

ISA 315 (Revised)¹—Issues and Recommendations

Objective of the IAASB Discussion

The objective of this agenda item is to present the final proposed changes to ISA 315 (Revised), with conforming amendments, for approval, as set out in **Agenda Item 3-A (Introductory Paragraphs and Requirements)**, **3-B (Application and Other Explanatory Material, and Appendices)** and **3-C (Conforming Amendments)**.

I. Structure of this Paper and Format of the IAASB Discussion

1. This paper sets out the ISA 315 Task Force's (the 'Task Force') views about proposed changes to ISA 315 (Revised) Exposure Draft (ED).
2. This Agenda Item is set out as follows:
 - (a) **Section II**—Describes the overarching considerations related to the revisions to the standard as a whole.
 - (b) **Section III**—Describes the substantial changes that have been made since March 2018, and the Task Force's considerations about various matters raised for further discussion. The proposed changes to ISA 315 (Revised) have been presented in:
 - **Agenda Item 3-A**: proposed changes to the requirements, revised for comments from the March 2018 and May 2018 IAASB discussions (marked to extant ISA 315 (Revised)).²
 - **Agenda Item 3-B**: proposed changes to the application and other explanatory material, revised for comments from the March 2018 IAASB discussions (marked to extant ISA 315 (Revised)).
 - **Agenda Item 3-D**: proposed changes to requirements at June 2018 marked to March 2018 (for reference only)
 - **Agenda Item 3-E**: proposed changes to application material at June 2018 marked to March 2018 (for reference only)
 - (c) **Section IV**—Describes the Task Force views about the conforming amendments arising from proposed changes to ISA 315 (Revised) (**Agenda Item 3-C**: sets out the proposed conforming and consequential amendments, revised for comments from the May 2018 Board discussions).

At the Board meeting, after covering the general matters set out in section II of this paper (and related questions), the Task Force Chair will walk through the requirements by section, together with related application material. The Conforming Amendments will be discussed after completion of the requirements and application material.

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

² Supplemental Agenda Items, Proposed ED marked to March 2018, will also be provided.

How the Proposed Changes to ISA 315 (Revised) Address Key Matters of Public Interest and Enhance Audit Quality

3. The following sets out the key public interest matters that, in the view of the Task Force, have been proposed to address the key public interest matters highlighted in the project proposal:

Key Public Interest Matter³	Description of Changes made to address identified issues	Relevant paragraph in this Agenda Item explaining changes, with relevant reference to requirements and application material
<p>Enhancing the auditor’s approach to risk assessment in recognition of an evolving environment:</p> <ul style="list-style-type: none"> • Well informed risk assessment critical to audit quality • Understanding what can go wrong and focusing the auditor’s work effort on those areas • Recognizing evolving environment, including the entity’s and auditor’s use of technology (for example specifically addressing using data analytics for risk assessment procedures) • Clarifying when controls are relevant to the audit • Risk assessments need to be more rigorous and more comprehensive • Performing risk assessment procedures specific to the entity to support appropriate overall responses, and further audit procedures to address the assessed risks of material misstatement 	<p>Enhanced requirements and application material related to the auditor’s understanding of the entity and its environment and its applicable financial reporting framework</p>	<p>Paragraphs 41-42 Data analytics paragraphs 19-21; Appendix 3, Table 4</p>
	<p>Enhanced requirements and application material related to the auditor’s understanding of the system of internal control, including when controls are relevant to the audit and the related work effort to obtain the understanding</p>	<p>Paragraphs 43-47</p>
	<p>Clarification of the auditor’s requirements relating to identifying and assessing the risks of material misstatement, including clarification of the concept of significant risk</p>	<p>Paragraph 48-65 and definition of internal control</p>

³ As noted in the Project Proposal for the revisions of ISA 315 (Revised)

Key Public Interest Matter ³	Description of Changes made to address identified issues	Relevant paragraph in this Agenda Item explaining changes, with relevant reference to requirements and application material
<ul style="list-style-type: none"> • Clarifying significant risks so that they are more consistently identified • Clarifying the relationship between risk assessment and estimation uncertainty, complexity and judgment, and management bias. 		
Emphasis on considerations for auditing smaller and less complex entities	The Task Force has continued to focus its efforts on scalability of the standard.	Paragraphs 10-13; Appendix 3, Table 1
Developing considerations relevant to public sector entities	Enhancing the considerations for auditors with a broader public remit	Paragraphs 16-18; Appendix 3 Table 3
Enhancing the application of professional skepticism	Enhancements to drive more skeptical behavior	Paragraphs 22-23; Appendix 3, Table 5
Identifying and proposing conforming and consequential amendments to other ISAs		Paragraphs 72-76
Determining whether non-authoritative guidance or other support tools are needed.		Paragraphs 4-5

4. In its outreach efforts the Task Force continues to hear that more is needed in order to implement the changes effectively. In working through the changes to the standard, and taking into account the feedback from the Board, the ISA 315 Task Force continues to consider whether additional non-authoritative guidance should be developed (e.g., an International Auditing Practice Note, a Staff Questions and Answers (e.g., setting out the specific ‘scalability’ paragraphs within the standard), or a publication with the flowcharts described in paragraph 5). In addition to the nature and content of further guidance, the Task Force will also need to consider the timing of this as well as who will develop the material.
5. In the March 2018 IAASB discussions, and in light of the need for more regarding implementation of the changes, the Board continued to emphasize the need for flowcharts or decision trees, as it was noted that the linear order of the requirements and application material could still be confusing, and that the iterative and interactive nature of the various aspects of the standard may not be readily understandable. The Task Force has therefore developed several flowcharts, which can be found in Appendix 4,⁴ as follows:

⁴ Appendix 4 to be posted as a supplement to the Agenda Paper after the main posting.

- (a) Flowchart A – illustrates the flow of the overall standard.
 - (b) Flowchart B – illustrates how the auditor’s understanding of the entity’s system of internal control is obtained.
6. As it has progressed the changes throughout the process to develop the proposed changes to ISA 315 (Revised), the Task Force has continued its outreach with groups representing a wide range of stakeholders, including with the Forum of Firms, the International Federation of Accountants Small and medium practices Committee, national standard-setters and the International Forum of Independent Audit Regulators Standards Coordination Working Group (IFIAR SCWG). Appendix 1 sets out upcoming planned outreach before the Board discussions in June 2018. The Task Force’s member’ activities also included outreach and coordination with other IAASB Task Forces or Working Groups, including the ISA 540 Task Force⁵ and Data Analytics Working Group. Further discussion regarding the coordination with the ISA 540 Task Force can be found in paragraph 75.
7. The revisions as set out in Agenda Items 3-A and 3-B reflect significant input from a firm information technology (IT) specialist.⁶ In addition, the proposals have been reviewed by others who are also specialists in IT matters, and accordingly the changes proposed in respect of IT reflect the broader views of those involved with providing input to this project.

II. General Matters Relating to the Proposed Changes in ISA 315 (Revised)

8. In considering the changes relating to the overall presentation of the standard, changes have been made to restructure various aspects (which are explained further in this paper), as well as making sure that there is consistency in the way that the various aspects are presented. In addition, the Task Force has considered whether any of the application material is superfluous, and has agreed that two further paragraphs be moved to the Appendices,⁷ because although helpful for the auditor’s understanding of the relevant matters, it is not seen to be essential material for the implementation of the requirements. In working through the requirements and application material the Task Force has also made editorials for clarity or understandability as necessary.
9. The following describes public interest matters that are applicable to the standard more pervasively.

Scalability of ISA 315 (Revised)

10. The Task Force continues to recognize the need for balance in the standard, by providing sufficient guidance for entities of all sizes to be able to effectively apply the ISA while keeping in mind the purpose of the application and explanatory material in the international standards.
11. As noted in the Appendix of Agenda Item 1 from the May 2018 Board Teleconference, the Task Force continued to consider how to illustrate the scalability of the requirements by providing guidance within the standard for this purpose, to enable the standard to be applied to a wide variety of entities with different circumstances and complexities.

⁵ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

⁶ The firm IT specialist has a broad range of IT and auditing expertise, and is well versed in content of the ISAs, COSO 2013 and COBIT

⁷ Extant paragraphs A63 (re IT benefits) and A89b (re business risks arising from IT)

12. Based on the focused efforts of the Task Force, further changes to the application and other explanatory material have been proposed as follows:
- (a) The Task Force has agreed that the term ‘small- and medium-sized entities’ is not the only driver of scalability, and has agreed that complexity is also key to scalability. Accordingly, the Task Force has agreed to describe matters of scalability as relating to “*smaller and less complex*” entities. The Task Force debated whether the term should be smaller and less complex, or smaller or less complex, because there could be medium to large sized entities that were less complex and would therefore find the guidance helpful. On balance though, the Task Force agreed that using the term ‘smaller’ would be relative in different jurisdictions (i.e., judgment would be required about how to apply this) and consistent with the description of “smaller entity” in ISA 200.⁸ Of importance was adding an explicit reference to complexity, and therefore by using the term ‘smaller and less complex’ this captured the intended types of entities.
 - (b) Further proposed editorial changes have been considered within the examples and illustrations throughout to convey different complexities and sizes.
 - (c) The placement of matters related to scalability (i.e., for those entities that are smaller and less complex) have been advanced to the start of some sections so that auditors in a smaller and less complex environment are able to better consider the material that follows in context.
13. Appendix 3, Table 1, sets out the paragraphs that in the Task Force’s view demonstrates scalability.

Matter for IAASB Consideration

- 1. The IAASB is asked whether the changes made relating to scalability, as explained in paragraphs 10 to 13 above, will adequately illustrate how the standard is scalable in a wide variety of circumstances. Are there other changes that should be made?
- 2. What are the Board’s views about matters relating to further implementation support for the proposed changes (as set out in paragraphs 4–5), and what is the nature of such implementation guidance?

Fraud

14. Some Board members and the Public Interest Oversight Board representative emphasized the need to further consider how the auditor’s considerations about fraud were presented in ISA 315 (Revised), but the Task Force was also cautioned to not cause confusion with the fraud requirements in ISA 240.
15. In addition to adding an explicit reference to fraud in the definition of ‘inherent risk factors,’ (see paragraph 4cb of ISA 315 (Revised)) the Task Force has considered the extent of current references to fraud or ISA 240⁹ in proposed ISA 315 (Revised). Appendix 3, Table 2, sets out the specific references to fraud or ISA 240 in ISA 315 (Revised). Notwithstanding an explicit reference to ‘fraud’ as an inherent risk factor, the Task Force believes that the magnitude of these references appropriately underscore the importance of the consideration of fraud when identifying and assessing risks of material misstatement in accordance with ISA 315 (Revised). Accordingly, with the exception of changes to paragraphs A1b, A21, A49h, A89a and A100f in ISA 315 (Revised), the Task Force does not propose further changes to emphasize

⁸ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph A66

⁹ ISA 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*

fraud in ISA 315 (Revised), in particular in light of the robust requirements and guidance set out in ISA 240.

