ISA 540 (Revised) Post-Implementation Survey

Response ID:398 Data

3. Section II: About the Respondent

1. Please provide the following information about your organization (if applicable) and other contact information:

Organization (or leave blank if you are completing the survey in your personal capacity) : PricewaterhouseCoopers International Limited
Name(s) of contact(s) for this submission : Wes Bricker, Sarah Isted
Job title or role : Global Assurance Leader, Global Policy & Regulation Leader
E-mail address(es) of contact(s) : wesley.bricker@pwc.com, sarah.t.isted@pwc.com

2. Please select from the following options the stakeholder group to which you or your organization belongs:

Accounting Firm

Specify the type of accounting firm you represent:

Global accounting firm

3. Please select from the following options the geographical region that best matches you or your organization:

Global

4. Did you undertake outreach activities with other stakeholders outside your organization to inform your responses to this survey?

No

5. You are welcome to provide any additional information you believe may be relevant to clarify the context in which you are completing the survey, or the circumstances or experiences that have informed your views or perspectives (or you can choose to leave this question blank).

4. Section III: Overall Questions

6. Please provide overall views about whether ISA 540 (Revised) has achieved its intended purpose and the objectives of the IAASB in developing the revised standard.

Overall, we consider ISA 540 (Revised) has largely achieved the IAASB's intended purpose of strengthening audit quality in relation to the audit of accounting estimates and related disclosures by driving a risk-based audit approach.

The standard appropriately reflects that accounting estimates vary widely in nature and are inherently affected by estimation uncertainty, complexity and subjectivity, and that these characteristics influence susceptibility to misstatement and therefore the nature and extent of the required audit response.

We note, however, that alongside the feedback from respondents to the specific historical implementation questions set out in this PIR, it is important for the Board to also evaluate the impact of emerging technologies, including AI, on how entities prepare accounting estimates and how auditors may design and perform audit procedures over such estimates developed using emerging technologies, to ensure ISA 540 (Revised) remains fit for purpose. We note that ISA 540 (Revised) does not currently feature on the IAASB's Technology Catalog and recommend that this be incorporated as part of the ongoing consideration of standards that may be impacted by technological impacts.

7. Are you aware of the non-authoritative guidance and support tools developed to support the implementation of ISA 540 (Revised)?

Yes

7A. Do you agree that the non-authoritative guidance and support tools developed to support the implementation of ISA 540 (Revised) are useful?

4 – Strongly Agree

Comments: The non-authoritative materials provide meaningful guidance by illustrating the application of the intended risk-based approach and how to tailor responses appropriately to the assessed risks of material misstatement, as well as the intended scalability of the requirements when applied to simple through to more complex estimates. Such materials also help support consistent implementation, especially during first-time adoption and training.

5. Section IV: Perceived Benefits from ISA 540 (Revised)

8. For each perceived benefit, indicate the extent to which you agree that ISA 540 (Revised) has led to benefits or improvements.

	4 – Strongly Agree	3 – Agree	2 – Disagree	1 – Strongly Disagree	0 – No Response
(a) Enhanced exercise of professional skepticism when auditing accounting estimates.		X			
(b) Greater consideration of the skills and competencies of the engagement team, including the need to involve specialists or experts.		X			
(c) Greater attention to understanding management's process for making estimates, including the selection of methods, assumptions and data (and the consistency of selection between periods).	X				
(d) Better or more focused assessments of the risks of material misstatements for accounting estimates.		X			
(e) More focus on understanding and testing controls related to accounting estimates.		X			
(f) Increased auditor attention to disclosures related to accounting estimates, including disclosures about estimation uncertainty.	X				
(g) Enhanced interactions and communications between the auditor and management and those charged with governance related to the audit of accounting estimates.		X			
(h) Enhanced quality of financial reporting related to accounting estimates.	X				

9. Are there any additional benefits or positive outcomes arising from the implementation of ISA 540 (Revised) that you would like to highlight?

Yes

Please specify:

We have not identified specific additional benefits but would like to emphasize the following points referred to in our response to Question 8 above. In our view, the revised standard has strengthened the audit of accounting estimates by providing a clearer and more robust framework for identifying and responding to the assessed risks of material misstatement arising from estimation uncertainty, complexity and subjectivity.

The revised standard has enhanced working practices by more explicitly driving audit responses that address the methods, significant assumptions and data used by management, and by clarifying expectations around evaluating whether accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework. This has helped to support clearer documentation of significant judgements and conclusions, particularly for estimates that have higher estimation uncertainty.

We furthermore believe that the emphasis on disclosures (and in particular, disclosures about estimation uncertainty) has also supported more effective communications with management and those charged with governance regarding their estimates.

6. Section V: Potential Issues or Challenges Relating to ISA 540 (Revised)

10. ISA 540 (Revised) was designed to be capable of being applied to all accounting estimates, and for the nature, timing and extent of the risk assessment and further audit procedures to be varied in relation to the estimation uncertainty and the assessment of the risks of material misstatement. Indicate the extent to which you have experienced or are aware of any issues or challenges related to scalability and proportionality.

