

Responses to ED-315¹
Comments on ‘Separate Assessments of Inherent and Control Risk’
NVivo Report 5A
(FOR REFERENCE)

01. Basel

The following improvements are particularly important to us:

- introduction of new concepts such as inherent risk factors and spectrum of inherent risk;
- clarification that the auditor should perform a separate assessment of inherent risk and control risk;
- approach of scalability;
- introduction of a “stand-back test”;
- additional emphasis in the standard and application material that focuses on obtaining a sufficient understanding of information technology (IT); and
- references to the use of automated tools and techniques, including data analytics, to perform risk assessment procedures (application material and flowchart).

05. IAIS

The IAIS is supportive of the IAASB’s initiatives on improving the auditor’s risk assessment procedures. These improvements are particularly important in the following areas:

- Introduction of new concepts of inherent risk factors and spectrum of risks.
- Clarification that the auditor should perform a separate assessment of inherent risk and control risk.
- Additional emphasis in the standard and application guidance focused on obtaining a sufficient understanding of information technology.
- Additional requirement regarding approach to be based on controls when it is not possible to perform only substantive procedure.
- Reference to the use of automated tools and techniques including data analytics to perform risk assessment procedures.

06. IFIAR

As a starting point, we are encouraged by some of the improvements seen in the proposed standard that have the potential to improve the auditor’s risk assessment procedures including:

- Clarification that the auditor should perform a separate assessment of inherent risk and control risk.
- Additional emphasis in the standard and application guidance focused on obtaining a sufficient understanding of information technology.
- ...

¹ Exposure Draft International Standard on Auditing 315, *Identifying and Assessing Risks of Material Misstatement*

08. IRBA

- We support separate assessments of inherent and control risk at the assertion level; and the revised requirements and guidance are appropriate to support the separate assessments. This approach is also aligned to the approach encapsulated in ISA 200.
- We further support paragraph 50(b) of ED-315 which requires an auditor to assess control risk at the maximum where the auditor does not plan to test the operating effectiveness of controls in designing further audit procedures to be performed in response to a risk of material misstatement at the assertion level. This is because control risk can only be reduced by testing the operating effectiveness of the controls.

09. UK Financial Reporting Council

We agree strongly with the introduction of the separate assessments of inherent risk and control risk at the assertion level and believe the revised requirements and guidance are sufficiently comprehensive to support the separate assessments. The separate assessments of inherent and control risk at the assertion level, have the potential to drive significant improvements in the auditor's risk assessment process and subsequent design and performance of further audit procedures through:

- Driving a greater understanding of the interaction of ED-315 with ISA 330 (Revised). In particular, to address the assessed risks identified by the procedures in ISA 315 (Revised), ISA 330 paragraph 7 of requires the auditor to consider the reasons for the assessment given to the risk of material misstatement at the assertion level *separately* for inherent risk and control risk in order to design appropriate audit procedures to be performed to respond to the assessed risks.
- Combined with the introduction of inherent risk factors and the placement of inherent risks on the spectrum of inherent risks, supporting an enhanced understanding of the underlying reasons for the risk assessments which is critical to tailoring further audit procedures so that they are responsive to the risk.
- Addressing the challenge noted in the ISA 315 (Revised) IAASB Project Proposal (project proposal) that auditors find it confusing that whilst ISA 200 paragraph A40 states that the combined assessments of inherent risk and control risk may be performed, inherent risk by definition is assessed, and significant risks identified, before the consideration of any related controls. We understand from the project proposal, that because of this ambiguity some auditors find it challenging in practice to not allow the overall knowledge of internal control to influence the auditor's assessment of inherent risk. The consequence of this may be an assumed operating effectiveness of controls when assessing inherent risk, potentially resulting in a lower than appropriate assessment of the risk of material misstatement and an insufficient audit response.

10. AASB of ICAI

We support separate assessments of inherent and control risk at the assertion level. However, we are not in agreement with the requirement of adjusting risk of material misstatement based on the auditor's expectation of operating effectiveness of controls. The Standard presumes that the auditor would be able

to develop a valid expectation about operating effectiveness of controls just by testing the design and implementation of controls.

Australian A&A Standards Board

The AUASB supports the separate assessments of inherent and control risk at the assertion level. We are also supportive of the explicit requirement to assess control risk at maximum if the operating effectiveness of controls is not being tested. However we recommend that the IAASB provide clarity on how this separate assessment is to be performed as follows:

- The inconsistent use of the term “risk of material misstatement” in paragraphs 45 - 47 of ED 315 prior to and after the requirement to identify and assess inherent and control risk separately was raised as being potentially confusing for practitioners. As the concepts relating to the identification and assessment of risk are initially based on inherent risk alone we recommend that the terminology associated with the identification of risks in this paragraph 45 be amended so it relates solely to the identification of inherent risks, and the use of the term “risk of material misstatement” is applied solely in relation to the combined assessment of inherent and control risk.
- Providing additional detail on how to assess control risk at various levels of the spectrum of risk. ED 315 currently only refers to the concepts of maximum, or less than maximum. Whilst we understand the IAASB’s reticence to define the methodology under which an auditor may assess the level of risk (as described in paragraph A225), more guidance on how a practitioner may define the assessment of different levels of control risk would be helpful.
- Describing in greater granularity in ED 315 the process the auditor undertakes to combine their separate inherent and control risk assessments for each classes of transactions, account balances, and disclosures to determine the risk of material misstatement. Currently paragraphs 48 – 50 of the ED describe the requirements to identify and assess inherent and control risk separately, but there is no explicit requirement in ED 315 to consider these together, as currently required by ISA 200.

