

**Auditing Complex Financial Instruments—Issues and IAASB Task Force
Proposals****I. Background**

1. At the September 2009 meeting, the IAASB agreed that there were certain matters that should be addressed in revising IAPS 1012.¹ The IAASB's Consultation Paper² released in October 2009 therefore seeks feedback from stakeholders on how the revised IAPS should deal with these matters, including:
 - (a) The definition of complex financial instruments and the applicability of the proposed guidance to audits of entities of all sizes;
 - (b) Application of the audit risk standards;
 - (c) Sufficient appropriate audit evidence, including relevance and reliability of fair value information; and
 - (d) Disclosure and reporting considerations.
2. While responses to the Consultation Paper are not expected until January 15, 2010, the Task Force has endeavored to progress the project by beginning to redraft the UK Auditing Practices Board's (APB) Practice Note (PN) 23³ as a revised IAPS 1012. This paper describes the initial changes that were made in redrafting the UK's Practice Note (Section II) and the Task Force's discussion to date on some of the issues included in the Consultation Paper for which it would be helpful to have the IAASB's views and direction on the way forward (Section III).
3. **Agenda Item 6-B** is presented for reference purposes only to illustrate matters included in this paper. Accordingly, it is not anticipated that the IAASB will discuss the content of that agenda item at its December 2009 meeting. The Task Force intends to further revise Agenda Item 6-B based on the IAASB's consideration of the matters set forth in this paper, as well as the responses received from the Consultation Paper.

II. Redrafting of the UK's Practice Note**Elimination of Present Tense**

4. The project proposal acknowledged that the final output of the complex financial instruments project is subject to decisions arising from the IAASB's separate project to review the status and authority of the IAPSs on a prospective basis. **Agenda Item 7-A** outlines that project's Working Group's preliminary views that new or revised IAPSs should have an equal status to application and other explanatory material in the ISAs.

¹ International Auditing Practice Statement (IAPS) 1012, "Auditing Derivative Financial Instruments."

² IAASB's Consultation Paper, "Auditing Complex Financial Instruments," issued in October 2009.

³ Practice Note 23, "Auditing Derivative Financial Instruments," issued in April 2002 and based on IAPS 1012.

5. Staff has made revisions to the UK’s PN on that basis. The most substantive change that is necessary throughout the document as a result is the elimination of the present tense in the guidance material. In the draft IAPS, the present tense is used only to place specific requirements of the ISAs in the context of auditing complex financial instruments.
6. The extant IAPSs were issued to provide interpretive guidance and practical assistance to professional accountants in implementing ISAs and to promote good practice. IAPS 1012 specifically provided “guidance to the auditor in planning and performing auditing procedures for financial statement assertions related to derivative financial instruments.” Accordingly, it is reasonable that a revised IAPS 1012 should not include new requirements for the audits of complex financial instruments; rather it should provide further explanation of the requirements most applicable in audits of complex financial instruments (for example, ISA 315,⁴ ISA 330,⁵ ISA 540⁶) and include examples of procedures that may be appropriate in the circumstances.

Linkage to the Clarified ISAs

7. The UK’s PN was based on the extant ISAs rather than the clarified ISAs. Conforming changes were therefore made to the PN to update it to the clarified ISAs. In some cases, this involved simply updating the references to the documents or ensuring that the language as quoted remained applicable. In other cases, it involved adding context to ensure that it was clear what the auditor’s obligations were as set out in the ISAs and how the guidance was meant to assist the auditor in fulfilling the requirement.
8. Further changes will be made to Agenda Item 6-B in light of respondents’ views on whether guidance is insufficient or not applicable in an international context. In addition, the Task Force intends to review the Clarified ISAs to determine whether there are additional requirements for which specific guidance relating to complex financial instruments could be developed and whether the guidance could be strengthened by linking it more closely to the requirements. For example, this may include further discussion on:
 - Professional judgment and professional skepticism;
 - Fraud and management bias;
 - Communication with those charged with governance and others (for example, regulators and prudential supervisors)
 - Materiality;
 - Responses to significant risks;
 - Evaluating audit evidence;

⁴ ISA 315, “Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment.”

