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# Exposure Draft, ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement*



1 November 2018

The Technical Director  
IAASB Technical Director

Dear Sir/Madam

**Chartered Accountants Academy(CAA) and Training and Advisory Services (TAS) Submission – Consultation Paper “Professional Skepticism – Meeting Public Expectations.”**

In response to your request for comments for **Exposure Draft, ISA 315 (Revised), Identifying and Assessing the Risks of Material Misstatement**, attached is the comment letter prepared by Chartered Accountants Academy and Training & Advisory Services. The comment letter is a result of deliberations of members of CAA and TAS which comprises chartered accountants who have experience in auditing, IFRS specialists and academics.

We are grateful for the opportunity to provide our comments on this project.

Please do not hesitate to contact us should you wish to discuss any of our comments.

Yours faithfully,

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## Overall questions

1. Has ED-315 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risk of material misstatement. In particular:

**a. Do the proposed changes help with the understandability of the risk identification and assessment process? Are the flowcharts helpful in understanding the flow of the standard (i.e., how the requirements interact and how are they iterative in nature)?**

Yes, the proposed changes set out the risk assessment procedures that form the foundation for an audit of financial statements. The consideration of information technology and data analytics assists in ensuring that the risk assessment process is now robust and up to date with trends emerging in the market currently. The standard contains essential enhancements to the auditor's risk assessment process with the objective of establishing more robust requirements and appropriately detailed guidance to drive auditors to perform consistent and effective identification and assessment of the risks of material misstatement. This enhances the basis upon which auditors design and perform audit procedures that are responsive to the risks of material misstatement, leading to the attainment of sufficient appropriate audit evidence.

The flowcharts are useful in the understanding of the risk identification and assessment process as they clearly elaborate how the steps interact from how risks are identified and the related responses. The risk identification and assessment processes are iterative in nature from the gathering process and analysing of information.

**b. Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6-28?**

The issues of public interest have been addressed more adequately than in the current ISA 315 as the ED-315 is proposing to include in the application material scalability considerations. There has been proposed revisions to enhance the specific considerations relevant to audits of public sector entities and this will go a long way in addressing and protecting public interests. Even auditors of smaller and less complex entities have been considered in scalability.

ED-315 also introduces a new concept of inherent risk factors intended to provide a link to the auditor's consideration of susceptibility of misstatement due to fraud. There is emphasis on professional skepticism throughout the rest of the audit.

**c. Are the new introductory paragraphs helpful?**

Yes, the new introductory paragraphs are helpful as they provide useful guidance on the application material for risk assessment processes. They also help clarify what is inherent risk and control risk and also how the risk assessment process is meant to be iterative and dynamic. This should help with regards to understanding of the standard on the part of the users even before they dig into the deeper more specific concepts.

2. **Are the requirements and application material of ED-315 sufficiently scalable, including the ability to apply ED-315 to audits of entities with a wide range of sizes, complexities and circumstances?**

Yes, the requirements are mainly for larger more complex entities this, in our view, is ideal in that the auditor can then apply judgement to less complex areas and apply the standard accordingly. Further to this, the application guidance which will be for audits of smaller entities which are also less complex, should help the auditor to further scale the standard.

- 3. Do respondents agree with the approach taken to enhancing ED-315 in relation to automated tools and techniques, including data analytics, through use of examples to illustrate how these are used in an audit (see Appendix 1 for references to the relevant paragraphs in ED-315)? Are there other areas within ED-315 where further guidance is needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?**

Yes, we agree with the approach taken to enhancing ED-315 in relation to automated tools and techniques, including data analytics. With new technology that is being developed, for example block chain and robotics, this moves auditing to an advanced level and places a further expectation on the part of the auditor to be able to audit transactions processed through such advanced technology, hence these sections should help address that. The auditors need to keep abreast with new technologies and emphasize on critical thinking so that their relevance is seen by the public at large. It is also important that the examples of automation be added in the standard as they can also help the auditor to understand how to apply the requirements of ISA 315 (Revised). The IAASB does need to ensure that the examples cover a wide array of scenarios in which automated tools are used covering different industries.

No areas that require further guidance in relation to automated tools and techniques were noted.

- 4. Do the proposals sufficiently support the appropriate exercise of professional skepticism throughout the risk identification and risk assessment process? Do you support the proposed change for the auditor to obtain 'sufficient appropriate audit evidence' through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional skepticism?**

Yes, the proposals sufficiently support the appropriate exercise of professional skepticism throughout the risk identification and risk assessment process. In order to deliver due care in an audit, there is need for that critical assessment in gathering audit evidence and a questioning mind. Since audit evidence is gathered and evaluated throughout the audit, professional skepticism should be exercised throughout the audit. With this in mind, ED-315 has proposed for the emphasizing the importance of exercising professional skepticism in the introductory paragraphs.

Yes, we support the proposed changes regarding the use of risk assessment procedures to provide evidence which then serves as the basis for the identification and assessment of risks of material misstatement. The clarification will further increase professional scepticism, this is because risk assessment procedures only give audit evidence and judgement, i.e. professional scepticism, to come up with the sufficient appropriate evidence.

### Specific Questions

- 5. Do the proposals made relating to the auditor's understanding of the entity's system of internal control assist with the understanding the nature and extend of work effort required and the relationship of the work effort to the identification and assessment of the risks of material misstatement? Specifically:**

- a) **Have the requirements related to the auditor's understanding of each component of the entity's system of internal control been appropriately enhanced and clarified? Is it clear**

**why the understanding is obtained and how this informs the risk identification and assessment process.**

The requirements related to the auditor's understanding of each component of the entity's system of internal control have been clarified. Through use of the flow chart, the steps clearly show where exactly the use of IT comes in, in the evaluation and design of controls and implementation. The five components of the system of internal control process have been identified and guidance has been provided in the flow chart.

