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Submitted electronically

<http://www.ifac.org/publications-resources/proposed-international-standard-auditing-540-revised-auditing-accounting>

Mr Matt Waldron
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New York
10017 USA

Dear Matt

Comments on the IAASB's Proposed International Standard on Auditing 540 (Revised), Auditing Accounting Estimates and Related Disclosures

The Independent Regulatory Board for Auditors (IRBA) is both the audit regulator and national auditing standard setter in South Africa. Its statutory objectives include the protection of the public by regulating audits performed by registered auditors, and the promotion of investment and employment in the Republic.

We appreciate this opportunity to comment on the proposed International Standard on Auditing 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*, (E D - 5 4 0), developed by the International Auditing and Assurance Standards Board (IAASB).

Our response has been prepared from comments provided by departments of the IRBA and by a few technical and lead partners of banks from firms.

Our comments are presented under the following sections:

1. General comments;
2. Request for specific comments and responses;
3. Other matters; and
4. Editorial comments.

If further clarity is required on any of our comments, kindly e-mail us at nbester@irba.co.za. Alternatively, phone us directly on +27 87 940 8862.

Yours faithfully

Signed electronically

Bernard Peter Agulhas
Chief Executive Officer

General comments

1. The IRBA welcomes the IAASB's holistic revision of ISA 540, through its issue for comment on ED-540, for the following reasons:
 - a. Globally, through the International Forum of Independent Audit Regulators¹ (IFIAR), and in South Africa² inspection findings relating to the audit of accounting estimates remain one of the key inspection findings on the inspection of individual audit engagement files; and
 - b. The increasing complexity of financial reporting standards, for example, the recent issue of International Financial Reporting Standard (IFRS) 9, *Financial Instruments*.
2. There are several matters discussed in the "request for specific comments and responses" and "other matters" sections below that the IRBA would like to bring to the IAASB's attention where ED-540 could be further strengthened. This strengthening is necessary to close the gap between the proposals and need to address shortcomings in audit quality in the audit of accounting estimates. We see this as an important opportunity for the IAASB to be alert to the potential that a suitable ED-540 could have on audit practice. This would be a missed opportunity and would further widen the expectation gap between users and auditors if the IAASB falls short in its efforts to enhance extant ISA 540.
3. We also request that the IAASB be alert to feedback received from the pilot testing of ED-540 and comments received from practitioners about how ED-540 can be practically implemented.

Request for specific comments and responses

Overall questions

Question 1

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

4. In South Africa, a company is required to prepare its financial statements in accordance with International Accounting Standards Board's International Financial Reporting Standards (IFRS) or International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs). Other standards may apply to entities in the public sector, and to entities in specialised industries. Financial reporting frameworks are in a constant state of evolution, and the IAASB's monitoring efforts should keep pace with the developments.
5. The upcoming implementation of IFRS 9, especially the introduction of the expected credit loss model, introduces implementation challenges to preparers, auditors and the users.

¹ [2012 IFIAR Inspection Survey](#), [2013 IFIAR Inspection Survey](#), [2014 IFIAR Inspection Survey](#), [2015 IFIAR Inspection Survey](#) and [2016 IFIAR Inspection Survey](#).

² IRBA [Public Inspections Report 2015](#) and [Public Inspections Report 2016](#).

Although ED-540 is an appropriate response to deal with IFRS 9, without IFRS 9 being effective and without the auditor having had to respond thereto in practice, it is too early to conclude whether further updates to ED-540 may be necessary. Our comment letter addresses a few areas where the audit response should be enhanced, keeping in mind some of the practical challenges with implementation that could arise.

6. Refer also to our comments contained in paragraph 21 below.

Question 2

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

7. ED-540 appropriately reinforces the application of professional scepticism when auditing accounting estimates.
8. The following requirements, in particular, reinforce the application of professional scepticism when auditing accounting estimates:
 - a. Enhanced risk assessment requirements, including the requirements for retrospective review and the determination of whether specialised skills or knowledge is required. (Paragraphs 10-12 of ED-540.)
 - b. More granular objective-based requirements for work-effort. (Paragraphs 17-20 of ED-540.)
 - c. “Stand-back” requirements. (Paragraphs 22-23 of ED-540.)
9. The introduction of requirements generally has an impact on improving the application of professional scepticism. We would therefore not object, in any area of the standard, to further requirements that have the effect of addressing such scepticism.

