

Addressing Disclosures in the Audit of Financial Statements

1. This [preliminary]¹ document highlights matters that may be of relevance for auditors when addressing disclosures as part of an audit of financial statements. In particular, it describes financial reporting disclosure trends and their possible implications from an audit perspective and highlights how the International Standards on Auditing™ (ISAs™) guide the auditor in addressing disclosures. It is intended to help the consistent, effective and proper application of the ISAs.²
2. This preliminary document refers to requirements and application material of the ISAs, including those proposed amendments made by the International Auditing and Assurance Standards Board[®] (IAASB[®]) included in the Exposure Draft (ED), [Proposed Changes to the International Standards on Auditing—Addressing Disclosures in the Audit of Financial Statements](#). This material has been written in the context of an audit of general purpose financial statements prepared in accordance with a fair presentation framework, but may also be useful for audits of financial statements prepared in accordance with other financial reporting frameworks. Disclosures are ordinarily found in the notes to the financial statements, but may also be found on the face of the financial statements or outside the financial statements but incorporated by cross-reference (where permitted by the applicable financial reporting framework).³

Today's financial statements are becoming progressively more complex, and therefore appropriate, relevant and high-quality disclosures have become increasingly important to users of financial statements. Financial statements are now more likely to include a variety of disclosures, ranging from the more traditional disclosure items to more subjective or explanatory non-quantitative disclosures. Different financial reporting frameworks may establish diverse disclosure requirements, and preparers may find it necessary to supplement these requirements with additional disclosures in order for the financial statements to achieve fair presentation.

The Importance of the Role of the Auditor in Financial Statement Disclosures

3. The recent financial crisis highlighted that immediate action was needed to address the quality of financial statement disclosures. Users rely on information in financial statements to make economic

¹ It is intended that this Staff document will be finalized once the changes to the ISAs for disclosures have been approved by the IAASB. Any amendments that are made to those proposed in the Exposure Draft will be replicated in this document.

² This publication does not constitute an authoritative pronouncement of the IAASB nor does it amend or override the ISAs. The document does not introduce new requirements in addition to those contained in the ISAs. Rather, it is meant to provide auditors with relevant guidance in relation to auditing financial statement disclosures. Further, this publication is not meant to be exhaustive and reading this is not a substitute for reading the ISAs.

³ For example, International Financial Reporting Standard (IFRS) 7, *Financial Instruments: Disclosures*, states that “the disclosures required ... shall either be given in the financial statements or incorporated by cross-reference from the financial statements to some other statement ...”

decisions, and rely on the audit to enhance the degree of confidence they may place on the financial information contained therein. The auditor’s role in enhancing the credibility of the financial statements can contribute, through the audit process itself, to an improvement in the quality of financial statement disclosures.

4. Auditing disclosures is an integral part of the audit. It is therefore important that audit procedures during all stages of the audit include appropriate consideration of, and work effort on, disclosures. The ISAs already recognize the role of disclosures in performing risk assessments and developing responses to assessed risks, gathering and evaluating audit evidence, and in forming an opinion on the financial statements, including evaluating the fair presentation of the financial statements. In addition, the ISAs often refer to “classes of transactions, account balances and disclosures” when describing the auditor’s responsibilities in many areas, indicating that disclosures are treated in the same way as classes of transactions and account balances in the application of these requirements.
5. Auditing disclosures has become more complex as the disclosures themselves have evolved. As the focus has shifted to providing more non-quantitative information in the disclosures (for example, disclosures about risks affecting the entity, disclosure of estimation uncertainty, or other narrative disclosures), applying the requirements in the ISAs to disclosures when planning the audit, identifying and assessing the risks of material misstatement, obtaining sufficient appropriate audit evidence, and forming an opinion has become more challenging. Notwithstanding that there may be challenges in auditing certain disclosures, attention to disclosures in applying the requirements of the ISAs throughout the audit process, enhances the quality of the audit and achieves compliance with the ISAs.
6. The following table illustrates some of the relevant ISAs when auditing disclosures:

Planning the Audit, and Identifying, Assessing and Responding to Risks of Material Misstatement	Obtaining Sufficient Appropriate Audit Evidence	Completing the Audit
<p style="text-align: center;">ISA 200</p> <p style="text-align: center;"><i>Overall Objectives of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing</i></p>	<p style="text-align: center;">ISA 500</p> <p style="text-align: center;"><i>Audit Evidence</i></p>	<p style="text-align: center;">ISA 450</p> <p style="text-align: center;"><i>Evaluation of Misstatements Identified during the Audit</i></p>
<p style="text-align: center;">ISA 210</p> <p style="text-align: center;"><i>Agreeing the Terms of Audit Engagements</i></p>	<p style="text-align: center;">ISA 501</p> <p style="text-align: center;"><i>Audit Evidence—Specific Considerations for Selected Items</i></p>	<p style="text-align: center;">ISA 700</p> <p style="text-align: center;"><i>Forming an Opinion and Reporting on Financial Statements</i></p>
<p style="text-align: center;">ISA 240</p> <p style="text-align: center;"><i>The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements</i></p>	<p style="text-align: center;">ISA 540</p> <p style="text-align: center;"><i>Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures</i></p>	
<p style="text-align: center;">ISA 260</p> <p style="text-align: center;"><i>Communication with Those Charged with Governance</i></p>	<p style="text-align: center;">ISA 550</p> <p style="text-align: center;"><i>Related Parties</i></p>	