⁵ ISA 330, “The Auditor’s Responses to Assessed Risks.”

⁶ ISA 540, “Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures.”

- Management’s use of an expert;
- The use of the going concern assumption; and
- Reporting considerations, including modified reports when an inability to obtain sufficient appropriate audit evidence results in a scope limitation.

Use of Specialized Skill or Knowledge in the Audit

9. The PN also did not reflect the changes that the IAASB has made to clarify the distinction between a person with specialized skills or knowledge who is part of the engagement team and an auditor’s expert as defined by ISA 620.⁷ Changes to the PN were required to differentiate between these two scenarios (see paragraphs 29a-34 of Agenda Item 6-B).
10. The Task Force believes it is also necessary to enhance the guidance on when and how such specialized skills may be needed in auditing complex financial instruments. For example, an engagement partner may want to involve firm specialists in complex financial instruments in planning the audit, to identify the risks of material misstatement associated with such instruments and effectively design audit procedures to respond to those risks. These specialists may only be able to assist with the understanding of the instruments, and others may be needed to assist the engagement team’s testing of management’s valuation or if the auditor intends to develop a model to compare with management’s valuation.
11. The distinction between when this expertise would be considered to be “accounting or auditing expertise” (and therefore be scoped into the engagement team) or expertise in another field may not always be clear. Paragraph A1 of ISA 620 notes that expertise in a field other than accounting or auditing may include expertise in relation to the valuation of complex financial instruments, and paragraph A2 of the ISA explains that there is a distinction between expertise in methods of accounting for financial instruments, and expertise in complex modeling for the purpose of valuing financial instruments. This distinction has been incorporated into the revised IAPS.

Estimation Uncertainty and Significant Risks

12. In revising ISA 540, the IAASB determined it necessary to emphasize the concepts of estimation uncertainty and significant risks. In the Task Force’s view, these concepts were not highlighted in sufficient detail in the PN. Therefore, changes have been made to the revised IAPS to illustrate the relationship between estimation uncertainty and the auditor’s assessment of the risks of material misstatement (see paragraphs 20 and 23a). Further discussion of how estimation uncertainty and significant risks relate to the auditor’s obligations to disclosures has also been included (see new paragraphs 139a-139c). The Task Force is still considering potential responses to significant risks associated with complex financial instruments.

⁷ ISA 620, “Using the Work of an Auditor’s Expert,” defines an auditor’s expert as: “An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence. An auditor’s expert may be either an auditor’s internal expert (who is a partner or staff, including temporary staff, of the auditor’s firm or a network firm), or an auditor’s external expert.”

Management's Expert

13. Paragraphs 128-132 of Agenda Item 6-B provide guidance on the auditor's procedures when management uses an expert. In such circumstances, the provisions of ISA 500⁸ apply to the auditor's evaluation of the management expert's work. This scenario is fairly common when management uses a pricing service or broker for a valuation. In such cases, management's reliance on the expert may be substantial. There are differing views among auditors and others as to whether the auditor's degree of understanding of the entity and its complex financial instruments changes depending on whether the process is done within the entity or whether one or more third-party experts are used. For example, if the management's expert is a well-known, competent and objective expert, some argue that the auditor can rely on the expert's competency and experience and may not need as thorough of an understanding of the valuation processes, assumptions and methods for a particular instrument. They likewise argue that in such cases the auditor does not need to test the assumptions and methods as thoroughly. However, others contend that reliance on the expert's competency and expertise is not sufficient to discharge the auditor's responsibility to obtain an understanding of the expert's assumptions and methods and also to evaluate the reasonableness and appropriateness of them.
14. The Task Force believes it will be necessary to include additional guidance to make it more clear that the requirements for the auditor to understand how management makes the valuation, including the method used and the underlying assumptions,⁹ and obtain sufficient appropriate evidence supporting that valuation¹⁰ are not mitigated by the involvement of a management's expert. The degree in which this is done will depend on the IAASB's views as to whether there is in fact a distinction in the work effort.