Matter for IAASB Consideration

3. The IAASB is asked, based on the explanation in paragraphs 14 to 15 above, whether further changes in respect of the auditor’s consideration of fraud in ISA 315 (revised) is needed?

Considerations Specific to Public Sector Entities

16. The Task Force has agreed that the separate paragraphs relating to “considerations specific to public sector entities” should be retained due to the broader remit of some public sector audits and the unique nature of some aspects of these entities, with further consideration given to whether any additional considerations should be added.
17. The Chair of the Task Force and Staff held a teleconference with representatives from the International Organisation of Supreme Audit Institutions (INTOSAI) Financial Audit and Accounting Sub-Group (FAAS) in May 2018 to discuss whether extant references to public sector perspectives in the application and other explanatory material of ISA 315 (Revised) remain relevant and appropriate. In addition, matters included in ISSAI¹⁰ Practice Note 1315 – this practice note provides supplementary guidance to auditors of public sector entities on the application of ISA 315 (Revised) – were also discussed for further consideration of including these matters in the ISA. The Task Force has therefore proposed additions or amendments to public sector specific paragraphs of the standard. The content of these paragraphs has also been reviewed by a representative of the INTOSAI FAAS.
18. Appendix 3, Table 3, sets out the supplementary explanatory material provided in respect of public sector audits.

Data Analytics

19. At the March 2018 IAASB meeting, the Board expressed mixed views on whether an explicit reference to ‘data analytics’ in the standard is appropriate. In further considering this, the Task Force retains the view that the term ‘data analytics’ is potentially too narrow, has different meanings to different people and may not therefore encompass all the various forms of emerging technologies that may be used in performing audit procedures and that are broader than analytics (such as robotics and drones). The Task Force refers to these types of technologies, collectively with data analytics, as automated tools and techniques. The Task Force also highlighted that the focus in the proposed standard should be on gathering sufficient appropriate audit evidence, and not on being prescriptive or limiting in terms of how that evidence is necessarily obtained. The Task Force still recognizes that references to how audit evidence is obtained, i.e., using automated tools and techniques, is essential to understanding how to apply the requirements. The Task Force also notes that the use of these automated tools and techniques have broader implications for other ISAs, especially (but not limited to) ISA 500, ISA 520 and ISA 530. Accordingly the Task Force continues to have the view that the terms for such tools and techniques should not be definitively described by the work on this project alone.
20. Notwithstanding the Task Force’s views described in the preceding paragraph, the Task Force also recognizes the view, as also expressed by the Public Interest Oversight Board observer, that the

¹⁰ The International Standards of Supreme Audit Institutions

term ‘data analytics’ is being widely used today and is generally understood to apply in a broader sense than the term may strictly otherwise suggest. The Task Force has therefore acknowledged in the proposed changes that ‘data analytics’ is a possible term that may describe the types of procedures being performed using automated tools and techniques.¹¹ In addition, the Task Force has reconsidered the proposals made in March 2018 to more fully describe the types of automated tools and techniques used, rather than attempting to label such procedures (which may be seen as a ‘definition’ and may have unintended consequences).¹²

21. Appendix 3, Table 4, sets out the paragraphs where references are made to automated tools and techniques (including data analytics).

Professional Skepticism

22. The Task Force has reconsidered how the standard has been revised to drive more skeptical behavior. The Task Force is of the view that no further enhancements are necessary, and that the standard reflects sufficient encouragement for the exercise of professional skepticism when identifying and assessing the risks of material misstatement.
23. Appendix 3, Table 5, sets out the relevant paragraphs relating to the auditor’s professional skepticism.

Matter for IAASB Consideration

4. Does the IAASB believe, based on the explanation set out in paragraphs 16 to 23 above, that changes made in respect of the public sector considerations, data analytics and professional skepticism are adequately addressed in the proposed changes?

III. Specific Matters Relating to the Proposed Changes in ISA 315 (Revised)

24. This section describes significant changes made to the requirements, and application and other explanatory material, since the March 2018 Board Agenda Papers.

Introductory Paragraphs (Requirements: paragraphs 1A–1G of ISA 315 (Revised))

25. At the March 2018 IAASB meeting, the Task Force proposed and presented to the Board the inclusion of introductory paragraphs to ISA 315 (Revised). The Board supported the inclusion of introductory paragraphs; however, concerns were expressed that these paragraphs were too complex and repetitive, and moreover, the paragraphs did not address key public interest matters such as the auditor’s consideration of fraud and the use of data analytics (an example of emerging developments in the use of technology in the performance of audit procedures, which we now refer to more generally as automated techniques and tools (see paragraph 19 above)). In addition, inconsistencies with the language in extant ISAs and the most recent draft of ISA 540 (Revised) were noted.¹³
26. The Task Force agreed that it was important to introduce key concepts in these introductory paragraphs, including describing the spectrum of inherent risk, to help with the understanding of the standard. To

¹¹ See ISA 315 (Revised), paragraph A16a

¹² See ISA 315 (Revised), paragraph A16a for an example

¹³ The Task Force continues to coordinate with the ISA 540 Task Force to align the language as much as possible. As further changes are made to ISA 540 (Revised), the ISA 315 Task Force will further consider whether changes need to be made to ISA 315 (revised), or whether further conforming amendments will be needed.

address concerns by the Board, the Task Force has revised these paragraphs, keeping in mind that it is important to capture the key principles in a clearer and more succinct manner, whilst still using language that is consistent with other ISAs. Because of the nature of the introductory paragraphs, and in keeping them focused on ‘key concepts’ in ISA 315 (Revised), the Task Force did not believe that automated tools and techniques (data analytics) should be included, as these would apply to the ISAs more broadly.

Definitions

27. The Board indicated general support for the new and revised definitions during the March 2018 meeting and the May 2018 Board call, with the exception of those described below and where changes have been made.
28. Although Board members had commented on some of the other definitions, such as controls, relevant assertions and the significant account “threshold” (reasonable possibility and more than remote), the Task Force has further considered whether changes should be made, but agreed that on balance no further changes were needed to the definitions.

Application Controls (Definition: paragraph 4(a) of ISA 315 (Revised))

29. In response to Board comments during the May 2018 Board call, the definition has been updated to include the role of application controls to support the entity’s ability to maintain the completeness and accuracy of information in the entity’s information system.

Assertions (Definition: paragraph 4(aa) of ISA 315 (Revised); Application Material – paragraph A0d–A0g of ISA 315 (Revised))

30. Concern was expressed at the March 2018 IAASB meeting that the definition of ‘assertions’ still didn’t distinguish management’s assertions from management representations in accordance with ISA 580.¹⁴
31. Further revisions to the definition of ‘assertion’ have been proposed to make clear that the assertions for the purposes of the ISAs are inherent in management’s representation that the financial statements have been prepared in accordance with the applicable financial reporting framework, and are not necessarily made explicitly.

Inherent Risk Factors (IRFs) (Definition: paragraph 4(cb) of ISA 315 (Revised); Application Material – paragraph A0d–A0g of ISA 315 (Revised))

32. At the March 2018 IAASB meeting, Board members had mixed views about the inclusion of ‘susceptibility to management bias’ (instead of susceptibility to fraud) as one of the IRFs. Some Board members supported the broadening of the concept to include unintentional aspects, while others still had the view that fraud should be more explicitly recognized in the inherent risk factors. It was also noted by some Board members that fraud does not necessarily or exclusively result from management bias.
33. On further reflection and with further coordination with the ISA 540 Task Force as discussed on the April 2018 Board call, the Task Force agreed that the inherent risk factor described as “*susceptibility to management bias*” is not the only factor that gives rise to fraud. Further, the Task Force agreed that “management bias” should remain in the description of the factor because although intentional bias gives

¹⁴ ISA 580, *Written Representations*

rise to fraud risk, unintentional bias can give rise to risk of error. As a result, the Task Force decided to revise the description of the inherent risk factor as: “*susceptibility to misstatement due to management bias or fraud.*” The Task Force added the words ‘*susceptibility to misstatement*’ because, in its view, it is important to signal that this only includes factors that affect inherent risk. It does so by mirroring language in the definition of ‘inherent risk,’ which refers to the *susceptibility to misstatement* of an assertion before consideration of controls. In contrast, if the inherent risk factor were to be articulated as ‘*the susceptibility to management bias or fraud,*’ it may also be taken to include factors that affect the control risk component of risks of material misstatement due to fraud.

34. The Task Force has also continued to coordinate with the ISA 540 Task Force as to the articulation of the inherent risk factors (with particular emphasis on the IRF relating to the susceptibility to misstatement due to management bias or fraud), and changes have been made to the descriptions of the inherent risk factors in the application material taking into account the way that these are described in proposed ISA 540 (Revised), while acknowledging that the descriptions of these factors in proposed ISA 540 (Revised) are provided in the context of accounting estimates only.
35. For discussion in March 2018, the Task Force had also proposed changes to the definition and description of IRFs to incorporate quantitative characteristics of events or conditions that may increase susceptibility to inherent risk, to respond to Board comments from the December 2017 IAASB discussions. The Board had mixed views about whether the broadening of IRFs to include quantitative aspects was appropriate or may introduce confusion. On further consideration, the Task Force agreed that it was important to keep the quantitative aspects as they are relevant to the auditor’s consideration of the susceptibility to misstatement of assertions about classes of transactions, account balances and disclosures. Further enhancements have also been made to the explanatory material as appropriate.

Significant Risks (Definition: paragraph 4(e) of ISA 315 (Revised); Application Material – paragraph A0h of ISA 315 (Revised))

36. The definition of significant risk is discussed with the requirements and application material in paragraphs 50–62.

Requirements—Risk Assessment Procedures and Related Activities (Requirements: paragraphs 5–10 of ISA 315 (Revised); Application Material – paragraphs A1–A23a of ISA 315 (Revised))

37. The Board continued to support the expansion to paragraph 5 being made to the description of the purpose of the risk assessment procedures, but asked the Task Force to further consider the use of ‘sufficient and appropriate evidence’ when describing the outcome of the procedures. While some Board members believed that the introduction of this concept would help clarify why risk assessment procedures are performed, others were not supportive of introducing the concept of evidence, as well as others who did not think that ‘sufficient and appropriate’ was needed.
38. The Task Force further deliberated the inclusion of ‘sufficient appropriate audit evidence’ in paragraph 5, and generally continue to have the view that this term is important to clarify that the purpose of obtaining the required understanding is to obtain sufficient appropriate audit evidence as the basis for the identification and assessment of risks. The inclusion of this criterion is consistent with ISA 500, which makes it clear that risk assessment procedures enable the auditor to obtain audit evidence. This has been highlighted in the application material. The Task Force believes that it is important for the auditor to have regard to both the quantity (sufficiency) and the quality (appropriateness) of the audit evidence obtained through risk assessment procedures in considering

whether that evidence provides a suitable basis for identifying and assessing risks of material misstatement. However, the Task Force did agree that this could be further clarified by highlighting that the sufficient appropriate audit evidence provides ‘the basis’ for the identification and assessment of risks of material misstatement. The Task Force also agreed that the evidence is ‘obtained’ and not ‘provided.’ Clarifications have also been made to the application material in relation to the enhancements made to the requirement.

