Prof. Arnold Schilder

Chairman

IAASB

529 5th Avenue

10017, New York

The US

Submitted via website

Brussels, 31 July 2017

SUBJECT: IAASB PROPOSES MODERNIZATION OF FINANCIAL ESTIMATE AUDITS IN SUPPORT OF AUDIT QUALITY

Dear Sir,

(1) Accountancy Europe is pleased to provide you with its comments on the IAASB's proposal to modernise the financial estimate audits in support of audit quality. We support the IAASB´s decision to explore this topic. The revision of ISA 540 is essential to ensure the standard remains fit for purpose in light of today's evolving and complex business environment.

(2) We acknowledge that ISA 540 is an important standard which deals with various issues. We recognise IAASB's effort to provide sufficient guidance in the diverse circumstances in which ISA 540 should apply, ranging from simple accounting estimates to very complex ones. Accounting estimates are one of the major issues identified globally in regulatory audit inspections, specifically around the lack of auditor challenge and apparent shortcomings in the application of professional scepticism.

(3) The introduction explains that accounting estimates are subject to inherent limitations, which means that it is impossible for either preparers or auditors to reduce estimation uncertainty beyond certain limits. This statement should be more explicitly linked to the requirements in the standard, in particular related to the resulting challenge for preparers and the auditor in relation to such measurement uncertainty.

(4) We are also aware of concerns expressed in the past that a narrow-scoped ISA 540 could result in auditors overlooking some accounting estimates that ought to be addressed in a specific way, if auditors erroneously would assess the ISA 540 standard as not applicable to individual client circumstances. The IAASB should make sure this is considered as part of the revision of ISA 315.

(5) Furthermore, there is anticipation of possible changes of ISA 315 already in ED-540 and therefore we would have favoured that the revision of both standards be done in parallel. Whilst we understand the urgency of delivering on ISA 540, this could cause some confusion and we urge the IAASB to coordinate the finalisation of ISA 540 with its project to revise ISA 315.

(6) Whilst helpful, the application material is lengthy and reads like implementation guidance. It might be seen as excessive in comparison with application and other explanatory material in other ISAs; the IAASB might consider whether it would be better supplied in another form outside of the standard to auditors who wish to have a comprehensive reference, i.e. perhaps in the form of an International Auditing Practice Note (IAPN), particularly for the aspects of the explanatory material that are linked to the financial sector.

(7) We welcome the IAASB's supplement to proposed ISA 540 (Revised)[1], which illustrates the work effort requirements. It explains the reasoning behind paragraphs 13-23 of the Exposure Draft (ED-540) and thus facilitates the understanding of the requirements. The IAASB should consider including this flowchart as an appendix to the revised standard.

SPECIFIC ISSUES CONSIDERED IN THE APPENDIX TO THIS LETTER

(8) The explanatory memorandum to ED-540 gives a lot of prominence to the application of professional scepticism. Whilst we welcome the steps taken by the IAASB to drive actions that promote professional scepticism, we think it remains a challenging area and, even with the best effort, applying professional scepticism can never overcome the inherent estimation uncertainty of accounting estimates included in the financial statements. Being more explicit regarding this might help manage expectations. We draw your attention to our response to question 2 that expands upon this point.

(9) Moreover, we recognise the IAASB's attempt to address scalability in ED-540. Although the proposal may be a step in the right direction, we have some concerns that it will not achieve the level of scalability that is desired. One example of this is with regards to paragraph 10, which on one hand provides a good framework for assessing the inherent risk of an estimate, but equally creates a significant work effort even in cases where the estimate is clearly of a low inherent risk. Equally, we are also concerned that requirements in paragraph 10 (f) create confusion as to the extent to which the auditor should consider internal controls, and the benefit of doing so in those cases where the auditor has reason to believe inherent risk is low. With the inherent risk consideration as a cornerstone of the revised standard approach, the extent of and reasons for auditor's work on the internal control assessment needs to be clear. Considering audits that may have to deal with a large number of low inherent risk estimates, both of these matters could create a significant work effort for which the value is unclear. We draw your attention to our response to question 3 that expands upon this point.

