Supplement B to Agenda Item 2

Comparison of Current Draft of Proposed ISA 540 (Revised) with ED-540 – Requirements

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Scope of this ISA	
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 315 (Revised),[1] ISA 330,[2] ISA 500[3] 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.	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 includes requirements and guidance that expand on how ISA 315 (Revised),[4] ISA 330,[5] ISA 450,[6] ISA 500[7] and other relevant ISAs are to be applied in relation to accounting estimates. It also deals with the evaluation of misstatements of accounting estimates and related disclosures, and indicators of possible management bias.
Nature of Accounting Estimates	
2. Many financial statement items are susceptible to an inherent lack of precision in their measurement, which is referred to as estimation uncertainty. In the ISAs, such financial statement items are referred to as accounting estimates. Accounting estimates vary widely in nature, and their measurement may also be subject to, or affected by, complexity and the need for the use of judgment by management. The extent to which they are subject to or affected by complexity and judgment is	2. Many financial statement items are susceptible to an inherent lack of precision in their measurement, which is referred to as estimation uncertainty. In the ISAs, such financial statement items are referred to as accounting estimates. (Ref: Para. A1)

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

2 ISA 330, *The Auditor's Responses to Assessed Risks*

3 ISA 500, *Audit Evidence*

4 ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

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

6 ISA 450, *Evaluation of Misstatements Identified during the Audit*

7 ISA 500, *Audit Evidence*

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often related closely to the extent to which they are subject to or affected by estimation uncertainty. Accordingly, the auditor's identification and assessment of the risks of material misstatement relating to accounting estimates, and the auditor's responses to those assessed risks are affected by these three factors, and the interrelationship among them. (Ref: Para: A1, Appendix 1, Appendix 2)	
	2A. Accounting estimates vary widely in nature. The measurement objectives and other requirements of the applicable financial reporting framework, and the possible methods, data sources and types of assumptions that could be used to make an accounting estimate, may involve complexity and subjectivity. This may give rise to variation in the possible outcomes of the measurement process. (Ref: Para. A1A–A1H, Appendix 1, Appendix 2)
3. When an accounting estimate is being made, its susceptibility to misstatement may increase because of the need to: (a) With respect to complexity: (i) Apply appropriate specialized skills or knowledge in the selection, design or application of the method used to make the accounting estimate, including when the method involves complex modelling. (ii) Appropriately consider the relevance and reliability of the data used, whether the data is obtained from internal sources or from external information sources. (iii) Maintain the integrity of the data used.	

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(b) With respect to the use of judgment by management: (i) Appropriately take into account available information when selecting methods, assumptions, or data. (ii) Mitigate the risk of management bias. (c) With respect to estimation uncertainty: (i) Take appropriate steps to address estimation uncertainty. (ii) Select an appropriate management point estimate or make appropriate related disclosures in the financial statements.	
Key Concepts of This ISA	
4. 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 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.	3A. This ISA recognizes that there is a spectrum of inherent risk relating to accounting estimates. Depending on the nature of a particular accounting estimate, its susceptibility to misstatement may be affected, to a greater or lesser degree, by estimation uncertainty, subjectivity, complexity or other inherent risk factors and the interrelationship among them. The degree to which the susceptibility to misstatement is affected by inherent risk factors influences the auditor's separate assessment of inherent risk for an accounting estimate, including where that assessment falls along the spectrum of inherent risk. (Ref: Para. A1I-A1P, Appendix 2)
	3B. The entity's system of internal control relating to accounting estimates is likely to be designed and implemented in a manner that responds to the susceptibility to misstatement. Accordingly, the auditor's consideration of control risk affects the assessment of the risks of material misstatement, and the auditor's planned reliance on relevant