39. During the March 2018 Board discussions, concern was raised about whether the enhancement to the requirement regarding previous audit evidence,¹⁵ to evaluate whether it not only remains relevant but also remains reliable as audit evidence for the current audit. The concern was that the enhancement may not be correct, as previous audit evidence would only be relevant if it was also reliable. The Task Force reconsidered this and concluded that relevance and reliability are independent, but inter-related concepts. Accordingly no further change has been made.
40. Other changes have been made to address Board comments, in particular in the application material, including:
 - (a) *Sources of information* for the risk assessment procedures: to include external sources such as publicly available information. (See paragraph A4c)
 - (b) *Analytical procedures*: introduction of application material to emphasize scalability (see further discussion in paragraphs 10–13)(see ISA 315 (Revised) paragraphs A16-A16a)
 - (c) *Observation and inspection*: adding the observation of the behaviours and actions of management or those charged with governance (See paragraph A18)
 - (d) Clarifications relating to *information obtained from the client acceptance and continuance process and other engagements relating to the entity*. (see paragraph A18b)
 - (e) *Engagement team discussion*: further clarifications have been made about the circumstances where the audit is conducted by a sole practitioner. In addition, the guidance in such circumstances has been ordered in the related application material to address first the simplest circumstances, which may therefore provide context for the more detailed discussions where there is a larger engagement team. In addition, the ISA 240 requirement for the engagement team discussion to place particular emphasis on how and where the entity’s financial statements may be susceptible to material misstatement due to fraud has been highlighted. (See paragraph A21)
 - (f) *Professional skepticism*: in light of the Board discussions relating to professional skepticism and how it should be articulated in the ISAs in March 2018, the Task Force concluded that the references in proposed draft ISA 315 (Revised) to ‘inconsistent and contradictory’ information or evidence should be to ‘contradictory’ and has reflected this throughout the revised draft.

The Required Understanding of the Entity and Its Environment, Including the Applicable Financial Reporting Framework (Requirements: paragraphs 11–11A of ISA 315 (Revised); Application Material – paragraphs A24a–A49h of ISA 315 (Revised))

41. At the March 2018 Board meeting, the Board was generally supportive of the changes proposed to the requirements, but some members questioned whether the reason for obtaining the required

¹⁵ ISA 315 (Revised), paragraph 9

understanding was appropriately articulated in the requirement. The Task Force has accordingly made clarifications to the lead-in to paragraph 11 of ISA 315 (Revised). It was also suggested that consideration be given to describing how to undertake the required understanding rather than listing the matters to be understood, but the Task Force was of the view that the ‘how’ was better left to implementation activities because of the wide variety of circumstances there may be.

42. The Task Force has proposed changes in the application material to address Board comments, including:
- (a) Clarifying the focus for the auditor when obtaining an understanding of the relevant aspects of the entity and its environment, and the applicable financial reporting framework. The Task Force has also enhanced the application material in relation to applying professional judgment when considering the nature and extent of understanding required. (See paragraph A24a)
 - (b) Adding an example of the use of automated tools and techniques where the outcome of procedures to understand the information system may be to obtain information about the entity’s organizational structure or with whom the entity does business (See paragraph A24b)
 - (c) Restructuring and clarification relating to what is required to be understood in relation to the entity’s business model, and related business risks. (See paragraphs A31c–g and A38a)).
 - (d) Making a clearer link between the relevant measures used to assess the entity’s financial performance and fraud, (paragraph A44a) and added guidance on inherent risk factors that address susceptibility to misstatement due to management bias or fraud (paragraph A49h of ISA 315 (Revised))

The Required Understanding of the Entity’s Internal Control (Requirements: paragraphs 12–21D of ISA 315 (Revised); Application Material – paragraphs A50–A109g of ISA 315 (Revised))

43. As the project has progressed, the Task Force has continued to restructure and refine the section on the auditor’s understanding of the system of internal control. In particular, the Task Force has focused on the flow of the section, including consistency in addressing different aspects of the system, and eliminating repetition while striking a balance with the need for ‘introductory or explanatory material’ that helps the auditor to understand what is being referred to and therefore how to apply the requirements of the ISA. The Task Force has also developed and enhanced the application material to support the effective application of the requirements, by enhancing the nature and sufficiency of guidance addressing the application of new concepts, in particular around IT considerations.¹⁶ Further, the Task Force has continued to address, as appropriate, Board comments that have been raised as this section has been amended and enhanced.
44. In the March 2018 IAASB discussions, although the Board continued to support the direction of the changes being made, the Board noted various specific concerns and issues related to the changes that had been proposed to the required understanding of the system of internal control. This included that further consideration should be given to consolidating the requirement for addressing control deficiencies identified in the various components of internal control, what the auditor has to do to understand that the information system has been ‘placed in operation,’ and further clarifying the guidance relating to various IT aspects, in particular general IT controls relevant to the audit.

¹⁶ The Task Force has continued to engage with a firm’s IT specialist on the changes, but has also obtained input from other IT specialists more broadly on the proposed changes.

45. In response to Board comments, the Task Force has further restructured and refined this section, and:
- Consolidated the requirement relating to control deficiencies within the system of internal control,¹⁷ which had previously been presented as separate requirements in the control environment, the entity's risk assessment process and the process to monitor the entity's system of internal control components. In considering the new combined requirement, the Task Force is of the view that control deficiencies could also arise in the information and communication and control activities components, and has therefore crafted the requirement to be broader than just the first three components of the system of internal control, as previously presented. The related application material has also been consolidated, and changes made to reflect the auditor's considerations relating to the new combined requirement more appropriately.
 - Clarified the requirement for the evaluation of the design of the entity's information system and determining whether it has been 'placed into operation' by changing the phrase 'placed into operation' to 'implemented', as no difference in meaning was intended.
 - Clarified the requirement for evaluating the design and implementation of controls relevant to the audit by separating the requirements for those that directly address the risks of material misstatement at the assertion level from those that support the operation of other controls (see ISA 315 (Revised) paragraph 21B). In the related application material, it has been clarified that the auditor's procedures in relation to evaluating the design and implementation of a control assist in determining the nature and extent of further audit procedures designed to address the risks identified, whether related to testing the operating effectiveness of the control or to substantive procedures.
 - Clarified what needs to be understood relating to the IT environment, to be able to appropriately identify the risks arising from the use of IT and the general IT controls that are relevant to the audit (see ISA 315 (Revised) paragraphs 18(d), 21 and 21A). In effect, the auditor is required to understand the IT environment and to identify IT applications and other aspects of the IT environment that are relevant to the audit. This provides the context for identifying the risks arising from the use of IT and the general IT controls relevant to the audit that address those risks. A summary of the clarified approach to understanding IT and determining its relevance to the audit was included in **Appendix 2 of Agenda Item 1** of the IAASB conference call held on May 22, 2018 (reference to this agenda item: [Ref](#)). Further application material has been added to support the auditor's considerations in relation to understanding the entity's IT environment, as part of understanding the information system component and significant enhancements were made to the application material addressing controls relevant to the audit, to support the revised requirements in paragraphs 21 and 21A. In addition, Appendix 4 in ISA 315 (Revised) has been added that includes considerations for understanding general IT controls.
 - Clarified that understanding how the entity demonstrates those charged with governance are separate from management, is required when those charged with governance are actually separate from management, which is often not the case in smaller and less complex entities. (Paragraphs 14(b); A77a)

¹⁷ ISA 315 (Revised) paragraphs 21C–21D

- Clarified the interaction between paragraph 13, which requires the auditor to identify controls relevant to the audit, evaluate the design of those controls, and determine whether they have been implemented, and paragraph 19A, which sets out what the auditor is required to do to understand the ‘control activities’ component, which is in effect limited to applying the requirement in paragraph 13 to controls within that component. Paragraph 19A, although not strictly a requirement (i.e., there is no ‘shall’), is essential application material that in the view of the Task Force helps make the link between paragraph 13 (which contains the ‘shall’) and identifying controls relevant to the audit.¹⁸ The requirements relating to the evaluation of the design of the controls, and the determination of whether they have been implemented, can be found in paragraph 21B.
- Made further enhancements and changes in the application and other explanatory material as follows:
 - Further clarified how to obtain the understanding in entities that are smaller and less complex, highlighting that professional judgment is needed when applying the requirements of the ISA in circumstances that are simpler and less complex (see paragraph A50). In addition, the various aspects of the system of internal control have been restructured to order the guidance on each requirement so that it first addresses how application of the requirement may be accomplished when the entity is smaller and less complex (in particular when there is direct management involvement in relevant aspects of the system of internal control, and when understanding IT environments that are simpler and less complex) (see further discussion in paragraphs 10–13).
 - Added guidance about when management is dominated by a single individual and the possible effects on the control environment (ISA 315 (Revised) paragraph A81a)
 - Made a stronger link between controls and fraud (see ISA 315 (Revised), paragraph A100f).
 - Clarified that the entity’s process to monitor the system of internal control may consist of ongoing activities, separate evaluations conducted periodically, or a combination of the two (See ISA 315 (Revised) paragraph A89e).
 - Clarified how the components, such as the entity’s process to monitor the system of internal control, may include controls that address risks of material misstatement at the assertion level (i.e., direct controls) and the impact thereof.(See ISA 315 (Revised) paragraph A89i)
 - Clarified the circumstances under which there may be requirement that the operating effectiveness of controls would be tested (i.e., when risks for which substantive procedures alone do not provide sufficient appropriate audit evidence exist) and added a section of guidance on other circumstances when the auditor may plan to test the operating effectiveness of controls. (See ISA 315 (Revised) paragraph A100j-A100l)
 - Enhanced the guidance relating to ‘controls relevant to the audit,’ in particular in relation to the fact that such controls are primarily direct controls in the control activities component and; the factors that influence the auditor’s judgment to determine a control is relevant to the audit; (See ISA 315 (Revised) paragraphs A100 and A100m)

¹⁸ There are other instances within the ISAs that are similar in nature, see ISA 200, paragraph 12 and ISA 610, paragraph 26.

