agrees with the engaging party, in the terms of engagement, to comply with independence requirements. For example, the practitioner may have initially determined that the practitioner is not required by relevant ethical requirements, law or regulation, or other reasons to comply with independence requirements. However, when considering engagement acceptance and continuance or agreeing the terms of engagement, the practitioner’s knowledge of the following matters may indicate that a discussion with the engaging party as to whether compliance with certain identified independence requirements is appropriate for the purpose of the agreed-upon procedures engagement:
- The purpose of the agreed-upon procedures engagement;
  - The identity of the engaging party, other intended users and responsible party (if different from the engaging party);
  - The nature, timing and extent of the procedures to be performed; or
  - Other engagements that the practitioner is performing or has performed for the engaging party, other intended users or the responsible party (if different from the engaging party),
- A38. The practitioner may be the auditor of the financial report of the engaging party (or responsible party if different from the engaging party). In such a circumstance, if the practitioner is also engaged to conduct an agreed-upon procedures engagement, intended users of the agreed-upon procedures report may assume that the practitioner is independent for the purpose of the agreed-upon procedures engagement. Therefore, the practitioner may agree with the engaging party that the practitioner’s compliance with the independence requirements applicable to audits of financial report is appropriate for the purpose of the agreed-upon procedures engagement. In such a case, a statement that the practitioner is required to comply with such independence requirements is included in the terms of the engagement, in accordance with paragraph 24(e).

**Agreeing the Terms of the Engagement** (Ref: Para. 24-25)

- A39. When relevant, additional matters may be included in the engagement letter, for example:
- Arrangements concerning the involvement of a practitioner's expert in some aspects of the agreed-upon procedures engagement.
  - Any restrictions on the use or distribution of the agreed-upon procedures report.
- A40. An illustrative engagement letter for an agreed-upon procedures engagement is set out in Appendix 1.
- A41. The practitioner may agree with the engaging party that the procedures to be performed will include quantitative thresholds for determining exceptions. If so, these quantitative thresholds are included in the descriptions of the procedures in the terms of the engagement.
- A42. In some circumstances, law or regulation may prescribe only the nature of the procedures to be performed. In such circumstances, in accordance with paragraph 24(i), the practitioner agrees the timing and extent of procedures to be performed with the engaging party so that the engaging party has a basis to acknowledge that the procedures to be performed are appropriate for the purpose of the engagement.
- A43. In some circumstances, agreeing the terms of engagement and performing the agreed-upon procedures takes place in a linear and discrete manner. In other circumstances, agreeing the terms of engagement and performing the agreed-upon procedures is an iterative process, with changes to the agreed-upon procedures being agreed as the engagement progresses in response to new information coming to light. If procedures that have been previously agreed upon need to be modified, paragraph 25 requires the practitioner to agree the amended terms of engagement with the engaging party. The amended terms of engagement may, for example, take the form of an updated engagement letter, an addendum to an existing engagement letter, or other form of written acknowledgement.

***Recurring Engagements*** (Ref: Para. 26)

- A44. The practitioner may decide not to send a new engagement letter or other written agreement for a recurring engagement. However, the following factors may indicate that it is appropriate to revise the terms of the engagement, or to remind the engaging party of the existing terms of the engagement:
- Any indication that the engaging party misunderstands the purpose of the agreed-upon procedures engagement or the nature, timing or extent of the agreed-upon procedures.
  - Any revised or special terms of the engagement, including any changes in the previously agreed-upon procedures.
  - A change in legal, regulatory or contractual requirements affecting the engagement.
  - A change in management or those charged with governance of the engaging party.

**Performing the Agreed-Upon Procedures** (Ref: Para. 28)

- A45. The practitioner may decide to request written representations in some circumstances, for example:
- If the agreed-upon procedures involve enquiries, the practitioner may request written representations on the responses that have been provided verbally.
  - If the engaging party is not the responsible party, the practitioner may agree with the engaging party to include, as an agreed-upon procedure, requests for written representations from the responsible party.

**Using the Work of a Practitioner's Expert** (Ref: Para. 29)

- A46. Using the work of a practitioner's expert may involve the use of an expert to assist the practitioner in:
- Discussing with the engaging party the agreed-upon procedures to be performed. For example, a lawyer may provide suggestions to the practitioner on the design of a procedure to address legal aspects of a contract; or
  - Performing one or more of the agreed-upon procedure(s). For example, a chemist may perform one of the agreed-upon procedures such as determining the toxin levels in a sample of grains.
- A47. A practitioner's expert may be an external expert engaged by the practitioner or an internal expert who is part of the firm and therefore subject to the firm's system of quality control. The practitioner is 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 matters such as:
- Competence and capabilities, through recruitment and training programs.
  - The practitioner's evaluation of the objectivity of the practitioner's expert.
  - Agreement with the practitioner's expert.
- Such reliance does not reduce the practitioner's responsibility to meet the requirements of this ASRS.
- A48. If the practitioner's expert is performing one or more of the agreed-upon procedure(s), the agreement of the nature, scope and objectives of that expert's work as required by paragraph 29(b) includes the nature, timing and extent of the procedure(s) to be performed by the practitioner's expert. In addition to the matters required by paragraph 29(b), it may be appropriate for the practitioner's agreement with the practitioner's expert to include matters such as the following:
- (a) The respective roles and responsibilities of the practitioner and that expert;
  - (b) The nature, timing and extent of communication between the practitioner and that expert, including the form of any report to be provided by that expert; and
  - (c) The need for the practitioner's expert to observe confidentiality requirements.
- A49. The matters noted in paragraph A47 may affect the level of detail and formality of the agreement between the practitioner and the practitioner's expert, including whether it is appropriate that the agreement be in writing. The agreement between the practitioner and the practitioner's external expert is often in the form of an engagement letter.
- A50. When the work of a practitioner's expert is to be used, it may be appropriate to perform some of the procedures required by paragraph 29 at the engagement acceptance or continuance stage.

**The Agreed-Upon Procedures Report** (Ref: Para. 30-33)

- A51. Appendix 2 contains illustrations of agreed-upon procedures reports.

*Subject Matter on which the Agreed-Upon Procedures are Performed* (Ref: Para. 30(c))

- A52. If applicable, to avoid misunderstanding, the practitioner may wish to clarify that the agreed-upon procedures report does not extend to information beyond subject matters on which the



agreed-upon procedures are performed. For example, if the practitioner was engaged to perform agreed-upon procedures on an entity's accounts receivable and inventory, the practitioner may wish to include a statement that the agreed-upon procedures report relates only to these accounts and does not extend to the entity's financial report taken as a whole.

*Purpose of the Agreed-Upon Procedures Report* (Ref: Para. 30(d))

- A53. In addition to the statement required by paragraph 30(d), the practitioner may consider it appropriate to indicate that the agreed-upon procedures report is intended solely for the engaging party and the intended users. Depending on the law or regulation of the particular jurisdiction, this may be achieved by restricting the distribution or use of the agreed-upon procedures report. In some jurisdictions, it may be possible to restrict the use of the agreed-upon procedures report but not its distribution. In other jurisdictions, it may be possible to restrict the distribution of the agreed-upon procedures report but not its use.
- A54. Factors that the practitioner may consider in deciding whether to restrict the distribution or use of agreed-upon procedures report (if permitted to do so) include, for example whether:
- There is an elevated risk of users other than the intended users misunderstanding the purpose of the agreed-upon procedures engagement or misinterpreting the findings.
  - The agreed-upon procedures are designed solely for the use of internal users such as management and those charged with governance of the engaging party.
  - The agreed-upon procedures or findings involve confidential information.

*Agreed-Upon Procedures and Findings* (Ref: Para. 30(n)-30(o))

- A55. If the practitioner is unable to describe the agreed-upon procedures or findings without including confidential or sensitive information, the practitioner may consider:
- Consulting internally (for example, within the firm or network firm);
  - Consulting externally (for example, with the relevant professional body or another practitioner); or
  - Obtaining legal advice,
  - to understand the professional or legal implications of taking any particular course of action.
- A56. There may be circumstances when the fact that previously agreed-upon procedures have not been performed or have been modified is important to the intended users' consideration of the agreed-upon procedures and findings. For example, this may be the case when the procedures are set out in law or regulation. In such circumstances, the practitioner may identify, in the agreed-upon procedures report, the procedures agreed in the original terms of the engagement which could not be performed or were modified, and why that has arisen.
- A57. The practitioner may refer to the date when the agreed-upon procedures were agreed in the terms of the engagement.

*Reference to Practitioner's Expert* (Ref: Para. 31)

- A58. In some circumstances, law or regulation may require a reference, in the agreed-upon procedures report, to a practitioner's expert who performed any of the agreed-upon procedures. For example, such a reference may be required for the purposes of transparency in the public sector. The practitioner may also consider it appropriate in other circumstances, for example, when referring to the practitioner's expert when describing the agreed-upon procedures. Nonetheless, the practitioner has sole responsibility for the findings included in

the agreed-upon procedures report, and that responsibility is not reduced by the use of the practitioner's expert. It is important therefore that if the agreed-upon procedures report refers to the practitioner's expert, the report does not imply that the practitioner's responsibility is reduced because of the reference to the practitioner's expert.

**Undertaking an Agreed-Upon Procedures Engagement Together with another Engagement** (Ref: Para. 34)

A59. A practitioner may be requested to perform other engagements together with the agreed-upon procedures engagement, such as providing recommendations arising from the agreed-upon procedures engagement. Such requests may take the form of one request for the practitioner to perform agreed-upon procedures and make recommendations, and the terms of the various engagements may be set out in a single engagement letter. To avoid misunderstanding, paragraph 34 requires that the agreed-upon procedures report be clearly distinguished from the reports of other engagements. For example, the recommendations may be:

- Provided in a separate document from the agreed-upon procedures report; or
- Included in a document that contains both the agreed-upon procedures report and recommendations but the recommendations are clearly differentiated from the agreed-upon procedures report, for example, by including the agreed-upon procedures report and the recommendations in separate sections of the document.

**Documentation** (Ref: Para. 35)

A60. Documentation of the nature, timing and extent of the agreed-upon procedures performed may include a record of, for example:

- The identifying characteristics of the subject matters on which the agreed-upon procedures are performed. Identifying characteristics will vary depending on the nature of the agreed-upon procedure and the subject matters on which the agreed-upon procedure is performed. For example:
  - For a procedure on purchase orders, the practitioner may identify the documents selected by their dates and unique purchase order numbers.
  - For a procedure requiring selection of all items over a specific amount from a given population, the practitioner may record the scope of the procedure and identify the population (for example, all journal entries over a specified amount from the journal register for a specific period, all timesheets for hours recorded over a certain number for specified months or every tenth item on a specific list).
  - For a procedure requiring enquiries of specific personnel, the practitioner may record the dates of the enquiries, the names and job designations of the personnel and the specific enquiries made.
  - For an observation procedure, the practitioner may record the process or matter being observed, the relevant individuals, their respective responsibilities, and where and when the observation was carried out.
- Who performed the agreed-upon procedures and the date such procedures were performed.
- Who reviewed the agreed-upon procedures performed, and the date and extent of such review.

## **Appendix 1**

(Ref: Para A40)

### **Illustrative Engagement Letter for an Agreed-Upon Procedures Engagement**

The following is an example of an engagement letter for an agreed-upon procedures engagement that illustrates the relevant requirements and guidance contained in this ASRS. This letter is not authoritative and is intended only to be a guide that may be used in conjunction with the considerations outlined in this ASRS. It will need to be adapted according to the requirements and circumstances of individual agreed-upon procedures engagements. It is drafted to refer to an agreed-upon procedures engagement for a single reporting period and would require adaptation if intended or expected to apply to a recurring engagement as described in this ASRS. It may be appropriate to seek legal advice that any proposed letter is suitable.

To [Engaging Party]

You have requested that we perform an agreed-upon procedures engagement on the procurement of [xyz] products. This letter is to confirm our understanding of the terms and objectives of our engagement and the nature and limitations of the services that we will provide. Our engagement will be conducted in accordance with the Australian Standard on Related Services ASRS 4400, *Agreed-Upon Procedures Engagements*. In performing the agreed-upon procedures engagement, we will comply with [describe the relevant ethical requirements], which does not require us to be independent.

An agreed-upon procedures engagement performed under ASRS 4400 involves our performing the procedures agreed with you, and communicating the findings in the agreed-upon procedures report. Findings are the factual results of the agreed-upon procedures performed. You [and if relevant, other parties] acknowledge that the procedures are appropriate for the purpose of the engagement. We make no representation regarding the appropriateness of the procedures. This agreed-upon procedures engagement will be conducted on the basis that [Responsible Party] is responsible for the subject matter on which the agreed-upon procedures are performed. Further, this agreed-upon procedures engagement is not an assurance engagement. Accordingly, we do not express an opinion or an assurance conclusion.

The procedures that we will perform are solely for the purpose of assisting you in determining whether your procurement of [xyz] products is compliant with your procurement policies<sup>7</sup>. Accordingly, our report will be addressed to you and our report may not be suitable for another purpose.

We have agreed to perform the following procedures and report to you the findings resulting from our work:

- Obtain from management of [Engaging Party] a listing of all contracts signed between [January 1, 20X8] and [December 31, 20X8] for [xyz] products (“listing”) and identify all contracts valued at over \$25,000.
- For each identified contract valued at over \$25,000 on the listing, compare the contract to the records of bidding and determine whether each contract was subject to bidding by at least 3 contractors from [Engaging Party]’s “Pre-qualified Contractors List.”
- For each identified contract valued at over \$25,000 on the listing, compare the amount payable per the signed contract to the amount ultimately paid by [Engaging Party] to the contractor and determine whether the amount ultimately paid is the same as the agreed amount in the contract.

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<sup>7</sup> In this case, the engaging party is also the intended user.

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***Agreed-Upon Procedures Engagements***

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The procedures are to be performed between [Date] and [Date].

**Our Agreed-Upon Procedures Report**

As part of our engagement, we will issue our report, which will describe the agreed-upon procedures and the findings of the procedures performed [Insert appropriate reference to the expected form and content of the agreed-upon procedures report].

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our engagement, including the specific procedures which we have agreed will be performed and that they are appropriate for the purpose of the engagement.

[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]

[Firm's name]

Acknowledged and agreed on behalf of [Engaging party's name] by:

[Signature]

[Name and Title]

[Date]

## **Appendix 2**

(Ref: Para A51)

### **Illustrations of Agreed-Upon Procedures Reports**

#### **Illustration 1**

For purposes of this illustrative agreed-upon procedures report, the following circumstances are assumed:

- The engaging party is the addressee and the only intended user. The engaging party is not the responsible party. For example, the regulator is the engaging party and intended user, and the entity overseen by the regulator is the responsible party.
- No exceptions were found.
- The practitioner did not engage a practitioner's expert to perform any of the agreed-upon procedures.
- There is no restriction on the use or distribution of the report.
- There are no independence requirements with which the practitioner is required to comply.
- A quantitative threshold of \$100 for reporting exceptions in Procedure 3 has been agreed with the engaging party.

#### **AGREED-UPON PROCEDURES REPORT ON PROCUREMENT OF [XYZ] PRODUCTS**

To [Addressee]

#### **Purpose of this Agreed-Upon Procedures Report**

Our report is solely for the purpose of assisting [Engaging Party] in determining whether its procurement of [xyz] products is compliant with its procurement policies and may not be suitable for another purpose.

#### **Responsibilities of the Engaging Party and the Responsible Party**

[Engaging Party] has acknowledged that the agreed-upon procedures are appropriate for the purpose of the engagement.

[Responsible Party], as identified by [Engaging Party], is responsible for the subject matter on which the agreed-upon procedures are performed.

#### **Practitioner's Responsibilities**

We have conducted the agreed-upon procedures engagement in accordance with the Australian Standard on Related Services ASRS 4400, *Agreed-Upon Procedures Engagements*. An agreed-upon procedures engagement involves our performing the procedures that have been agreed with [Engaging Party], and reporting the findings, which are the factual results of the agreed-upon procedures performed. We make no representation regarding the appropriateness of the agreed-upon procedures.

This agreed-upon procedures engagement is not an assurance engagement. Accordingly, we do not express an opinion or an assurance conclusion.

Had we performed additional procedures, other matters might have come to our attention that would have been reported.

**Proposed Standard on Related Services ASRS 4400**  
***Agreed-Upon Procedures Engagements***

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*Professional Ethics and Quality Control*

We have complied with the ethical requirements in [describe the relevant ethical requirements]. For the purpose of this engagement, there are no independence requirements with which we are required to comply.

Our firm applies Australian Standard on Quality Control ASQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance Engagements and Related Services Engagements*, and accordingly, 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.

**Procedures and Findings**

We have performed the procedures described below, which were agreed upon with [Engaging Party], on the procurement of [xyz] products.

	<b>Procedures</b>	<b>Findings</b>
1	Obtain from management of [Responsible Party] a listing of all contracts signed between [January 1, 20X8] and [December 31, 20X8] for [xyz] products (“listing”) and identify all contracts valued at over \$25,000.	We obtained from management a listing of all contracts for [xyz] products which were signed between [January 1, 20X8] and [December 31, 20X8].  Of the 125 contracts on the listing, we identified 37 contracts valued at over \$25,000.
2	For each identified contract valued at over \$25,000 on the listing, compare the contract to the records of bidding and determine whether the contract was subject to bidding by at least 3 contractors from [Responsible Party]’s “Pre-qualified Contractors List.”	We inspected the records of bidding related to the 37 contracts valued at over \$25,000. We found that all of the 37 contracts were subject to bidding by at least 3 contractors from the [Responsible Party]’s “Pre-qualified Contractors List.”
3	For each identified contract valued at over \$25,000 on the listing, compare the amount payable per the signed contract to the amount ultimately paid by [Responsible] to the contractor and determine whether the amount ultimately paid is within \$100 of the agreed amount in the contract.	We obtained the signed contracts for the 37 contracts valued at over \$25,000 on the listing and compared the amounts payable in the contracts to the amounts ultimately paid by [Responsible Party] to the contractor.  We found that the amounts ultimately paid were within \$100 of the agreed amounts in all of the 37 contracts with no exceptions noted.

[Practitioner’s signature]

[Date of practitioner’s report]

[Practitioner’s address]

**Illustration 2**

For purposes of this illustrative agreed-upon procedures report, the following circumstances are assumed:

- The engaging party is the responsible party. The intended user, who is different from the engaging party, is an addressee in addition to the engaging party. For example, the regulator is the intended user and the entity overseen by the regulator is the engaging party and responsible party.
- Exceptions were found.
- The practitioner engaged a practitioner's expert to perform an agreed-upon procedure and a reference to that expert is included in the agreed-upon procedures report.
- There is a restriction on the use and distribution of the report.
- The practitioner is the auditor of the financial report of the engaging party (who is the responsible party). The practitioner has agreed with the engaging party that the practitioner's compliance with the independence requirements applicable to audits of financial reports is appropriate for the purpose of the agreed-upon procedures engagement. The practitioner has agreed to include, in the terms of engagement, compliance with the independence requirements applicable to audits of financial reports for the purpose of the agreed-upon procedures engagement.
- The practitioner included a reference to the date when the agreed-upon procedures were agreed in the terms of the engagement.

**AGREED-UPON PROCEDURES REPORT ON PROCUREMENT OF [XYZ] PRODUCTS**

To [Addressees]

**Purpose of this Agreed-Upon Procedures report and Restriction on Use and Distribution**

Our report is solely for the purpose of assisting [Intended User] in determining whether the [Engaging Party]'s procurement of [xyz] products is compliant with [Intended User]'s procurement policies and may not be suitable for another purpose. This report is intended solely for [Engaging Party] and [Intended Users], and should not be used by, or distributed to, any other parties.

**Responsibilities of the Engaging Party**

[Engaging Party] has acknowledged that the agreed-upon procedures are appropriate for the purpose of the engagement.

[Engaging Party (also the Responsible Party)] is responsible for the subject matter on which the agreed-upon procedures are performed.

**Practitioner's Responsibilities**

We have conducted the agreed-upon procedures engagement in accordance with the Australian Standard on Related Services ASRS 4400, *Agreed-Upon Procedures Engagements*. An agreed-upon procedures engagement involves our performing the procedures that have been agreed with [Engaging Party], and reporting the findings, which are the factual results of the agreed-upon procedures performed. We make no representation regarding the appropriateness of the agreed-upon procedures.

This agreed-upon procedures engagement is not an assurance engagement. Accordingly, we do not express an opinion or an assurance conclusion.

**Proposed Standard on Related Services ASRS 4400**  
***Agreed-Upon Procedures Engagements***

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Had we performed additional procedures, other matters might have come to our attention that would have been reported.

**Professional Ethics and Quality Control**

We have complied with the ethical requirements in [describe the relevant ethical requirements] and the independence requirements in accordance with [describe the relevant independence requirements]<sup>8</sup>.