(10) Where inherent risk is not low, ISA 540 requires the auditor to consider three factors, being measurement uncertainty, judgement and complexity. We question whether these three factors should be seen as equivalent in terms of importance and suggest an alternative two-step approach that focuses primarily on significant estimation uncertainty to address this issue. We draw your attention to our response to question 4 that explains this argument further.

[1] IFAC (2017) *Supplement to Proposed ISA 540 (Revised) Work flow chart* [online] Available at: https://www.ifac.org/system/files/publications/files/Supplement-to-Proposed-ISA-540-Revised-Work-Flow-Chart.pdf

(11) Moreover, in some situations where the inherent risk is not low, we think that the response to the assessed risks of material misstatements could be disproportionately high. We refer to the wording of paragraph 19 (b) of the ISA 540. The explanation in paragraph A126 of the application material and the work effort that it may entail for the auditor –could be read as if ISA 540 encourages the auditor to carry out work that falls under the responsibility of management. In addition, it is noted in paragraph A134 of the application material that, in certain circumstances, the auditor's range for an accounting estimate may be multiples of materiality for the financial statements as a whole; in our opinion, this is important for all stakeholders to understand and, as such, the IAASB should give more prominence to this statement. We draw your attention to our response to question 5 that expands upon this point.

(12) Regarding complex accounting estimates, we anticipate that the field testing exercise will provide a valuable feedback as to whether the proposed requirements will lead to more effective identification and assessment of, and responses to, risks of material misstatement (including significant risks) relating to accounting estimates. We applaud the IAASB for initiating this field testing. We expect that the IAASB will evaluate the operability of the proposed new requirements based on the feedback received from the audit firms. We draw your attention to our response to question 4 for further information on complex accounting estimates.

(13) Our responses to the specific questions can be found in the attached appendix to this letter.

For further information on this letter, please contact Eleni Ashioti on +32(0)28933387 or via email at elenia@accountancyeurope.eu or Noémi Robert on +32(0)28933380 or via email at noemi@accountancyeurope.eu.

Sincerely,

Olivier Boutellis-Taft

Chief Executive

ABOUT ACCOUNTANCY EUROPE

Accountancy Europe unites 50 professional organisations from 37 countries that represent close to **1 million** professional accountants, auditors, and advisors. They make numbers work for people. Accountancy Europe translates their daily experience to inform the public policy debate in Europe and beyond.

Accountancy Europe is in the EU Transparency Register (No 4713568401-18).

ANNEX

OVERALL QUESTIONS

Question 1

Has ED-540 been appropriately updated to deal with evolving financial reporting frameworks as they relate to accounting estimates?

(1) We acknowledge the efforts to revise ISA 540 to deal with evolving financial reporting frameworks and their inclusion of accounting estimates, especially IFRS 9 Financial Instruments. Notwithstanding this, we share some observations below where some aspects of ED-540 might need further consideration.

(2) In addition to IFRS 9, we also acknowledge and support the fact that the revisions address further complexities arising from other new international accounting standards, for example IFRS 16 *Leases*, IFRS 15 *Revenue from Contracts with Customers*, IFRS 4 *Insurance Contracts.*

(3) A number of our members who deal with audits of insurance companies though are of the view that ED-540 is more focused on financial institutions' issues than on insurance companies' ones. IFRS 9 has been considered, but the timing did not allow consideration of IFRS 17. Yet, we note that there are a few areas where the proposals in the ED-540 have not proven to be adequate neither for the banking nor the insurance sector.

(4) Our members working in banking and insurance have expressed scepticism as to how the proposals as they stand, will enhance consistency in the audit of financial institutions. The material on the expected credit loss model (ECL) under IFRS 9 and technical provisions under IFRS 17 is thin.

(5) We strongly suggest that IAASB considers the development of guidance for the application of ISA 540 to the financial sector in the form of an IAPN. This should provide guidance on, among other things, the audit of forward-looking information and approaches to determining when a significant increase in credit risk has occurred. We understand that the Basle Committee is in favour of an IAPN for this sector.