Planning the Audit, and Identifying, Assessing and Responding to Risks of Material Misstatement	Obtaining Sufficient Appropriate Audit Evidence	Completing the Audit
ISA 300 <i>Planning an Audit of Financial Statements</i>	ISA 560 <i>Subsequent Events</i>	
ISA 315 (Revised) <i>Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment</i>	ISA 570 <i>Going Concern</i>	
ISA 320 <i>Materiality in Planning and Performing an Audit</i>		
ISA 330 <i>The Auditor's Responses to Assessed Risks</i>		

7. In light of the complexity and importance of disclosures, the quality of the audit may be enhanced if the auditor:

- Gives appropriate attention to disclosures early in the audit process;
- Takes into account how management prepares the disclosures, including understanding the systems or processes for doing so, including those that are not part of the general ledger system, and the related controls;
- Recognizes the unique challenges in doing so, by considering disclosures, including non-quantitative disclosures, when identifying risks of material misstatements and when evaluating misstatements identified; and
- Considers disclosures in light of the facts and circumstance of the entity based on the auditor's knowledge of the entity and the audit evidence obtained during the audit when evaluating the overall presentation of the financial statements.

8. Disclosures are likely to be more challenging to prepare and audit when the business model and transactions of the entity are complex. As such, the challenges relating to auditing disclosures may be more significant for these types of entities. Notwithstanding that some financial reporting frameworks for small- and medium-sized entities (SMEs) may have less complex disclosure requirements, auditors of SMEs may also encounter auditing challenges, and the guidance that follows may also assist auditors of SMEs.

Financial Reporting Disclosure Trends

9. Financial reporting has evolved to provide greater transparency about an entity's financial and operational risks. Business and capital markets have also become more challenging, and there is

now greater complexity in business models, and more diversity in sources of risk and uncertainty, as well as greater sophistication in how risk is managed.

10. This evolution has led to a need for entities to provide new types of information that may be more subjective but also more relevant to users. Financial reporting standards, and in particular their disclosure requirements, and practices have responded to these changes by shifting from simply providing breakdowns of line items on the face of the financial statements to providing a broad variety of disclosures, some of which are more explanatory or narrative in nature. Today, disclosures in the financial statements may include:
- **Significant accounting policies**—Descriptions of the accounting policies adopted by the entity, relevant to understanding the line items on the face of the financial statements, including the basis of measurement used in preparing the financial statements.
 - **Components of line items**—Such as breakdowns of line items into smaller categories or reconciliations.
 - **Judgments and reasons**—Nature of judgments made in the process of applying accounting policies, and management decisions and the rationale supporting them. Examples include how an entity distinguishes investment properties from owner-occupied properties and from property held for sale in the ordinary course of business. This category may also include disclosures about why an entity's ownership interest constitutes control in respect of an investee where less than half of its voting rights or potential voting rights are owned directly or indirectly.
 - **Models, including assumptions and inputs**—May include disclosures of information relevant to the calculation of items in the financial statements, such as possible ranges of values. This may also include forward-looking information, to the extent that it is used to support amounts recognized in the balance sheet, such as discount rates, effective interest rates and growth rates used in impairment testing.
 - **Financial exposure to risks and uncertainties arising from recognized and unrecognized resources and obligations**—Disclosures to enable users to understand the underlying measurement variability or estimation uncertainty of an item in the financial statements, such as a sensitivity analysis. An example of a disclosure about exposure to risks is value-at-risk disclosures.
 - **Material uncertainties in relation to the entity's ability to continue as a going concern**—Disclosures about material uncertainties related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.
 - **Related party disclosures**—Descriptions of related party relationships and amounts of transactions, including key management compensation.
 - **Unrecognized assets and unrecognized liabilities**—Disclosures about assets or liabilities that do not meet the criteria for recognition in the financial statements, but that are useful for the users of the financial statements.
 - **Pro forma financial information**—Disclosures may be required relating to business combinations that have occurred after the balance sheet date but before the financial statements are issued.

- **Descriptions of internal processes**—Disclosures such as risk management policies and practices of an entity. An example is the disclosure of the policies and procedures for managing financial instrument risks.
- **Disclosure of the fair value of an amount recorded using a different measurement basis**—Such as a requirement to disclose fair values for items measured using another measurement basis than that which is presented on the face of the financial statements, for example, historical cost or amortized cost.
- **“Objective-based disclosure requirements”⁴**—Overarching requirements in financial reporting frameworks that set out the objectives of the disclosures to be provided rather than require specific disclosures. Under this regime, preparers are expected to provide additional disclosures when compliance with the specific disclosure requirements in a standard would be insufficient for users to be able to understand the impact of particular transactions, other events and conditions on the entity’s financial position and performance.
- **Factual information about the entity**—Such as addresses, names of group entities, composition of share capital and dividend payments.