Matters for IAASB Consideration

1. Does the IAASB believe the changes made to paragraphs 29a-34 are appropriate, including the addition of new guidance?
2. Should more be said in these paragraphs to promote the use of experts on an engagement involving complex financial instruments?
3. Is the new guidance on estimation uncertainty and significant risks in paragraphs 20, 23a, and 139a-139c sufficient and appropriate? Should the Task Force develop potential responses to significant risks associated with complex financial instruments?
4. Does the IAASB have preliminary views on the level of understanding needed when management uses an expert? Would further guidance in the IAPS be helpful to enhance consistency in practice, other than those stated in paragraphs 128-132?

⁸ ISA 500, "Audit Evidence."

⁹ ISA 540, paragraph 8.

¹⁰ ISA 540, paragraphs 12-17.

III. Key Issues Considered by the Task Force

Structure of Revised IAPS 1012

15. Extant IAPS 1012 includes guidance on derivative instruments and activities, and then follows the typical progression of an auditor's work – outlining the responsibilities of management, those charged with governance and the auditor, discussing the auditor's need to understand the business and key financial risks, and highlighting substantive procedures that may be typical in an audit of derivative financial instruments.
16. On the other hand, more than a third of the PN as currently drafted focuses on the auditor's need to understand the entity and its environment, including the understanding of the complex financial instruments to which an entity is exposed. While this understanding is integral to the auditor's risk assessment, and therefore the designing and performing of audit procedures in order to obtain sufficient appropriate audit evidence, it may be that either (a) more is needed to adequately balance the IAPS or (b) some of this material should be condensed. Some Task Force members are of the view that Agenda Item 6-B is too lengthy for readers of the document, especially those who would need to translate the IAPS. This may discourage the intended audience from reading it, which may obscure its usefulness. Others, however, believed that the guidance that has been included is appropriate and would be useful to auditors.
17. Respondents to the Consultation Paper have been asked for their views as to the overall structure and content of the PN. In analyzing these responses, the Task Force will consider whether improvements can be made to condense some of the material.

Extent of Material Relating to Best Practices

18. The PN contained a number of references to procedures that entities using complex financial instruments should have in place or actions entities should take in valuing complex financial instruments. These present tense statements seem to be best practices, but may not necessarily be in place at non-financial institutions or smaller entities. See, for example, paragraphs 75 to 84 of Agenda Item 6-B, among others.
19. The Task Force considers that it is useful for auditors to have an expectation about what procedures may be in place at an entity and what type of evidence management may have to support its valuations of complex financial instruments. However, in setting auditing standards, the IAASB can only impose requirements on auditors, and cannot dictate management's policies and procedures. Accordingly, the PN has been revised to remove these present tense.
20. Softening the language in the IAPS may, however, lessen the effect that raising auditors' awareness to these best practices may have. The Task Force believes that such guidance provides useful context to auditors (although in some cases it may represent what is already commonly understood about complex financial instruments) but has mixed views on whether this information should be included in the body of the IAPS or whether it would be more appropriate to include such material as best practice examples in an Appendix, in part to reduce the length of the document. The Task Force intends to consider this matter further in light of respondents' views.

Applicability of the IAPS to SMEs and the Public Sector

21. While complex financial instruments are often held by large entities with sophisticated systems of controls, this is not always the case, as they are sometimes held by smaller entities including SMEs. In addition, auditors dealing with less complex financial instruments may still encounter issues relating to valuation of those instruments, for example, when markets become illiquid. The challenges of auditing complex financial instruments vary depending, in part, on the size of the entity and the complexity of the instruments themselves. The Consultation Paper noted the expectation that a revised IAPS 1012, like the ISAs, would be able to be applied in a manner proportionate with the size and complexity of an entity and its financial instruments and would be of assistance to auditors in a variety of environments.
22. The PN explains that the general principles applicable to auditing complex financial instruments are applicable to all entities and provides guidance on how it can be applied when auditing entities of all sizes and to financial instruments of varying complexity (see paragraphs 7-12 of Agenda Item 6-B).
23. Some Task Force members were of the view that the content of the PN focuses on larger financial institutions and it is not entirely clear how the PN can be applied in audits of smaller entities or non-financial institutions. Another Task Force member noted financial institutions whose primary business involves complex financial instruments may have different risks relating to complex financial instruments, for example, involving the use of the going concern assumption, and it may be necessary to provide further guidance to clarify the scenarios in which these instruments may be used and how that affects the auditor's risk assessment and further procedures.
24. Respondents to the Consultation Paper have been asked for their views as to the balance of the guidance and if the IAPS would be more helpful if it was focused at another level, and further changes to Agenda Item 6-B will need to be made. One means of doing so would be to include considerations specific to smaller entities within the IAPS.
25. Additionally, valuation of complex financial instruments may have particular implications for public sector auditors, for example when governments provide financial assistance to companies and assume an ownership interest in the entity. Depending upon comments received, it may also be necessary to include considerations specific to public sector entities within the IAPS after consultation with representatives from the International Organization of Supreme Audit Institutions (INTOSAI) and Staff of the International Public Sector Accounting Standards Board (IPSASB).

