

Proposed ISA 315 (Revised)¹—Issues and Recommendations

Objectives of the Agenda Item

The objectives of this agenda item are:

1. To approve the revised standard ISA 315 (Revised), and related conforming and consequential amendments to other ISAs arising from the revisions to ISA 315 (Revised).
2. To obtain Board member's views about the guidance that will be published together with revised ISA 315 (Revised).

I. Introduction and Approach to this Paper

1. Since the June 2019 IAASB meeting, the ISA 315 Task Force (the Task Force) has focused on addressing the comments received from Board members (both during the Board meeting and offline) and continuing to look for ways to improve the readability and understandability of the standard. In doing so, a key objective has been to ensure that the substantive remaining issues raised by Board members were adequately redeliberated and addressed by the Task Force in preparation for Board approval. This Agenda Item provides information and explanation of the matters presented for discussion at the September 2019 Board meeting.

Papers Presented for Discussion and Structure of this Paper

2. **Section II** of this paper sets out certain matters raised by respondents to ED-315² that have not yet been discussed with the Board as follows:
 - Public sector considerations (see paragraphs 16–17);
 - Automated tools and techniques (see paragraphs 18–22);
 - Translations (see paragraphs 23–26); and
 - Effective date (see paragraphs 27–29).
 - Any changes for the matters set out in these paragraphs are included in Agenda Items 2A to 2D.
3. **Section III** of this paper explains the proposed changes made to the requirements, definitions, application material and appendices since the June 2019 IAASB meeting. The proposed changes have been presented as follows:
 - (a) The **requirements** have been revised to address individual issues and concerns raised in the June 2019 Board meeting (see paragraphs 33–35 of this paper). **Agenda Item 2-A** sets out a mark-up to the version that the Board previously received in June 2019 (including revisions made during that week).

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

² Proposed ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement* (ED-315)

- (b) The **definitions** have been revised to address individual issues and concerns raised in the June 2019 Board meeting (see paragraphs 36–39 of this paper). **Agenda Item 2-B** sets out a mark-up to the version that the Board previously received in June 2019 (including revisions made during that week).
- (c) The **application material** has been revised to reflect the specific changes raised in the June 2019 Board meeting, as well as respondent comments not yet dealt with (see paragraphs 40–50 of this paper). **Agenda Item 2-C** sets out a mark-up to the version that the Board previously received in June 2019.
- (d) The **Appendices** to ISA 315 (Revised) have been changed as explained in paragraph 51 below. **Agenda Item 2-D** sets out the revised Appendices, marked to the version that the Board previously received in June 2019.

The focus of the initial (i.e., Monday) IAASB discussions will be on the marked versions as set out above. However, **Agenda Item 2-E**, a clean version of the full standard, has also been provided. Changes made during the Board meeting will be made to this agenda item, and it is this document that the Board will be asked to vote on.

- 4. With regard to the introductory paragraphs to the standard, paragraphs 11–15 and **Appendix 3** of this Agenda Item provide context.

A listing of the supporting NVivo reports and the corresponding Excel spreadsheets are set out in **Appendix 4** of this Agenda Item, with the NVivo reports and spreadsheets to be presented as **Supplemental Documents to Agenda Item 2**.

- 5. In addition to the standard and this issues paper supporting the changes that have been proposed, the following have also been presented for IAASB discussion:

- (a) Draft implementation guide and related materials (**Agenda Item 2-F**), including:
 - (i) Draft First-Time Implementation Guide; and
 - (ii) Draft Frequently Asked Questions (FAQs).

These documents have been provided to give an indication of the content of the supplemental guidance that will be developed and therefore do not form part of the package of documents being voted on. The guidance will require more work before being finalized, at which time Board input will be sought.

- (b) Conforming Amendments (**Agenda Item 2-I and Supplement**)—revised to address specific comments and issues raised in the August 2019 Board teleconference, and to address consistency changes resulting from ongoing updates to ISA 315 (Revised). The changes are explained in Agenda Item 2-I. In addition, the Supplement to Agenda Item 2-I will present all of the proposed conforming amendments highlighted in Appendix 2 of the Explanatory Memorandum to ED-315 (i.e., those that were considered generally straightforward and not within the ISAs that were presented with ED-315), updated as appropriate. The conforming amendments will be separately voted on.
- (c) Paper for Re-exposure (**Agenda item 2-H**) and Table of Requirements—Extant/ED/Current (**Agenda Item-2-G**)—After a vote on the approval of ISA 315 (Revised), the Task Force will, as applicable, discuss re-exposure. The Task Force will discuss its analysis of the provisions of the due process related to whether an approved ISA needs to be re-exposed and its conclusion

(**Agenda Item 2-H** and **Agenda Item 2-G** set out the analysis and Task Force views on re-exposure).

6. **Section IV** of this paper sets out other matters related to due process.

Approach to the Board Discussion

7. At the September 2019 Board meeting, the Task Force Chair will:

- Walk through the standard in the order of the proposed revised requirements with related definitions and application material.
- Invite any comments on the appendices.
- Invite any comments on the introductory paragraphs.
- Invite any comments about the proposed implementation guidance that has been presented; and
- Ask for views in relation to the conforming and consequential amendments.

The Board will then be asked to vote on the revised standard, and the conforming and consequential amendments (separately).

8. After the vote on the approval of ISA 315 (Revised), the Task Force Chair will, as applicable:

- (a) Ask for overall views about the Task Force's analysis of the provisions of due process related to whether an approved ISA needs to be re-exposed; and
- (b) Ask for overall views on the effective date of the approved ISA 315 (Revised) standard.

Task Force, Its Activities and Outreach

9. The members of the Task Force and its activities and outreach since June 2019 have been noted in **Appendix 1**.

Draft Minutes

10. An extract of the draft minutes of the June 2019 IAASB meeting and August 1st, 2019 IAASB teleconference are set out in **Appendix 2** of this paper and **Agenda Item 2-I**, respectively.

II. Certain Matters Not Discussed Previously With the IAASB

Introductory Paragraphs

Summary of Respondent's Comments (NVivo Report 3A; Excel Summary, tab 3B)

- 11. The majority of the respondents supported the introductory paragraphs, however many of these respondents had further comments or suggestions related to these paragraphs. Two respondents did not support the introductory paragraphs, noting that the paragraphs may confuse, rather than assist, when performing risk assessment procedures, and therefore added no value.
- 12. Those that supported the introductory paragraphs did, however, note that these paragraphs should not substitute the need for understanding the standard. Respondents were also unsure about the authority of the introductory paragraphs and noted that certain concepts were only used in the introductory paragraphs, the definitions and the application material (e.g., spectrum of inherent risk). It was also noted

that there are various inconsistencies in the way certain terms are used in the introductory paragraphs and the standard, and that certain paragraphs were not needed.