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	controls in testing the accounting estimate. (Ref: Para. A1L-A1M)
	4. This ISA emphasizes that the auditor's further audit procedures (including, where appropriate, tests of relevant controls) need to be responsive to the assessment of risks of material misstatement at the assertion level, considering whether the reasons for the assessment given to those risks relate to one or more inherent risk factors.
5. 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 risk of management bias affecting accounting estimates due to their subjective, potentially complex and uncertain nature.	5. The exercise of professional skepticism by the auditor is particularly important to the auditor's work relating to accounting estimates because of the potential for management bias due to their subjective, potentially complex and uncertain nature.
6. 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. (Ref: Para. A2–A3).	6. This ISA requires the auditor to evaluate, based on the audit procedures performed and the audit evidence obtained, whether the accounting estimates and related disclosures are reasonable[8] in the context of the applicable financial reporting framework or are misstated. For purposes of this ISA, reasonable, in the context of the applicable financial reporting framework, means that all the relevant requirements of the applicable financial reporting framework have been applied appropriately, including those that address: • The making of the accounting estimate, including the selection of the method, assumptions and data from available alternatives in view of the nature of the accounting estimate and the facts and circumstances of the entity; • The selection of a management's point estimate that is representative of the range of reasonably possible outcomes of the measurement process; and

8 See also ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 13(c).

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	• The disclosures about the accounting estimate, including disclosures about how the accounting estimate was developed and that explain the nature, extent, and sources of estimation uncertainty. (Ref: Para. A1Q–A3).
Effective Date	
7. This ISA is effective for audits of financial statements for periods beginning on or after [TBA].	7. This ISA is effective for audits of financial statements for periods ending on or after December 15, 2019.
Objective	
8. The objective of the auditor is to obtain sufficient appropriate audit evidence about whether: (a) Accounting estimates, whether recognized or disclosed in the financial statements; and (b) Related disclosures in the financial statements, are reasonable in the context of the applicable financial reporting framework.	8. The objective of the auditor is to obtain sufficient appropriate audit evidence about whether accounting estimates and related disclosures in the financial statements are reasonable in the context of the applicable financial reporting framework.
Definitions	
9. For purposes of the ISAs, the following terms have the meanings attributed below: (a) Accounting estimate – A monetary amount, prepared in accordance with the requirements of the applicable financial reporting framework, the measurement of which is subject to estimation uncertainty. (Ref: Para. A4) (b) Auditor's point estimate or auditor's range – An amount, or range of amounts, respectively, developed by the auditor in evaluating management's point estimate. (Ref: Para. A5)	9. For purposes of the ISAs, the following terms have the meanings attributed below: (a) Accounting estimate – A monetary amount the measurement of which, in accordance with the requirements of the applicable financial reporting framework, is subject to estimation uncertainty. (Ref: Para. A4) (b) Auditor's point estimate or auditor's range – An amount, or range of amounts, respectively, developed by the auditor in evaluating management's point estimate. (Ref: Para. A5)

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(c) Estimation uncertainty – The susceptibility of an accounting estimate to an inherent lack of precision in its measurement. (Ref: Para. A6) (d) Management bias – A lack of neutrality by management in the preparation of information. (Ref: Para. A7) (e) Management's point estimate – The amount selected by management for recognition or disclosure in the financial statements as an accounting estimate. (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. (Ref: Para A8)	(c) Estimation uncertainty – Susceptibility to an inherent lack of precision in measurement. (Ref: Para. A6, Appendix 2) (d) Management bias – A lack of neutrality by management in the preparation of information. (Ref: Para. A7) (e) Management's point estimate – The amount selected by management for recognition or disclosure in the financial statements as an accounting estimate. (f) Outcome of an accounting estimate – The actual monetary amount that results from the resolution of the transaction(s), event(s) or condition(s) addressed by an accounting estimate. (Ref: Para. A8)
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),[9] the auditor shall obtain an understanding of the following: (Ref: Para. A9–A10) (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.[10] (Ref: Para. A14–A15)	10. When obtaining an understanding of the entity and its environment and the system of internal control, as required by ISA 315 (Revised),[12] in relation to the entity's accounting estimates, the auditor shall obtain an understanding, to the degree relevant in the circumstances, of the following matters: (Ref: Para. A8A–A10A) The Entity and Its Environment (a) [Previously 10(c)] The entity's transactions and other events and conditions that may give rise to the need for, or changes in, accounting estimates to be recognized or disclosed in the financial statements. (Ref: Para. A10B) (b) The requirements of the applicable financial reporting framework, including the recognition criteria, measurement bases,