Other Financial Reporting Considerations

11. The requirements of the applicable financial reporting framework,⁵ including those relating to disclosures, determine the form and content of the financial statements.⁶ Although financial reporting frameworks do not specify how to disclose every transaction, event or account balance, broad principles underlying the preparation and presentation of financial statements may be embodied in an applicable conceptual framework,⁷ and may be used by auditors to help assess whether the financial statements comply with the financial reporting requirements. Whether information communicated in the financial statements is useful to users of the financial statements in making economic decisions is highly dependent on how an entity presents and discloses such information.
12. In representing that the financial statements have been prepared in accordance with the applicable financial reporting framework, management implicitly, or explicitly, is expected to make assertions regarding the recognition, measurement, presentation and disclosure of the various elements of financial statements and related disclosures.⁸ Some conceptual frameworks call this the

⁴ That is, disclosure requirements that establish the objectives to be accomplished, while not expressly requiring specific disclosure items

⁵ Some financial reporting frameworks are a “fair presentation” framework, which requires compliance with the requirements of the framework and acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework (ISA 200, paragraph 13(a)).

⁶ ISA 200, paragraph A6

⁷ For example, the International Accounting Standards Board’s (IASB) *Conceptual Framework for Financial Reporting* (Framework 2010). The IASB is currently in the process of revising parts of its Framework 2010.

⁸ ISA 315 (Revised), paragraph A110

fundamental characteristics of useful information,⁹ and in contemporary accounting standards often include “relevance” and “faithful representation”,¹⁰ or similar characteristics.

13. As accounting standards have continued to evolve, some accounting standard setters have found it necessary to make changes to their conceptual frameworks. For example, in some accounting frameworks, “reliability” was once a principal qualitative characteristic of financial information but has been superseded by other concepts, such as “faithful representation.”
14. Given this new emphasis on faithful representation, it has been argued that, in some circumstances, the disclosures that provide further context to a financial statement line item may become at least as important, if not more useful and relevant, to users as the amount disclosed on the face of the financial statements. The supporting disclosures are necessary to inform users about judgments and assumptions made in the measurement of the line item, the reasons for these judgments, facts, and circumstances and the measurement uncertainty related to that line item. In effect, the disclosures in these cases are being used to achieve the principles of relevance or faithful representation, or both.

Audit Considerations Relating to Disclosures

15. The auditor addresses disclosures in the context of the auditor’s overall objectives in conducting an audit in accordance with the ISAs, which are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.¹¹
16. Throughout the ISAs, the use of the term “financial statements,” by definition, includes disclosures.¹² Accordingly, where the requirements and guidance in the ISAs refer to “financial statements”, this is intended to include considerations about disclosures as well as classes of transactions and account balances. However, although gathering sufficient appropriate audit evidence for disclosures is an integral part of the audit, it is not the auditor’s objective to form a separate opinion on each individual disclosure in the financial statements.
17. The auditor considers the common financial information needs of intended users of the financial statements, including when making decisions related to materiality. The determination of materiality under the ISAs assumes that users have a reasonable knowledge of business and economic activities and accounting. It also assumes that they have a willingness to study the information in the financial statements with reasonable diligence; understand that the financial statements are prepared, presented and audited to levels of materiality; recognize the uncertainties inherent in the

⁹ The IASB’s Framework 2010 notes that the fundamental qualitative characteristics include the types of information that is most useful to users for making economic decisions.

¹⁰ Relevance and faithful representation are the fundamental qualitative characteristics of the IASB’s Framework 2010, and are used as examples to represent the characteristics of accounting information included in disclosures. Other accounting frameworks may use similar terms, which are to be considered in a similar way when assessing the accounting requirements of information to be included in disclosures. Notwithstanding that the IASB is currently revising its Conceptual Framework, it is not expected that further changes will be made to their fundamental qualitative characteristics.

¹¹ ISA 200, paragraph 11

¹² ED: Revisions to ISA 200, paragraph 13(f) (The definition has been revised to clarify what is meant by disclosures.)

measurement of amounts based on estimates, judgment and the consideration of future events; and make reasonable economic decisions on the basis of the information in the financial statements.¹³

18. The concepts of professional judgment¹⁴ and professional skepticism¹⁵ are fundamental to audits of financial statements and therefore apply to the audit work performed on disclosures. The need for professional skepticism is essential when considering disclosures, for example with regard to:
- Evaluating whether sufficient appropriate evidence has been obtained, which can be particularly challenging for some disclosures, such as non-quantitative disclosures.
 - Evaluating management's judgment, and the potential for management bias, in applying the requirements of the applicable financial reporting framework, for example in disclosing related party relationships and transactions, or in omitting such disclosures.
 - Drawing conclusions based on the audit evidence obtained, for example, assessing whether the presentation and disclosures achieve fair presentation.