Matters for IAASB Consideration

5. What are the IAASB's preliminary views as to the overall structure and content of the revised IAPS 1012, for example, in relating to the length and flow of the document, and whether it is appropriate that the entire document be drafted to apply to entities of all sizes?
6. The IAASB is asked for its preliminary views on the appropriateness of this best practice material, in particular whether it should:
 - (a) Remain in the body of the revised IAPS;

- (b) Be moved to an Appendix; or
- (c) Be eliminated altogether from the document.

7. Should considerations specific to SMEs or the public sector be developed?

Disclosure and Reporting Considerations

26. The question of the nature and extent of the auditor’s procedures on disclosures included in the financial statements is growing in importance. For that reason, the Consultation Paper solicited views on whether more guidance is needed to address how the auditor would obtain sufficient appropriate audit evidence when the disclosures about risks and uncertainties are qualitative in nature or the information is derived from information systems that are not otherwise used to generate information for inclusion in the financial statements. While responses to the Consultation Paper on this issue will be fully considered at the March 2010 IAASB meeting, the Task Force is of the view that more is needed in the revised IAPS on how the auditor deals with disclosures and believes it is useful to get the IAASB’s preliminary views on the way forward.
27. Accounting standard setters and regulatory bodies are also establishing more requirements for disclosures both in the body of the financial statements and outside the financial statements, for example in management’s discussion and analysis. In April 2009, the International Accounting Standards Board (IASB) issued amendments to International Financial Reporting Standard (IFRS) 7.¹¹ The IASB acknowledged that enhanced disclosures were needed to provide users of financial statements with useful information about valuations, methodologies and the uncertainty associated with fair value measurements. The amendments clarify and enhance disclosure requirements about the nature and extent of liquidity risk arising from financial instruments, and were developed in response to application issues raised by preparers and auditors. Enhanced disclosure requirements result in disclosure that better enable users to evaluate an entity’s exposure to liquidity risk arising from financial instruments and how the entity manages this risk.
28. The US Financial Accounting Standards Board (FASB) has also issued an exposure draft, “Improving Disclosures about Fair Value Measurements,”¹² which aims to fine-tune the FASB’s existing standard so as to mirror the IASB’s amendments to IFRS 7. Other accounting standard setting boards, including the Accounting Standards Board of Japan (ASBJ), are working toward the same direction. These new disclosures relate to the hierarchy of inputs to valuation, ranging from level 1 (the most observable, quoted prices in active markets) to level 3 (inputs not based on observable market data, known as unobservable inputs). A summary of the disclosure requirements of IFRS 7 is included in the Appendix. The preparation of disclosures in accordance with these revised standards requires a significant amount of professional judgment by the preparer to determine the

¹¹ IFRS 7, “Financial Instruments: Disclosures.” The amendments to IFRS 7 are to be applied for annual periods beginning on or after January 1, 2009.

¹² The exposure draft relates to Subtopic 820-10 of the *FASB Accounting Standards Codification*, originally issued as FASB Statement No. 157, *Fair Value Measurements*.

nature and extent of the disclosures needed to properly comply with the requirements.