- b) Have the requirements related to the auditor's identification of controls relevant to the audit been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?**

The process of how the auditor identifies controls relevant to the audit has been clarified. The flow chart clearly gives guidance on what to do the results of the auditor's understanding of the system of internal controls, which includes among others the identification of risks of material misstatements at the financial statements level. For smaller and less complex entities, this clearly articulates how the application of these internal controls will ensure that the proper policies, procedures and all relevant documentation is followed by management and allows for the auditor to easily identify discrepancies and errors.

- c) Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor's understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor's consideration of the effects of the entity's use of IT on the identification and assessment of the risks of material misstatement?**

Yes, the IT -related concepts and definitions are useful in the auditor's understanding of the IT environment. The auditor can sceptically identify risks (what can go wrong) within the internal control environment and perform risk assessment effectively.

- 6. Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:**

- a) Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments?**

The separate assessments of inherent and control risk at assertion level are useful in the risk assessment process and the guidance provided is appropriate. Given that ISA 330 requires the separate assessment of inherent risk and control risk, this responses to ISA 330 and is a step in the right direction.

- b) Do you support the introduction of the concepts and definitions of 'inherent risk factors' to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor's risk assessment process?**

The introduction of the concepts and definitions of inherent risk are helpful and provide necessary guidance, given that the same concepts are to be applied to both private and public sector entities. The factors clearly explain how these risk factors are used in risk assessment, for example, complexity and how it affects an assertion's susceptibility to misstatement, leading to more focused identification.

- c) **In your view, will the introduction of the ‘spectrum of inherent risk’(and related concepts of assessing the likelihood of occurrence, and magnitude of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?**

We believe the introduction of the spectrum of inherent risk will assist in achieve greater consistency in identification and assessment of risks of material misstatement. The new proposal provides guidance on how the degree to which inherent risk varies, creating a framework for auditors to refer to at any point in time.

- d) **Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e. an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion) and how they assist the auditor in identifying where risks of material misstatement exist?**

The guidance on how relevant assertions are identified is appropriate. Although firms have different methods in identification of significant classes of transactions, account balances and disclosures, what matters is that all requirements are complied with and the auditor clearly understands the client’s internal control based on the assessed risks. When such guidance is provided, the expectations from the auditor are clear in the risk assessment process.

- e) **Do you support the revised definition and related material on the determination of ‘significant risks’? What are your views on the matters presented in paragraph 57 of the Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?**

The definition of significant risks currently focuses on auditor response rather than the nature of the risk. The new definition will include additional risks that were once scoped out due to the definition. By inclusion of the term spectrum in the definition, the likelihood of occurrence and magnitude is also considered in coming up with a significant risk.

7. **Do you support the additional guidance in relation to the auditor’s assessment of risks of material misstatement at the financial statement level, including the determination about how and the degree to which, such risks may affect the assessment of risks at assertion level?**

The guidance provided in the application material is appropriate especially given the pervasive nature of risks at financial statements level which have more than one assertion affected.

8. **What are your views about the proposed stand-back requirement in paragraph of ED-315 and the revisions made to paragraph 18 of ISA 330 and its supporting application material? Should either or both requirements be retained? Why or why not?**

We think that both requirements should be retained because they complement each other. Requirements of ED-315 further enhances risk assessment procedures and ISA 330 safeguards against imperfect risk identification.

### **Conforming and Consequential Amendments**

9. **With respect to the proposed conforming and consequential amendments to:**

- a) **ISA 200 and ISA 240, are these appropriate to reflect the corresponding changes made in ISA 315 (revised)?**

Yes, these are appropriate to reflect the changes in ISA 315 (revised). The new sections that are to be added in help to explain the purpose of the auditor’s assessment and

identification of risks of material misstatement. This is appropriate in reflecting the corresponding changes.

- b) ISA 330 are the changes appropriate in light of the enhancements that have been made in ISA 315 (Revised), in particular as a consequence of the introduction of the concept of general IT controls relevant to the audit?**

Yes, the changes are appropriate. Stemming from changes in the risk assessment process, it is vital that the responses also change and allow for professional scepticism.

- c) The other ISAs as presented in Appendix 2, are these appropriate and complete?**

Yes, they are appropriate and complete. The key standards which are affected are mentioned.

- d) ISA 540 (Revised) and related conforming amendments (as presented in the Supplement to this exposure draft) are these appropriate and complete?**

Yes. They highlight important amendments regarding the auditing of estimates including fair value estimates and related disclosures. This is a fairly risky area and as such the amendments are appropriate.

- 10. Do you support the proposed revisions to paragraph 18 of ISA 330 to apply to classes of transactions, account balances or disclosures that are 'quantitatively or qualitatively material' to align with the scope of the proposed stand-back in ED-315?**

Yes, we support the proposed revisions to apply to classes of transactions, account balances or disclosures that are 'quantitatively or qualitatively material' to align with the scope of the proposed stand-back in ED-315. This provides coverage of all the sections to be audited

## **11. General Comments**

**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 – 315**

No comment

**Effective date – Recognizing that ED – 315 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 beginning at least 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.**

Appropriate effective date for financial reporting periods beginning at least 18 months after the approval of a final ISA is sufficient to allow for due process. It should allow auditors to make the necessary system amendments and also train personnel to understand the differences and how the revised ISA will alter the way they do work.