Our firm applies Australian Standard on Quality Control ASQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance and Related Services Engagements*, and accordingly, 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.

**Procedures and Findings**

We have performed the procedures described below, which were agreed upon with [Engaging Party] in the terms of engagement dated [DATE], on the procurement of [xyz] products.

	<b>Procedures</b>	<b>Findings</b>
1	Obtain from management of [Engaging Party] a listing of all contracts signed between [January 1, 20X8] and [December 31, 20X8] for [xyz] products (“listing”) and identify all contracts valued at over \$25,000.	We obtained from management a listing of all contracts for [xyz] products which were signed between [January 1, 20X8] and [December 31, 20X8].  Of the 125 contracts on the listing, we identified 37 contracts valued at over \$25,000.

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<sup>8</sup> For example, if the APESB Code is the relevant ethical requirements and Part 4A of the APESB Code is the relevant independence requirements, this sentence may be worded along the following: “We have complied with the ethical requirements of the Accounting Professional & Ethical Standards Board *Code of Ethics for Professional Accountants* (APESB Code) and the independence requirements in Part 4A of the APESB Code.”



**Proposed Standard on Related Services ASRS 4400**  
***Agreed-Upon Procedures Engagements***

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	<b>Procedures</b>	<b>Findings</b>
2	For each identified contract valued at over \$25,000 on the listing, compare the contract to the records of bidding and determine whether the contract was subject to bidding by at least 3 contractors from [Engaging Party]’s “Pre-qualified Contractors List.” For records of bidding that were submitted in [foreign language], translate the records of bidding with the assistance of a translator engaged by the practitioner before performing the comparison.	<p>We inspected the records of bidding related to the 37 contracts valued at over \$25,000. Of the records of bidding related to the 37 contracts, 5 were submitted in [foreign language]. We engaged a translator to assist us in the translation of these 5 records of bidding.</p> <p>We found that 36 of the 37 contracts were subject to bidding by at least 3 contractors from [Engaging Party]’s “Pre-qualified Contractors List.”</p> <p>We found 1 contract valued at \$65,000 that was not subject to bidding. Management has represented to us that the reason that this contract was not subject to bidding was due to an emergency to meet a contractual deadline.</p> <p>The engagement of the translator to assist us in the translation of the records of bidding does not reduce our responsibility for performing the procedures and reporting the findings.</p>
3	For each identified contract valued at over \$25,000 on the listing, compare the amount payable per the signed contract to the amount ultimately paid by [Engaging Party] to the supplier and determine whether the amount ultimately paid is the same as the agreed amount in the contract.	<p>We obtained the signed contracts for the 37 contracts valued at over \$25,000 on the listing and compared the amounts payable in the contracts to the amounts ultimately paid by [Engaging Party] to the supplier.</p> <p>We found that the amounts payable in the signed contracts differed from the amounts ultimately paid by [Engaging Party] for 26 of the 37 contracts. In all these cases, management has represented to us that the difference in the amounts were to accommodate an increase of 1% in the sales tax rate of [jurisdiction] that became effective in September 20X8.</p>

[Practitioner’s signature]

[Date of practitioner’s report]

[Practitioner’s address]



# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO. **4.0**

Meeting Date: 4 February 2020

Subject: Update: Ethics Code Conforming Amendments – *Australian Auditing Standards made under Section 336 of the Corporations Act 2001*

Date Prepared: 10 January 2020

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☐ Action Required

☒ For Information Purposes Only

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## Agenda Item Objectives

To provide an update on the project to amend the AUASB's 'Force of Law' Auditing Standards made under section 336 of the *Corporations Act 2001* to conform with revised IAASB Standards, which are being updated in response to the revised and restructured IESBA's *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code).

## Background

1. On 15 November 2019, the IAASB issued Exposure Draft (ED) '*Proposed Changes to the IAASB Standards as a result of the Revised IESBA Code*', with comments due by 10 January 2020. The Explanatory Memorandum accompanying the ED provides background to, and an explanation of, the IAASB's proposed conforming amendments to its International Standards.

The ED and Explanatory Memorandum can be accessed through the following link: [IAASB Conforming Amendments Exposure Draft](#)

2. The revised and restructured IESBA Code became operational from 15 June 2019. The Accounting Professional & Ethical Standards Board (APESB) has revised its Code to incorporate the changes to the IESBA's Code. The revised and restructured APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (APES 110) became effective from 1 January 2020. In developing the revised APES 110, the APESB used the IESBA Code as base document and then tailored the Code for the Australian environment.
3. A concurrent project is being undertaken in Australia to implement necessary conforming amendments to AUASB Standards to:
  - (a) conform with the amended IAASB Standards; and

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

- (b) update references in AUASB Standards to the extant APES 110 to refer to the revised and restructured APES 110.

Refer to Agenda Item 6 of the December 2019 AUASB meeting for background information on the project and the approach adopted by the AUASB Technical Group (ATG) to implement the necessary conforming amendments to AUASB Standards.

4. A revised ASA 102 *Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements* (ASA 102) was approved at the 3-4 December 2019 AUASB meeting, and formally issued late December 2019 to provide a 'force of law' requirement to comply with the revised and restructured APES 110, which became effective from 1 January 2020.
5. The revised ASA 102 reflect revised terminology and other revisions to the IESBA Code which have been adopted in IAASB Standards, and updates references to APES 110 to refer to the revised and restructured APES 110. ASA 102 enables references to relevant ethical requirements in other AUASB Standards to remain current as they are explicitly linked to ASA 102.

Refer to Agenda Item 6.1 of December 2019 AUASB meeting for the ATG analysis in support of conforming amendments to ASA 102.

6. At the December 2019 AUASB meeting, a number of Board members enquired whether it would be possible to have the commencement dates of the revised ASA 102 and APES 110 aligned so that both standards apply to audit work in progress at 1 January 2020, regardless of the financial reporting period to which such work relates - that is, that the revised ASA 102 be operative "from 1 January 2020", instead of "for engagements with financial reporting periods ending on or after 31 December 2019".
7. Consequently, Gadens Lawyers was engaged to provide formal advice on this matter (refer to Agenda Item 4.2). The advice concluded that the relevant provisions in section 336 the *Corporations Act 2001* apply to limit the power of the AUASB to create auditing standards with mandatory application only in respect of reporting periods ending after the commencement of the standard or a later date.

In line with this legal advice, ASA 102 was issued to be operative for engagements with financial reporting periods ending on or after 31 December 2019, with early adoption of the standard permitted.

8. The ATG has undertaken a review of the IAASB's proposed changes to its International Standards (see above link to the IAASB's ED issued in November 2019), to determine the impact on the AUASB's other 'force of law' Auditing Standards.

The attached proposed (draft) Auditing Standard ASA 2020-1 *Amendments to Australian Auditing Standards made under Section 336 of the Corporations Act 2001* has been drafted for this purpose - please refer to **Agenda Item 4.1**.

9. The attached draft ASA 2020-1 is a working document only and includes proposed conforming amendments based on the IAASB's November 2019 ED. It will need to be updated for any changes in response to comments received as a part of the IAASB's ED process. The closing date for comments was 10 January 2020.
10. The ATG has also undertaken a review of Australian domestic standards and Australian specific paragraphs included in auditing standards (prefix "Aus"), to identify further cross references to 'relevant ethical requirements' and the APES 110 Code, and to identify any relevant terminology that may need to be updated.
11. It is expected that the IAASB will approve its final conforming amendments at its 11 February 2020 teleconference meeting. Once issued by the IAASB, the ATG will finalise the

proposed Amending Standard ASA 2020-1. The final updated draft will also be circulated to the APESB technical staff for review before it is finalised by the ATG.

12. The final proposed Amending Standard ASA 2020-1 will then be circulated to the AUASB for consideration and approval out of session.

## **Matters to Consider**

### *Operative Date*

13. In line with legal advice obtained by the AUASB in December 2019 (refer Agenda Item 4.2), it is proposed that ASA 2020-1 be operative for reporting periods ending on or after the first month end date after the ASA is approved by the AUASB. The *Legislation Act 2003* expressly prohibits retrospective legislation.

### *ASRE 2410 Review of a Financial Report Performed by the Independent Auditor of the Entity (July 2013)*

14. The AUASB's 'force of law' auditing standards, made under section 226 of the *Corporations Act 2001*, includes ASRE 2410.
15. The ATG has identified several general updates to ASRE 2410 that will be necessary to reference and reflect relevant ethical requirements in the same manner as in other auditing standards. Conforming amendments related to the revised codes of ethics will be considered as part of the AUASB's current review of ASRE 2410 – refer to December 2019 AUASB meeting, Agenda Item 8.

### *Other 'force of law' Australian Auditing Standards (ASA 100, ASA 101 and ASRE 2415) for which no international equivalent standards exist.*

16. ASA 100 *Preamble to AUASB Standards* (April 2006), ASA 101 *Preamble to Australian Auditing Standards* (June 2011) and ASRE 2415 *Review of a Financial Report: Company Limited by Guarantee or an Entity Reporting under the ACNC Act or Other Applicable Legislation or Regulation* (July 2013) have been made for Australian legislative purposes only - no equivalent international standards exist.
17. The ATG's review of these standards indicate that amendments will only be necessary in relation to paragraph 39 of ASA 100, which still refers to relevant ethical requirements contained in the respective codes of professional conduct of the professional accounting bodies in Australia (with a specific footnote reference to the extant codes of conduct issued by the CPA, ICAA and NIA).

It is proposed that this paragraph be replaced with wording similar to that used in other auditing standards to refer to relevant ethical requirements as defined in ASA 102:

For example, based on ASA 220 paragraph A4: "*The auditor is subject to relevant ethical requirements, including those pertaining to independence, relating to audit engagements as defined in ASA 102*".

### *Framework and Glossary*

18. The ATG has reviewed all *AUASB Framework Pronouncements* in order to identify the need for these pronouncements to be updated to align with revised international standards and the revised ethical codes.
19. The Framework and Glossary do not in themselves establish requirements for the performance of an audit, review or other assurance engagement and are not issued for the purpose of the *Corporations Act 2001*. However, as these documents provide a frame of reference for the AUASB in its

development of standards and for stakeholders to refer to, these pronouncements will also need to be updated.

20. Limited amendments are proposed in relation to the following:

*Framework for Assurance Engagements*

- As the Australian Framework includes references to relevant ethical requirements as defined in ASA 102, instead of direct references to any ethical code, many of the proposed changes to the International Framework will not be necessary in Australia.
- The only proposed amendment to the Australian Framework is in relation to paragraph 7, to reflect enhancements to the conceptual framework included in the revised codes of ethics for addressing threats to compliance with fundamental principles. For example, the revised codes of ethics clarify that not all threats can be addressed by the application of safeguards.

*AUASB Glossary*

- ‘Independence’ is not defined in the AUASB Glossary but APES 110 includes a definition that aligns with that included in the IAASB Glossary and IESBA Code. The ATG will recommend inclusion of a similar definition for ‘Independence’ (or reference to the APES 110 definition) in the AUASB Glossary.

*ASA 700 and illustrative reports included in Appendix to ASA 700*

21. As the body of ASA 700 does not include any direct references to APES 110, many of the proposed amendments to ISA 700 will not be necessary in Australia. For example, paragraph 28(c) has been deleted by the AUASB and replaced by Aus 28.1 which refers to ‘relevant ethical requirements applicable within Australia’ instead of a direct reference to the IESBA Code (or local equivalent).
22. Paragraph 40 of ASA 700 will need to be updated in accordance with the IAASB proposed changes to reflect the revised codes of ethics’ framework for addressing threats to compliance with fundamental principles. The change is necessary because, under the extant Codes, safeguards included actions or measures that eliminate or reduce threats to an acceptable level. Under the revised Codes, safeguards are measures that are applied to reduce the threats, while measures to eliminate threats are separate from safeguards.

Proposed change to paragraph 40 of ASA 700:

The Auditor’s Responsibilities for the Audit of the Financial Report’ section of the auditor’s report also shall: (Ref: Para. A50)

- (a) ...
- (b) For audits of the financial report 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 communicate with them all relationships and other matters that may reasonably be thought to bear on the auditor’s independence, and where applicable, related safeguards how threats have been eliminated or safeguards applied; and
- (c) ...

23. Proposed changes to illustrative examples of auditor’s reports included in Appendix 1 of ASA 700:

- (a) Direct references to APES 110, for example, in the ‘Basis for Opinion’ paragraph of the auditor’s report, will need to be updated to refer to the revised title of APES 110:

“APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*”

- (b) The section ‘Auditor’s Responsibilities for the Audit of the Financial Report’ will need to be updated to reflect the updated paragraph 40 of ASA 700 (see above):

...

“We also provide the directors 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~~ how threats have been eliminated or safeguards applied.”

...

**Note:**

- Various other illustrative reports in Appendices to other Auditing Standards will also require similar updating, for example, Appendices to ASA 705, 706, ASA 710 and ASA 720.
- Furthermore, the AUASB’s website includes examples of descriptions of the Auditor’s Responsibilities that can be referenced in auditor’s reports to the AUASB website descriptions. These example descriptions will need to be updated in line with paragraph 40 of ASA 700 (see above) – (only Statements 1 and 2 require updating).

**Material Presented**

Agenda Item 4.0	AUASB Board Meeting Summary Paper
Agenda Item 4.1	(Draft) Proposed Amending Standard ASA 2020-1 <i>Amendments to Australian Auditing Standards made under Section 336 of the Corporations Act 2001</i> .
Agenda Item 4.2	Legal advice relating to the operative date of AUASB Standards: Letter from Gadens Lawyers (18 December 2019).

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**Action Required**

For the AUASB to:

- endorse the approach the ATG is taking to update auditing standards; and
  - agree to approve the finalised AUASB Amending Standard ASA 2020-1 out of session, once the IAASB conforming amendments have been formally approved.
-

**ASA 2020-1**  
(March 2020)

**Auditing Standard ASA 2020-1**  
***Amendments to Australian Auditing***  
***Standards made under Section 336 of the***  
***Corporations Act 2001***

Issued by the **Auditing and Assurance Standards Board**

Draft



**Australian Government**

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**Auditing and Assurance Standards Board**

## Obtaining a Copy of this Auditing Standard

This Auditing Standard is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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Draft

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## PREFACE

### Reasons for Issuing ASA 2020-1

The AUASB issues Auditing Standard ASA 2020-1 *Amendments to Australian Auditing Standards made under Section 336 of the Corporations Act 2001* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is a non corporate Commonwealth entity of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislation Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required, inter alia, to develop auditing standards that have a clear public interest focus and are of the highest quality.

### Main Features

This Auditing Standard makes amendments to the following Auditing Standards:

ASQC 1	<i>Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance Engagements and Related Services Engagements</i> (30 May 2017)
ASA 100	<i>Preamble to AUASB Standards</i> (28 April 2006)
ASA 200	<i>Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards</i> (5 December 2018)
ASA 220	<i>Quality Control for an Audit of a Financial Report and Other Historical Financial Information</i> (30 May 2017)
ASA 240	<i>The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report</i> (5 December 2018)
ASA 250	<i>Consideration of Laws and Regulations in an Audit of a Financial Report</i> (30 May 2017)
ASA 260	<i>Communication With Those Charged With Governance</i> (5 December 2018)
ASA 510	<i>Initial Audit Engagements – Opening Balances</i>
ASA 570	<i>Going Concern</i> (1 December 2015)
ASA 600	<i>Special Considerations-Audits of a Group Financial Report</i> (1 December 2015)
ASA 620	<i>Using the Work of an Auditor's Expert</i> (27 October 2009)
ASA 700	<i>Forming an Opinion and Reporting on a Financial Report</i> (5 December 2018)
ASA 705	<i>Modifications to the Opinion in the Independent Auditor's Report</i> (1 December 2015)
ASA 706	<i>Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report</i> (1 December 2015)

## **Auditing Standard ASA 2020-1**

### ***Amendments to Australian Auditing Standards made under Section 336 of the Corporations Act 2001***

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ASA 710	<i>Comparative Information-Corresponding Figures and Comparative Financial Reports</i> (1 December 2015)
ASA 720	<i>The Auditor's Responsibilities Relating to Other Information</i> (1 December 2015)
ASA 800	<i>Special Considerations-Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks</i> (30 May 2017)

The amendments arise from changes made by the International Auditing and Assurance Standards Board (IAASB) to numerous International Standards on Auditing (ISAs) in response to the revised and restructured International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code). Under the Strategic Direction given to the AUASB by FRC, the AUASB is required to have regard to any programme initiated by the IAASB for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards.

Draft

## **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 2020-1 *Amendments to Australian Auditing Standards made under Section 336 of the Corporations Act 2001* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

Dated: <TypeHere>

R Simnett AO  
Chair - AUASB

## **Conformity with International Standards on Auditing**

This Auditing Standard has been made for Australian legislative purposes. It contains a series of amendments to various Australian Auditing Standards (as shown) arising from changes made by the International Auditing and Assurance Standards Board (IAASB) to numerous International Standards on Auditing (ISAs) in response to the revised and restructured International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) and accordingly there is no equivalent International Standard on Auditing (ISA) issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

*Draft*

## AUDITING STANDARD ASA 2020-1

### *Amendments to Australian Auditing Standards made under Section 336 of the Corporations Act 2001*

#### Application

1. This Auditing Standard applies to:
  - (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
  - (b) an audit of a financial report, or a complete set of financial statements, for any other purpose.
2. This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

#### Operative Date

3. This Auditing Standard is operative for engagements with financial reporting periods ending on or after <date> 2020. [Early adoption of this Auditing Standard is permitted prior to this date.]

#### Introduction

##### Scope of this Auditing Standard

4. This Auditing Standard makes amendments to the Australian Auditing Standards. The amendments to the Australian Auditing Standards arise from changes made by the International Auditing and Assurance Standards Board (IAASB) to numerous International Standards on Auditing (ISAs) in response to the revised and restructured International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code) made under Section 336 of the *Corporations Act 2001*.
5. This Auditing Standard uses underlining, striking out and other typographical material to identify the amendments to Auditing Standards, in order to make the amendments more understandable. Amendments made to text contained in footnotes are shown within the footnotes and underlining and striking out are also used to identify amendments. However, the amendments made by this Auditing Standard do not include that underlining, striking out or other typographical material.

#### Objective

6. The objective of this Auditing Standard is to make amendments to the following Auditing Standards:
  - ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance Engagements and Related Services Engagements* (30 May 2017)
  - ASA 100 *Preamble to AUASB Standards* (28 April 2006)
  - ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards* (5 December 2018)

- 
- ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Financial Information* (30 May 2017)
- ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* (5 December 2018)
- ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report* (30 May 2017)
- ASA 260 *Communication With Those Charged With Governance* (5 December 2018)
- ASA 510 *Initial Audit Engagements—Opening Balances* (15 December 2016)
- ASA 570 *Going Concern* (15 December 2016)
- ASA 600 *Special Considerations—Audits of a Group Financial Report* (1 December 2015)
- ASA 620 *Using the Work of an Auditor's Expert* (27 October 2009)
- ASA 700 *Forming an Opinion and Reporting on a Financial Report* (5 December 2018)
- ASA 705 *Modifications to the Opinion in the Independent Auditor's Report* (15 December 2016)
- ASA 706 *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* (15 December 2016)
- ASA 710 *Comparative Information—Corresponding Figures and Comparative Financial Reports* (15 December 2016)
- ASA 720 *The Auditor's Responsibilities Relating to Other Information* (15 December 2016)
- ASA 800 *Special Considerations—Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* (15 December 2016)

## **Definition**

7. For the purposes of this Auditing Standard, the meanings of terms are set out in each Auditing Standard and in the *AUASB Glossary*. This Auditing Standard does not introduce new definitions.

## **Amendments to Auditing Standards**

### **Amendments to ASQC 1**

8. Paragraph 21 is amended to read as follows:

...

- (b) ~~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, 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.~~

AUST R400.12.1

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Where a Member in Public Practice identified multiple threats to Independence, which individually might not be significant, the Member shall evaluate the significance of those threats in aggregate and the safeguards applied or in place to eliminate some or all of the threats or reduce them to an Acceptable Level in aggregate.

9. Paragraph 22 is amended to read as follows:

...

- (b) Personnel to promptly notify the firm of ~~circumstances and relationships that create a~~ threats to compliance with independence requirements so that 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~~; and

...

10. Paragraph 25 is amended to read as follows:

...

- (a) Eliminating the threat or setting out criteria for applying determining the need for safeguards to reduce the threat of the long association with an entity to an acceptable level, the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and

...

11. Paragraph A11 is amended to read as follows:

Written confirmation may be in paper or electronic form. By obtaining confirmation and taking appropriate action on information indicating a breach non-compliance, the firm demonstrates the importance that it attaches to independence and makes the issue current for, and visible to, its personnel.

