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Professor Arnold Schilder  
Chairman  
International Auditing and Assurance Standards Board  
529 Fifth Avenue  
New York NY 10017  
United States of America

2 November 2018

Dear Professor Schilder,

**Proposed International Standard on Auditing 315 (Revised) - Identifying and Assessing the Risks of Material Misstatement**

RSM International Limited, a worldwide network of independent audit, tax and consulting firms, appreciates the opportunity to comment on the IAASB's Exposure Draft, Proposed International Standard on Auditing 315 (Revised) – Identifying and Assessing the Risks of Material Misstatement ('the ED').

We support the direction of the proposals in the ED because they would require auditors to carry out a more robust risk assessment process which would, in turn, lead to more focussed audit responses. However, we have a number of concerns about some of the definitions in the ED as well as the practical implications for the audits of small or less complex entities.

Responses to the specific questions posed in the Explanatory Memorandum are attached.

We would be pleased to discuss our views further with you. If you have any questions regarding our comments, please contact Steve Whitcher ([steve.whitcher@rsm.global](mailto:steve.whitcher@rsm.global)) or me at ([marion.hannon@rsm.global](mailto:marion.hannon@rsm.global)).

Yours sincerely,

A handwritten signature in blue ink that reads 'Marion Hannon'.

Marion Hannon  
Global Leader, Quality & Risk

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## Comments

### Question 1a:

- We welcome the clarifications in the Exposure Draft, particularly of some of the existing principles which currently cause a certain amount of confusion, although we do believe that some of these concepts could be further refined as set out in our responses below.
- The flowcharts are helpful, however there is a danger that they take a more significant role due to the complexity of the standard as a whole.
- We believe that the overall length and complexity of the proposals should be addressed. There is a risk that the proposals are interpreted inconsistently due to this size and complexity.
- The inherent risk factors could also be simplified and clarified.

### Question 1b

- We appreciate the intention to provide a more robust risk assessment process. However, while there is language within the Application and Introductory paragraphs of the ED that notes the auditor's risk assessment process is iterative and dynamic, we are concerned that this language may be overlooked or overshadowed by the language in the Requirements paragraphs which seems to imply that there is a prescribed order and approach that should be followed. This may, therefore, impact on the robustness of the process which itself depends on auditors re-evaluating their risk assessments in the light of new information that they may gather. We recommend expanding upon the intended flexibility of the process in the Introductory section and re-evaluating the specific language used in the Requirements paragraphs.
- With regards to addressing public interest issues we note that it is specifically mentioned in the Explanatory Memorandum but our view is that the link between ED-315 and addressing public interest issues could be more explicitly referred to in the final ISA itself.

### Question 1c

The new introductory paragraphs are helpful and clearly written. However, due to the complexity of the rest of the proposals, auditors may unduly rely on these introductory paragraphs rather than reading the very lengthy standard and they might therefore take on greater significance than is intended.

### Question 2:

- We appreciate and agree with the various paragraphs (as summarised in Appendix 1 to the Explanatory Memorandum) which set out how the ED can be applied to audits of small or less complex entities. However, in overall terms, it appears that the ED is more applicable to large, complex entities.
- We do consider that more could be done to give guidance on how these provisions could easily be applied to these small or less complex entities. Any additional guidance for audits of small or less complex entities should be contained within the standard. We would not want to see separate guidance or, worse, a separate standard for small or less complex entities.

### Question 3

We welcome the paragraphs and associated guidance in the ED which deal with automated tools and techniques. However, without the accompanying completion of the project on data analytics by the IAASB, it is incomplete.

### Question 4

- Whilst we appreciate the references in paragraphs 26-27 and Appendix 1 to professional scepticism, we are not convinced that professional scepticism will be enhanced by the standard as it is more of a behavioural issue and an attitude of mind.

