Supplement J
to Agenda Item 9

RESPONSES RECEIVED ON THE EXPOSURE DRAFT

PROPOSED INTERNATIONAL STANDARD ON AUDITING 540 (REVISED), *AUDITING ACCOUNTING ESTIMATES AND RELATED DISCLOSURES*

DRAFTING COMMENTS

Note: This supplement has been prepared for information only. A comprehensive summary of the significant comments received on the April 2017 Exposure Draft, Proposed International Standard on Auditing 540 (Revised), *Auditing Accounting Estimates and Related Disclosures* (ED-540) and related analyses of significant issues will be presented at subsequent IAASB meetings. All comment letters on the Exposure Draft can be accessed here.

#	Respondent	Comments
Regulators and Oversight Authorities		
1.	IRBA	**Editorial comments** 1. Editorial changes recommended below are denoted as ~~strike through~~ for words that should be deleted and underlined for words that should be inserted.

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
1	This International Standard on Auditing (ISA) deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements. Specifically, it expands on how ISA 230, ISA 315 (Revised), ISA 330, ISA 500 and other relevant ISAs are to be applied in relation to accounting estimates. It also includes requirements and guidance on misstatements of individual accounting estimates, and indicators of possible management bias.	Since the lack of preparation of sufficient audit documentation is a key inspection finding in South Africa[1], ISA 230 should be identified as one of the auditing standards that ISA 540 (Revised) expands on. This will assist auditors with keeping the documentation requirements "front-of-mind" when auditing accounting estimates. In addition, please refer to our comments on documentation in paragraph 34(a) above.

[1] IRBA Public Inspections Report 2015 and Public Inspections Report 2016.

		4	This ISA focuses the auditor's attention on designing and performing further audit procedures relating to accounting estimates (including, where appropriate, tests of controls) responsive to the reasons for the assessment given to the assessed risks of material misstatement, particularly when those reasons include complexity, judgment or estimation uncertainty. This ISA also recognizes that the factors of complexity, judgment or estimation uncertainty are interrelated and that there are inherent limitations in reducing estimation uncertainty beyond certain limits.	It is necessary to focus the auditor's attention on accounting estimates.
		Footnote 25	ISA 315 (Revised), paragraphs 5–6 and 11–12.	The footnote reference to ISA 315 (Revised) should also include paragraph 12 of ISA 315 (Revised).
		17	In complying with paragraph 15(b), when the reasons for the assessment given to the risk of material misstatement include complexity related to management's use of a complex method (including complex modelling), or when management's method otherwise involves the use of specialized skills or knowledge [FN], the auditor shall obtain sufficient appropriate audit evidence about the following matters: (Ref: Para A101–A104)	A footnote (FN) reference to ISA 500, paragraph 8, should be made. Please refer to our response to questions 4(c), paragraph 23 above.
		21	The auditor shall obtain sufficient appropriate audit evidence about whether the disclosures related to accounting estimates are reasonable in the context of the requirements of the applicable financial reporting framework including: (Ref: Para. A2, A135–A138) **Key Concepts** (Ref: Para. 6, 21, 23)	Paragraph 21 should include a reference to application material paragraph A2 and vice versa.
		27	The audit documentation shall include: (a) The auditor's professional judgments on the basis for the auditor's evaluation of the reasonableness of the accounting estimates and related disclosures in the context of the applicable financial reporting framework; and (b) Indicators of possible management bias, if any, and	Please refer to our comments on documentation in paragraphs 32-37 above.

			the auditor's evaluation thereof in forming the auditor's opinion on whether the financial statements as a whole are materially misstated. (Ref: Para. ~~A158–~~A159)
		27A (Previously paragraph A158)	Paragraph 8 of ISA 230 requires the auditor to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand, among other things, significant professional judgments. The audit documentation of the auditor's professional judgment shall include: (a) The auditor's judgments about the assessed risk of material misstatement related to accounting estimates, and the auditor's response; (b) Procedures performed to address matters in paragraphs 17-21, including the auditor's judgment about management's selection of methods, significant data and significant assumptions; (c) The overall evaluation required by paragraphs 22-23; and (d) Communications with those charged with governance and management. ~~In the context of auditing accounting estimates, these professional judgments include the basis for the auditor's evaluation of whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework. The auditor's judgments are likely to be supported by the documentation of the procedures performed to address the matters in paragraphs 17–21 including the auditor's judgment about management's selection of methods, significant data, and significant assumptions, as well as the overall evaluation required by paragraphs 22–23, of this ISA. In addition, the auditor's judgments about the assessed risk of material misstatement related to accounting estimates, and the auditor's~~

			~~response, may likely be further supported by documentation of communications with those charged with governance and management, particularly for accounting estimates for which the assessed risk of material misstatement is based on inherent risk that is not low.~~	
		Footnote 35	See also ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 13(c) and 39(b)(iii).	The footnote reference to ISA 700 (Revised) should also include paragraph 39(b)(iii) of ISA 700 (Revised).
		A10 A158A	Considerations Specific to Smaller Entities ISA 315 (Revised) notes that smaller entities may use less structured means and simpler processes and procedures to achieve their objectives. Further, for entities that have simple businesses, processes relevant to financial reporting may also be uncomplicated, including as they relate to accounting estimates. In those situations, the extent of the understanding of the matters in paragraph 10 is likely influenced by the extent to which these matters are relevant to the entity (for example the entity may be subject to few, if any, regulatory factors or specialized skills or knowledge may not have been applied in making the accounting estimates). Obtaining this understanding may be primarily achieved through inquiries from management with appropriate responsibilities for the financial statements. Considerations Specific to Smaller Entities ISA 315 (Revised) ~~also~~ notes that the manner in which the auditor's understanding of the entity and its environment are documented is for the auditor to determine using professional judgment. For example, in audits of small entities the documentation may be incorporated in the auditor's documentation of the overall strategy and audit plan. For entities that have simple businesses and processes relevant to financial reporting, the auditor's documentation may be simple in	Paragraph A10 should be included as a paragraph that is headed "Considerations Specific to Smaller Entities". This will provide more prominence to considerations that are specific for smaller entities. In addition, the last three sentences of paragraph A10 should be moved to the application material on documentation as paragraph A158A.

			form and relatively brief.	
		A24	The preparation of the financial statements also requires management to establish financial reporting processes for making accounting estimates, including adequate internal control. Such processes include the following: • Selecting appropriate accounting policies and prescribing estimation processes, including appropriate estimation or valuation methods, ~~including~~ and, where applicable, models. • Developing or identifying relevant data and assumptions that are used in making accounting estimates. • Periodically reviewing the circumstances that give rise to the accounting estimates and re-estimating as necessary.	This edit is proposed to avoid using the word "including" twice in one bullet.
		A29	A model is complex when: • The method it applies requires specialized skills or knowledge; • Relevant and reliable data needed for use in the model is difficult to obtain; • The integrity of the data is difficult to maintain; • It exhibits a significant degree of ~~complexity~~ [real-time processing or flexibility to make use of real-time economic data or data analytics to predict the future] in its design or operation, which may, for example, involve more extensive use of information technology or large volumes of data; or • It uses multiple data sources or assumptions with complex-interrelationships.	We noted that the word "complexity" is used to define a "model that is complex". One of the three suggested wordings should be used to replace the word "complexity".
		Footnote 44	ISA 315 (Revised) paragraph ~~A52, A56, A57, A88, A93, A95, A101, A102 and A108~~ A53, A57-A58, A85-A87, A89, A96, A98, A105-A106 and A112	The footnote references to ISA 315 (Revised) should be updated.
		A95	Paragraph ~~A40~~A42 of ISA 200 states that the ISAs do	The reference to ISA 200 should be updated.

			not ordinarily refer to inherent risk and control risk separately. However, the auditor may make separate or combined assessments of inherent and control risk. Although this ISA neither implies nor requires a separate assessment of inherent and control risk, it highlights the importance of the auditor's consideration of both inherent and control risk in designing and performing further audit procedures to respond to the assessed risks of material misstatement, including significant risks, at the assertion level in accordance with ISA 330.	
		A105 (heading above)	Understanding or Interpreting Significant Data (Ref: Para. 17(c))	It is necessary to insert the word "significant" in the heading.
		A107 A107A	Audit evidence regarding management's selection of methods and significant data and significant assumptions may be obtained from inquiries of management regarding management's continuing processes of strategic analysis and risk management and inspection of relevant documents (such as committee minutes). Considerations Specific to Smaller Entities Even without formal established processes, such as may be the case in smaller entities, the auditor may be able to evaluate the significant data and significant assumptions through inquiries of, and discussions with, management, along with other audit procedures in order to obtain sufficient appropriate audit evidence.	We believe that the last sentence of paragraph A107 should be included as a separate paragraph and be headed "Considerations Specific to Smaller Entities". This will provide more prominence to considerations that are specific for smaller entities. In addition, it is necessary to insert the word "significant".
		Appendix 2, paragraph 8	Complexity in making accounting estimates arises when there are multiple valuation attributes and multiple or non-linear relationships between them. Management may require specialized skills or knowledge that may, for example, be needed in relation to:	It is necessary to insert the word "that".

National Auditing Standard Setters		
2.	IDW	Comments by Paragraph Title The proposed title and the existing title both refer to “auditing accounting estimates…”. A number of standards had similar titles using the term “audit of” or “auditing” in the past, but these titles were changed over the years to reflect the fact that, in line with ISA 200.11 (a), the objective of an audit is “…To obtain reasonable assurance that the financial statements as a whole are free from material misstatement” [underlining added for emphasis]. When auditing financial statements, auditors do not give an opinion on accounting estimates individually – that would be a separate engagement under ISA 805. In line with a number of other standards (e.g. “Related Parties”, “Subsequent Events”, etc.) we therefore suggest that the title be changed to “Accounting Estimates and Related Disclosures” or “Special Audit Considerations Relating to Accounting Estimates and Related Disclosures”. 1. Upon close examination, the first sentence of the standard does not appropriately describe the scope of the standard because the standard does NOT deal with all of an auditor’s responsibilities relating to accounting estimates and related disclosures in an audit of financial statements. Rather, the standard deals only with the audit consideration of measurement issues in relation to accounting estimates. Furthermore, the standard only deals with the audit consideration of issues relating to recognition and disclosure of accounting estimates to the extent that these relate to measurement issues. The standard does not deal with the audit consideration of issues concerning the recognition, classification, presentation or disclosure of accounting estimates that are not related to measurement issues: for these issues, ISAs 315 and 330 etc. would apply. We recognize that what makes accounting estimates special are the measurement issues associated with estimation uncertainty and the related recognition and disclosure issues, but the other audit considerations are important too. The way this first sentence is written, it suggests that these other considerations need not be dealt with beyond what the standard addresses, which is not the case. We therefore suggest that the first sentence be changed to read “… relating to the measurement of accounting estimates and making related disclosures. This matter about referring to “measurement” might need to be put through many of the sentences in the rest of the standard. To show this impact, we have only provided examples hereof in the introduction and objective section in our comments on the following paragraphs. The second sentence claims that “it” (we presume “it” means the standard) “expands on” how ISA 315, ISA 330, ISA 500 and other relevant ISAs are to be applied in relation to accounting estimates. If this statement is true, this statement is of concern to us because indicates a drastic change in how IAASB engagement standards are written. Pursuant to ISA 200.18, an auditor shall comply with all of the ISAs relevant to the audit. If ISA 540 expands on how all of the relevant ISAs are to be applied, then this would imply that the standard ought to expand upon all of the requirements of these standards. While the draft standard is long, it certainly does not expand on all of these requirements, nor should it. Rather, the standard seeks to deal with the special considerations related to the measurement of accounting estimates and related disclosures when applying these other ISAs. For these reasons, we suggest that the second sentence read as follows: “This standard deals with the special considerations on how ISA 315 … and other relevant ISAs are to be applied in relation to the measurement of accounting estimates and making related disclosures.” One of the matters the IAASB might need to consider is whether some of the requirements in the standard do in fact “expand” on the requirements in these other standards, rather than dealing with just the special considerations as noted, and that perhaps some rationalization of the requirements might be applicable.

		2. In line with our comments on paragraph 1 and the content of the first three sentences of paragraph 2, the third sentence should be changed to read "The extent to which the measurement of accounting estimates and making related disclosures are subject to …". 3. In line with our comments on the first two paragraphs, the first sentence should be changed to read "When an accounting estimate is being measured and related disclosures are being made, the susceptibility of this measurement and related disclosures to misstatement may increase …". 4. In line with our comments on the first two paragraphs, the following should be inserted near the end of the first sentence: "… assessed risk of material misstatement in relation to measurement and related disclosures, …" The word "in" in the last sentence should be changed to "to". 5. In line with our comments on the first two paragraphs, the first sentence should be changed to read "… relating to the measurement of accounting estimates and making related disclosures". Likewise the second sentence should be changed to read "… affecting the measurement of accounting estimates and related disclosures …". 6. In line with our comments on the first two paragraphs, the first sentence should read "This ISA requires an evaluation of the measurement, and related disclosures, of accounting estimates …". Likewise, the second sentence would read "… required to evaluate whether the measurement, and related disclosures, of accounting estimates are reasonable ….". 8. In line with our comments on the first two paragraphs, the objective in (a) should read "The measurement of accounting estimates, … ". 9. (a) We are concerned with the definition of an accounting estimate, which determines the scope of ISA 540 and when this standard is required to be applied. We would like to point out that with the possible exception of cash in local currency and share capital at par and the like, almost every other monetary item disclosed in the financial statements is an estimate of some sort. Even many assets purchased at cost are subject to estimation uncertainty because, for example, decisions are made about which costs are allocated to product costs or costs of acquisition and issues about impairment or depreciation or amortization involve judgment and hence estimation uncertainty. Some estimation uncertainty also applies to the valuation of simple liabilities (the decision whether to discount at all, for example, and if so, at what rate). The issue is whether the estimate is subject to significant estimation uncertainty – that is, whether it is worth it to consider such estimation uncertainty at all when preparing and auditing financial statements given materiality considerations. It would be disproportionate to require the application of the standard as currently drafted – even with the response to low inherent risk as contemplated in paragraphs 10 and 15 (a) – to all of these estimates because there would be hardly any monetary item in the financial statements to which this standard would not apply. We recognize that some application material would need to be developed so that the word "significant" is not subject to abuse such that estimates with considerable estimation uncertainty are then nefariously scoped out of the standard. However, such application material can be developed to hinder this. For this reason, we believe that the definition of accounting estimate should refer to "significant" estimation uncertainty. We also have a number of technical concerns with the definition of accounting estimate. We note that the definition of estimation uncertainty refers to the inherent lack of precision in measurement. Consequently, the words "the measurement of which" currently included in the definition of accounting estimate together with the definition of estimation uncertainty would lead to the meaning "the measurement of which is subject to the susceptibility of an accounting estimate to an inherent lack of precision in its measurement". Some of the wording is therefore redundant. We therefore suggest deleting the words "the measurement of which". In addition, the positioning of the words "prepared in accordance with the requirements of the applicable financial reporting framework" suggests that the monetary amount is prepared in accordance with the financial reporting framework, which is in fact the determination that needs to be made in the audit. What is meant is that estimation uncertainty arises when the monetary amount is prepared in accordance with the requirements of the applicable financial reporting framework.