12. Canadian AASB

- Yes, we support the requirements to separately assess inherent and control risk. Some practitioners were already separately assessing inherent and control risk under extant 315.
- Specifically relating to control risk, we support the language used in ED-315 of “control risk less than maximum” as we interpret this as allowing practitioners flexibility in their respective methodologies to either rely on controls or use more than one category of control risk that is less than maximum.

13. CNCC-CSOEC

We support separate assessment of inherent and control risk at the assertion level and the revised requirements and guidance thereon. This is in line with the approach retained in revised ISA 540.

14. Hong Kong Institute of CPAs

- Risk of material misstatement is a function of inherent risk and control risk. Assessing separately the inherent and control risks would require auditor's in-depth understanding of the entity and relevant internal controls.

- As part of the scalability application, paragraph A90 highlights that the nature, timing and extent of procedures to understand the entity's system of internal control will vary from entity to entity and may depend on factors such as size and complexity of the entity. Consequently, the separate assessments may result in substantial increase in work and documentation in case of a small and less complex entity.
- Our SMPs stakeholders have commented that as the assessed risks of material misstatements at assertion level are determined by considering both the inherent risk and control risk, they should be considered collectively rather than separately. Such collective consideration allows for inherent risks to be reduced or mitigated by reduced or low control risks. If such mitigation or reduction of risks is allowed, separate assessments are not necessary.

15. IDW

Reference 1:

- Since our greatest concerns with the draft relate to some fundamental issues addressed in this question, we will address the main fundamental issue first before addressing the impact on each of the sub-questions in (a) to (e).
- We would like to point out that the current ISAs contain a number of definitions related to “misstatement” and “risks of misstatement” that are not being changed by the draft. This means that these existing definitions continue to apply. In particular, we note the following:
 - Both ISA 200.13 (i) and ISA 450.4 (a) essentially define a misstatement as the difference between what the financial statements actually depict and what they ought to depict. This means that, unless there is a visible impact on what is depicted in the financial statements, there is no misstatement. It follows that a material misstatement only exists when the difference between what is actually depicted in the financial statements and what ought to be depicted is material.
 - ISA 200.13 (n) defines the risk of a material misstatement as the risk that the financial statements are materially misstated prior to audit. This means that the term “risk of a material misstatement” relates to the risk that the difference between what is actually depicted in the financial statements and what ought to be depicted is material. Hence, if for the sake of argument, one disregards the following definitions of inherent and control risk in ISA 200.3 (n) and the description of “risks of material misstatement at the financial statement level” in ISA 315.A122, under the current ISAs there is no such thing as a risk of material misstatement for something other than what is depicted in the financial statements.
 - The word “risk” is not defined in the current ISAs, but ISA 315.26 (d) clarifies that it involves the “likelihood” of misstatement – i.e., its probability. By definition, the likelihood or “risk” of misstatement therefore ranges from 0% to 100%. This also implies that there is “no risk” of misstatement only when such risk is 0 %. Due to the pervasiveness of the completeness issue, it is difficult to envisage circumstances in which it is absolutely certain that risks of misstatement, and hence risks of material misstatement, are zero.
 - ISA 200.13 (n) does define inherent and control risks, but in doing so addresses the sources of risks of material misstatement (i.e., the two factors – inherence and the effect of controls – that affect the probability of misstatement). In addition, inherent and control risk are defined at

assertion level, and thereby the definition moves beyond what is depicted in the financial statements to what management implicitly or explicitly asserts when depicting matters in the financial statements (see ISA 315.A127) in terms of recognition, measurement and presentation of classes of transactions and events, account balances and disclosures. ISA 315.A128-.A130 explain how assertions are used as a tool by auditors to consider potential misstatements and provides some useful categories of assertions that need to be covered but that can be expressed differently by auditors.