13. Respondents made various suggestions for additional material within the introductory paragraphs, including:
- (a) Emphasizing the importance of understanding the entity's business and systems as a basis for the risk assessment procedures.
 - (b) More on the identification and assessment of risk at the financial statement level, in particular clarifying the risk assessment process.
 - (c) Linking to the audit risk model to reinforce the concepts therein.
 - (d) More is needed about the nature and extent of the work to be performed.
 - (e) Relating to the spectrum of inherent risk.

There was also a suggestion to include references to the relevant paragraphs within the standard.

Task Force Views

14. Although there were a number of respondents who were very supportive of the introductory paragraphs, in particular because the paragraphs "told the story" of ISA 315 (Revised), the Task Force has pared these paragraphs down to only reflect relationships with other ISAs and significant overall messages regarding the standard (such as the iterative nature of the standard), which is largely how the other ISAs use these paragraphs. In doing so, the unintended consequences between language that may not be consistent with the language used within the standard, is significantly reduced. However, the Task Force is mindful of the usefulness of these paragraphs and is therefore reluctant to lose the content altogether. Accordingly, the Task Force has used these paragraphs as the basis for the introduction to the First-time Implementation Guide. In doing so, many of the good suggestions for expanding these paragraphs have also been considered for inclusion in the guide. It is intended that this guide be published at the same time as the revised standard and stakeholders using the revised standard would therefore benefit from the explanations included in these paragraphs (see **Agenda Item 2-F**).
15. **Appendix 3** sets out the revised proposed introductory paragraphs to the standard for IAASB consideration.

Considerations Specific to Public Sector (NVivo Report 5A; Excel Summary, tab 5B)

Summary of Respondent's Comments and Task Force Views

16. There was no specific question regarding the separate paragraphs addressing 'Considerations Specific to Public Sector Entities.'
17. Two respondents welcomed the changes that had been made in these paragraphs. Two respondents also suggested that the public sector entity considerations rather be consolidated in an appendix rather than spread throughout the standard. Other matters raised had only been raised by an individual respondent, and therefore the Task Force has agreed on balance to make no further changes to these paragraphs.

Automated Tools and Techniques (NVivo Report 4A; Excel Summary, tab 4B)

18. The feedback from respondents relating to automated tools and techniques broadly supported the approach to the enhanced and focused application material. However, there were respondents, including

one Monitoring Group member who called for more prominence within the standard, including further consideration about adding a new requirement. One respondent did not support the enhanced application material, noting that it did not address certain issues relating to the use of automated tools and techniques.

19. A number of respondents called for more guidance relating to the use of automated tools and techniques during the risk assessment process, including relating to documentation. It was also emphasized that the use of automated tools and techniques is a judgment by the auditor, and the requirements set by the IAASB should be neutral regard to the tools used, and as many smaller firms did not have access to these tools. Respondents also called for more when a procedure performed using an automated tool or technique is used as a risk assessment procedure and a further audit procedure. There were respondents still also called for a definition of automated tools and techniques.

Task Force Views

20. With regard to additional requirements, the Task Force continues to have the view that using automated tools and techniques is the way that a procedure is carried out, and the Board cannot mandate its use (also taking into account that not all practitioners will have access to such tools). The Task Force has therefore continued to include the focused considerations around the use of automated tools and techniques in separate paragraphs, with changes or enhancements to address respondent comments as appropriate.
21. The Task Force has also considered the input of the IAASB's Technology Working Group (TWG) which is the separate group specifically looking into technology related matters. The analysis of comments as summarized above was shared with the TWG, and the TWG have worked with the Task Force in enhancing the paragraphs within the standard where appropriate. However, many of the issues that were raised do not relate to ISA 315 (Revised) specifically, but rather relate more broadly to the use of automated tools and techniques throughout the audit, and are therefore outside of the scope of the ISA 315 (Revised) project. These comments have therefore not been addressed as part of this project, but form part of the remit of the TWG's work.
22. For the purposes of the risk assessment process and the pending approval of ISA 315 (Revised) with its enhancements related to the use of automated tools and techniques, the TWG has developed a draft FAQ that is intended to support the changes made to ISA 315 (Revised) – see **Agenda Item 10** (Agenda Item 10 also sets out the planned work of the TWG going forward, which will incorporate consideration of the issues raised in the respondent's comments but not wholly applicable to ISA 315 (Revised)).

Translations

Summary of Respondent's Comments (NVivo Report 1A; Excel Summary, tab 1B)

23. With regard to question 11(a) in ED-315 relating to translations, respondents who answered this question had the following comments:
 - (a) It was noted that various terms used may create challenges for translation, including the distinction between the terms 'significant' and 'material,' 'more than remote,' 'close to the upper end,' 'spectrum of inherent risk,' and various additional terms that were noted by one respondent.
 - (b) The need to be consistent with the terminology used in other ISAs was emphasized.
 - (c) General caution about using words with a 'similar meaning' in close proximity.

24. In addition, a general point was made that the longer and more complex the standard is, the more difficult it would be to translate.

Task Force Views

25. As the Task Force has proposed revisions to ED-315, it has remained mindful of the issues that have been raised regarding translation and made changes where appropriate (e.g., the term 'widget' has been replaced). However, in some instances, the terms that have been highlighted as causing challenges have been removed (e.g., 'more than remote') and in other instances, the use of the terms is consistent with their current use within the suite of ISAs, so no further changes have been proposed (e.g., the terms 'material' and 'significant').
26. The Task Force has also spent significant time on making the standard less complex and more understandable, and the requirements are now articulated in a more direct, consistent way.

Matter for IAASB Consideration

1. The IAASB is asked to comment on the Task Force's proposals in respect of the public sector, automated tools and techniques, or translations. The IAASB is also asked whether there are any other matters raised by respondent's in relation to these areas that need to be further considered.

Effective Date

Summary of Respondent's Comments (NVivo Report 2A; Excel Summary, tab 2B)

27. Question 11(b) in ED-315 asked for views about a proposed effective date for period commencing on or after 18 months after approval of the final standard. Twenty nine respondents supported the proposal and fifteen respondents did not.
28. Those that did not agree with the proposed timeline highlighted that a more realistic timeline is required for such substantial changes, and more time was needed for translation of the revised standard. Some of these respondents noted timelines of 24–30 months would be more realistic. It was also noted by a few respondents who supported the timeline, that their support was on the basis of suggested simplifications to ED-315 and that, if ISA 315 (Revised) were to remain complex, a longer time period should be considered.