		Based on these reasons, we believe that the definition of accounting estimate should read as follows: "A monetary amount subject to significant estimation uncertainty when that amount is prepared in accordance with the requirements of the applicable financial reporting framework." (c) The definition of estimation uncertainty refers to "accounting estimate", which is circular when the definition of accounting estimate then also includes the term "estimation uncertainty". This issue can be resolved by not having the definition refer to "accounting". Furthermore, the phrase "lack of precision in its measurement" is awkward. We therefore suggest that the definition read as follows: A12. Footnote 39 reflects a substantive point that generally ought to be taken up in the text of the application material under the Clarity Conventions. A14. The paragraph could be understood as suggesting that auditors have a duty to regulators in relation to regulatory requirements for accounting estimates even when these regulatory requirements do not affect the financial statements and there are no legal or regulatory requirements for the auditor of the financial statements to deal with such regulatory requirements for accounting estimates. Consequently, more clarification is needed in this paragraph that these regulatory matters are relevant to the auditor only if they have an impact on the measurement of accounting estimates or making related disclosures in the financial statements. A18. The use of the word "requires" in the first sentence suggests that the IAASB is setting requirements for management preparation of the financial statements. We suggest changing the word "requires" to "involves" (and then changing "determine" to "determining") so that the sentence represents a statement of fact. A26. As a matter of principle, definitions that have a significant impact on the work effort of auditors ought to be placed in the definitions section of the ISAs and not be relegated to the application material. This applies to the definition of "method" in this paragraph, but also applies to the definition of " model" in paragraph A27, and in particular to the definition of a "complex model" in paragraph A29. If the IAASB does not want to include these as formal definitions in the definitions section, then an additional paragraph can be added to the definitions section with more informal descriptions (see, for example, paragraph 5 in ISA 210, paragraph 8 in ISA 580, or paragraph 10 in ISA 600). A27. See comments in comments to A26. A28. See comments in comments to A26. A29. See comments in comments to A26. A35. As a matter of principle, definitions that have a significant impact on the work effort of auditors ought to be placed in the definitions section of the ISAs and not be relegated to the application material. This applies in particular to the definition of "significant data and significant assumptions", which has a central role in determining when and how certain requirements apply. . If the IAASB does not want to include these as formal definitions in the definitions section, then an additional paragraph can be added to the definitions section with more informal descriptions (see, for example, paragraph 5 in ISA 210, paragraph 8 in ISA 580, or paragraph 10 in ISA 600). A82. Data sources are not "reliable" as noted at the beginning of the first bullet – the data that the sources provide is or is not reliable. This is clarified in the next sentence. We therefore suggest that the words be changed to "The reliability of data from different sources".
3.	JICPA	• Paragraph 17 There seems to be inconsistency between paragraphs 13 (a) and 17. At the beginning of paragraph 17 "management's use of a complex method" and "when management's method otherwise involves the use of specialized skills or knowledge" are referred to as factors of complexity. In addition to those two factors, paragraph 13(a) includes "the difficulty, if any, in obtaining relevant and reliable data and maintaining the integrity of that data" as a factor of complexity (paragraph 13(a)(ii)). We propose to simplify the structure of paragraph 17 like that of paragraph 18 or 19 as follows:

		"In complying with paragraph 15(b), when the reasons for the assessment given to the risk of material misstatement include complexity in making the accounting estimate~~related to management's use of a complex method (including complex modelling), or when management's method otherwise involves the use of specialized skills or knowledge, the auditor shall obtain sufficient appropriate audit evidence about the following matters~~:…" • The fourth bullet of paragraph A73 We propose to delete the clause "that is active in different markets". An expected credit loss model in a financial institution uses various assumptions and data from various information sources. Therefore, inherent risk is usually not low even if the financial institution only operates in one jurisdiction. If the board decides to retain the clause, we propose to change it to "that operates in different markets" to be simple to understand; As the word "active" is often used as an adjective that illustrates the market conditions, it is hard to understand what it means when used as an adjective to "the financial institution" in this bullet. • Other paragraphs that need simplification and clarification The following paragraphs are complex and the points are difficult to understand. We believe that use of more plain and simple wording is helpful: - Paragraph 3: We understand paragraph 3 intends to provide explanation relating to the descriptions of the three factors in paragraph 13. However, some of the descriptions in the two paragraphs seem to be inconsistent, particularly those on estimation uncertainty (paragraph 3(c) and 13(c)). As paragraph 4 refers to laying emphasis on the three factors in identifying and assessing risks of material misstatement and designing and performing further audit procedures, we consider that paragraph 3 is not necessary and that it should be deleted. - Paragraph A144: The word "amounts" is used several times. However, it is not clear whether "amounts" means "management amounts" or "auditor's amounts". Also, the fifth sentence uses the phrase "the amounts identified or supported". The difference between what "identified" and "supported" mean is not clear. - Appendix 1, paragraph 23: The last sentence seems to repeat the same points as in the previous sentences and the intended meaning of this sentence is not clear. - Appendix 2, the fourth bullet of paragraph 14: It is not clear what the phrase "relative likelihood" means. - Appendix 2, paragraph 20: Overall, sentences are long and difficult to understand. We propose the following simplification: "In other cases, it may be necessary to consider information about past conditions and events, together with current trends and expectations about future developments. Past conditions and events provide historical information from which repeating historical

		patterns of behavior relating to uncertain valuation attributes may be discerned and extrapolated in evaluating future outcomes. Such historical information may also indicate changing patterns of such behavior over time (cycles or trends)~~. These~~, or may suggest that the underlying historical patterns of behavior have been changing in somewhat predictable ways ~~that may also be extrapolated in evaluating future outcomes~~. ~~Other types of information may also be available that indicate possible changes in historical patterns of such behavior or in related cycles or trends~~. Difficult judgments may be needed about the predictive value of such information.”
Accounting Firms		
4.	BDO	Other Comments We propose the following amendments to ED-540 for consideration: • The use of ‘they’ in paragraph 2 could refer to either management or the estimate. We recommend amending the use of ‘they’ to either management or the estimate as appropriate. • Paragraph 2 refers to the three factors of complexity, judgment and estimation uncertainty which are not specifically defined as such until paragraph 3. We recommend improving the linkage of the three factors mentioned in paragraph 2 with paragraph 3 to provide clarity for the reader. • Paragraph 6 includes an implicit requirement to evaluate the reasonableness of accounting estimates and related disclosures in accordance with the applicable financial reporting framework. We recommend that this requirement be made explicit. • Paragraph A2 in the application and other explanatory material section lists three requirements and two other considerations relating to making the assessment of reasonableness with respect to the accounting estimate. We propose that these other considerations be aligned to the wording used in ISA 240 The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements, specifically paragraph 240.32(b)(i) relating to ‘free from bias’, such as: ‘The data and assumptions used in making the accounting estimates are free from bias and are consistent with each other and with those used in other accounting estimates or areas of the entity’s business activities.’ The second item in other considerations should also be consistent with paragraph 240.A39 relating to ‘understanding the entity’, such as: ‘The accounting estimate takes into account appropriate information, including understanding the entity, as required by the applicable financial reporting framework.’ • Paragraph A10 uses the terms ‘smaller entities’ and ‘small entities’. We recommend the use of only one of these terms to ensure greater consistency of interpretation. • For paragraphs A12 and A13, we recommend adding ‘applicable’ prior to ‘financial reporting frameworks’. • It would be helpful for the ED-540 basis of conclusions to highlight the difference between assessing disclosures for adequacy (see existing ISA 540 objective paragraph) versus reasonableness in order to clarify that there has been a change in emphasis and work effort.

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• Where it is clearly apparent that an accounting estimate is low risk, that ED-540 considers a means of making this conclusion without performing all the steps listed in paragraphs 10(a) to 10(f).
• Paragraphs 25, A153 and A154 list additional representations to be obtained from management relating to accounting estimates which seem to transfer some of the auditor’s responsibilities to management. We recommend that the representations relate more to management’s responsibilities under the applicable financial reporting framework concerning the accounting estimates in the financial statements.
• ED-540 paragraph 19(a)(i) requires the auditor to ‘obtain sufficient appropriate audit evidence about whether, in the context of the applicable financial reporting framework, management has taken appropriate steps to understand and address the estimation uncertainty, and develop a point estimate that meets the measurement objective’ . We are of the view that it may be more appropriate to use the term ‘consider’ or ‘evaluate’ rather than ‘to obtain sufficient appropriate audit evidence’, as it is difficult to envisage how, in practice, the auditor can obtain sufficient appropriate audit evidence that management has understood the estimation uncertainty.
• ED-540 paragraph 15(a)(i) states ‘[o]btaining audit evidence about events occurring up to the date of the auditor’s report’ . This appears to be a broad procedure on subsequent events. We propose to retain the wording in extant ISA 540 paragraph 13(a) which is better phrased in the context of accounting estimates, that is ‘Determine whether events occurring up to the date of the auditor’s report provide audit evidence regarding the accounting estimate.’
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<h2>APPENDIX II</h2>
<h2>EDITORIAL COMMENTS AND OTHER RECOMMENDATIONS</h2>
DTTL has editorial comments and other recommendations with respect to ED-540 as set forth below. Certain of the proposed editorial comments and other recommendations may not be applicable depending on the outcome of the overall deliberations of the IAASB, as well as the response of the Board to the matters discussed in the cover letter and Appendix I. In these comments, recommended additional text is shown using <u>bold underline</u>; recommended deletions to the text are shown using double <s>strikethrough</s>.
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<tr><th>ISA-540
Paragraph Number</th><th>Editorial Comments and Other Recommendations</th></tr>
<tr><td>2</td><td>Amend wording to reflect that estimation uncertainty is actually defined – see paragraph 9(a) of ED-540.
Many financial statement items are susceptible to an inherent lack of precision in their measurement, which is <s>referred to</s> <u>defined</u> as estimation uncertainty. In the ISAs, such</td></tr>
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			financial statement items are referred to as accounting estimates….
		3(a)(ii)	Clarify the wording as currently drafted. Appropriately consider the relevance and reliability of the data used, **regardless of** whether the data is obtained from internal sources or from external information sources.
		4	Clarify the wording as currently drafted, and eliminate duplication of sentences and phrases. This ISA focuses the auditor's attention on designing and performing further audit procedures (including, where appropriate, tests of controls) responsive to the reasons for the assessment given to the **identified and** assessed risks of material misstatement, particularly when those reasons include complexity, **use of** judgment **by management,** or estimation uncertainty. ~~This ISA also recognizes that the factors of complexity, judgment or estimation uncertainty are interrelated and that there are inherent limitations in reducing estimation uncertainty beyond certain limits.~~
		5	Redraft paragraph for additional clarity and deletion of words/phrases that are repeated. The application of professional skepticism by the auditor is particularly important to the auditor's work relating to accounting estimates~~. Professional skepticism also is important because there is a particular~~ **as there is the** risk of management bias affecting accounting estimates due to their subjective, potentially complex and uncertain nature.
		6	Delete last sentence as the paragraph is merely re-stating the objective. This ISA requires an evaluation of accounting estimates based on the audit procedures performed and the audit evidence obtained. ~~In doing so, the auditor is required to evaluate whether the accounting estimates, and related disclosures, are reasonable in the context of the applicable financial reporting framework.~~
		9(f) A58 A138	The phrase "underlying transaction(s)" is used in the definition relating to "Outcome of an accounting estimate." Throughout ED-540 "transactions" is used without the "underlying" qualifier (except in two other instances – see paragraphs A58 and A138 of ED-540). Consideration should be given to deleting the word "underlying" in paragraphs 9(f), A58 and A138 of ED-540, so as to be consistent with how the phrase is used elsewhere in the proposed standard, for example, paragraphs 10(d), A18, A22, and ISA 260 (Revised) Appendix 2 – Accounting Estimates of ED-540. 9(f). Outcome of an accounting estimate – The actual monetary amount that results from the resolution of the ~~underlying~~ transaction(s), event(s) or condition(s) addressed by an accounting estimate. A58. The segregation of duties between those committing the entity to the ~~underlying~~ transactions and those responsible for making the accounting estimates,

			including whether the assignment of responsibilities appropriately takes account of the nature of the entity and its products or services. For example, in the case of a large financial institution, relevant segregation of duties may consist of an independent function responsible for estimation and validation of fair value pricing of the entity's financial products staffed by individuals whose remuneration is not tied to such products. A138. When the financial statements are prepared in accordance with a fair presentation framework, the auditor's evaluation as to whether the financial statements achieve fair presentation include the consideration of 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.
		10(a)	The objective in paragraph 8 of ED-540 only refers to the "related disclosures," yet in paragraph 10(a) of ED-540 there is a reference to "related presentation and disclosure requirements." Consistency is recommended throughout ED-540 where disclosures are mentioned. The requirements of the applicable financial reporting framework relevant to accounting estimates, including the recognition criteria, measurement bases and the related ~~presentation and~~ disclosure requirements.
		10(d)	The terms "revise" accounting estimates (e.g., paragraphs 10(d) and A21 of ED-540) and "re-estimate" accounting estimates (for example, paragraph A61 and A65 of ED-540) have been used interchangeably. Consistency is recommended throughout the proposed standard. Terms to be addressed also include "re-estimating," "re-estimation" and "re-estimated"
		10(e)(i)	Paragraph A30 of ED-540 discusses that management may design and implement specific controls around models used for making accounting estimates, yet there is no reference to control activities in the related requirement. Additionally, Paragraph 12 of Extant 540 discusses whether the method for making the accounting estimates have been applied consistently, however this concept is not as clear in ED 540. Recommend additional wording be added to paragraph 10(e)(i) of ED-540 to address these issues and emphasize the importance of controls and achieve consistency with the application material. The methods used, how they are selected or designed, and how they are applied **including the consistency of their application**, including the extent to which they involve modelling**, and the related control activities, as applicable**;
		10(e)(iii)	This is the first instance of the use "significant data" in the requirements, yet there is no cross-reference to the related guidance in paragraph A35 of ED-540

			The process used to select data, including the source(s) of that data and how management identifies significant data; (Ref: Para. **A35,** A39–A42)
		10(e)(v)	Paragraph 3(b)(ii) of ED-540 uses the word "mitigate" for describing management bias. The wording should be aligned with the more commonly used wording in the proposed standard of "addressed" and such wording should be used consistently. (ii) ~~Mitigate~~**Address** the risk of management bias.
		10(e)(vii	DTTL suggests additional clarity in this paragraphs as to the auditor's considerations as to whether or not the outcome of management's process is appropriate or not (e.g., if management decided that no change was necessary, however the auditor decided a change was necessary), as well as the responsibility of the auditor in such a circumstance. Additionally, DTTL believes that the wording in this paragraph should be modified in order to provide clarity as to the meaning, as follows. (vii) How management has addressed the need for a change from the prior period in the methods, assumptions or data used, and if **management has made a change**~~so~~, the nature of, and reasons for, such changes. (Ref: Para. A47).
		10(f)	Additional clarity needed to reflect that this requirement may already have been addressed when complying with ISA 315 (Revised). Each of the components of internal control as they relate to making accounting estimates**, to the extent an understanding of these components of internal control has not already been obtained**.
		11	Recommend additional wording be added to clarify the purpose of the retrospective review. DTTL also notes the change in the use of the word "prior" in extant paragraph 9 of ISA 540 to "previous" in paragraph 11 of ED-540. If there is no underlying reason for this change, DTTL recommends reverting back to the extant terminology to avoid any confusion as to the reason or intent of the change. (Note this editorial comment affects numerous paragraphs throughout the proposed standard) …. The review is not intended to call into question judgments about ~~previous~~ **prior** period accounting estimates that were appropriate based on the information available at the time they were made**, instead the review informs the auditor in applying professional judgment about the validity of the process undertaken by management**.
		13(a)(ii)	The phrase "obtain[ing] relevant and reliable data and maintaining the integrity of that data" used in the requirement should be consistent with the phrase in the related application material (paragraph A82 of ED-540). Further, paragraph 3 of ED-540 highlights "maintain[ing] the integrity of the data used" as a separate bullet, yet in

			paragraphs 13(a)(ii) and A82 of ED-540, it is not a separate sub-bullet. Recommend aligning these three paragraphs. DTTL also recommends that in order to clarify what is meant by "maintaining the integrity of [that] data" an example be added, such as the following: For example; by testing the operating effectiveness of relevant controls within the applicable information technology systems
		17(b)	When referring to relevant and reliable data in paragraph 3(a) of ED-540 as it relates to complexity, there is no reference to "significant" data. It is not clear why the requirement in paragraph 17(b) of ED-540, therefore, refers only to "significant" data. DTTL suggests deleting "significant" as it would be important to obtain audit evidence about the relevance and reliability of data if it gives rise to a risk of material misstatement (regardless of whether it was deemed "significant" data or not). (Refer also to the discussion on "*Data and Assumptions*" in our cover letter). (b) Whether ~~significant~~ data is relevant and reliable.…
		18(a)(iii)	As currently drafted, the requirement to extend the auditors procedures to obtaining sufficient appropriate audit evidence about whether significant assumptions are consistent with assumptions used in other areas of the entity's business activities is very broad and open-ended. DTTL believes that the evidence required to be obtained to address this requirement should be limited to the auditor's knowledge obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit (similar to the requirement in paragraph 14(b) of ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*). Whether significant assumptions are consistent with each other and with those used in other accounting estimates or with assumptions used in other areas of the entity's business activities. **The other areas of the entity's business activities are limited to those areas of which the auditor has knowledge as obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit.**
		19(b)	DTTL believes that it is likely that a control deficiency exists when management has not appropriately understood and addressed estimation uncertainty, and that the requirement therefore needs to be expanded to address the auditor's consideration of control implications. When, based on the audit evidence obtained, in the auditor's judgment, management has not appropriately understood and addressed the estimation uncertainty, the auditor shall, to the extent possible, develop an auditor's point estimate or range to enable the auditor to evaluate the reasonableness of management's point estimate and the related disclosures in the financial statements that describe the estimation uncertainty. **When management has not appropriately understood and addressed the estimation uncertainty, the auditor shall evaluate whether a deficiency in internal control exists, and where**