12. Paragraph A12.1 is amended to read as follows:

Long Association with an Entity Familiarity Threat (Ref: Para. 25)

A ~~familiarity~~ threat may be created as a result of an individual's long association with:

- The entity and its operations;
- The entity's senior management; or
- The underlying subject matter and subject matter information of the assurance engagement.

~~by using the same senior personnel on an assurance engagement over a long period of time.~~

13. Paragraph Aus A13.1 is amended to read as follows:

The APES 110 Code of Ethics for Professional Accountants (including Independence Standards) includes examples of factors 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. APES 110 also provides examples of actions:

- Eliminating the threats by rotating the individual off the engagement team; or



- Applying safeguards to reduce the threats to an acceptable level.

~~Determining appropriate criteria to address familiarity threats may include matters such as:~~

- ~~The nature of the engagement, including the extent to which it involves a matter of public interest; and~~
- ~~The length of service of the senior personnel on the engagement.~~

~~Examples of safeguards that might be appropriate to address familiarity threats include rotating the senior personnel or requiring an engagement quality control review.~~

14. Paragraph A14.1 is amended to read as follows:

The Corporations Act 2001 and relevant ethical requirements require the rotation of the engagement partner, the engagement quality control reviewer, and other key audit partners in respect of certain engagements. A familiarity threat is particularly relevant in the context of financial report audits of listed entities. For these audits, relevant ethical requirements and the Corporations Act 2001 specify partner rotation requirements.

15. The following footnote, referenced to paragraph A56 of this Auditing Standard, is amended as footnote 5:

- <sup>5.</sup> See for example, paragraphs R114.1, 114.1 A1, 114.1 A1.1 and R360.26 Section 140.7 and Section 225.35 of APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

#### **Amendments to ASA 100**

16. Paragraph 39 is amended to read as follows:

The auditor is subject to relevant ethical requirements, including those pertaining to independence, relating to audit engagements as defined in ASA 102. The relevant ethical requirements relating to audit engagements referred to in Auditing Standards are contained in the respective codes of professional conduct of the professional accounting bodies in Australia.<sup>6</sup> The codes of professional conduct are aligned with the equivalent international code.<sup>7</sup>

#### **Amendments to ASA 200**

17. Paragraph A19 is amended to read as follows:

ASQC 1<sup>9</sup> deals with the firm's responsibilities to establish and maintain its system of quality control for audit engagements.<sup>10</sup> ASQC 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.<sup>11</sup> ASA 220 sets out the engagement partner's responsibilities with respect to relevant ethical requirements. These include remaining alert, through observation and making enquiries as necessary, for evidence of breaches 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 breached ~~not complied with~~ relevant ethical requirements, and forming a conclusion on compliance with independence requirements that apply to the audit engagement.<sup>12</sup> ASA 220 recognises 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.

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**Amendments to ASA 220**

18. Paragraph 9 is amended to read as follows:

Throughout the audit engagement, the engagement partner shall remain alert, through observation and making enquiries as necessary, for evidence of breaches of non-compliance ~~with~~ relevant ethical requirements by members of the engagement team. (Ref: Para. A4-A5)

19. Paragraph 10 is amended to read as follows:

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~~ breached relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)

20. Paragraph 11 is amended to read as follows:

...

- (a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate ~~circumstances and relationships that create~~ threats to independence;

...

- (c) Evaluate whether the identified threats are at an acceptable level; and

- (d) Take appropriate action to address the threats by eliminating the circumstances that create the threats, applying safeguards, or withdrawing ~~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. Aus A5.1, A6-A7)

21. Paragraph A6 is amended to read as follows:

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 the appropriate action, which may include eliminating the circumstance that is creating activity or interest that creates the threat, or withdrawing from the audit engagement, where withdrawal is possible under applicable law or regulation.

22. The following footnotes, referenced to paragraph A9 of this Auditing Standard, are amended as footnotes 6 and 7:

<sup>6.</sup> See, for example, paragraph R320.8 Sections 240.14 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

<sup>7.</sup> See, for example, paragraph R360.22 Sections 225.34 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

**Amendments to ASA 240**

23. Paragraph A6 is amended to read as follows:

Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* issued by the Accounting and

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Professional and Ethical Standards Board 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 report.<sup>15</sup>

15. See paragraphs R360.16-360.18 A1 Sections 225.21 225.22 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

#### **Amendments to ASA 250**

24. Paragraph A8 is amended to read as follows:

Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further action. For example, the APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* issued by the Accounting Professional and Ethical Standards Board (APES 110) 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 report.<sup>11</sup>

11. See paragraphs R360.16-360.18 A1 Sections 225.21 225.22 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

25. The following footnotes, referenced to paragraph A30 of this Auditing Standard, are amended as footnotes 17 and 18:

17. See, for example, paragraphs 360.21 A1 and 360.25 A1–R360.27 Section 225.29 and Sections 225.33 225.36 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

18. See, for example, paragraphs R114.1– R114.1 A1 and R360.26 Section 140.7 and Section 225.35 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

26. The following footnote, referenced to paragraph A36 of this Auditing Standard, are amended as footnote 19:

19. See, for example, paragraph R360.28 Section 225.37 of the APES 110 Code of Ethics for Professional Accountants (including Independence Standards).

#### **Amendments to ASA 260**

27. Paragraph 17 is amended to read as follows:

In the case of listed entities, the auditor shall communicate with those charged with governance:

...

- (ii) 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 The related safeguards that have been applied to eliminate identified threats to independence or reduce them the threats to an acceptable level. (Ref: Para. A29–A32)

...

28. Paragraph A30 is amended to read as follows:

The communication about relationships and other matters, and how threats to independence that are not at an acceptable level have been addressed ~~safeguards to be communicated, vary~~ varies with the circumstances of the engagement and generally addresses the threats to independence, safeguards to reduce the threats, and measures to eliminate threats., ~~but generally address:~~

- (a) ~~Threats to independence, which may be categorised as: self interest threats, self review threats, advocacy threats, familiarity threats, and intimidation threats; and~~
- (b) ~~Safeguards created by the profession, legislation or regulation, safeguards within the entity, and safeguards within the firm's own systems and procedures.~~

29. Paragraph A49 is amended to read as follows:

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:

...

- Communications regarding independence may be appropriate whenever significant judgements are made about threats to independence and how threats to independence that are not at an acceptable level will be addressed ~~related safeguards~~, for example, when accepting an engagement to provide non-audit services, and at a concluding discussion.

...

## **Amendments to ASA 510**

### *Amendments to ASA 510 Appendix 1 Illustration 1 and [Aus] Illustration 2A*

30. The eighth point of both Illustration 1 and [Aus] Illustration 2A are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

31. Example Auditor's Report for Qualified opinion – Jurisdiction Prohibits a Qualified Opinion on Performance and Cash Flows and an Unmodified Opinion on Financial Position (Fair Presentation Framework) is amended to read as follows:

...

#### **Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Report section of our report. We are independent of the Entity in

accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

...

32. Example of Auditor's Report for Qualified opinion – Jurisdiction Prohibits a Qualified Opinion on Performance and Cash Flows and an Unmodified Opinion on Financial Position *Corporations Act 2001* (Fair Presentation Framework) are amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

**Amendments to ASA 570**

*Amendments to ASA 570 Appendix 2 [Aus] Illustration 1A, [Aus] Illustration 2A, [Aus] Illustration 3A and [Aus] Illustration 4A*

33. The fifth point of [Aus] Illustration 1A and fourth point of [Aus] Illustration 2A, [Aus] Illustration 3A and [Aus] Illustration 4A are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

34. Example Auditor's Report for Unmodified Opinion, Material Uncertainty Exists, Adequate Disclosure for Single Company – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act*

2001 and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

35. Example Auditor's Report for Qualified Opinion, Material Uncertainty Exists, Inadequate Disclosure for Single Listed Company – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

36. Example Auditor's Report for Adverse Opinion, Material Uncertainty Exists, Inadequate Disclosure for Single Listed Company – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Adverse Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

**Amendments to ASA 600**

*Amendments to ASA 600 Appendix 1 Illustration 1 and [Aus] Illustration 1A*

37. The seventh point of both Illustration 1 and [Aus] Illustration 1A are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

38. Example Auditors' Reports on General Purpose Financial Report – Qualified Opinion where the group engagement team is not able to obtain sufficient appropriate audit evidence on which to base the group audit opinion (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

39. Example Auditors' Reports on General Purpose Financial Report – Qualified Opinion under *Corporations Act 2001* where the group engagement team is not able to obtain sufficient appropriate audit evidence on which to base the group audit opinion (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

**Amendments to ASA 620**

40. Paragraph A18 is amended to read as follows:

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 example, the auditor's expert's profession, legislation or regulation).~~ Such threats may be addressed by

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eliminating the circumstances that create the threats, applying safeguards, 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.

41. Paragraph A19 is amended to read as follows:

The evaluation of ~~whether the threats to objectivity are at an acceptable level~~ 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 information that is being audited, that is, if the auditor's expert is a management's expert.

#### **Amendments to ASA 700**

42. Paragraph 40 is amended to read as follows:

The Auditor's Responsibilities for the Audit of the Financial Report section of the auditor's report also shall: (Ref: Para. A50)

...

- (b) For audits of the financial report 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 communicate with them all relationships and other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, related safeguards how threats have been eliminated or safeguards applied; and

...

*Amendments to ASA 700 Appendix 1 [Aus] Illustration 1A, [Aus] Illustration 2A, Illustration 3 and Illustration 4*

43. The fifth point of [Aus] Illustration 1A, [Aus] Illustration 2A, Illustration 3 and Illustration 4 are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (including Independence Standards).

44. Example Auditor's Report for Single Company – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

#### **Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (including Independence



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*Standards*) (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

**Auditor's Responsibilities for the Audit of the Financial Report**

...

We also provide the directors 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~~ how threats have been eliminated or safeguards applied.

...

45. Example Auditor's Report for Group Entity – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

**Auditor's Responsibilities for the Audit of the Financial Report**

...

We also provide the directors 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~~ how threats have been eliminated or safeguards applied.

...

46. Example Auditor's Report for Single Entity (not listed) (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in

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accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

...

47. Example Auditor's Report for Single Entity (not listed) (Compliance Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

...

**Amendments to ASA 705**

*Amendments to ASA 705 Appendix [Aus] Illustration 1A, [Aus] Illustration 2A, [Aus] Illustration 3A, Illustration 4 and Illustration 5*

48. The fifth point of [Aus] Illustration 1A, [Aus] Illustration 2A, [Aus] Illustration 3A, Illustration 4 and Illustration 5 are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

49. Example Auditor's Report for Single Company – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

50. Example Auditor's Report for Consolidated Entity – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Adverse Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

51. Example Auditor's Report for Consolidated Entity – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

52. Example Auditor's Report for Consolidated Entity (not listed) (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Disclaimer Opinion**

...

We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

**Amendments to ASA 706**

*Amendments to ASA 706 Appendix 3 [Aus] Illustration 1A and [Aus] Illustration 2A*

53. The fifth point of [Aus] Illustration 1A and [Aus] Illustration 2A are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

54. Example Auditor's Report for Single Company – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

55. Example Auditor's Report for Single Company (not listed) (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

...

## **Amendments to ASA 710**

*Amendments to ASA 710 Appendix 1 Illustration 1, [Aus] Illustration 1A, Illustration 2, [Aus] Illustration 2A, Illustration 3 and Illustration 4*

56. The seventh point of Illustration 1, [Aus] Illustration 1A, Illustration 2, [Aus] Illustration 2A, Illustration 3 and eighth point of Illustration 4 are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

57. Example Auditor's Report of General Purpose Financial Report on Corresponding Figures, Qualified Opinion on prior year, which materially affects current year financial report (Fair Presentation Framework) is amended to read as follows:

...

### **Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

...

58. Example Auditor's Report of General Purpose Financial Report on Corresponding Figures, Qualified Opinion on prior year, which materially affects current year financial report – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

### **Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

59. Example Auditor's Report of General Purpose Financial Report on Corresponding Figures, Qualified Opinion on prior year, which affects the comparability of the current year financial report (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

...

60. Example Auditor's Report of General Purpose Financial Report on Corresponding Figures, Qualified Opinion on prior year, which affects the comparability of the current year financial report – *Corporations Act 2001* (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

61. Example Auditor's Report of General Purpose Financial Report on Corresponding Figures, Prior year financial report audited by a predecessor auditor, and is referred to in the auditor's report on the current year financial report (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the

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Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

...

62. Example Auditor's Report of General Purpose Financial Report on Comparative Financial Reports, Qualified opinion on prior year financial report, which materially affects current year financial report (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our qualified audit opinion.

...

**Amendments to ASA 720**

*Amendments to ASA 720 Appendix 3 [Aus] Illustration 1A, [Aus] Illustration 2A, Illustration 3, [Aus] Illustration 4A, [Aus] Illustration 5A, [Aus] Illustration 6A and [Aus] Illustration 7A*

63. The fifth point of [Aus] Illustration 1A, [Aus] Illustration 2A, Illustration 3, [Aus] Illustration 4A, [Aus] Illustration 5A, [Aus] Illustration 6A and [Aus] Illustration 7A are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

64. Example Auditor's Report of Single Company – *Corporations Act 2001* Unmodified opinion – all of the Other Information obtained (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

- ...
65. Example Auditor's Report of Single Company – *Corporations Act 2001* Unmodified opinion – part of the Other Information obtained (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

66. Example Auditor's Report of Single Company – non *Corporations Act 2001* Unmodified opinion – part of the Other Information obtained (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

...

67. Example Auditor's Report of Single Company – *Corporations Act 2001* Unmodified opinion – No Other Information obtained (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards



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Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

68. Example Auditor's Report of Single Company – *Corporations Act 2001* Unmodified opinion – All Other Information obtained; material misstatement exists (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

69. Example Auditor's Report of Consolidated Entity – *Corporations Act 2001* Qualified opinion that affects the Other Information obtained (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Qualified Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

70. Example Auditor's Report of Consolidated Entity – *Corporations Act 2001* Adverse opinion that affects the Other Information obtained (Fair Presentation Framework) is amended to read as follows:

...

**Basis for Adverse Opinion**

...

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We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

#### **Amendments to ASA 800**

*Amendments to ASA 800 Appendix 1 Illustration 1, Illustration 2, [Aus] Illustration 4 and [Aus] Illustration 5*

71. The sixth point of Illustration 1, [Aus] Illustration 4, [Aus] Illustration 5 and fifth point of Illustration 2 are amended to read as follows:

The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*.

72. Example Auditor's Report of Illustration 1: An auditor's report on a financial report of an entity other than a listed entity prepared in accordance with the financial reporting provisions of a contract (for purposes of this illustration, a compliance framework) is amended to read as follows:

...

#### **Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia, and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

...

73. Example Auditor's Report of Illustration 2: An auditor's report on a financial report of an entity other than a listed entity prepared in accordance with the tax basis of accounting in Jurisdiction X (for purposes of this illustration, a compliance framework) is amended to read as follows:

...

#### **Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Partnership in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia, and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

...

74. Example Auditor's Report of [Aus] Illustration 4: An auditor's report on a financial report prepared by a non-reporting entity under the *Corporations Act 2001* (for purposes of this illustration, a fair presentation framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...

75. Example Auditor's Report of [Aus] Illustration 5: An auditor's report on a financial report prepared by a not-for-profit incorporated association in accordance with the financial reporting provisions of the applicable legislation (for purposes of this illustration, a fair presentation framework) is amended to read as follows:

...

**Basis for Opinion**

...

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Entity in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

...



# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO. **5**

**Meeting Date:** 4 February 2020  
**Subject:** ASA 315 Identifying and Assessing Risks of Material Misstatement  
**Date Prepared:** 28 January 2020  
**Prepared By:** Anne Waters – AUASB Senior Project Manager

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☒ **Action Required**

☐ **For Information Purposes Only**

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## Agenda Item Objectives

1. For the AUASB to consider and agree if there are any compelling reasons amendments that need to be reflected in the final ASA 315 *Identifying and Assessing the Risks of Material Misstatement*.
2. For the AUASB to consider whether ASA 315 should be re-exposed.
3. Dependent on 1 and 2, for the AUASB consider and approve to issue:
  - (a) ASA 315;
  - (b) ASA 315 Explanatory Statement.
4. Provide feedback on the draft ASA 315 Basis for Conclusions
5. Provide input into the Communications and Implementation Guidance Plan.

## Background

6. The IAASB has been working on a project to revise ISA 315. The final ISA 315 was approved at the September 2019 IAASB meeting and has been released effective for engagements commencing on or after 15 December 2021.
7. The AUASB exposed for public comment the IAASB's proposed amendments to ISA 315 in Australia concurrently with the IAASB's exposure draft. The AUASB issued exposure drafts (ED

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

01/18<sup>1</sup> and ED 02/18<sup>2</sup>) in August 2018 with a 70 day comment period, as well as holding roundtables in Melbourne, Sydney, Perth, Adelaide, Brisbane and Canberra, and held a webinar, in order to gather feedback on the proposed amendments.

8. On 2 November 2018 the AUASB provided a submission to the IAASB noting that there were a number of matters that in the AUASB's view needed to be addressed by the IAASB. The AUASB have been actively monitoring the IAASB's revisions to ISA 315 to ensure that the matters raised in our submission have been addressed.
9. The AUASB has actively monitored the development of ISA 315 and have provided feedback to the AUASB Chair to consider in his capacity as an IAASB member.
10. At its September 2019 meeting the AUASB reviewed the latest draft of ISA 315 which was being presented at the IAASB September 2019 meeting for approval as a standard. The AUASB agreed that the matters raised in its submission to the IAASB on ED 315 had been substantially addressed, however were of the view that the latest version of ISA 315 was still quite complex, and scalability was still an issue. The AUASB highlighted areas where further clarification was required to the proposed ISA 315 for the AUASB Chair to consider in his capacity as an IAASB member. In particular the AUASB gave feedback that:
  - (a) A clearer link between ISA 315 and the definition of risk of material misstatement in ISA 200 was required; and
  - (b) Further consideration of the requirements determining which control activities require design and implementation testing was necessary.

The points raised by the AUASB were provided to the IAASB's ISA 315 Task Force for consideration. The AUASB received an email from AUASB Chair Roger Simnett on 24 September 2019 with a summary of how this feedback was addressed in the final version of ISA 315. This is also included in the Board papers for the AUASB information (refer Feb20\_5.0.1\_SummaryIAASBSepMeeting.)

11. ISA 315 and the related conforming amendments were approved by the IAASB at its September 2019 meeting, and they voted that re-exposure was not necessary.

### **Matters for the AUASB to consider:**

#### ***Compelling reason analysis***

12. As detailed in the AUASB's [\*Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board \(IAASB\) and Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board \(NZAuASB\)\*](#),<sup>1</sup>:
  - (a) In implementing the FRC's strategic direction, the AUASB has determined the following objectives:
    - (i) To adopt international auditing and assurance standards in Australia unless there are strong reasons not to (which the AUASB describes as "compelling reasons"); and

<sup>1</sup> Exposure Draft 01/18: Proposed ASA 315 Identifying and Assessing the Risks of Material Misstatement (ED 01/18)

<sup>2</sup> Exposure Draft 02/18: Proposed ASA 2018-1 Amendments to Australian Auditing Standards (ED 02/18) (Consequential and conforming amendments)

- (ii) To work with the New Zealand Auditing and Assurance Standards Board (NZAuASB) towards the establishment of harmonised standards based on international standards.
- (b) The AUASB may consider modifying international standards for application in Australia under either of those objectives. The AUASB considers such modifications acceptable provided that they consider the public interest<sup>3</sup>, and do not conflict with, or result in lesser requirements than, the international standards.
- (c) The international standards should be adopted and should be modified only if there are compelling reasons to do so. In the case of an international standard that is being reviewed for the purpose of adoption in Australia, the **compelling reasons test** for modifications in the public interest is triggered where the international standard does not reflect, or is not consistent with:
  - (i) The Australian regulatory arrangements; or
  - (ii) Principles and practices that are considered appropriate in Australia (including in the use of significant terminology).
- 13. The AUASB Technical Group (ATG) have not identified any matters in ISA 315 which meet the compelling reason test above.
- 14. The NZAuASB have approved one compelling reason change which is carried forward from extant ISA (NZ) 315. The change is underlined below:

#### ISA (NZ) 315

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;
- 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

This difference does not exist in the Australian extant ASA 315. The NZAuASB have agreed to make this amendment to remain consistent with a current compelling reason adjustments made to ISA (NZ) 580<sup>4</sup> paragraphs 9 – 12 which require representations must be obtained from those charged with governance, whilst the ISA and ASA requirements refer only to management. The NZAuASB have made this amendment as those charged with governance are have ultimate responsibility for ensuring an entity meets its legal obligations. The NZAuASB amendment is not included in ASA 580.