A Focus on Disclosures throughout the Audit Process

19. Disclosures are an integral part of the financial statements. Accordingly, it is important for the auditor to give attention to disclosures throughout the audit. Various aspects of the ISAs are intended to help auditors focus on disclosures earlier in the audit process, and when relevant in performing audit procedures on classes of transactions, events, account balances, and disclosures, in particular in relation to:
- **Terms of the engagement**—Additional matters may be included in the audit engagement letter, for example:¹⁶
 - A description of the responsibilities of management relating to disclosures, particularly relating to making information available for the audit, as well as the draft financial statements, including related disclosures, to allow sufficient time to complete the audit; and
 - The expectation that management will provide written representations.
 - **Communication with those charged with governance**—When communicating about the planned time and scope of the audit, the auditor may also consider discussing the impact on the audit of significant changes to the applicable financial reporting framework, or the entity's environment, financial condition or activities, which may affect the required disclosures in the financial statements, to obtain the views of those charged with governance.¹⁷

¹³ ISA 320, paragraph 4

¹⁴ ISA 200, paragraph 16

¹⁵ ISA 200, paragraph 15

¹⁶ ED: Revisions to ISA 210, paragraph A23 (new example on management making information available for purposes of the audit included) and Example Audit Engagement Letter in Appendix 1 (footnote added to highlight examples of additional items that may be added to the audit engagement letter).

¹⁷ ED: Revisions to ISA 260, paragraph A12 (additional example added of disclosure related matters that may be discussed with those charged with governance)

- **Planning**—Auditor consideration earlier in the audit process about some of the challenges related to disclosures may also help meet the objectives for effective planning, in particular when disclosures may contain information from systems or processes that are not part of the general ledger system, as this may also lead to additional challenges.¹⁸ Consideration about disclosures early in the audit process may also help the auditor to identify the impact on the audit from:
 - Significant new or revised disclosures arising from changes in the entity’s environment, financial condition or activities (for example, that result in a change in the segments that should be identified and reported if a significant new subsidiary has been acquired).
 - Significant new or revised disclosures arising from changes to the applicable financial reporting framework.
 - The need for the involvement of an auditor’s expert to assist with particular disclosures (for example, disclosures related to pension or other retirement benefit obligations).
 - Matters relating to disclosures that the auditor may wish to discuss with those charged with governance.¹⁹

Understanding the Entity and Its Environment, and the Auditor’s Risk Assessment and Response in Relation to Disclosures

ISA 300 requires the auditor to develop an audit plan that includes, among other things, a description of the nature, timing and extent of planned further audit procedures at the assertion level, as determined under ISA 330.²⁰ As part of planning the audit and developing the audit plan, the auditor is required to understand the entity and its environment, including internal control.²¹

20. Consideration of the nature, timing and extent of work to be performed on disclosures is integral to this process of developing an appropriate audit plan. The following areas may be particularly important in the context of disclosures in understanding the entity and its environment:²²
- Regulatory factors, such as the required disclosures in a regulated industry or disclosure of environmental requirements affecting the industry and the entity’s business;
 - Disclosures about investments and investment activities, such as investments in non-consolidated entities, including partnerships, joint ventures and special-purpose entities;
 - Disclosures about financing and financing activities such as debt structure and related terms, including off-balance-sheet financing arrangements and leasing arrangements; and

¹⁸ ED: Revisions to ISA 300, Para A12a (new guidance for auditors to consider the effect of disclosures on the nature, timing and extent of planned audit procedures)

¹⁹ ED: Revisions to ISA 300, paragraph A12b (new guidance to provide examples of matters that may be dealt with on a more timely basis in the audit if disclosures considered earlier in the audit process)

²⁰ ISA 300, paragraph 9(b)

²¹ ISA 315 (Revised), paragraphs 11–12

²² See ISA 315 (Revised), paragraph 11(a).

- Financial reporting practices, such as industry-specific disclosures,²³ as well as understanding whether an entity's complex business structures have been adequately disclosed, or whether related party disclosures properly describe, as required, the relationship and transactions between the owners of the entity and other people or entities.²⁴
21. Some of the required understanding may also come from the auditor's previous experience with the entity and audit procedures performed in previous audits. For example, areas where the auditor previously experienced difficulty in performing the necessary audit procedures may inform the auditor for the current year's audit.²⁵
 22. Understanding the information system, including related business processes, may also be important for auditors in order to understand the generation of information and its processing for disclosures. Disclosures may contain some information from systems or processes that are not part of the general ledger system – this information may come from sources such as an entity's risk management system, a valuation report produced by an expert, models or other calculations used to develop estimates recognized or disclosed in the financial statements, or sensitivity analyses derived from financial models to demonstrate that management has considered alternative assumptions.²⁶

ISA 315 (Revised) requires discussion by the engagement partner and other key engagement team members about the susceptibility of the entity's financial statements to material misstatement, and the application of the applicable financial reporting framework to the entity's facts and circumstances.²⁷

23. Matters the audit engagement team may discuss, relating to disclosures, include:
 - New 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.²⁸
24. The discussion required by ISA 315 (Revised) places particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud might occur. This also includes consideration of the risk that management may attempt to obscure information by presenting disclosures that are not clear and understandable. Examples of