Focus on risk assessment and responses

Question 3

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

10. As a regulator and standard setter, our experience is always that too little work is done in the area of account estimates, or there is inadequate evidence of the work performed. Any focus on scalability should not have the unintended consequence of auditors doing less work than they should for each account estimate.
11. ED-540 has introduced scalability with respect to auditing accounting estimates by introducing a conditional requirement when the auditor has assessed the inherent risk of material misstatement as low.
12. However, there are a number of observations that the IRBA would like to bring to the IAASB’s attention:
 - a. ED-540 is unclear on how the auditor should respond when inherent risk has been assessed as low but the accounting estimate is considered material. We consider this to be a significant gap, and one that will create implementation challenges if not

addressed in the requirements. There should be no circumstances, where material balances are under audited, and a low risk assessment used to justify that approach.

- b. We understand that paragraph 13 of ED-540 requires the auditor to take into account the extent to which the accounting estimate is subject to, or affected by, one or more of the relevant factors in identifying and assessing the risk of material misstatement. However, it is unclear from ED-540 whether inherent risk cannot be assessed as low when one or more of the relevant factors are present.
 - c. Paragraph 22 of ED-540 requires the auditor, for each accounting estimate for which the auditor's further audit procedures were required to address the matters in paragraphs 17-19, to evaluate certain matters set out therein. Since this requirement only makes reference to the further audit procedures that the auditor performs in paragraphs 17-19, this stand-back requirement is not required to be performed when the auditor has assessed inherent risk as low and performs the procedures set out in paragraph 15(a).
13. ED-540 should be clarified and strengthened regarding the matters set out in paragraph 12 above.

Questions 4(a)

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

14. The enhanced risk identification and assessment process, including the three relevant factors, introduced in paragraphs 10-13 of ED-540 will assist the auditor in identifying and assessing the risk of material misstatement, whether inherent risk is low or not.
15. However, there are several observations that the IRBA would like to bring to the IAASB's attention:
 - a. Please refer to the uncertainty expressed in paragraph 12(b) above that should be addressed.
 - b. Paragraph A9 of ED-540 sets out the purpose for performing risk assessment procedures. As a result, paragraph A9 should be elevated to a requirement and introduced as paragraph 10A. If it is not elevated, it may have the effect of the auditor not considering whether the understanding obtained of the entity and its environment, including its internal controls, is sufficient to identify and assess the risks of material misstatement, including determining whether, in the auditor's judgment, any of those risks are significant risks; and plan the nature, timing and extent of further audit procedures.
 - c. Paragraph A39 of ED-540 provides application material on data, including data that is observed directly and derived data. Although derived data is explained, it would be beneficial to provide examples of derived data.
 - d. Paragraph A49 of ED-540 notes that some accounting estimates may be significantly

affected by, or subject to, complexity, the need for use of judgment by management and estimation uncertainty. It further notes that in such cases it will be more important for the auditor to understand the design and implementation of relevant controls, and also to test their operating effectiveness in addressing the assessed risks of material misstatements. The first part of this statement, as it relates to it being more important to understand the design and implementation of relevant controls, may be misleading because the auditor is always required to understand the design and implementation of relevant controls (ISA 315 (Revised), paragraphs 26(a) and A132) and this paragraph should therefore be amended.

- e. Paragraph A55 of ED-540 deals with understanding an entity's risk assessment process when the entity has such a process in place. Paragraph A55 does not deal with the situation when an entity does not have a formal risk assessment process in place, as anticipated in paragraph 17 of ISA 315 (Revised). Even though ED-540 should be read together with ISA 315 (Revised), ED-540 should also deal with the situation when an entity does not have a formal risk assessment process in place.
- f. Paragraphs A72 and A73 of ED-540 provides examples, respectively, of accounting estimates with low inherent risk and with inherent risk that is not low. These two paragraphs would be better placed as application material to paragraph 15 of ED-540, with paragraph A72 placed above paragraph A96 and paragraph A73 placed above paragraph A97.

Question 4(b)

When inherent risk is not low (see paragraphs 13,15 and 17-20), 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 judgement by management and the potential for management bias, and estimation uncertainty?

- 16. We do support the requirement in ED-540 for the auditor to take into account the extent to which the accounting estimate is subject to, or affected by, one or more of the relevant factors. However, ED-540 only includes objective-based requirements (paragraphs 17-19) to address the three relevant factors (complexity, judgment and estimation uncertainty).
- 17. ED-540 does anticipate that there may be other relevant factors that the auditor may consider in identifying and assessing the risks of material misstatement. This is explained in paragraph A78 of ED-540.
- 18. A more robust explanation about other relevant factors should be included in the requirements of ED-540. This could be achieved by elevating paragraph A78 to a requirement and having it introduced as paragraph 13A.
- 19. In addition, it should be clarified more clearly in paragraph 15 of ED-540 that the auditor's further audit procedures shall also be responsive to those risks of material misstatement over accounting estimates that are subject to, or affected by, any other relevant factors that have been identified.