(6) Our members in the banking sector are also rightly concerned about a lack of relevant guidance on internal control within the proposals. This is part of a wider issue about the audit of highly complex estimates. The quality of internal controls, and the control environment in particular, is critical in the audit of such estimates. While sector specific guidance is not appropriate for a general-purpose ISA, and we are satisfied that most of the proposed material on internal control is in the application material, these concerns point strongly to the need for an IAPN, developed on a timely basis, for the financial sector.

(7) Other examples of areas in which the proposals seem light, especially in the context of ECL and technical provisions under IFRS 17, include:

- the requirements relating to the 'stand back' and bias assessment;
- different types of reporting, including regulatory reporting;
- disclosures.

(8) Moreover, the references in paragraph A5 to the development of point estimates and ranges for components of estimates such as assumptions and data can be confusing for companies that operate in the banking sector. In effect, they amount to developing different assumptions and data against which to benchmark those used by management. What is critical is the impact of those on the actual ECL estimated by management.

(9) We also list below other comments with particular relevance to the audit of ECL:

- The application material on management's point estimate, 9(e), and on 17(a) and (b) on complexity, is limited. Ditto 17(e), 18(a) (iii), 18(c) (i) and (ii).
- The extent and depth of the required auditor understanding of applicable regulatory factors are not made clear in paragraph A15.
- There is a lack of application material addressing the audit of mid-sized entities. These are critical in the financial sector which has many, including smaller investment businesses and banks, which are nonetheless Public Interest Entities (PIEs).
- Paragraph A30 on auditing policy is light in relation to issues such as changes in credit risk, ditto paragraph A31 on model validation.
- Paragraph A73 is simplistic as a bank does not need to be active internally for ECL to be complex, subject to estimation uncertainty and involve judgement.
- Paragraphs A76 and A77 are insufficiently granular for the audit of ECL.
- Paragraph A86 seems to imply that estimation and judgemental differences are not misstatements, only known and factual ones are. The sentence beginning 'The variation in the measurement of an accounting estimate…' should perhaps state 'The variation in the measurement of an accounting estimate that results from estimation uncertainty is not necessarily, in itself, a misstatement'.
- Paragraph A104 is light in terms of ensuring that appropriate data is used in a model and assessing the appropriateness of management assumptions.

Question 2

Do the requirements and application material of ED-540 appropriately reinforce the application of professional scepticism when auditing accounting estimates?

(10) The explanatory memorandum to ED-540 includes significant discussion of professional scepticism to the extent that it suggests the matter would be given greater prominence in the revised standard than it actually is. Having said that, the overall evaluation based on the audit procedures performed is a good aspect of ED-540 that implicitly reinforces the application of professional scepticism.

(11) Whilst we welcome the steps taken by the IAASB to drive actions that promote professional scepticism, we think it still remains a challenging area, particularly since the effective application of it is judged by others with the benefit of hindsight. In such instances, it is easy to conclude, sometimes unfairly, that the auditor did not take all the reasonable steps to evaluate the requirements in paragraphs 22 (a)-(c). Applying adequate professional scepticism is critical and we fully support and encourage the continuing work undertaken by the IAASB with the professional scepticism working group. When the work of this group is finalised, it will likely be necessary to consider consequential impact to existing ISAs, including ISA 540.

(12) Regulators have been significant contributors to the professional scepticism debate and we suggest that the IAASB continue liaising with these stakeholders for dialogue on external inspection findings in the area of accounting estimates. Accounting estimates with a high degree of inherent uncertainty require the application of greater judgement. The judgment as to whether there has been sufficient application of professional scepticism can be challenged at a later date by someone who has the benefit of hindsight. As such, even if ISA 540 appropriately reinforces the application of professional scepticism, this will not solve the issue of someone looking at the audit work and having the benefit of hindsight in comparison with the auditor performing the work with the facts and circumstances available at the time of the audit.

Question 3

Is ED-540 sufficiently scalable with respect to auditing accounting estimates, including when there is low inherent risk?

(13) We recognise the IAASB's attempt to properly address scalability in ED-540. The delineation for estimates of low-inherent risk is a practical approach that we favour. Including such a threshold clarifies the requirements for low-risk accounting estimates and is intended to help ensure that estimates assessed as low inherent risk are not subject to inappropriate audit procedures and that the work effort is focussed on those risks that have been evaluated as being other than low.