²³ ED: Revisions to ISA 315 (Revised), paragraph A31 (revised to emphasize disclosure considerations in specific areas already included in this paragraph)

²⁴ ED: Revisions to ISA 315 (Revised), paragraph A30 (revised guidance to emphasize disclosures)

²⁵ ED: Revisions to ISA 315 (Revised), paragraph A19 (example added about matters arising from disclosures in previous period audits for the auditor to consider in obtaining an understanding of the entity)

²⁶ ISA 315 (Revised), paragraph A68 and ED: Revisions to ISA 315 (Revised), paragraph A89a (new guidance with examples of where this information may come from)

²⁷ ISA 315 (Revised), paragraph 10

²⁸ ED: Revisions to ISA 315 (Revised), paragraph A21a (new guidance for possible related matters that could be discussed)

areas where there may be an increased risk of misstatement resulting from fraudulent financial reporting may include disclosure of related party relationships and transactions; and areas of subjectivity or judgment (for example, maturity analysis tables; sensitivity disclosures; and disclosures required to achieve fair presentation).²⁹

The auditor is required by ISA 315 (Revised) to identify and assess the risk of material misstatement at the financial statement level; and at the assertion level for classes of transactions, account balances, and disclosures.³⁰

25. This risk assessment provides a basis for designing and performing further audit procedures. Deficiencies such as a lack of management competence or inadequate controls over the preparation of the information (including disclosures) in the financial statements may have a more pervasive effect on the financial statements, and require an overall response by the auditor,³¹ such as considering the knowledge and experience of the engagement team members responsible for reviewing the financial statements.
26. Since many disclosures are directly related to line items in the financial statements, consideration of the risk of material misstatement at the assertion level for disclosures may be done at the same time as, and in conjunction with, the related line item. For example, when assessing the risk of material misstatement for impairment amounts recognized (for example, relating to the valuation of goodwill), the auditor may also assess the risk of material misstatement about the related disclosures, such as the information about the impairment model (model used, growth rates, interest rates, etc.). For disclosures, the level at which the risk assessment is carried out is a matter of the auditor's professional judgment, and is performed using the knowledge that the auditor has gained about the entity and its activities such that the assessment is made at the appropriate level.³²
27. Financial reporting frameworks may require disclosures that are not directly related to a recorded transaction, event or account balance (for example, disclosure of a contingent liability). The auditor's assessment of the risks of material misstatement also extends to these disclosures, and the same assertions described for classes of transactions and events and account balances, and related disclosures, may be used (adapted as appropriate).³³
28. The auditor's risk assessment determines the nature, timing and extent of further audit procedures.³⁴ As explained in paragraph A1 of ISA 320, materiality and audit risk are considered when identifying and assessing the risks of material misstatement in classes of transactions,

²⁹ ED: Revisions to ISA 240, paragraph A11 (guidance on the discussion enhanced to include consideration of disclosures where the risks of material misstatement arising from fraud may be increased)

³⁰ ISA 315 (Revised), paragraph 25

³¹ ISA 315 (Revised), paragraph A118 and ED: Revisions to ISA 315 (Revised), paragraph A119 (new example added to explain when a matter relating to disclosures is pervasive to the financial statements)

³² ED: Revisions to ISA 315 (Revised), paragraphs A124 (a)–(b) (assertions for classes of transactions and events, and account balances, revised to include assertions for related disclosures and presentation)

³³ ED: Revisions to ISA 315 (Revised), paragraph A124a (new guidance for those disclosures that are not necessarily covered by paragraphs A124(a)–(b))

³⁴ ISA 315 (Revised), paragraph 25

account balances and disclosures. The auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements.³⁵

29. In identifying the risks of material misstatement, the auditor also considers non-quantitative disclosures.³⁶ A misstatement in non-quantitative disclosures may be significant enough to affect the economic decision of users of financial statements. For example, non-disclosure about a possible liability that does not meet the recognition criteria may be important enough to affect such decisions. When planning the audit, the auditor not only makes judgments about the size of amounts disclosed, but also considers the nature of quantitative and non-quantitative disclosures that reasonably could be expected to influence the economic decisions of users. Depending on the circumstances of the entity and the engagement, examples could include disclosures about:
- Liquidity and debt covenants of an entity in financial distress.
 - Events or circumstances that have led to the recognition of an impairment loss.
 - Key sources of estimation uncertainty, including assumptions about the future.
 - The nature of a change in accounting policy, and other relevant disclosures required by the applicable financial reporting framework where, for example, new financial reporting requirements are expected to have a significant impact on the financial position and financial performance of the entity.
 - Share-based payment arrangements, including information about how any amounts recognized were determined, and other relevant disclosures.
 - Related parties, and related party transactions.
 - Sensitivity analyses intended to enable users to understand the underlying measurement uncertainty of a recorded or disclosed amount.³⁷
30. Appendix 2 of ISA 315 (Revised) provides examples of conditions and events that may indicate the existence of risks of material misstatement. Among other things, events or transactions that involve significant measurement uncertainty, and the possibility of omission of, or obscuring, useful and relevant information, may be particularly relevant in the context of the auditor's work on disclosures.³⁸
31. The timing of the preparation of the financial statements, particularly for those disclosures that do not relate to a line item on the balance sheet, income statement, cash flow statement or statement of changes in equity, may be a relevant consideration in the auditor's determination of when to