Task Force Views

29. The Task Force continues to have the view that an 18-month implementation period is appropriate to allow sufficient time to prepare for the changes. However, because expected final approval from the Public Interest Oversight Board is expected late in 2019, and in line with historical implementation dates coinciding with a calendar year, the Task Force proposes that the targeted implementation date is periods commencing on or after [December 15, 2021] (which effectively extends the 18-month implementation period). This is later than the time initially indicated within ED-315 (paragraph 14 of ED-315) as more time

has been taken to properly respond to the comments to ED-315 and therefore the expected approval of the standard is later than initially targeted.

Matter for IAASB Consideration

2. The IAASB is asked whether it agrees with the proposed implementation date as noted in paragraph 29 above.

III. Proposed Changes Made to the Requirements, Definitions, Application Material and Appendices

Iterative Nature of the Standard

30. There have been ongoing concerns expressed about the order of the requirements, as there are interdependencies between certain requirements, such that the execution of certain requirements that are presented earlier in the standard have dependencies upon the execution of other requirements that are presented at a later stage. The Task Force considered whether to change the way that the standard is presented to be more representative of how some of the concepts within the standard interact. However, in doing so, the Task Force felt this created other (unintended) consequences. Therefore, the Task Force continues to have the view that the order that the requirements are presented in, although linear, is still the most effective way, as all requirements for risk identification and assessment are presented in a common section.
31. However, new application material in paragraphs A135f to A135i (in **Agenda Item 2-C**) has been developed to provide context for the iterations that are required. In particular, these explain the iterative nature of:
 - (a) Determining significant classes of transactions, account balances and disclosures, including for the purpose of understanding the entity's information system.
 - (b) Identifying and evaluating controls in the control activities component for which their identification is based on the identification and assessment of risks of material misstatement, which comes later in the standard.
32. The iterative nature of the standard has been highlighted in the introductory paragraphs (see paragraph 30 of this Agenda Item and **Appendix 3**) and will also be emphasized within the first-time implementation guide to accompany the revised standard, with particular emphasis on the matters described in paragraph 14 above. The Task Force will also consider whether an FAQ (one of a series of FAQs about a variety of matters – see Agenda Item 2-F) is needed to explain why controls are not taken into account in the identification of the risks of material misstatement when the auditor plans to take a primarily substantive approach.

Improving Readability and Understandability, and Scalability (Agenda Item 2-A)

33. The Task Force further considered the Board's comments regarding the modified approach to the presentation of specific requirements in tables, which was intended to further clarify the nature and extent required for understanding the entity and its environment, and the applicable financial reporting framework, and the components of the entity's system of internal control. Changes were made to:
 - (a) Revise the lead-in, as appropriate, to ringfence the required understanding to the information "relevant to the preparation of the financial statements" (as this concept had been lost and

concern had been raised that an understanding broader than intended may be interpreted to be required). The Task Force also considered whether to include the ‘boundary’ within the definition of the system of internal control but had the view that this boundary was better placed within the requirements themselves;

- (b) Clarify that the understanding is to be obtained by ‘performing risk assessment procedures,’ and
- (c) Explain in the application material that the various ‘evaluations’ of the components of the system of internal control are in the context of the ‘understanding’ of the specific matters required to be understood for each component, and not to the extent that would be required to support a ‘separate opinion’ on the component of the system of internal control. In addition, various changes have been made to the text of the requirements relating to obtaining an understanding of each component, for consistency between the requirements for each component, where appropriate. For example, to ensure that scalability is explicitly addressed in the requirements to evaluate each of the indirect components of internal control, “appropriate in the circumstances considering the nature and circumstances of the entity” has been added to the requirements for those components where it had not yet been made explicit.

Other Specific Changes to the Requirements (Agenda Item 2-A)

34. Other substantial changes made to the requirements include changes to:

- (a) Paragraph 17—to rearticulate the auditor’s considerations in relation to corroborating and contradictory information to clarify that the scope of this requirement is evidence that is corroborative or contradictory to management’s assertions. The Task Force also reconsidered whether this hanging paragraph is needed (as some Board members had expressed a view that it was not needed), but the Task Force continued to feel strongly that this addition would further enhance the robustness of the standard and therefore should be kept. This enhancement is also in line with similar concepts in ISA 540 (Revised).³
- (b) Paragraph 18(a)—the explicit requirement to include inquiries of ‘individuals within the internal audit function’ has been reinstated. Although implicit within the requirement, the Task Force recognized the concerns of those Board members who had the view that it appeared the standard had been weakened by the removal of the explicit requirement, and therefore reinstated this.
- (c) Inherent risk factors (paragraphs 23 and 48)—the Task Force reconsidered how reference to the inherent risk factors, in the requirement to obtain an understanding of the entity and the applicable financial reporting framework, has been articulated, to address some concerns expressed about potential inconsistency between the articulation in the requirement and the definition of inherent risk factors. Accordingly, paragraph 23 has been revised to replace “How events and conditions are subject to, or affected by, the inherent risk factors” with “the inherent risk factors that affect susceptibility to misstatement of assertions, and how they do so.” This revision replaces “events and conditions” in the requirement, with “inherent risk factors” (i.e., as defined, “**the characteristics of** events or conditions ...”). A corresponding revision has also been made to the requirement for assessing inherent risk (paragraph 48), which now requires the auditor to take into account how, and the degree to which, inherent risk factors

³ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

affect the susceptibility to misstatement of relevant assertions. The Task Force is of the view that these clarifications will also assist practitioners in understanding how the inherent risk factors are applied at the different stages of the risk assessment process.