3 – Moderate Issues or Challenges

11. Briefly describe these or any other issues or challenges you encountered related to scalability and proportionality.

We observe that the standard's baseline requirements applicable to all estimates are considered too onerous for less complex, lower-risk estimates. In cases where the entity has less complex estimates, the level of effort and related documentation is generally seen as excessive and not sufficiently differentiated from the work effort necessary for highly complex estimates or those for which a significant risk has been identified. For example, ISA 540 (Revised) requires an evaluation and documentation of inherent risk factors for all estimates, even where such factors may not meaningfully be present in non complex estimates. Similarly, the stand back requirement seems to have limited impact on the quality of audit work for less complex estimates involving limited management judgement and where no contradictory evidence exists.

We also observe that, due to the professional judgement involved in auditing estimates, there can be different perspectives about, and a lack of consistency in, the appropriate extent of audit procedures and documentation. Although ISA 540 (Revised) acknowledges that significant judgement may be involved, differences in how auditors assess non complex estimates in comparable circumstances (for example, as low versus medium risk) can lead to substantially different audit responses and inconsistency, which can give rise to comparability questions by audited entities and regulators.

12. In your view, are the issues or challenges due to a lack of clarity or insufficiency of the requirements or application material in the standard?

No

13. What specific suggestions do you have for how the IAASB can best address the issues or challenges you have identified (e.g., standard-setting, non-authoritative guidance, or other actions)?

While we appreciate the IAASB's Simple and Complex Illustrative Examples, issued in May 2020, we believe it would be helpful, to drive greater consistency, for the IAASB to provide some additional illustrative examples that practically demonstrate relevant considerations, application, and specifically documentation, to comply with the requirements for less complex estimates that are assessed as lower on the spectrum of inherent risk.

7. Section V: Potential Issues or Challenges Relating to ISA 540 (Revised) (continued)

14. Indicate the extent to which you have experienced or are aware of the following issues or challenges in applying ISA 540 (Revised) with respect the auditor exercising professional skepticism when auditing accounting estimates and related disclosures.

	4 – Significant Issues or Challenges	3 – Moderate Issues or Challenges	2 – Minor Issues or Challenges	1 – No Issues or Challenges	0 – No Response
(a) Appropriately challenging management's judgments used in making accounting estimates, particularly when they involve complex or subjective inputs.		X			
(b) Identifying and appropriately responding to potential indicators of management bias in the development of accounting estimates.			X		
(c) Appropriately considering all relevant audit evidence obtained, whether corroborative or contradictory.			X		

15. Briefly describe these or any other issues or challenges you encountered related to exercising professional skepticism.

ISA 540 (Revised) has contributed positively by explicitly elevating the importance of professional scepticism in auditing accounting estimates. When the evidence supporting management's assumptions is predominantly qualitative, or when external data is limited, not directly comparable, or unavailable, both the application and documentation of professional scepticism become difficult, since a less objective basis for questioning management's assumptions or conclusions is available and greater judgement needs to be applied.

Additional challenges relate to determining the extent of audit documentation required to clearly demonstrate the nature and extent of the auditor's challenge of management and questioning mindset, including the nature and extent of challenge, discussions, and corroborative evidence in order to conclude on the reasonableness of management's assumptions.

16. In your view, are the observed issues or challenges due to a lack of clarity or insufficiency of the requirements or application material in the standard?

Difficult to Determine

17. What specific suggestions do you have for how the IAASB can best address the issues or challenges you have identified (e.g., standard-setting, non-authoritative guidance, or other actions)?

No response

8. Section V: Potential Issues or Challenges Relating to ISA 540 (Revised) (continued)

18. Indicate the extent to which you have experienced the following issues or challenges in applying ISA 540 (Revised) with respect to *risk assessment procedures and identifying and assessing the risks of material misstatement related to accounting estimates*.

	4 – Significant Issues or Challenges	3 – Moderate Issues or Challenges	2 – Minor Issues or Challenges	1 – No Issues or Challenges	0 – No Response
(a) The consideration of inherent risk factors and the interrelationship between them in identifying and assessing risks of material misstatement related to accounting estimates.			X		
(b) How the understanding of the entity and its environment, and the entity's internal control for accounting estimates, relates to the understanding required by ISA 315 (Revised 2019) (i.e., whether it is clear that the requirements in paragraph 13 of ISA 540 (Revised) relate specifically to accounting estimates and build on the broader requirements in ISA 315 (Revised 2019)).			X		
(c) Reviewing the outcome of previous accounting estimates or, where applicable, their subsequent re-estimation (i.e., the retrospective review of accounting estimates).			X		
(d) Understanding management's process for making accounting estimates, including how management identifies and selects relevant methods, assumptions and data, and how management understands and addresses estimation uncertainty.			X		
(e) The separate assessments of inherent and control risk relating to an accounting estimate.			X		
(f) Whether any of the assessed risks of material misstatement are significant risks.			X		

19. Briefly describe these or any other issues or challenges you encountered related to risk assessment procedures and whether such issues or challenges relate primarily to estimates that have a high degree of estimation uncertainty or complexity.