			appropriate communicate in accordance with ISA 265, Communicating Deficiencies in Internal Control to Those Charged With Governance and Management [Footnote] **[Footnote] Paragraphs 7-11 of ISA 265**
		27	DTTL believes that it would be helpful for additional clarity to be provided in the requirement in paragraph 27 (and the related application material) as to the documentation that would be needed to evidence how the requirements have been addressed, in particular with respect to supporting judgments that inherent risks are low and the requirements of paragraphs 17-21, which DTTL believes should be called out more specifically. DTTL further notes that the documentation requirement should be more closely aligned with paragraphs 8 and 24 of ED-540, as well as the language in paragraph 37(a) of ISA 700 (Revised). The audit documentation shall include: (a) The basis for the auditor's evaluation of the reasonableness of the accounting estimates**, whether recognized or disclosed,** and related disclosures **in the context of the applicable financial reporting framework**; and (b) Indicators of possible management bias, if any, and the auditor's evaluation **of the implications on the audit and** ~~thereof~~ in forming the auditor's opinion **to obtain reasonable assurance about** ~~on~~ whether the financial statements as a whole are **free from** material~~ly~~ misstate~~d~~**ment, whether due to error or fraud**.
		A1	The following matters are noted as it pertains to paragraph A1 of ED-540. (1) Lead-in. Clarify that the estimates are those that are both included or disclosed in the financial statements (2) DTTL believes that "outcome of long term contracts' may not be sufficiently clear and may mean different things; for example does it relate to the percentage of completion used to determine revenue, or does it relate to the need to assess whether a provision is required because a long-term contract is onerous, or is there another meaning? DTTL recommends that this bullet be clarified or additional examples provided to add clarity. (3) Edit to clarify that the financial instruments are those that are both complex and not traded in an active market (4) DTTL recommends striking the words "goodwill and" because goodwill itself is not evaluated, it is a residual balance. (5) DTTL recommends that an example be provided of an "infrastructure asset valuation" as it is not clear what is encompassed by this bullet. In addition, DTTL also suggests that other relevant examples be added to the application

			material; for example situations relating to revenue recognition (e.g., allocation of transaction price to performance) and impairment of long-lived assets. Examples of situations where accounting estimates may be required **to be included or disclosed in the financial statements** include: • …. • Outcome of long term contracts. • ….. • Financial instruments, including complex financial instruments **or those** that are not traded in an active market. • …. • Assets or liabilities acquired in a business combination, including ~~goodwill and~~ intangible assets. • … • Infrastructure asset valuation.
		A4	DTTL recommends that the following edit be made because judgments inform the decisions of management. Accounting estimates are monetary amounts that may be classes of transactions or account balances recognized in the financial statements, but also include accounting estimates used in disclosures or used to make ~~judgments~~ **decisions** about whether or not to recognize or disclose a monetary amount.
		A5	The following edits are proposed: (1) Delete “significant” as it implies that one should only test the assumptions or data if significant, but this may not necessarily be the case, also the phrase that has been used is “significant data or significant assumptions,” with data being noted first. (2) Insert “making” for consistency with similar use of phrases in ED-540. (3) Delete “item” and use “component” for consistency within the paragraph, and to clarify that the approach being referred to relates to developing a point estimate for a component (4) Provide a more relevant example An auditor’s point estimate or range may be developed for an accounting estimate as a whole (for example, the expected credit losses for a particular loan portfolio or the fair value of different types of financial instruments), or a component of an accounting

			estimate (for example, an amount to be used as ~~a significant assumption or significant~~ data **or an assumption** for **making** an accounting estimate). A similar approach may be taken by the auditor in developing an amount or range of amounts in evaluating ~~an item of~~ data or an assumption **of a component of an accounting estimate** (for example, **developing a range of lives to evaluate the entity's determination of the** ~~an~~estimated useful life of an asset).
		A7	The following edits are proposed to the application material: (1) Insertion of a reference to complexity, as DTTL believes that the lack of precision in the measurement of accounting estimates can also lead to complexity (2) Other editorial suggestion. Financial reporting frameworks often call for neutrality, that is, freedom from bias. The inherent lack of precision in the measurement of accounting estimates gives rise to the need for the use of judgment by management**, as well as result in added complexity when measuring the accounting estimate**. Such judgment may be influenced by unintentional or intentional management bias (for example, as a result of motivation to achieve a desired profit target or capital ratio). The susceptibility of an accounting estimate to management bias increases with the extent to which there is a need for judgment in making the accounting estimate. Management bias may be difficult to detect at an account level and may only be identified when considered in **relation to** groups of accounting estimates, all accounting estimates in aggregate, or when observed over a number of accounting periods.
		A11	DTTL recommends, in addition to the editorial suggestions related to punctuation, that the guidance in extant paragraph A13 of ISA 540 be incorporated into the paragraph A11 of ED-540 to improve the context of this guidance. Obtaining an understanding of the requirements of the applicable financial reporting framework provides the auditor with a basis for discussion with management and, where applicable, those charged with governance**,** about how management has applied those requirements relevant to the accounting estimates, and about the auditor's determination of whether they have been applied appropriately. This understanding also may assist the auditor in communicating with those charged with governance when the auditor considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be the most appropriate in the circumstances of the entity. **In addition, obtaining an understanding of the requirements of the applicable financial reporting framework assists the auditor in determining whether it, for example:** • **Prescribes certain criteria for the recognition, or methods for the measurement of accounting estimates.**

			• **Specifies certain criteria that permit or require measurement at a fair value, for example, by referring to management's intentions to carry out certain courses of action with respect to an asset or liability.** • **Specifies required or suggested disclosures.**
		A12	Suggested edits to provide clarity for what "determined directly" means, as this is not a phrase used elsewhere in the ISAs and it will therefore be unfamiliar.. For certain accounting estimates, financial reporting frameworks may prescribe or provide guidance on the basis for selecting management's point estimate, which may be, for example, the most likely outcome or a discounted probability-weighted expected value. Depending on the circumstances, it may be possible for the accounting estimate to be determined directly **(for example, there is only one option or source from which to select or determine the point estimate)** or it may be possible to select a management point estimate only after considering alternative assumptions or the range of possible measurement outcomes.
		A13	DTTL believes that the application material as drafted implies that *assumptions* prescribed by the financial reporting framework always give rise to estimation uncertainty, which DTTL does not believe is accurate. Further, DTTL believes the context of extant paragraph A15 of ISA 540 is not captured in paragraph A13 of ED-540. Suggested edits are noted below (in addition to reformatting the paragraph for further clarity): Financial reporting frameworks may specify criteria for, or guidance on, the disclosure of information concerning ~~judgments,~~ assumptions~~,~~ **and judgments,** or other sources of estimation uncertainty relating to accounting estimates. **Examples where the financial reporting framework requires the disclosure of information include:** • **Significant assumptions to which the accounting estimate is particularly sensitive, or** • **Situations where the financial reporting framework does not permit recognition of an accounting estimate when there is a high degree of estimation uncertainty but instead requires that certain disclosures be made in the notes to the financial statements.**
		A14	Recommendations encompass inserting wording to clarify that (a) regulatory factors include relevant regulatory frameworks, and (b) management bias may occur relating to achieving compliance with regulatory requirements. There are also other editorial suggestions. Obtaining an understanding of the regulatory factors that are relevant to accounting estimates (for example regulations established by banking and insurance regulators) may

			assist the auditor in **, identifying any relevant regulatory framework, and** determining whether the regulatory framework: • Addresses conditions for the recognition, or methods for the measurement, of accounting estimates, or provides related guidance thereon; • Specifies, or provides guidance about, **necessary or expected** disclosures in addition to the requirements of the applicable financial reporting framework; or • Provides an indication of areas for which there may be a potential for management bias **in making accounting estimates in amounts that will result in achieving compliance with** ~~to meet~~ regulatory requirements.
		A15	DTTL recommends that the example be deleted as it is confusing and not necessary in order to understand the application material. Obtaining an understanding of the applicable regulatory factors may also highlight requirements for regulatory purposes that are not consistent with requirements of the applicable financial reporting framework, which may indicate potential risks of material misstatement. ~~For example, for certain financial statement items, the measurement basis for regulatory capital maintenance purposes may require earlier recognition of losses than the measurement basis required by the applicable financial reporting framework.~~
		A16 and A17	DTTL proposes edits to provide further clarity as to what aspects underlying the accounting estimate would need to be understood in order to assist "the auditor in understanding the measurement basis," and "the nature and extent of disclosures." Further, DTTL believes this understanding may only assist the auditor with discussion regarding certain of the accounting estimates. There is also duplication with paragraph A17 of ED-540, and DTTL recommends combining the two guidance paragraphs. An edit has also been proposed in order to more closely align the wording with paragraph 11 of ISA 315 (Revised). Obtaining an understanding of the nature of accounting estimates that the auditor expects to be included in the entity's financial statements**, together with an understanding of the applicable financial reporting framework,** assists the auditor in understanding the measurement basis of such accounting estimates and the nature and extent of disclosures that may be relevant**, as well as an understanding of whether the accounting estimates are complex to make, require significant judgment by management, or have high estimation uncertainty**. Such an understanding provides the auditor with a basis for discussion with management about how management has made **certain of** the accounting estimates. The auditor may obtain an understanding of the accounting estimates that the auditor expects to be included in the financial statements through the auditor's: • Understanding of the nature of the entity, including the nature of the assets and liabilities and other financial statement items that it would be expected to have, given the nature of its operations, ownership and governance structures**,** ~~and~~ **types** of

			investments, the way it is structured and financed, its objectives and strategies and related business risks; • ...
		A19	DTTL believes that management's knowledge of the implementation of business strategies in both *prior* and current periods could be relevant to accounting estimates, accordingly the following edit is recommended. Management's identification of transactions, events and conditions that give rise to the need for accounting estimates is likely to be based on: • ... • Management's knowledge of the implementation of business strategies ~~in the current period~~. • ...
		A20	DTTL recommends that paragraph A20 of ED-540 be deleted because it is repetitive of what is already stated in paragraph 10(d) of ED-540.
		A21	Editorial recommendation to eliminate superfluous wording and improve clarity. Inquiries of management about changes in circumstances ~~may~~ **that may give rise to the need for new or revised accounting estimates** include, for example, whether: • The entity has engaged in new types of transactions ~~that may give rise to accounting estimates~~. • Terms of transactions ~~that give rise to accounting estimates~~ have changed. • Accounting policies relating to accounting estimates have changed, as a result of changes to the requirements of the applicable financial reporting framework ~~or otherwise~~. • Regulatory or other changes outside the control of management have occurred ~~that may require management to revise, or make new, accounting estimates~~. • New conditions or events have occurred ~~that may give rise to the need for new or revised accounting estimates~~.
		A23	As previously discussed (**see response to Question 3 in Appendix I**), the perception given by the heading "Considerations specific to smaller entities" is that smaller entities have estimates with low inherent risk. DTTL acknowledges that the intent is to focus on those less complex entities, many of which happen to be smaller. DTTL recommends that in each instance where there are specific considerations relating to smaller entities, that the lead-in could perhaps be more descriptive, for example, "In

			less complex entities, many of which may be smaller, obtaining ….” This is a repeat comment for the following guidance paragraphs – paragraphs A44, A60, A100, and A110 of ED-540. Additionally edits are recommended to (1) align wording with drafting conventions used in the application material relating to the auditors work effort and related actions and (2) provide additional clarity as to what “accordingly” means. **In less complex entities, many of which may be smaller,** ~~O~~**o**btaining this understanding ~~for smaller entities is often~~ **may be** less ~~complex~~ **complicated** as ~~there are~~ **the nature of the underlying** business activities and transactions **may often be simpler** ~~be less complex~~. Further, often a single person, for example the owner-manager, identifies the need to make the accounting estimates and the auditor’s inquiries may be focused ~~accordingly~~ **toward that person**.
		A24	Editorial suggestions to provide additional clarity and consistency. … • Selecting appropriate accounting policies and prescribing estimation processes, including appropriate estimation or valuation methods, including, where applicable, **the use of** models. • …. • Periodically reviewing the circumstances that give rise to the accounting estimates and re-estimating **the accounting estimate** as necessary.
		A27 and A28	DTTL recommends reordering these paragraphs as paragraph A28 of ED-540 describes what a model is, yet paragraph A27 of ED-540 already refers to a model, namely Black Scholes.
		A29	DTTL recommends that the lead-in be re-worded for additional clarity. In relation to the second and third bullet point of paragraph A29 of ED-540, DTTL noted the usage of the term “difficult.” As this term is relative, DTTL suggest that guidance as to how to assess this criteria will be of benefit to auditors. A model is **more likely to be** complex when: • The method it applies requires specialized skills or knowledge; • Relevant and reliable data needed for use in the model is **more** difficult to obtain; • The integrity of the data is **more** difficult to maintain; • It exhibits a significant degree of complexity in its design or operation, which may, for example, involve more extensive use of information technology or large volumes of data; or

			• It uses multiple data sources or assumptions with **more** complex ~~-~~interrelationships.
		A30	DTTL recommends revising paragraph A30 of ED-540 to provide additional clarity as well as to make other editorial changes. These proposed edits address primarily the following matters: (1) Eliminate redundancies in the sentence addressing complex models, as well as including an example of the need to focus on complex controls. (2) Delete the example pertaining to insurance contract liabilities and instead include an example that is related to the example previously included in the paragraph, namely the expected credit loss model. (3) Factors for the auditor to consider in obtaining an understanding of the model should not be limited to control *activities*, rather all controls are to be considered. (4) Sub-bullets three and four addressing considerations relating to the data and assumptions do not assist with the entity's validation of the model itself, as these are inputs used in the model. Accordingly, the lead-in to the sub-bullets has been amended. (5) Sub-bullet four addresses assumptions; however, DTTL believes that the assessment should address both the assumptions made, and used. An additional sub-bullet has been added to cover this consideration. The sub-bullets have also been re-ordered as management would likely make the assumptions, before using them in the model. (6) The overlays made by management could be subject to management bias. Wording inserted to the application material to remind the auditor of this consideration. (7) It is for the auditor to determine the *key* parameters using professional judgment. In obtaining an understanding the auditor should be evaluating all the parameters documented by the entity. Management may design and implement specific controls around **a** model used for making accounting estimates, whether **such model is** management's own model or an external model. . ~~Controls that address complexity around models are more likely to be relevant to the audit when the model used is complex, such as an expected credit loss model or a model used for the~~ **When the model itself has an increased level of complexity, such as an expected credit loss model, controls that specifically address complexity are likely more relevant to the audit, for example, understanding the controls around the integrity of the calculations when valuing**~~ation of~~ **the fair value of financial assets**~~insurance contract liabilities~~. Factors that may be appropriate for the auditor to consider in obtaining an understanding of the model and of related control**s** ~~activities~~ include the following: • How management determines the relevance and accuracy of the model; • The validation or back testing of the model, including whether the model is validated prior to use and revalidated at regular intervals to determine whether it remains

			suitable for its intended use. The entity's validation of the model**, and the related inputs,** may include evaluation of: o The model's theoretical soundness; o The model's mathematical integrity; o The accuracy and completeness of the data and appropriate assumptions used in the model; ~~and~~ o **Whether** appropriate assumptions have been made**; and** o Whether the appropriate data **and assumptions are** ~~is~~ used in the model; • How the model is appropriately changed or adjusted on a timely basis for changes in market or other conditions and whether there are appropriate change control policies over the model; • Whether adjustments, also referred to as overlays in certain industries, are made to the output of the model ~~and~~ **,**whether such adjustments are appropriate under the circumstances and in accordance with the requirements of the applicable financial reporting framework. **Where the adjustments are inappropriate or not in accordance with the requirements of the applicable financial reporting framework, whether such adjustments are the indicators of possible management bias**; and • Whether the model is adequately documented, including its intended applications, limitations, ~~key~~ parameters, required data and assumptions, the results of any validation performed on it and the nature of, and basis for, any adjustments made to its output.
		A31	Recommended edit provides additional clarity when using an internally developed model in which the output, in this case the accounting estimate, may have a greater susceptibility to material misstatement. When providing an example, DTTL does not believe that referring to [all] internally developed models is appropriate to address the circumstances, rather the example should instead refer to complex models. For example, an internally developed depreciation model for a simple accounting estimate is unlikely to have material misstatement. Estimates may have greater susceptibility to material misstatement relating to the use of models in certain circumstances. For example, in cases when management has developed a **complex** model internally and has relatively little experience in doing so, or uses a model that applies a method that is not established or commonly used in a particular industry or environment.
		A33	It is noted that the application material for *significant assumptions* is included in paragraph A35 of ED-540 which is subsequent to the use of the phrase in this paragraph, therefore DTTL recommends a cross-reference to the related guidance

			paragraph. An additional editorial suggestion is also noted. … • How the assumptions are consistent with other matters **that are**: o … • … • How management identifies significant assumptions **(see paragraph A35)**
		A35	DTTL noted that while the first instance of the terms “significant data” and “significant assumptions” is used in requirement paragraph 10(e)(iii) and 10(e)(ii) of ED-540, respectively, these terms are actually first used in the application material paragraph A5 of ED-540 relating to an example for definition of an auditor’s point estimate or auditor’s point range. DTTL recommends that since the concepts of data and assumptions are fundamental to the ED-540, this paragraph addressing the terms be moved to under the heading “Key Concepts.”
		A36	Certain valuation techniques selected may work in a liquid market, but may not work in an illiquid market, and as such DTTL recommends an edit to convey this understanding as a statement of fact. Further, DTTL believes that it is not clearly understood what is meant by “prices achieved,” and that an example may be appropriate. An editorial suggestion related to punctuation has also been proposed. Some financial reporting frameworks require different accounting treatments depending on the level of activity in the market. Estimation uncertainty increases and valuation is more complex when the markets in which financial instruments**,** or their component parts are traded become inactive. Valuation techniques selected when market information ~~was~~**is** available may not provide appropriate valuations in times of stress. However, even where markets are inactive, prices achieved**, for example the price at which a financial instrument is traded,** may still provide relevant evidence about fair value. …
		A38	DTTL recommends the edits below based on the following observations (1) First bullet. Delete the words “in such circumstances” as the circumstances are already referred to in the lead-in to the paragraph, namely “[w]hen markets are inactive or illiquid.” Delete the second sentence as it has already been encompassed in paragraph A37 of ED-540. (2) Second bullet. (a) Clarifying that the circumstances when the valuation technique is selected refers to both when the model is being adapted or developed. (b) Combine with third bullet.