- (d) Paragraph 31A(b)—moved the requirement relating to understanding the sources of information used in the entity's process to monitor the system of internal control into the 'table' for the overall requirement for understanding the entity's process to monitor the system of internal control as it is, in the view of the Task Force, an integral part of the understanding of the component to be obtained.
 - (e) Paragraph 39(a)(ii)—rearticulated the requirement to identify controls in the control activities component because of where the assessments of the related risks of material misstatement fall on the spectrum of inherent risk, to better reflect the nature of the controls required to be understood. The Task Force continues to have the view that the purpose of identifying these controls is to assist the auditor with designing better-informed further audit procedures in accordance with ISA 330, that are responsive to risks that fall higher on the spectrum of inherent risk. In rearticulating this requirement, the Task Force described them in the context of the auditor's determination of 'significant risks', with the intention to capture those risks that are assessed higher on the spectrum of inherent risk because of the influence of the inherent risk factors and which therefore may be "close calls" in determining significant risks. In the same way that significant risks are determined using judgment, it is intended that these 'other' risks are also determined using judgment. In addition, because of the way that these controls are now articulated, i.e., that they address risks for which there is a reasonable possibility that they could be significant risks but which were determined not to be significant risks, this category of controls has been reordered to be presented directly after controls related to significant risks.
 - (f) A new heading has been inserted above paragraph 45 to make it clearer that paragraphs 45 and 46 relate to the *identification* of the risks of material misstatement.
 - (g) Paragraph 51—the requirement to assess control risk has been rearticulated to explain more directly how control risk is assessed when the auditor does not plan to test the operating effectiveness of controls. This change better facilitates the statements made in ISA 200 and ISA 540 (Revised) that the auditor separately assesses inherent risk and control risk, but it also makes clear that the assessment of control risk would only change the auditor's assessment of the risk of material misstatement if the auditor plans to test the operating effectiveness of controls.
 - (h) Paragraph 54(c)—in further considering the specific documentation requirements, the Task Force believed there may be merit in explicitly requiring the design and implementation (D&I) of controls in the control activities component to be documented because of the importance of these procedures in determining further audit procedures.
 - (i) Paragraph 54(d)—the Task Force has also enhanced the requirement relating to the documentation of assessed risks of material misstatement to include documentation for risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence for completeness of the requirements.
35. With regard to the *identification of the risks of material misstatement* in accordance with paragraph 45 and the threshold for identification discussed in proposed conforming amendments to ISA 200 (in

essence, before taking account of controls), continued concerns have been expressed by IAASB members about the use of the term ‘risk of material misstatement’ and the possible confusion it may cause because the risk of material misstatement at the assertion level includes both inherent risk and control risk components. The Task Force has further considered the concerns raised, and continues to have the view that no further changes are needed:

- Explanation of the identification of risks of material misstatement has been included in the proposed conforming amendments to ISA 200 (see **Agenda Item 2-I**) and reiterated in paragraph A208a of ISA 315 (Revised) (i.e., in identifying risks of material misstatement, the auditor considers those misstatements that could (i.e., have a reasonable possibility to: (a) occur (i.e., its likelihood), and (b) be material if they were to occur (i.e., its magnitude). The Task Force is also proposing that a FAQ be developed to provide further supporting explanation.
- The risks identified are representative of ‘what can go wrong,’ and are not actual risks of material misstatement until they are assessed in paragraphs 48 and 51. However, they are referred to as risks of material misstatement in paragraph 45 as this is part of the process for which the outcome will be assessed risks of material misstatement.
- The auditor is required to separately assess inherent risk and control risk (control risk is not identified), which together comprise the assessed risk of material misstatement.

Proposed Changes to the Definitions and Its Related Application Material (Agenda Item 2-B and Paragraphs A1–A10 of Agenda Item 2-C))

Assertions

36. A concern has continued to be raised about the potential for confusion in the definition of assertions as used by the auditor (“representations ... with respect to ... information in the financial statements, inherent in management representing that the financial statements are prepared in accordance with the applicable financial reporting framework”). The concern expressed was that, because the definition refers to “management representing”, it could be read as referring to representations actually made by management in the financial statements or to detailed representations in the financial statements that would be valid when the applicable financial reporting framework has been properly applied in preparing the financial statements. Rather the definition is intended to be read as the categories of such assertions used by the auditor. Application material had been added in paragraphs A1–A2 to clarify that there is a difference. The Task Force considered whether it is necessary to provide further explanation, but has agreed, on balance, to propose no further changes noting that this has not been widely raised.

Controls

37. Proposed changes to the definition and its related application material include:
- (a) To add the description of ‘direct and indirect controls’ into paragraph A4a of the application material because the definition of ‘control activities’ was deleted at the March 2019 IAASB meeting and this aspect of the prior application material to control activities was thought useful to be retained.
 - (b) To remove extraneous words about controls being embedded in the components from the definition and instead to describe this in paragraph A2a of application material.

Relevant Assertions

38. The definition of relevant assertions has been updated to be consistent with the way that the assessment of control risk has been articulated (i.e., whether the auditor plans to take into account the operating effectiveness of controls).

Definitions Related to Information Technology (IT)

39. In relation to the new definitions related to IT:
- (a) General IT controls—clarifying early in the definition that these are controls over the entity's IT processes.
 - (b) Information processing controls—simplifying the definition to focus on the role of these controls in addressing risks to the integrity of information in the information system. Further explanation about the nature of these controls has been moved and included in A4b, including to describe these controls in relation to the entity's policies that define the information system.
 - (c) Risks rising from the use of IT—clarifying the defined term to include *the use of* and adding clarification of the meaning of 'integrity of information.'

Proposed Changes to the Application Material (Agenda Item 2-C)

40. In light of the changes that have been made to the requirements, Board comments from the June 2019 IAASB meeting, and the need to further consider how the application material could be made more understandable and clear, the Task Force has made substantial changes to the application material, in particular moving paragraphs within the application material to reflect the revised flow of the requirements. In doing so, the Task Force remained mindful of the Board's broad support for the revised presentation of the application material and has further considered whether any further changes in presentation are required (for example, changes were made to address comments that various aspects of the application guidance were examples and therefore should be in a separate box). The hierarchy of heading levels has also been reconsidered.
41. The Task Force also reconsidered the 'why' paragraphs in light of Board comments that some of these appeared redundant, and concern that they had been articulated in the present tense in many instances. Although some of the paragraphs may appear obvious, they have been retained where the Task Force is still of the view that the paragraphs are helpful in the context of the particular aspect of a requirement. However, some, such as paragraphs A11a and A11b in the June 2019 agenda papers, have been deleted as the Task Force agreed that they were not of value.
42. The Task Force also considered whether there were any additional 'why' paragraphs needed. With the exception of a few new 'why' paragraphs, the Task Force had the view that, on balance, those paragraphs that were most helpful were already in the standard and that the addition of further paragraphs that may be viewed to be 'obvious' may lengthen the standard without added benefit. Examples of new 'why' paragraphs include; paragraph A135a relating to why the auditor obtains an understanding of the sources of information used in the entity's process to monitor the system of internal control and paragraph A239a about why the auditor needs to evaluate audit evidence from risk assessment procedures. However, there were also a few paragraphs already within the application material that explained a 'why' but were not labeled as such, and therefore, where this was the case, these paragraphs have been recharacterized as a 'why' paragraph.