<sup>3</sup> IFAC defines the public interest as "The net benefits derived for, and procedural rigor employed on behalf of, all society in relation to any action, decision or policy". Refer IFAC Policy Position 5, A Definition of the Public Interest, June 2012.

<sup>4</sup> ISA (NZ) 580 *Written Representations*

The ATG have concluded that this amendment by the NZAuASB does not meet the compelling reason test and is not a required amendment to ASA 315 as:

- this is not required for consistency with ASA 580;
- ASA 315 (A51) is related to “Why an understanding of the entity and its environment... is required” and explains that this understanding assists auditors in assessing the appropriateness and completeness of management’s representations. ASA 580 requires auditors to obtain representations from the appropriate individuals who are responsible for the preparation of the financial report and for the completeness of the information provided to the auditor, which may be those charged with governance, or management, depending on the governance structure of the entity. Whilst adding “those charged with governance” to A51 is not incorrect, and would assist with consistency with other standards which require representations, the ATG are of the view that this will have minimal impact in practice, and it is not necessary to change this.

#### **ATG’s conclusion and recommendation**

The ATG have not identified any matters which meet the compelling reason test. When forming this view the ATG have taken the following into account:

- (a) The matters raised by the AUASB in its submission to the IAASB have largely been addressed, and in particular the more significant matters;
- (b) Whilst Australian stakeholders had considerable feedback on ED 315 this was reflected in the AUASB’s submission and have been addressed. No stakeholder raised any compelling reasons due to Australian regulatory matters in submissions or at the roundtables;
- (c) The matters raised by the AUASB on the final draft of ISA 315 being considered by the IAASB have largely been addressed, and in particular the more significant matters (refer to paragraph 10);
- (d) The compelling reason adjustment made by NZAuASB is not applicable or required in Australia (refer paragraph 14 above);
- (e) The ATG have reviewed final ISA 315 and have not noted any matters which meet the definition of compelling reasons; and
- (f) There are no compelling reason adjustments in extant ASA 315.

#### **Action for the AUASB**

Consider if you agree with the ATG’s assessment that there are no compelling reasons and no Australian amendments to ASA 315?

#### **Re-exposure**

15. Following approval of the standard at its September 2019 meeting the IAASB voted on whether ISA 315 should be re-exposed. Refer to the IAASB’s paper which details the matters they considered ([IAASB ISA 315 re-exposure considerations](#)) when evaluating this decision (a link is provided for the AUASB’s information).
16. The principal consideration in the IAASB’s due process is “whether there has been substantial change to the exposed document such that re-exposure is necessary.” The IAASB’s due process includes three examples of situations that may constitute potential grounds for a decision to re-expose:

- (a) Substantial change to a proposal arising from matters not aired in the exposure draft (ED) such that commentators have not had an opportunity to make their views known to the IAASB before it reaches a final conclusion;
  - (b) Substantial change arising from matters not previously deliberated by the IAASB; or
  - (c) Substantial change to the substance of a proposed international pronouncement.
17. To facilitate the IAASB's consideration the ISA 315 Task Force prepared an analysis comparing final ISA 315 to ED-315 and extant ISA 315. The Task Force concluded that the changes from ED-315 were responding to the feedback received about the complexity of the standard, whilst the key elements of ED-315 have been retained. The Task Force have also noted that they believe re-exposing will not result in new information or concerns which have not been raised through the exposure process and the subsequent outreach performed.
18. The IAASB voted not to re-expose ISA 315.
19. [The AUASB's Function and Processes document](#) does not explicitly cover the matters to consider when considering re-exposure as this document is based on the process of exposing the final ASA. However it does include the following:

In extremely rare cases, the AUASB may decide that proposed changes to the original exposure draft, arising from the public exposure, are of such significance that the standard should be publically exposed for a second time.

#### **ATG's conclusion and recommendation**

The ATG recommend that ASA 315 is not re-exposed in Australia. The ATG also considered that as we are required to adopt ISAs the only purpose of re-exposure would be the identification of compelling reasons, and given the nature of the standard (i.e. risk assessment) there are unlikely to be matters which meet this test.

#### **Action for the AUASB**

Consider if you agree with the ATG's conclusion and recommendation to not re-expose ASA 315?.

#### ***Consider and approve standards***

20. Dependent on the outcome of the above, the AUASB is asked to consider and approve proposed ASA 315 (Paper Feb20\_5.0.2\_ASA315.) and ASA 315 Explanatory Statement (Paper Feb20\_5.0.3\_Explanatory Statement).
21. ASA 315 mirrors ISA 315 with no Australian specific amendments except for the following standard Australian changes:
- (a) Add the Australian application paragraph;
  - (b) Financial statements changed to financial report
  - (c) Spelling from American to Australian
  - (d) Footnotes changed where required.



22. As part of our quality review process the ATG have noted some footnotes in ISA 315 which require amending to refer correctly to the ASAs. This cannot be finalised until the ASA 315 conforming amendments are finalised to ensure all paragraph references are correct.
23. The ATG have also prepared the ASA 315 Basis of Conclusion (Paper Feb20\_5.0.4\_ASA315Basis for Conclusion) which includes a link to the IAASB's Basis of Conclusions.

#### **Action for the AUASB**

Do you approve ASA 315 and ASA 315 Explanatory Statement for issue, subject to the ATG finalising the quality review of footnote references?

Do you agree with the operative date of periods commencing on or after 15 December 2021?

Provide feedback of changes to ASA 315 Basis for Conclusions.

#### **Conforming Amendments**

24. The IAASB issued Conforming and Consequential Amendments to Other International Standards at the time of issuing ISA 315. Based on this the ATG commenced drafting the Conforming Amendments to other ASAs through Auditing Standard 2020-2 *Amendments to Australian Auditing Standards I* (ASA 2020-2), for approval by the AUASB at this meeting.
25. When conducting a quality review of ASA 2020-2 we identified a number of amendments which were not included in the IAASB's document. NZAuASB Staff also notified us that they had also noted some missing amendments. The matters we identified as missing mainly related to references to the name of ISA 315 which has now changed, and footnote cross references.
26. We advised IAASB staff of this and they have acknowledged that there are a number of amendments not included in their document and they are conducting a review to identify them all. We are waiting for the complete list of amendments.
27. This has resulted in a delay in the finalising of ASA 2020-2. The ATG will forward the amending standard to the AUASB for approval out of session in the coming weeks.

#### **Communications / Implementation support plan**

28. The ATG have a communications plan with two stages:
  - (a) Initial release of ASA 315; and
  - (b) Implementation support plan
29. The initial release of ASA 315 will be communicated via email to AUASB subscribers, AUASB newsletter, professional bodies, social media (Linked In and Twitter).
30. The IAASB have committed to provide implementation support which will commence first quarter 2020 (refer Feb20\_5.0.5\_ISA315ImplementationPlan). The IAASB will also hold a webinar. The ATG will issue the IAASB's support documents and webinar as they become available.
31. The ATG will also:
  - (a) Consider if further implementation support is required, including for smaller audits and practitioners, and

- (b) Work with the professional bodies and present at appropriate educational forums.

**Action for the AUASB**

Any other communications or implementation support required?

**Part B – NZAuASB**

32. The NZAuASB have approved ISA 315 for issue with one compelling reason as discussed above. The NZAuASB are yet to consider the conforming amendments. The ATG are working with the NZAuASB staff on ensuring all conforming amendments are identified.

**Material Presented**

Agenda Item	Feb20_5.0.0_AUASB Board Meeting Summary Paper
Agenda Item	Feb20_5.0.1_SummaryIAASBSepMeeting
	Feb20_5.0.2_ASA 315
	Feb20_5.0.3_ASA315ExplanatoryStatement
	Feb20_5.0.4_ASA315Basis for Conclusion
	Feb20_5.0.5_ISA315ImplementationPlan

**ASA 315**  
(February 2020)

# **Auditing Standard ASA 315**

## ***Identifying and Assessing the Risks of Material Misstatement***

Issued by the **Auditing and Assurance Standards Board**



**Australian Government**

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**Auditing and Assurance Standards Board**

## Obtaining a Copy of this Auditing Standard

This Auditing Standard is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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## PREFACE

### Reasons for Issuing ASA 315


The AUASB issues Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is a Non Corporate Commonwealth entity of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislation Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required, inter alia, to develop auditing standards that have a clear public interest focus and are of the highest quality.

### Main Features

This Auditing Standard represents the Australian equivalent of ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement* and will replace the current ASA 315 issued by the AUASB in December 2015 (as amended).

This Auditing Standard contains differences / no differences from the reissued ISA 315, which have been made to <TypeHere> 

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

This Auditing Standard is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. This Auditing Standard is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

Dated: <TypeHere>

R Simnett AO  
Chair - AUASB

## **Conformity with International Standards on Auditing**

This Auditing Standard conforms with International Standard on Auditing ISA 315 (Revised 2019) *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 Auditing Standard (and do not appear in the text of the equivalent ) are identified with the prefix “Aus”.

Compliance with this Auditing Standard enables compliance with ISA 315.



## AUDITING STANDARD ASA 315

### *Identifying and Assessing the Risks of Material Misstatement*

#### Application

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
  - (b) an audit of a financial report, or a complete set of financial statements, for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

#### Operative Date

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 15 December 2021.

#### Introduction

##### Scope of this Auditing Standard

1. This Auditing Standard deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial report.

##### Key Concepts in this ASA

2. ASA 200 deals with the overall objectives of the auditor in conducting an audit of the financial report,<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> ASA 200 explains that the risks of material misstatement may exist at two levels:<sup>4</sup> the overall financial report level; and the assertion level for classes of transactions, account balances and disclosures.
3. ASA 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 report to be materially misstated.<sup>5</sup>
4. Risks at the financial report level relate pervasively to the financial report 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.

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<sup>1</sup> See ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

<sup>2</sup> See ASA 200, paragraph 17.

<sup>3</sup> See ASA 200, paragraph 13(c).

<sup>4</sup> See ASA 200, paragraph A36.

<sup>5</sup> See ASA 200, paragraphs 15–16.

- 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. ASA 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 control risk is required by this ASA. As explained in ASA 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 ASA 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 ASA, the significance of fraud is such that further requirements and guidance are included in ASA 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 ASA, 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 ASA and ASA 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 ASA 330, or if new information is obtained.
  8. ASA 330 requires the auditor to design and implement overall responses to address the assessed risks of material misstatement at the financial report level.<sup>8</sup> ASA 330 further explains that the auditor's assessment of the risks of material misstatement at the financial report level, and the auditor's overall responses, is affected by the auditor's understanding of the control environment. ASA 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. ASA 200 states that some ASAs 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 ASA 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.

### **Effective Date**

10. [Deleted by the AUASB. Refer to Aus 0.3]

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<sup>6</sup> See ASA 200, paragraph A43 and ASA 330 *The Auditor's Responses to Assessed Risks*, paragraph 6.

<sup>7</sup> See ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Report*.

<sup>8</sup> See ASA 330, paragraph 5.

<sup>9</sup> See ASA 330, paragraph 6.

<sup>10</sup> See ASA 200, paragraph A65.

## **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 report and assertion levels thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement.

## **Definitions**

12. For the purposes of this Auditing Standard, 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 report which are inherent in management representing that the financial report is 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 ASA:

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<sup>11</sup> See ASA 240, paragraphs A24–A27.

- (i) 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) The IT infrastructure comprises the network, operating systems, and databases and their related hardware and software.
  - (iii) 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 report 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
  - (ii) That is to be treated as a significant risk in accordance with the requirements of other ASAs.<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 ASAs, 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.

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<sup>12</sup> See ASA 240, paragraph 27 and ASA 550, *Related Parties*, paragraph 18.

## **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 report and assertion levels; and
  - (b) The design of further audit procedures in accordance with ASA 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
  - (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 report 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 report 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

21.	The auditor shall obtain an understanding of the control environment relevant to the preparation of the financial report, through performing risk assessment procedures, by: (Ref: Para. A99–A100)	
(a)	Understanding the set of controls, processes and structures that address: (Ref: Para. A101–A102)	and (b) Evaluating whether: (Ref: Para. A103–A108) <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>
	<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> </ul>	

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(v)	How the entity holds individuals accountable for their responsibilities in the pursuit of the objectives of the system of internal control;	
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The entity's risk assessment process

22. The auditor shall obtain an understanding of the entity's risk assessment process relevant to the preparation of the financial report, through performing risk assessment procedures, by:		
(a)	Understanding the entity's process for: (Ref: Para. A109–A110)	and
(i)	Identifying business risks relevant to financial reporting objectives; (Ref: Para. A62)	(b)
(ii)	Assessing the significance of those risks, including the likelihood of their occurrence; and	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)
(iii)	Addressing those risks;	

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

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 report, through performing risk assessment procedures, by: (Ref: Para. A114–A115)		
(a)	Understanding those aspects of the entity's process that address:	and
(i)	Ongoing and separate evaluations for monitoring the effectiveness of controls, and the identification and remediation of control	(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)

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

The information system and communication

<p>25. The auditor shall obtain an understanding of the entity’s information system and communication relevant to the preparation of the financial report, 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 report; and</p> <p>b. Information about events and conditions, other than transactions, is captured, processed and disclosed in the financial report;</p> <p>(ii) The accounting records, specific accounts in the financial report</p>	<p>and</p> <p>(c) Evaluating whether the entity’s information system and communication appropriately support the preparation of the entity’s financial report in accordance with the applicable financial reporting framework. (Ref: Para. A146)</p>



<p>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 report, 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 report 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

26. The auditor shall obtain an understanding of the control activities component, through performing risk assessment procedures, by: (Ref: Para. A147–A157)		
<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-recurring, unusual transactions or adjustments; (Ref: Para. A160–A161)</li> <li>(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)</li> <li>(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)</li> </ul> <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> <ul style="list-style-type: none"> <li>(i) The related risks arising from the use of IT; and</li> <li>(ii) The entity’s general IT controls that address such risks.</li> </ul>	<p>and</p> <p>(d) For each control identified in (a) or (c)(ii): (Ref: Para. A175–A181)</p> <ul style="list-style-type: none"> <li>(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</li> <li>(ii) Determining whether the control has been implemented by performing procedures in addition to enquiry of the entity’s personnel.</li> </ul>	

*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 report 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 Report Level*

30. For identified risks of material misstatement at the financial report 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 report.

*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 report 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 report 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.

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<sup>13</sup> See ASA 230, *Audit Documentation*, paragraphs 8–11, and A6–A7.

## **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 ASA 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 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))

<b>Appendix 2</b> sets out further considerations relating to understanding inherent risk factors.
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- 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

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<sup>14</sup> See ASA 580 *Written Representations*.

- 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 ASA. However, the significance of fraud is such that further requirements and guidance are included in ASA 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 ASAs provide further requirements and guidance on identifying and assessing risks of material misstatement regarding specific matters or circumstances:
- ASA 540<sup>16</sup> in regard to accounting estimates;
  - ASA 550\* in regard to related party relationships and transactions;
  - ASA 570<sup>17</sup> in regard to going concern; and
  - ASA 600<sup>18</sup> in regard to group financial report.
- 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.

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<sup>15</sup> See ASA 240, paragraphs 12–27.

<sup>16</sup> See ASA 540 *Auditing Accounting Estimates and Related Disclosures*.

\* See ASA 550 *Related Parties*.

<sup>17</sup> See ASA 570 *Going Concern*.

<sup>18</sup> See ASA 600 *Special Considerations—Audits of a Group Financial Report*.

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
- 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 ASA 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 ASA.

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

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

<sup>20</sup> See ASA 500 *Audit Evidence*, paragraph 7.

**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 enquiry.

Other entities, typically more complex entities, are expected to have more formalised 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. ASA 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 ASA 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.

*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.

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<sup>21</sup> See ASA 500, paragraphs A14–A17 and A21–A25.

<sup>22</sup> See ASA 500, paragraph A12.



- 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 report by management. ASA 260<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.

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.

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<sup>23</sup> See ASA 260 *Communication with Those Charged with Governance*, paragraph 4(b).

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 ASA deals with the auditor's use of analytical procedures as risk assessment procedures. ASA 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 ASA 520. However, the requirements and application material in ASA 520 may provide useful guidance to the auditor when performing analytical procedures as part of the risk assessment procedures.

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<sup>24</sup> See ASA 520 *Analytical 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 visualization 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.

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 reports) 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 ASA 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.

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<sup>25</sup> See ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Financial Information*, paragraph 12.

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.

*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 report 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 report 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 report 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 report 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.

ASA 240 requires the engagement team discussion to place particular emphasis on how and where the entity's financial report 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.

#### 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 a group financial report, 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.

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<sup>26</sup> See ASA 240, paragraph 16.

**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 report, 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 report in accordance with ASA 315 or other relevant standards (e.g., relating to risks of fraud in accordance with ASA 240 or when identifying or assessing risks related to accounting estimates in accordance with ASA 540);
  - Performing procedures to help identify instances of non-compliance with laws and regulations that may have a material effect on the financial report in accordance with ASA 250;<sup>27</sup>
  - Evaluating whether the financial report provide adequate disclosures in accordance with ASA 700;<sup>28</sup>
  - Determining materiality or performance materiality in accordance with ASA 320;<sup>29</sup> or
  - Considering the appropriateness of the selection and application of accounting policies, and the adequacy of financial report disclosures.

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<sup>27</sup> See ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*, paragraph 14.

<sup>28</sup> See ASA 700 *Forming an Opinion and Reporting on a Financial Report*, paragraph 13(c).

<sup>29</sup> See ASA 320 *Materiality in Planning and Performing an Audit*, paragraphs 10–11.

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 ASA 520;<sup>30</sup>
- Designing and performing further audit procedures to obtain sufficient appropriate audit evidence in accordance with ASA 330; and
- Evaluating the sufficiency and appropriateness of audit evidence obtained (e.g., relating to assumptions or management'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 report. 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 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

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<sup>30</sup> See ASA 520, paragraph 5.



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 report 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 report.<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.

**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

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

<sup>32</sup> ASA 260, 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.

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 report 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 report.

**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 report 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 report.

**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 report, 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 report 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 programs.
- Program 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>

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<sup>33</sup> See ASA 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, labour 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), and tariffs or trade restriction policies.
  - Environmental requirements affecting the industry and the entity's business.
- A71. ASA 250 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 report) (see ASA 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 report 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

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<sup>34</sup> See ASA 250, paragraph 13.

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:

- 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 program).

*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 report (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 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 ASA 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 ASAs (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 ASA 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 ASAs.

- 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 ASA 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 ASA 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 report 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 report. 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 report 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 report level affect the auditor's design of overall responses, including, as explained in ASA 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.
- 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.

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<sup>35</sup> See ASA 330, paragraphs A1–A3.

**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 emphasises 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 report 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 report, 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 report 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 report 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.

**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.

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<sup>36</sup> See ASA 240, paragraph 19.

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, ASA 610<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.

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 report 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 report, and evaluating whether the component appropriately supports the preparation of the entity's financial report, supports the auditor's identification and assessment of risks of material misstatement at the assertion level. This understanding and evaluation may also

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<sup>37</sup> See ASA 610 *Using the Work of Internal Auditors*.



result in the identification of risks of material misstatement at the financial report 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 ASA 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 ASA 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 report. 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 reports 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 report.
- Information disclosed in the financial report that is produced by an entity's risk management system.
- Fair value information produced by management's experts and disclosed in the financial report.
- Information disclosed in the financial report that has been obtained from models, or from other calculations used to develop accounting estimates recognised or disclosed in the financial report, 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 report about sensitivity analyses derived from financial models that demonstrates that management has considered alternative assumptions.
- Information recognised or disclosed in the financial report that has been obtained from an entity's tax returns and records.

- Information disclosed in the financial report 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 report (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.

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 report (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 report is based on the understanding obtained in paragraphs 25(a)–(b).

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<sup>38</sup> See ASA 570, paragraphs 19–20.

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 ASA 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 report 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 ASA 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 ASA 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 report.

A159. ASA 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

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<sup>39</sup> See ASA 240, paragraph A28.

<sup>40</sup> See ASA 330, paragraph 21.

<sup>41</sup> See ASA 240, paragraphs 28 and A33.

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 reports, 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 ASA 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 ASA 330, such controls are also required to be identified because ASA 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.
- Relating to operations and compliance objectives when they relate to data the auditor evaluates or uses in applying audit procedures.

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<sup>42</sup> See ASA 330, paragraph 8(b).

<sup>43</sup> See ASA 330, paragraph 8(a).



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 report 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;

**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

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<sup>44</sup> See ASA 402 *Audit Considerations Relating to an Entity Using a Service Organisation*.

