



Audit Conference 2019

REFLECT, REFORM, REFOCUS

Hear insights from Sir Donald Brydon and other notable experts on UK audit market reform.

Refocus for the future with essential technical updates.

Friday 4 October
Chartered Accountants' Hall, Moorgate, London

#icaewAudit

BOOK NOW



icaew.com/auditconference



Auditing estimates and related disclosures – ISA 540 (Revised)

JULY 2019

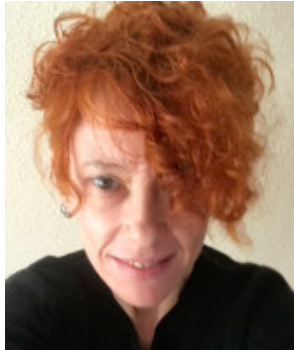
JOHN SELWOOD

GILL SPAUL – MOORE STEPHENS INTERNATIONAL

Presenters

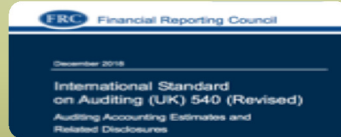


John Selwood



Gill Spaul
Moore Stephens International

Webinar highlights



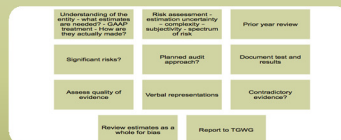
Revised ISA 540 - Overview



Risk assessment



Scepticism



Documentation



Practical examples



What is the Audit & Assurance Faculty doing

Auditing estimates and related disclosures – ISA 540 (Revised)

REVISED ISA 540 - OVERVIEW

ISA 540 Accounting estimates

New standard

- Periods commencing 15 December 2019
- Early adoption permitted

Standard

Audit and Assurance



Financial Reporting Council

December 2018

International Standard
on Auditing (UK) 540 (Revised)

Auditing Accounting Estimates and
Related Disclosures

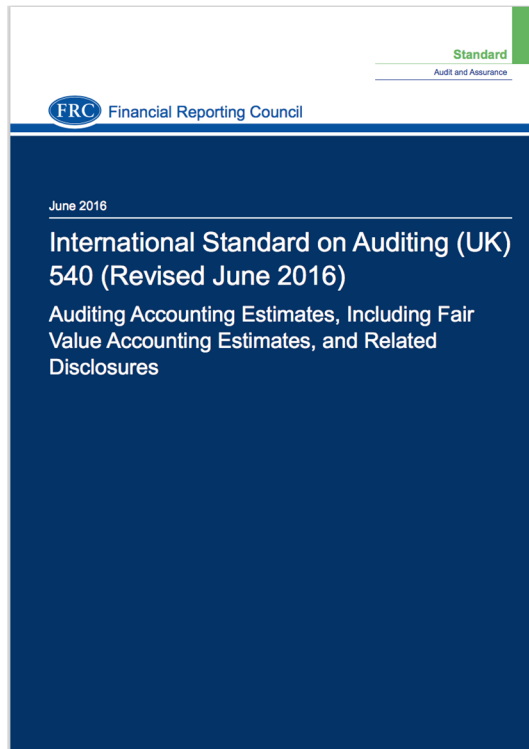
ISA 540 Accounting estimates



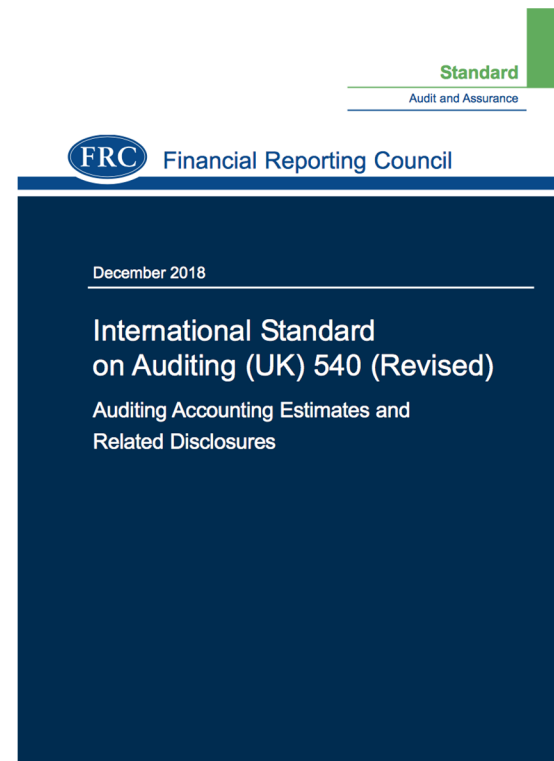
The problems

- Numerous enhanced requirements
- Already a difficult area
- ISA 540 already not well complied with?
- Weak spot in some audit methodologies?