- Highlighted the iterative nature of obtaining the understanding, in particular how obtaining an understanding of the entity and its environment, may also impact the auditor's understanding of the components of the system of internal control, such as the information system. (See ISA 315 (Revised) paragraph A90e)
46. In making revisions to the application material, the Task Force has deliberated whether there could be audits where there are no 'controls relevant to the audit' (i.e., in terms of the requirements of ISA 315 (Revised) and its definitions). The Task Force notes that because controls over journal entries are required to be 'controls relevant to the audit,'¹⁹ there will always be at least one 'control relevant to the audit' because even in the simplest information systems journal entries are used to capture an entity's financial information in its information system. The application material to ISA 315 (revised) paragraph 20 has been updated accordingly (see ISA 315 (Revised) paragraph A100a).
47. The Task Force considered whether changes were required arising from the recently revised *International Code of Ethics for Professional Accountants (Including International Independence Standards)*, as issued by the International Ethics Standards Board for Accountants, in particular in relation to the description of ethics in the control environment. The Task Force continues to believe that it is appropriate to base the requirements and guidance in the control environment component on the principles and guidance provided in COSO 2013.²⁰ The Task Force therefore agreed that no changes should be made because in addition to losing consistency with COSO if such changes were to be made. The Task Force also notes that references to ethics in ISA 315 (Revised) are in the context of the ethics and values of management and those charged with governance, and these parties may not be professional accountants in all circumstances, or, if professional accountants, they may not be subject to the requirements of the IESBA Code.

Identifying and Assessing the Risks of Material Misstatement (Requirements: paragraphs 25–31 of ISA 315 (Revised); Application Material – paragraphs A121a–A151 of ISA 315 (Revised))

48. The Task Force has continued to explore how best to present the requirements related to the identification and assessment of the risks of material misstatement, in particular in light of the new concepts introduced related to significant classes of transactions, account balances and disclosures, and their relevant assertions. In addition, the Task Force has focused on how the spectrum of inherent could be better described within the standard to help auditors make more consistent and effective assessments of such risks (including whether they are significant risks), thereby providing an enhanced basis for the design and performance of overall responses to risks at the financial statement level and further audit procedures (as required by ISA 330).²¹
49. In March 2018, the Board cautioned that the revised structure of paragraphs 25 and 26 of ISA 315 (Revised) was complex and confusing, and requested that the Task Force give further consideration to how the risk identification and assessment process could be made clearer. In particular, the Board did not support the proposed 'two-step' process, i.e., identifying potential risks of material misstatement then confirming this identification, in particular because this was unnecessarily complex and could lead to confusion and unnecessary documentation. The Board also highlighted that further clarification was needed in relation to risks at the financial statement level, in particular how they

¹⁹ ISA 315 (Revised), paragraph 20(c)

²⁰ The Committee of Sponsoring Organizations of the Treadway Commission's (COSO) *Internal Control – Integrated Framework (2013)*

²¹ ISA 330, *The Auditor's Responses to Assessed Risks*

related to risks of material misstatement at the assertion level, and whether they could be significant risks.

Identifying and Assessing the Risks of Material Misstatement

50. The Task Force has further deliberated how to present the requirements for identifying and assessing the risks of material misstatement in paragraphs 25 and 26 of ISA 315 (Revised). The Task Force agreed to simplify the requirements, and has the view that keeping the identification and assessment of risks separate will enhance the understandability of these requirements.
51. The Task Force also debated the order in which these requirements should be presented, in particular in light of the new concepts of significant classes of transactions, account balances and disclosures, and their relevant assertions. However, the Task Force also acknowledged that the order in which these requirements are applied should not be prescribed narrowly. In addition the process is iterative and is likely to be applied differently in an initial audit engagement versus a recurring engagement. What matters most is that each of the relevant requirements is applied but firms may have different methodologies for addressing the requirements for the identification and assessment of the risks of material misstatement.
52. The Task Force has accordingly simplified the requirements in paragraphs 25 through 26 of ISA 315 (Revised):
 - (a) Paragraph 25 comprises the requirement for the identification of risks of material misstatement that exist at both the financial statement level (explained further below) and at the assertion level. It has also been highlighted that in identifying the risks of material misstatement at the assertion level the IRFs are taken into account, to make clear that the IRFs are important in this process but also to make the link back to paragraph 11, where the IRF's are first considered as the auditor obtains the understanding of the entity and its environment. The application material further explains this link.
 - (b) Clarified that the assessments of inherent risk and control risk are only required at the assertion level.
 - (c) Paragraph 25A relates to the assessment of risks at the financial statement level – see explanation below.
 - (d) A new heading has been inserted to make clear that paragraphs 25B and 26 relate to the *assessment of inherent risk*.
 - (e) Paragraph 25B addresses the determination of significant classes of transactions, account balances and disclosures, and their relevant assertions and is placed here to be the link between the identification of the risks of material misstatement at the assertion level and the assessment of these risks, recognizing that this is an iterative process. It is the view of the Task Force, taking into account the interaction of the definitions of these concepts, that *possible* significant classes of transactions, account balances and disclosures, and their relevant assertions, would have been inherently identified through the auditor's process to *identify* risks of material misstatement at the assertion level. This requirement would effectively confirm that process (without requiring a preliminary determination, and then confirming it at a later stage). As the identification and assessment of the risks of material misstatement is a very iterative process, the Task Force is of the view that this is the most appropriate way to present this requirement and to acknowledge these new concepts in the most appropriate place in the standard.
 - (f) Paragraph 26 addresses the inherent risk assessment for the risks of material misstatement at the assertion level, taking into account the likelihood and magnitude of misstatement, as well as the

effect that risks of misstatement at the financial statement level may have on individual risks at the assertion level.

Further changes have also been proposed to the application material further clarifying how the various steps interact, in particular in relation to the assessment of inherent risk on the spectrum of inherent risk.

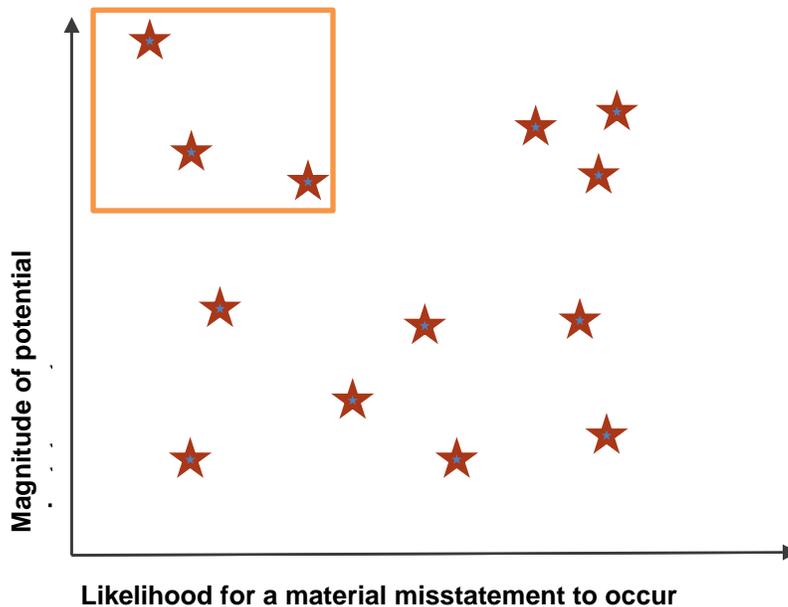
Identified and Assessed Risks of Material Misstatement at the Financial Statement Level

53. The Task Force has extensively deliberated the nature of risks at the financial statement, reflecting carefully on how they are described in ISA 200, in order to adequately describe them in ISA 315 (revised), and help the auditor to design and implement overall responses to address such risks.
54. In the view of the Task Force, every risk of material misstatement identified will either relate specifically to an individual assertion, or to a number of assertions (which could be in one or more classes of transactions, account balances or disclosures). When the risk relates to a number of assertions (i.e., is more pervasive) and can't be attributed specifically to an assertion(s), then the risk exists at the financial statement level.
55. In further considering risks of material misstatement at the financial statement level, the Task Force is also of the view that these risks will often arise from the higher-level components of the system of internal control, in particular the control environment, which will likely have a more pervasive effect on a number of, or all, classes of transactions, account balances and disclosures in the financial statements. Accordingly, the auditor's understanding of these components and the results of the evaluations required in paragraphs 14 to 17D of ISA 315 (Revised), as well as the effect of any identified deficiencies in accordance with paragraphs 21C and 21D, should be considered when identifying and assessing the risks of material misstatement at the financial statement level.
56. Taking into account the Task Force's conclusions on these matters, the relevant requirements in paragraph 25(a) (the requirement for the identification of financial statement level risks) and 25A (the requirement for assessing the risks at the financial statement level) have been revised. In doing so, the Task Force has emphasized the need:
 - (a) For the risk to relate more pervasively to many assertions to be considered a financial statement level risk; and
 - (b) To determine how, and the degree to which, these risks affect the assessment of risks of material misstatement at the assertion level (with a corresponding change made in relation to the assessment of inherent risks at the assertion level (see paragraph 26(b))).
57. The related application material in paragraphs A126a–A126g of ISA 315 (Revised) has also been updated accordingly, including providing:
 - (a) Further descriptions of what pervasive risks could be, such as those resulting from weaknesses in the control environment or pervasive risks arising from the risk of fraud.
 - (b) Examples of specific matters giving rise to risks that may affect a number of assertions, such as poorly implemented revenue application systems.

Significant Risks

58. The Task Force continues to consider how best to present the requirements and guidance in relation to significant risks, in light of Board agreement that the concept should be retained and the other changes that are being made. In particular, the Task Force has focused on the definition of significant risks to drive a more consistent application.

