



Exposure Draft Supplement

Proposed Canadian Auditing Standard

Identifying and Assessing the Risks of Material Misstatement – Proposed Conforming Amendments to CAS 540 and CAS 200 (Paragraph A42)

January 2019

COMMENTS TO THE AASB MUST BE RECEIVED BY
May 1, 2019

We value your input and look forward to your feedback on this Exposure Draft Supplement. Respondents are asked to email their comment letters (in a Word file) to: info@aasbcanada.ca.

Please address your comments to:

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This Exposure Draft Supplement reflects proposals made by the International Auditing and Assurance Standards Board that the Auditing and Assurance Standards Board (AASB) intends to include in the final standard, subject to deliberating comments received, as Canadian generally accepted auditing standards.

Individuals and organizations are invited to send written comments on the Exposure Draft Supplement proposals. Comments are requested from those who agree with the Exposure Draft Supplement as well as from those who do not.

Comments are most helpful if they relate to a specific paragraph or group of paragraphs. Any comments that express disagreement with the proposals in the Exposure Draft Supplement should clearly explain the problem and include a suggested alternative, supported by specific reasoning. All comments received by the AASB will be available on the website shortly after the comment deadline, unless confidentiality is requested. The request for confidentiality must be stated explicitly within the response.

Highlights

This supplement to the Auditing and Assurance Standards Board's (AASB) September 2018 [Exposure Draft, "Identifying and Assessing the Risks of Material Misstatement"](#) (ED-CAS 315), explains and illustrates the proposed conforming amendments to revised CAS 540, *Auditing Accounting Estimates and Related Disclosures*, and paragraph A42 of CAS 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Canadian Auditing Standards*, arising from ED-CAS 315 and should be read with ED-CAS 315 and revised CAS 540.

The International Auditing and Assurance Standards Board (IAASB) approved International Standard on Auditing (ISA) 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*, at its June 2018 meeting; the same meeting that it approved its Exposure Draft, "[Proposed ISA 315 \(Revised\), Identifying and Assessing the Risks of Material Misstatement and Proposed Consequential and Conforming Amendments to Other ISAs](#)" (ED-ISA 315). In August 2018, the IAASB issued a supplement to its ED-ISA 315 titled "[ISA 315 \(Revised\), Identifying and Assessing the Risks of Material Misstatement – Proposed Conforming Amendments to ISA 540 \(Revised\) and ISA 200 \(Paragraph A42\)](#)" (IAASB Supplement). In October 2018, the IAASB completed its due process on ISA 540 (Revised).

When the AASB issued ED-CAS 315 in September 2018, the Board had not approved the adoption of ISA 540 (Revised) as CAS 540. Accordingly, the Board was not able to consider the conforming amendments to ISA 540 (Revised) resulting from the IAASB Supplement until the IAASB completed its due process on ISA 540 (Revised) and the AASB finalized CAS 540.

In October 2018, the AASB approved CAS 540 and, in December 2018, the Auditing and Assurance Standards Oversight Council confirmed that the Board followed due process with proper regard for the public interest when approving this CAS. CAS 540 will be issued in the CPA Canada Handbook – Assurance in March 2019.

The AASB is now proposing in this supplement to ED-CAS 315 (Exposure Draft Supplement), subject to comments received following exposure, to adopt conforming amendments to:

- ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*; and
- ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*;

proposed by the IAASB in its IAASB Supplement. The result would be amended respective CAS 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Canadian Auditing Standards*, and CAS 540, *Auditing Accounting Estimates and Related Disclosures*.

This Exposure Draft Supplement consists of:

- proposed changes;
- a description of the AASB's process for adopting ISAs;
- a discussion of proposed significant Canadian amendments; and
- a proposed effective date.

The text of revised ISA 540 is included in this Exposure Draft Supplement for readers to consider.

Please review "**Comments requested**" on page 3 for information on preparing your response to this Exposure Draft Supplement.

Proposed changes

The Exposure Draft Supplement proposes several key changes to revised CAS 540:

- To reflect the new name of ED-CAS 315 and terminology used in ED-CAS 315, including the names of the components of the entity's system of internal control.
- To reflect specific aspects of ED-CAS 315, such as an increased focus on the applicable financial reporting framework and the system of internal control.
- To modernize the presentation of information technology (IT) matters and provide more specificity about matters relating to IT (such as specifying that it is the IT applications and IT environment that are relevant to the auditor when identifying and assessing risks of material misstatement).
- To introduce new concepts such as "significant" classes of transactions, account balances and disclosures, and their "relevant" assertions.
- To recognize the broader inherent risk factors in ED-CAS 315, and to explain that the inherent risk factors in revised CAS 540 are those that are considered in the context of accounting estimates.
- To enhance consistency of terms used:
 - In ED-CAS 315, "control activities" refers to a specific component of the system of internal control. In revised CAS 540, where the term "control activities" has been used in a different context (i.e., to refer to controls and not that specific component), the term has been changed.
 - In revised CAS 540, references to "lower end" of the spectrum of inherent risk have been changed to "close to the lower end" to be consistent with the terminology used in ED-CAS 315.
 - Many of the concepts and matters relating to the auditor's understanding of the entity's system of internal control, and assessment of control risk, are explained in the context of accounting estimates in revised CAS 540. Accordingly, various conforming amendments have been proposed to revised CAS 540 to align the concepts and terminology with ED-CAS 315.