- ISA 315.A122 describes the “risk of material misstatement at the financial statement level” as those risks that relate pervasively to the financial statements as a whole and potentially affect many assertions – that is, circumstances that may increase the risks of material misstatement at assertion level. In this case, the ISAs are also dealing with causes of risks of misstatement at the assertion level, but in particular those that affect multiple assertions.
- In conclusion the ISAs currently only require consideration of risks of material misstatement in terms of the impact on what is depicted in the financial statements, and at assertion level. ***There is no requirement for a “drill-down” below assertion level (that is, the determination of risks of material misstatement or inherent or control risks such that there is more than one such risk for each assertion).*** Consequently, although of course the ISAs do not forbid such a drill-down, and some firm methodologies and other guidance do use or address a drill-down to assist auditors, the fact that such a drill-down is not a requirement means that when the term “risks of material misstatement” is used in the current ISAs, it refers to inherent and control risks (which are at assertion level), and in some cases the risks of material misstatement at financial statement level, *collectively* – not to one or more risks within an assertion. The use of the term “identify and assess risks of material misstatement” to refer to these risks collectively in many of the requirements in extant ISA 315 works well because the current ISAs accept a combined identification and assessment of the inherent and control risks.
- The draft of ISA 315 proposes that inherent risks and control risks each be assessed separately, with which we agree for the reasons noted in our response to (a) below. However, the current draft continues to use the term “risks of material misstatement” and “susceptibility to misstatement” (which means the same thing) in relation to identification and assessment of risks throughout the requirements and guidance, even though a separate assessment of inherent and control risk is required. It begs the question as to why the term “inherent risk” is not used when seeking to address the susceptibility of an assertion to misstatement without consideration of control or when addressing the risks of material misstatement that controls address. Furthermore, we note that paragraph A9 in the application material to the definition of “relevant assertion” states

“There will be one or more risks of material misstatement that relate to a relevant assertion”
 [underlining added]
- The second bullet of paragraph 48 in the explanatory memorandum explains the same point. ***On the basis of this analysis, we can only come to the conclusion that the draft intends to require a drill-down below assertion level and that the term “risk of material misstatement” is being used to describe the possibility of multiple risks of material misstatement for each relevant assertion.*** The use of terminology in this way is also confusing to practitioners because it is unclear when in fact the term is used to describe inherent and control risks (and the risks of material misstatement at financial statement level) collectively, rather than for the drill down as described in

paragraph A9. Furthermore, the use of “risk of material misstatement” to refer to the drilled-down risks violates the definitions in the ISAs that continue to be applicable to the draft.

- We recognize that no separate “identification” of control risks can take place, because once an inherent risk has been identified, a concomitant control risk automatically exists (albeit without any consideration of whether it is below maximum or not). However, we believe that rather than using “risk of material misstatement” with the thought of covering this fact throughout the standard, it would be much clearer to speak of inherent risks and that application material to paragraph 50 explains that the control risks need not be separately identified for the reasons noted.
- We do not believe that the impact of the change to effectively requiring such a drill-down has been appropriately exposed because we have become aware that most readers of the draft around the world did not recognize the impact of paragraph A9 or why “risks of material misstatement” was used when “inherent risk” would have otherwise sufficed. In addition, we do not believe that the benefits of such a drill-down are worth the benefits in all cases – particularly for audits of financial statements of smaller and less complex entities – and would undermine the scalability of audits in that sector. For these reasons, we believe that paragraph A9 needs to be deleted, or at least changed so that it clarifies that firm methodologies and other guidance may address risks of material misstatement at below assertion level, but that this is not required. Furthermore, the use of terminology needs to be simplified throughout the draft so that when addressing any risks of material misstatement at assertion level before consideration of controls, the term “inherent risk” (which is defined at assertion level) is used. Such simplification would go a long way to improving the understandability of the draft.

Reference 2:

- We note that extant ISA 315.2 requires auditors to identify significant risks by excluding the effects of controls related to that risk. Given our response to the main question 6 above that extant ISA 315 only requires the identification and assessment of inherent and control risks, both of which are at assertion level, and not any drill-down below assertion level, extant ISA 315.27 has therefore always required a separate assessment of inherent risk for the purposes of identifying significant risks. For these reasons, we do not believe that the introduction of separate assessments of inherent and control risk would involve a significantly greater burden, if at all. Furthermore, we believe that separate consideration of inherent risk helps auditors consider the impact of controls in a systematic manner. For these reasons, we support the separate assessment of inherent and control risks.
- However, as noted in our response to the main question 6 above, we believe that the terminology used needs to be clear by referring to the identification, and assessment, of inherent risk, and the assessment of control risk separately, rather than referring to the “identification” or “assessment” of the “risks of material misstatement”. This would also result in a rationalization and simplification of the requirements in paragraphs 45 to 50 of the draft.

16. Japanese Institute of Certified Public Accountants

We support requiring separate assessments of inherent and control risk at the assertion level. However, we have the following comments.

Identification of the risks of material misstatement (paragraphs 45 and 46)

- In accordance with paragraph 45 of ED-315, the auditor is required to identify the risks of material misstatement at the assertion level before consideration of any controls, which are inherent risks.

However, paragraph 13(n) of ISA 200 defines that a risk of material misstatement at the assertion level consists of inherent risk and control risk and indicates that it is a concept after consideration of any controls. Therefore, it is difficult to understand how the definitions and concepts in ISA 200 flow to those in ED-315. In order to maintain a consistency with ISA 200 definitions, we believe that at least the following clarification is necessary. Alternatively, as stated in our comments to Question 5), we believe the order of the requirements should be changed to require the auditor to identify and assess inherent risks first and then controls relating to the assessed inherent risk.

45. The auditor shall identify the risks of material misstatement and determine whether they exist at: (Ref: Para. A201-A210)
- a) The financial statement level, by evaluating whether the identified risks relate more pervasively to the financial statements as a whole, including potentially affecting many assertions; or
 - b) The assertion level for classes of transactions, account balances, and disclosures, taking in account the inherent risk factors (i.e., identification of inherent risks).
46. The auditor shall determine significant classes of transactions, account balances and disclosures and their relevant assertions, based on the identified inherent risks ~~risks of material misstatement~~.”