³⁵ ED: Revisions to ISA 315 (Revised), paragraph A128a (guidance added for assessing the risks of material misstatements in disclosures)

³⁶ ED: Revisions to ISA 315 (Revised), paragraph A128b (new guidance to emphasize that non-quantitative disclosures are also included in the auditor's identification and assessment of the risks of material misstatement)

³⁷ ED: Revisions to ISA 315 (Revised), paragraph A128c (new guidance providing examples of material non-quantitative disclosures)

³⁸ ED: Revisions to ISA 315 (Revised), paragraph A128 and Appendix 2 (new examples added to emphasize disclosures)

perform audit procedures in accordance with ISA 330.³⁹ There may be various reasons why disclosures may be prepared late in the financial reporting process, including that: management's focus may initially be on the line items in the financial statements (i.e., the amounts recognized) as these may often be used for preliminary announcements; or the financial statements may be prepared in a separate process which is done after the information generated by the general ledger is completed. Nonetheless, as indicated in paragraph 19 above, emphasizing management's responsibilities relating to the preparation of the draft financial statements, including disclosures, when agreeing the terms of engagement is an important consideration for the auditor.

32. When designing audit procedures in relation to disclosures, the auditor may also consider:
- The controls over the preparation of the financial statements,⁴⁰ such as the adequate review of the preparation of the financial statements, including for information for those disclosures from systems or processes that are not part of the general ledger system. For example, those charged with governance have responsibility for overseeing the preparation of the financial statements but there may be other controls involving review of the disclosures that are directly related to the underlying amounts recognized, with any discrepancies being followed up.
 - Procedures performed on the related line items in the financial statements. For example, some parts of the required disclosures may already have been audited when the underlying numbers have been audited.
 - The assessed risks for the disclosures, which may affect the disclosures selected for testing.
33. The audit procedures performed on disclosures are based on the auditor's assessment of risk and materiality for the financial statements as a whole or the materiality for particular financial statement items, when applicable. For example, the disclosure of the objectives, policies and processes for managing credit risk⁴¹ may not be considered a risk of material misstatement for some entities and therefore the auditor may consider it appropriate to refer to relevant risk manuals, minutes of meetings etc. in order to assess the accuracy with which the disclosure describes the entity's process. However, for entities with banking and insurance activities, the objectives, policies and processes for managing credit risk are more fundamental to the entity, and the work effort required would likely be more comprehensive. In this case, the auditor's focus may be more on whether the disclosure properly describes the process the entity has followed, and audit procedures could include detailed testing of the sources from which the disclosed information was derived or testing the operating effectiveness of controls over the information used in the preparation of these disclosures. The auditor's procedures may also involve using those with specialized skills and knowledge in this area.

³⁹ ED: Revisions to ISA 330, paragraph A14 (new example added relating to disclosures when considering the planned timing of audit procedures on disclosures)

⁴⁰ ED: Revisions to ISA 315 (Revised), paragraph A99a (example of a control activity added relating to the preparation of the financial statements)

⁴¹ For example, IFRS 7, *Financial Instruments: Disclosures*, paragraph 33(b) requires qualitative disclosures for risks arising from financial instruments, such as credit risk, to be disclosed.

ISA 330 also requires the auditor to agree or reconcile the financial statements, including disclosures, with the underlying accounting records, including information from systems or processes that are not part of the general ledger system.⁴²

34. The auditor uses professional judgment, taking into account the risks of material misstatement, in determining the nature and extent to which the disclosures are agreed or reconciled.⁴³

In responding to the risks of material misstatement, the auditor is also required to perform audit procedures to evaluate whether the overall presentation of the financial statements, including the related disclosures, is in accordance with the applicable financial reporting framework.⁴⁴

35. This evaluation relates to whether the financial statements, including related disclosures, are presented in a manner that reflects:
- The appropriate classification and description of financial information and the underlying transactions and events; and
 - The appropriate form, arrangement, and content of the financial statements. This includes, for example, the terminology used as required by the applicable financial reporting framework, the level of detail provided, the aggregation and disaggregation of amounts, and the classification of items in the financial statements and the bases of amounts set forth.⁴⁵

Sufficient Appropriate Audit Evidence for Disclosures

The auditor is required to design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.⁴⁶

36. Audit evidence is necessary to support the auditor's opinion and report. Whether sufficient appropriate audit evidence has been obtained to enable the auditor to form an opinion is a matter of professional judgment. The requirement for the auditor to obtain sufficient appropriate audit evidence for disclosures is the same as for obtaining audit evidence for classes of transactions and account balances, which in some cases will be done concurrently.
37. For example, procedures for obtaining audit evidence for amounts recognized in the financial statements may also satisfy the auditor's consideration of whether the disclosure is an accurate portrayal of the basis for the calculation, recognizing that the disclosure is often an integral part of the presentation of the related financial statement amount (for example, the model used, the assumptions such as growth rates, discount rates, etc.).