Some challenges encountered in risk assessment procedures relate to appropriately identifying and articulating inherent risk factors that have a greater impact on the level of inherent risk associated with accounting estimates. We observe that these challenges are most pronounced for estimates with a high degree of estimation uncertainty or complexity, where significant judgement, complex models or assumptions, or less observable inputs increase the difficulty in assessing the likelihood and magnitude of potential misstatement and in clearly documenting the rationale for the assessed risks, i.e., which inherent risk factors are the predominant drivers of the assessed risks.

Challenges were also identified in the risk assessment procedures related to accounting estimates for which the auditor determines there to be limited inherent risk factors that affect the level of inherent risk, and the extent of procedures required relating to retrospective reviews where engagement circumstances indicate the accounting estimate has a lower degree of estimation uncertainty and complexity. In those circumstances, certain engagement teams are of the view that retrospective reviews provide limited benefits to the quality of risk assessment.

20. In your view, are the observed issues or challenges due to a lack of clarity or insufficiency of the requirements or application material in the standard?

Difficult to Determine

21. What specific suggestions do you have for how the IAASB can best address the issues or challenges you have identified (e.g., standard-setting, non-authoritative guidance, or other actions)?

It would be helpful to provide further guidance and illustrative examples on how retrospective reviews can be performed and documented in a proportionate manner, particularly where engagement circumstances indicate a lower degree of estimation uncertainty and complexity.

9. Section V: Potential Issues or Challenges Relating to ISA 540 (Revised) (continued)

22. Indicate the extent to which you have experienced the following issues or challenges in applying ISA 540 (Revised) with respect to *responding to the assessed risks of material misstatement*

	4 – Significant Issues or Challenges	3 – Moderate Issues or Challenges	2 – Minor Issues or Challenges	1 – No Issues or Challenges	0 – No Response
Responses to the Assessed Risks of Material Misstatement (a) Determining the most appropriate response(s) to the assessed risks of material misstatement at the assertion level from among the testing approaches in paragraph 18 of ISA 540 (Revised).			X		
(b) Determining whether to test the operating effectiveness of controls related to an accounting estimate.			X		
(c) Appropriately applying the testing approach of obtaining audit evidence about events occurring up to the date of the auditor’s report, either alone or with another testing approach(es).				X	
(d) Testing how management made the accounting estimate.			X		
(e) Developing an auditor’s point estimate or range.			X		
Overall Evaluation (f) Determining whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated.			X		
(g) Evaluating identified misstatements related to accounting estimates, including when the audit evidence supports a point estimate that differs from management’s point estimate or a range that does not include management’s point estimate, or when the auditor’s range is wide (in some cases, multiples of materiality for the financial statements as a whole).			X		

23. Briefly describe these or any other issues or challenges you encountered related to responding to risks of material misstatement and whether such issues or challenges relate primarily to estimates that have a high degree of estimation uncertainty or complexity.

Some engagement teams tend to identify too many significant assumptions and do not feel confident in categorising assumptions as significant vs. non-significant. We observe that this can dilute focus and drive additional, unnecessary work effort. This typically arises in relation to estimates with higher estimation uncertainty and/or complexity. In particular, where outcomes are sensitive to multiple interdependent assumptions, inputs are less observable, or management's method involves complex modelling, it is more difficult to distinguish assumptions that truly drive the measurement of the estimate and therefore the potential source of related risks from those that are ancillary.

24. In your view, are the observed issues or challenges due to a lack of clarity or insufficiency of the requirements or application material in the standard?

Difficult to Determine

25. What specific suggestions do you have for how the IAASB can best address the issues or challenges you have identified (e.g., standard-setting, non-authoritative guidance, or other actions)?

No response

10. Section V: Potential Issues or Challenges Relating to ISA 540 (Revised) (continued)

26. Indicate the extent to which you have experienced the following issues or challenges in applying ISA 540 (Revised) with respect to *communication, specialized skills or knowledge, including using the work of an auditor's expert, and documentation*.

	4 – Significant Issues or Challenges	3 – Moderate Issues or Challenges	2 – Minor Issues or Challenges	1 – No Issues or Challenges	0 – No Response
Communication (a) Determining the matters, if any, to communicate related to accounting estimates, (including about significant qualitative aspects of the entity's accounting practices and significant deficiencies in internal control).			X		
Specialized Skills or Knowledge, Including Using the Work of an Auditor's Expert (b) Determining when it is appropriate to involve an auditor's expert(s) (an internal or external expert) and using the work of an auditor's expert(s) in auditing an accounting estimate(s).			X		
Documentation (c) Preparing appropriate audit documentation in accordance with the requirements in paragraph 39 of ISA 540 (Revised).			X		

27. Briefly describe these or any other issues or challenges you encountered or observed related to communications, specialized skills or knowledge (including using the work of an auditor's expert) and documentation.

No response

28. In your view, are the observed issues or challenges due to a lack of clarity or insufficiency of the requirements or application material in the standard?

No

29. What specific suggestions do you have for how the IAASB can best address the issues or challenges you have identified (e.g., standard-setting, non-authoritative guidance, or other actions)?

N/A