Assessment of control risk (paragraphs 50 and A233)

- We believe that it is necessary to clarify the meanings of “assess control risk at less than maximum” and “assess control risk at the maximum” (paragraph 50). We propose to add guidance in paragraph A233 explaining the impact on the assessment of risks of material misstatement. For example, guidance could clarify that the risk of material misstatement will be assessed as less than the assessed inherent risk if the auditor intends to rely on the operating effectiveness of controls, and the risk of material misstatement will remain as the assessed inherent risk if the auditor does not intend to rely on controls.

17. Malaysian Institute of Accountants

We support the separate assessments and consider the revised requirements and guidance to be appropriate.

18. Nederlandse Beroepsorganisatie van Accountants

We support separate assessments.

19. National Board of Accountants (Tanzania)

We support separate assessments of inherent and control risk.

20. NZ Auditing and Assurance Standards Board

- The NZAuASB supports the separate assessment and considers the proposed requirements and application material to be appropriate. To further clarify the separation between inherent and control risk assessment, the NZAuASB suggests the following changes to paragraph 4 of ED-315.

“The required understanding of the entity and the environment, the applicable financial reporting framework, and the system of internal controls form the basis for the auditor's identification of risks of material misstatement. The identification of the inherent risk component of risks of material misstatement at the assertion level is performed before consideration of any controls. The auditor does so based on a preliminary assessment of inherent risk that involve by identifying those risks for which a preliminary inherent risk assessment indicates there is a reasonable possibility of misstatement.”

21. Altaf Noor Ali Chartered Accountants

- Yes. We support separate assessment of inherent and control risk at the assertion level.
- Yes, revised requirements to carry out separate assessments of inherent and control risk are appropriate.

22. BDO International

We support the separate assessments of inherent and control risk at the assertion level. We believe, subject to our responses to other questions in this comment letter, that the guidance on separate assessments of inherent risk and control risk is appropriate.

24. Crowe International

We support separate assessments of inherent risk and control risk at the assertion level. The revised requirements and guidance are appropriate.

25. Deloitte

- As noted in the cover letter and as previously addressed by the Board in ISA 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures* (ISA 540), DTTL believes that the separate assessment of inherent risk and control risk in relation to all risks of material misstatement at the assertion level provides for a more robust risk assessment that will positively impact audit quality. DTTL believes that the “ISA 315 (Revised) Identifying and Assessing Risks of Material Misstatement” flowchart supports the understanding of the separate assessment of inherent risk and control risk. DTTL believes that it is imperative that auditors understand this fundamental change in the risk assessment process. To support this understanding, additional non-authoritative guidance, in addition to the flowcharts, should be provided to assist auditors that are implementing the concept for the first time.
- While DTTL supports the separate assessment of inherent risk, DTTL believes that paragraph 48 of the proposed standard needs to be re-evaluated. The paragraph states that for identified risks of material misstatement at the assertion level the auditor should assess inherent risk; however, paragraph 14 of ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, states that risk of material misstatement is based on inherent and control risk. As such, the proposed standard appears to indicate that inherent risk is required to be evaluated twice. DTTL notes that the same issue is present in the “ISA 315 (Revised) Identifying and Assessing Risks of Material Misstatement” flowchart as it indicates that risks of material misstatement are identified first and then separately inherent risk is assessed for risks of material misstatement at the assertion level. DTTL believes that inherent risk is assessed

when determining if a risk of material misstatement exists at the financial statement level and the assertion level. However, DTTL acknowledges that risk assessment is an iterative process, and that often (e.g., in a recurring audit) the auditor may already have an idea or preliminary conclusion as to whether risks of material misstatement exist. The iterative nature of risk assessment is not sufficiently addressed and may lead to viewing risk assessment as a linear process (e.g., the flowcharts imply that risk assessment is linear and that there is a strict order in which risk assessment always occurs).

26. EY Global Limited

Yes.

27. Grant Thornton International

We are supportive of the requirement to perform separate assessments of inherent and control risk at the assertion level. However, as stated above, we have concerns about when control risk has to be assessed at maximum. Inherent risk and control risk are the entity's risks. As auditors, we may place reliance on the entity's controls to address risks of material misstatement. The requirements in the standard, as drafted, are not allowing for situations where the entity does have controls that are designed and implemented (i.e., reliance on design). Control risk is an entity risk that exists independent of the audit. From a methodology perspective, control risk can be assessed by determining control reliance. Audit procedures to evaluate design, determine implementation, and determine operating effectiveness support the control risk (or control reliance) assessment. Audit sampling theory, including the audit risk model, also supports this approach.