(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 report. 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 centre 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 ASA 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 ASA 330.
- A183. If the auditor has identified one or more control deficiencies, ASA 265<sup>47</sup> requires the auditor to determine whether, individually or in combination, the deficiencies constitute a significant deficiency. The auditor uses professional judgement in determining whether a deficiency represents a significant control deficiency.<sup>48</sup>

**Examples:**

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<sup>45</sup> See ASA 330, paragraphs 8–11.

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

<sup>47</sup> See ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*, paragraph 8.

<sup>48</sup> ASA 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.

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 reports.

**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 report 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 report 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 ASA 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.

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<sup>49</sup> See ASA 200, paragraph A15(a).

### 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 report 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) Cut-off—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 report have been included.
    - (iv) Accuracy, valuation and allocation—assets, liabilities and equity interests have been included in the financial report 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 report 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 report audit.

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

**Why the Auditor Identifies and Assesses Risks of Material Misstatement at the Financial Report Level**

- A193. The auditor identifies risks of material misstatement at the financial report level to determine whether the risks have a pervasive effect on the financial report, and would therefore require an overall response in accordance with ASA 330.<sup>50</sup>
- A194. In addition, risks of material misstatement at the financial report 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 Report Level**

- A195. Risks of material misstatement at the financial report level refer to risks that relate pervasively to the financial report 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 report supports the auditor's assessment of the risks of material misstatement at the financial report 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 report level. In this

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<sup>50</sup> See ASA 330, paragraph 5.



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 report 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 report 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 report level.

**Example:**

The auditor understands from enquiries of management that the entity's financial report is 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 report 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 report 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 report.

A199. ASA 705<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 report level may include consideration of matters related to the political climate, public interest and program 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 report 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 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 re-imbursements 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.

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<sup>51</sup> See ASA 705 *Modifications to the Opinion in the Independent Auditor's Report*.

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 ASA 330 and other ASAs.
- 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 report 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 report level.
- A216. In circumstances in which risks of material misstatement are identified as financial report 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 of inherent risk, 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).
- ASA 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>
- ASA 330 requires the auditor to obtain more persuasive audit evidence the higher the auditor's assessment of risk.<sup>53</sup>
- ASA 260 requires communicating with those charged with governance about the significant risks identified by the auditor.<sup>54</sup>
- ASA 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>
- ASA 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 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 ASA. ASA 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>

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<sup>52</sup> See ASA 330, paragraphs 15 and 21.

<sup>53</sup> See ASA 330, paragraph 7(b).

<sup>54</sup> See ASA 260, paragraph 15.

<sup>55</sup> See ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*, paragraph 9.

<sup>56</sup> See ASA 220, paragraphs 17 and A19.

<sup>57</sup> See ASA 600, paragraphs 30 and 31.

<sup>58</sup> See ASA 240, paragraphs 26–28.

**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.

**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 ASA 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 ASA 330,<sup>59</sup> to design and perform tests of such controls.

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<sup>59</sup> See ASA 330, paragraph 8.

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. ASA 540 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 ASA 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.

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<sup>60</sup> See ASA 540, paragraphs A87–A89.

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 ASA 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, in accordance with ASA 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 report 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 ASA 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 report.<sup>64</sup> For the purpose of this ASA and paragraph 18 of ASA 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 report 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).

<b>Example:</b>
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<sup>61</sup> See ASA 330, paragraphs A29–A30.

<sup>62</sup> See ASA 500, paragraph A1.

<sup>63</sup> See ASA 320, paragraph A1.

<sup>64</sup> See ASA 320, paragraph 4.



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 ASA 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 ASA 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 ASA 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. ASA 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 ASA 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;

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<sup>65</sup> See ASA 330, paragraph 18.

<sup>66</sup> See ASA 230, paragraph A7.

- 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 report 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 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.

#### **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>67</sup> See ASA 230, paragraph 8.

<sup>68</sup> See ASA 300, *Planning an Audit of a Financial Report*, paragraphs 7, 9 and A11.

<sup>69</sup> See ASA 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 report. 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, globalization, 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 report 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:
- (e) 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, superannuation and other post-employment benefits, stock option or incentive bonus arrangements, and government regulation related to employment matters).
    - Research and development activities and expenditures.
    - Transactions with related parties.
  - (f) 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.
  - (g) 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 (for example, 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 ASA 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> See ASA 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 the 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 report.
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 report. 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 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

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<sup>71</sup> See ASA 240, paragraphs A24–A27.

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 report 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 ASA 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 report, at the financial report 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.

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Relevant Inherent Risk Factor:	Examples of Events or 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> <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>



Relevant Inherent Risk Factor:	Examples of Events or Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:
	<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>
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> </ul>

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Relevant Inherent Risk Factor:	Examples of Events or Conditions That May Indicate the Existence of Risks of Material Misstatement at the Assertion Level:
	<ul style="list-style-type: none"><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 report 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 report 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 report.

### **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 report is prepared in accordance with the applicable financial reporting framework, including whether the financial report 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 resources 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 report 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 report.
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 report. 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 report.
- *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 support 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

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<sup>72</sup> ASA 610 and Appendix 4 of this ASA provides further guidance related to internal audit.

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 report 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 report 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 report.
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 report 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 the person 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.

## **Appendix 4**

(Ref: Para. 14(a), 24(a)(ii), A25–A28, A118)

### **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 report 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 report, 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 ASA 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.

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<sup>73</sup> The relevant requirements are contained in ASA 610.

<sup>74</sup> See ASA 240, paragraph 19.

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 report, 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, ASA 610 applies.
10. As is further discussed in ASA 610, 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. ASA 200 discusses the importance of the auditor planning and performing the audit with professional scepticism,<sup>75</sup> 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.

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<sup>75</sup> See ASA 200, paragraph 7.

## **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 report 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

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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:			
• The extent of automated procedures for processing, and the complexity of those procedures, including, whether there is highly automated, paperless processing.	N/A	N/A	Extensive and often complex automated procedures
• The extent of the entity's reliance on system-generated reports in the processing of information.	Simple automated report logic	Simple relevant automated report logic	Complex automated report logic; Report-writer software
• How data is input (i.e., manual input, customer or vendor input, or file load).	Manual data inputs	Small number of data inputs or simple interfaces	Large number of data inputs or complex interfaces
• How IT facilitates communication between applications, databases or other aspects of the IT environment, internally and externally, as appropriate, through system interfaces.	No automated interfaces (manual inputs only)	Small number of data inputs or simple interfaces	Large number of data inputs or complex interfaces
• The volume and complexity of data in digital form being processed by the	Low volume of data or simple data that is able to be verified	Low volume of data or simple data	Large volume of data or complex data; Data

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	Examples of typical characteristics of:		
information system, including whether accounting records or other information are stored in digital form and the location of stored data.	manually; Data available locally		warehouses; <sup>76</sup> 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 customization, 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 customization	Purchased application or simple legacy or low-end ERP applications with little or no customization	Custom developed applications or more complex ERPs with significant customization
<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, 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</li> </ul>	Few personnel with limited IT knowledge to process vendor	Limited personnel with IT skills / dedicated to IT	Dedicated IT departments with skilled personnel,

<sup>76</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.

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	Examples of typical characteristics of:		
number and skill level of the IT support resources that manage security and changes to the IT environment).	upgrades and manage access		including programming skills
• The complexity of processes to manage access rights.	Single individual with administrative access manages access rights	Few individuals with administrative access manage access rights	Complex processes managed by IT department for access rights
• 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.	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
• Whether program changes have been made to the manner in which information is processed, and the extent of such changes during the period.	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
• 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).	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 customization
• 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.	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*

5. 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 report, 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 report 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 report. 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 utilize 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>• Stand-alone 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> </ul> </li> </ul>

	<ul style="list-style-type: none"> <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, it does not rely on these reports. Instead, it reconciles the reports back to the hard copy documentation and verifies 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 report. 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 report 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 report may include data protection legislation. Considering an entity's compliance with such laws or regulations, in accordance with ASA 250,<sup>77</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>77</sup> See ASA 250.

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 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 the user's 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 centre 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*

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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



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		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	Access is authenticated through unique user IDs and passwords or other methods as a mechanism for validating that users are	Yes – password authentication only	Yes – mix of password and multi-factor authentication	Yes

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	authorised and appropriate users.	authorised to gain access to the system. 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: Inappropriate changes are made to application systems or programs that contain relevant automated controls (i.e., configurable settings, automated algorithms, automated calculations, and automated data 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 development environment	N/A	Yes for non-commercial software	Yes
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	N/A – no database changes made at entity	Yes – for non-commercial software	Yes

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		production environment			
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 the conversion is performed in accordance with established conversion policies and procedures	N/A – Addressed through manual controls	Yes	Yes
IT Operations	Network: 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	N/A – no separate network authentication method exists	Yes	Yes

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		standards (e.g., password minimum length and complexity, expiration, account lockout)			
		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	N/A – no VPN	Yes – with judgement	Yes – with judgement

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		authorised 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 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

# **Explanatory Statement**

## ***ASA 315 Identifying and Assessing the Risks of Material Misstatement and ASA 2020-2 Amendments to Australian Auditing Standards***

Issued by the Auditing and Assurance Standards Board



**Australian Government**

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**Auditing and Assurance Standards Board**

## **Obtaining a Copy of this Explanatory Statement**

This Explanatory Statement is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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## **Reasons for Issuing Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards***

The AUASB issues Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is a Non Corporate Commonwealth entity of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislation Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required, *inter alia*, to develop auditing standards that have a clear public interest focus and are of the highest quality.

The Auditing Standard conforms with ISA 315 (Revised 2019) *Identifying and Assessing the Risks of Material Misstatement* issued by the International Auditing and Assurance Standards Board.

## **Purpose of Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement***

The purpose of the Auditing Standard represents the Australian equivalent of ISA 315 (Revised 2019) *Identifying and Assessing the Risks of Material Misstatement* and will replace the current ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment* issued by the AUASB in December 2015 (as amended).

## **Main Features**

The revisions to ASA 315 are consistent with recent enhancements to ISA 315 and include a more robust and consistent risk identification and assessment process. The revised standard sets out clarified and enhanced requirements, and enhanced application material, to support the auditor's risk assessment process. The revised standard also includes enhanced guidance on considerations in relation to Information Technology risks, and considerations in relation to the auditor's use of automated tools and techniques. ASA 2020-2 includes the conforming and consequential amendments to other Auditing Standards as a result of ASA 315.

## **Operative Date**

ASA 315 is operative for financial reporting periods commencing on or after 15 December 2021.

## **Process of making Australian Auditing Standards**

The AUASB's Strategic Direction, *inter alia*, provides that the AUASB develop Australian Auditing Standards that:

- have a clear public interest focus and are of the highest quality;
- use the International Standards on Auditing (ISAs) of the International Auditing and Assurance Standards Board (IAASB) as the underlying standards;
- conform with the Australian regulatory environment; and
- are capable of enforcement.



### **Consultation Process prior to issuing the Auditing Standard**

The AUASB has consulted publicly as part of its due process in developing the Auditing Standard. Exposure Draft ED 01/18 Proposed Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* was issued in August 2018 with a 70 day comment period.

Submissions were received by the AUASB and these were considered as part of the development and finalisation of this Auditing Standard.

### **Regulatory Impact Statement**

A Regulatory Impact Statement (RIA) has been prepared in connection with the preparation of ASA 315 *Identifying and Assessing the Risks of Material Misstatement*. The RIA has been cleared by the Office of Best Practice Regulation (OBPR).

## **STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS**

*Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011*

**Legislative Instrument:**        ***Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement****

***Auditing Standard ASA 2020-2 *Amendments to Australian Auditing Standards****

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

### **Overview of the Legislative Instrument**

#### *Background*

The AUASB is an independent statutory committee of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

#### *Purpose of Auditing Standard ASA 315*

The purpose of ASA 315 represents the Australian equivalent of ISA 315 *Identifying and Assessing the Risks of Material Misstatement* recently issued by the International Auditing and Assurance Standard Board.

The purpose of ASA 2020-2 is to make consequential and conforming amendments to Australian Auditing Standards as a result of the issuance of ASA 315.

#### *Main Features*

The revisions to ASA 315 are consistent with recent enhancements to ISA 315 and include a more robust and consistent risk identification and assessment process. The revised standard sets out clarified and enhanced requirements, and enhanced application material, to support the auditor's risk assessment process. The revised standard also includes enhanced guidance on considerations in relation to information technology risks, and considerations in relation to the auditor's use of automated tools and techniques.

### **Human Rights Implications**

The Auditing Standards are issued by the AUASB in furtherance of the objective of facilitating the Australian economy. The standards do not diminish or limit any of the applicable human rights or freedoms, and thus do not raise any human rights issues.

#### *Conclusion*

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.

February 2020

# **Basis for Conclusions**

## ***ASA 315 Identifying and Assessing the Risks of Material Misstatement and ASA 2020-2 Amendments to Australian Auditing Standards***

Prepared by the Auditing and Assurance Standards Board



**Australian Government**

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**Auditing and Assurance Standards Board**

## **Obtaining a Copy of this Basis for Conclusions**

This Basis for Conclusions is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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ISSN 2201-3628

Basis for Conclusions ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards* has been developed by the Auditing and Assurance Standards Board (AUASB) to provide a background to, and rationale for the development and approval of the Standard by the AUASB. The Basis for Conclusions relates to, but does not form part of, ASA 315 and ASA 2020-2.

No responsibility is taken for the results of actions or omissions to act on the basis of any information contained in this document or for any errors or omissions in it.

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## **BASIS FOR CONCLUSIONS**

### **ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards***

This Basis for Conclusions is issued by the Auditing and Assurance Standards Board (AUASB). It provides a background to, and rationale for the development and approval of the Standard by the AUASB. The Basis of Conclusions relates to, but does not form part of, ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards*, and is not a substitute for reading the Standard.

#### **Background**

1. The International Auditing and Assurance Standards Board (IAASB) issued ISA 315 (Revised 2019) *Identifying and Assessing the Risks of Material Misstatement* and conforming and consequential amendments in December 2019. This project was initiated to respond to key findings from the IAASB's ISA Implementation Project which found inconsistent risk assessment processes in practice and a concern that information technology risks were not sufficiently addressed in the existing ISA 315.
2. Further details regarding the development of the International Standard on Auditing (ISA) including the Basis of Conclusions prepared by the Staff of the IAASB, can be found on the IAASB's website: [ISA 315 Basis for Conclusions](#).
3. In accordance with its mandates under section 227 of the *Australian Securities and Investments Commission Act 2001* and the Financial Reporting Council's *Strategic Direction*, the AUASB's policy is to adopt the IAASB's ISAs, unless there is a compelling reason not to do so, and to amend the ISAs only when there is a compelling reason to do so.
4. In line with this direction, the AUASB issued Exposure Drafts ED 01/18 *Identifying and Assessing the Risks of Material Misstatement* and ED 02/18 *Proposed Auditing Standard ASA 2020-2 Amendments to Australian Auditing Standards* in August 2018 with comments due 15 October 2018. The exposure drafts were based on the IAASB's equivalent exposure drafts and no Australian specific amendments were proposed in either Exposure Draft.
5. The AUASB issued a revised Australian Auditing Standard, ASA 315 *Identifying and Assessing the Risks of Material Misstatement* in February 2020. As a consequence of the making of ASA 315, the AUASB issued ASA 2020-2 *Amendments to Australian Auditing Standards* which contained amendments to:
  - (a) ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*;
  - (b) ASA 210 *Agreeing the Terms of Audit Engagements*
  - (c) ASA 230 *Audit Documentation*
  - (d) ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*
  - (e) ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*
  - (f) ASA 260 *Communication with Those Charged with Governance*
  - (g) ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance*
  - (h) ASA 330 *The Auditor's Responses to Assessed Risks*

- (i) ASA 402 *Audit Considerations to an Entity Using a Service Organisation*
- (j) ASA 500 *Audit Evidence*
- (k) ASA 501 *Audit Evidence – Special Considerations for Inventory and Segment Information*
- (l) ASA 530 *Audit Sampling*
- (m) ASA 540 *Auditing Accounting Estimates and Related Disclosures*
- (n) ASA 550 *Related Parties*
- (o) ASA 600 *Special Considerations – Audits of a Group Financial Report*
- (p) ASA 610 *Using the Work of Internal Auditors*
- (q) ASA 620 *Using the Work of an Auditor’s Expert*
- (r) ISA 701 *Communicating Key Audit Matters in the Independent Auditor’s Report*
- (s) ISA 720 *The Auditor’s Responsibilities Relating to Other Information*

## **Scope**

6. This Basis for Conclusions applies to ASA 315 primarily, but is also relevant for ASA 2020-2.

## **Major Issues raised by Respondents on Exposure**

7. The adoption of international standards and any changes to adopted standards are governed by the AUASB’s policies regarding convergence with IAASB standards and harmonisation with the standards of the NZAuASB. The policies and procedures incorporate “compelling reasons” tests which must be used to support changes to the international standards. Changes are made only when the AUASB is satisfied that there are persuasive reasons to do so.
8. Respondents raised a number of issues on exposure which were included in the AUASB’s submission to the IAASB on their exposure drafts. The AUASB have concluded that all major issues raised by respondents have been addressed by the IAASB. Further detail on how the IAASB have addressed comments on their exposure draft is included in the [IAASB’s Basis for Conclusion](#).

## **Conclusion**

9. In reaching its conclusions, the AUASB considered all stakeholder feedback.
10. The AUASB voted to approve and issue ASA 315 on 4 February 2020.

\* \* \*



## ***ISA 315 (Revised 2019) Implementation Plan***

**At December 2019**

	<i>Timing</i>	<i>Format</i>
<b>First Time Implementation Guide</b> Highlighting significant changes in the revised standard from extant ISA 315 (Revised)	First Quarter 2020	Published document
<b>Fact Sheets</b> <ul style="list-style-type: none"><li>• Overall summary of the revised standard</li><li>• Understanding the Entity and Its Environment</li><li>• Understanding the Entity's System of Internal Control</li><li>• Control Activities</li><li>• Information Technology</li><li>• Identifying and Assessing the Risks of Material Misstatement</li><li>• Documentation</li><li>• "Why" Procedures Within ISA 315 (Revised 2019) are Required</li></ul>	First quarter 2020	Published documents – to include flowcharts where relevant
<b>Staff Publication – Questions and Answers</b>	First quarter 2020	Published documents relating to matters not addressed in the First Time Implementation Guide or the Fact Sheets
<b>Webinar- Explaining the Significant Changes in ISA 315 (Revised 2019)</b>	First quarter 2020	Webinar

	<i>Timing</i>	<i>Format</i>
<b>Focused Education Sessions</b>	March – June 2020	<p>1 – 1.5 days presentation (by members of the ISA 315 Task Force and IAASB Staff), and audience discussion relating to the changes that have been made to the revised standard. These sessions will be targeted at representatives from national standard setters, regulators and audit oversight bodies, software providers involved in making changes to audit software/methodologies and member bodies (as appropriate) in the following locations:<sup>1</sup></p> <ul style="list-style-type: none"> <li>• Europe</li> <li>• Asia Pacific</li> <li>• Africa</li> <li>• South America</li> <li>• North America</li> </ul>

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<sup>1</sup> Further information as to the exact location and the dates for each session will be confirmed in early 2020.



# AUASB Board Meeting Summary Paper

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**AGENDA ITEM NO. 6.0.1**

**Meeting Date:** 4 February 2020  
**Subject:** Less Complex Entities – Implications for Australian Standard-Setting  
**Prepared By:** Tim Austin  
**Date Prepared:** 16 January 2020

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☒ **Action Required**

☐ **For Information Purposes Only**

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## Agenda Item Objectives

1. For AUASB Members to provide feedback to the AUASB Technical Group (ATG) on the proposed actions to support auditors of Less Complex Entities (LCE) in Australia whilst the IAASB undertakes further research activities.

## Background

2. At the September 2019 AUASB Meeting, the AUASB discussed and approved its submission to the IAASB's Discussion Paper of Audits on Less Complex Entities. As part of the September Agenda Item, the ATG prepared a paper to discuss with the AUASB how to best utilise the Australian feedback ([AUASB LCE Survey](#)) to support auditors of LCEs whilst the IAASB formulated their response. The AUASB decided to defer the discussion to the first AUASB meeting in 2020 so that any response considered the IAASB's proposed approach which was being discussed at the IAASB December 2019 Meeting.
3. At the IAASB December 2019 meeting, an overview of the global feedback received to date was provided to the IAASB by the LCE Working Group along with an indicative way forward which involved:
  - (a) A broader focussed ISA workstream which would explore improving the ISAs as a whole to respond to concerns raised by stakeholders about the complexity, scalability and understandability of the standards; and
  - (b) A narrower focussed LCE workstream.
4. The IAASB considered that it was too early to discuss workstreams and that the LCE Working Group should continue to analyse feedback from stakeholders and undertake further information gathering activities. A project proposal is expected to be provided to the IAASB at the June 2020 IAASB Meeting.