(14) Whilst some explanation in the introduction to ISA 540 is helpful, the wording included in paragraph 3 implies that the more extensive requirements apply to almost all financial statement line items. We do not believe this was the intention and, as such, the wording of this paragraph should be made clearer.

(15) The procedures listed in paragraph 10 provide a practical framework for risk assessment. However, even though these are clear, the fact that the auditor needs to prescriptively undertake all the procedures is cumbersome. The following related matters should be considered: firstly, there is no 'shortcut': even if it is clear and obvious that the estimate is of low risk, all procedures listed in paragraph 10 still have to be complied with. Secondly, it is unclear as to the extent of work required by paragraph 10 (f) related to controls and the value that this would bring to the audit in all instances, but especially when the auditor has reason to believe the inherent risk is low. Both matters could impose significant burden for non-complex SME audits which might have proportionately more low inherent risk estimates than complex larger entities. We understand that ISA 540 should be an application of ISA 315 and thus the introduction to paragraph 10 of a reference to the ISAs being founded upon an overriding principles-based framework, along with a list of potential procedures that might be advantageous.

(16) We also ask the IAASB to clarify if it should be understood that most SME audits have many low risk estimates. As this aspect is insufficiently clear, the issue of scalability has therefore, at best, only partly been addressed by the proposals. More relevant examples of better quality should be provided of the types of estimate and circumstances that might be evaluated as low risk.

(17) The interaction with the applicable financial reporting framework is important; albeit we acknowledge not under the control of the IAASB. Accounting frameworks applicable to SMEs are becoming more and more complex resulting in the creation of more complex accounting estimates in these entities. Preparers and users of financial statements start questioning the value of some of these complexities - which are often far removed from the key drivers of the business, such as operating profits leading to cash generation. Such estimates are for example those relating to certain intangible assets or financial instruments. It is likely that, under the proposed ED-540, such estimates would be considered not of low inherent risk. The result is likely to be that for the whole reporting chain that includes the preparer, the user and the auditor, the audit work effort will be considered as disproportionate. As already noted, the root cause likely lies with the accounting framework, but as views on the scalability of ISA 540 is likely to be linked to this, it is important to draw the attention of the IAASB to it.

(18) The above could perhaps be mitigated to some extent if the IAASB would reinforce the need to look at the concept of 'material misstatement' from the users' perspective. For instance, an accounting estimate may have inherent risk that is low not because the measurement uncertainty is low, but because the issue does not influence the economic decisions of the users of the financial statements.

(19) Expanding on the point made above, some amendments to the wording of the work effort should be considered when the inherent risk is low. According to paragraph 15 of the proposed requirements, the auditor is not required to design and perform test of controls. Nonetheless, in paragraph 10 (f), when discussing about the risk assessment procedures and related activities, the auditor is required to obtain an understanding of each component of internal controls in relation to accounting estimates. These will likely require quite detailed analysis and could create significant amount of work in respect of 'low inherent risk' accounting estimates. We do not believe this was the intention, but it creates at least confusion as to whether the auditor should consider internal controls or not when inherent risk is low. We suggest as a minimum that this ambiguity be removed and that the IAASB consider whether there would be any value from the auditor undertaking step 10 (f) in all instances, but especially when the auditor has reason to believe the inherent risk is low.

(20) In addition, the extensive related application material is largely applicable to larger audits and the only reference to the need for auditors to understand controls relevant to the audit (as required by ISA 315) is in paragraph A100 and even then, only in the context of 'very small entities'. The absence of reference to controls 'relevant to the audit' in paragraph 10 (f) has the effect of overstating the case. Paragraph A100 errs on the side of caution in this respect stating that controls may not be relevant to the audit in audits of all sizes.