The Exposure Draft Supplement also proposes a key change to CAS 200:

- Revised CAS 540 introduced a new requirement to separately assess inherent risk and control risk, which also resulted in a consequential change to paragraph A42 of CAS 200. ED-CAS 315 also proposes a separate assessment of inherent risk and control risk, and changes have been proposed to revised CAS 540 to indicate that these separate assessments are required by CAS 315. In addition, this has resulted in a further proposed change to paragraph A42 of CAS 200.

IAASB Exposure Draft

The comment period on the IAASB's Exposure Draft closed November 2, 2018. However, the IAASB is deliberating the results of the comments it received on exposure and do not plan to finalize ISA 315 (Revised) until June 2019.

The AASB will consider all responses to this Exposure Draft Supplement and provide feedback to the IAASB as it works to finalize the changes to ISA 315 (Revised) and the related conforming amendments.

Process for adopting ISAs

In adopting the ISAs as CASs, the AASB issues as a Canadian exposure draft, every IAASB exposure draft of a proposed ISA. However, in doing so, the AASB recognizes that it has a vital role to play in monitoring changes made by the IAASB to ensure that standards remain in the Canadian public interest

and that adopting an ISA is not automatic. The AASB follows amendment criteria set out in the [Appendix](#) that allow the AASB to make amendments in specific circumstances.

The AASB normally uses the same effective date for the CASs as the IAASB does for the ISAs. The AASB makes CASs available shortly after they are approved, so Canadian auditors can become familiar with them and prepare to implement them by the effective date.

Proposed significant Canadian amendments

The AASB proposes no Canadian amendments to the proposed conforming amendments to the revised ISAs.

Proposed effective date

The IAASB proposes that the revised ISAs be effective for audits of financial statements for periods beginning on or after December 15, 2020. The revised CASs are expected to have the same effective date as the revised ISAs. Auditors will be permitted to apply these revised CASs before the effective date.

Comments requested

Comments are most helpful if they relate to a specific paragraph or group of paragraphs. Any comments that express disagreement with the proposals in the Exposure Draft Supplement should clearly explain the problem and include a suggested alternative, supported by specific reasoning. When a respondent agrees with proposals in the Exposure Draft Supplement, it will be helpful for the AASB to be made aware of this view.

Providing comments to the AASB

The AASB would appreciate receiving responses to the questions set out below.

1. Are the related conforming amendments as presented in this Exposure Draft Supplement appropriate and complete?
2. Do you believe the AASB should make any Canadian amendments to the proposed conforming amendments to the revised ISAs? If so, please include your reasoning and describe their nature and extent. Any proposed amendments would need to meet the criteria set out in the Appendix.

Responses to these questions should be sent directly to the AASB.

You may email your comments (in a Word file) to: info@aabscanada.ca

The deadline for responding to the AASB on its Exposure Draft Supplement is May 1, 2019.

Appendix

Criteria for amending ISAs when adopting them as CASs

With respect to the adoption of ISAs, the AASB's overriding goal is to adopt ISAs into the CPA Canada Handbook – Assurance without amendment. However, there may be circumstances when amendments are required. The following sets out the limited circumstances when the AASB will make amendments to ISAs:

1. The AASB limits additions to an ISA to those required to comply with Canadian legal and regulatory requirements.¹
2. The AASB limits deletions from, or other amendments to, an ISA to the following:
 - (a) The elimination of options (alternatives) provided for in the ISA.
 - (b) Requirements or guidance, the application of which Canadian law or regulation¹ does not permit, or which require amendments to be consistent with law or regulation.
 - (c) Requirements or guidance, where the ISA recognizes that different practices may apply in different jurisdictions and Canada is such a jurisdiction.
3. The AASB may make amendments to an ISA with respect to requirements or guidance that do not fall within 1 or 2 above when it believes that there are circumstances particular to the Canadian environment where such amendments are required to serve the Canadian public interest and maintain the quality of auditing and reporting in Canada.
4. To the extent possible, amendments that are:
 - (a) additions to an ISA will not be inconsistent with the current requirements or guidance in the ISA; and
 - (b) deletions from, or other amendments to, an ISA will be replaced by an appropriate alternative that achieves the objective of the deleted requirement.

Proposed amendments to an ISA are highlighted in exposure drafts of proposed Canadian standards. The AASB indicates the reasoning for the amendments and respondents are invited to comment on them, including when the amendment will not result in convergence with the ISA in accordance with the IAASB's guide for national standard setters. Amendments to ISAs are separately identified in the final Handbook material.

¹ Canadian incorporating and other governing legislation often require entities to prepare financial statements in accordance with Canadian generally accepted accounting principles (GAAP). Accordingly, if Canadian GAAP necessitates a different audit response in Canada, these differences fall within the definition of a legal or regulatory requirement.

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