Question 4(c)

When inherent risk is not low (see paragraphs 13,15 and 17-20), is there sufficient guidance in

relation to the proposed objective-based requirements in paragraphs 17 to 19 of ED-540? If not, what additional guidance should be included?

20. We agree with the introduction of the granular objective-based requirements contained in paragraphs 17-19 of ED-540.
21. The objective-based requirements contained in paragraphs 17-19 of ED-540 provide good guidance to the auditor. However, there are several comments provided to us by a few technical and lead partners of banks from firms on where the guidance contained in paragraphs 17-19 and the related application material could be strengthened. Those comments are as follows:
 - a. Regarding paragraphs 17-19 of ED-540, guidance should be provided on how the auditor should respond when an event that may affect the forward-looking inputs/variables/assumptions and ultimately the impairment provision (e.g. sovereign credit downgrade or severe devaluation in currencies) occurs after the balance sheet date, but before the audit report is signed.
 - b. Paragraph 19(b) of ED-540 requires that only when in the auditor's judgment management has not appropriately understood and addressed the estimation uncertainty shall the auditor, to the extent possible, develop an auditor's point estimate or range. Our view is that the auditor should always be required to develop a point estimate or range when the reasons for the assessment given to the risk of material uncertainty includes estimation uncertainty. Our reason for this is that without the auditor developing a point estimate or range, the auditor may not be able to assess whether management has appropriately understood and addressed the estimation uncertainty.
 - c. Regarding paragraphs 19(b) and 20 of ED-540:
 - i. It is noted that the more obscure the inputs/variables/assumptions are within a model to develop an impairment provision, the more difficult it will be for management and the auditor to develop a close/tight range. This, along with other obscure inputs/variables/assumptions, may adversely affect the extent of estimation uncertainty related to an impairment provision. Therefore, it is necessary that ED-540 provide more guidance on this matter as it will likely be more prevalent in developing economies.
 - ii. The auditor may be required to "stress-test" each input/variable/assumption where the auditor concludes that management's input/variable/assumption does not fall within the auditor's range and determine the effect of that difference on the impairment provisions. The ED-540 should provide more guidance on this matter.
 - iii. It is important for the auditor to test that the inputs/variables/assumptions used when calculating an impairment provision should be the same inputs/variables/assumptions as those used by management when developing budgets and considering pricing. ED-540 should provide more guidance on this matter.

22. Regarding paragraphs 13 and A74, ED-540 should provide more guidance on the extent of further audit procedures and how the auditor should respond when the auditor has identified that an accounting estimate is subject to, or affected by, more than one of the relevant factors.
23. It is necessary for paragraph 17 of ED-540 to be cross-referenced to paragraph 8 of ISA 500³ that deals with audit evidence that has been prepared using the work of a management expert. (Refer to the “editorial comments” section below.)

Significant risks

24. Paragraph 15 of ED-540 concludes with the sentence: “*The auditor’s further audit procedures shall be responsive to the reasons for the assessment given to the risk of material misstatement in accordance with paragraph 13, recognizing that the higher the assessed risk of material misstatement the more persuasive the audit evidence needs to be.*” However, ED-540 does not provide sufficient guidance to auditors on the extent of further audit procedures and how the auditor should respond when the auditor has identified a significant risk. Additional guidance in this regard should be provided.

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?

25. The requirement in paragraph 20 and related application material in ED-540 appropriately establishes how the auditor’s range should be developed. This approach is more effective than the approach contained in extant ISA 540. This is an area where the enhancement proposed would also enhance the application of professional scepticism and we would be reluctant to see the IAASB revert to the approach of 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?

26. The requirement in paragraph 23 and related application material in ED-540 will result in a more consistent determination of the misstatement, including when the auditor uses an auditor’s range to evaluate management’s point estimate.
27. However, with reference to paragraph A144 of ED-540, the variation in the auditor’s range may be significant and multiples of materiality. Therefore, it is necessary for ED-540 to provide more guidance on how the auditor addresses a significant variance that is multiples of materiality. This is particularly relevant in the financial services audit environment.
28. We support the inclusion in paragraph 23 of ED-540 that the auditor shall consider all relevant audit evidence obtained, whether corroborative or contradictory.