			(3) Third bullet. Delete and combine the second and third bullets, with a common lead-in. Delete the last sentence related to “sensitivity analysis,” as a sensitivity analysis is not used to determine ranges. (4) Fifth bullet. Delete the words “in such circumstances” as the circumstances are already referred to in the lead-in to the paragraph, namely “[w]hen markets are inactive or illiquid.” When markets are inactive or illiquid, the auditor’s understanding of how management selects assumptions may include understanding whether management has: • Implemented appropriate policies for adapting the application of the method ~~in such circumstances~~. ~~Such adaptation may include making model adjustments or developing new models that are appropriate in the circumstances~~; • Resources with the necessary skills or knowledge to o **A**~~a~~dapt or develop a model, ~~if necessary~~ on an urgent basis **if needed**, including selecting the valuation technique that is appropriate in **both** ~~such~~ circumstances; o Determine the range of outcomes, given the uncertainties involved~~, for example by performing a sensitivity analysis~~; • ~~The resources to determine the range of outcomes, given the uncertainties involved, for example by performing a sensitivity analysis~~ • The means to assess how, when applicable, the deterioration in market conditions has affected the entity’s operations, environment and relevant business risks and the implications for the entity’s accounting estimates, in such circumstances; and • An appropriate understanding of how the price data from particular external information sources may vary ~~in such circumstances~~.
		A39	DTTL notes that a distinction is made in the lead-in between factual data and derived data, yet the examples of data listed do not make a similar distinction. DTTL recommends that the distinction be removed, as it is unnecessary. If the concept is retained, DTTL recommends that the examples be similarly split in order to assist the auditor in identifying the underlying nature of the data.
		A40	Paragraph 13 of ED-540 requires the auditor to identify and assess risks of material misstatements. In doing so the auditor obtains an understanding of the entity and its environment, and in the context of accounting estimates, this includes the process used to select the data, including the sources. To that end DTTL believes it is important to understand the data sources, but not in the context of risks associated with respect to relevance and reliability of the data itself, but rather as it relates to the identification and assessment of risks of material misstatements. Further the relevance and reliability of data is not addressed in paragraph 10(e)(iii) of ED-540. See edits proposed below:

			... Understanding the source of the data used to make the accounting estimates may help the auditor in **<u>identifying and assessing risks of material misstatement.</u>**~~understanding the risks with respect to the relevance and reliability of the data~~.
		A41	One of the matters the auditor may consider in obtaining an understanding of the data relates to the "nature of the data" (refer to the first bullet of paragraph A41 of ED-540). DTTL believes further clarity on what the "nature of the data" actually represents is necessary; for example, internal or external data, factual data, or derived data, developed internally, by management's expert, or is it a reference to external information sources? Additionally, the fifth bullet refers to "when *this* involves handling large volumes of data," it is unclear what *this* is referring to. See proposed edit below to address the latter comment. • ... • The complexity of the information technology systems used to obtain and process the data, including when **<u>the information technology systems</u>** ~~this involves~~ handl**<u>e</u>**~~ing~~ large volumes of data.
		A42	DTTL does not believe that the second bullet reflected in paragraph A42 of ED-540 appropriately describes the transfer of data between systems and accordingly suggests re-wording the application material and adding another bullet to address modifications to data. DTTL recommends for clarity that a separate bullet address the automated calculations, and the related example. DTTL also recommends that the last sentence of the second bullet be separately reflected in order to highlight the risks relating to controls over the maintenance of the integrity and security of the data. When making an accounting estimate involves large volumes of data or otherwise involves complex processing, management may make extensive use of information technology. In such cases, controls relevant to the audit are likely to include general IT controls and application controls. Such controls may address risks related to: • The complete and accurate extraction of data from the entity's records or from external information sources; ~~and~~ • **<u>The appropriateness of any modifications to the data;</u>** • **<u>Automated or manual interfaces that allow for the transfer of data between various systems;</u>** ~~The complete and accurate flow of data through the entity's information systems and the appropriateness of any modification to the data used in making accounting estimates,~~ • **<u>Automated calculations,</u>** such as the translation of data into a different currency~~. Controls to maintain the integrity and security of the data are also likely to be relevant to the audit~~.**<u>; and</u>**

			• **The maintenance of the integrity and security of the data.**
		A43	DTTL has proposed edits that address the following matters as it relates to paragraph A43 of ED-540: (1) Lead-in. DTTL believes that there should be a reference to paragraph A33 of ED-540 where it is noted that when management's expert makes or identifies assumptions to assist management in making the accounting estimate, such assumptions become management's assumptions. (2) First bullet. The example relating to the evaluation of the likely outcome of applying complex contractual terms could be applicable to many estimates, and is not necessarily indicative of an expert; therefore, DTTL suggests deleting. (3) Final paragraph. DTTL noted that within this paragraph, reference is made only to an increase in control risk, it is DTTL's view that the failure by management to apply the required specialized skills or knowledge may increase risks of material misstatements. (4) DTTL believes that the last phrase in paragraph A33 of ED-540, "Assumptions may be made or identified by a management's expert to assist management in making the accounting estimates. Such assumptions, when used by management, become management's assumptions." would be better suited in paragraph A43 of ED-540, as this paragraph is discussing experts. Management may have, or the entity may employ individuals with, the skills and knowledge necessary to make the accounting estimates. In some cases, however, management may need to engage an expert to make, or assist in making, them **(see paragraph A33)**. This need may arise because of, for example: • The specialized nature of the matter requiring estimation, for example, the accounting estimate may involve measurement of mineral or hydrocarbon reserves in extractive industries ~~or the evaluation of the likely outcome of applying complex contractual terms~~. • ... A failure by management to apply the required specialized skills or knowledge, including engaging an expert when management does not otherwise have access to an individual with such skills and knowledge, increases ~~control risk~~ **risks of material misstatements**.
		A44	DTTL does not believe that this paragraph provides guidance to the auditor in addressing the requirements of paragraph 10. Rather it highlights the benefits for management of having early discussions with the auditor about complex estimates. While DTTL agrees that such discussions may be helpful to management in highlighting the need for a management expert, DTTL does not believe that such guidance should be included in an auditing standard.

		A45 and A46	DTTL noted that the phrase "significant sources of data" has been used in paragraph 45 of ED-540 (fourth bullet), yet in paragraph 46 of ED-540 (first bullet) the phrase is "sources of significant data." The phrases have two different meanings; therefore, it is unclear what the intent is of the IAASB. DTTL recommends that the concepts be aligned and consistently used. •
		A47	DTTL recommends the edits noted below to address the following matters: (1) As drafted, management may only change the method for certain reasons, there is no permitted flexibility. DTTL recommends inserting wording to allow for additional reasons given supportable facts and circumstances (2) DTTL believes that management should not be placed in a position to support why they did not change the method. Discussing the reasons for no change in the method with management is, instead part of the auditor's understanding in determining as to whether or not the continued use of the method is appropriate. In evaluating how management makes the accounting estimates, the auditor is required to understand the extent to which management has identified and addressed the need for change in the methods, assumptions or data used. If management has changed the method for making an accounting estimate, it is important that management can demonstrate that the new method is more appropriate, or is itself a response to changes in the environment or circumstances affecting the entity, or to changes in the requirements of the applicable financial reporting framework or regulatory environment **or another reason suitably supportable by management**. It is also important that **the auditor understands** ~~management can demonstrate,~~ when no change has been made, ~~that~~ **whether** the continued use **by management** of the previous methods, assumptions and data is appropriate in view of the current environment or circumstances (for example, whether management's assumptions about marketplace transactions or price quotes reflect fair value when there is reduced market activity).
		A49	DTTL believes that the last sentence infers that understanding the design and implementation of relevant controls is an appropriate response to address assessed risks of material misstatements, which would be inconsistent with the requirements of ISA 330. See proposed edits to provide clarity. Some entities may have a wide range of accounting estimates, some of which may be significantly affected by, or subject to, complexity, the need for use of judgment by management, and estimation uncertainty. In such circumstances, there may be an increased need for the application of specialized skills or knowledge, and management may make extensive use of information technology in making the estimates. In such cases, it will likely be more important for the auditor to understand the design and implementation of relevant controls **that address the assessed risks of material misstatement.** ~~,~~

			~~and~~**.** **It may** also **be appropriate** to test the~~ir~~ operating effectiveness **of the relevant controls** ~~in addressing the assessed risks of material misstatements~~.
		A50	DTTL notes that the wording used in the first sentence is not consistent with how ISA 315 (Revised) discusses the understanding of internal control, including the control environment. The following edits are proposed: The auditor's understanding of the control environment relevant to making accounting estimates ~~includes consideration of the influence that the elements of the control environment would be expected to have on the risks of material misstatement. This~~ may include, for example, whether: • Management, with the oversight of those charged with governance, has created and maintained a culture of transparency and proper ethical behavior; and • The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control and whether those other components are not undermined by deficiencies in the control environment.
		A51	DTTL does not believe the footnote cross-reference is correct, and it should be to paragraph A76 of ISA 315 (Revised).
		A55	DTTL notes that the first sentence is a requirement – see paragraph 16 of ISA 315 (Revised). The remainder of the paragraph is guidance. See proposed wording changes. **As required by ISA 315 (Revised), i**~~I~~f the entity has a risk assessment process, the auditor is required to obtain an understanding of the process and its results in relation to the entity's accounting estimates~~,~~**.** **This understanding may** includ**e**~~ing~~ how management determines the risks to be managed arising from changes in: • The requirements of the applicable financial reporting framework related to the accounting estimates; • The availability or nature of data sources that are relevant to making the accounting estimates or that may affect the reliability of the data used; • The entity's information systems or IT environment; and • Key personnel.
		A56	The fifth bullet appears to discuss management's responsibilities in terms of external information sources. DTTL recommends deleting this wording as it is unnecessary. With respect to the entity's information system relevant to making accounting estimates, it may be appropriate for the auditor to obtain an understanding as to whether: • ...

	• When using external information sources, management considers and appropriately addresses the risks related to processing or recording the data, ~~recognizing management's responsibility for appropriately reconciling and challenging the data from those sources~~; and • ...
A57	DTTL believes that paragraph A57 of ED-540 is a factual statement and would be better located as a lead-in to the section as to why auditors need to understand information systems (i.e., above paragraph A56 of ED-540).
A58	DTTL believes that there should be further context around the reference to the cross-references (paragraphs A30 and A42 of ED-540) in the last bullet, as neither of those paragraphs relate only to control activities.
A60	Refer to the comment above in paragraph 23 of ED-540 regarding amending the lead-in to paragraphs addressing "Considerations specific to smaller entities." Edits made to highlight that controls are typically performed by an owner-manager in a smaller entity, but that does not necessarily mean they are of a limited nature. In addition, where the owner-manager is making the estimate, it appears redundant to state that the owner-manager may have significant influence over the determination of the estimate. Further management bias is considered because it is a risk, edits proposed to clarify that point. In **less complex entities, many of which may be** smaller ~~entities~~, accounting estimates may be ~~generated~~ **made** outside the general ledger **and recorded in the general ledger by journal entries. In such instances, the** controls over the~~ir development~~ **making of accounting estimates**~~may be limited~~ **are generally performed by the owner-manager**~~, and an owner-manager may have significant influence over the determination~~. The owner-manager's role in making the accounting estimates **is likely** ~~may need~~ to be taken into account by the auditor ~~both~~ when identifying the risks of material misstatement**,** ~~and when~~ **including** considering the risk of management bias. ISA 315 (Revised) includes specific considerations to smaller entities that the auditor might find helpful in obtaining an understanding of the components of internal control as it relates to making accounting estimates.
A61 - Heading	DTTL noted that the heading above paragraph A61 of ED-540 is in bold, and there is no corresponding heading above the requirement paragraph 11 of ED-540. This is inconsistent with the formatting in the proposed standard. A heading, at the appropriate level, should either be inserted above paragraph 11 of ED-540 or the heading level should be amended in the application material
A61	Editorial suggestion to provide additional clarity in the lead-in paragraph and the second bullet. DTTL believes that the third and fourth bullets overlap and should be combined. The last phrase of the fifth bullet should be deleted as it is vague and not really pertinent

			to the risk assessment process. A review of the outcome or re-estimation of accounting estimates made in previous periods (retrospective review) assists in identifying and assessing the risks of material misstatement, specifically in circumstances when previous period accounting estimates have an outcome through transfer or realization of the asset or liability **in the current period**, or are re-estimated for the purpose of the current period. Through performing a retrospective review, the auditor may obtain: • Information regarding the effectiveness of management's previous estimation process, from which the auditor can obtain insight about the likely effectiveness of management's current process. • Audit evidence that is pertinent to the re-estimation, in the current period, of **accounting estimates that existed in** previous period**s** ~~accounting estimates~~. • Audit evidence of matters, such as estimation uncertainty, that may be required to be disclosed in the financial statements. • Information regarding the complexity and estimation uncertainty pertaining to the accounting estimates. • Information regarding the susceptibility of accounting estimates to, or that may be an indicator of, possible management bias. The auditor's professional skepticism assists in identifying such circumstances or conditions**.** ~~and in determining the nature, timing and extent of further audit procedures.~~
		A62	DTTL believes this paragraph provides a better lead-in to the section. Recommend including it before A61. Other edits suggested for clarity. A retrospective review may be performed over accounting estimates made for prior period financial statements but also for accounting estimates made **for** ~~over~~ several periods or a shorter period (such as half-yearly or quarterly). …
		A64	DTTL proposed edits to clarify that the review is retrospective. Further, DTTL believes that data was inadvertently omitted from the paragraph and is relevant when performing a retrospective review. The auditor may judge that a more detailed **retrospective** review is required for those accounting estimates that have changed significantly from the previous period, or for those accounting estimates for which the inherent risks were not low in the previous periods. As part of the detailed **retrospective** review, the auditor may pay particular attention, when possible, to the effect of **data and** significant assumptions used in making the previous estimates. On the other hand, for example, for accounting estimates that arise from the recording of routine and recurring transactions, the auditor may judge that the application of analytical procedures as risk assessment procedures is sufficient for purposes of the review.