- The concept of having “sufficient appropriate audit evidence” to support risk assessment is in danger of creating circularity where there is already a need to obtain “sufficient appropriate audit evidence” in response to risk assessment.
- We also see a lack of clarity on what is intended by obtaining “sufficient appropriate audit evidence” during risk assessment procedures. Is it simply reinforcing that all risk-assessments have to be documented and grounded in facts? Is it just a clarification regarding the importance of documentation? Or is it introducing a requirement for unspecified new procedures?
- Specifically, we are concerned that the reference in paragraph 17 to obtaining “sufficient appropriate audit evidence” in relation to the entity’s system of internal control will be confused with the use of the term “sufficient” as used throughout other ISA sections, including ISA 500, which defines sufficiency of audit evidence as “the measure of quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor’s assessment of risks of material misstatement and also by the quality of such audit evidence.” We recommend removing the reference to “sufficient appropriate audit evidence” and state that the auditor should perform the required procedures “as the basis for the identification...”

#### Question 5 (a)

- The flowchart dealing with understanding the entity’s internal control is much clearer than the words within the ED.
- In addition, we welcome the intention of ED to set out a more holistic approach to the assessment of Internal Control and risk assessment. The standard could still make it clearer that understanding internal control is an integral part of understanding the entity and identifying and assessing the risk of material misstatement. Auditors who generally perform substantive audits can sometimes struggle to understand why, when no reliance is placed on controls, the ISAs require them to assess Internal Control. We consider, therefore, that there should be a much stronger link between understanding internal control and the risk of material misstatement.
- We have concerns regarding the level of effort required to understand the entity’s system of internal control and when consideration of the design and implementation of controls is necessary. The requirement in paragraph 36 to “evaluate” the design and implementation of system controls relevant to financial reporting is very broad and should be clarified. The language at the end of paragraph 39 notes that not all controls relevant to financial reporting are relevant to the audit, yet the language in paragraph 36 seems to imply that all controls within this component are required to be evaluated. Also, the term, “information systems controls” is confusing and not consistent with other terms used in the requirements. We recommend that the focus of paragraph 36 should be on identifying controls relevant to the **audit** and evaluating the design and implementation of those controls.

#### Question 5 (b)

- The listing of controls relevant to the audit in the application paragraphs is helpful.
- More guidance could be provided for understanding the distinction between direct and indirect controls within paragraph A166.
- We consider that the application material should address how such controls should be identified and the factors influencing the auditor’s judgement in determining whether it is appropriate to evaluate their design and implementation.
- As a scalability issue, it would help if there were acknowledgement of the fact that in audits of small or less complex entities in which a fully substantive approach is taken, there are likely to be fewer controls on which to rely.

Question 5 (c)

- The new IT related concepts and definitions are welcome.
- The material relating to situations in which the entity uses an off the shelf accounting package with limited or no modifications could be given more prominence by including it in the standard itself rather than in the application material. This will often be the case in small or less complex entities.

Question 6 (a)

Yes, we do support the separate assessments of inherent and control risk at the assertion level. The guidance is also appropriate and useful in helping the auditor to understand these assessments.

Question 6 (b)

- We support the concept of inherent risk factors which will assist the identification and assessment of risk at the assertion level.
- Fraud is an inherent risk factor which needs to be considered, however, we believe that the IAASB should re-consider whether including the susceptibility to fraud as an inherent risk factor is unnecessary duplication with ISA 240.

Question 6 (c)

- The introduction of the concept of the 'spectrum of inherent risk' reflects the existing assessment of inherent risks where auditors often categorise these risks as high, medium or low.
- We question whether it will achieve greater consistency in the identification and assessment of risk, including significant risks, as many firms have a similar existing approach to identifying risks and therefore we doubt that it will really change behaviour.