(21) There is also a difference in volume of material in the standard between the sections dealing with low inherent risk and not low inherent risk. We acknowledge the examples provided in the application material in paragraph A72, where the auditor's assessment of the risk of material misstatement may be based on low inherent risk but note that, even in these selected examples, depending on the facts and circumstances, an accounting estimate might result in being an inherent risk that is not low. For instance, regarding bonus accrual for management, we would argue that there is an increased risk of management bias where the profitability of the entity may affect the accounting estimate (namely their bonus) which will lead to the conclusion that the inherent risk is not low. To avoid any possible misinterpretation of these examples, we suggest including a sentence in paragraph A71 to reflect how important it is for the auditor to consider the specific facts and circumstances before concluding if an inherent risk is low or not low. Also, the IAASB should include better quality examples or at least give a more nuanced description of the current examples.

(22) Related to this, it is currently unclear how inherent risk, as a concept, ties in with the requirements in ISA 315. For instance, the concept of significant risk does not explicitly include a reference to inherent risk. There is scope for confusion in the application of the standard because inherent risk is not defined with reference to significant risk. We would therefore welcome guidance reconciling the two concepts.

(23) There is also little information in ISA 315 or ISA 200 to support what is meant by inherent risk. The IAASB needs to explore this further to avoid confusion between inherent risk, business risk and significant risk.

(24) Furthermore, we would suggest clarifying the wording in paragraph 15 (a) where it states ''when inherent risk is low, the auditor shall determine whether one or more of the following further audit procedures would provide sufficient appropriate audit evidence regarding the assessed risk(s) of material misstatement''. The use of the word 'whether' could be aggressively interpreted to allow an auditor to choose not to do any further audit procedures at all. We would welcome clarification on this issue.

(25) If it is what was intended, we believe the IAASB should also clarify in ED-540 that the auditor is required to set the inherent risk on an account balance level rather than to the entire entity.

When inherent risk is not low (see paragraphs 13, 15 and 17–20):

- *a) Will these requirements support more effective identification and assessment of, and responses to, risks of material misstatement (including significant risks) relating to accounting estimates, together with the relevant requirements in ISA 315 (Revised) and ISA 330?*
- *b) Do you support the requirement in ED-540 (Revised) for the auditor to take into account the extent to which the accounting estimate is subject to, or affected by, one or more relevant factors, including complexity, the need for the use of judgment by management and the potential for management bias, and estimation uncertainty?*
- *c) Is there sufficient guidance in relation to the proposed objectives-based requirements in paragraphs 17 to 19 of ED-540? If not, what additional guidance should be included?*

QUESTION 4A

(26) We agree that the requirements when an inherent risk is not low should support more effective identification and assessment of, and responses to, risks of material misstatement (including significant risks) relating to accounting estimates. As drafted, the proposed paragraph 13 of ED-540 would require the auditor to take into account – at least – these three factors specifically when complying with these requirements of ISA 315 (i.e. in assessing the risk of material misstatement attaching to an accounting estimate). Thus, this paragraph explains how ISA 315 should be applied in relation to accounting estimates, but goes further in specifically requiring the auditor to take into account one or more factors that may be relevant to the risk assessment in the case of an accounting estimate. There is also sufficient application material to help the user of the standard apply the requirements effectively.

(27) In relation to significant risk, the relative significance of the measurement uncertainty factor in any given accounting estimate plays the key role in the approach as included in the revised standard. In our view, on the basis of the revised definition, the final standard needs to include more material than currently proposed in the context of determining significant risk to support the auditor's compliance with paragraph 27 of ISA 315. Currently, paragraph 27 of ISA 315 is referred to, but not explained beyond consideration of complexity, need for management judgement, and estimation uncertainty amongst possible other factors. Paragraph A76 of ED-540 merely refers to ISA 315 in this context.

(28) The measurement of items that are subject to measurement uncertainty involves the use of one or more assumptions. The "relative precision" of an assumption is of primary relevance in determining whether an accounting estimate is, in the auditor's judgement, a significant risk. We agree that this should be specified along the lines proposed in paragraph 13 (c) and explained in paragraph A35, since when a reasonable variation in the data or assumption would materially affect the measurement of the accounting estimate, the measurement of this accounting estimate would constitute a significant risk.

(29) We also anticipate that the field testing exercise will provide a valuable feedback on whether the proposed requirements will lead to more effective identification and assessment of, and responses to, risks of material misstatement (including significant risks) relating to accounting estimates. We applaud the IAASB for initiating this. We expect that the IAASB will evaluate the operability of the proposed new requirements based on the feedback received from the audit firms.