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

## **Overview of feedback**

5. As outlined above in paragraph 2, the AUASB was provided a summary of all [Australian feedback](#) at the September 2019 AUASB Meeting. For this discussion on the way forward, the ATG has considered responses only to the following questions:
- (a) **Question 2(a)** – What are the particular aspects of the ASAs which make them difficult to apply, including particular standards and paragraphs;
  - (b) **Question 2(b)** – What are the underlying causes of the challenges; and
  - (c) **Question 3** – Are there challenges which are not specifically audit focussed but could be addressed by the AUASB/IAASB.
6. The IAASB has also released a [Feedback Statement](#) of the global responses received. The top global responses have been included below alongside the list of top Australian challenges.

### *Challenges with the standards for auditors of LCEs (Qn2(a) and (b))*

7. The main challenges identified by Australian stakeholders were:
- (a) Requirements which result in procedures being performed solely to comply with auditing standard requirements with no additional assurance or measurable increase in audit quality (90% of respondents);
  - (b) There is a lack of clarity and different interpretations as to what, and how, certain matters are documented (84% of respondents);
  - (c) There is insufficient application or inadequate application material in the auditing standards addressing scalability and proportionality considerations (84% of respondents);
  - (d) Documentation requirements are extensive and onerous (83% of respondents);
  - (e) The auditing standards are long and voluminous (81% of respondents); and
  - (f) There is a lack of separate implementation support/guidance in respect of the application of the auditing to the audit of LCEs (83% of respondents).

The top underlying challenges for stakeholders globally were consistent with those raised in Australia.

8. The standards which created the most challenges for Australian stakeholders were:
- (a) *ASA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment;*
  - (b) *ASA 540 Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures;*
  - (c) Other ASAs in the 500 series.
9. The standards which created the most challenges for stakeholders globally, in addition to those already raised by Australian stakeholders were:
- (a) *ISA 230 Audit Documentation; and*
  - (b) *ISA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements.*

*Challenges raised not specific to the auditing standards (Qn3):*

10. The challenges raised by Australian stakeholders were:
  - (a) Expectation gap between auditors and users;
  - (b) Value of the audit; and
  - (c) Complexity of the accounting standards.
11. The challenges raised by global stakeholders in addition to those of Australian stakeholders were:
  - (a) Pressure from regulators driving a “checklist approach” and overshadowing professional judgement;
  - (b) Fee pressures;
  - (c) Issues related to attracting and retaining talent in the auditing profession; and
  - (d) Lack of resources to invest in education and training.

**Possible responses to the challenges raised**

12. A key insight from the feedback received from auditors of LCEs was that largely the challenges raised were consistent with challenges raised by other stakeholders. Importantly, the same standards (ASA/ISA 315 and ASA/ISA 540) have been raised as challenging by different stakeholder groups.
13. Therefore, the ATG is of the view that a specific LCE focussed approach is not required in Australia to assist auditors of LCEs, instead the ATG is planning to formalise a broader support strategy for all stakeholders with specific areas of that support tailored to respond to the particular issues for each stakeholder group.

*Planned actions for challenges which are standards related (Qn2(a) and (b)):*

14. The first action that the ATG considers important is the formalisation of the form and content of AUASB implementation packs for all future standards. The ATG’s proposed approach to implementation packs will be to supplement any planned implementation assistance from the IAASB. The ATG considers that the implementation packs should include:
  - (a) Summary of what has changed to assist stakeholders in updating methodology and delivering training. The format of this may change for each standard but could be a side by side comparison of the revised to the extant standard;
  - (b) Worked-examples of the standard at both ends of “scalability”;
  - (c) Flowcharts and other visual representations of concepts in the standards;
  - (d) Webinars and podcasts; and
  - (e) FAQs and other short publications aimed to deliver key points.
15. Any activities to supplement the IAASB implementation guidance will be coordinated at a National Standard-Setters level. The expectation is that the IAASB will provide some implementation assistance for all future standards. For example, **Agenda Item 5** outlines the IAASB’s planned implementation support for the recently issued ISA 315 *Identifying and Assessing the Risks of Material Misstatement*.

### Questions

1. Does the AUASB have any other items that should be included as part of future planned AUASB implementation packs?
2. Are there any items listed above which the AUASB does not consider appropriate to include in an implementation pack?

16. Another key action the ATG is undertaking is the digitisation of the AUASB's standards to improve navigation and ease of use for stakeholders. Whilst the initial aim of the project is to improve accessibility of the standards, the long-term plan is to improve the way that all guidance and implementation support is delivered, for example, interactive flow charts of standards.

### Questions

3. Does the AUASB have any other suggested actions to address the challenges outlined in paragraphs 7-9?

### *Challenges raised not specific to the auditing standards*

17. The ATG's proposed response to challenges that are not specifically audit standards focussed are:
  - (a) To finalise and issue the planned AUASB publications aimed at addressing the audit expectation gap and value of the assurance (in-progress). This was last presented to the AUASB at the December 2019 Meeting as **Agenda Item 9**.
  - (b) To work with the AASB to better understand how accounting standards interact with the requirements of the auditing standards to be able to support stakeholders.

### Questions

4. Does the AUASB have any other suggested actions to address the challenges outlined in paragraphs 10 and 11?

### **Material Presented**

Agenda Item 6.0.1

AUASB Board Meeting Summary Paper

### **Action Required**

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	Provided feedback	Provided feedback	AUASB	4 February 2020	



# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO. **7.0**

Meeting Date: 4 February 2020

Subject: GS 008 *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001*

Date Prepared: 20 January 2020

Prepared By: See Wen Ewe

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☒ Action Required

☐ For Information Purposes Only

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## Agenda Item Objectives

1. For the AUASB to review and approve the revision of GS 008 *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001*, as included at **Agenda Item 7.1**.

## Background

2. An update on GS 008 was presented to the AUASB as part of the December 2019 AUASB meeting papers. There were two key issues that the ATG seek AUASB input:
  - (a) Inconsistency in practice in terms of applying materiality in the audit of the remuneration report. We understand that some practitioners:
    - (i) are of the view that the remuneration report is by its nature material; and accordingly there is no determination of quantitative and qualitative materiality, with everything in the remuneration report considered to be material other than 'clearly trivial';
    - (ii) while others apply quantitative and qualitative materiality to the audit of the remuneration report.
  - (b) The extant Report on the Remuneration Report may be too simplistic in meeting the requirements of ASAE 3100 and an expansion of the opinion or scope should be considered.
3. At the December 2019 meeting, the AUASB determined that the wording related to materiality in GS 008 needed to be revised and better linked to ASA 320 *Materiality in Planning and Performing an Audit* and ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical*

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*Financial Information.* The AUASB Technical Group were also directed to undertake further outreach about the options for the wording of Auditor's Report on the Remuneration Report.

## **Matters to Consider**

### ***Issue 1: Materiality***

4. At the December 2019 meeting, the AUASB was presented with two possible actions to address this issue:
  - (a) Include additional guidance around materiality within GS 008; or
  - (b) Status quo, no amendment to GS 008 in relation to materiality.
5. The AUASB decided that additional guidance around materiality should be included within GS 008 and the wording needed to be revised and better linked to ASA 320 *Materiality in Planning and Performing an Audit* and ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*.
6. The ATG seeks the AUASB's feedback on the revised wording below to address this matter:

*In conducting an audit of a remuneration report, the overall objectives of the auditor are to obtain reasonable assurance about whether the remuneration report as a whole is free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the remuneration report is prepared, in all material respects, in accordance with section 300A of the Corporations Act 2001. The auditor obtains reasonable assurance by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level. Materiality and audit risk are considered throughout the audit of the remuneration report, in particular, when:*

- (a) *Identifying and assessing the risks of material misstatement;*
- (b) *Determining the nature, timing and extent of further audit procedures; and*
- (c) *Evaluating the effect of uncorrected misstatements, if any, on the remuneration report and in forming the opinion in the auditor's report on the remuneration report.*

*Materiality is considered in the context of qualitative factors and, when applicable, quantitative factors. The relative importance of qualitative factors and quantitative factors when considering materiality is a matter for the auditor's professional judgement, and is affected by the auditor's perception of the common information needs of intended users as a group.*

*Quantitative and qualitative factors which the auditor may consider when assessing materiality include:*

- *The magnitude of the misstatements in the remuneration report;*
- *Omissions of disclosures of required by section 300A of the Corporations Act 2001;*
- *The nature of any non-compliance with section 300A of the Corporations Act 2001;*
- *The risk of fraud relating to the misstatements and/or non-compliance in the remuneration report;*
- *Remuneration reporting framework and controls ie. instance(s) of deficiency that are significant in the context of the entity's control environment; and/or*



- *Commonly accepted practices within the relevant industry.*

**Action for the AUASB**

Do you agree with the proposed wording in paragraph 6 to be included in GS 008?

***Issue 2: Wording of Auditor's Report on the Remuneration Report***

7. At the December 2019 meeting, the AUASB was presented with two possible actions to address this issue:
  - (a) Carry out further investigation and seek consultation on a change to reporting; or
  - (b) Status quo, no change to reporting.
8. The AUASB decided that the wording needs to be expanded but a long-form report will not be necessary. It was also decided that a Project Advisory Group will not be necessary.
9. The ATG consulted with some AUASB members on the wording and it has been brought to the attention of the ATG that there is ambiguity on whether the underlying work performed on the remuneration report is purely compliance in nature or a combination of audit and compliance (multi-scope engagements). We understand that some practitioners:
  - are of the view that the work performed on the remuneration report is compliance in nature and should be carried out in accordance to ASAE 3100 *Compliance Engagements*,
  - while others are of the view that the work performed on the remuneration report is a combination of an audit of a specific element (in this case, the remuneration report) and compliance in nature, which constitutes a multi-scope engagement comprising ASA 805 *Special Considerations-Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement* and ASAE 3100.
10. Based on this the ATG propose two wording options to the AUASB (refer to **Appendix 1**):
  - Option A – If the AUASB decide that the Report on the Remuneration Report should be drafted in accordance with ASAE 3100, or
  - Option B – If the AUASB decide that the Report on the Remuneration Report should be drafted in accordance with ASA 805 and ASAE 3100.
11. In the ATG's view the audit of the Remuneration Report is a multi-scope engagement and therefore recommend Option B.

**Action for the AUASB**

Refer to Appendix 1 and Review Option A and Option B and provide feedback on what is the appropriate wording. Do you agree with the ATG's recommendation in paragraph 11?

### ***Other Matters***

12. At the December 2019 meeting, the AUASB agreed that the unmodified audit report and the remuneration report in Appendix 1 Unmodified Opinion of the extant should be excluded and referenced to ASA 700 in paragraph 10 of the revised GS 008 to reduce duplication of content.
13. However, with the change in the wording of the Report on the Remuneration Report, ATG is of the view that the unmodified audit report and the remuneration report in Appendix 1 can no longer be excluded. Please refer to **Agenda Item 7.1** for the revised GS 008 for more details.

#### **Action for the AUASB**

Do you agree to retain an example of an unmodified audit report in GS 008?

### ***Approval of GS 008***

#### **Action for the AUASB**

Review draft GS 008 in Agenda item 7.1 which has been drafted using the proposed wording in paragraph 6 and option B.

Subject to the AUASB's feedback on these matters:

- are there any other changes to draft GS 008?
- does the AUASB approve GS 008 for issue?

### **Material Presented**

Agenda Item 7.0

AUASB Board Meeting Summary Paper

Agenda Item 7.1

Revision of GS 008 *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporation Act 2001* (mark-up version with Option B of **Appendix 1**)

## Option A

### Report on the Remuneration Report

#### *Opinion on the Remuneration Report*

We have undertaken a reasonable assurance engagement on ABC's compliance, in all material respects, of ~~audited~~ the Remuneration Report included in [paragraphs a to b or pages x to y] of the directors' report for the year ended 30 June 20X1 with the requirements of section 300A of the Corporations Act 2001.

In our opinion, the Remuneration Report of ABC Company Ltd., for the year [period] ended 30 June 20X1, has complied in all material respects ~~complies~~ with section 300A of the *Corporations Act 2001*.

#### *Basis for Opinion*

We conducted our engagement in accordance with Assurance Engagements ASAE 3100 Compliance Engagements issued by the Auditing Assurance Standards Board.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### *ABC's Responsibilities*

The directors of the Company are responsible for the preparation, including the identification, design and implementation of controls, and presentation of the Remuneration Report to meet the requirements of ~~in accordance with~~ section 300A of the *Corporations Act 2001*.

#### *Auditor's Responsibilities*

Our responsibility is to express an opinion on the compliance of the Remuneration Report of ABC Company Ltd., in all material respects, with section 300A of the Corporations Act 2001 based on our audit conducted in accordance with Standard on Assurance Engagements ASAE 3100 Compliance Engagements. Our procedures involved obtaining evidence about the preparation and presentation of the Remuneration Report, including the implementation of controls, to meet the requirements of section 300A of the Corporations Act 2001. Procedures were selected based on our judgement, including the identification and assessment of risks of material non-compliance.

[Auditor's name and signature]\*

[Name of Firm]

[Date of the auditor's report]#

[Auditor's address]

\* The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

# The date of the auditor's report is the date the auditor signs the report.

## Option B

### Report on the Remuneration Report

#### *Opinion on the Remuneration Report*

We have audited the Remuneration Report of ABC Limited (ABC) included in [paragraphs a to b or pages x to y] of the directors' report for the year ended 30 June 20X1 as required by section 308 (3C) of the *Corporations Act 2001* and undertaken a reasonable assurance engagement on ABC's compliance, with the requirements of section 300A of the *Corporations Act 2001*.

In our opinion, the Remuneration Report of ABC Company Ltd., for the year [period] ended 30 June 20X1:

- (a) presents fairly, in all material respects, in accordance with the requirements of section 300A of the *Corporations Act 2001*
- (b) has complied in all material respects ~~complies~~ with section 300A of the *Corporations Act 2001*.

#### *Basis for Opinion*

We conducted our audit in accordance with Australian Auditing Standards and Assurance Engagements ASAE 3100 *Compliance Engagements* issued by the Auditing Assurance Standards Board.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### *ABC's Responsibilities*

The directors of the Company are responsible for the preparation and fair presentation of the Remuneration Report including the identification, design and implementation of controls, to meet the requirements of ~~in accordance with~~ section 300A of the *Corporations Act 2001*.

#### *Auditor's Responsibilities*

Our responsibility is to obtain reasonable assurance and express an opinion whether the Remuneration Report of ABC Company Ltd as a whole is free from material misstatements, due to fraud or error, and complies with section 300A of the *Corporations Act 2001*.

Our procedures involved obtaining evidence about the preparation and presentation of the Remuneration Report, including the implementation of controls, to meet the requirements of section 300A of the *Corporations Act 2001*. Procedures were selected based on our judgement, including the identification and assessment of risks of material non-compliance.

[Auditor's name and signature]\*

[Name of Firm]

[Date of the auditor's report]#

[Auditor's address]

---

\* The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.  
# The date of the auditor's report is the date the auditor signs the report.

# **Guidance Statement GS 008**

## ***The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001***

Issued by the **Auditing and Assurance Standards Board**

Draft

### **DISCLAIMER**

This document contains draft proposals to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions and/or proposals to be contained in a published Exposure Draft or Auditing Standard. No responsibility is taken by the AUASB for the results of reliance, actions or omissions to act on the basis of any information contained in this document (including appendices), or for any errors or omissions in it.



**Australian Government**

**Auditing and Assurance Standards Board**

## Obtaining a Copy of this Guidance Statement

This Guidance Statement is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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ISSN 1833-7600

*Important Note*

Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

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## **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 008 *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

This Guidance Statement provides guidance to assist the auditor to fulfil the objectives of the audit or assurance engagement. It includes explanatory material on specific matters for the purposes of understanding and complying with AUASB Standards. The auditor exercises professional judgement when using this Guidance Statement.

This Guidance Statement does not prescribe or create new requirements.

Dated: <TypeHere>

R Simnett AO  
Chair - AUASB

## GUIDANCE STATEMENT GS 008

### *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001*

#### Application

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors reporting pursuant to section 308(3C) of the *Corporations Act 2001* ("the Act") regarding the Remuneration Report required to be included in the annual directors' report pursuant to section 300A of the Act ("the Remuneration Report").

#### Issuance Date

2. This Guidance Statement is issued on 1 October 2019 by the AUASB and replaces GS 008 *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001* issued in March 2010.

#### Introduction

3. Section 300A of the Act specifies information to be provided by listed companies<sup>1</sup> in the annual directors' report. This information includes a Remuneration Report. The auditor's objective is to express an opinion on whether the Remuneration Report complies with section 300A of the Act.

#### Auditor's Reporting Requirements

##### Responsibility to Express an Opinion on the Remuneration Report

4. Section 308(3C) of the Act requires that, if the directors' report for the financial year includes a Remuneration Report, the auditor must also report to members on whether the auditor is of the opinion that the Remuneration Report complies with section 300A of the Act. If not of that opinion, the auditor's report must state why.
5. The requirement to express a distinct opinion on the Remuneration Report in the directors' report is additional to the auditor's responsibility to express an opinion on the financial report. In accordance with Auditing Standard ASA 700 *Forming an Opinion and Reporting on a Financial Report*, the auditor is required to address other reporting responsibilities in a separate section of the auditor's report that under the section with the heading of "Report on the Audit of the Financial Report" follows the opinion paragraph on the financial report, in order to clearly distinguish them from the auditor's primary responsibility to express an opinion on the financial report.<sup>2</sup>
6. Where a listed company has included a Remuneration Report in the annual directors' report pursuant to section 300A of the Act, the auditor's report identifies clearly the paragraph numbers or pages or other identifying characteristics specific to the subject matter being audited of the directors' report that have been audited pursuant to section 308(3C) of the Act. This is necessary to avoid any misunderstanding by users as to which part of the directors' report has been subjected to audit.

<sup>1</sup> Listed companies is defined in the *Corporations Act 2001*.  
<sup>2</sup> See ASA 700, paragraph ~~38~~43 to 45.

7. Furthermore, the auditor's report describes the respective responsibilities of the directors and the auditor in relation to the Remuneration Report. See Appendix 1 for an illustrative example of an unmodified report.

### **Materiality**

8. In conducting an audit of a remuneration report, the overall objectives of the auditor are to obtain reasonable assurance about whether the remuneration report as a whole is free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the remuneration report is prepared, in all material respects, in accordance with section 300A of the *Corporations Act 2001*. The auditor obtains reasonable assurance by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level. Materiality and audit risk are considered throughout the audit of the remuneration report, in particular, when:
- (a) Identifying and assessing the risks of material misstatement;
  - (b) Determining the nature, timing and extent of further audit procedures; and
  - (c) Evaluating the effect of uncorrected misstatements, if any, on the remuneration report and in forming the opinion in the auditor's report on the remuneration report.

Materiality is considered in the context of qualitative factors and, when applicable, quantitative factors. The relative importance of qualitative factors and quantitative factors when considering materiality is a matter for the auditor's professional judgement, and is affected by the auditor's perception of the common information needs of intended users as a group.

Quantitative and qualitative factors which the auditor may consider when assessing materiality include:

- The magnitude of the misstatements in the remuneration report;
- Omissions of disclosures of required by section 300A of the *Corporations Act 2001*;
- The nature of any non-compliance with section 300A of the *Corporations Act 2001*;
- The risk of fraud relating to the misstatements and/or non-compliance in the remuneration report;
- Remuneration reporting framework and controls ie. instance(s) of deficiency that are significant in the context of the entity's control environment; and/or
- Commonly accepted practices within the relevant industry. The suggested form of opinion on the Remuneration Report, included in the Appendices to this Guidance Statement, does not make reference to materiality. An auditor exercises professional judgement in considering reporting responsibilities under the Act, including considering additional regulatory reporting obligations, such as under section 311 of the Act, for significant breaches of the Act.

### **Modifications**

- 8.9. Modifications to the auditor's report in relation to the Remuneration Report are made in accordance with ASA 705 *Modifications to the Opinion in the Independent Auditor's Report*. See Appendix 2 for an illustrative example of a modified report.

## **The Auditor's Report**

~~9.~~10. The example of an unmodified auditor's report, included as [Aus] Illustration 1A in Appendix 1 of ASA 700 incorporates the audit reporting requirements of the Act and the Auditing Standards. This auditor's report format has been used in the Appendices to this Guidance Statement to illustrate example wording regarding the auditor's reporting responsibilities over the Remuneration Report, pursuant to section 308(3C) of the Act.

## **Conformity with International Pronouncements**

~~10.~~11. As this Guidance Statement relates to Australian legislative requirements under the Act, there is no equivalent International Standard on Auditing or Auditing Practice Statement to this Guidance Statement.