		A66	DTTL proposes a drafting change to improve clarity. A difference between the outcome of an accounting estimate and the amount recognized in the previous period's financial statements does not necessarily represent a misstatement of the previous period's financial statements. However, ~~it~~ **such a difference** may **represent a misstatement** ~~do so if~~, for example, **if** the difference arises from information that was available to management when the previous period's financial statements were finalized, or that could reasonably be expected to have been obtained and taken into account in the preparation of those financial statements. …
		A67	Wording is proposed to improve the "linkage" to the requirement in paragraph 11. …. During the course of the audit, **including when performing risk assessment procedures and related activities,** the auditor may identify a need for specialized skills or knowledge to be applied in relation to **auditing** one or more aspects of the accounting estimates.
		A68	DTTL notes that in paragraph A68 of ED-540 there is a reference to the judgment of management in the sixth and seventh bullets. It is requested that additional clarity be provided as to whether it is the judgment of management or the auditor's judgment that is being referred to.
		A69	DTTL recommends that the third sentence of the paragraph be clarified such that it is clear whether or not this is also an example. In addition, DTTL believes that individuals with specialized skills or knowledge may be involved for all active banking institutions, not just those that are internationally active. Recommend the following edits be made: Many accounting estimates do not require the application of specialized skills or knowledge. For example, for most audits it is unlikely that specialized skills or knowledge would be necessary for an auditor to evaluate a bonus accrual or inventory obsolescence. However, ~~for~~ **when auditing** expected credit losses of an ~~internationally~~ active banking institution or the insurance contract liability for an insurance entity, the auditor is likely to conclude that it is necessary to ~~apply~~ **involve individuals with appropriate** specialized skills or knowledge.
		A70	DTTL questions the relevance of the first sentence and recommends that it be deleted. Further DTTL recommends that the second sentence be combined with paragraph A67 of ED-540
		A73	Recommend the following edits to provide further clarity, and ensure technical accuracy in ED-540 (see similar proposed edits relating to level 3 inputs in paragraphs A81 and A88 of ED-540). DTTL also recommends striking the example relating to the valuation of goodwill, because goodwill is not itself the subject of the evaluation rather it is the residual balance Instead it may be relevant to refer to the valuation of intangible assets

			acquired in a business combination. DTTL has also proposed adding another example. For some accounting estimates, the auditor's assessment of the risks of material misstatement may be influenced by inherent risk that is not low. Examples may include: • ... • Accounting estimates for which a complex model is used or for which there are assumptions or data that cannot be observed directly in the marketplace (**fair values using** level 3 **inputs** ~~fair values~~). • ... • ~~Valuation of goodwill in a business combination.~~ • **Valuations subsequent to business combinations, such as an annual impairment assessment**
		A74	The following edits are proposed for further clarity. It is important to qualify whose judgments are being referred to (i.e., the auditor's use of professional judgment, or the use of judgment by management). The reasons for the auditor's assessment of the risks of material misstatement **relating to an accounting estimate** may result from one or more of the factors of complexity, judgment and estimation uncertainty. For example: (a) Accounting estimates of expected credit losses are likely to be complex because the expected credit losses cannot be directly observed and may require the use of a complex model. The model may use a complex set of historical data and assumptions about future developments in a variety of entity specific scenarios that may be difficult to predict. Accounting estimates for expected credit losses are also likely to involve high estimation uncertainty and significant subjectivity **by management** in making judgments about future events or conditions. Similar considerations apply to insurance contract liabilities. (b) An accounting estimate for an **inventory** obsolescence **allowance** ~~provision~~ for an entity with a wide range of different inventory types may require complex systems and processes, but may involve little judgment and the estimation uncertainty may be low, depending on the nature of the inventory. (c) ....
		A80	DTTL notes that the application material refers to "valuation attributes." While this terminology is used in subsequent application material, it is not defined or further explained in the proposed standard. Consideration should be given to including the description in paragraph 4 of Appendix 1 to ED-540 in the application material.

		A81	The examples in this paragraph are intended to be examples of estimates that are likely to involve complex models. DTTL notes however that the first and last bullets are rather estimates where the determination (and auditing) of the assumptions is likely to be the more complex or difficult aspect. For example, a cash flow model may not be very complex, but the assumptions about future revenues may be. DTTL therefore recommends deleting the first and last bullets. The second bullet refers to "historical experience data"; DTTL suggests that additional clarity be provided in order to determine whether this is factual data (historical data) or derived data (historical experience data). Examples of accounting estimates for which complex models are likely to be used include: • ~~An impairment loss for goodwill or an intangible asset, which may require expectations about future cash flows from the business, asset or a group of related assets to be developed based on historical data and forward looking assumptions.~~ • An expected credit loss, which may require expectations of future credit repayments and other cash flows, based on **consideration of** historical experience data and **the application of** forward looking assumptions. • **Valuation of** ~~A~~**a**n insurance contract liability, which may require expectations about future insurance contract payments to be projected based on historical experience and current and assumed future trends. • ~~A level 3 fair value based on cash flow projections and historical market related data.~~
		A82	The following edits are recommended: (1) Lead-in – edits to align with paragraph 13(a)(ii) (2) First bullet. Edit to address why the data may be more susceptible to misstatements. (3) Second bullet. DTTL would like clarification on why the data is only relevant in making a fair value estimate. Also recommended that the bullet follows the construct of other bullets in paragraph A82 of ED-540. (4) Third bullet. Clarify that the auditor may test the operating effectiveness of these controls. (5) Fifth bullet. DTTL does not believe there is appropriate linkage between the volume of data and the risk it may be inappropriately used. Suggest deleting the last sentence Risks of material misstatement related to complexity in making accounting estimates may arise when such complexity leads to greater difficulty in obtaining **relevant and reliable data and** ~~, or in~~ maintaining the integrity of ~~, relevant and reliable~~ **that** data, stemming from one or more of the following:

			• The reliability of the data source. Data from certain sources may be more reliable than from others. For example, data obtained from internal systems outside the general and subsidiary ledgers may be more susceptible to misstatements **than data obtained from the general and subsidiary ledgers,** because in some entities it may be difficult to determine whether there were appropriate controls and governance over ~~that~~ data **obtained from outside the general and subsidiary ledgers**. • Data from an external information source**. Such data** may be less relevant in making a fair value estimate if it is not based on observable market transactions. For example, it may be less relevant when it is based on brokers' quotes that reflect brokers' subjective judgments in the context of an inactive market. In addition, for confidentiality or proprietary reasons, some external information sources will not (or not fully) disclose information that may be relevant in considering the relevance and reliability of the data they provide, such as the sources of the underlying data they used or how it was accumulated and processed (including any controls over the process). It may be more difficult to consider the relevance and reliability of such data than in the case of data from more transparent external information sources. • The integrity of the information systems. Data that is used to make the accounting estimates may be processed by information systems**. In order to maintain the integrity of the information systems,** ~~that may require~~ effective general IT controls, and controls over the flow of data through the system **are necessary**. **In such circumstances the auditor will likely identify these controls as relevant to the auditor's understanding and may also determine that it is necessary to test their operating effectiveness.** • A complex organizational structure or a lack of integration between systems in different parts of the entity may give rise to difficulty in reliably and consistently aggregating. • The volume of data or the source of the data, including data that comes from a wide variety of sources. ~~This may lead to the risk that the data may be inappropriately used, or may be incomplete or from an incorrect data set.~~
		A83	The following edits are recommended: (1) Lead-in. Judgment may be used to develop both appropriate and inappropriate assumptions. Delete "appropriate." (2) First bullet. Edit made to encompass both when management decides not to use and does not consider using an expert. (3) First Sub-bullet. Edit made to address that the method selected by management may either not comply or may be inappropriate. (4) Second Sub-bullet. Insert an additional risk related to assumptions. (5) Second bullet. Delete as management bias is an underlying factor to consider when

			auditing all accounting estimates. (6) Third bullet. Delete reference to judgment as the lead-in already indicates that these are risks of material misstatement relating to judgment. Judgment may be used by management in the selection or application of appropriate methods, the selection or development of ~~appropriate~~ assumptions, and the selection or interpretation of data. The risks of material misstatement related to judgment involved in making accounting estimates may relate to one or a combination of the following: • A lack of experience or competence by management, including a lack of availability to management of necessary skills or knowledge. These factors may result in risks related to the selection of inappropriate methods, assumptions and data. When management lacks the competence or experience in a certain area and ~~decides not to~~ **does not** use a management's expert, there may be a risk that: o The method selected may not **be appropriate or** comply with the applicable financial reporting framework. o **The assumptions used are not appropriate in the context of the measurement objectives and other requirements of the applicable financial reporting framework.** o Management may select a data source that is not relevant and reliable. • ~~Indicators of management bias~~. • The extent to which the applicable financial reporting framework does not specify the appropriate valuation approaches, concepts, techniques and factors to use in the estimation method ~~and therefore may require significant judgment~~.
		A84	DTTL noted that in paragraph A84 of ED-540 the phrase "high degree of judgment was introduced." DTTL recommends there be guidance to explain what the difference is between "significant judgment" as used in paragraph A83 (and elsewhere in ED-540) and a "high degree of judgment" used in the paragraph below as well as in paragraph A85 of ED-540. DTTL also recommends that an example be provided for the last bullet, so as to be consistent with other bullets. Edits are proposed to clarify that the examples are applicable to those estimates that have risks of material misstatement related to management using a high degree of judgment. Examples of accounting estimates that are likely **to have risks of material misstatement related** ~~to be subject~~ to **management using** a high degree of judgment include the following: • Accounting estimates that are based on expected future cash flows for which there is uncertainty regarding the amount or timing. • Accounting estimates that are based on complex contractual terms. For example, the determination of cash inflows or outflows arising from commercial supplier or customer

			rebates may depend on very complex contractual terms that require specific expertise or competence **to understand or interpret**. • Accounting estimates with a long forecast period.
		A86	DTTL recommends that additional clarity be given as to what the variation is that is being referred to; i.e., variation between companies, from one period to the next. DTTL suggests that factors (or potentially "matters") be used instead of variables, consistent with the usage of the term in the first sentence. DTTL also recommends that the wording in this paragraph be aligned with the definition.
		A88	Deleted "material" as the phrase "material disclosure" is not defined or commonly used within the ISAs. Editorial suggestion to provide additional clarity (see similar proposed edits relating to level 3 inputs in paragraphs A73 and A81of ED-540). The risks of material misstatement related to estimation uncertainty may relate to one or **both** ~~a combination~~ of the following: • The applicable financial reporting framework, which may require: o The use of a method to make the accounting estimates that inherently has a high level of estimation uncertainty. For example, the financial reporting framework may require the use of a **fair value using** level 3 **inputs** ~~fair value~~. o The use of assumptions that inherently have a high level of estimation uncertainty, such as future cash flows for a long-term contract, assumptions that are based on data that is unobservable and are therefore difficult for management to develop or the use of the various assumptions that are interrelated. o Disclosures about estimation uncertainty. There may be a risk of material misstatement related to the failure to make a ~~material~~ disclosure ~~about~~ **related to** estimation uncertainty.
		A92	DTTL believes that changes in assumptions when using a sensitivity analysis will always result in some level of sensitivity. Further it is not clear whether this paragraph is referring to an analysis being performed by the auditor or management. DTTL also recommends that guidance be added to address what the focus of the auditor's attention should be, as currently drafted this remains open-ended. The following edits are suggested: A sensitivity analysis **performed by the auditor**~~may~~ demonstrate**s** ~~that~~ the ~~accounting estimate is~~ sensitivit**y**~~e~~ **of the accounting estimate** to one or more assumptions that then become the focus of the auditor's attention. **This focus may result in additional risks of material misstatement being identified.**

		A94	The final wording of Paragraph A94 states "…thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively." This wording appears to be somewhat similar with ISA 330.7(a)(iii); however, it may also be interpreted as having a different meaning (as the words are not consistent). DTTL suggest adding the parenthetical from ISA 330.7(a)(iii) or including a more specific reference to Paragraph 7 of ISA 330.
		A96	DTTL believes that the sentence as drafted needs to be re-worded to more accurately reflect the objective of ISA 330. ~~If the further audit procedures in paragraph 15(a) do not provide sufficient appropriate audit evidence, t~~**T**he auditor is required by ISA 330 to design and perform **further** ~~othe~~r **audit** procedures **whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. In doing so, if the further audit procedures in paragraph 15(a) do not provide sufficient appropriate audit evidence, the auditor would be responsible for designing and implementing other procedures in order to achieve the objective of ISA 330. [Footnote]** **[Footnote] Paragraph 3 of ISA 330.**
		A97	DTTL believes the last sentence of paragraph A97 of ED-540 is unnecessary. When inherent risk is not low, this ISA does not specify the nature of the further audit procedures to be performed to respond to the assessed risk of material misstatement. Procedures such as obtaining audit evidence about events occurring up to the date of the auditor's report, testing how management made the accounting estimate, developing an auditor's point estimate or range, or performing other types of substantive analytical procedures, may assist the auditor in obtaining audit evidence about the matters in paragraphs 17–19. ~~However, such procedures need to be designed to address the matters in paragraphs 17–19.~~
		A98	DTTL is unclear in the first bullet why volume of transactions is an indicator that substantive procedures alone are insufficient and suggest that additional explanation as to *why* volume would indicate such. Likewise, DTTL believes similar clarity is needed around the third bullet.
		A104	DTTL recommends aligning the guidance with that in paragraph A30 of ED-540, which deals with the auditor's initial understanding of the validity of models.
		A106	DTTL believes that data can also be sourced from management's expert and this should be separately identified. Further, when determining the integrity of data and assumptions, the auditor would need to make sure it is reliable, in doing so the auditor may compare the data and assumptions with an external information source. DTTL

			recommends that the linkage be reinforced. Data may be developed internally, or may be obtained from **management's expert or** an external information source. When obtaining audit evidence about the integrity of data and assumptions, it may be appropriate for the auditor, **when assessing the reliability of such data and assumptions,** to compare the data and assumptions with an external information source.
		A109	DTTL noted that while the requirement in paragraph 18(a)(ii) of ED-540 and the heading above the application material paragraphs A108 and A109 of ED-540 refer to *significant* data and *significant* assumptions, the application material paragraphs refer only to data and assumptions. It is unclear if this is intentional or if the application material needs to be aligned with the requirement.
		A113	DTTL recommends the deletion of the last sentence of paragraph A113 of ED-540. As previously mentioned, DTTL believes that the three factors of complexity, the use of judgment by management, and estimation uncertainty are interlinked and cannot be discretely separated. In particular, DTTL does not believe it is appropriate to state that the selection of management's point estimates is based solely on estimation uncertainty. To determine an appropriate management point estimate, and related disclosures, it is necessary to understand the sources of inherent variability in the measurement outcomes, the extent of that variability, and the range of reasonably possible measurement outcomes. It also is necessary for management to identify and address the effects of complexity and judgment in the measurement process that increase the susceptibility of the accounting estimate to misstatement. ~~This is important so that the selection of management's point estimate, and the development of related disclosures, is based only on estimation uncertainty~~
		A114	DTTL believes the last sentence of the paragraph requires additional clarity. It appears that the intent is for the auditor to request support for a consideration that was not as yet performed by management, either because management is unable or unwilling. In such an instance, while there is nothing preventing the auditor from making the request, it is unlikely that anything will be forthcoming. In such an instance the auditor should consider the impact on the auditor's further audit procedures and whether there is a control deficiency that warrants communication with those charged with management and management; therefore, additional wording reflecting these considerations is recommended.
		A116	DTTL has proposed edits to reflect terminology that is used throughout ED-540. DTTL also proposes language to align management's point estimate with that of the definition in paragraph 9(e) of ED-540. Management's point estimate is not a "range of reasonably possible outcomes" as stated in the paragraph.