28. KPMG IFRG Limited

- We support this change and we consider that the related requirements and guidance are generally clear. We believe this amendment results in better alignment to ISA 330.7, which requires the auditor to consider inherent risk and control risk separately in order to respond, and it also aligns to the amendments already made to ISA 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures* in this regard. We agree with the statement in the EM that the separation of these assessments helps to avoid auditors subconsciously "taking credit" for testing effectiveness of controls when they have not or do not plan to perform such procedures.
- We note that there is a lack of clarity at paragraphs 3 and 48, when describing, under risks of material misstatement at the assertion level, that inherent risk is the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls, regarding whether such aggregation of misstatements is intended to mean misstatements resulting from the same underlying risk, or from multiple risks. Clarification of this is important for auditors as it affects whether auditors need to consider risks of misstatement individually for each assertion, with aggregation referring only to misstatements related to that particular risk, or whether auditors consider risks of misstatement that in the aggregate may cause a material misstatement in an assertion, which may involve multiple risks of misstatement that individually may not represent a risk of material misstatement but in combination with others may give rise to a material misstatement. We believe the latter interpretation, i.e. that the aggregation of misstatements is intended to mean misstatements resulting from multiple risks, is appropriate, and accordingly, we suggest that the IAASB state this.

- In addition, we note that, in separating the inherent risk and control risk assessments, the standard does not explicitly require the auditor to consider the combination of inherent risk and control risk in order to assess the risk of material misstatement at the assertion level. Paragraph 7, in the introduction, refers to this, however, given the flow of requirements at paragraphs 45-50, this appears to be an omission, and we recommend including this specific requirement immediately after paragraph 49, as well as including guidance in the application material as to how to make a combined assessment.

29. MNP LLP

Yes. We support separate assessments of inherent and control risk at the assertion level and believe the revised requirements and guidance will assist the auditor to perform those separate assessments.

30. PwC International

- We support the explicit introduction of requiring a separate assessment of inherent risk. However, while we support the concept we believe the manner in which the requirements have been drafted can be clarified. We comment in our overarching points above on the circularity and confusion created by the separation of the identification and assessment requirements, the “educated guess” and the use of the term risk of material misstatement. As described in our cover letter we also believe there is an opportunity to reframe the control risk element of the audit risk equation to focus more explicitly on the fact that this can be accomplished through the auditor’s assessment of the extent to which the auditor plans to obtain evidence from testing the operating effectiveness of controls to reduce audit risk to an acceptably low level.

Control risk

- Audit risk is a well understood concept, being the product of both inherent and control risk. However, we believe that control risk is often misunderstood as a concept. In discussions, we often hear that some confuse the concept of “control risk” as implying a possible increase in inherent risk.
- We agree with the introductory and application material that explains that this concept is more commonly thought of today, in the context of planning an audit, in terms of the auditor’s “planned controls reliance” i.e., where the auditor expects to be able to obtain evidence to reduce the overall risk of material misstatement by testing the operating effectiveness of controls. We believe more can be done within the requirements themselves to make this linkage clearer.
- In a financial statement audit, once inherent risk has been assessed, the auditor’s concern is obtaining audit evidence to reduce that risk to an appropriately low level. It is not necessary for the auditor to make a discrete identification and assessment of control “risk” similar to what is needed when the auditor plans an audit designed to give an opinion on internal control. Instead, the auditor’s focus is whether to obtain evidence in response to an identified inherent risk from evaluating the design, and testing operating effectiveness, of controls, or from performing substantive procedures, or from a combination thereof. While the risk of material misstatement comprises both inherent risk and control risk, the latter concept is more readily understandable, and better supports scalability in the risk assessment and planning stage of the audit, by focusing on assessing the “planned control reliance”.
- Reframing the control risk part of the traditional audit risk equation to focus on planned controls reliance was not possible in the extant ISA because a combined risk assessment was allowed (i.e.,

the auditor's risk assessment could be a combined assessment of inherent risk taking into account the expected effectiveness of related controls). Because inherent risk is now proposed to be a separate assessment, there is now an opportunity to simplify and bring clarity to the area of the extant ISA that has caused the most confusion.

- In our view, reframing the proposed separate assessment of control risk to more explicitly focus on the fact that this can be accomplished through the auditor's assessment of the extent to which the auditor plans to obtain evidence from testing the operating effectiveness of controls would also bring clarity within the standard to how much understanding of direct controls is needed – see our response to question 5 for further detail. This is an area that requires clarification, particularly for those circumstances when the audit approach is expected to be based primarily on substantive procedures.
- We acknowledge that the application material that discusses control risk is an attempt to reconcile control risk and planned controls reliance (e.g., if the auditor is not intending to test the operating effectiveness of controls, control risk is assessed at maximum), but application material is not the solution to fixing a broader problem of misunderstanding. We believe the requirements could better support this concept.
- In addition, we believe reframing control risk in this way would help more clearly illustrate that firms may think about this assessment within their methodologies in a variety of ways, including by considering how planned controls reliance can appropriately reduce the overall risk of material misstatement.
- We believe that the required separate identification and assessment of control risk may exacerbate the confusion about the objective of a financial statement audit if the necessary clarity described above is not provided. Without this clarification, referring more explicitly to control risk identification and assessment, together with the new requirements on control deficiencies, promotes expectations that auditors are forming a view on the overall effectiveness of an entity's controls. That is not part of an ISA audit.
- See also our comments in response to questions 2 and 5 on the nature and extent of understanding of controls to support the decision around planned reliance.