43. With regard to the concern about the use of present tense, the Task Force believes that the new ‘why’ paragraphs do not (and are not intended to) create new obligations and are largely written in the context of existing requirements (i.e., matters of fact). The Task Force has reviewed these to make sure that they are consistent with the current articulation of the requirements. Accordingly, no further changes are proposed with regard to the use of present tense within these paragraphs, but explicit reference to these paragraphs has been added to ISA 200 as part of the conforming amendments to explain their purpose (see **Agenda Item 2-D**).
44. Changes have also been made to the application material for the changes discussed during the June Board meeting (i.e., for the turnaround document), as only the revised requirements and definitions were presented to the Board for discussion at the end of the week (see Updated Agenda Item 2-F from the June 2019 IAASB meeting). For example, the definition of ‘control activities’ was deleted, therefore in **Agenda Item 2-C** any related application material has now either been deleted, or aspects that are still relevant have been relocated. In addition, the application material paragraphs relating to the spectrum of inherent risk (paragraphs A221a–A225) have also been updated to reflect the update made in describing the assessment of inherent risk in the context of determining significant risks. In addition, it has been made clear that when referring to a point on the spectrum of inherent risk, that this is referring to the assessment of inherent risk.
45. Changes made to specific aspects of the application material that are more substantial include:
- (a) Paragraph A10—has been updated to conform to the articulation of how likelihood and magnitude are considered.
 - (b) Paragraph A35—clarified that “inquiry alone is not enough” as a risk assessment procedure to address concerns that this was still unclear in the standard.
 - (c) Paragraph A89—the broad requirement for the auditor to obtain an understanding of the entity’s system of internal control has been removed in the new approach to presenting the understanding for each of the components of the entity’s system of internal control (previously was an explicit requirement). However, even under the new proposed approach the requirement is still implicitly there, and paragraph A89 has been added to make clear that the understanding of the *system of internal control* is obtained by understanding each of the components.
 - (d) Paragraph A200c—the requirement to determine whether one or more control deficiencies have been identified (paragraph 43) no longer makes the link to determining whether these are significant deficiencies. In the view of the Task Force, the determination of significant deficiencies is already covered by ISA 265,⁴ however, application material has been added to remind auditors of this requirement.
46. The revised tabular presentation of the requirements to obtain an understanding of each of the components of the entity’s system of internal control has highlighted the two aspects of the requirement, the specific matters required to be understood and the required evaluation(s) of aspects of the component, in the context of the nature and circumstance of the entity. Supporting application material to further explain the nature of the evaluations has been added (see paragraphs A110a, A119a and A135c)

⁴ ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

47. The Task Force has also focused on the flow of the paragraphs supporting the information system and control activities components, in particular to better explain the nature of the controls required to be identified and why these controls are identified.
48. With regard to IT:
 - (a) Changes have been made in paragraph A144b and A179a to also include considerations about direct access to data, based on input from the IT specialist with whom the Task Force has been working.
 - (b) Clarifying in paragraph A235a that the auditor's further audit procedures may need to include substantive procedures to address risks arising from the use of IT when such risks are not effectively addressed through planned tests of operating effectiveness of controls.
49. With regard to documentation, similar to application material within ISA 540 (Revised), the Task Force has added guidance as to more specific matters that the auditor may consider when considering what to document in relation to professional skepticism (see paragraph A248).
50. The Task Force has also made changes throughout for consistency, and to avoid introducing terms that may cause confusion or have unintended consequences (for example, the way that risks on the spectrum of inherent risk have been described and the use of the term 'higher').

Appendices

51. Changes have been made in the Appendices, as needed for consistency with changes that have been made to terms and how they are described or explained in the requirements, definitions and application material (for example, changes have been made in Appendix 2 relating to the inherent risk factors and the way that fraud has been incorporated therein). In addition, other more substantial changes include:
 - (a) Cybersecurity—although a current issue, the lack of application material related to cybersecurity continues to be raised. However, the Task Force continue to have the view that the existing material remains appropriate, and have not made further changes within the application material as doing so could date the application material in the near future. However, paragraph 19 of Appendix 5 (see **Agenda Item 2-D**) now expands on the concept of cybersecurity.
 - (b) Emerging Technologies—For the same reasons as in (a) above, emerging technologies have not been addressed within the application material, but Appendix 5 has been enhanced to recognize the emerging technologies (see paragraph 5) (**Agenda Item 2-D**).
 - (c) The examples of general IT controls in Appendix 6 have been enhanced and presented in a table to help with understanding when they may, or may not, apply in different circumstances.

Matters Where No Further Changes Have Been Proposed

52. The Task Force considered various matters noted, and has reflected on the most appropriate way forward. The Task Force considered the following matters and concluded that no further changes within the standard were appropriate:
 - (a) Significant risk—and whether the application material should address why risks at the financial statement level are generally not a significant risk. In the view of the Task Force, significant risks relate to inherent risk, which is identified and assessed only at the assertion level.

However, the Task Force does recognize that a risk that exists at the financial statement level, which is identified after consideration of controls may need an overall response and could therefore be considered “significant”. However, the Task Force does not propose to address this in the application material, as doing so could cause confusion in the context of the definition of a significant risk, but instead proposes to develop a separate FAQ to address this.

- (b) Risks of material misstatement that the entity’s risk assessment process failed to identify (paragraph 30 in Agenda Item 2-A)—it was suggested that this requirement be incorporated with the other matters required to be understood in relation to the entity’s risk assessment process (i.e., within the table). The Task Force considered this, but have the view that it is not only the information understood from the auditor’s understanding of the entity’s risk assessment process that will drive the auditor’s considerations, and has therefore left this as a separate requirement in paragraph 31 of **Agenda Item 2-A**.
- (c) Considering whether a control has been designed ‘effectively’ (paragraph 39(d) in **Agenda Item 2-A**)—concern was expressed that the concept of the ‘*effectiveness of controls*’ falls within the scope of ISA 330,⁵ and not ISA 315 (Revised), and therefore that consideration should be given to using a different word, such as “appropriate.” The Task Force considered whether a change was needed but as this concept is from extant and it is related to the “design” of the control and not its operating effectiveness, the Task Force agreed that no further change be made.

Other Relevant Matters

- 53. The Task Force has continued to discuss the ‘threshold’ when identifying the risks of material misstatement, which form the basis for the determination of the relevant assertions, and how to appropriately reflect this in the standards. This matter is further discussed in **Agenda Item 2-I** (Conforming Amendments).
- 54. Proposals for activities supporting the implementation of the revised standard once it is published can be found in **Agenda Item 2-F**.

Matters for IAASB Consideration

- 3. The IAASB is asked for its views on the revised requirements, definitions, application material and appendices.

IV. Due Process Matters

Significant Matters Identified by the Task Force

- 55. In the Task Force’s view, the significant matters it has identified as a result of its deliberations since the beginning of this project, and its conclusions and recommendations thereon, have been reflected in the agenda material presented to the IAASB at its meetings. In the Task Force’s view, there are no significant matters discussed in the course of this project that have not been brought to the IAASB’s attention.