			When preparing the financial statements, it also is important for management to determine that the estimation uncertainty has been properly **disclosed** ~~depicted~~ **in accordance with the applicable financial reporting framework.** ~~This includes the selection of an appropriate point estimate and the related disclosures in the financial statements that describe the estimation uncertainty. For this purpose, a~~**A**n appropriate management point estimate is an amount that **is selected by management for recognition or disclosure in the financial statements as an accounting estimate and is in accordance with the applicable financial reporting framework** ~~appropriately represents the range of reasonably possible outcomes, and appropriate~~ **The** related disclosures **may** describe the extent of the variability in reasonably possible measurement outcomes.
		A123	DTTL believes calculations may not only be applied in developing the outputs, consequently edits are proposed to clarify the wording in the application material. … • The calculations applied in ~~developing the outputs from~~ the measurement process were mathematically accurate. • …
		A124	DTTL believes thatthe first sentence of paragraph A124 in ED-540 is inconsistent with the paragraph A123 as it implies that the assessment of what is reasonable extends beyond the requirements of, or the context of the applicable financial reporting framework. DTTL does not agree with this, and further notes that this sentence is also inconsistent with the requirement in paragraph 21 and the guidance in paragraph A2 which explains that “reasonable” is considered in the context of the framework. When determining whether the disclosures are reasonable in the context of a fair presentation framework, one of the auditor’s considerations would be whether disclosures beyond the specified requirements of the framework are necessary to achieve fair presentation based on the specific facts and circumstances, i.e., the auditor would not be able to conclude that the requirements of the fair presentation framework have been addressed if additional disclosures are required to achieve fair presentation. DTTL is also not clear how this would work for a compliance framework and what the basis would be for the auditor’s determination that additional disclosures are required beyond the framework’s requirements. DTTL therefore recommends deleting the first sentence of paragraph A 124 and further recommends that he second sentence be added after the bullet list in paragraph A123 of ED-540 (as a separate paragraph).
		A126	DTTL believes that the focus from the auditor’s perspective should be on whether or not management appropriately addressed estimation uncertainty. The response of the auditor is based on management’s actions. DTTL also believes that where management hasn’t appropriately addressed estimation uncertainty, a request for management to enhance the disclosures around estimation uncertainty is not an appropriate response to amend what is essentially a scope limitation. In such circumstances the auditor should

			also consider the impact on the auditor's further audit procedures and whether there is a control deficiency that warrants communication with those charged with management and management. The recommendations have been noted as follows: When the auditor believes that management has not appropriately ~~understood or~~ addressed estimation uncertainty, the auditor may consider requesting management to consider alternative assumptions ~~or to provide additional disclosure relating to the estimation uncertainty~~. **In these circumstances the auditor is required by ISA 265, *Communicating Deficiencies in Internal Control to Those Charged With Governance and Management*, to determine if the internal control deficiency identified is a significant deficiency such that it is required to be communicated to those charged with governance and management.**
		A128	DTTL does not understand why paragraph A128 was included in ED-540 and recommends that it be deleted. As drafted, it implies that the requirements of ISA 520 are always to be applied when developing an auditor's point estimate or auditor's range; however no additional context is provided as to how to do so in the context of addressing the requirements of ISA 540, and it will therefore be confusing to auditors as to what is expected or required. DTTL also does not believe that it is appropriate for application material to include requirements in this way. DTTL also believes that t is contrary to the approach of the ISAs to specifically designate a further audit procedure as being specifically a "substantive analytical procedure" .
		A140	DTTL recommends further edits to the application material to better describe the circumstances when the auditor would apply procedures addressing the matters relating to more than one factor. For example, **when identifying and assessing risks of material misstatement relating to an assertion,** the auditor ~~may have~~ identifie**s**~~d~~ that the ~~only~~ reason**s** for ~~an~~ **the**~~-assessed~~ risk**s** of material misstatement ~~is~~ **are** the need for the use of judgment by management **and estimation uncertainty** in making the accounting estimate. ~~However, w~~**W**hile performing procedures to address the matters in paragraph**s** 18 **and 19**, as applicable**, and in order to respond to the assessed risks of material misstatement where inherent risk is not low,** the auditor ~~may~~ discover**s** that the accounting estimate is more complex than originally contemplated~~,~~**. This** indicat**es**~~ing~~ that the assessment of the risk**s** of material misstatement ~~may need~~ **needs** to be revised (that is, the reasons for the assessment now include complexity)**, as required by paragraph 15(b)**. Therefore, the auditor needs to perform additional audit procedures to address the matters in paragraph 17, as applicable. ISA 315 (Revised) contains further guidance on revising the auditor's risk assessment.
		A143	Edits recommended to clarify that the auditor's determination goes to whether there is sufficient appropriate audit evidence to draw a conclusion relating to whether management's point estimate falls within the auditor's range. Paragraphs A113 to A118

			provide guidance to assist the auditor in evaluating management's selection of a point estimate to be included in the financial statements. Based on the audit evidence obtained, the auditor may conclude that there is sufficient appropriate audit evidence supporting a point estimate that does not differ from management's point estimate. When the auditor uses a range, and provided that the auditor's range only includes amounts that are supported by audit evidence obtained and the auditor has evaluated **such a range** to be reasonable as required by paragraph 20 of this ISA, the auditor may determine that **there is sufficient appropriate audit evidence to conclude that** management's point estimate falls within the auditor's range. In either of these situations, the auditor may **also** conclude that the accounting estimate is reasonable in the context of the applicable financial reporting framework.
		A149	DTTL believes the statement that where "there is intention to mislead, management bias is fraudulent in nature" is a legal determination, the outcome of which may vary by jurisdiction. See recommended edits below: Management bias may be more difficult to detect at an account level than when considering groups of accounting estimates or all accounting estimates, or when observed over a number of accounting periods. Although some form of management bias is inherent in subjective decisions, in making such judgments there may be no intention by management to mislead the users of financial statements. When, however, there is intention to mislead, management bias ~~is~~ **may be** fraudulent in nature**, however such an interpretation would be made in the context of the laws and regulations in the applicable jurisdiction. In such instances the auditor may consider the need to obtain legal advice.**
		A153	DTTL believes that as constructed the second sentence of paragraph A153 of ED-540 implies that as part of obtaining the written representations relating to significant data and significant assumptions, the auditor is required to consider the need to obtain representations about specific accounting estimates. The requirement in paragraph of 25 of ED-540 discusses those written representations as two discrete items. Further the lead-in to the application material refers to *significant* data and *significant* assumptions, yet the fourth bullet refers to [all] assumptions, and data. There appears to be an inconsistency as to what is required in the written representation. (See additional discussion regarding the deletion of the word *significant* in "Written Representations (paragraph 25)" in **Appendix I**). The following edits are made to address the comments highlighted: ISA 580 discusses the use of written representations. ~~In obtaining w~~**W**ritten representations **are required to be obtained from** ~~that~~ management and, when appropriate, those charged with governance, **about whether they** believe the methods**,** ~~and significant~~ data and ~~significant~~ assumptions used in making the accounting estimates and their related disclosures are appropriate~~, t~~**. T**he auditor is **also** required to consider the need to obtain representations about specific accounting estimates. …

		A157	Communications with regulators or prudential supervisors may highlight information that is relevant to identifying, assessing and responding to risks of material misstatement (i.e., not limited to only identification). For example, in some jurisdictions, financial institution regulators seek to cooperate with auditors to share information about the operation and application of controls over financial instrument activities, challenges in valuing financial instruments in inactive markets, expected credit losses, and insurance reserves while other regulators may seek to understand the auditor's views on significant aspects of the entity's operations including the entity's costs estimates. This communication may be helpful to the auditor in identifying**, assessing** **and responding to** risks of material misstatement.
		A159	DTTL notes the last sentence that includes a reference to paragraph A147 for examples of indicators of possible management bias. For consistency, should this sentence should be included in all application material paragraphs where there is a reference to the indicators, including, but not limited to, paragraphs A83 and A85 of ED-540?
		Appendix 1, paragraph 9	DTTL recommends deleting the word "statement" from the paragraph. See the following edit. Some measurement bases require the use of monetary amounts at initial recognition that reflect the cost paid or consideration given (and transaction costs) for a**n** ~~statement~~ asset acquired or built, and the consideration received (less transaction costs) for a liability incurred or assumed, based on the terms of the transactions that gave rise to them (historical cost).
		Appendix 1, paragraph 15	As noted in **Appendix I** to our comment letter, DTTL recommends the following edit be made so that Appendix 1 is drafted in a more framework neutral manner: The amount recoverable from disposal may be required to be determined based on a fair value measurement or at net realizable value, and may require estimation. Similarly the amount recoverable from use (**defined in certain financial reporting framework as "**value in use**"**) will ordinarily require estimation. There can also be complex considerations relating to the appropriate unit of account.
		Appendix 1, paragraph 17	DTTL notes that the concept of economic consumption of economic benefits exists for IFRS as well as other financial accounting frameworks, such as U.S. Generally Accepted Accounting Policies (U.S. GAAP). However, the guidance for U.S. GAAP refers to depreciation as a method of allocation, not valuation which may cause confusion to the user of the Appendix, as the measurement bases addressed in Appendix 1 are intended to be framework neutral. Similar observations are made as it relates to the concepts of decline or residual considerations.
		Appendix 1, paragraph 19	As noted in **Appendix I** to our comment letter, DTTL recommends that Appendix 1 be

			drafted in a more framework neutral manner. The definition of fair value is as contemplated by IFRS, and may not necessarily be used by all financial reporting frameworks. DTTL recommends that this definition be used as an example of an objective of a fair value measurement. See the following recommended edits: **Under some financial reporting frameworks a** ~~The~~ fair value measurement basis requires measurement of the price for which an asset would have been sold, or a liability transferred, in an orderly transaction (or, if no such transaction has occurred, in an assumed transaction) between market participants in an active market at the measurement date. The objective of **such** a fair value measurement is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions **(i.e., an exit price). Under other financial reporting frameworks the objective of a fair value measurement may be to reflect a current entry price.**
		Appendix 1, paragraph 20	As noted in **Appendix I** to our comment letter, DTTL recommends the following edits be made so that Appendix 1 is drafted in a more framework neutral manner: Financial reporting frameworks often establish a 'fair value hierarchy' that categorises the inputs used to measure fair value into ~~three~~ levels and gives priority to using those in the higher levels over using those in lower levels. The purpose of doing so is to increase consistency and comparability in fair value measurements and related disclosures. Quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date and that are not subject to adjustment, provide the most relevant evidence of fair value and are included in the highest level of the hierarchy (these are **often referred to as** level 1 inputs).
		Appendix 1, paragraph 21	As noted in **Appendix I** to our comment letter, DTTL recommends the following edits be made so that Appendix 1 is drafted in a more framework neutral manner: If a level 1 input is not available or accessible, it may be possible to measure the fair value using other observable inputs, such as quoted prices for similar items in an active market or quoted prices for identical items in a non-active market or other inputs observed in or corroborated with active markets (e.g., interest rates, yield curves, implied volatilities or credit spreads) ~~(such other observable inputs are level 2 inputs)~~.
		Appendix 1, paragraph 22	As noted in **Appendix I** to our comment letter, DTTL recommends the following edits be made so that Appendix 1 is drafted in a more framework neutral manner: Otherwise, it may be necessary to measure the fair value, sometimes using discounted cash flow techniques, based on the best information available in the circumstances, including unobservable inputs to the extent observable inputs are not available, and taking into account all information about market participant assumptions that is reasonably available ~~(unobservable inputs are level 3 inputs)~~.
		Appendix 1, paragraph 23	DTTL recommends that paragraph 23 be deleted as it is not necessary within the context of Appendix 1.

		Appendix 1, paragraph 24	As noted in **Appendix I** to our comment letter, DTTL recommends the following edits be made so that Appendix 1 is drafted in a more framework neutral manner: Some measurement bases require the use of monetary amounts that reflect the present value of the future cash flows that the entity will obtain from using and disposing of an asset (value in use) or will incur in fulfilling its obligations inherent in a liability (fulfilment value). For example, value in use **as defined above** is ~~frequently~~ used **in some financial reporting frameworks** to test for impairment (see paragraph 15). ….
		Appendix 1, paragraph 26	As noted in **Appendix I** to our comment letter, DTTL recommends the following edits be made so that Appendix 1 is drafted in a more framework neutral manner: Valuation techniques within the market approach typically use prices and other relevant information generated by market transactions involving identical or similar assets, liabilities or groups of assets and liabilities, such as businesses. Examples include the use of valuation techniques for measuring fair value that use **quoted prices in active markets for identical assets or liabilities** ~~level 1 and level 2 inputs~~ and valuation techniques for measuring fair value of real estate by reference to comparable properties.
		Appendix 2	In order to be consistent with the order in which the three factors are discussed throughout ED-540, DTTL recommends reordering the paragraphs such that layout addresses complexity, followed by use of judgment by management, and then estimation uncertainty. DTTL also notes that the phrase "use of judgment by management" should be used consistently throughout Appendix 2 to add clarity and to align with the use of the phrase in ED-540.
		Appendix 2, paragraph 4	DTTL notes that the definition of estimation uncertainty does not align with that in paragraph 9(c) of ED-540. See the following proposed edits. Estimation uncertainty is the **susceptibility of an** ~~inherent uncertainty that makes~~ accounting estimate~~s susceptible~~ to a**n inherent** lack of precision in ~~their~~ **its** measurement. …
		Appendix 2, paragraph 7	DTTL noted a reference to "residual estimation uncertainty" – this concept is not addressed in the proposed standard and should therefore be deleted from **Appendix 2**.
		Conforming and Consequential Amendments – ISA 260 (Revised), ***Communication with Those Charged with***	**Editorial Comments and Other Recommendations**

		Governance **Paragraph Number**	
		Appendix 2 – Accounting Estimates	DTTL recommends that the IAASB review and align the wording in this Appendix upon finalization of the proposed standard. Areas identified for possible improvement include: • Third Sub-bullet. There is a reference to "presentation" (in the context of addressing disclosures), yet this term is not used consistently throughout ED-540. DTTL suggests a conformed approach. • Sixth Sub-bullet. There is a reference to "significant data and assumptions." ED-540 refers to "significant assumptions." Terminology and phrases should be aligned. • Sixth Sub-bullet. DTTL questions whether the use of "reasonable" is appropriate when referring to how data and assumptions are described for the purpose of ISA 260 (Revised), *Communication with Those Charged with Governance*, (ISA 260 (Revised)) Appendix 2. When referring to paragraph A35 of ED-540, reasonable is used in terms of variations in the data or assumptions and how such a variation would materially affect the measurement of the accounting estimate, which is inconsistent with the context this term is used in ISA 260 (Revised) Appendix 2. DTTL believes that term should be consistently used in the context of data and assumptions. • Eleventh Sub-Bullet. DTTL believes that there is duplication as it relates to disclosures, as it is already addressed in the third sub-bullet. As drafted the sub-bullet also does not align with objective of ED-540.
		Conforming and Consequential Amendments – ISA 500, *Audit Evidence* **Paragraph Number**	**Editorial Comments and Other Recommendations**
		7 & A31	As noted in our response to Question 7, DTTL suggests removing the edit to paragraph 7. However, if the proposed edit is retained, DTTL believes that the wording in existing paragraph A31 of ISA 500 should be re-considered to better align with the terminology pertaining to an *external information source* in paragraph 7 of the amendments to ISA 500 and include specific mention of an "external information source".
		A1A	DTTL believes that determining whether an individual or organization meets the definition of a management expert is more than an "important consideration" as to whether an individual or organization is acting as an external information sources; rather it is the basis for making the distinction. It is the understanding of DTTL that if the definition of "management's expert" is met per paragraph 6(c) of ISA 620, *Using the Work of an Auditor's Expert*, then the information used by management would not be considered to be from an external information source. DTTL

			also suggests including the wording that the source may in fact not be an external information source, as this phrasing aligns with what is already included in paragraph A1C. Other conforming edits are also proposed below: In preparing the financial statements, management may make use of information obtained from an external information source **or may make use of** ~~An important consideration in determining whether an individual or organization is acting as an external information source is whether the individual or organization meets the definition of~~ a management's expert **[footnote].** ~~with respect to that information.~~ Indicators that an **individual or organization** ~~external organization~~ may be acting as an external information source rather than as a management's expert **in relation to information used by the entity in preparing the financial statements** include the following: … **[Footnote]: Paragraph 6(c) of ISA 620.**
		A1C	DTTL recommends edits to paragraph A1C of the amendments to ISA 500 in ED-540 as it relates to the following matters: (1) Lead-in. Edits to clarify the language. (2) First bullet. Clarification to highlight that an external organization may make use of generally available information in delivering the service to management, but that the objective of the service is to provide information specifically tailored for the entity and will necessarily involve entity-specific information, data and assumptions. (3) Second bullet. Clarification, an estimate is not calculated, but rather is determined through a process (which might involve one or more calculations). Depending on the facts and circumstances, an individual or organization may, in ~~respect of~~ **relation to** any particular set of information, be either an external information source or a management's expert**,** but not both. Professional judgment may be needed to determine whether a**n individual or organization** ~~specific organization~~ is acting as an external information source or as a management's expert ~~with respect to~~ **in relation to** a particular set of information. For example: • An external organization may be acting as an external information source with respect to data about real estate prices for a particular geographical region that it makes generally available to the public and that management uses in preparing the financial statements. The same external organization may ~~at the same time be acting~~ **also serve** as a management's expert ~~for the same entity~~ in providing management with a valuation service with respect to the entity's real estate portfolio. **When delivering the valuation service, the external organization may make use of the same information that is made generally available. However, when acting as a management's expert and performing the valuation service, the deliverable will be specifically tailored for the entity's facts and circumstances and will**

			involve entity-specific information, data or assumptions. **Such deliverable will also not be made generally available to the public.** • Some actuarial organizations publish mortality tables for general use which, when used by an entity, may **be considered to** be information from an external information source**.**~~, while t~~**T**he same actuarial organization may **also serve as**~~be~~ a management's expert**, for example** when ~~helping~~ **engaged by** management to **determine** ~~calculate~~ the pension liability for several of ~~its~~**the entity's** pension plans. • ...
		A33B	DTTL notes in this paragraph and throughout the conforming amendments to ISA 500 in ED-540 that the phrases "provided by," and "obtained from" have been used interchangeably. DTTL believes the meaning is the same in the context used and that the phrases should be conformed and consistently used. DTTL also proposes deleting the phrase "from [the] external information sources" as it is repetitive and already included in the lead-in to the bulleted list. (Additionally, there may be other amendments to ISA 500 that have used "provided by" that need to be aligned for consistency.) See proposed edits below: Depending on the circumstances, the following factors may be important ~~considerations in~~ **when considering or evaluating** ~~about~~ the relevance and reliability of information obtained from an external information source: • The nature and authority of the external information source used by the entity. For example, a central bank or government statistics office with a legislative mandate to provide industry information to the public is likely to be an authority for certain types of information; • The ability of management to influence the information obtained ~~from the external information sources~~; • The competence and reputation of the external information source with respect to ~~that particular type of~~ **the** information; • Past experience of the auditor with the reliability of the information **obtained** ~~provided by the external information source~~; • ... • The entity's controls over the information obtained ~~from external information sources~~; • ... • The nature and extent of disclaimers or other restrictive language relating to the information obtained; and • Whether information is available regarding the appropriateness of techniques,