³ ISA 500, *Audit Evidence*.

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?

29. The conforming amendments to ISA 260 (Revised)⁴, ISA 500 and ISA 580⁵ are appropriate.

Request for general comments

Question 8

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

Question 8(a)

Translations—Recognising 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.

30. No comment.

Question 8(b)

Effective date—Recognising 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.

31. It is important that the IAASB provides a sufficient period to support the effective implementation of the final ISA 540 (Revised). This is particularly important since one of the focus areas of ED-540 is the enhanced risk assessment and response requirements that will be performed by auditors early on in their client's financial reporting period immediately before the effective date. As such, we agree with the IAASB's proposed effective date for financial reporting periods ending 18 months after the approval of the final ISA 540 (Revised). The IAASB should consider this date, alongside its process to finalise the ED, such that there is no further delay in this necessary standard.

Other matters

Documentation

32. Audit documentation that meets the requirements of ISA 230⁶ and the specific

⁴ ISA 260 (Revised), Communication with Those Charged with Governance.

⁵ ISA 580, Written Representations.

⁶ ISA 230, *Audit Documentation*.

documentation requirements of other relevant ISAs provides:

- a. Evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor; and
 - b. Evidence that the audit was planned and performed in accordance with ISAs and applicable legal and regulatory requirements.⁷
33. Despite the purpose of audit documentation described in paragraph 32 above, the lack of preparation of sufficient audit documentation is a key inspection finding in South Africa⁸.
34. As such, despite the audit documentation requirements set out in ISA 230, ED-540 documentation requirements should be enhanced, as follows:
- a. Paragraph 1 of ED-540 should include ISA 230 as one of the standards ED-540 expands upon. (Refer to the "editorial comments" section below.)
 - b. Paragraph A158 of ED-540 should be elevated and included as a requirement of the standard. In addition, paragraph A158 should be re-constructed as part of the requirements to clearly articulate that the auditor shall document (refer to the "editorial comments" section below):
 - iv. The auditor's judgments about the assessed risk of material misstatement related to accounting estimates, and the auditor's response;
 - v. Procedures performed to address matters in paragraphs 17-21, including the auditor's judgment about management's selection of methods, significant data and significant assumptions;
 - vi. The overall evaluation required by paragraphs 22-23;
 - vii. Communications with those charged with governance and management; and
 - viii. Professional judgments on the basis for the auditor's evaluation of whether accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework.
 - c. More specifically, incorporating or referencing the relevant documentation requirements contained in ISA 315 (Revised)⁹ and ISA 330¹⁰.
35. In addition, the last three sentences of paragraph A10 of ED-540 should be moved to the application material on documentation. (Refer to the "editorial comments" section below.)
36. A few technical and lead partners of banks from firms also commented on documentation where they suggested that more guidance be provided on documentation, especially as it relates to the audit of the expected credit loss model used in developing impairment

⁷ ISA 230, paragraph 2.

⁸ IRBA [Public Inspections Report 2015](#) and [Public Inspections Report 2016](#).

⁹ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment*, paragraph 32.

¹⁰ ISA 330, *The Auditor's Responses to Assessed Risks*, paragraphs 28-30.

provisions.

37. A key consideration of the IAASB in considering this input must be the heavily increased requirements introduced in this standard, and the ability of the audit file to stand up to scrutiny by internal and external inspections. It would be contrary to the objective of the standard, and the goals of the IAASB to enhance quality, if auditors perform the work, but are unable to demonstrate through documented evidence that such work has been performed. A spike in unsatisfactory external inspection findings, beyond the current high level, is unsustainable, and will serve to undermine the public confidence in the audit.

Stand-back requirement, paragraph 22

38. ED-540 recognises in paragraph A78 that there may be other relevant factors that the auditor may consider in identifying and assessing the risks of material misstatement other than the three relevant factors identified in paragraph 13.
39. Paragraph 22 of ED-540 requires the auditor, for each accounting estimate for which the auditor's further audit procedures were required, to address the matters in paragraphs 17-19 to evaluate certain matters set out therein.
40. As such, paragraph 22 of ED-540 appears to only require the auditor to evaluate certain matters in relation to the further audit procedures performed on each accounting estimate that is subject to, or affected by, one or more of the three relevant factors.
41. Paragraph 22 of ED-540 should be enhanced to require the auditor to evaluate certain matters in relation to the further audit procedures performed on each accounting estimate in response to any other relevant factor identified by the auditor.
42. In addition, paragraph 20 forms part of the work-effort that the auditor performs in response to the assessed risk of material misstatement and therefore should be referred to in the first sentence of paragraph 22 along with paragraphs 17-19 that are already referenced. Likewise, paragraph A139 should also make reference to paragraphs 17-20.