Consideration of the Need for Re-Exposure

- 56. The Task Force considered whether re-exposure is needed and believes, based on the draft that is presented to the Board for the September 2019 meeting, that it is not. **Agenda Item 2-H** presents the

⁵ ISA 330, *The Auditor’s Responses to Assessed Risks*

Task Force's analysis of the provisions of due process related to whether an approved ISA needs to be re-exposed and its conclusion, along with other background material that may assist the Board in coming to a view on re-exposure. **Agenda Item 2-G** shows a comparison of Agenda Item 2-A with the requirements of ED-315 the requirements of extant ISA 315 (Revised).

Appendix 1

ISA 315 Task Force and Details of Meetings & Outreach

The following sets out the activities of the Task Force, including outreach with others and coordination with other IAASB Task Forces and Working Groups relating to the ISA 315 (Revised) project, since June 2019.

Task Force Members

1. The Task Force consists of the following members:
 - Fiona Campbell – Chair (supported by Denise Weber)
 - Karin French
 - Marek Grabowski (supported by Josephine Jackson)
 - Susan Jones
 - Kai Morten Hagen

Further information about the project can be found [here](#).

Task Force Activities since the June 2019 IAASB Discussion

2. The ISA 315 Task Force has met once in person and held 3 videoconferences since the last IAASB discussion in June 2019.

Outreach

3. Fiona Campbell provided an update to the Small and Medium Practices Committee (SMPC) meeting in June 2019. The new drafting approach was presented and matters related to scalability of the requirements and application materials were discussed.
4. Fiona Campbell provided an IAASB update by teleconference to the IAASB's Consultative Advisory Group (CAG) in July 2019. The presentation included the new drafting approach, to address the CAG's concerns with the length, complexity and understandability of the standard.
5. Fiona Campbell provided an IAASB update to representatives from the International Forum of Independent Audit Regulators (IFIAR) Standards Coordination Working Group meeting in July 2019. The presentation included the new drafting approach, with specific reference to matters that were raised by IFIAR and how the IAASB intended to address (or has addressed) such matters.

Appendix 2

Extract From Draft IAASB Minutes – June 2019⁶

ISA 315 (Revised)

BACKGROUND

Ms. Campbell presented the issues paper (**Agenda Item 2**) and walked through a full version of the standard, including the application material (**Agenda Item 2–F**), which was prepared using the ‘drafting approach’ that was agreed to by the Board at the March 2019 IAASB meeting (at its meeting in March 2019, the Board noted that a full version of the standard was necessary to fully assess or evaluate the consequences of such approach).

OVERALL REACTIONS TO THE DRAFTING APPROACH

The Board broadly supported the overall redrafting of the standard, as presented in **Agenda Item 2–F**, and in particular regarding the efforts to:

- Make the standard more understandable (and easier to read, in particular the shorter, more focused requirements);
- Enhance the application material, noting that the introduction of the “why” was very helpful, as well as separately signposting the examples, the scalability and automated tools and techniques paragraphs; and
- Enhance and revise the appendices.

Notwithstanding the support for the broader changes, Board members expressed concern with the way that some of the new definitions had been presented, specifically noting that there may be challenges in navigating efficiently through the standard when considering related matters or material, in particular for non-native English speakers. Although it was recognized that technology may be a solution to improve navigation, the Board agreed that this would unlikely be an achievable solution considering the stage of completion of the project. In addition, some Board members expressed concern about the authority of the new definitions, noting that this may have unintended consequences, as key criteria would now be excluded from the ‘requirements’ section of the standard and may not be seen to form an integral part of the requirement as intended. Concern was also expressed about the way that some of these new definitions were articulated, in particular the introduction of ‘relevant aspects’ to be understood.

Concern was also expressed that the flow of the standard still made it complex to understand, and the ISA 315 Task Force were encouraged to further consider the flow, as well as how the standard could be shortened (although some Board members noted that the standard should be as long as it needs to be).

With regard to the application material:

- One Board member expressed concern that some of the ‘why’s’ were obvious and therefore were not needed.
- Comments were raised about some of the specific examples, while there were also concerns expressed about how some of the examples were relevant today but may ‘date’ the standard.

⁶ Draft minutes are still subject to IAASB review and may therefore still change

In considering revisions⁷ (**Agenda Item 2–F Updated**) to ‘reconnect’ the definitions to the requirements, the Board generally supported the reincorporation of the matters moved to definitions back into the body of the requirement, and also, in particular, the revised presentation in a 2-column table. It was highlighted that this presentation made it clearer what was required to be understood in relation to each component of the system of internal control (i.e., that certain matters were required to be understood and, where relevant, evaluated in context of that understanding).

In progressing the finalization and presentation of the requirements, the Board agreed to the further development and implementation of this approach by the Task Force.

In relation to the new aspects of the presentation of the application material, the Board agreed to the principles and approach taken as set out in **Agenda Item 2–C**, but asked the Task Force to further consider the use of present tense in places.

It was also recognized by the Board that the new drafting approach to ISA 315 (Revised) would need to be considered for other standards being revised, and maybe the ISAs more broadly, but that this was not part of the ISA 315 (Revised) project and should therefore not hold up the approval of ISA 315 (Revised) in any way.

DEFINITIONS

One Board member expressed concern about how some aspects of requirements would be documented in light of the changes to the definitions. In addition, the Board:

- Continued to express mixed views whether or how to include ‘*fraud*’ into the definition of the inherent risk factors. On balance, the Board supported a proposal to specifically include a reference to the ‘*fraud risk factors*⁸ insofar as they affect inherent risk.’
- Requested the ISA 315 Task Force to further consider the following aspects of the definition of ‘*assertions*:’
 - How this definition distinguishes between assertions used in preparing the financial statements made by management and the assertions used by the auditor.
 - Aligning the application material (assertions used as a tool by auditors) with the proposed definition (assertions that are used in context of the applicable financial reporting framework).

RISK ASSESSMENT PROCEDURES

Although broadly supportive of the proposals, the Task Force was asked to further consider:

- The enhancement to paragraph 17 that requires the auditor to perform risk assessment procedures that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory. Some Board members questioned why there was a focus on ‘*bias*,’ noting that the scope should be broader and include, for example, the overall mindset of the auditor. A few Board members, however, did not agree with this addition for this stage of the risk assessment process.
- Whether it is appropriate to move the extant requirement in relation to inquiries with internal audit to the application material, recognizing that application material is non-authoritative.