9 ISA 315 (Revised), paragraphs 5–6 and 11

10 ISA 315 (Revised), paragraph 11(a)

12 ISA 315 (Revised), paragraphs 3, 5–6, 9, 11–12, 15-17, and 20-21

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(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) (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	and the related presentation and disclosure requirements. (Ref: Para. A11–A11A) (c) Regulatory factors relevant to the entity's accounting estimates. (Ref: Para. A14) (d) The nature of the accounting estimates and related disclosures that the auditor would expect to be included in the entity's financial statements, based on the auditor's understanding of the matters in 10(a)–(c) above. (Ref: Para. A16) The Entity's System of Internal Control Relevant to the Audit *Control Environment* (e) The nature and extent of oversight and governance that the entity has in place over management's process for making accounting estimates. (Ref: Para. A17A–A17C). (f) How management identifies the need for, and applies, specialized skills or knowledge related to accounting estimates, including with respect to the use of a management's expert. (Ref: Para. A17D) *Management's Risk Assessment Process* (h) How estimation uncertainty, complexity, subjectivity or other inherent risk factors are taken into account in making the accounting estimates, including how susceptibility to management bias is identified and addressed. (Ref: Para. A17E–A17G) *The Information System Relevant to Financial Reporting* (i) How management makes accounting estimates, including how management: (Ref: Para. A25–A25A) (i) Identifies transactions and other events and conditions that give rise to the need for, or changes in, accounting estimates to be recognized

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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) (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 internal control as they relate to making accounting estimates.[11] (Ref: Para. A48–A60)	or disclosed in the financial statements and related disclosures; (ii) Identifies the relevant methods, assumptions or sources of data, and the need for changes in them, that are appropriate in the context of the applicable financial reporting framework, including how management: (Ref: Para. A25B–A25D) a. Selects or designs, and applies, the methods used, including the use of models; (Ref: Para. A26–A30) b. Selects the assumptions to be used, including consideration of alternatives, and identifies significant assumptions; (Ref: Para. A33–A38); and c. Selects the data to be used and identifies significant data; (Ref: Para. A41) (iii) Understands the degree of estimation uncertainty associated with accounting estimates, including through considering the range of possible measurement outcomes; and (iv) Selects a point estimate and related disclosures for inclusion in the financial statements. (Ref: Para. A57) *Control Activities Relevant to the Audit* (ia) Controls relating to management's process for making accounting estimates (see paragraph 10(i)). (Ref: Para. A58–A58D) (j) How management reviews the outcome(s) of previous accounting estimates and responds to the results of that review.

11 ISA 315 (Revised), paragraphs 14–24

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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)	11. The auditor shall review the outcome of previous accounting estimates, 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)
12. 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. (Ref: Para. A67–A70)	12. The auditor shall determine whether specialized skills or knowledge are required to perform the risk assessment procedures, to identify and assess the risks of material misstatement, to design and perform audit procedures to respond to those risks, or to evaluate the audit evidence obtained. (Ref: Para. A67–A69)
Identifying and Assessing the Risks of Material Misstatement	
13. In applying ISA 315 (Revised), the auditor is required to identify and assess the risks of material misstatement, at the financial statement and assertion levels, and to determine 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, 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)	13. In identifying and assessing the risks of material misstatement relating to an accounting estimate and related disclosures at the assertion level, as required by ISA 315 (Revised),[13] the auditor shall separately assess inherent risk and control risk, taking into account: (Ref: Para. A1P, A71–A75A) (a) The degree to which the accounting estimate is subject to estimation uncertainty; and (Ref: Para. A75B–A75E) (b) The degree to which complexity, subjectivity, or other inherent risk factors affect: (i) The selection and application of the methods, assumptions and data in making the accounting estimate; or