29. Other regulatory authorities have also recently issued publications relating to disclosures, primarily relating to financial institutions. The UK Financial Services Authority recently issued a publication “Enhancing Financial Reporting Disclosures by UK Credit Institutions”¹³ and is considering whether it would be appropriate to make enhanced disclosures mandatory for UK credit institutions to promote international best practice.
30. The Committee of European Banking Supervisors has also recently published for public consultation its draft disclosure guidelines¹⁴ intended to help institutions improve their risk disclosures in the wake of the financial crisis and in response to calls from the Financial Stability Board for such disclosures to be more transparent.

Matters for IAASB’s Consideration

31. Paragraphs 136-141 of Agenda Item 6-B deal with the concepts of presentation and disclosure. The draft IAPS explains that the auditor’s conclusion as to whether the complex financial instruments are presented in conformity with relevant legislation, regulations and applicable financial reporting framework is based on the auditor’s judgment relative to a number of factors (see paragraph 139). One important factor is whether the financial statements show a true and fair view (or, alternatively in the ISAs, present fairly, in all material respects); the auditor’s conclusion in this regard is likely to have implications on the auditor’s report.
32. The presentation of financial statements in accordance with the applicable financial reporting framework includes adequate disclosure of material matters. Consequently, the auditor’s responsibility to form an opinion on the financial statements in accordance with ISA 700¹⁵ includes evaluating the adequacy of disclosures in the financial statements. In forming an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor evaluates whether the financial statements provide adequate disclosures to enable the intended users to understand these material matters.
33. Such disclosures are relevant to users in understanding the accounting estimates recognized or disclosed in the financial statements, and sufficient appropriate audit evidence needs to be obtained about whether the disclosures are in accordance with the requirements of the applicable financial reporting framework. However, the ISAs currently do not contain a substantive amount of guidance in doing so and the Task Force believes there is a need for further guidance to promote consistency in practice with respect to the auditor’s procedures on disclosures.
34. Evaluating the reasonableness of disclosures in the financial statements relating to complex financial instruments, whether required by the applicable financial reporting framework or

¹³ The FSA’s discussion paper can be accessed at http://www.fsa.gov.uk/pubs/discussion/dp09_05.pdf.

¹⁴ The CEBS’s proposed guidelines can be accessed at: <http://www.c-ebs.org/getdoc/bfc84fba-a46d-4f47-943c-b8e88a691e38/CP30-CEBS-Disclosure-guidelines.aspx>.

¹⁵ ISA 700, “Forming and Opinion and Reporting on Financial Statements.”

disclosed voluntarily, involves essentially the same types of considerations applied when auditing complex financial instruments recognized in the financial statements. This could be made clearer in the IAPS and parallels can be drawn to the information included in ISA 540 for understanding and testing accounting estimates to suggest this (see new paragraphs 138d-138e of Agenda Item 6-B).

35. The Task Force believes it would also be helpful for the IAPS to acknowledge the implications of more qualitative or quantitative disclosures on the auditor's procedures, in particular as the accounting frameworks are converging with respect to disclosures relating to financial instruments. Paragraphs 137-138a of the IAPS describe their nature, under IFRS, of disclosures about risks and uncertainties related to complex financial instruments, but the Task Force is of the view that the IAPS could expand upon the nature and extent of audit procedures to be performed to provide reasonable assurance as to the reliability of such disclosures.
36. Some concern has been expressed, in particular by auditors, that any new guidance should not be prescriptive and should allow for flexibility. The varying nature of the disclosures and their complexity require the auditor to exercise professional judgment in determining the amount of audit evidence needed, and the procedures to be performed, to support the auditor's opinion on whether such disclosures are adequate in accordance with the applicable financial reporting framework. The more qualitative analysis, i.e., the auditor's assessment of whether such disclosures achieve fair presentation, is difficult to describe and is a subjective process.
37. Bearing this in mind, the Task Force believes it may be useful to provide some key principles adapted from the FSA and CEBS guidance discussed above to highlight factors for the auditor to consider in evaluating whether the financial statements achieve fair presentation. These factors may include whether:
 - The disclosures faithfully represent the underlying transactions and event and adequately discuss areas of uncertainty.
 - The disclosures include relevant information to enable users to make a meaningful assessment of an entity's risks and financial situation.
 - Disclosures adequately allow for comparison over time.
 - The entity has adequate internal verification processes in place to support its disclosures.
 - Disclosures are presented in a meaningful way, for example in one place in the financial statements with appropriate cross-references as necessary.
 - Disclosures are provided at an appropriate level of detail to achieve transparency, while avoiding boilerplate or formulaic disclosures.