⁷ The revised proposals focused on changes mainly in relation to the understanding of the system of internal control

⁸ ISA 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraphs A24–A27

UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT AND THE APPLICABLE FINANCIAL REPORTING FRAMEWORK

Although the Board supported the presentation of this requirement in the new 2-column drafting format (as set out in **Agenda 2–F Updated**), it was questioned whether the proposed lead-in was appropriate for both columns. In addition:

- A Board member questioned whether risks are affected by the inherent risk factors rather than ‘*events and conditions*,’ while another Board member encouraged the ISA 315 Task Force to consider which aspects of the understanding are affected by the inherent risk factors and to make that clear in the requirement.
- It was agreed to re-instate the wording ‘*perform risk assessment procedures*’ in the lead-in to this requirement, as it provides appropriate context on how to obtain the overall understanding. For consistency purposes, it was agreed to also include this wording when obtaining the understanding of each component of the system of internal control.

UNDERSTANDING THE ENTITY’S SYSTEM OF INTERNAL CONTROL

In addition to the comments about the revised presentation for the auditor’s understanding of the system of internal control, the Board also asked the Task Force to further consider:

- Clarifying the meaning of what an ‘*appropriate*’ understanding is in the context of the entity’s risk assessment process and the entity’s process to monitor the system of internal control. In doing so, the Board agreed that it may be helpful to reintroduce the wording ‘*to the entity’s circumstances considering the nature and size of the entity*’ (as included in ED–315).
- In the control activities component, the wording of the requirement to identify controls to meet the objectives in paragraph 17(a) and 17(b)(i.e., paragraph 39(c)), as concern continued to be expressed about how this aspect of the requirement may be interpreted. Although generally supportive of the application material, some Board members expressed concern that the wording included in the requirement of ‘*controls that are necessary*’ may be interpreted too widely and does not reconcile with the guidance included in the application material (which was noted to be clearer than the requirement as to what these controls may be).
- The wording used to describe the scope of the understanding of the information system (‘*policies that define significant classes of transactions, account balances and disclosures*’), as this may be interpreted as a ‘deep dive’ understanding that may go beyond the intended required understanding.
- Specific aspects of the requirement to evaluate the design of a control and determining whether it has been implemented (D&I procedures):
 - One Board member questioned whether the use of the term ‘*effectively*’ is appropriate in the context of evaluating whether a control is ‘*designed effectively*’ (paragraph 42(a)). The concern was expressed that the concept of the ‘*effectiveness of controls*’ falls within the scope of ISA 330,⁹ and not ISA 315 (Revised). The Board member suggested that it may be more appropriate to use the word ‘*appropriately*.’
 - Whether ‘*inquiry*’ is always required in addition to other procedures.

⁹ ISA 330, *The Auditor’s Responses to Assessed Risks*

IDENTIFYING AND ASSESSING THE RISKS OF MATERIAL MISSTATEMENT

To better align the definition of a significant risk to its related application material, the Board supported a revision to the definition that emphasizes that the auditor considers the **combination** of magnitude and likelihood in determining whether an identified risk of material misstatement is a significant risk.

In progressing other proposed changes, the Board requested that the Task Force further consider:

- How to describe and distinguish the ‘threshold’ when *identifying* a risk of material misstatement (in ISA 200,¹⁰ proposed paragraph A15a). Some Board members also continued to express concern about the explicit use of the term ‘*reasonable possibility*’ in the proposed new paragraph. In addition, it was questioned whether the material related to the ‘threshold’ should rather be located in ISA 315 (Revised) rather than ISA 200.
- How to better incorporate the consideration of the inherent risk factors in the requirement to assess inherent risk at the assertion level, as there may be circularity.
- How the iterative nature of the standard is emphasized upfront. Although there is a recognition that the standard is not a linear process, Board members noted the need for more prominent explanatory material, including in the introductory paragraphs and the ‘Basis for Conclusions’ document.
- Clarifying in the application material that if there is no intent or requirement to test the operating effectiveness of controls, and the auditor chooses not to test the operating effectiveness of controls, that this decision or course of action in itself represents an ‘implicit’ assessment of control risk.

Board members also expressed concern about the interaction of the definition of significant risk and the requirement to determine significant risks, noting that it was still not clear where on the spectrum of inherent risk an identified risk may be determined to be a significant risk. The ISA 315 Task Force revised the definition of significant risk (**Agenda Item 2-F Updated**) to more clearly articulate that it was the *combination* of the likelihood of a misstatement and the magnitude of that misstatement that would help the auditor determine whether an identified risk is a significant risk.

DOCUMENTATION

The Board supported the proposed changes to the documentation requirements.

APPENDICES

Subject to minor editorial suggestions, the Board expressed their general support for the appendices as included in **Agenda Item 2-D**.

GUIDANCE

The Board expressed its support for the Task Force’s initial views about the development of implementation guidance relating to ISA 315 (Revised), as set out in **Agenda Item 2-E**. The Board strongly supported the revised flowchart, with some Board members continuing to encourage consideration of adding the flowchart to the standard.

¹⁰ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

IAASB CAG CHAIR REMARKS

Mr. Dalkin noted the CAG's continuing support for the proposals, with particular reference to the efforts by the Task Force to address overarching concerns in relation to the length and complexity of the standard.

PIOB REMARKS

Subject to the inclusion of all needed requirements, Prof. van Hulle expressed strong support for the new drafting approach as agreed to by the Board. Prof. van Hulle further encouraged the Task Force to introduce the term 'scalability' explicitly within the body of the requirements. However, recognizing that the requirements are intended to be principles-based, the Task Force Chair cautioned that this term may be better described within the introductory paragraphs. In considering the definition of the inherent risk factors, Prof. van Hulle supported the proposed revision which explicitly refers to the consideration of '*the fraud risk factors insofar as they affect inherent risk.*'

WAY FORWARD

The ISA 315 Task Force will work towards finalizing the standard for approval at the September 2019 IAASB meeting, including the final proposed conforming and consequential amendments. The Task Force will also develop draft guidance to accompany the standard for the Board's consideration. The ISA 315 Task Force will undertake specific outreach with International Forum of Independent Audit Regulators (IFIAR) Standards Coordination Working Group and the CAG, recognizing the expected approval of the final standard in September 2019.

The Task Force will present conforming and consequential amendments, based on the changes to ISA 315 (Revised) already discussed with the Board at the March and June 2019 IAASB meetings at a Board teleconference in August 2019. Other conforming amendments arising from new changes to ISA 315 (Revised) to respond to Board comments from June 2019 will be presented for discussion at the September 2019 IAASB meeting.

Draft Introductory Paragraphs

[Presented as a mark-up to introductory paragraphs in ED-315]

Introduction

Scope of this ISA

1. ...