⁴² ED: Revisions to ISA 330, paragraph 20 (requirement revised to make clear that the reconciliation applies to the financial statements, regardless of where the information comes from)

⁴³ ED: Revisions to ISA 330, paragraph A52 (revised guidance to make clear that the auditor uses professional judgment when deciding the work effort in agreeing or reconciling the financial statements)

⁴⁴ See ISA 330, paragraph 24.

⁴⁵ ED: Revisions to ISA 330, paragraph A59 (revised guidance for additional considerations for the auditor when performing the overall evaluation of the presentation of the financial statements)

⁴⁶ ISA 500, paragraph 6

38. Various ISAs, in particular ISA 500, ISA 501, ISA 540 and ISA 550, establish requirements and provide guidance about obtaining audit evidence for the wide variety of disclosures in financial statements, for example:
- Requirements and guidance for obtaining sufficient appropriate audit evidence, including types of procedures, the relevance and reliability of audit evidence, and considerations where audit evidence is prepared by management's expert.⁴⁷
 - Obtaining audit evidence for selected items, such as litigation and claims,⁴⁸ and segment information.⁴⁹
 - Requirements and guidance for disclosures related to accounting estimates.⁵⁰
 - Requirements and guidance for auditing related party disclosures.⁵¹
 - Requirements and guidance for obtaining evidence for events between reporting date and the date of the financial statements, including adequate disclosures in the financial statements.⁵²
 - The auditor's responsibilities relating to disclosures about going concern required by a financial reporting framework.⁵³

How Misstatements in Disclosures Are Evaluated

ISA 450 requires the accumulation of misstatements identified during the audit ...⁵⁴

39. Misstatements in disclosures can be as important to users as misstatements of line items in the financial statements. For example, in the recent financial crisis, users placed heavy emphasis on the maturity analysis of liabilities to ascertain the difficulty the entity may have in rolling over debt facilities. A misstatement in this disclosure could affect users' decisions to buy, hold, or sell investments in that entity, extend finance or take another economic action.
40. ISA 450 applies equally to classes of transactions, account balances and disclosures. Misstatements in disclosures may result from:
- An omission of a disclosure, including non-quantitative disclosures and objective-based disclosures⁵⁵ required by certain financial reporting frameworks.

⁴⁷ See ISA 500

⁴⁸ ISA 501, paragraphs 9–11

⁴⁹ ISA 501, paragraph 13

⁵⁰ ISA 540, paragraphs 19–20 and A120–A123. In addition, International Auditing Practice Note (IAPN) 1000, *Special Considerations in Auditing Financial Instruments*, provides further guidance for obtaining sufficient appropriate audit evidence for accounting estimates, including fair value accounting estimates.

⁵¹ See ISA 550.

⁵² See ISA 560.

⁵³ See ISA 570.

⁵⁴ ISA 450, paragraph 5

⁵⁵ For example, IFRS 7, paragraph 42H, states that "an entity shall disclose any additional information that it considers necessary to meet the disclosure objectives..."

- An inappropriate classification, aggregation or disaggregation, of information.
- For financial statements prepared in accordance with a fair presentation framework, the omission of disclosures beyond that specifically required by the applicable financial reporting framework necessary for fair presentation.⁵⁶

Misstatements in disclosures (other than those that are clearly trivial) are also accumulated, and aggregated where appropriate, to assist the auditor in evaluating their effect on the disclosures and the financial statements as a whole.⁵⁷

41. In addition to assessing misstatements individually, professional judgment is used in aggregating misstatements to determine whether they are material. Although misstatements in non-quantitative disclosures cannot be aggregated in the same manner as misstatements of amounts, they are still evaluated individually, and collectively, with other misstatements.⁵⁸
42. As part of the auditor's considerations about misstatements in disclosures, the auditor may also consider whether individual misstatements could be indicative of bias in management's judgments that results in misleading information, or a trend towards duplicative or uninformative disclosures that may obscure important financial information.⁵⁹

Forming an Opinion on the Financial Statements

In forming an opinion on the financial statements, the auditor is required to evaluate whether, in view of the requirements of the applicable financial reporting framework, the financial statements adequately disclose the significant accounting policies selected and applied; ... the information presented in the financial statements is relevant, reliable, comparable and understandable; and the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements...⁶⁰

43. When evaluating the financial statements, the auditor exercises professional skepticism in assessing whether disclosures are, in the auditor's view, insufficient or inappropriate, and consequently whether to challenge management. Therefore, in addition to considerations about the individual and aggregated effect of misstatements in disclosures, in accordance with ISA 700, the auditor also considers whether:⁶¹
 - The financial statements adequately disclose the significant accounting policies selected and applied. This may include the relevance of the accounting policies to the entity, and the clarity