Changes Made to the Practice Note

38. Initial changes made to the PN include:

- Including additional material in the context of the issues described above;
- Linking to the presentation and disclosure assertions included in ISA 315;¹⁶
- Incorporating relevant requirements from ISA 540 and other standards;
- Describing the auditor’s responsibilities for disclosures in forming an opinion in ISA 700; and
- Including general references to matters that may be required to be disclosed by financial reporting frameworks.

Further changes are anticipated in light of the IAASB’s views on the matters discussed above and responses to the Consultation Paper and will be discussed in more detail at the March 2010 meeting.

Matters for IAASB Consideration

8. Is the guidance included in paragraphs 136-141 of Agenda Item 6-B on disclosures helpful?
9. Is more guidance needed on the audit of disclosures? For example, does the IAASB agree that the principles in paragraph 37 of this paper could be incorporated in a revised IAPS?

¹⁶ For reference, these include: (i) Occurrence and rights and obligations—disclosed events, transactions, and other matters have occurred and pertain to the entity; (ii) Completeness—all disclosures that should have been included in the financial statements have been included; (iii) Classification and understandability—financial information is appropriately presented and described, and disclosures are clearly expressed; and (iv) Accuracy and valuation—financial and other information are disclosed fairly and at appropriate amounts.

Appendix

Disclosure Requirements in Amended IFRS 7

The following table illustrates the significant disclosures relating to financial instruments included in IFRS 7. The US FASB is in the process of amending its fair value standard to converge with the amended requirements in IFRS 7, similar requirements were noted in the exposure draft.

Disclosures required by IFRS 7 are intended to enable users of the financial statements to evaluate:

- (a) The significance of financial instruments to an entity's financial position and performance; and
- (b) The nature and extent of risks arising from financial instruments to which the entity is exposed at the end of the reporting period, and how the entity manages those risks.

While the IASB characterizes the majority of the disclosures of IFRS 7 as quantitative disclosures,¹⁷ many of the disclosures will require significant judgment by preparers and auditors. Accordingly, the Task Force is of the view that disclosure requirements can typically be characterized in three main categories:

- (a) Quantitative disclosures that are derived from the amounts included in the financial statements – for example, categories of financial assets and liabilities;
- (b) Quantitative disclosures that require significant judgment – for example, sensitivity analysis for each type of market risk to which the entity is exposed; and
- (c) Qualitative disclosures – for example, those describe the entity's objectives, policies and procedures for managing each type of risk arising from financial instruments and the methods used to measure the risks.

Changes have been made to paragraphs within Agenda Item 6-B to bring in the most relevant disclosure requirement from amended IFRS 7 to the extent such information was not included in the UK's Practice Note. Preliminary views on where issues may arise for preparers and auditors are highlighted in the table on the following page.

¹⁷ Only the requirement in paragraph 33 of amended IFRS 7 is classified as a qualitative disclosure. It states:

“For each type of risk arising from financial instruments, an entity shall disclose:

- (a) the exposures to risk and how they arise;
- (b) its objectives, policies and processes for managing the risk and the methods used to measure the risk; and
- (c) any changes in (a) or (b) from the previous period.”