QUESTION 4B

(30) We agree with the work effort as included in paragraphs 17-19 and with the concept as proposed. It is helpful to emphasise the concepts of management judgement and complexity, particularly in light of the new accounting standards introducing greater management judgement when determining accounting estimates, as well as a greater level of complexity in relation to some techniques and methodologies being applied.

(31) However, one consequence of this is that it may result in "routine" estimates that can be reliably measured, but which are based on management judgement such as general accruals, or are simply complex, to be included within the scope of ISA 540. We do not believe that this is the intention, but it needs to be clear to all stakeholders.

(32) We also observe that the three factors proposed are rather conceptual, not equivalent in terms of importance, and very different in nature. They are also not exclusive; depending on the circumstances, they can overlap. We anticipate that this could cause practical difficulties in application and one suggestion to overcome this would be to give greater prominence to the measurement uncertainty factor compared to the others, and perhaps a reordering of the factors; making it clear that the approach is a two-step one. The first step would be to identify if an accounting estimate is subject to significant measurement uncertainty and, if the case, the accounting estimate should be dealt with in ISA 540. If, however, there is no significant measurement uncertainty, then there is no reason to treat an accounting estimate differently from any other item of the financial statements provided that the matter that distinguishes them from other items in the financial statements (their measurement uncertainty) is not significant.

QUESTION 4C

(33) We suggest considering revising the wording in paragraph 16 which considers the design and testing of controls as it is currently unclear how this paragraph derives from paragraph 15. We suggest to explicitly link paragraph 16 to paragraph 15 (b) when inherent risk is not low since paragraph 15 (a) discusses situations where the inherent risk is low - which will not be relevant in the consideration of controls.

(34) We consider the definition of the term 'significant data', which is mentioned several times in paragraphs 17-18, to be important in the understanding of the respective requirements. We would therefore suggest moving the explanation included in paragraph A35 to the requirements' section 'Definitions' in page 31 of ED-540 - or otherwise have it properly signposted.

Question 5

Does the requirement in paragraph 20 (and related application material in paragraphs A128–A134) appropriately establish how the auditor's range should be developed? Will this approach be more effective than the approach of "narrowing the range", as in extant ISA 540, in evaluating whether management's point estimate is reasonable or misstated?

(35) The requirements in paragraph 20 do appropriately establish how the auditor's range should be developed. This approach should be more effective than the approach of "narrowing the range", as currently included in extant ISA 540, in evaluating whether management's point estimate is reasonable or misstated. The extant standard requires to ''narrow the range, based on audit evidence available, until all outcomes within the range are considered reasonable''. Such a requirement could result in an auditor's range that is inappropriately wide, as noted in ED-540.

(36) Nevertheless, in some respects, this response to the assessed risks of material misstatements can be seen as disproportionately high from the auditor's perspective. We refer to the wording of 19 (b) of the ISA 540. The explanation in paragraph A126 of the application material and the work effort that it may entail for the auditor – it can be read as if ISA 540 encourages the auditor to carry out the work that should rightly be undertaken by management. For instance, paragraph A126 states that the auditor may consider requesting management to consider alternative assumptions relating to estimation uncertainty. We would suggest that the IAASB take a firmer stance by requiring the auditor to first request such information from management and only if management is unable to provide this information then the auditor should proceed with developing a point of estimated or a range. In the case of the latter, the IAASB could also consider whether there should be an impact on the auditor's opinion in such a case. The same suggestion applies for paragraph 19 in ISA 540 where the IAASB only refers to the auditor obtaining sufficient appropriate audit evidence.

(37) The difference between the second and fourth bullets of paragraph A131 is also unclear. The former uses management's model and selects alternative assumptions or data sources to develop a point estimate or range, the latter uses alternative assumptions to those used by management. If the former involves independent inputs to management's model to assess the actual estimate, this can and should be clearer.

(38) Furthermore, it is noted in paragraph A134 of the application material that, in certain circumstances, the auditor's range for an accounting estimate may be multiples of materiality for the financial statements as a whole and that this measure might be relatively small in relation to assets or other balance sheet measures. The IAASB should give more prominence to this statement and to the fact that a reasonable auditor's range may often be larger than materiality.