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## **Appendix 1**

(Ref: Para. 9)

### **ILLUSTRATIVE EXAMPLE OF AN UNMODIFIED AUDITOR'S REPORT ADDRESSING THE AUDITOR'S ADDITIONAL REPORTING RESPONSIBILITIES PURSUANT TO SECTION 308(3C) OF THE *CORPORATIONS ACT 2001***

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- Audit of the financial report of a single listed company. The audit is not a group audit (i.e. ASA 600 does not apply).
- The financial report is prepared by the directors of the company in accordance with Australian Accounting Standards (a general purpose framework) and under the *Corporations Act 2001*.
- The terms of the audit engagement reflect the description of the directors' responsibility for the financial report in ASA 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 are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants*.
- 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 company's ability to continue as a going concern in accordance with ASA 570.
- Key audit matters have been communicated in accordance with ASA 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 report, the auditor has other reporting responsibilities required under section 308(3C) of the *Corporations Act 2001*.

The auditor's reporting requirements over the Remuneration Report are additional to the auditor's reporting requirements regarding the financial report and, accordingly, are contained in a separate section of the auditor's report following the opinion paragraph on the financial report—see ASA 700, paragraphs 43-45.

## INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

### **Report on the Audit of the Financial Report**

#### **Opinion**

We have audited the financial report of ABC Company Ltd. (the Company), which comprises the statement of financial position as at 30 June 20X1, 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, and the directors' declaration.

In our opinion, the accompanying financial report of ABC Company Ltd., is in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the company's financial position as at 30 June 20X1 and of its financial performance for the year then ended; and
- (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

#### **Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report.\*

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Key Audit Matters**

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

[Description of each key audit matter in accordance with ASA 701.]

#### **Other Information [or another title if appropriate such as "Information Other than the Financial Report and Auditor's Report Thereon"]**

[Reporting in accordance with the reporting requirements in ASA 720 – see [Aus] Illustration 1A in Appendix 3 of ASA 720.]

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\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

The directors are responsible for the other information. The other information comprises the information included in the Company's annual report for the year ended 30 June 20X1, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

### **Responsibilities of the Directors for the Financial Report**

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the Company'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 the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

### **Auditor's Responsibilities for the Audit of the Financial Report**

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

[A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: <http://www.auasb.gov.au/Home.aspx>. This description forms part of our auditor's report.]

Paragraph 41(b) of ASA 700 explains that the shaded material below can be located in an Appendix to the auditor's report.

Paragraph 41(c) of ASA 700 explains that when law, regulation or national auditing standards expressly permit, reference can be made to a website of an appropriate authority that contains the description of the auditor's responsibilities, rather than including this material in the auditor's report, provided that the description on the website addresses, and is not inconsistent with, the description of the auditor's responsibilities below. When the auditor refers to a description of the auditor's responsibilities on a website, the appropriate authority is the Auditing and Assurance Standards Board and the website address is <http://www.auasb.gov.au/Home.aspx> (Ref: Para. Aus A57.1 of ASA 700)

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors 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.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the financial report of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

## **Report on the Remuneration Report**

### *Opinion on the Remuneration Report*

We have audited the Remuneration Report of ABC Limited (ABC) included in [paragraphs a to b or pages x to y] of the directors' report for the year ended 30 June 20X1 as required by section 308 (3C) of the Corporations Act 2001 and undertaken a reasonable assurance engagement on ABC's compliance, with the requirements of section 300A of the Corporations Act 2001.

In our opinion, the Remuneration Report of ABC Company Ltd., for the year [period] ended 30 June 20X1:

- (a) presents fairly, in all material respects, in accordance with the requirements of section 300A of the Corporations Act 2001
- (b) has complied in all material respects ~~complies~~ with section 300A of the Corporations Act 2001.

### *Basis for Opinion*

We conducted our audit in accordance with Australian Auditing Standards and Assurance Engagements ASAE 3100 Compliance Engagements issued by the Auditing Assurance Standards Board.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### *ABC's Responsibilities*

The directors of the Company are responsible for the preparation and fair presentation of the Remuneration Report including the identification, design and implementation of controls, to meet the requirements of ~~in accordance with~~ section 300A of the Corporations Act 2001.



*Auditor's Responsibilities*

Our responsibility is to obtain reasonable assurance and express an opinion whether the Remuneration Report of ABC Company Ltd as a whole is free from material misstatements, due to fraud or error, and complies with section 300A of the *Corporations Act 2001*.

Our procedures involved obtaining evidence about the preparation and presentation of the Remuneration Report, including the implementation of controls, to meet the requirements of section 300A of the *Corporations Act 2001*. Procedures were selected based on our judgement, including the identification and assessment of risks of material non-compliance.

[Auditor's name and signature]\*

[Name of Firm]

[Date of the auditor's report]#

[Auditor's address]

Draft

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\* The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

# The date of the auditor's report is the date the auditor signs the report.

## **Appendix 2**

(Ref: Para. 11)

### **ILLUSTRATIVE EXAMPLE OF A MODIFIED AUDITOR'S REPORT ADDRESSING THE AUDITOR'S ADDITIONAL REPORTING RESPONSIBILITIES PURSUANT TO SECTION 308(3C) OF THE *CORPORATIONS ACT 2001*—QUALIFIED OPINION**

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- Audit of the financial report of a single listed company. The audit is not a group audit (i.e. ASA 600 does not apply).
- The financial report is prepared by the directors of the company in accordance with Australian Accounting Standards (a general purpose framework) and under the *Corporations Act 2001*.
- The terms of the audit engagement reflect the description of the directors' responsibility for the financial report in ASA 210.
- The auditor has concluded an unmodified (i.e. "clean") opinion on the financial report is appropriate based on the audit evidence obtained.
- The relevant ethical requirements that apply to the audit are the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants*.
- 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 company's ability to continue as a going concern in accordance with ASA 570.
- Key audit matters have been communicated in accordance with ASA 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 report, the auditor has other reporting responsibilities required under section 308(3C) of the *Corporations Act 2001*.
- The auditor's reporting requirements regarding the Remuneration Report are additional to the auditor's reporting requirements regarding the financial report and, accordingly, are contained in a separate section of the auditor's report following the opinion paragraph on the financial report—see ASA 700, paragraphs 43-45.
- The auditor has concluded a qualified opinion on the remuneration report is necessary based on the audit evidence obtained.

Note: As the example below relates to a qualified opinion, the report on the Remuneration Report will need to be amended accordingly where an adverse or disclaimer of opinion is required.

INDEPENDENT AUDITOR'S REPORT

[Appropriate Addressee]

**Report on the Audit of the Financial Report**

**Opinion**

We have audited the financial report of ABC Company Ltd. (the Company), which comprises the statement of financial position as at 30 June 20X1, 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, and the directors' declaration.

In our opinion, the accompanying financial report of ABC Company Ltd., is in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the company's financial position as at 30 June 20X1 and of its financial performance for the year then ended; and
- (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

**Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report.\*

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Key Audit Matters**

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

[Description of each key audit matter in accordance with ASA 701.]

**Other Information [or another title if appropriate such as "Information Other than the Financial Report and Auditor's Report Thereon"]**

[Reporting in accordance with the reporting requirements in ASA 720 – see [Aus] Illustration 6A in Appendix 3 of ASA 720.]

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\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

~~The directors are responsible for the other information. The other information comprises the information included in the Company's annual report for the year ended 30 June 20X1, but does not include the financial report and our auditor's report thereon.~~

~~Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.~~

~~In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.~~

~~If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.~~

### **Responsibilities of the Directors for the Financial Report**

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the Company'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 the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

### **Auditor's Responsibilities for the Audit of the Financial Report**

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

[A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: <http://www.auasb.gov.au/Home.aspx>. This description forms part of our auditor's report.]

Paragraph 41(b) of ASA 700 explains that the shaded material below can be located in an Appendix to the auditor's report.

Paragraph 41(c) of ASA 700 explains that when law, regulation or national auditing standards expressly permit, reference can be made to a website of an appropriate authority that contains the description of the auditor's responsibilities, rather than including this material in the auditor's report, provided that the description on the website addresses, and is not inconsistent with, the description of the auditor's responsibilities below. When the auditor refers to a description of the auditor's responsibilities on a website, the appropriate authority is the Auditing and Assurance Standards Board and the website address is <http://www.auasb.gov.au/Home.aspx> (Ref: Para. Aus A57.1 of ASA 700)

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors 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.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the financial report of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

## **Report on the Remuneration Report**

### *Qualified Opinion on the Remuneration Report*

We have audited the Remuneration Report of ABC Limited (ABC) included in [paragraphs a to b or pages x to y] of the directors' report for the year ended 30 June 20X1 as required by section 308 (3C) of the *Corporations Act 2001* and undertaken a reasonable assurance engagement on ABC's compliance, with the requirements of section 300A of the *Corporations Act 2001*.

In our opinion, except for the effect(s) on the Remuneration Report of the matter(s) referred to in the following paragraph, the Remuneration Report of ABC Company Ltd., for the year [period] ended 30 June 20X1:

- (a) presents fairly, in all material respects, in accordance with the requirements of section 300A of the *Corporations Act 2001*
- (b) has complied in all material respects ~~complies~~ with section 300A of the *Corporations Act 2001*.

### *Basis for Qualified Opinion on the Remuneration Report*

[Include a clear description of all the substantive reasons for the modification].

### *ABC's Responsibilities*

The directors of the Company are responsible for the preparation and fair presentation of the Remuneration Report including the identification, design and implementation of controls, to meet the requirements of ~~in~~ accordance with section 300A of the *Corporations Act 2001*.

### *Auditor's Responsibilities*

Our responsibility is to obtain reasonable assurance and express an opinion whether the Remuneration Report of ABC Company Ltd as a whole is free from material misstatements, due to fraud or error, and complies with section 300A of the *Corporations Act 2001*.

Our procedures involved obtaining evidence about the preparation and presentation of the Remuneration Report, including the implementation of controls, to meet the requirements of section 300A of the *Corporations Act 2001*. Procedures were selected based on our judgement, including the identification and assessment of risks of material non-compliance.

[Auditor's name and signature]\*

[Name of Firm]

[Date of the auditor's report]#

[Auditor's address]

Draft

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\* The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

# The date of the auditor's report is the date the auditor signs the report.



# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO. **8.0**

Meeting Date: 4 February 2020  
Subject: AUASB Technical Work Program Update  
Date Prepared: 28 January 2020  
Prepared by: Matthew Zappulla

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☐ Action Required

☒ For Information Purposes Only

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## Agenda Item Objectives

1. To provide the AUASB with a status update of the 2019-20 AUASB Technical Work Program.

## Background

2. The AUASB Technical Group prepared the final 2019-20 AUASB Technical Work Program and it was approved by the AUASB Chair in September 2019 (after the last AUASB meeting). A public version of the 2019-20 AUASB Technical Work Program has now been posted on the AUASB Website.
3. The AUASB Technical Group has produced a status update of the 2019-20 AUASB Technical Work Program for the AUASB to review. The format of this update aligns to the reporting we are required to present to the FRC to ensure consistency and reduce duplication. This is provided to the board at the first meeting following the end of each quarter.

## Matters to Consider

4. The status update of the 2019-20 AUASB Technical Work Program for the 2nd quarter of 2019-20 is provided to board members for review at **Agenda Item 8.1**.
5. The Final 2019-20 AUASB Technical Work Program will be used as the basis for information that populates our AUASB Performance Report in the AASB-AUASB 2019-20 Annual Report.

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

**AUASB Technical Group Recommendations**

- 6. Provide feedback to the AUASB Technical Group on the status update of the Q2 2019-20 AUASB Technical Work Program presented at **Agenda Item 8.1**.
- 7. Provide suggestions to the AUASB Technical Group about additions and changes AUASB members would like included in the 2019-20 AUASB Technical Work Program document.

**Material Presented**

Agenda Item 8.0	AUASB Board Meeting Summary Paper
Agenda Item 8.1	2019-20 AUASB Technical Work Program – Q2 Status Update





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




## AUASB Technical Work Program – 2019-2020 Q2 Report for AUASB


This table records the AUASB's activities in support of its strategic objectives and key performance indicators in the 2019-20 AUASB Corporate Plan, with a status report and update of activities for the reporting period for each high-level priority area provided.





**Performance Measure One:** Issue Australian Auditing and Assurance Standards based on IAASB equivalent standards in accordance with AUASB functions and mandate from the Financial Reporting Council (FRC).

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Develop and issue Australian Auditing and Assurance Standards following the release of their IAASB equivalent, ensuring all Australian legislative and regulatory requirements are considered, including changes required by the AUASB's "compelling reason" test.	<ul style="list-style-type: none"> <li>Issue all Australian IAASB equivalent Standards and Exposure Drafts within 3 months of PIOB clearance or 1 month of AUASB approval, as appropriate</li> </ul>		<ul style="list-style-type: none"> <li><b>The IAASB approved for issue ISA 315 Identifying and Assessing the Risks of Material Misstatement at its September 2019 meeting, with PIOB approval in November 2019. AUASB to consider Australian equivalent standards in February 2020.</b></li> <li><b>Final version of International ASRS 4400 on Agreed Upon Procedures approved by IAASB in December 2019. AUASB to issue Australian equivalent ED in February 2020.</b></li> </ul>
Coordinate and develop high quality responses from the AUASB to all IAASB exposure drafts, other IAASB pronouncements and invitations to comment, incorporating relevant feedback from AUASB members and Australian stakeholders.	<ul style="list-style-type: none"> <li>Release Exposure Drafts/Discussion Papers via the AUASB Website within two weeks of approval by AUASB</li> <li>Stakeholder engagement plan developed and implemented for each IAASB pronouncement</li> <li>Responses developed with appropriate AUASB input and sent to the IAASB by the closing date</li> </ul>		<ul style="list-style-type: none"> <li>The AUASB submitted its response to the IAASB's Quality Management Exposure Drafts in July 2019.</li> <li>The AUASB developed a local survey to support the receipt of feedback on the IAASB's LCE Discussion Paper and then submitted its response to the IAASB in September 2019.</li> <li><b>AUASB Technical Group to conduct local outreach on Audit Evidence on behalf of IAASB in March 2020.</b></li> </ul>
Develop and issue implementation support materials and activities for all new IAASB/AUASB standards.	<ul style="list-style-type: none"> <li>AUASB implementation support materials and activities for all new IAASB/AUASB standards in place before effective date</li> </ul>		<ul style="list-style-type: none"> <li>AUASB Technical Staff presented a webinar for CPA Australia on revised ASA 540.</li> <li><b>Bulletin to support the implementation of ASA 540 released in December 2019.</b></li> <li><b>'AUASB Bulletin: Auditor's Responsibilities for the Financial Reporting Framework' issued in July 2019. To be updated following outcome from AASB ED's finalised in March 2020.</b></li> </ul>
Conduct post-implementation reviews of IAASB equivalent issued AUASB Standards, feeding into the IAASB's post-implementation review projects as required.	<ul style="list-style-type: none"> <li>Obtain evidence appropriately evaluating implementation of IAASB equivalent AUASB Standards in Australia</li> <li>Provide feedback to IAASB as requested</li> </ul>		<ul style="list-style-type: none"> <li>Waiting on the IAASB's Auditor Reporting post implementation review project to commence.</li> </ul>





 <b>Completed / On track</b>	 <b>In progress / Partially Completed / Delayed due to issues beyond AUASB control</b>	 <b>Yet to commence</b>	 <b>Delays / Issues encountered</b>
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

## AUASB Technical Work Program – 2019-2020 Q2 Report for AUASB

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Finalise and implement revised AUASB Due Process procedures and documentation for exposing and issuing International Exposure Drafts.	<ul style="list-style-type: none"> <li>Revised AUASB Due Process for exposing and issuing International Exposure Drafts in place for all IAASB EDs issued in 2020 and beyond</li> </ul>		<ul style="list-style-type: none"> <li>To commence in second half of 2019-20. Work to be performed in collaboration with the NZAuASB.</li> </ul>




 Completed / On track	 In progress / Partially Completed / Delayed due to issues beyond AUASB control	 Yet to commence	 Delays / Issues encountered
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

**Performance Measure Two:** Develop, update and maintain Australian specific Standards and/or Guidance Statements for topics not specifically addressed by IAASB Standards as required.

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Develop and issue Australian specific AUASB Standards and Exposure Drafts within one month of AUASB approval, in accordance with AUASB legislative drafting and registration requirements.	<ul style="list-style-type: none"> <li>Issue all Australian specific AUASB Standards and Exposure Drafts within one month of AUASB approval</li> <li>Finalise conforming amendments and compilation standards as a result of changes to AUASB standards within one month of the AUASB standard being issued</li> </ul>		<ul style="list-style-type: none"> <li><b>ASRE 2410 being updated in conjunction with the NZAuASB. The AUASB considered feedback from Australian stakeholders at its September and December meetings. ASRE 2410 to be reconsidered by the AUASB at its March 2020 meeting</b></li> <li><b>ASA 102 Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements updated for change to Ethics Code and approved in December 2020.</b></li> </ul>
Update existing AUASB pronouncements, including identifying and revising AUASB Guidance Statements which are out of date or need revision determined by AUASB member and stakeholder feedback.	<ul style="list-style-type: none"> <li>Complete project to review all AUASB Guidance Statements (GS) by December 2019</li> <li>Develop and implement Project Plans for the update all GS identified as out of date over the next 3 year (i.e. from 2019-2022)</li> <li>Release updated GS within two weeks of approval by AUASB</li> </ul>		<ul style="list-style-type: none"> <li><b>AUASB Discussion Paper on Revision of AUASB Guidance Statements (GS) and survey issued in October 2019 seeking feedback from stakeholders on which GSs should be withdrawn, revised or where no change required. Final paper to be considered at March 2020 AUASB meeting.</b></li> <li><b>Updated GS's considered by the AUASB for review and approval at its December 2019, February 2020 and March 2020 meetings:</b> <ul style="list-style-type: none"> <li><b>GS 005 Using the Work of a Management's Expert.</b></li> <li><b>GS 008 The Auditor's Report on a Remuneration Report Under 300A of the Corporations Act 2001</b></li> </ul> </li> <li><b>Update to GS 012 Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions in progress with updates to be reviewed by AUASB in March 2020.</b></li> <li><b>Project plan to update GS 009 Auditing Self-Managed Superannuation Funds in progress.</b></li> </ul>
Determine where other AUASB Framework Pronouncements require updating.	<ul style="list-style-type: none"> <li>Review and update other AUASB Framework Pronouncements, as required.</li> </ul>		<ul style="list-style-type: none"> <li>No AUASB Framework Pronouncements require updating at this time</li> </ul>
Conduct post-implementation reviews of Australian specific AUASB Standards, as required.	<ul style="list-style-type: none"> <li>Conduct post-implementation reviews of Australian specific AUASB Standards, within 2 years of their operative date.</li> </ul>		<ul style="list-style-type: none"> <li>To commence in second half of 2019-20. Work for ASAE 3100 Compliance Engagements to be performed in collaboration with the NZAuASB.</li> </ul>





 <b>Completed / On track</b>	 <b>In progress / Partially Completed / Delayed due to issues beyond AUASB control</b>	 <b>Yet to commence</b>	 <b>Delays / Issues encountered</b>
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

**Performance Measure Three:** Monitor the Assurance Environment (including the impact of regulatory inspection findings) and address any implications for Australian auditing and assurance standards and guidance.