59. However, some Board members noted, in reference to the changes proposed in March 2018, that the description of a significant risk, with particular reference to the wording ‘*relative to other risks of material misstatement*’, may suggest that because it is a relative concept on every audit there would be at least one significant risk, which is not consistent with extant, and not something that the Task Force is seeking to change. In addition, it was also noted that by defining significant risks at the ‘highest end’ of the spectrum of risk also might suggest that there is only one significant risk (i.e., that risk that is at the very top end).
60. On further consideration, the Task Force is of the view that it is important to describe significant risks in terms of where they are on the spectrum of inherent risk, and considered various ways of describing this. Although there is not one distinct description that all of the Task Force members preferred, on balance the Task Force has agreed to change the way to describe where they lie on the spectrum as “close to the upper end” of the spectrum of inherent risk. Other positional terms that the Task Force discussed included “approaching”, “nearing”, or “towards” the upper end. Additional application material has been added that is intended to further explain how significant risks are determined.
61. In determining whether an identified risk is a significant risk, the definition as currently revised (i.e., as presented to the Board in March 2018) allows the auditor to take into account the likelihood OR the magnitude of the identified risks of material misstatement. Some Board members have queried whether the auditor should instead make the determination as to whether a significant risk exists based on the likelihood AND magnitude of the potential misstatement. In previous discussions with the Board (at more than one Board meeting), it was agreed that in instances where there is a very high magnitude, even if there is a low likelihood, that the related risk could still represent a significant risk. It has been noted that it would not be in the public interest if a risk with a possibly very high magnitude of misstatement was not considered in the auditor’s determination of significant risks, however the standard should not necessarily prescribe that such risks would in all cases be significant risks. (see illustration below – these identified risks relate to those in the orange box).



62. Accordingly the Task Force does not propose to change the “or” to an “and.”

Assessing Control Risk

63. Although no significant issues were raised by the Board at the March 2018 IAASB meeting, the Task Force further considered whether amendments were needed in light of the other changes being proposed related to identifying and assessing the risks of material misstatement. The Task Force agreed that no further significant changes were needed, but have proposed some clarifications.
64. In addition, the Task Force has enhanced the application material to:
- (a) Emphasize that the auditor’s primary consideration in assessing control risk is whether the auditor is required to, or intends to, test the operating effectiveness of controls (see ISA 315 (Revised) paragraph A150a).
 - (b) To further explain the interaction of control risk and inherent risk.(see ISA 315 (Revised) paragraph A150a)
 - (c) To address situations where there is more than one control that addresses a risk of material misstatement at the assertion level.(see ISA 315 (Revised) paragraph A150b)
 - (d) To clarify how the effectiveness of general IT controls is considered in assessing control risk (see ISA 315 (Revised) paragraph 150d).

Risks for Which Substantive Procedures Alone Do Not Provide Sufficient Appropriate Audit Evidence

65. The Task Force has clarified, in the requirement, that risks for substantive procedures alone that do not provide sufficient appropriate audit evidence are part of the determination of the risks of material misstatement *at the assertion level*, and has provided additional examples to illustrate such a situation.

Stand-Back Requirement

66. In March 2018, the Task Force presented a new requirement for a stand-back in paragraph 30B in ISA 315 (Revised) related to whether all the significant classes of transactions, account balances and disclosures, and their relevant assertions, had been identified. The Board noted various concerns related to the new ‘stand-back’ requirement, and asked the Task Force to simplify this requirement and make it more understandable. In particular, the introduction of qualitative and quantitative materiality into the stand-back was noted as confusing.
67. The following explains the interaction of the stand-back in paragraph 30B of ISA 315 (Revised) and paragraph 18 of ISA 330 and the Task Force view of the classes of transactions, account balances and disclosure to which paragraph 18 applies:
- The proposed stand-back in ISA 315 (Revised) is specifically focused on those classes of transactions, account balances and disclosures for which no risk of material misstatement has been identified (i.e., those classes of transactions, account balances and disclosures that have not been determined to be significant classes of transactions, account balances or disclosures).
 - For those classes of transactions, account balances of disclosures, the stand-back requires the auditor to identify those that are quantitatively or qualitatively material and confirm that there are no risks of material misstatement related to these (i.e., if risks of material misstatement are identified,

the class of transaction, account balance, or disclosure would become significant and the auditor would revise the risk assessment accordingly).

- The stand-back therefore has a purpose of assisting the auditor in achieving a more thorough risk assessment prior to designing and performing responses in accordance with ISA 330. The outcome of the stand-back will also be such that the auditor will identify any classes of transactions, account balances or disclosures that are quantitatively or qualitatively material but are not significant.
 - The requirement in ISA 330, paragraph 18 has a similar purpose and is directed at an ‘imperfect’ risk assessment (i.e., regardless of the auditor’s risk assessment, the auditor is required to design and perform substantive procedures for any class of transactions, account balance or disclosure that is quantitatively or qualitatively material). The Task Force debated which classes of transactions, account balances and disclosures are subject to paragraph 18 and agreed the following:
 - *Significant classes of transactions, account balances and disclosures are to be treated as quantitatively or qualitatively material.* Paragraph 6 of ISA 330 requires the auditor to design further audit procedures for significant classes of transactions, account balances and disclosures. Therefore, when the auditor has designed and performed substantive procedures in accordance with paragraph 6, the auditor has covered the requirement in paragraph 18. However, if there are any significant classes of transactions, account balances or disclosures for which the auditor only designed and performed tests of controls, then the auditor is required to design substantive procedures in accordance with paragraph 18.
 - *Classes of transactions, account balances and disclosures that are quantitatively or qualitatively material as identified in accordance with paragraph 30B of ISA 315.* For these, the auditor would not have designed or performed substantive procedure in accordance with paragraph 6 but is required to do so in accordance with paragraph 18 of ISA 330. Application material has been added to explain how the auditor may design such procedures in light of the fact that no risks of material misstatement were identified for these classes of transactions, account balances or disclosures.
68. Because both paragraph 30B of ISA 315 and paragraph 18 of ISA 330 are directed at dealing with “imperfect” risk assessment, the Task Force discussed whether the stand-back in ISA 315 (Revised) is needed. The Task Force discussed whether the requirement in ISA 330 would be sufficient for the auditor to identify those classes of transactions, account balances or disclosures that were material but were not determined to be significant classes of transactions, account balances or disclosures (i.e. a risk of material misstatement had not been identified).
69. On balance, the Task Force agreed that it would be appropriate to retain the requirement for a stand-back so that auditors are required to reconsider as part of their risk assessment that all significant classes of transactions, account balances and disclosures have been appropriately captured. Despite the stand-back, it is still possible that risks of material misstatement will not be identified by the auditor, in which case paragraph 18 of ISA 330 continues to protect against imperfect risk assessment by requiring that work be performed on classes of transactions, account balances or disclosures that are of importance to users (i.e., material). The Task Force recommends, however, that stakeholder views be obtained on whether the stand-back is needed or whether the enhanced application material to paragraph 18 of ISA 330 may be sufficient. (i.e., by asking a specific question in the explanatory memorandum).

70. The Task Force has also revised the relevant application material, through using relevant examples, to help explain how the stand-back could be operationalized. The Task Force confirmed its view that including both quantitative and qualitative aspects related to materiality is appropriate, but also noted that further guidance about matters that could be qualitatively material would help auditors understand how to apply the stand-back. Proposed guidance has been included in the updated application material.

Documentation

71. There are no significant changes in relation to documentation, however the Task Force has confirmed that the relevant references to ISA 230²² have been included.

Matters for IAASB Consideration

5. The IAASB is asked:
- (a) For its views on the proposed changes to ISA 315 (Revised) (requirements as set out in **Agenda Item 3-A** and application material as set out in **Agenda Item 3-B**, including the Appendices).
 - (b) Whether it agrees that a requirement for the stand-back, described in paragraphs 66–71, should be included in the Exposure Draft, with a specific question included in the Explanatory Memorandum, as described in paragraph 69, to obtain respondents views.

IV. Conforming Amendments

72. The Task Force presented its view on the approach to presenting the conforming amendments for discussion on the May 2018 Board Teleconference. This included proposed conforming amendments to ISA 200, ISA 240 and ISA 330, and a description of proposed changes throughout the other ISAs. The Board had mixed views about the latter, in particular questioning the ability to approve the ED and its proposed conforming amendments without seeing the specific changes that will be made. The Board also did not support changes to certain terms, such as ‘deficiency in internal control’, because the terms were viewed to be well understood both in practice and by management and those charged with governance. Accordingly, Agenda Item 1-C sets out:
- (a) Proposed changes to ISA 200, ISA 240 and ISA 330, amended as appropriate for Board comments. (It should be noted that paragraphs A29-A31 in ISA 330 have been subject to amendments as a result of the updates to ISA 315 (Revised) related to IT. These amendments were noted to be forthcoming in the issues paper for the May 2018 Board call).
 - (b) A table setting out the specific paragraph references, together with a description of the changes that will be made, in the other ISAs not presented.

In the view of the Task Force, this will allow respondents to the ED to be fully informed about the changes that will arise in other ISAs from the proposed changes in ISA 315 (Revised).

73. Although the Board did not support making wholesale changes to the term ‘deficiency in internal control’ as proposed for the May 2018 Board teleconference, the Task Force is still of the view that because the definition of this term explains that the deficiency relates to a control or combination of controls, the term “control deficiency” is an appropriate term. Further, “control deficiency” may be a more appropriate

²² ISA 230, *Documentation*

term depending on the context in which such deficiencies are described in the ISAs. Accordingly, the Task Force has proposed to take a pragmatic approach by retaining the definitions of ‘deficiency in internal control’ and ‘significant deficiency in internal control’ in ISA 265,²³ other ISAs with the exception of ISA 315 (Revised), and the Handbook Glossary, but amending the glossary to acknowledge that the terms “control deficiency” (or “significant control deficiency”) are also used in some ISAs with the same meaning. The Task Force is proposing to use the terms “control deficiency” and “significant control deficiency” exclusively in proposed ISA 315 (Revised).

74. A similar approach will be taken to changing ‘internal control’ to the ‘system of internal control’ throughout the ISAs (with the exception of ISA 315 (Revised)), unless the matter is referring to something specific in ISA 315 (Revised) (e.g., a component of internal control) or is related to the process to identify and assess the risks of material misstatement. Accordingly, **Agenda Item 3-C** sets out a proposed change to indicate that in some ISAs the term internal control is used instead.
75. With regard to the conforming amendments to ISA 540 (Revised), the Board broadly agreed to the proposed approach, presented for discussion on the May 2018 IAASB Teleconference, of presenting and approving conforming amendments to the final ISA 540 (Revised) in July 2018 as a supplement to ED ISA 315 (Revised). However, this would be subject to the Board understanding the nature and scope of those conforming amendments during the IAASB meeting week when the approval of final ISA 540 (Revised) and ED ISA 315 (Revised) are discussed and voted on. To facilitate this approach, the Board will be presented with an analysis of the nature and scope of the conforming amendments prior to a final vote on ISA 540 (Revised).
76. In addition to the changes noted above, the Task Force has made further changes to the conforming amendments to address Board comments and concerns raised on the May 2018 IAASB teleconference, including:
 - Further changes for consistency with the proposed changes in ISA 315 (revised);
 - Changes to ISA 330 relating to conforming amendments to the application material to paragraph 10 regarding tests of indirect controls, arising from the revised and enhanced requirements and application material in ISA 315 (Revised) relating to IT. Specifically, the application material has been revised to reflect the introduction of the concept of general IT controls relevant to the audit in ISA 315 (Revised) and to explain that the auditor may have identified such controls as part of the requirements of ISA 315 (Revised) and also planned to test them. The revisions also clarify the considerations of the auditor when such general IT controls are found to be ineffective. Although these revisions regarding additional procedures to be performed in these circumstances may appear more than consequential amendments, the Task Force is of the view that this additional guidance is needed such that the auditor is able to appropriately determine the effect of the deficient general IT controls on the auditor’s control risk assessment (i.e., whether audit evidence can be obtained that the controls relevant to the audit that are supported by the deficient general IT control are nevertheless effective).