Disclosure Requirement (Amended IFRS 7 reference)	Potential issues for preparers and auditors	Paragraph reference in Agenda Item 6-B
<i>Disclosures about the significance of financial instruments to an entity's financial position and performance</i>		
<p>Hedge accounting, including:</p> <ul style="list-style-type: none"> • a description of each type of hedge, a description of the financial instruments designated as hedging instruments and their fair values at the end of the reporting period, and the nature of risks being hedged; • Cash flow hedges • Gains or losses on hedging instruments and the hedged item, and the ineffectiveness of cash flow hedges and hedges of net investments in foreign operations. (para. 22-24) 	Evidence and its assessment by auditors is required to support management's designation as a hedge. Cash flow hedges will also require more substantive judgment about the periods when cash flows are expected to occur and when they are expected to affect profit or loss.	133-135, 136e.
<i>Fair Value Disclosures</i>		
The fair value of each class of assets and liabilities at the end of the annual reporting period (para. 25-26)	Measurement at fair values can be challenging depending on the instrument being reported.	Valuation guidance, including para. 110-132
The methods used and the assumptions applied in determining fair value and any changes in valuation techniques and the reason for the change (para. 27)	Deciding when to change valuation techniques may be arbitrary and auditors may not agree with the proposed change.	Valuation guidance, including para. 110-132, 136d.
The level within the fair value hierarchy into which the fair value measurements are categorized in their entirety (para. 27a)	Classification in the hierarchy may be subjective. When management uses a third party to prepare valuations, they may be dependent on the third party for these classifications. Auditors will need to understand how this information is derived.	136f.
<p>For fair value measurements recognized in the statement of financial position:</p> <ul style="list-style-type: none"> • The amount of any significant transfers into and/or out of Levels 1 	While these appear on the surface to be quantitative disclosures, preparing these disclosures requires significant judgment. In particular, the sensitivity analysis	138b.-138c., 138e.

Disclosure Requirement (Amended IFRS 7 reference)	Potential issues for preparers and auditors	Paragraph reference in Agenda Item 6-B
<p>and 2, and the reasons for those transfers</p> <ul style="list-style-type: none"> • Level 3 Roll-forward: <ul style="list-style-type: none"> ○ Total gains or losses for the period ○ Purchases, sales, issues and settlements ○ Transfers into and/or out of Level 3 • Amount of gains or losses for the period included in profit or loss related to assets or liabilities still held at the reporting date • Sensitivity analysis for Level 3 (para. 27B) 	<p>for level 3 instruments requires disclosure of reasonably possible changes in assumptions which would significantly change their value.</p> <p>These disclosures may also not be derived from the financial reporting system and may be prepared by third parties, such as a management's expert.</p>	
Financial instruments in inactive markets (para. 28)	Difficulties in valuation will result from inactive or illiquid markets. The amount of evidence that may be available may also be limited, and/or auditors may need to use multiple sources of evidence	5, 79, 116-117
Disclosures when fair value information cannot be measured reliably (para. 30)	These disclosures become more important and are likely more judgmental.	139d.
<i>Disclosures about the nature and extent of risks arising from financial instruments</i>		
<p>Qualitative disclosures for each type of risk arising from financial instruments:</p> <ul style="list-style-type: none"> • The exposures to risk and how they arise • The entity's objectives, policies and processes for managing the risk and the methods used to measure the risk • Any changes in the above from the previous period (para. 33) 	These disclosures can often become boilerplate and lengthy. It is important for the auditor to assess whether they provide clear and meaningful disclosure.	137-138, 138e, 139-141
Quantitative disclosures about each type of risks arising from financial instruments:	Auditors should perform the same level of procedures on the quantitative amounts as if these	138d,136g, 140

Disclosure Requirement (Amended IFRS 7 reference)	Potential issues for preparers and auditors	Paragraph reference in Agenda Item 6-B
<ul style="list-style-type: none"> • Summary quantitative data about exposure to risk at the end of • Concentrations of risk • Additional information if the quantitative data is underrepresentative of the exposure to risk • Credit risk (including maximum exposure) (para. 34-36) 	<p>amounts were recorded in the financial statements. However, the risk assessment is a subjective process.</p> <p>IFRS 7 notes the disclosure is based on information provided to key management personnel. This information most likely not derived from the financial reporting system.</p>	<p style="text-align: center;">High estimation uncertainty and Significant risks 139a-139c</p>
<p>Liquidity risk, including a maturity analysis for derivative financial liabilities, including the remaining contractual maturities for those derivative financial liabilities for which contractual maturities are essential for an understanding of the timing of the cash flows, and how the entity manages its liquidity risk (para. 39)</p>	<p>This disclosure is meant to illustrate the risk that the entity will encounter difficulty in meeting commitments associated with financial liabilities. This is a subjective analysis that may be subject to management bias.</p>	<p style="text-align: center;">59(b), 145-147</p>