Communication with regulators or prudential supervisors

43. We support the inclusion of paragraph A157 in ED-540, which recognises that direct communication with regulators or prudential supervisors may be permitted or required. Communication between auditors and regulators or prudential supervisors, particularly in the banking industry, is especially important and useful.

Editorial comments

44. Editorial changes recommended below are denoted as ~~strike through~~ for words that should be deleted and underlined for words that should be inserted.

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
1	This International Standard on Auditing (ISA) deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements. Specifically, it expands on how <u>ISA 230</u> , ISA 315 (Revised), ISA 330, ISA 500 and other relevant ISAs are to be applied in relation to accounting estimates. It also includes requirements and guidance on misstatements of individual accounting estimates, and indicators of possible management bias.	Since the lack of preparation of sufficient audit documentation is a key inspection finding in South Africa ¹¹ , ISA 230 should be identified as one of the auditing standards that ISA 540 (Revised) expands on. This will assist auditors with keeping the documentation requirements "front-of-mind" when auditing accounting estimates. In addition, please refer to our comments on documentation in paragraph 34(a) above.
4	This ISA focuses the auditor's attention on designing and performing further audit procedures <u>relating to accounting estimates</u> (including, where appropriate, tests of controls) responsive to the reasons for the assessment given to the assessed risks of material misstatement, particularly when those reasons include complexity, judgment or estimation uncertainty. This ISA also recognizes that the factors of complexity, judgment or estimation uncertainty	It is necessary to focus the auditor's attention on accounting estimates.

¹¹ IRBA [Public Inspections Report 2015](#) and [Public Inspections Report 2016](#).

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
	are interrelated and that there are inherent limitations in reducing estimation uncertainty beyond certain limits.	
Footnote 25	ISA 315 (Revised), paragraphs 5–6 and 11– <u>12</u> .	The footnote reference to ISA 315 (Revised) should also include paragraph 12 of ISA 315 (Revised).
17	In complying with paragraph 15(b), when the reasons for the assessment given to the risk of material misstatement include complexity related to management’s use of a complex method (including complex modelling), or when management’s method otherwise involves the use of specialized skills or knowledge ^{FN} , the auditor shall obtain sufficient appropriate audit evidence about the following matters: (Ref: Para A101–A104)	A footnote (FN) reference to ISA 500, paragraph 8, should be made. Please refer to our response to questions 4(c), paragraph 23 above.
21	The auditor shall obtain sufficient appropriate audit evidence about whether the disclosures related to accounting estimates are reasonable in the context of the requirements of the applicable financial reporting framework including: (Ref: Para. <u>A2</u> , A135–A138) Key Concepts (Ref: Para. 6, <u>21</u> , 23)	Paragraph 21 should include a reference to application material paragraph A2 and vice versa.
27	The audit documentation shall include: (a) <u>The auditor’s professional judgments</u> on the basis for the auditor’s evaluation of the reasonableness of the accounting estimates and related disclosures <u>in the context of the applicable financial reporting framework</u> ; and	Please refer to our comments on documentation in paragraphs 32-37 above.

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
27A (Previously paragraph A158)	<p>(b) Indicators of possible management bias, if any, and the auditor’s evaluation thereof in forming the auditor’s opinion on whether the financial statements as a whole are materially misstated. (Ref: Para. A158–A159)</p> <p>Paragraph 8 of ISA 230 requires the auditor to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand, among other things, significant professional judgments. <u>The audit documentation of the auditor’s professional judgment shall include:</u></p> <ul style="list-style-type: none"> (a) <u>The auditor’s judgments about the assessed risk of material misstatement related to accounting estimates, and the auditor’s response;</u> (b) <u>Procedures performed to address matters in paragraphs 17-21, including the auditor’s judgment about management’s selection of methods, significant data and significant assumptions;</u> (c) <u>The overall evaluation required by paragraphs 22-23; and</u> (d) <u>Communications with those charged with governance and management.</u> <p>In the context of auditing accounting estimates, these professional judgments include the basis for the auditor’s evaluation of whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework. The auditor’s judgments are likely to be supported by the documentation of the procedures performed to address the matters in paragraphs 17–21 including the auditor’s judgment about</p>	