			assumptions and inputs applied by the external information sources in developing the information obtained.
		A33C	DTTL believes that paragraph A33C of the amendments to ISA 500 in ED-540 should be more closely aligned with the discussion relating to the reliability of information in paragraph A31 of ISA 500, in particular the first bullet (which paragraph is not presented in ED-540). Additionally, DTTL believes that a better connection needs to be made between the concept of reliability that is discussed in the first sentence and consideration of accuracy and completeness in the second sentence. As discussed in paragraph A31 of ISA 500, reliability is broader than just the accuracy and completeness of information.
		A33D	DTTL believes that further guidance should be provided to expand on how different types of information would influence the nature, timing and extent of procedures to "test management's use of the sources." This is an area that is challenging in practice and therefore additional guidance would be very helpful.
		A33E	DTTL believes that the latter part of paragraph A33E of the amendments to ISA 500 of ED-540 is worded in such a manner that implies the reliability of the information is required to be specifically or discretely tested; DTTL believes rather that reliability of the information is addressed in designing procedures to support conclusions about whether sufficient appropriate audit evidence has been obtained. See the following recommended edits: The observability of inputs and complexity of methods used to generate the information **obtained** from the external information source may also influence the auditor's considerations related to the reliability of information **obtained** from the external information source, including considerations related to ~~the nature and extent of procedures to perform~~ **the procedures that may be performed** to **obtain sufficient appropriate audit evidence about**~~test thereliability of that~~ **such** information.
		A33F	DTTL suggests the following clarifications are necessary: (1) First bullet. As drafted, the phrase "test the controls and processes, techniques, and assumptions used" implies the testing of operating effectiveness applies to processes, techniques, and assumptions in addition to testing relevant controls, which DTTL does not believe is required or intended. Rather DTTL believes that in identifying and assessing the related risks of material misstatement, the auditor would be expected to understand the processes, techniques and assumptions (noting also that there would be more than one assumption), and identify and understand the relevant controls. In responding to the risks, the auditor may decide to, or may determine that it is necessary to, test the operating effectiveness of relevant controls, which is addressed in the second bullet

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<td>(2) Third bullet. Additional clarity is needed to explain the intention or meaning of this consideration, as its relevance to the auditor's consideration of the relevance and reliability of information is not apparent.

(3) Fourth bullet. DTTL believes that this paragraph is overly specific and should be redrafted more generally with an example relating to security prices. See suggested edits for this final bullet.

~~As part of the~~ **In** consider**ing**~~ation of~~ the relevance and reliability of information from external information sources, one or more of the following **procedures** may be **appropriate**~~relevant~~:

• ...

• ~~When the~~ **Performing a comparison of** information ~~received~~ **obtained** from the external information source **with information obtained** ~~relates to security prices, obtaining an independent price~~ from another **independent** information source**, for example, when the information from the external information source is a security quote, obtaining price quotes for the same securities from another independent external information source and comparing the two.**</td>
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<td>A33H</td>
<td>This paragraph requires additional clarity:

(1) First sentence. It's not clear what the auditor is using the information for; this understanding is necessary to put the guidance in context.

(2) Third sentence. When using "in such cases" it is not clear whether the auditor should be referring to the first sentence where there is one source and provider, or to the second sentence where there is a reference to obtaining additional audit evidence.

(3) Fourth sentence. The guidance to access a different source does not appear to make sense given that the first sentence indicates that there is only one source and provider.</td>
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<td>6.</td>
<td>EYG*</td>
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Appendix 3: Editorial suggestions and observations
<table>
<tr>
<th>ISA 540 paragraph reference</th>
<th>Observation/suggestion</th>
<th>Rationale</th>
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<tr>
<td>4</td>
<td>This ISA focuses the auditor's attention on<u>, in relation to accounting estimates,</u> designing and performing further audit procedures…</td>
<td>Clarification that the scope of 540 is limited to accounting estimates</td>
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<td>5</td>
<td>The application of professional skepticism by the auditor is particularly important to the auditor's work related to accounting estimates. ~~Professional skepticism also is important~~ because there is a particular risk of management bias affecting accounting</td>
<td>As written, the second sentence implies that the first sentence included a reason for the importance of professional skepticism, which it does not.</td>
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			estimates due to their subjective, potentially complex and uncertain nature.		
		10 (e)	How management makes accounting estimates, including: … (v) How the risk of management bias is ~~identified~~ assessed (vi) How management ~~has addressed~~ assesses estimation uncertainty; and (vii) How management ~~has addressed~~ assesses the need for a change from the prior period…..	As these are risk assessment procedures, we believe the auditor should be understanding how management assesses these areas and not how management has addressed them (which would be a substantive procedure)	
		A1	Examples of ~~situations where~~ accounting estimates that may be required by the applicable financial reporting framework include: • Inventory obsolescence • ….	To provide the explicit context of the requirements of the applicable financial reporting framework	
		A2	… means that all the relevant requirements of the applicable financial reporting framework have been addressed appropriately.~~,~~ ~~including those that address~~ The requirements of the applicable financial reporting framework may include requirements that address:	As written, the requirement implies that all frameworks would include specific requirements related to the bullets that follow.	
		A5	An auditor's point estimate or range may be developed for an accounting estimate as a whole (for example, ~~the expected credit losses for a particular loan portfolio~~ the impairment of an asset or the fair value…..	We do not believe that a point estimate or range is likely to be applied to an entity's expected credit loss estimate as a whole, and the application to a particular portfolio of the entity's loans would not represent application to the estimate as a whole.	
		A12	Depending on the circumstances, it may be possible for the accounting estimate to be determined directly….	The meaning of "determined directly" is not clear	
		A12	…., or it may be possible for management to select a ~~management~~ point estimate only after considering….	To clarify that management selects the point estimate, not the auditor	
		A14	Obtaining an understanding of the regulatory factors that are relevant to accounting estimates…….. may assist the auditor in determining whether the regulatory framework: • … • Provides an indication of areas for which there may be a potential for management bias towards consistency between ~~to meet~~ regulatory ~~requirements~~ reporting and financial reporting to the extent the respective requirements will allow	A suggested clarification to reflect the motivation by management that we encounter in practice	

		A39	Examples of data include: • … • In respect of expected credit losses, examples include default rates, credit ratings (including evolution of the rating through the loan life), days past due, collateral value based on appraisals, risk management categories specified by the entity	To provide additional examples of data specific to accounting estimates related to expected credit losses	
		A43	A failure by management to apply the required skills or knowledge, including engaging an expert….., ~~increases control risk~~ may constitute a deficiency in internal control	To clarify that such failure by management may be a deficiency in internal control (and to remove reference to control risk because ISA 540 does not require a separate assessment of control risk)	
		A50	The Relevance of the Control Environment ~~Relevant~~ to Making Accounting Estimates The auditor's understanding of the control environment ~~relevant to making accounting estimates~~ includes considerations of the influence that the elements of the control environment would be expected to have on the risks of material misstatement, including as it relates to accounting estimates.	To clarify that there is a single control environment within the entity, and not a separate control environment for accounting estimates	
		A54	In considering the relevance of the control environment to accounting estimates, t~~T~~he oversight of the financial reporting process by those charged with governance may ~~be particularly important for~~ include oversight of management's preparation of accounting estimates that, in particular:	To clarify that oversight of estimates by those charged with governance would be part of their oversight of the financial reporting process and that such oversight may be focused on higher risk estimates	
		A82	• The integrity of the information systems. Data that is used to make the accounting estimates may be processed by information systems ~~that may require effective general IT controls, and~~ for which controls over the flow of data through the system together with relevant general IT controls may be necessary to maintain data integrity.	To clarify how the controls identified contribute towards data integrity.	
		A108	~~The auditor's consideration of a change in an accounting estimate, or in the method for making it from previous periods, is important because a~~ A change from previous periods in the method, or significant data or significant assumptions, that is not based on a change in circumstances or new information is unlikely to be reasonable……	To align the application material to the revised requirement which does not focus on changes in the estimate, rather the changes in the method, significant assumptions or significant data	
		A114	There ~~is no~~ may not be a particular method of addressing estimation uncertainty that is more suitable than another. For example, management may employ sensitivity analysis, scenario analysis, ~~or,~~	To clarify that all methods may be suitable in certain circumstances, and that sensitivity analysis and scenario analysis are valid	

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<tr><td></td><td>~~when more robust evaluation is considered necessary (for example, in the banking or insurance industries)~~, stress testing ~~and~~ <u>or</u> reverse stress testing.</td><td>methods for banking and insurance industries.</td></tr>
<tr><td>A126</td><td>When the auditor believes that management has not appropriately understood or addressed estimation uncertainty, the auditor may consider requesting management <u>to take steps to address it, for example, by </u>~~to~~ consider<u>ing</u> alternative assumptions or ~~to~~<u>by</u> provide<u>ing</u> additional disclosure relating to the estimation uncertainty.</td><td>To clarify that the auditor's primary action should be to request management to address the estimation uncertainty and that there may be more alternatives to those that are mentioned in this paragraph</td></tr>
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<tr><td>7.</td><td>GTI*</td><td>
Detailed Drafting comments
Detailed below are our suggested drafting comments:
A35.Data and assumptions used in making an accounting estimate are referred to as significant data or significant assumptions…For example, an accounting estimate may be applied by applying a method that uses several data sets and several assumptions…
A89.A seemingly immaterial accounting estimate may have the potential to result in a material misstatement due to the estimation uncertainty associated with the accounting estimate; that is, the size of the amount recognized or disclosed in the financial statements for an accounting estimate is generally not, in itself, an indicator of its estimation uncertainty.
We note that the follow paragraph in the application material is inconsistent with the requirements in ED 540 to determine whether the estimate is of low or not low inherent risk.
A95. Paragraph 40 of ISA 200 states that the ISAs do not ordinarily refer to inherent risk and control risk separately. However, the auditor may make separate or combined assessments of inherent and control risk. Although this ISA neither implies nor requires a separate assessment of inherent and control risk, it highlights the importance of the auditor's consideration of both inherent and control risk in designing and performing further audit procedures to respond to the assessed risks of material misstatement, including significant risks, at the assertion level in accordance with ISA 330
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<tr><td>8.</td><td>PWC*</td><td>
Requirements
Risk Assessment Procedures and Related Activities
10. When performing risk assessment procedures and related activities to obtain an understanding of the entity and its environment, including its internal control, as required by ISA 315 (Revised), the auditor shall obtain an understanding of the following: (Ref: Para. A9–A10)
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		(a) The requirements of the applicable financial reporting framework relevant to accounting estimates, including the recognition criteria, measurement bases and the related presentation and disclosure requirements. (Ref: Para. A11–A13) (b) Regulatory factors, if any, relevant to accounting estimates. (Ref: Para. A14–A15) (c) ~~The nature of the accounting estimates and related disclosures that the auditor expects to be included in the entity's financial statements. (Ref: Para. A16–A17)~~ [*Relocated to proposed paragraph 11A*] (d) How management identifies those transactions, events and conditions that may give rise to the need for accounting estimates to be recognized or disclosed in the financial statements. In obtaining this understanding, the auditor shall make inquiries of management about changes in circumstances that may give rise to new, or the need to revise existing, accounting estimates. (Ref: Para. A18–A23) (e) How management makes accounting estimates, including: (Ref: Para. A24–A25) (i) The methods used, how they are selected or designed, and how they are applied, including the extent to which they involve modelling; (Ref: Para. A26–A31) (ii) The process used to select assumptions, including alternatives considered and how management identifies significant assumptions; (Ref: Para. A32–A38) (iii) The process used to select data, including the source(s) of that data and how management identifies significant data; (Ref: Para. A39–A42) (iv) The extent to which management has applied specialized skills or knowledge, including whether a management's expert has been used; (Ref: Para. A43–A44) ~~(v) How the risk of management bias is identified and addressed; (Ref: Para. A45)~~ [*Relocated to point (f)*] (vi) How management has addressed estimation uncertainty; and (Ref: Para. A46) (vii) How management has addressed the need for a change from the prior period in the methods, assumptions or data used, and if so, the nature of, and reasons for, such changes. (Ref: Para. A47). (f) ~~Each of the components of~~ Relevant internal control ~~as they~~ related to ~~making~~ accounting estimates, including the nature and extent of oversight and governance that the entity has in place over management's process, including controls that address the potential for management bias in making significant judgments. (Ref: Para. A48–A60) 11. The auditor shall review the outcome of accounting estimates included in the previous period financial statements, or, where applicable, their subsequent re-estimation to assist in identifying and assessing the risk of material misstatement in the current period. The auditor shall take into account the characteristics of the accounting estimates in determining the nature and extent of that review. The review is not intended to call into question judgments about previous period accounting estimates that were appropriate based on the information available at the time they were made. (Ref: Para. A61–A66)

11A. In discussing the susceptibility of the entity's financial statements to material misstatement, as required by ISA 315[2], the engagement partner and other key engagement team members shall discuss, based on the understanding obtained, the nature of the accounting estimates and related disclosures that the auditor expects to be included in the entity's financial statements, and how and where the entity's accounting estimates may be susceptible to material misstatement due to fraud or management bias. (Ref: Para. A16–A17)

12. Based on auditor's understanding of the nature of the accounting estimates and related disclosures included in the entity's financial statements, ~~T~~the auditor shall determine whether specialized skills or knowledge are required~~,~~ in order to perform ~~the~~ risk assessment procedures, ~~or to~~ identify and assess the risks of material misstatement, design and perform audit procedures to respond to those risks, or evaluate the audit evidence obtained. (Ref: Para. A67–A70)

Identifying and Assessing the Risks of Material Misstatement

13. In identifying and assessing the risks of material misstatement, as required by ~~applying~~ ISA 315 (Revised), the auditor ~~is required to~~ shall identify and assess the risks of material misstatement~~,~~ at the ~~financial statement and~~ assertion level in relation to accounting estimates (whether recognised or disclosed in the financial statements) and related disclosures, including ~~determine~~ determining whether any of the risks of material misstatement identified are, in the auditor's judgment, significant risks. ~~In identifying and assessing risks of material misstatements in relation to an accounting estimate~~ In making this risk assessment, the auditor shall take into account: ~~the extent to which the accounting estimate is subject to, or affected by, one or more, relevant factors, including: (Ref: Para. A71–A78)~~

(a) The complexity of the method used for making the accounting estimate, including the use of models;

(b) The number, complexity and source of significant assumptions and significant data used in making the accounting estimate;

(c) The extent to which the accounting estimate is sensitive to the selection of different methods or to variations in the assumptions and data used.