[13] ISA 315 (Revised), paragraph 25 and 26

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(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)	(ii) The selection of management's point estimate and related disclosures for inclusion in the financial statements. (Ref: Para. A79–A92A)
	13A. The auditor shall determine whether any of the risks of material misstatement identified in accordance with paragraph 13 are, in the auditor's judgment, a significant risk.[14] If the auditor has determined that a significant risk exists, the auditor shall obtain an understanding of the entity's controls, including control activities, relevant to that risk.[15] (Ref: Para. A92C)
Responses to the Assessed Risks of Material Misstatement	
14. In responding to the assessed risks of material misstatement related to accounting estimates, the auditor shall determine whether specialized skills or knowledge are	[Now combined with paragraph 12]

[14] ISA 315 (Revised), paragraph 27

[15] ISA 315 (Revised), paragraph 29

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required to design and perform audit procedures, or to evaluate the results of those procedures. (Ref: Para. A67–A70)	
15. In applying ISA 330, the auditor is required to design and perform further audit procedures to respond to the assessed risks of material misstatement, including significant risks, at the assertion level. In doing so: (Ref: Para A94–A95) (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	15. As required by ISA 330,[16] the auditor’s further audit procedures shall be responsive to the assessed risks of material misstatement[17] at the assertion level, considering the reasons for the assessment given to those risks, and shall include one or more of the following approaches: (a) Determining whether events occurring up to the date of the auditor’s report provide audit evidence regarding the accounting estimate (see paragraph 17); (b) Testing how management made the accounting estimate (see paragraphs 17A-17F); or (c) Developing an auditor’s point estimate or range based on available audit evidence to evaluate management’s point estimate and related disclosures about estimation uncertainty (see paragraphs 18-18C). The auditor’s further audit procedures shall take into account that the higher the assessed risk of material misstatement, the more persuasive the audit evidence needs to be.[18] The auditor shall design the further audit procedures to seek audit evidence from relevant sources, regardless of whether such audit evidence is evaluated to be corroborative or contradictory. (Ref: Para. A92D–A94)

16 ISA 330, *The Auditor’s Responses to Assessed Risks*, paragraphs 6-15 and 18

17 ISA 330, paragraphs 6-7 and 21

18 ISA 330, paragraph 7(b)

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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.[19] (Ref: Para A98–A100)	16. As required by ISA 330,[20] the auditor shall design and perform tests of relevant controls to obtain sufficient appropriate audit evidence as to their operating effectiveness, if: (a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively, or (b) Substantive procedures alone cannot provide sufficient appropriate audit evidence about those risks. The auditor's design and performance of tests of relevant controls shall be responsive to the reasons for the assessment given to the risks of material misstatement. The auditor also shall take into account that the greater the reliance the auditor places on the effectiveness of a control, the more persuasive the audit evidence needs to be.[21] (Ref: Para. A97A–A99)
	16A. For a significant risk relating to an accounting estimate, the auditor's further audit procedures shall include tests of relevant controls in the current period if the auditor plans to rely on those controls, and tests of details when the approach consists only of substantive procedures.[22]
Note to IAASB CAG: The IAASB changed the structure of the work effort section below so that it follows an approach to auditing accounting estimates that is more closely aligned with the way management makes accounting estimates and how extant ISA 540 is structured. Under the new structure, the response to the assessed risks of material misstatement is driven by the selected testing strategy. For each of the testing	