The Task Force has not made changes in respect of various comments related to ‘controls relevant to the audit’ as this is now a specific explicit requirement in paragraph 20 of ISA 315 (Revised), with a related requirement for evaluating the design of such controls and determining whether they have been

²³ ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

implemented. The intentions of the Task Force were very specific in ISA 315 (Revised) to clarify what certain terms meant and have carried these specific meanings over to ISA 330.

Matter for IAASB Consideration

6. The IAASB is asked for its views on the proposed Conforming Amendments as set out in **Agenda Item 3-C**.

Other Matters

Implications of the Proposed Changes to ISA 315 (Revised) on the IAASB's Other Standards

77. Some of the standards in the IAASB's suite of standards that are not ISAs²⁴ (such as ISAE 3000)²⁵ include some of the risk assessment concepts embedded in ISA 315 (Revised) that have now been amended or enhanced. In the view of the Task Force these changes are particularly important in the context of an audit, and it is in the public interest to make those changes in the ISAs now. However, at this time it is not essential that these changes are replicated in the IAASB's other standards. Furthermore, there are other changes arising from the IAASB's current projects that will also likely impact the IAASB's other standards (such as those arising from the quality control projects), and the Task Force is of the view that it would make more sense to consider whether to make changes to these standards once (i.e., once revised standards for all of the relevant projects have been finalized) in a more comprehensive project. Accordingly, no further changes have been proposed to the IAASB's other standards.

Exposure Period

78. The Task Force believes it is in the public interest to minimize the time between the effective dates of ISA 540 (Revised) (to be determined at the June 2018 IAASB meeting) and the revisions to ISA 315 (Revised). In order to progress the final changes to ISA 315 (Revised) for approval in June 2019 (as targeted), with an proposed effective date for audits of periods commencing on or after December 15, 2020, the Task Force will need to provide the feedback, and initial thoughts on direction forward, arising from the responses to the ED to Board at the December 2018 IAASB meeting. To meet this timeline, the responses will need to have a deadline of October 31, 2018, with an assumed mid-July publication of the ED. This proposed timeline would allow an exposure period of more than 100 days, and although less than the 120-day period required by the IAASB's due process,²⁶ there are precedents where it is in the public interest to shorten this period, for example ISA 540 (Revised). Accordingly the Task Force proposes a deadline for the end of October for comments.

Effective Date

79. As noted above, and in light of the interaction of the changes to ISA 315 (Revised) with the changes being finalized with regard to ISA 540 (Revised), the Task Force is of the view that in order to minimize

²⁴ International Standard on Assurance Engagements, International Standards on Review Engagements, and International Standards on Related Services

²⁵ International Standard on Assurance Engagements (ISAE) 3000, *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

²⁶ The IAASB's due process requires that an ED ordinarily has a 120-day comment period.

the period between when ISA 540 (Revised) becomes effective (to be determined at the June 2018 IAASB meeting), and when the revisions to ISA 315 (Revised) become effective, an appropriate effective date would be for audits of periods beginning at least 18 months after approval²⁷ (i.e., audits of periods beginning on or after December 15, 2020). Because ISA 315 (Revised) is a performance standard that directly affects the planning phase of an audit, the effective date has been set using the convention of “periods beginning” as opposed to “periods ending”. Further, because of the significance of the revisions proposed and because the implementation efforts for the ISA may be substantial, the Task Force is of the view that a transition period of at least 18 months is warranted. A question of respondents will be asked in the Explanatory Memorandum related to the expected implementation efforts and the appropriateness of the transition period.

Due Process Matters

80. In the Task Force’s view, the significant matters identified as a result of its deliberations from the beginning of this project, have all been presented in the issues papers presented to the Board for discussion. In the view of the Task Force there are no significant matters that have not been brought to the attention of the IAASB.
81. The Task Force does not believe that a consultation paper, field testing or a roundtable is needed at this stage of the project, as substantial outreach with a wide range of stakeholders has been undertaken (see Paragraph 6).

Matters for IAASB Consideration

7. The IAASB is asked for its views on the above matters, in particular in relation to the exposure period and planned effective date.
8. Paragraph 10–13 describes the Task Force’s views about scalability in the standard, and the development of further non-authoritative guidance. Does the IAASB believe that further non-authoritative guidance is necessary, and in what form (i.e., for example, Staff Questions and Answers)?

Matters for the Explanatory Memorandum

82. The Task Force has considered some matters it believes are useful to address in the Explanatory Memorandum accompanying the ED.²⁸ These include:
 - Setting out the public interest matters and how they have been addressed in this project (along the lines as set out in paragraph 3).
 - Why the changes have been made and what the auditor will be doing differently, including the possible impacts of the proposed changes.
 - Explain the new concepts introduced (e.g., inherent risk factors, significant classes of transactions, account balances and disclosures, relevant assertions, relevant IT applications), how they interact and the benefits of applying these new concepts.

²⁷ Approval by the IAASB – it is assumed that firms will be able to commence plans to implement the revised standard before approval of the due process by the PIOB.

²⁸ The IAASB’s due process requires an ED to be accompanied by an Explanatory Memorandum that highlights the objectives of, and significant proposals contained in the proposed pronouncement.

- Explaining the changes to the procedures to identify and assess the risks of material misstatement, including the ‘spectrum of inherent risk’ and how the risks are assessed on this spectrum, as well as describing the changes to enhance the auditor’s understanding of risks at the financial statement level and significant risks (including the inclusion of risks with low likelihood or high magnitude as possible significant risks). This will also include an explanation of the changes to the definition of significant risk, and the expected impact of that change.
- Explain the new stand-back requirement, and how it interacts with ISA 330, paragraph 18, and the consequential amendments that have been proposed. A specific question will be asked regarding this.
- Explain how aspects of the standard relating to IT have been updated, in particular in relation to the IT environment, the IT applications relevant to the audit and general IT controls relevant to the audit, and the impact thereof,
- Explain how the standard has been modernized in relation to the auditor’s use of automated tool and techniques (including data analytics).
- Describe any difference to the US Public Company Accounting Oversight Board (PCAOB’s) risk assessment standard, including an explanation for the differences, as appropriate.
- Describe the changes made to the requirements for understanding the system of internal control for clarity and better understanding (including why that understanding has been obtained and what it is used for), including:
 - Explaining the changes made to each of the components of the system of internal control, and clarifying how to obtain an understanding of each of the components
 - Explaining what the effect is of the procedures that are performed to obtain an understanding of internal control on the risk identification and assessment process.
 - Clarifying what ‘controls relevant to the audit’ are, and providing further guidance about what is required to evaluate the design of the control and determine whether it has been implemented. .
- Explain the conforming amendments that have been proposed.
- Explain enhancements that have been made with regard to professional skepticism.
- Explain the changes made to address scalability of the standard, including the incorporation of considerations for audits of small and medium entities into the application material, the use of examples and illustrations to demonstrate scalability, and the restructuring to have some aspects relating to smaller and less complex entities upfront where appropriate.
- Explain the enhanced considerations for audits of public sector entities.
- Further explain the interaction with the ISA 540 Task Force as that group has finalized its standard.

Matters for IAASB Consideration

9. The IAASB is asked whether there are any other matters, not noted in paragraph 82 above, that should be addressed in the Explanatory Memorandum.

Task Force Members and Activities Including Outreach and Coordination with Other IAASB Task Forces

1. The following sets out the activities of the Task Force, including outreach with others and coordination with other IAASB Task Forces and Working Groups relating to the ISA 315 (Revised) project, since March 2018. The Task Force consists of the following members:
 - Fiona Campbell – Chair (supported by Denise Weber)
 - Megan Zietsman
 - Marek Grabowski (supported by Josephine Jackson)
 - Susan Jones
 - Katharine Bagshaw
 - Charles (Chuck) Landes – correspondent member (supported by Hiram Hasty)

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

Task Force Activities since the March 2018 IAASB Discussion

2. The ISA 315 Task Force has met twice in person and held 1 teleconference since the last IAASB discussion in March 2018.

The Task Force also presented certain aspects of the ED to the Board through a teleconference on May 22, 2018.

Outreach

3. The Chair of the ISA 315 Task Force and Staff discussed changes relating to public sector considerations on a teleconference with representatives from the public sector. The Task Force Chair has also engaged through teleconference with representatives from the International Association of Insurance Supervisors and presented the key proposed changes to ISA 315 (Revised).
4. Additional targeted outreach activities will be conducted by the Task Force Chair and Staff during early June 2018. Teleconferences have been scheduled with representatives from:
 - Consultative Advisory Group – voluntary call
 - Global Public Policy Committee
 - International Forum of Independent Audit Regulators' Standards Coordination Working Group
 - International Organization of Securities Commissions

Coordination with Other IAASB Task Forces and Working Groups

5. The Chair of the Task Force and Staff continue to coordinate with the Chairs of the ISA 540 Task Force and Staff to discuss matters that crossover both projects. In addition, Mr. Grabowski is a member of the ISA 315 Task Force and the Co-chair of the ISA 540 Task Force.

Extracts from Draft Minutes²⁹

ISA 315 (Revised) – March 2018

Ms. Campbell provided an overview of proposed changes to the requirements and application material of ISA 315 (Revised) as presented in **Agenda Items 3-A, 3-B and 3-C**.