⁵⁶ ED: Revisions to ISA 450, paragraph A1 (additional examples added to illustrate possible misstatements in disclosures)

⁵⁷ ED: Revisions to ISA 450, paragraph A2a (new paragraph to emphasize that misstatements in disclosures are also accumulated, and aggregated where appropriate, and assessed for material misstatements)

⁵⁸ ED: Revisions to ISA 450, paragraph A2a (new paragraph to emphasize that misstatements in non-quantitative disclosures are also accumulated and assessed notwithstanding that they cannot be aggregated in the same way as misstatements in amounts)

⁵⁹ ED: Revisions to ISA 450, paragraph A17a (new guidance added for pervasive issues that may be found in disclosures)

⁶⁰ ISA 700, paragraphs 13 (a), (d) and (e)

⁶¹ ED: Revisions to ISA 700, paragraphs A3a–A4 (new and revised guidance on considerations relating to disclosures for the auditor when carrying out this evaluation)

with which they have been presented.

- The information in the financial statements is relevant, reliable, comparable and understandable. This may include whether:
 - The financial statements, including disclosures, are appropriately classified and characterized and presented in a clear and concise manner, but do not omit relevant information.
 - The disclosures undermine the overall presentation of the financial statements by including information that is not relevant or in a manner that may obscure a proper understanding of the matters disclosed.
 - The placement of significant disclosures gives appropriate prominence to them (for example when there is perceived value of entity-specific information to users), and whether the disclosures are appropriately cross-referenced to draw attention to related matters, where appropriate.⁶²

In addition, the auditor may consider whether the financial statements are comparable to the entity's financial statements of previous periods.

- The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements. This may include the extent to which the information in the financial statements is useful and specific to the circumstances of the entity. For example, the auditor may consider whether the disclosures are adequate to assist the intended users to understand:
 - The nature and extent of the entity's potential assets and liabilities arising from those transactions or events that do not meet the criteria for recognition (or the criteria for derecognition) established by the applicable financial reporting framework.
 - The nature and extent of risks arising from those material transactions and events, for example, disclosure of the financial risks to which an entity may be exposed if it undertakes derivatives trading.
 - The methods used and the assumptions and judgments made, and changes to them, that affect amounts presented or otherwise disclosed, including relevant sensitivity analysis.⁶³

⁶² ED: Revisions to ISA 700, paragraph A3b (new paragraph to provide guidance on the auditors efforts in relation to the evaluation of the understandability and relevance of information presented in the financial statements)

⁶³ ED: Revisions to ISA 700, paragraph A4 (revised to include examples of the matters to consider when evaluating whether financial statements are relevant and specific to the entity)

Evaluating Whether the Financial Statements Achieve Fair Presentation

If the auditor is required to evaluate whether the financial statements are prepared in accordance with a fair presentation framework, the auditor also considers the overall presentation, structure and content of the financial statements, and whether the financial statements, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation in accordance with ISA 700.⁶⁴

44. The auditor's evaluation about whether the financial statements achieve fair presentation, both in respect of presentation and disclosure, is a matter of professional judgment. This evaluation takes into account matters such as the facts and circumstances of the entity, including changes thereto, based on the auditor's knowledge of the entity and the audit evidence obtained during the audit. The evaluation also includes consideration, for example, of the disclosures needed to achieve a fair presentation arising from matters that may be relevant to the economic decisions of the users of the financial statements, such as evolving financial reporting requirements or the changing economic environment.⁶⁵
45. In performing this evaluation, the auditor considers what is needed in order to achieve fair presentation of the financial statements. Some financial reporting frameworks explicitly address the concept of fair presentation. For example, IFRSs note that fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses. As noted in paragraph 7(b) of ISA 700, fair presentation involves not only compliance with the requirements of the applicable financial reporting framework, but also the possibility that additional disclosures may be necessary, regardless of whether there is a specific requirement for that information in the framework.⁶⁶
46. Finally, those charged with governance may have an important role to play in relation to the entity's disclosures. The auditor may discuss with management and those charged with governance, as appropriate, their views on why a particular presentation was chosen, as well as alternatives that may have been considered, including:
- The degree to which the amounts in the financial statements are aggregated or disaggregated, and whether the presentation of amounts or disclosures obscures useful information, or results in misleading information.
 - Consistency with appropriate industry practice, or whether any departures are relevant to the entity's circumstances and therefore warranted.⁶⁷

⁶⁴ See ISA 700, paragraph 14.

⁶⁵ ED: Revisions to ISA 700, paragraph A4b (new guidance added to emphasize that the evaluation of whether the financial statements achieve fair presentation is a matter of professional judgment)

⁶⁶ ED: Revisions to ISA 700, paragraph A4a (new guidance to emphasize that, when evaluating whether the financial statements achieve fair presentation, consideration is given to whether additional disclosures are required in addition to those required by the applicable financial reporting framework.)

⁶⁷ ED: Revisions to ISA 700, paragraph A4c (new guidance about the types of matters that may be discussed with management or those charged with governance when evaluating whether fair presentation has been achieved)

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