19 ISA 330, paragraph 8

20 ISA 330, paragraph 8

21 ISA 330, paragraph 9

22 ISA 330, paragraphs 15 and 21

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strategies, objectives-based requirements are structured around methods, assumptions and data. The objectives-based procedures that were included in ED-540 have been incorporated under this new structure with some changes in response to comments received on ED-540.	
Complexity 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, the auditor shall obtain sufficient appropriate audit evidence about the following matters: (Ref: Para A101–A104) (a) Whether the method, and significant data and significant assumptions, are appropriate in the context of the applicable financial reporting framework; (b) Whether significant data is relevant and reliable.[23] (c) Whether management has appropriately understood or interpreted significant data, including with respect to contractual terms. (Ref: Para. A105) (d) Whether the integrity of significant data and significant assumptions has been maintained in applying the method; and (Ref: Para. A106) (e) Whether the calculations are mathematically accurate and appropriately applied. *Judgment* 18. In complying with paragraph 15(b), when the reasons for the assessment given to the	*Determining Whether Events Occurring up to the Date of the Auditor's Report Provide Audit Evidence Regarding the Accounting Estimate* 17. When the auditor's further audit procedures include obtaining evidence about events occurring up to the date of the auditor's report, the auditor shall evaluate whether the audit evidence: (a) is sufficient and appropriate to address the risks of material misstatement at the assertion level relating to the accounting estimate, and (b) supports or contradicts relevant assertions relating to the accounting estimate, taking into account that changes in circumstances and other relevant conditions between the event and the measurement date may affect its relevance to the accounting estimate at the measurement date. (Ref: Para. A100A–A100F) *Testing How Management Made the Accounting Estimate* 17A. When the auditor's further audit procedures include testing how management made the accounting estimate, the nature, timing, and extent of those further audit procedures shall be designed and performed, in accordance with paragraphs 17B to 17F, to obtain sufficient appropriate audit evidence about: (a) The selection and application of methods, assumptions and data used by management in making the accounting estimate, and (b) How management selected the point estimate and disclosures to be included in the financial statements. (Ref: Para. A100G-A100H)

[23] ISA 500, paragraph 7

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risk of material misstatement include the need for the use of judgment by management, the auditor shall obtain sufficient appropriate audit evidence about the following matters: (a) When the accounting estimate involves the use of significant data or significant assumptions: (i) Whether management's judgments regarding the selection and use of the method and the significant data and significant assumptions: (Ref: Para A107) a. Are appropriate in the context of the measurement objectives and other requirements of the applicable financial reporting framework; or b. Give rise to indicators of possible management bias. (ii) Whether management's judgments about changes from previous periods in the method or the significant data or significant assumptions, are appropriate (Ref: Para. A108–A110). (iii) 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. (b) When relevant to the appropriateness of the significant assumptions or the appropriate	Methods 17B. With respect to the methods used by management to make the accounting estimate, the auditor shall obtain sufficient appropriate audit evidence about: (a) Whether the method selected is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate; (Ref: Para. A101–A107) (b) Whether the calculations are mathematically accurate and appropriately applied; (c) When management's application of the method involves complex modelling, whether judgments have been applied consistently and whether, when applicable: (i) The design of the model meets the measurement objective of the applicable financial reporting framework, is appropriate in the circumstances, and, if applicable, changes from the previous period's model are appropriate in the circumstances; and (ii) Adjustments to the output of the model are consistent with the measurement objective of the applicable financial reporting framework and are appropriate in the circumstances; (Ref: Para. A108C–A108D) (d) Whether the integrity of significant assumptions and significant data has been maintained in applying the method. Ref: Para. A108E) Significant Assumptions 17C. With respect to the significant assumptions selected by management, the auditor shall obtain sufficient appropriate audit evidence about: (a) Whether the significant assumptions: (i) Are appropriate in the context of the

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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. (Ref: Para. A111); (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. (Ref: Para A112) *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: (a) The auditor shall obtain sufficient appropriate audit evidence about whether, in the context of the applicable financial reporting framework:	requirements of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate; and (ii) Give rise to indicators of possible management bias; (Ref: Para. A108F–A109) (b) Whether significant assumptions are consistent with each other and with those used in other accounting estimates, or with related assumptions used in other areas of the entity's business activities; (c) 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. (Ref: Para. A111) Significant Data 17D. With respect to the significant data used by management, the auditor shall obtain sufficient appropriate audit evidence about: (a) Whether the significant data selected for use: (i) Is appropriate in the context of the requirements of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate; (ii) Gives rise to indicators of possible management bias; and (iii) Is relevant and reliable in the circumstances; (Ref: Para. A111A) (b) Whether management has appropriately understood or interpreted significant data, including with respect to contractual terms. (Ref: Para. A111C) Management's Selection of a Point Estimate and Related