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
	<p data-bbox="465 308 1021 336"><u>Considerations Specific to Smaller Entities</u></p> <p data-bbox="465 363 1478 660">ISA 315 (Revised) also notes that the manner in which the auditor's understanding of the entity and its environment are documented is for the auditor to determine using professional judgment. For example, in audits of small entities the documentation may be incorporated in the auditor's documentation of the overall strategy and audit plan. For entities that have simple businesses and processes relevant to financial reporting, the auditor's documentation may be simple in form and relatively brief.</p>	
A24	<p data-bbox="465 695 1478 810">The preparation of the financial statements also requires management to establish financial reporting processes for making accounting estimates, including adequate internal control. Such processes include the following:</p> <ul data-bbox="465 842 1478 1169" style="list-style-type: none"> <li data-bbox="465 842 1478 957">• Selecting appropriate accounting policies and prescribing estimation processes, including appropriate estimation or valuation methods, including and, where applicable, models. <li data-bbox="465 989 1478 1066">• Developing or identifying relevant data and assumptions that are used in making accounting estimates. <li data-bbox="465 1098 1478 1169">• Periodically reviewing the circumstances that give rise to the accounting estimates and re-estimating as necessary. 	<p data-bbox="1498 695 2092 767">This edit is proposed to avoid using the word "including" twice in one bullet.</p>
A29	<p data-bbox="465 1201 808 1230">A model is complex when:</p> <ul data-bbox="465 1262 1478 1350" style="list-style-type: none"> <li data-bbox="465 1262 1478 1307">• The method it applies requires specialized skills or knowledge; <li data-bbox="465 1323 1478 1350">• Relevant and reliable data needed for use in the model is difficult to obtain; 	<p data-bbox="1498 1201 2092 1361">We noted that the word "complexity" is used to define a "model that is complex". One of the three suggested wordings should be used to replace the word</p>

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
	<ul style="list-style-type: none"> • The integrity of the data is difficult to maintain; • It exhibits a significant degree of complexity [complexity <u>real-time processing or flexibility to make use of real-time economic data or data analytics to predict the future</u>] in its design or operation, which may, for example, involve more extensive use of information technology or large volumes of data; or • It uses multiple data sources or assumptions with complex-interrelationships. 	“complexity”.
Footnote 44	ISA 315 (Revised) paragraph A52, A56, A57, A88, A93, A95, A101, A102 and A108 <u>A53, A57-A58, A85-A87, A89, A96, A98, A105-A106 and A112</u>	The footnote references to ISA 315 (Revised) should be updated.
A95	Paragraph A40 <u>A42</u> of ISA 200 states that the ISAs do not ordinarily refer to inherent risk and control risk separately. However, the auditor may make separate or combined assessments of inherent and control risk. Although this ISA neither implies nor requires a separate assessment of inherent and control risk, it highlights the importance of the auditor’s consideration of both inherent and control risk in designing and performing further audit procedures to respond to the assessed risks of material misstatement, including significant risks, at the assertion level in accordance with ISA 330.	The reference to ISA 200 should be updated.
A105 (heading above)	Understanding or Interpreting <u>Significant</u> Data (Ref: Para. 17(c))	It is necessary to insert the word “significant” in the heading.
A107	Audit evidence regarding management’s selection of methods and significant data and significant assumptions may be obtained from inquiries of management regarding management’s continuing processes of strategic	We believe that the last sentence of paragraph A107 should be included as a separate paragraph and be headed “Considerations Specific to Smaller

ED-540 paragraph number	Recommended editorial changes to ED-540	Comment
A107A	<p>analysis and risk management and inspection of relevant documents (such as committee minutes).</p> <p><u>Considerations Specific to Smaller Entities</u></p> <p>Even without formal established processes, such as may be the case in smaller entities, the auditor may be able to evaluate the significant data and <u>significant</u> assumptions through inquiries of, and discussions with, management, along with other audit procedures in order to obtain sufficient appropriate audit evidence.</p>	<p>Entities”. This will provide more prominence to considerations that are specific for smaller entities.</p> <p>In addition, it is necessary to insert the word “significant”.</p>
Appendix 2, paragraph 8	<p>Complexity in making accounting estimates arises when there are multiple valuation attributes and multiple or non-linear relationships between them. Management may require specialized skills or knowledge <u>that</u> may, for example, be needed in relation to:</p>	<p>It is necessary to insert the word “that”.</p>