31. RSM International

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.

32. Office of the Auditor-General of Alberta

- Yes. However, we note guidance on how to combine inherent and control risk assessments would be useful. Can control risk only “reduce” inherent risk? If inherent risk is low, and control risk is high, is the resulting combined risk low or medium? Or can management systems sometimes also be a source of risk, such as implementation of complex software in which the controls are not adequately designed or operating effectively?
- We note the Board may be concerned with overstepping from a standard into methodology. However, this may be unavoidable if it desires consistency.

33. Office of the Auditor-General of Canada

Yes, we support the separation of the assessments of inherent and control risk at the assertion level and believe this will improve the quality of risk assessments and planned audit approaches. We found the revised requirements and guidance appropriately supportive of this change.

35. US Government Accountability Office

We support separate assessments of inherent and control risk at the assertion level. As noted in our response to question 1(a), we suggest that the IAASB consider clarifying that auditors should start their assessment of risk of material misstatement by identifying and assessing inherent risk and control risk at the assertion level.

36. Swedish National Audit Office

Yes, we support the **separate assessment of inherent vs. control risk** and we find the guidance in the application material to be robust enough.

38. ACCA-CAANZ

We support separate assessments of inherent and control risk at the assertion level.

39. Accountancy Europe

The separate assessments of inherent and control risk at the assertion level are inevitable and the revised requirements and guidance thereon are appropriate to support the separate assessments. This is also a logical consequence of the approach taken in revised ISA 540, as recently approved. We would also like to point out that logically it will also be necessary to identify inherent risk separately from control risk in order to perform such assessment.

40. AICPA

- We are generally supportive of the proposed changes, although we note that they are broad in nature and, if adopted, will likely impact the methodologies of many firms fairly significantly. Such changes often result in an iterative adoption process as the auditors become more familiar with the concepts over time. As such, we recommend that the IAASB consider some targeted outreach on certain of the changes (once ultimately adopted), such as those highlighted above. Notwithstanding our support for the changes, we have comments as follows:
- Paragraph 16(f) — Susceptibility to fraud is included as an inherent factor. We do not believe that susceptibility to fraud, intrinsically, is **inherent** in a characteristic of events or conditions. ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, defines fraud, as follows:
 - An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception that results in a misstatement in financial statements that are the subject of an audit.
- Fraud is characterized by the following factors defined in ISA 240:
 - Events or conditions that indicate an incentive or pressure to perpetrate fraud, provide an opportunity to commit fraud, or indicate attitudes or rationalizations to justify a fraudulent action.

- Given the definition of fraud and the related risk factors, we do not believe that susceptibility to fraud should be characterized as an inherent risk factor. If the IAASB determines it is important to specifically cite inherent risk factors related to fraud, we recommend the standard focus on incentives or pressures to commit fraud, accompanied by the inclusion of references to ISA 240 as appropriate.
- Paragraph 16(k) — We continue to believe that “significant risk” should be the product of the likelihood **and** magnitude of a potential misstatement. For example, we do not believe that a risk of material misstatement with a high likelihood of occurrence, but which has a remote likelihood of being material (both quantitatively and qualitatively) would ordinarily be assessed as a significant risk. Conversely, a potentially material misstatement with a remote likelihood of occurrence would not ordinarily not be assessed as a significant risk. We believe concluding either of these situations may result in a significant risk is inconsistent with the “reasonable possibility” concept which is core to ED 315’s definition of relevant assertions. Also, we recommend that the application material emphasize that the assessment of likelihood is done without consideration of controls, for purposes of this identification.
- Paragraphs 48 and 50 — To further highlight the importance of the focus on, and definition of, relevant assertions, we recommend the standard emphasize that the assessments called for by these paragraphs (and the corresponding response in ISA 330, *The Auditor’s Responses to Assessed*) are to be performed for each relevant assertion. We understand that the IAASB’s intent is for the auditor to design the work effort to the level at which assertions are relevant, and we believe emphasis of that point in these paragraphs will enhance the auditor’s focus on those assertions.

41. Center for Audit Quality

We are concerned that the potential implications of a separate “assessment” of control risk have not been appropriately considered, nor is the Exposure Draft sufficiently clear about the nature of what is expected. While auditors do consider control risk in identifying and assessing risks of material misstatement, it is in the context of whether to obtain evidence from evaluating the design, implementation and operating effectiveness of controls. Auditors also consider control risk when performing substantive procedures, either alone or in combination with control procedures in the risk assessment and planning stage, to help determine the planned control reliance. Therefore, we believe it is necessary for the final standard to clearly illustrate that auditors may think about this assessment within their methodologies in a variety of ways, including by considering how planned controls reliance can appropriately reduce the overall risk of material misstatement.

42. Chartered Institute of Public Finance & Accountancy

CIPFA supports the separate assessment of inherent and control risk.

43. CPA Australia

We support the separation of the risk assessment for inherent and control risks, as controls should be designed to mitigate inherent risks and the procedures to assess control risk are quite different to inherent risk. However, clarity regarding whether ROMM is based on inherent and control risk would be helpful, as the controls are designed to address the ROMM.