~~(a) Complexity in making the accounting estimate, including:~~

~~(i) The extent to which the method, including modelling, involves specialized skills or knowledge; and (Ref: Para. A79–A81)~~

~~(ii) The difficulty, if any, in obtaining relevant and reliable data and maintaining the integrity of that data; (Ref: Para. A82)~~

~~(b) The need for the use of judgment by management and the potential for management bias, including with respect to methods, assumptions, and data; and (Ref: Para. A83–A85)~~

~~(c) Estimation uncertainty, including the extent to which the accounting estimate is sensitive to the selection of different methods or to variations in the assumptions and data used. (Ref: Para. A86–A93)~~

[2] ISA 315, paragraph 10

		~~14. In responding to the assessed risks of material misstatement related to accounting estimates, the auditor shall determine whether specialized skills or knowledge are required to design and perform audit procedures, or to evaluate the results of those procedures. (Ref: Para. A67–A70)~~ [*Now merged with proposed paragraph 12*] 15. In ~~applying ISA 330, the auditor is required to~~ designing ~~and perform~~ further audit procedures to respond to the assessed risks of material misstatement, as required by ISA 330, the auditor shall design an approach to testing the accounting estimate that is responsive to the reasons for the assessment in paragraph 13 and that includes one or a combination of the following approaches: ~~including significant risks, at the assertion level. In doing so: (Ref: Para A94–A95)~~ (a) Obtaining audit evidence about events occurring up to the date of the auditor's report; (b) Testing how management made the accounting estimate and the data on which it is based; or (c) Developing a point estimate or range based on available audit evidence to evaluate management's point estimate. The approach shall take into account that more persuasive audit evidence is required the higher the auditor's assessment of risk, and that for risks assessed as significant risks ISA 330 requires the auditor, among other matters, to: (a) Test controls in the current period if the auditor plans to rely on controls over a risk; and (b) Include tests of details when the approach consists only of substantive procedures. The auditor shall also design and perform substantive procedures for each material class of transaction, account balance and disclosure, as required by ISA 330, related to accounting estimates, irrespective of the assessed risk of material misstatement. ~~(a) When inherent risk is low, the auditor shall determine whether one or more of the following further audit procedures would provide sufficient appropriate audit evidence regarding the assessed risk(s) of material misstatement in the circumstances: (Ref: Para A96)~~ ~~(i) Obtaining audit evidence about events occurring up to the date of the auditor's report;~~ ~~(ii) Testing how management made the accounting estimate and the data on which it is based; or~~ ~~(iii) Developing a point estimate or range based on available audit evidence to evaluate management's point estimate.~~ ~~(b) When inherent risk is not low, the auditor's further audit procedures shall include procedures to obtain audit evidence about the matters in paragraphs 17–20, when applicable. (Ref: Para A97)~~ ~~The auditor's further audit procedures shall be responsive to the reasons for the assessment given to the risk of material misstatement in accordance with paragraph 13, recognizing that the higher the assessed risk of material misstatement the more persuasive the audit evidence needs to be.~~ ~~16. If the auditor intends to rely on controls relating to accounting estimates, or if substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level, the auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to their operating effectiveness. (Ref: Para A98–A100)~~

		Obtaining audit evidence about events occurring up to the date of the auditor's report 15A. When the auditor obtains audit evidence from events that have occurred up to the date of the auditor's report, the auditor shall evaluate whether the audit evidence: (a) is sufficient, reliable and relevant to the accounting estimate, and (b) supports or contradicts the accounting estimate, taking into account that changes in circumstances and other relevant conditions between the event or transaction date and the measurement date may affect its relevance to the accounting estimate at the measurement date. **Testing how management made the accounting estimate and the data on which it is based** 15B. When testing how management made the accounting estimate and the data on which it is based the auditor's further audit procedures shall include procedures to: (a) obtain audit evidence about the method, significant assumptions and significant data used in making the accounting estimate (see paragraphs 17-18A); and (b) when applicable, address estimation uncertainty (see paragraph 19). [*Paragraphs 17-18A are not marked as they have been substantially redrafted. Application material references have been excluded as these would require re-mapping.*] *Method* 17. In responding to the assessed risks of material misstatement identified in accordance with paragraph 13, the auditor shall obtain evidence about: (a) whether the method selected for making the accounting estimate is appropriate in the context of the applicable financial reporting framework and changes, when applicable, from previous periods are appropriate; (b) whether the calculations are mathematically accurate and appropriately applied; and (c) when management's application of the method involves complex modelling, whether judgments made have been applied consistently and whether, when applicable: (i) the design of the model meets the measurement objective of the applicable financial reporting framework and is appropriate in the circumstances; (ii) changes, if any, from the previous period's model are appropriate in the circumstances; and (iii) adjustments, if any, to the output of the model are consistent with the measurement objective of the applicable financial reporting framework and are appropriate in the circumstances.

Significant Assumptions

18. In responding to the assessed risks of material misstatement identified in accordance with paragraph 13, the auditor shall, when the accounting estimate makes use of significant assumptions, obtain evidence about:

    (a) whether the significant assumptions selected for use:

        (i) are appropriate in the context of the measurement objectives and other requirements of the applicable financial reporting framework and changes from previous periods, when applicable, are appropriate;

        (ii) gives rise to indicators of possible management bias;

    (b) whether the integrity of significant assumptions has been maintained in applying the method;

    (c) whether significant assumptions are consistent with each other and with those used in other accounting estimates or with assumptions used in other areas of the entity's business activities; and

    (d) when relevant to the appropriateness of the significant assumptions or the appropriate application of the requirements of the applicable financial reporting framework, whether management has the intent to carry out specific courses of action and has the ability to do so.

Significant Data

18A. In responding to the assessed risks of material misstatement identified in accordance with paragraph 13, the auditor shall, when the accounting estimate makes use of significant data, obtain evidence about:

    (a) whether the significant data selected for use:

        (i) is appropriate in the context of the measurement objectives and other requirements of the applicable financial reporting framework and changes, when applicable, from previous periods are appropriate;

        (ii) gives rise to indicators of possible management bias;

        (iii) is relevant and reliable;

    (b) whether management has appropriately understood or interpreted significant data, including with respect to contractual terms; and

    (c) whether the integrity of significant data has been maintained in applying the method.

Estimation Uncertainty

19. ~~In complying with paragraph 15(b), when the reasons for the assessment given to the risk of material misstatement include estimation uncertainty:~~ In responding to the assessed risks of material misstatement identified in accordance with paragraph 13, when the accounting estimate is subject to estimation uncertainty the auditor shall:

    (a) ~~The auditor shall o~~Obtain sufficient appropriate audit evidence about whether, in the context of the applicable financial reporting framework:

        (i) Management has taken appropriate steps to understand and address the estimation uncertainty, and develop a point estimate that meets the measurement objective; and (Ref: Para. A113–A115)

        (ii) Management's point estimate ~~is reasonable,~~ and ~~the~~ related disclosures ~~in the financial statements~~ that describe the estimation uncertainty are reasonable. (Ref: Para. A116–A125)

    (b) When, based on the audit evidence obtained, in the auditor's judgment, management has not appropriately ~~understood and~~ addressed the estimation uncertainty, the auditor shall, to the extent possible, develop an auditor's point estimate or range to enable the auditor to evaluate the reasonableness of management's point estimate and the related disclosures in the financial statements that describe the estimation uncertainty. (Ref: Para A126–A134)

~~20. If the auditor concludes that it is appropriate to develop an auditor's range, the auditor shall only include in that range amounts that:~~

    ~~(a) Are supported by the audit evidence; and~~

    ~~(b) The auditor has evaluated to be reasonable in the context of the measurement objectives and other requirements of the applicable financial reporting framework.~~ *[Now addressed through paragraph 19B]*

External information sources

19A. When management makes use of information from an external information source, the auditor shall consider the relevance and reliability of the information to be used as audit evidence as required by ISA 500[3].

Developing a point estimate or range

19B. When developing a point estimate or range based on available audit evidence to evaluate management's point estimate, the auditor shall:

    (a) when using some or all of the auditor's own methods, data or assumptions to develop an expectation of the accounting estimate, or range, for comparison to the entity's accounting estimate:

        (i) Have a reasonable basis for the assumptions or method used;

        (ii) Evaluate the relevance and reliability of any data or assumptions obtained from an external information source in accordance with ISA 500.

[3] Proposed ISA 500 (Revised) paragraph 7

		(b) when using the entity's methods, or using data produced by the entity or significant assumptions used by the entity, obtain evidence about the matters in paragraphs 17-19A, as applicable. **Disclosures Related to Accounting Estimates** 21. The auditor shall obtain sufficient appropriate audit evidence about whether the disclosures related to accounting estimates are reasonable in accordance with ~~the context of~~ the requirements of the applicable financial reporting framework including: (Ref: Para. A135–A138) (a) In the case of a fair presentation framework, whether management has provided the disclosures beyond those specifically required by the framework that are necessary to achieve the fair presentation of the financial statements as a whole, or (b) In the case of a compliance framework, whether the disclosures are those that are necessary for the financial statements not to be misleading. **Overall Evaluation Based on Audit Procedures Performed** 22. ~~In applying ISA 330 to each accounting estimate for which the auditor's further audit procedures are required to address the matters in paragraphs 17–19, t~~The auditor shall evaluate for each accounting estimate, based on the audit procedures performed and audit evidence obtained, whether: (Ref: Para A139–A141) (a) The assessments of the risks of material misstatement at the assertion level remain appropriate~~, including when indicators of possible management bias have been identified~~; (b) Sufficient appropriate audit evidence has been obtained; and (c) Management's decisions relating to the recognition, measurement, presentation and disclosure of the~~se~~ accounting estimate~~s~~ in the financial statements are in accordance with the applicable financial reporting framework. 23. Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate, for each accounting estimate, whether the accounting estimate~~s~~ and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated. In making this evaluation, the auditor shall consider all relevant audit evidence obtained whether corroborative or contradictory. If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall evaluate the implications for the audit. (Ref: Para. A2, A142–A146) **Indicators of Possible Management Bias** 24. The auditor shall evaluate whether judgments and decisions made by management in making the accounting estimates included in the financial statements~~, even if they are individually reasonable,~~ indicate possible bias on the part of the entity's management, when assessing the financial statements as a whole. When indicators of possible bias are identified, the auditor shall evaluate the implications for the auditor's risk assessment and responses, in accordance with paragraph 22, and take this into account when evaluating whether the financial statements as a whole are free from material misstatement in accordance with ISA 700 (Revised) ~~audit~~. (Ref: Para. A147–A152)

		Written Representations 25. The auditor shall obtain written representations from management and, when appropriate, those charged with governance that they believe the methods, significant data, and significant assumptions used in making the accounting estimates and their related disclosures are appropriate to achieve recognition, measurement or disclosure ~~that is reasonable~~in accordance with ~~the context of~~ the applicable financial reporting framework. The auditor shall also consider the need to obtain representations about specific accounting estimates, including in relation to the methods, assumptions, or data used. (Ref: Para. A153–A154) **Communication with Those Charged With Governance or Management** 26. In applying ISA 260 (Revised) and ISA 265, the auditor is required to communicate with those charged with governance or management about certain matters, including significant qualitative aspects of the entity's accounting practices and significant deficiencies in internal control, respectively. In doing so, the auditor shall consider the matters, if any, to communicate related to the extent to which the accounting estimates and their related disclosures are affected by, or subject to, complexity, the need for the use of judgment by management, estimation uncertainty, or other relevant factors. (Ref: Para. A155–A157) **Documentation** 27. The audit documentation shall include: (a) The basis for the auditor's evaluation of the reasonableness of the accounting estimates and related disclosures; and (b) Indicators of possible management bias, if any, and the auditor's evaluation thereof in forming the auditor's opinion on whether the financial statements as a whole are materially misstated. (Ref: Para. A158–A159)
Member Bodies and Other Professional Organizations		
9.	ICAEW	MORE DETAILED DRAFTING COMMENTS 73. Changes in estimates: the current requirement to determine whether changes in estimates or methods from the prior period are appropriate does not appear to be fully replicated in the ED. 18(a) (ii) deals with the appropriateness of changes in methods, significant data or assumptions, but only where judgement is a factor. This is a critical area in practice and we do not believe that IAASB would want to be perceived as downgrading the extant requirement, especially given the relative lack of emphasis of significant risks which is also open to misinterpretation. 74. The proposed reference to ISA 265 and the auditor's responsibility to report on deficiencies in internal controls in paragraph 26 is useful.

		75. A95 states that the ISA does not require an assessment of IR. Paragraph 15 does require this. This appears to be an error. 76. 20A could make it clearer that it is intended to refer to audit evidence already obtained, not new evidence, if that is the case. 77. A35: this should read: 'For example, an accounting estimate may be applied by applying a method that uses several data sets and several assumptions'. 78. A62 suggests a retrospective review performed for estimates made over several periods or shorter periods but the related requirement only relates to the previous period. We believe that the requirements should also refer to one or more, or shorter periods, because a more useful history of estimates will emerge over a longer time period. 79. Critical accounting judgements and sources of estimation uncertainty are not distinguished in A112, which is unhelpful as financial reporting frameworks emphasise the difference. 80. The application material dealing with the assessment of differences between management and auditor ranges does not deal with bias in terms of aggressiveness, which is critical in practice. 81. The flowchart supplement illustrating the work effort requirements is helpful. IAASB should consider including it as an appendix to the revised standard. 82. Paragraph 19 in Appendix 1 on measurement bases for fair values ignores the fact that some frameworks define fair value in a different way, such as FRS 102 under UK GAAP which has the old IFRS definition. 83. Appendices 1 and 2 contain useful material relevant to the application of the ISA and should be retained as part of the ISA. Comments with particular relevance to the audit of ECL

		84. The application material on management's point estimate, 9(e), and on 17(a) and (b) on complexity, is limited. Ditto 17(e), 18(a)(iii), 18(c) (i) and (ii). 85. The extent and depth of the required auditor understanding of applicable regulatory factors are not made clear in A15. 86. There is a lack of application material addressing the audit of mid-sized entities. These are critical in the financial sector which has many, including smaller investment businesses and banks, which are nonetheless PIEs. 87. A30 on auditing policy is light in relation to issues such as changes in credit risk, ditto A31 on model validation. 88. A73 is simplistic as a bank does not need to be active internally for ECL to be complex, subject to estimation uncertainty and involve judgement. 89. A76 and A77 are insufficiently granular for the audit of ECL. 90. A86 can be read as implying seems to imply that estimation and judgemental differences are not misstatements, only known and factual ones are. The sentence beginning 'The variation in the measurement of an accounting estimate…' should perhaps state 'The variation in the measurement of an accounting estimate that results from estimation uncertainty is not necessarily, in itself, a misstatement'. 91. Paragraph A104 is light in terms of ensuring that appropriate data is used in a model and assessing the appropriateness of management assumptions.
10.	SAICA	D. EDITORIAL AND OTHER COMMENTS ON SPECIFIC PARAGRAPHS 87. Paragraph 13 makes reference to ISA 315 (Revised) without a specific paragraph reference in a footnote for the auditor to cross-reference to. Paragraphs A48 and A76 makes reference to specific paragraphs in ISA 315 (Revised) instead of using a footnote. Paragraph A50 makes no reference to ISA 315 but includes a footnote.

		Paragraphs 15, A94, A95 and A96 make reference to ISA 330 without a specific paragraph reference in a footnote for the auditor to cross-reference to. Paragraph A151 refers to ISA 700 (Revised) without a specific paragraph reference in a footnote for the auditor to cross-reference to. We suggest that referencing in the ED to other ISAs should be aligned to the referencing in all other ISAs. 88. We suggest that the words 'also is' in paragraphs 5, A113 and A116 should be changed to 'is also', similarly the words 'also may' in paragraphs A11, A99, A120, A122, A132, A133, A144 and the conforming amendment to ISA 260.A20 should be changed to 'may also'. 89. Paragraph A135 states that paragraph 21 applies regardless of whether the auditor is required to perform procedures under paragraph 19. It is not clear why paragraph 19 is referred to. It is suggested that either the correctness of the reference is considered or the paragraph should be deleted. 90. Paragraph 25 requires the auditor to obtain written representations regarding 'significant' data and 'significant' assumptions. We believe that 'significant' should be deleted to require the auditor to obtain written representation from management and those charged with governance for selected data and selected assumptions used in making the accounting estimate (this will be consistent with the wording used in paragraph 10(e)).
11.	SMPC	More detailed drafting comments In general, the new appendices were considered helpful with the information better placed there than in application material. However, the status must be very clear and be referred to in the introduction. The IAASB could consider publishing this separately from the standard, especially given the overall length. The application material is lengthy and reads more like a textbook than implementation guidance. Such material is valuable, but IAASB must consider going forward whether this type of material should be supplied in another form to those auditors who wish to have a comprehensive reference. We do not comment on the entire application material, but point to selected instances where we believe the IAASB could make further changes: • Some material could arguably be more appropriately placed in the introduction. For example, part of paragraph A7 is relevant to the paragraph 5.

		• We also note instances of departure from the IAASB's stated drafting conventions. For example paragraph A9 reads as though it is a part of the requirement of paragraph 10. • Some material in the ED appears to be nonessential or superfluous. For example, paragraph A13 does not add value to the Standard. • Inconsistency between regulatory requirements and the requirements of the applicable financial reporting framework may not indicate risks of material misstatements as they may not be comparable. Further explanation could be needed in A15. • The inclusion of A44 and considerations specific to smaller entities should be earlier in the standard. We suggest in the preamble prior to paragraph 10, rather than 10 (e) (iv). • The guidance in A43 could provide instances when management does not have an expert – it should not only apply to anything that requires an expert. In addition, the use of an expert in a valuation should not in itself necessarily result in the assessment of inherent risk other than low. • The guidance in A75 could be particularly helpful for SMPs who may well be conducting audits at a point in time when information is known, but it is currently difficult to understand. It could be made much clearer that it is intended to assist when the outcome of an accounting estimate became known during the audit and the inherent risk was assessed as not low during the planning stage. Furthermore, the use of "when relevant" could be seen as superfluous.