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Review and update the 2019-2023 AUASB Strategy and 2019-20 AUASB Technical Work Program based on feedback from AUASB members and key stakeholders and informed by the final 2020-2023 IAASB Strategy.	<ul style="list-style-type: none"> <li>Update AUASB 2019-23 Strategy based on AUASB feedback</li> <li>Finalise 2019-20 Technical Work Program and align it to AUASB 2019-23 Strategy</li> <li>Produce quarterly update and reporting of progress against AUASB 2019-20 Technical Work Program for FRC and AUASB for each relevant FRC and AUASB meeting</li> </ul>		<ul style="list-style-type: none"> <li>2019-23 Strategy updated by AUASB subcommittee and approved at the December 2019 meeting.</li> <li>2019-20 Technical Work Program has been finalised and is updated quarterly by the AUASB Technical Group.</li> </ul>
Work with the FRC to develop the FRC Audit Quality Plan and implement those elements that are the responsibility of the AUASB.	<ul style="list-style-type: none"> <li>AUASB involvement in FRC Audit Quality Plan approved by FRC</li> <li>AUASB Audit Quality activities delivered as required by the updated FRC Audit Quality Plan</li> </ul>		<ul style="list-style-type: none"> <li>CFO Survey on Audit Quality issued and results being finalised.</li> </ul>
Monitor developments associated with the Joint Parliamentary Inquiry on the regulation of Auditing, working across the profession to promote audit quality and the AUASB's role.	<ul style="list-style-type: none"> <li>Develop submission for parliamentary inquiry</li> <li>Coordinate with other key stakeholders across the profession (e.g. FRC, APESB) as required</li> <li>Prepare and assist the AUASB Chair with any presentations to the parliamentary joint committee</li> <li>Work with respected academics to produce background papers on state of Australian auditing and NAS markets to aid evidence-informed decision making</li> <li>Monitor and respond to any recommendations relevant to the AUASB</li> </ul>		<ul style="list-style-type: none"> <li><b>AUASB Submission to PJC inquiry issued October 2019.</b></li> <li><b>AUASB Chair gave evidence to the inquiry on 29 November 2019.</b></li> <li><b>Questions on notice to the AUASB Chair received in December 2019 and responded to in January 2020.</b></li> </ul>



 <b>Completed / On track</b>	 <b>In progress / Partially Completed / Delayed due to issues beyond AUASB control</b>	 <b>Yet to commence</b>	 <b>Delays / Issues encountered</b>
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


## AUASB Technical Work Program – 2019-2020 Q2 Report for AUASB

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Following on from the AUASB LCE Survey work with small and medium audit practitioners to determine implications for Australian Standard Setting.	<ul style="list-style-type: none"> <li>Develop additional guidance and initiatives to support LCE auditors based on LCE survey outcomes</li> <li>Provide input to IAASB on proposed response to LCE Discussion Paper</li> </ul>		<ul style="list-style-type: none"> <li>AUASB issued its submission to the IAASB on its LCE Discussion Paper in September 2019.</li> <li>Plan for taking the LCE project forward in Australia currently in development and scheduled for presentation to AUASB in February 2019.</li> </ul>
Monitor developments in public sector auditing and assurance issues by maintaining regular engagement with Auditors-General through the AUASB Public Sector Audit Issues Project Advisory Group (PAG) and the ACAG Auditing Standards Subcommittee.	<ul style="list-style-type: none"> <li>Develop and have approved specific AUASB guidance (in a form to be determined) for public sector auditors on issues raised by the Public Sector Audit Issues PAG</li> <li>Provide ongoing input to FRC subcommittee on Public Sector Reporting and Assurance matters</li> <li>Positive engagement with Auditors-General and ACAG Auditing Standards Committee</li> </ul>		<ul style="list-style-type: none"> <li>AUASB Technical Group continuing to work on issues raised by ACAG through Public Sector Audit Issues PAG.</li> <li><b>AUASB provided update at the December 2019 meeting focusing on whether the approach taken by the PAG to issues identified by ACAG is appropriate. Guidance (likely in the form of an AUASB Guidance Statement) targeted for April 2020.</b></li> <li>AUASB Technical staff continue to provide input into FRC subcommittee papers on Public Sector Reporting and Assurance matters.</li> </ul>
Working with regulators and auditing firms, assess and respond to implementation issues and issue AUASB guidance to address key inspection findings.	<ul style="list-style-type: none"> <li>Analyse and respond to 2019 ASIC inspection Findings</li> <li>Identify and produce relevant guidance materials addressing common inspection findings in key audit areas</li> <li>Work with AASB to identify accounting and auditing issues impacting audit quality</li> </ul>		<ul style="list-style-type: none"> <li><b>GS 005 Using the Work of a Management's Expert was updated and considered by the AUASB at its December 2019 meeting. Further updates to be provided to the PAG and AUASB in February/March 2020.</b></li> <li>Plan to develop AUASB guidance in relation to auditing of Revenue to be considered based on latest ASIC Audit Inspection Report released in December 2019 in second half of 2019-20.</li> </ul>
Monitor international auditing and assurance developments (including global audit inspection developments and trends) and consider the impact for the Australian auditing and assurance environment.	<ul style="list-style-type: none"> <li>Engage with IAASB and NSS representatives to monitor international developments</li> <li>Consider issues arising from UK audit inquiries</li> <li>Review IFIAR and other global publications to determine impact on Australian standard setting environment</li> </ul>		<ul style="list-style-type: none"> <li>Regular meetings held with NSS representatives from NZ, Canada and the Netherlands which discuss regulatory and professional developments in each territory.</li> <li><b>AUASB Technical Staff continuing to monitor the UK audit inquiries, including impact of Brydon Report and changes to UK going concern standard.</b></li> <li>Through connection with the IAASB and IFAC the AUASB Technical Staff have not identified any other major international auditing and assurance developments impacting the Australian auditing and assurance environment</li> </ul>





 <b>Completed / On track</b>	 <b>In progress / Partially Completed / Delayed due to issues beyond AUASB control</b>	 <b>Yet to commence</b>	 <b>Delays / Issues encountered</b>
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## AUASB Technical Work Program – 2019-2020 Q2 Report for AUASB

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Hold regular formal meetings with the professional accounting bodies, other standard setting bodies and regulators to discuss trends in assurance environment and identify the impact on the AUASB Agenda and Technical Work Program.	<ul style="list-style-type: none"> <li>Regular meetings (at least quarterly) to be held with key regulatory contacts and representatives from the professional bodies.</li> <li>Meeting with other key stakeholders to be held as necessary</li> <li>Maintain meeting register and report to AUASB at each meeting</li> </ul>		<ul style="list-style-type: none"> <li>Regular dialogue with CPA and CA ANZ representatives as a result of collaboration on Parliamentary Inquiry into the Regulation of Auditing and other topical issues</li> <li>Formal meetings with each professional body, to update them on AUASB work program, being arranged in early 2020.</li> <li>Regular formal meetings held with ASIC and APESB representatives on common areas of interest.</li> <li>AUASB Meeting Register updated for each AUASB meeting.</li> </ul>
Support the development of research into the Australian auditing and assurance environment	<ul style="list-style-type: none"> <li>Produce and publish AUASB research papers via the AUASB Research Centre and promote them with academics</li> </ul>		<ul style="list-style-type: none"> <li>Two AUASB Academic Scholars appointed and have commenced different projects working in collaboration with the AUASB.</li> <li><b>AUASB Research Report 3 Audit Market Structure and Competition in Australia issued in October 2019, and AUASB Research Report 4, The Provision of Non-Audit Services by Audit Firms issued in December 2019, authored by AUASB scholar.</b></li> <li><b>Additional AUASB Research Reports (Audit Issues for NFP entities, Audit Opinions and Climate Change) currently under development.</b></li> </ul>

 Completed / On track	 In progress / Partially Completed / Delayed due to issues beyond AUASB control	 Yet to commence	 Delays / Issues encountered
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**Performance Measure Four:** *Build, maintain and enhance key international relationships around key focus areas with both global and national standard-setters.*

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
AUASB to be represented at all IAASB meetings.	<ul style="list-style-type: none"> <li>AUASB Chair and Technical Team member to attend all IAASB meetings</li> <li>Summary of each IAASB meeting prepared and presented to the AUASB</li> </ul>		<ul style="list-style-type: none"> <li><b>AUASB Chair and Technical staff member attended September 2019 and December 2019 IAASB meetings, as well as numerous IAASB teleconferences.</b></li> </ul>
Arrange for AUASB review of relevant IAASB projects at each AUASB meeting and share feedback on key matters with regional IAASB members and relevant IAASB Task Force members before each IAASB meeting.	<ul style="list-style-type: none"> <li>IAASB papers reviewed and papers prepared by AUASB staff for each AUASB meeting.</li> <li>Feedback on AUASB key issues prepared and sent to Australasian IAASB members and relevant Task Forces prior to each IAASB meeting</li> </ul>		<ul style="list-style-type: none"> <li><b>IAASB September 2019 and December 2019 papers were reviewed by the AUASB.</b></li> <li><b>Final versions of IAASB standards (ISA 315, AUP) subject to 'fatal flaw' reviews by the AUASB, to capture feedback prior to being approved by the IAASB at each meeting.</b></li> </ul>
With the IAASB, Canadian AASB and NZAuASB, identify and implement initiatives to drive increased sharing and collaboration across the National Standards Setting (NSS) network, including attending and presenting relevant topics at regional and global IAASB NSS meetings.	<ul style="list-style-type: none"> <li>Develop and share updated NSS vision and roadmap</li> <li>Collaboration and support from IAASB steering committee for NSS initiatives</li> <li>Increased influence of NSS on IAASB Agenda and Outcomes</li> <li>Identify and implement initiatives to collaborate on key international auditing and assurance focus areas with other key NSS.</li> </ul>		<ul style="list-style-type: none"> <li>Meetings held with new IAASB Chair to gain support for AUASB NSS involvement.</li> <li>Regular meetings held with NSS representatives from NZ, Canada and the Netherlands to identify common projects in NSS work programs and act on actions arising from last IAASB NSS meeting in 2019.</li> <li><b>Planning with IAASB and NSS representatives for IAASB NSS meeting to be held in May 2020 underway.</b></li> <li><b>Draft NSS Vision and Roadmap complete and being socialised with other NSS's.</b></li> <li><b>Planning for IAASB Chair Visit to Australia in March 2020 in progress.</b></li> </ul>
Engage with relevant global standard setters and advisory groups (e.g. IAASB EER Project Advisory Panel, IIRC, GRI and WBCSD) on emerging forms of assurance.	<ul style="list-style-type: none"> <li>Monitor and contribute to IAASB EER Project Advisory Panel meetings</li> <li>Support associated regional activities and local panel members</li> <li>Link in Australian EER initiatives where appropriate</li> <li>Valuable input into to IIRC, GRI and WBCSD calls and meetings on behalf of the AUASB</li> </ul>		<ul style="list-style-type: none"> <li><b>Monitored and contributed to IAASB EER PAP meetings held in July, September &amp; November 2019.</b></li> <li><b>EER Assurance Survey issued to participants in September 2019. Responses being analysed and will be presented to AUASB at March 2020 meeting.</b></li> <li><b>Collaborating with other NSS's (NZ, Canada, Netherlands) on EER Assurance Survey results and linkages with IAASB EER Guidance.</b></li> </ul>



Completed / On track



In progress / Partially Completed / Delayed due to issues beyond AUASB control






Yet to commence







Delays / Issues encountered






**Performance Measure Five:** Maintain harmonisation of auditing and assurance standards in Australia and New Zealand in accordance with relevant agreements and protocols.





Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
AUASB Chair to attend all NZAuASB meetings as a NZAuASB Member.	<ul style="list-style-type: none"> <li>AUASB Chair input into NZAuASB meetings</li> <li>AUASB staff to review relevant NZAuASB board papers and provide feedback to AUASB Chair and NZAuASB staff where applicable</li> <li>Updates from the NZAuASB Chair to the AUASB at each meeting</li> </ul>		<ul style="list-style-type: none"> <li><b>AUASB Chair attended NZAuASB meetings on 24 July, 4 September, 24 October and 5 December 2019.</b></li> <li>AUASB staff reviewed all relevant NZAuASB board papers and provided summary feedback to the AUASB Chair.</li> </ul>
Ensure AUASB Standards are issued in accordance with the principles of harmonisation with New Zealand Standards.	<ul style="list-style-type: none"> <li>All AUASB Standards are issued in accordance with the common set of principles in relation to the standards that each board issues</li> </ul>		<ul style="list-style-type: none"> <li>ASRE 2410 currently being developed in conjunction with the NZAuASB.</li> <li><b>Standard reconsidered by the AUASB at its December 2019 meeting and further issues currently being reviewed by joint AUASB/NZAuASB subcommittee.</b></li> </ul>
Work collaboratively with NZAuASB Technical Staff to ensure co-operation and co-ordination between the AUASB and NZAuASB's activities, including on joint AUASB/NZAuASB projects where appropriate.	<ul style="list-style-type: none"> <li>Identification and prioritisation of joint AUASB/NZAuASB projects</li> <li>AUASB and NZAuASB staff to ensure collaboration on the 'high' rated joint projects</li> <li>For other potential joint projects, the AUASB and NZAuASB Technical Director to build joint activities into each board's respective technical work programs</li> </ul>		<ul style="list-style-type: none"> <li>AUASB Technical Director visited NZ in October 2019 to meet with NZAuASB Technical Director and NZAuASB Chair and collaborate on joint Board projects and other NSS matters.</li> <li>Additional joint projects for current year identified and built into final 2019-20 AUASB Technical Work Program.</li> </ul>

 <b>Completed / On track</b>	 <b>In progress / Partially Completed / Delayed due to issues beyond AUASB control</b>	 <b>Yet to commence</b>	 <b>Delays / Issues encountered</b>
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

**Performance Measure Six:** *Develop thought leadership by identifying and implementing strategic projects that address emerging issues in auditing and assurance.*

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
<p>Undertake strategic thought leadership projects in the following topical or emerging auditing and assurance areas:</p> <ul style="list-style-type: none"> <li>- Audit quality</li> <li>- Assurance over Emerging Forms of External Reporting (EER) and other information in annual reports and other public reports</li> <li>- Assurance of Financial Reporting Frameworks</li> <li>- Audit and assurance of Charities and Not for Profit organisations</li> <li>- The Value of Audit and reducing the Audit Expectation Gap</li> <li>- Use of Technology in the Audit, including Data Analytics</li> </ul>	<ul style="list-style-type: none"> <li>▪ Project plans developed and 2019-20 outputs identified for each strategic thought leadership project area</li> <li>▪ Develop and implement outreach and engagement plans with subject matter experts and key stakeholders for each strategic thought leadership project area</li> <li>▪ Regular updates provided to AUASB members at AUASB meetings</li> </ul>		<ul style="list-style-type: none"> <li>• Ongoing collaboration with the FRC on Audit Quality activities as outlined in the FRC Audit Quality Action Plan.</li> <li>• EER Survey in progress and other EER thought leadership activities currently under consideration.</li> <li>• AUASB staff assisted in developing materials and taking part in AASB outreach events on Reforming the Australian Reporting Framework in October 2019, covering both 'For profit' and 'Not for Profit' sector reporting.</li> <li>• Three new or updated AUASB publications addressing how to apply the AUASB Assurance Framework effectively currently under development.</li> <li>• <b>Initial scoping of AUASB specific guidance on the use of Technology in the Audit, including Data Analytics completed and numerous meetings held with Canadian standard setter to coordinate activities.</b></li> <li>• <b>New PAG for Data Integrity and related audit issues being set up.</b></li> </ul>
<p>In accordance with the AUASB Evidence Informed Standard Setting Strategy, support or conduct high quality research in these and other areas relevant to the AUASB's strategic thought leadership areas.</p>	<ul style="list-style-type: none"> <li>▪ Promote research opportunities in these strategic thought leadership projects through academic networks and conferences in accordance with the EISS strategy</li> <li>▪ Ensure current and past research undertaken with the AUASB are published on the AUASB Research Centre and promoted across the profession</li> </ul>		<ul style="list-style-type: none"> <li>• AUASB Research Centre launched on the AUASB Website.</li> <li>• AUASB Academic Scholar role being advertised for 2020 appointments.</li> <li>• <b>AUASB Research Report 3 Audit Market Structure and Competition in Australia issued in October 2019, and AUASB Research Report 4, The Provision of Non-Audit Services by Audit Firms issued in December 2019, authored by AUASB scholar.</b></li> <li>• <b>Additional AUASB Research Reports (Audit Issues for NFP entities, Audit Opinions and Climate Change) currently under development.</b></li> </ul>
<p>Author or contribute to publications on major auditing and assurance developments.</p>	<ul style="list-style-type: none"> <li>▪ Develop and publish articles or publications in selected strategic thought leadership project areas</li> </ul>		<ul style="list-style-type: none"> <li>• AUASB Chair featured in CPA Australia's 'In the Black' cover article and being interviewed for an upcoming CAANZ 'Acuity' magazine article.</li> <li>• AUASB Technical Staff developing an outline for a commentary piece for the Australian Accounting Review journal.</li> </ul>



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


**Performance Measure Seven:** Increase stakeholder satisfaction and engagement with AUASB activities, with a specific focus on assurance practitioners, regulators, the professional bodies and financial report users.

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Develop and issue AUASB Publications (e.g. Bulletins, FAQs) to provide guidance to Stakeholders as required on AUASB Pronouncements and topical/emerging auditing and assurance issues and in conjunction with the release of all major AUASB standards and guidance statements.	<ul style="list-style-type: none"> <li>Develop Bulletins based on evidence and existing AUASB requirements</li> <li>Engage with regulators, stakeholders, AUASB members and other stakeholders as required to develop content</li> <li>Promote availability of AUASB guidance through various communication channels</li> </ul>		<ul style="list-style-type: none"> <li><b>Bulletin to support the implementation of ASA 540 released in December 2019.</b></li> <li><b>'AUASB Bulletin: Auditor's Responsibilities for the Financial Reporting Framework' issued in July 2019. To be updated following outcome from AASB ED's finalised in March 2020.</b></li> </ul>
Implement and promote the AUASB Evidence Informed Standard Setting (EISS) Strategy.	<ul style="list-style-type: none"> <li>Communicate benefits of EISS Strategy to academic community at conferences and technical forums</li> <li>Promote engagement with AUASB to attain research in thought leadership areas</li> </ul>		<ul style="list-style-type: none"> <li>AUASB Research Centre launched on website.</li> <li>AUASB Senior Project Manager appointed to Deakin University Integrated Reporting Steering Committee.</li> </ul>
AUASB members or staff to attend and present at auditing or assurance related professional and academic events/conferences and regular professional and regulatory forums.	<ul style="list-style-type: none"> <li>Identify appropriate local and international professional and academic events/conferences for the AUASB to present at or attend</li> <li>Attendance at local professional and regulatory forums</li> </ul>		<ul style="list-style-type: none"> <li>AUASB Chair and Technical staff members attended July 2019 AFAANZ conference, with AUASB Chair being a Keynote speaker.</li> <li><b>AUASB Technical staff presented at ANCAAR Conference in December 2019.</b></li> <li><b>AUASB involvement in ALLNEC Audit Conference currently being finalised.</b></li> <li><b>Planning commenced for AUASB involvement in CA ANZ 2021 Audit Conferences from March – May 2020.</b></li> </ul>
Obtain positive feedback from FRC members on AUASB activities.	<ul style="list-style-type: none"> <li>Valuable engagement with FRC members at FRC meetings</li> <li>AUASB staff to develop auditing and assurance related papers for FRC meetings</li> </ul>		<ul style="list-style-type: none"> <li><b>AUASB Chair Update and AUASB Performance Report presented at FRC meetings in September 2019 and November 2019.</b></li> <li><b>AUASB Technical staff assisted with FRC response to JPC Inquiry into the regulation of Auditing.</b></li> <li>AUASB technical staff assisted in development of FRC papers on Public Sector Financial Report reform and Nominations Committee.</li> </ul>
Develop and distribute a quarterly AUASB Update publication.	<ul style="list-style-type: none"> <li>AUASB Newsletters developed and sent out every 3 months</li> </ul>		<ul style="list-style-type: none"> <li>AUASB Newsletters for 2019-20 issued <b>September 2019 and December 2019.</b></li> </ul>

 <b>Completed / On track</b>	 <b>In progress / Partially Completed / Delayed due to issues beyond AUASB control</b>	 <b>Yet to commence</b>	 <b>Delays / Issues encountered</b>
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## AUASB Technical Work Program – 2019-2020 Q2 Report for AUASB

Current Priorities	Targeted Outputs/Outcomes/Process	Status	Comments (Changes since last report are highlighted in <b>Bold</b> )
Conduct a regular AUASB Stakeholder Satisfaction Survey and respond to results.	<ul style="list-style-type: none"> <li>Evaluate results from and develop actions in response to inaugural AUASB Stakeholder Satisfaction Survey completed in July 2019</li> <li>Consider need for additional survey in 2020.</li> </ul>		<ul style="list-style-type: none"> <li>Results from the AUASB Stakeholder Satisfaction Survey currently being evaluated by AUASB Technical Staff.</li> <li><b>AUASB Technical Staff to work with AASB-AUASB Communication Manager to develop updated AUASB Communication Strategy in February/March 2020.</b></li> </ul>
Implement initiatives to support and grow stakeholder engagement, measured via increased media mentions, social media activity and level of participation at AUASB events.	<ul style="list-style-type: none"> <li>Develop AUASB Communications Strategy</li> <li>Develop AUASB Message Calendar process</li> <li>Greater use of on-line tools to communicate AUASB projects (e.g. Webinars)</li> <li>Improved processes and communications to drive attendance and promotion of AUASB meetings and events</li> </ul>		<ul style="list-style-type: none"> <li>Current AUASB communications processes operating as intended.</li> <li>Updates to AUASB Communications Strategy and review of other AUASB Communications processes yet to commence.</li> <li><b>AUASB Technical Staff to work with AASB-AUASB Communication Manager to develop updated AUASB Communication Strategy in February/March 2020.</b></li> </ul>

 Completed / On track	 In progress / Partially Completed / Delayed due to issues beyond AUASB control	 Yet to commence	 Delays / Issues encountered
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