44. EFAA

We have no comments.

45. Finnish Association of Authorised Public Accountants

Yes, a separate assessment is useful. More guidance is needed e.g. about what is the joint effect of these two on the audit procedures.

46. Fed of Prof Council of Economic Sciences (Argentina)

In current practice, this separation had already been taking place, so we support that the inherent risk assessment should be done separately from the control risk ones. The requirements and guidance are appropriate to support such evaluations.

47. FSR Danske Revisorer (Denmark)

- In our opinion, the risk assessment would be more scalable if it was less process driven and more focused on the inputs that are needed to achieve the intended outcome. It is, therefore, unclear how the separate assessment of control risk and inherent risk at the assertion level improves the robustness and consistency of the risk assessment, and how it interacts with a fully substantive audit approach that will often be used on small and less complex entities.
- We also believe that the definition and guidance for control risk needs to be revisited to fully address how this concept is applied in practice or be removed from the standard and instead be included in ISA 330.

48. Interamerican accounting association (South America)

Yes, we partially support. We believe that it is irrelevant to evaluate separately or concomitantly. However, if the separate form is approved, we believe that the proposed requirements and guidance will support the evaluations thus made.

49. Instituto dos Auditores Independentes do Brazil

Yes. The flowcharts are needed to facilitate the understanding of the separate assessments.

51. Institute of Chartered Accountants in England and Wales

We support the separate assessments of inherent and control risk at the assertion level, as this reflects common practice. It also represents what providers of audit software and methodologies to smaller firms seek to encourage users to do.

52. Institute of Chartered Accountants (Ghana)

Yes, we support separate assessments of inherent and control risk at the assertion level. We believe that in order to be able to identify the risk of material misstatement, we believe a separate assessment of the inherent and control risk should be done. In order to plan our approach we need to understand the inherent risks that exist at the assertion level in order for us to assess whether the existing controls can sufficiently detect/prevent significant misstatements. The requirements/guidance including inherent risk factors, spectrum of inherent risk, likelihood vs magnitude all provide sufficient guidance in assessing inherent risk separately.

53. Institute of Chartered Accountants of Pakistan

We support separate assessments of inherent and control risk at the assertion level and revised requirements and guidance are appropriate to support the separate assessments. This concept has already been approved in ISA 540 (revised) and ED 315 extends the requirement in relation to risks of all material misstatement.

54. Institute of Chartered Accountants of Scotland

The separate assessments of inherent and control risk at the assertion level are inevitable and the revised requirements and guidance thereon is appropriate to support the separate assessments. This is also a logical consequence of the approach taken in revised ISA 540, as recently approved. We would also like to point out that logically it will also be necessary to identify inherent risk separately from control risk in order to perform such an assessment.

55. Institute of Chartered Accountants (Zimbabwe)

Yes. The separate assessments of inherent and control risk at assertion level are useful in the risk assessment process and the guidance provided is appropriate as ISA 330 requires the separate assessment of inherent risk and control risk.

57. Institute of Public Accountants

While the IPA supports the separation of the assessment of inherent and control risk, we believe further guidance is required, including guidance on the interrelationship between inherent and control risk and inherent risk factors. The IPA is also of the view that when considering inherent risk, the recognition of factors contributing to a "motive to misstate" should be given greater prominence.

59. Malaysian Institute of CPAs

Yes, MICPA supports separate assessments of inherent and control risk at the assertion level based on the rationale spelt out in the Explanatory Memorandum and agrees that the revised requirements and guidance are appropriate to support the separate assessments.

60. New York state society of CPAs

We support the separate assessments of inherent and control risk at the assertion level other than in financial statement areas where the inherent risk for all assertions would be determined by the auditor to be the same, which generally are audit areas where inherent risk is low and control risk is high for all assertions.

61. PAFA

PAFA supports the separate assessments of inherent and control risks at assertion level and is comfortable that the revised requirements and guidance are appropriate to support the separate assessment.

62. SAICA

- One respondent commented that assessing control risk in terms of paragraph 50, at maximum or less than maximum based on whether the auditor plans to test the operating effectiveness of internal controls, is confusing when compared to ISA 200.A41, which states that control risk is the function of

the effectiveness of the design, implementation and maintenance of internal control by management to address identified risks. The conceptual link exists and is alluded to in the application material, in paragraphs A232-A233. What may be missing is a direct reference that the assessment of control risk is based on the auditor's evaluation of the design and implementation of the controls relevant to the audit at the assertion level.