(39) This is a challenging area where we would expect that the field testing exercise will help determine whether the approach proposed is indeed better than the ''narrowing the range'' approach in the extant ISA 540.

Question 6

Will the requirement in paragraph 23 and related application material (see paragraphs A2–A3 and A142–A146) result in more consistent determination of a misstatement, including when the auditor uses an auditor's range to evaluate management's point estimate?

(40) Pursuant to ISA 200, the auditor is required to obtain sufficient appropriate audit evidence to reduce the audit risk to an acceptably low level. ISA 200 paragraph 17 establishes this as a prerequisite to obtaining reasonable assurance and to enabling the auditor to draw reasonable conclusions on which to base the auditor's opinion. The proposed wording in paragraph 23 requires the auditor to evaluate "whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated". It would be useful to have clarity as to how this requirement ties into the auditor's opinion. The only other ISA that deals specifically with a line item in the financial statements is ISA 501.

(41) Moreover, we agree with using the term 'reasonable' when referring to accounting estimates. However, in relation to disclosures we recommend changing the word ''reasonable'' to ''appropriate'' Please refer to our response in question 8 (a).

(42) We also suggest placing paragraph 23 after paragraph 24 which deals with the auditor's evaluation whether there are indications of possible management bias.

CONFORMING AND CONSEQUENTIAL AMENDMENTS

Question 7

With respect to the proposed conforming and consequential amendments to ISA 500 regarding external information sources, will the revision to the requirement in paragraph 7 and the related new additional application material result in more appropriate and consistent evaluations of the relevance and reliability of information from external information sources?

(43) We generally agree with the proposed conforming and consequential amendments to ISA 500 regarding external information sources, but would counter that these may not always be publicly available. The revision to the requirement in paragraph 7 and the related new additional application material, will be helpful in resulting in more appropriate and consistent evaluations of the relevance and reliability of information from external information sources. It is important to think about information sources that are available from outside the organisation, considering the increased use of data analytics.

REQUEST FOR GENERAL COMMENTS

Question 8

In addition to the requests for specific comments above, the IAASB is also seeking comments on the matters set out below:

a) Translations—Recognizing that many respondents may intend to translate the final ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents note in reviewing the ED-540.

b) Effective Date—Recognizing that ED-540 is a substantive revision, and given the need for national due process and translation, as applicable, the IAASB believes that an appropriate effective date for the standard would be for financial reporting periods ending approximately 18 months after the approval of a final ISA. Earlier application would be permitted and encouraged. The IAASB welcomes comments on whether this would provide a sufficient period to support effective implementation of the ISA.

QUESTION 8A

(44) We previously noted that the consequences of using words such as “may” or “could” may, when translated, lead to different interpretations and meanings. The use of consistent terminology throughout the standards is particularly important to avoid difficulties in the eventual translation of the text. The IAASB has generally used “may” throughout its standards, and thus consistency would be appropriate going forward.

(45) We also recommend changing the word ‘reasonable’ to ‘appropriate’ when referring to disclosures. We refer to paragraph 21. As noted in paragraph A2, the word ‘reasonable’ means ‘all the relevant requirements of the applicable financial reporting framework have been applied appropriately’ whereas the term ‘appropriate’ includes also the element of judgement which is important when deciding what disclosures to make about the accounting estimates. Indeed, according to paragraph A3 ‘appropriate’ both conforms with the requirements of the applicable financial reporting framework and considers judgements that are consistent with the measurement basis in the applicable financial reporting framework.

QUESTION 8B

(46) We agree that an appropriate effective date for the standard would be for financial reporting periods ending approximately 18 months after the approval of a final ISA. We are also supportive of permitting and encouraging an earlier application.

(47) It is disappointing that ISA 540 cannot be published ahead of IFRS 9, which was the initial intention of the IAASB. Nevertheless, we understand that this standard is tackling several critical issues and therefore requires time to be developed. Having a well-developed standard will enhance the confidence of those using the standard and will help maintain audit quality.