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(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 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	Disclosures 17E. The auditor shall obtain sufficient appropriate audit evidence about whether, in the context of the applicable financial reporting framework: (a) Management has taken appropriate steps to understand and address the estimation uncertainty, and to develop a point estimate that meets the measurement objective; and (Ref: Para. A113) (b) Management's point estimate and the disclosures in the financial statements that describe the estimation uncertainty are reasonable in the context of the applicable financial reporting framework. (Ref: Para. A116–A125) 17F. When, in the auditor's judgment based on the audit evidence obtained, management has not appropriately understood and addressed the estimation uncertainty, the auditor shall: (a) Evaluate whether a deficiency in internal control exists and, if so, communicate in accordance with ISA 265.[24] (b) Request management to consider alternative assumptions or perform sensitivity analyses, or provide additional disclosures relating to the estimation uncertainty, and evaluate management's response in accordance with paragraph 17E; and (c) If, based on management's response to the auditor's request, the auditor determines that management still has not appropriately understood and addressed the estimation uncertainty, 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

[25] ISA 500, paragraph 7

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requirements of the applicable financial reporting framework.	uncertainty. (Ref: Para. A126A–A126B) *Developing an Auditor's Point Estimate or Range Based on Available Audit Evidence to Evaluate Management's Point Estimate and Related Disclosures About Estimation Uncertainty* 18. When the auditor's further audit procedures include developing a point estimate or range to evaluate management's point estimate, the auditor shall take into account the requirements of the applicable financial reporting framework and the auditor's understanding of the process used by management to make the accounting estimate. (Ref: Para. A126C–A134) 18A. If the auditor's point estimate or range is developed using the auditor's own methods, assumptions or data, the auditor shall: (a) Obtain sufficient appropriate audit evidence to enable the auditor to evaluate whether the methods, assumptions or data used are appropriate in the context of the applicable financial reporting framework, including with respect to the matters in paragraphs 17B-17D, as applicable; and (b) Consider the relevance and reliability of data obtained from an external information source.[25] 18B. When the auditor uses management's methods, assumptions or data in developing a point estimate or range to evaluate management's point estimate and related disclosures in the financial statements, the auditor shall obtain sufficient appropriate audit evidence in accordance with paragraphs 17B-17D to evaluate whether management's methods, assumptions or data are appropriate. 18C. If the auditor develops an auditor's range, the auditor shall determine that: (a) All amounts included that range are supported by sufficient appropriate audit

[25] ISA 500, paragraph 7

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	evidence, and have been evaluated by the auditor to be reasonable in the context of the measurement objectives and other requirements of the applicable financial reporting framework; and (b) Management's point estimate and the disclosures in the financial statements that describe the estimation uncertainty are reasonable in the context of the applicable financial reporting framework.
	Other Considerations Relating to Audit Evidence 18D. If information from an external information source or information prepared using the work of a management's expert is to be used as audit evidence, the auditor shall comply with the relevant requirements in ISA 500.[26] (Ref: Para. A134A–A134C)
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 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.	21. The auditor shall obtain sufficient appropriate audit evidence about whether the disclosures related to an accounting estimate are reasonable in the context of the requirements of the applicable financial reporting framework, including: (Ref: Para. A138–A138A) (a) In the case of a fair presentation framework, whether management has included 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.

[26] ISA 500, *Audit Evidence*, paragraphs 7 and 8

<table>
<tr><th>ED-540</th><th>Current Draft of Proposed ISA 540 (Revised)</th></tr>
<tr><td colspan="2">Overall Evaluation Based on Audit Procedures Performed</td></tr>
<tr><td>22. In applying ISA 330[27] to each accounting estimate for which the auditor's further audit procedures are required to address the matters in paragraphs 17–19, the auditor shall evaluate, 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 these accounting estimates in the financial statements are in accordance with the applicable financial reporting framework.</td><td>22. In applying ISA 330[28] to each accounting estimate, the auditor shall evaluate, based on the audit procedures performed and audit evidence obtained, whether: (Ref: Para A138F–A139)
(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) Management's decisions relating to the recognition, measurement, presentation and disclosure of these accounting estimates in the financial statements are in accordance with the applicable financial reporting framework; and
(c) Sufficient appropriate audit evidence has been obtained.</td></tr>
<tr><td></td><td>22A. In making the evaluation required by paragraph 22(c), the auditor shall take into account all relevant audit evidence obtained, whether corroborative or contradictory.[29] If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall evaluate the implications for the audit or the auditor's opinion on the financial statements in accordance with ISA 705 (Revised).[30]</td></tr>
</table>