- SAICA supports the separate assessment of inherent risk and control risk. There should be a better link between how evaluating the design and implementation of controls as well as the decision whether to test the operating effectiveness of controls affect the assessment of control risk, i.e. the auditor's planned reliance on controls should be based on his/her evaluation of the design and implementation of controls and decision to test the operating effectiveness of controls. The aspect around the auditor's decision to test controls is important in the context that even though the evaluation of the design and implementation of controls related to a relevant assertion(s) for a particular class of transactions, account balance or disclosure had a positive / satisfactory outcome, the auditor's decision may still be to rather perform substantive procedures based on, for example, audit efficiency considerations in the circumstances.
- The requirements to evaluate the design and implementation of internal controls should be further refined. We suggest that the words 'designed effectively' should be replaced with 'appropriately designed'. The fact that the auditor only determines implementation of appropriately designed controls should be part of the requirements and not only described in the application material. Suggested wording for paragraph 42:

"For each control identified as relevant to the audit in accordance with paragraphs 39 and 41, the auditor shall:

- Evaluate whether the control is appropriately designed ~~effectively~~ to address the risk of material misstatement at the assertion level, or ~~effectively~~ appropriately designed to support the operation of other controls; and
- Determine whether each ~~the~~ appropriately designed control has been implemented by performing procedures in addition to inquiry of the entity's personnel."

63. SMPC

- In general we support separate assessments of inherent and control risk at the assertion level. One concern is that it may lead to risks of material misstatement being overstated if inherent risks are no longer allowed to be reduced or mitigated by effective controls.
- It does not appear reasonable to require auditors to identify relevant assertions based on a combined identification of both inherent and control risks (the risk of material misstatement) in order to identify significant classes of transactions, account balances and disclosure and, in turn, to identify relevant controls.
- When identifying relevant assertions, the identification of whether a reasonable possibility of occurrence exists ought to be based on inherent risk alone and not on the combined inherent and control risk.
- In addition, both the auditor's risk identification and assessment would need to differentiate between inherent and control components. The overall risk assessment flowchart shows the identified risks at the assertion level as one step (cross-referenced to para 45 (b)), only to split the steps to inherent

and control for assessment (cross-referenced to paras. 48 and 50 respectively) subsequently. It does not seem logical to assess distinct risks unless they have first been identified as distinct.

65. Chartered Accountants Academy

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.

66. FocusRoi Inc.

We support the separate assessments of inherent and control risk but do not see them as being performed independently of each other. Identify and assess the inherent risks first and then inquire how management mitigates the risk. Refer to our response to question 1a above.

67. Lynessa Dias

I agree with the proposal to separately assess inherent and control risk.

71. UNSW Research Network

- Although not specifically related to separate assessments of inherent and control risk, we (Chen Khalifa and Trotman 2015) find that auditors identify more potential frauds when sequentially considering one risk area at a time (e.g., revenue recognition/receivables, inventory, non-current assets and management estimates). If applied to the unpacking of risk of material misstatement assessments (and we have no reason to expect that our findings would not be applicable), these findings suggest that separate assessments of inherent risk and control risk would result in the identification of more risk factors and a more robust risk assessment process. We therefore support the separate assessment of inherent and control risk.
- As a word of caution, however, while more fraud risk factors were identified, auditors in our study assigned a lower likelihood to these fraud risk factors, suggesting that lower levels of skepticism may accompany the 'unpacking' of assessments of risk of material misstatement. Simon, Smith and Zimbleman (2018) similarly report that decomposition of fraud risk assessments into likelihood and magnitude components (compared to a holistic assessment) led auditors to "...discount their fraud risk assessment for higher-risk fraud schemes"(p.3). These results suggest that while unpacking/decomposing the risk of material misstatement may be beneficial by way of increasing auditors' sensitivity to information, it may limit the skepticism applied to the risks identified. We therefore recommend that the application and other explanatory material relating to paragraph 48 be expanded to reinforce the need to exercise an appropriate level of skepticism across the greater number of identified risks that are likely to follow from the unpacking / decomposition of the components of risk of material misstatement assessments.

72. American Accounting Association

- We generally support the revised guidance requiring separate assessments of inherent and control risk at the assertion level (paragraphs 45-50 of ED-315). However, it is important to note that research has consistently shown that auditors tend to spontaneously combine the two assessments. Vandervelde, Tubbs, Schepanski, and Messier (2009) note that auditors appear to use what they

refer to as a “range model,” where risk factors are weighted and combined in a way that places more weight on factors that are perceived as having the highest risk and less on factors perceived as low risk. Messier and Austin (2000) find there is a “knowledge-based dependence” between inherent and control risk assessment; and Miller, Cipriano, and Ramsay (2012) report that even when auditors are instructed to perform separate inherent and control risk assessments, they tend to evaluate inherent risk with a presumption that controls are effective and revise their combined risk assessments upward only when explicitly informed that controls are not effective. Thus, even though ED-315 provides guidance to assess each of these components in separate sections or paragraphs, it may be difficult or impossible for auditors to not combine these two risk assessments in the absence of specific guidance to the contrary. More explicitly identifying the order in which the assessments should occur might reduce auditors’ tendency to combine their assessments of inherent and control risk.

- In addition, although the changes proposed by ED-315 are generally expected to aid in promoting professional skepticism, it is possible that increasing the focus on separating assessments of inherent and control risk could have a negative impact. Rasso (2015) finds that more broad, abstract interpretations of audit evidence result in heightened skepticism. Combined assessments such as those described by Vandervelde et al. (2009) allow individuals to connect individual pieces of information or evidence and develop more complete mental representations of the “big picture” (e.g., Christ 1993). It is important that the Board monitor the adoption of ISA 315 (Revised) for implementation issues and unintended consequences.