Noting that some aspects of the revisions to ISA 315 (Revised) still require clarification and that some terms, such as automated techniques and tools, need to be consistently articulated, the IAASB broadly supported the direction of the proposed changes, in particular as the proposed changes continued to address the matters included in the project proposal. The Board also generally noted support for the changes that had been made in relation to information technology (IT). Notwithstanding this support, the Board cautioned about the complexity that had been introduced by some of the revisions, and therefore continued to encourage the ISA 315 Task Force to develop explanatory material to practically demonstrate the application of the standard, for example through implementation guidance or flow charts. In addition, the Board asked for further consideration by the ISA 315 Task Force on specific broader matters, including:

- Scalability of the standard. The Board expressed its appreciation of the table included in the issues paper (agenda item 3), setting out those paragraphs where scalability could be applied. However, the ISA 315 Task Force was requested to further consider how the scalability paragraphs could be more distinct and gain more prominence, for example, by including the paragraphs in an appendix to the standard. Board members also asked the ISA 315 Task Force to further consider the paragraphs describing scalability that have been added to the introductory paragraphs, as these may be misinterpreted.
- The content and length of the introductory paragraphs. Although the Board generally supported the inclusion of the introductory paragraphs to highlight key risk assessment concepts; it was noted that these paragraphs could be simplified as they were too repetitive and complex in some places. In addition, some concerns were expressed, including that:
 - Some terms or concepts are introduced too early and in some cases not consistent with the wording in the relevant other standards. Suggestions included to rather utilize references back to other standards, or alternatively, to include these concepts in an appendix;
 - The paragraphs do not adequately describe the purpose behind obtaining an understanding of the entity's system of internal control and its relationship to tailoring further audit procedures.
 - The description of the spectrum of risk did not adequately describe the concept so that it would be understandable by all auditors, particularly how it relates to testing the operating effectiveness of the controls. One Board member queried whether a definition for the 'spectrum of risk' was required.
 - The paragraphs do not:
 - Provide a link to ISA 240³⁰ to recognize how the risks of fraud are dealt with in ISA 315 (Revised);
 - Do not recognize automated techniques or tools, including data analytics; and

²⁹ The draft minutes are still subject to IAASB review and therefore may still change.

³⁰ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

- The description of a significant risk in paragraph 1D, with particular reference to the wording ‘*relative to other risks of material misstatement*’, which may suggest that because it is a relative concept on every audit there would be at least one significant risk, which is not consistent with extant.
- How to articulate the use of ‘automated techniques and tools’ in the standard. The Board expressed mixed views on whether an explicit reference to ‘data analytics’ is appropriate.

DEFINITIONS

In relation to the proposed changes to the definitions, the Board continued to support the further changes that have been proposed, as well as the inclusion and planned modernization of the new definitions of application controls in information technology and general IT controls, but still noted the following concerns in relation to:

- The definition of ‘assertions’, further consideration was needed to distinguish this definition from management representations in accordance with ISA 580.³¹
- The definition of ‘inherent risk factors’ (IRFs), the Board encouraged further consideration about:
 - Broadening of the definition to include quantitative aspects as this may detract from the qualitative aspects that this concept was focusing on. However, other Board members agreed with broadening this to include quantitative aspects.
 - The susceptibility to management bias as an inherent risk factor, as it may be more of an overarching inherent risk factor. Other Board members supported the introduction of unintentional aspects of management bias.
 - How the IRFs interact with the risk of fraud. Currently, the ‘susceptibility to management bias’ only covers part of the fraud triangle and therefore the link to the fraud risk factors of ISA 240 appears incomplete. However, the ISA 315 Task Force was cautioned not to confuse further explanations in ISA 315 (Revised) with the auditor’s considerations about fraud already required in ISA 240.
- The definition for ‘relevant assertions,’ noting that further clarification was needed to explain the threshold of ‘*more than remote*’ was not different from ‘reasonably possible.’
- The definition of ‘significant risk,’ with some Board members still expressing concern whether terms such as ‘relative to other risks’ and ‘highest end of the spectrum’ would be applied consistently by auditors and may be inconsistently interpreted. In addition, some Board members questioned the use of the word ‘or’ with reference to the phrase ‘*the likelihood of a misstatement occurring or the magnitude of potential misstatement,*’ however, Ms. Campbell explained the rationale and referred to previous Board discussions in support thereof to help make clear that significant risks could exist if there was a low likelihood of occurrence but a high magnitude of the event did occur. The Board generally agreed that the use of the word ‘or’ in this context remains appropriate.

³¹ ISA 580, *Written Representations*

RISK ASSESSMENT PROCEDURES

Although supportive of the further changes that have been proposed, the Board asked that further consideration be given to:

- The use of the term ‘sufficient appropriate audit evidence’ in paragraph 5 of ISA 315 (Revised). Although some Board members believed that the introduction of this concept would help with why risk assessment procedures are performed (i.e., what the outcome should be when performing risk assessment procedures), and with the boundaries about how much audit evidence is needed (and therefore also assist with the documentation requirements). Other Board members believed that the use of ‘sufficient and appropriate’ is superfluous and may not change auditor behavior;
- Aligning the relevant parties in paragraphs 7 to 10 between the requirements and the application material.
- How analytical procedures are described in the application material, as this currently provides examples but may be better described as characteristics of effective analytical procedures as risk assessment procedures.
- Whether the engagement team discussion should focus on the risks inherent in the applicable financial reporting framework for the entity, rather than the entity’s application thereof.
- The nature of audit evidence obtained through the use of automated techniques and tools as part of risk assessment procedures.

UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

The Board was generally supportive about the further changes that have been proposed, but asked that further consideration be given to:

- Better describing the reason or expected outcomes when obtaining an understanding the entity and its environment. Some Board members were also concerned that the requirement may be interpreted too narrowly as it only focuses on what may impact the expected classes of transactions, account balances and disclosures in the financial statements, and there may be other aspects that should be included to effectively identify all risks.
- Describing how to undertake the risk analysis rather than listing the matters to be understood to identify the risks.

OBTAINING AN UNDERSTANDING OF THE SYSTEM OF INTERNAL CONTROL

There was support for the proposals relating to the further changes made for the auditor’s understanding of the entity’s system of internal control, however, the Board asked that the descriptions provided be written in a simpler way and that aspects of scalability still be considered. The Board also asked that further consideration be given to:

- Whether the scope of the required understanding, being ‘*relevant to financial reporting*,’ is not too broad.
- Clarifying why the auditor is required to obtain an understanding of the system of internal control.
- Consolidating the auditor’s response when identifying deficiencies in the various components of internal control into a single requirement.

- Better describing, and developing guidance to practically demonstrate (for example through a flowchart) how the requirements ‘fit together,’ in particular in relation to information technology.
- Related to whether a control has been placed into operation in paragraph 18A, clarifying the work effort to determine whether the control has been ‘*placed into operation*’ in paragraph 18A.
- Distinguishing the concepts of direct and indirect controls through the application material and clarifying what the impact of the difference is.
- Clarifying under which circumstances general information technology controls are expected to be relevant.

IDENTIFICATION AND ASSESSMENT OF RISKS OF MATERIAL MISSTATEMENT

The Board cautioned that the revised structure was complex and some noted that reordering the required steps may be appropriate. The ISA 315 Task Force was also encouraged to enhance the related application material to clarify the process, highlighting that a flowchart may be very helpful for implementing the new and revised requirements in this area. In addition, the ISA 315 Task Force was asked to further consider:

- Financial statement level risks, in particular:
 - The auditor’s response to financial statement level risks and how these risks interact with risks at the assertion level; and
 - Whether a financial statement risk could be classified as a significant risk, and if so, the consequences for the auditor.
- The stand-back requirement in paragraph 30B:
 - Concern was expressed with the use of the terms ‘significant’ and ‘material’ in the same requirement; and
 - how this the link with ISA 330³² paragraph 18 could be better explained.

DOCUMENTATION

One Board member noted that the documentation requirements stayed largely consistent compared to extant, and questioned whether it sufficiently recognizes the enhancements to the standard.

APPENDICES

The Board expressed their support for the appendices as included in Agenda Item 3-B.

IAASB CAG CHAIR REMARKS

Mr. Dalkin noted continuing support for the direction of the changes being developed. Mr. Dalkin specifically noted support for the coordination efforts to align ISA 315 (Revised) with ISA 540, and the inclusion of an explicit link to ISA 240 to recognize that the risk of fraud is integral to the auditor’s risk assessment in accordance with ISA 315 (Revised). He also noted the CAG’s concerns about the description of significant risk being at the ‘highest end’ of the spectrum of risk, which may suggest that there is only one significant risk.

³² ISA 330, *The Auditor’s Responses to Assessed Risks*

PIOB REMARKS

Ms. Stothers continued to support the direction of the changes, specifically acknowledging the separation of the assessment of inherent risk and control risk. She further encouraged the ISA 315 Task Force to continue its efforts to clarify and explain, in the standard, that the consideration of the risk of fraud is fundamental to the auditor's identification and assessment of risk of material misstatement. And accordingly, irrespective whether the risk of fraud is included as an inherent risk factor or not, from a public interest perspective, a clear link to ISA 240 may be required. Ms. Stothers also encouraged the Task Force to continue to consider how the use of data analytics or automation is presented in the standard, including how this is described, and how professional skepticism could be further emphasized within the standard.

WAY FORWARD

The ISA 315 Task Force will undertake specific outreach with public sector representatives in order to make amendments in relation to public sector considerations as appropriate. The Task Force will present specific matters at a Board teleconference in May 2018 and an Exposure Draft of the proposed changes to ISA 315 (Revised) for IAASB approval at the June 2018 IAASB meeting.

This Appendix sets out the relevant references as explained in paragraphs 15–27.

Scalability – refer paragraphs 10–13

Agenda Item 3-B: Paragraph reference and summary of content (Application material)	
A3	Explaining that the risk assessment procedures to obtain the overall understanding may be less extensive in the audits of smaller and less complex entities
A16 & A16a	Explaining how analytical procedures as a risk assessment tool are scalable: <ul style="list-style-type: none"> - The auditor may perform a simple comparison of information from an interim or month end period with balances from prior periods. - Alternatively, the auditor may perform a more advanced procedure by extracting data from the entity’s information system, and further analyze this data by using visualization techniques.
A20a	Providing guidance where an engagement team discussion may not be possible, for example, where an engagement is carried out by a single partner.
A22	Clarifying that during the engagement team discussion, the consideration of disclosure requirements are considered even where the financial reporting framework may only require simplified disclosures.
A24a	Describing the depth of the auditor’s required understanding of the entity and its environment – this will vary according to the nature, size and complexity of the entity.
A31	Explaining that the auditor’s understanding of the entity’s organizational structure and ownership is dependent on the particular circumstances, such as complexity.
A44	Emphasizing that the procedures to measure the performance of an entity may vary depending on the size and complexity of the entity, as well as the involvement of management and those charged with governance in the management of the entity.
A49d	Explaining that disclosures in financial statements of smaller and less complex entities may be simpler and less detailed, but this does not relieve auditor of obtaining understanding of the applicable financial reporting framework
A49k	Highlighting an increased susceptibility to risks of material misstatement due to fraud in owner–managed entities.