27 ISA 330, paragraphs 25 and 26

28 ISA 330, paragraphs 25 and 26

29 ISA 500, *Audit Evidence*, paragraph 11

30 ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

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23. Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate whether the accounting estimates 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.[31] (Ref: Para. A2, A142–A146)	23. Based on the auditor's evaluation in accordance with paragraph 22, the auditor shall evaluate whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated. ISA 450[32] provides guidance on distinguishing misstatements (whether factual, judgmental, or projected) for purposes of the auditor's evaluation of the effect of uncorrected misstatements on the financial statements. (Ref: Para. A1Q–A3, A143–A146A)
Indicators of Possible Management Bias *The paragraph that requires the auditor to evaluate whether there are indicators of possible management bias moved before the stand back requirement. For comparison purposes it has been included here.*	
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 indicators of possible bias are identified the auditor shall evaluate the implications for the audit. (Ref: Para. A147–A152)	21A. 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 management bias. When indicators of possible management bias are identified, the auditor shall evaluate the implications for the audit. (Ref: Para. A138B–A138E)
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	25. The auditor shall obtain written representations from management and, when appropriate, those charged with governance that they believe the methods, significant assumptions and significant data used in making the accounting estimates and their related disclosures are appropriate to achieve recognition, measurement or disclosure that is in accordance with the applicable financial reporting framework. The auditor shall also consider the

[31] ISA 330, paragraph 27

[32] ISA 450, *Evaluation of Misstatements Identified during the Audit*

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reasonable in 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)	need to obtain representations about specific accounting estimates, including in relation to the methods, assumptions, or data used. (Ref: Para. A153)
Communication with Those Charged With Governance or Management	
26. In applying ISA 260 (Revised)[33] and ISA 265,[34] 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)	26. In applying ISA 260 (Revised)[35] and ISA 265,[36] 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 regarding accounting estimates, taking into account whether the reasons given to the risks of material misstatement relate to estimation uncertainty, or the effects of complexity, subjectivity or other inherent risk factors in making accounting estimates and related disclosures. (Ref: Para. A155–A157)
Documentation	
27. The audit documentation shall include:[37] (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	27. The audit documentation[38] shall include the basis for the significant professional judgments relating to the auditor's evaluation of the reasonableness of the accounting estimates and related disclosures in the context of the applicable financial reporting framework, including: (a) Key elements of the auditor's understanding

33 ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 16(a)

34 ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* paragraph 9

35 ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 16(a)

36 ISA 265, paragraph 9

37 ISA 230, *Audit Documentation*

38 ISA 230, *Audit Documentation*, paragraphs 8-11, A6 and A10

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evaluation thereof in forming the auditor's opinion on whether the financial statements as a whole are materially misstated. (Ref: Para. A158–A159)	of the entity and its environment, and the system of internal control, in relation to the entity's accounting estimates, as required by paragraph 10; (b) The reasons given to the separate assessments of inherent risk and control risk for the risks of material misstatement relating to accounting estimates as required by paragraph 13; (c) For accounting estimates subject to a greater degree of estimation uncertainty, or affected to a greater degree by subjectivity, complexity, or other inherent risk factors, the auditor's rationale for selecting one or more of the approaches to testing the accounting estimate, as required by paragraph 15; (d) The auditor's response when management has not appropriately understood and addressed estimation uncertainty as required by paragraph 17F; and (e) Indicators of possible management bias related to accounting estimates, if any, and the auditor's evaluation thereof in forming the auditor's opinion as to whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. (Ref: Para. A158–A158B)