Key Concepts in this ISA

2. ISA 200 deals with the overall objectives of the auditor in conducting an audit of the financial statements,¹¹ including to obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level.¹² Audit risk is a function of the risks of material misstatement and detection risk.¹³ ISA 200 explains that the risks of material misstatement may exist at two levels:¹⁴¹⁵ the overall financial statement level; and the assertion level for classes of transactions, account balances and disclosures.
3. ISA 200 ~~further~~ requires the auditor to exercise professional judgment in planning and performing an audit, and to plan and perform an audit with professional skepticism recognizing that circumstances may exist that cause the financial statements to be materially misstated.¹⁶
- 4.3. Risks at the financial statement level relate pervasively to the financial statements as a whole and potentially affect many assertions. Risks of material misstatement at the assertion level consist of two components, inherent and control risk:
 - Inherent risk is described as the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
 - Control risk is described as the risk that a misstatement that could occur in an assertion about a class of transactions, 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 controls.
4. ~~The required understanding of the entity and the environment, the applicable financial reporting framework, and the system of internal control forms the basis for the auditor's identification of risks~~

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

¹² ISA 200, paragraph 17

¹³ ISA 200, paragraphs 13(c)

¹⁴ ISA 200, paragraphs 13(e) and 13(n)

¹⁵ ISA 200, paragraph A36

¹⁶ ISA 200, paragraphs 15–16

~~of material misstatement. The identification of risks of material misstatement at the assertion level is performed before consideration of any controls. The auditor does so based on a preliminary assessment of inherent risk that involves identifying those risks for which there is a reasonable possibility of material misstatement. In this ISA the assertions to which such risks of material misstatement relate are referred to as ‘relevant assertions,’ and the classes of transactions, account balances and disclosures to which the relevant assertions relate are referred to as ‘significant classes of transactions, account balances and disclosures.’~~

5. ISA 330 requires the auditor to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.¹⁷ ISA 330 further explains that the auditor’s assessment of the risks of material misstatement at the financial statement level, and the auditor’s overall responses, is affected by the auditor’s understanding of the control environment. ISA 330 also requires the auditor to design and perform further audit procedures whose nature, timing and extent are based on and responsive to the assessed risks of material misstatement at the assertion level.¹⁸
6. Risks of material misstatement identified and assessed by the auditor include both those due to error and those due to fraud. Although both are addressed by this ISA, the significance of fraud is such that further requirements and guidance are included in ISA 240¹⁹ 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. ISA 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.²⁰ For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk and control risk is required by this ISA. ~~The auditor assesses the inherent risk by assessing the likelihood and magnitude of material misstatement, and by taking into account inherent risk factors. Inherent risk factors individually or in combination increase inherent risk to varying degrees.~~ As explained in ISA 200, inherent risk is higher for some assertions and related classes of transactions, account balances and disclosures than for others. The degree to which inherent risk varies, is referred to in this ISA as the ‘spectrum of inherent risk.’
86. The auditor’s risk identification and assessment process is iterative and dynamic. The auditor’s understanding of the entity and its environment, the applicable financial reporting framework, and the entity’s system of internal control are interdependent with concepts within the requirements to identify and assess the risks of material misstatement. In obtaining the understanding required by this ISA, initial expectations may be developed, which may be further refined as the auditor progresses through the risk identification and assessment process. In addition, ~~t~~This ISA requires the auditor to revise the risk assessments and modify further overall responses, and further audit procedures, based on audit evidence obtained from performing further audit procedures in accordance with ISA 330, or if new information is obtained. In assessing control risk, the auditor takes into account whether the auditor’s further audit procedures contemplate planned reliance on the operating effectiveness of controls (that is, control risk is assessed as less than maximum). The auditor’s understanding of the

¹⁷ ISA 330, *The Auditor’s Responses to Assessed Risks*, paragraph 5

¹⁸ ISA 330, paragraph 6

¹⁹ ISA 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*

²⁰ ISA 200, [paragraph A43a] (*conforming amendment*) and ISA 330, paragraph 6

~~system of internal control forms the basis for the auditor's intentions about whether to place reliance on the operating effectiveness of controls. That is, the auditor may identify specific controls that address the identified risks of material misstatement and for which the auditor intends to test operating effectiveness. If the auditor does not intend to test the operating effectiveness of controls related to certain identified risks of material misstatement,, the auditor's assessment of control risk cannot be reduced for the effective operation of controls with respect to the particular assertion (that is, control risk is assessed at maximum).~~

- ~~7. The auditor's assessment of the risks of material misstatement at the assertion level is based on the auditor's assessments of inherent risk and control risk at the assertion level. The auditor designs and performs further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement at the assertion level. The auditor also identifies and assesses the risks of material misstatement at the financial statement level in accordance with this ISA in order to design and implement overall responses to address such risks.~~
- ~~8. Risks of material misstatement identified and assessed by the auditor include both those due to error and those due to fraud. Although both are addressed by this ISA, the significance of fraud is such that further requirements and guidance are included in ISA 240 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.~~

The iterative nature of the auditor's risk assessment process

- ~~9. The auditor's risk assessment process is iterative and dynamic. The auditor develops initial expectations about the potential risks of material misstatement and the potential significant classes of transactions, account balances and disclosures based on the auditor's understanding of the entity and its environment and the applicable financial reporting framework. The auditor's understanding of the system of the internal control, and in particular the information system component, provides further information to assist the auditor in developing those expectations.~~
- ~~10. After identifying the risks of material misstatement, the auditor determines the significant classes of transactions, account balances and disclosures. The auditor is also required to perform a stand-back to confirm that this identification is appropriate.~~
- ~~11. The auditor's process of assessing the identified risks of material misstatement at the assertion level also results in the auditor's determination of any significant risks and risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence.~~
- ~~12. This ISA requires 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, or if new information is obtained.~~

Scalability

- ~~1310.~~ ISA 200 states that the some ISAs include scalability considerations specific to smaller entities within the application and explanatory material which illustrate the application of the requirements to entities whose nature and circumstances are less complex, as well as those that are more complex.²¹ This ISA is intended for audits of all entities, regardless of size or complexity and. However, the application material of this ISA therefore incorporates specific considerations specific to both audits of smaller

²¹ ISA 200, paragraphs tbc

~~entities when such entities are also less and more complex entities where appropriate. Accordingly, in this context, this ISA refers to 'smaller and less complex entities.'~~ 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. ~~Some of the considerations however may be useful in audits of larger and less complex entities.~~

Appendix 4

| Description | Question # in Explanatory Memorandum | NVivo Word Report Reference | Excel Summary Sheet Reference |
|--------------------------------|--------------------------------------|-----------------------------|-------------------------------|
| Introductory paragraphs | 1(c) | 3A | 3B |
| Public Sector | N/A | 5A | 5B |
| Translations | 11(a) | 1A | 1B |
| Effective Date | 11(b) | 2A | 2B |
| Automated Tools and Techniques | 3 | 4A | 4B |