A50a	Explaining that the nature, timing and extent of the auditor’s risk assessment procedures will vary and depend on matters such as the size and complexity of the entity.
A52	Clarifying that the way in which internal control is designed, implemented and maintained, varies with an entity’s size and complexity.
A77 a–b	<ul style="list-style-type: none"> • Highlighting that the control environment relating to smaller and less complex entities is likely to vary from larger or more complex entities. And therefore, some considerations about the entity’s control environment may not be applicable or less relevant. • Clarifying that audit evidence for elements of the control environment in smaller and less complex entities may not be available in documentary form. <p>In both instances, examples are also provided.</p>
A80a	Explaining that the auditor’s consideration of the entity’s use of IT, as it relates to the control environment, is commensurate with the nature and size of the entity and its business operations, including the complexity or maturity of the entity’s technology platform or architecture.
A81a	Clarifying that domination of management by a single individual in a smaller and less complex entity does not generally indicate a failure by management to display and communicate an appropriate attitude regarding the entity’s stem of internal control and the financial reporting process.
A89	Explaining that some smaller and less complex entities, and particularly owner-managed entities, may not have established a formal risk assessment process, or the risk assessment process may not be documented or performed on regular basis.
A89c	Highlighting that for some smaller and less complex entities, and particularly owner-managed entities, an appropriate risk assessment may be performed through the direct involvement of management or the owner-manager.
A89f	Clarifying that in smaller and less complex entities, and particularly owner-managed entities, management’s monitoring of control is often accomplished by the owner-manager’s direct involvement in operations and there may not be any other monitoring activities.
A89g	Providing guidance to the auditor where an entity may not have a distinct process for monitoring the system of internal control.
A90c	Explaining that the auditor’s understanding of the entity’s information system relevant to financial reporting may require less effort in an audit of smaller or less complex entities, and may be more dependent on inquiry than on review of documentation.

A92f	Clarifying that the auditor’s understanding of the entity’s IT environment may be simpler for a smaller and less complex entity that uses commercial software and the entity does not have access to the source code to make any program changes.
A97a	Clarifying that the communication of financial reporting roles and responsibilities within smaller and less complex entities may be less structured and less formal.
A99a	Explaining the nature or type of controls in smaller and less complex entities.
A99e	Explaining that smaller entities may be limited in the extent to which segregation of duties is practicable, and the consequences thereof.
A100a	Explaining that controls relevant to the audit are expected to include, at a minimum, controls over journal entries, and that in audits of smaller and less complex entities with a non-complex information system, there may not be any other controls relevant to the audit (if no significant risks and no intention to test the operating effectiveness of controls)
A106b	Providing guidance where an entity uses commercial software and management does not have access to the source code to make any program changes. And consequently, there may be circumstances where no IT applications are relevant to the audit or when understanding program change controls are not required (because the program can’t be changed).
A106i	Explaining that when there are no IT applications relevant to the audit, other aspects of the entity’s IT environment are also not relevant.
A127f	Acknowledging that, in relation to audits of smaller and non-complex entities, a greater proportion of assessed inherent risks are likely to be at the lower end of the spectrum of inherent risk.
A150a	A reminder that the control risk assessment remains at the maximum level when the auditor does not intend to test the operating effectiveness of controls that address the assessed inherent risks.
A152-A153	Emphasizing that the form and extent of audit documentation may be simple in form and relatively brief for audits of smaller and less complex entities, and may be incorporated in the documentation of the overall strategy and audit plan..

Fraud – refer paragraphs 14–15

ISA 315 (Revised) Requirements	
Introductory paragraph 1-F	Explaining that risks to be identified and assessed by the auditor in accordance with ISA 315 (Revised) include both those due to error and fraud. Due to the significance of fraud, further reference to ISA 240 is required.
Para. 3:	Stating the objective of the standard, i.e. the auditor is to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.
Para. 4(d)	Risk assessment procedures – The audit procedures designed and performed to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.
ISA 315 (Revised) Application Material	
Para. A0d & A0e	Explanatory material on the ‘susceptibility to misstatement due to management bias or fraud’ inherent risk factor.
Para. A1a	Confirming that the risks of material misstatement are identified and assessed due to both error and fraud. However, due to the significance of fraud, further reference to ISA 240 is required.
Para. A1b	Explaining that the understanding of the auditor, as required by ISA 315 (Revised), establishes a frame of reference within which the auditor plans the audit and exercises professional judgment throughout the audit, including during the auditor’s consideration of fraud in accordance with ISA 240.
Para. A7	Clarifying that inquiries, as part of risk assessment procedures, may provide information about matters such as fraud or suspected fraud affecting the entity.
Para. A11	Reminding the auditor of ISA 240 para. 19: If internal audit function provides information regarding fraud, the auditor takes this into account in the auditor’s identification of risk of material misstatement due to fraud.
Para. A15	Explaining that analytical procedures may help identify unusual or unexpected relationships that may assist the auditor in identifying risks of material misstatement due to fraud.
Para. A21	Emphasizing that: <ul style="list-style-type: none"> The engagement team discussion allows the engagement team to exchange information about how the financial statements might be susceptible to material misstatement due to fraud and error.

	<ul style="list-style-type: none"> ISA 240 requires that the discussion place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud.
A31c	Explaining that the understanding of the business model may assist the auditor in identifying incentives or pressures on management that may result in intentional or unintentional bias.
Para. A44a	Explaining that an understanding of the entity's performance measures may assist the auditor in identifying performance targets that increase the susceptibility to misstatement due to management bias or fraud.
Para. A49g & A49h	<ul style="list-style-type: none"> Emphasizing that when the auditor obtains an understanding of the entity, the auditor may identify events or conditions that are indicative of risks of material misstatement due to fraud. If so, the auditor is required to consider whether one or more fraud risk factors are present in accordance with ISA 240 para. 24.
Para. A49k	Highlighting an increased susceptibility to risks of material misstatement due to fraud in owner–managed entities.
Para. A82	Clarifying that although the control environment may help reduce the risk of fraud, it is not an absolute deterrent to fraud.
Para. A89a	Explaining that an understanding of the entity's risk assessment process may include how management or those charged with governance consider the potential for fraud.
A99e	Explaining that domination of management by a single individual (and when segregation of duties doesn't exist) is an opportunity for management override of controls.
A100f	Reminding the auditor of the importance to obtain an understanding of the controls management has implemented to prevent and detect fraud, as well as referring to the fraud risk factors included in ISA 240.
Para. A144	Emphasizing that ISA 240 provides requirements and guidance in relation to the identification and assessment of risks of material misstatement due to fraud.
Appendix 2	An example of events and conditions relating to the 'susceptibility to misstatement due to management bias or fraud' – Fraudulent financial reporting.
Appendix 3	Explaining that the segregation of duties is intended to reduce the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of the person's duties.

Public Sector – refer paragraphs 16–18

Agenda Item 3-A	
1J	Highlighting that the objectives of a financial audit in the public sector are often broader than an audit for a non-public entity. For example, the audit mandate for public sector entities may arise from legislation, regulation, ministerial directives, etc.
Agenda Item 3-B	
A8a	Explaining that when the auditor makes inquiries of management (or others within the entity) to identify risks of material misstatement, public sector auditors may obtain information from additional sources.
A13	Emphasizing that auditors of public sector entities often have additional responsibilities with regard to internal control and compliance with applicable laws and regulations.
A18a	Highlighting that risk assessment procedures by public sector auditors may include observation and inspection of documents prepared by management for the legislature.
A23a	Explaining that for public sector audits, the engagement team discussion may consider broader objectives and related risks arising from the audit mandate or obligations of the entity.
A31a	Providing guidance on the concept of ‘the entity’s organizational structure and ownership’ from a public sector perspective.
A36a	Explaining the concept of ‘the entity’s business model’ from a public sector perspective.
A43	Clarifying the meaning of “management objectives” from a public sector perspective.
A43e	Explaining that for public sector entities, law, regulation or other authority may affect the entity’s operations.
A49a	Describing specific measures that may be used to assess an entity’s financial performance from a public sector perspective.
A53a	Highlighting that public sector auditors often have additional responsibilities with respect to internal control, and therefore, considerations about the system of internal control may be broader and more detailed.

A121e	Clarifying the application and scope of assertions, as described in paragraphs A121c (a)-(b), from a public sector perspective.
-------	---

Data Analytics – refer paragraphs 19–21

Agenda Item 3–B: Paragraph reference and summary of content (Application material)	
A2	Emphasizing that technology may be used on large volumes of data, which may result in evidence that informs the identification and assessment of risks of material misstatement.
A4b	Clarifying that the auditor may use automated tools and techniques to perform risk assessment procedures, including for analysis, recalculations, re-performance or reconciliations.
A16a	Describing that: <ul style="list-style-type: none"> • Risk assessment analytical procedures may be automated, for example by using visualization techniques to analyze data to identify more specific areas of possible misstatement. • The application of automated analytical procedures to data may be referred to as data analytics.
A24b	Highlighting that the auditor may be able to enhance the understanding of the entity and its environment by using automated tools and techniques, and providing an example.
A96b	Explaining the option to use automated techniques to assist in confirming that the information system has been implemented.
A100i	Describing that automated tools may be used to understand the nature and extent of controls over journal entries.
A127b	Clarifying that automated techniques may be used to confirm whether all significant classes of transactions and account balances have been identified by, for example, analyzing types of transactions and their volume.

Professional Skepticism – refer paragraphs 22–23

Agenda Item X	
A4c	Explaining that sources of information, other than management, may provide potentially contradictory information from that provided by management, which may assist the auditor in exercising effective professional skepticism in identifying and assessing the risks of material misstatement.
A21	Describes the benefits of the engagement team discussion, and in particular, assisting engagement team members in further considering inconsistent

	information based on each member's own understanding of the nature and circumstances of the entity.
A22a	Explaining that when performing risk assessment procedures, the engagement team has the opportunity to exercise professional skepticism through identifying and discussing inconsistent or contradictory information obtained in performing those procedures, as well as considering whether there are indicators of possible management bias (both intentional and unintentional).
A24a	Clarifying that the ability of the engagement team to effectively exercise professional skepticism throughout the audit is enhanced through obtaining a thorough understanding of the entity and its environment and the applicable financial reporting framework.
A89r	Emphasizing that the auditor's communications with the internal audit function may provide opportunities for the auditor to obtain information that brings into question the reliability of documents and responses to inquiries to be used as audit evidence. Contradictory information enables the auditor to exercise professional skepticism.
A121a	Reminding the auditor that in identifying and assessing the risks of material misstatement, the auditor exercises professional skepticism in accordance with ISA 200. ³³

³³ ISA 200 paragraph 15