Question 6 (d)

- We support the concepts of 'significant classes of transactions, account balances and disclosures' and 'relevant assertions', and we believe that they will contribute to a more focused risk assessment at the assertion level. However, the definitions and articulation of these could be amended and simplified as suggested in our bullet points which follow.
- In our view, there is a danger that, by linking the definition of 'significant classes of transactions, account balances and disclosures' to 'relevant assertions', the process becomes somewhat circular. We would prefer to link 'significant classes of transactions, account balances and disclosures' to materiality (ensuring that both qualitative and quantitative aspects were considered). This would then remove the need to clarify ISA 330 paragraph 18 and negate the need for the 'stand back' requirement in ED-315 paragraph 52.
- The terms 'probable', 'possible' and 'remote' are distinct and widely used terms within financial reporting. We do see some potential confusion in this area since "reasonable possibility" can be viewed as somewhat higher than "more than remote". If the terminology is retained then we suggest simplifying the drafting such that "an assertion is relevant.....are such that there is a *more than remote possibility* of occurrence of a misstatement....." The sentence starting "There is such a possibility...." would then no longer be required.
- We suggest that more guidance is provided to assist auditors in determining the level at which significant classes of transactions and account balances are assessed. Is it at the primary statement level, eg Income Statement or Balance Sheet? Or should items in the notes to the financial statements also be assessed? We appreciate that auditor judgment will be key in this assessment but we believe that more guidance is required in this critical area of the risk assessment process otherwise it may appear that the Board is avoiding the issue.

#### Question 6 (e)

- We support the concept that a significant risk is toward the upper end of the spectrum of inherent risk and, in our view, the new proposed definition of 'significant risk' is an improvement on the existing one and may help to reduce inconsistencies in practice.
- However, we are concerned that the requirement to consider risks with a high magnitude or likelihood may result in more significant risks being identified than is currently the case and where little value is added by the additional work required. For example, risks with low likelihood but, were they to occur, high magnitude and vice versa. An extreme example could be a natural disaster which may be unlikely to occur but would be devastating for the entity.
- We note that the proposed definition in paragraph 16(k) is inconsistent with the description provided in paragraph A222, which states, "the higher the combination of likelihood and magnitude, the higher the inherent risk," and, "Significant risks, which are identified in accordance with paragraph 49, are those close to the upper end of the spectrum of inherent risk." We believe these concepts should be aligned.
- The third sentence in paragraph A10 states, "The significance of a risk of material misstatement at the assertion level is considered in the context of the implications of the assessment of its inherent risk for the performance of the audit, including the nature, timing and extent of the auditor's further audit procedures and the persuasiveness of the audit evidence that will be required to reduce audit risk to an acceptable level." This seems to be inconsistent with the definition of significant risk in paragraph 16(k) in that the definition refers to the inherent risk's position on the spectrum of inherent risk, whereas paragraph A10 seems to suggest that the determination is related to the eventual audit procedures to be performed to address the risk. This represents a different concept that should not, in our view, be introduced in an application paragraph. We believe this will create confusion and inconsistency when determining which inherent risks are significant risks.

#### Question 7

We support the additional guidance to paragraph 47. However, we believe that determining financial statement level risk with reference to 'the degree to which' such a risk may affect risk at the assertion level is likely to be subjective and inconsistent. It is not clear, for example, how auditors can assess 'the degree to which' a common financial statement level risk such as going concern affects risks at the assertion level.

#### Question 8

- Consistent with our response to question 6d, we believe that, when an auditor has appropriately applied the risk assessment standards and adequately considered risk considering the inherent risk factors, the stand-back requirement would be redundant, and therefore should not be a requirement within the standard.
- In addition, we do not support the revision to paragraph 18 of ISA 330 since a qualitative risk would be expected to be identified as a risk of material misstatement as, by definition, materiality encompasses both quantitative and qualitative considerations. We therefore consider that there is no need for either paragraph 52 in ISA 315 or paragraph 18 in ISA 330. The latter often results in 'notional' substantive procedures being performed for compliance purposes only. The proposed standard is clear enough without it.

#### Question 9, 10 and 11(a)

We have no comment, other than in respect of paragraph 18 in ISA 330 as mentioned above in our response to questions 6d and 8.

#### Question 11 (b)

The length and complexity of the ED could require significant time and effort for implementation. Audit firms may need to develop effective quality control processes as well as make changes to methodology, which in many cases will require changes to manuals, audit programs, forms,



trainings, and other processes. We encourage the Board to take these matters into consideration when determining an effective date which, in our view, should not be before the date proposed in the Exposure Draft.