More requirements

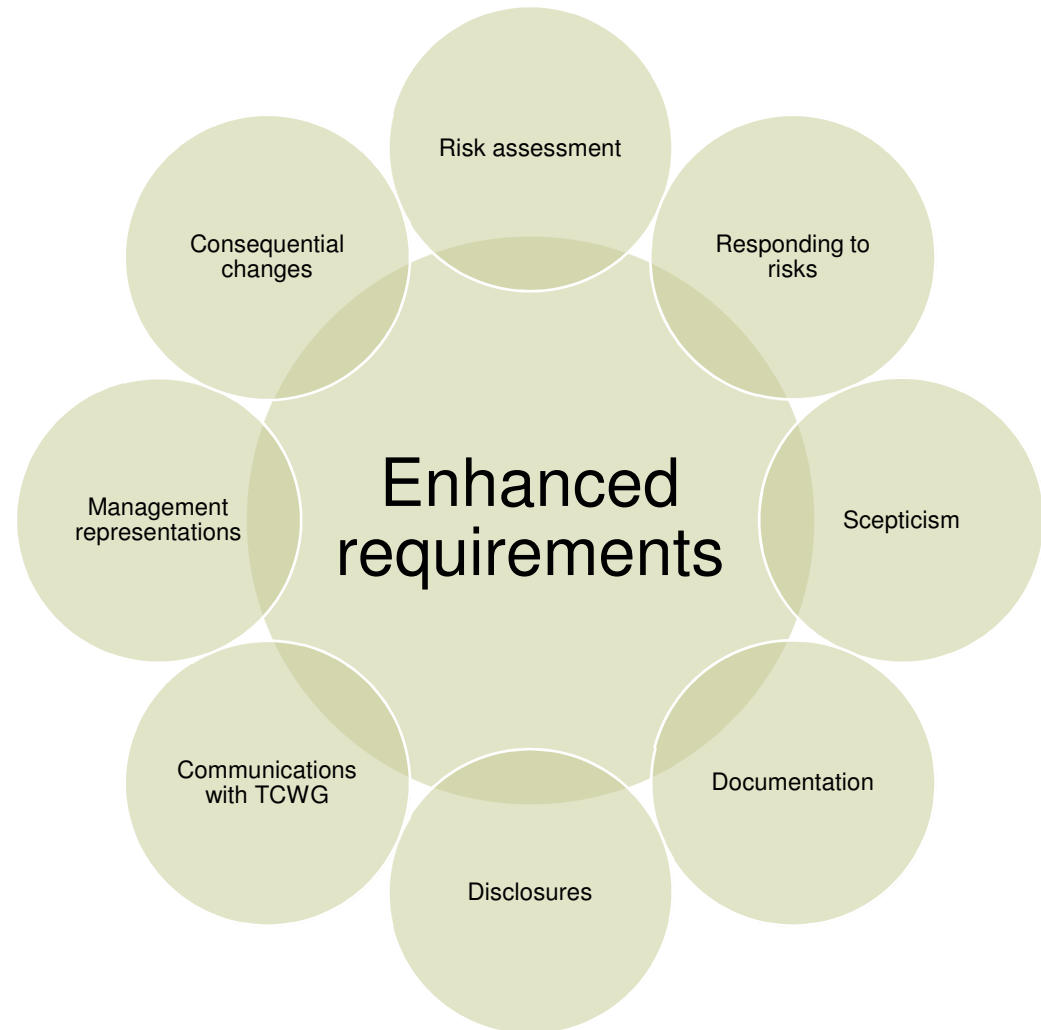


23



39

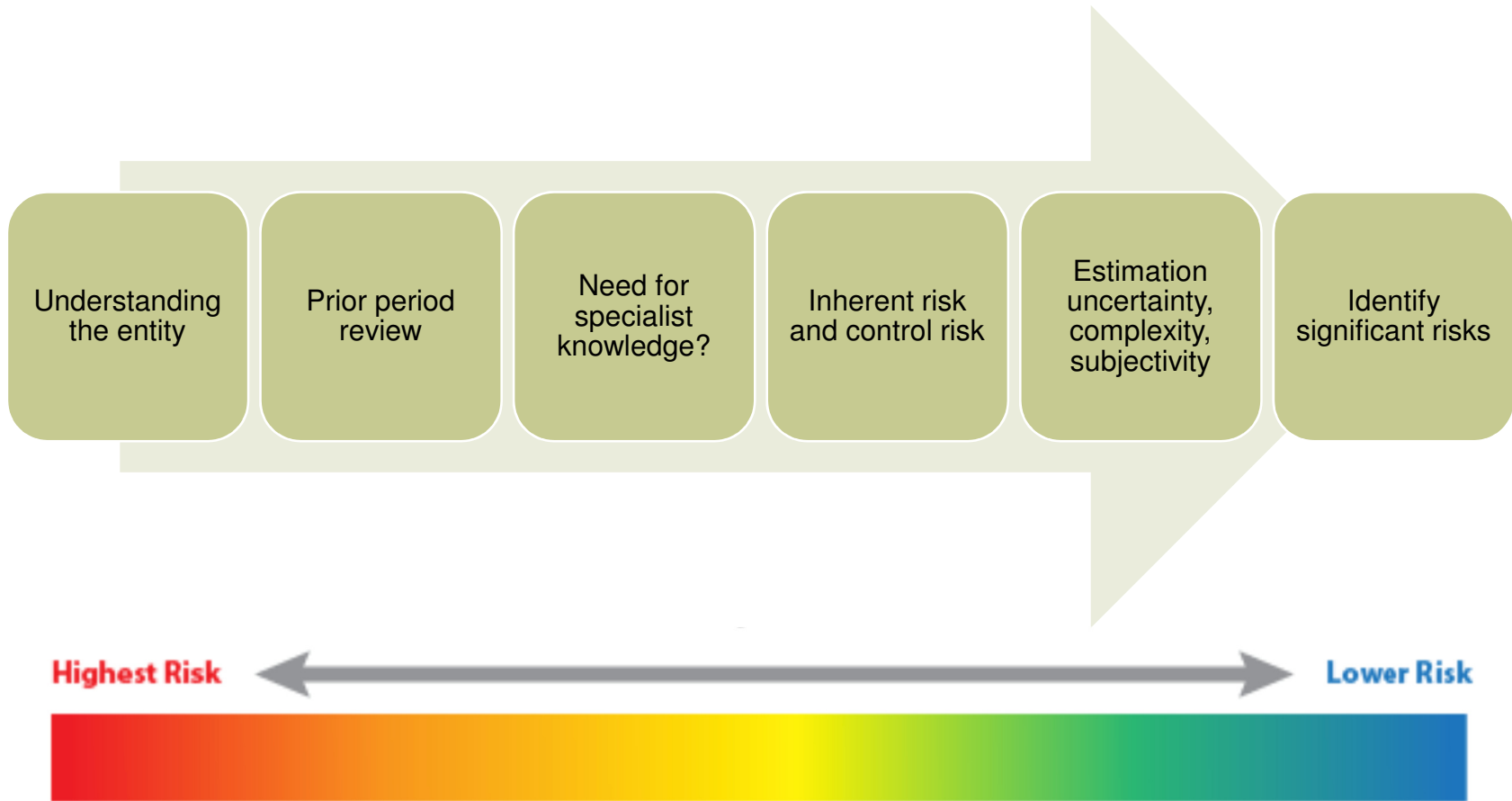
ISA 540 Numerous enhancements



Auditing estimates and related disclosures – ISA 540 (Revised)

RISK ASSESSMENT

Accounting estimates – risk assessment



Spectrum of inherent risk

Auditing estimates and related disclosures – ISA 540 (Revised)

SCEPTICISM

Scepticism



New in ISA 540

- More questioning and challenge
- Not just seeking corroboration
- Looking for contradictory evidence

Scepticism

How?

- A checklist is not the answer
- Good audit team training
- Thorough file review and coaching



Scepticism



The result?

- Improved audit evidence

Auditing estimates and related disclosures – ISA 540 (Revised)

DOCUMENTATION

Audit documentation

Understanding of the entity - what estimates are needed? - GAAP treatment - How are they actually made?

Risk assessment - estimation uncertainty – complexity – subjectivity - spectrum of risk

Prior year review

Significant risks?

Planned audit approach?

Document test and results

Assess quality of evidence

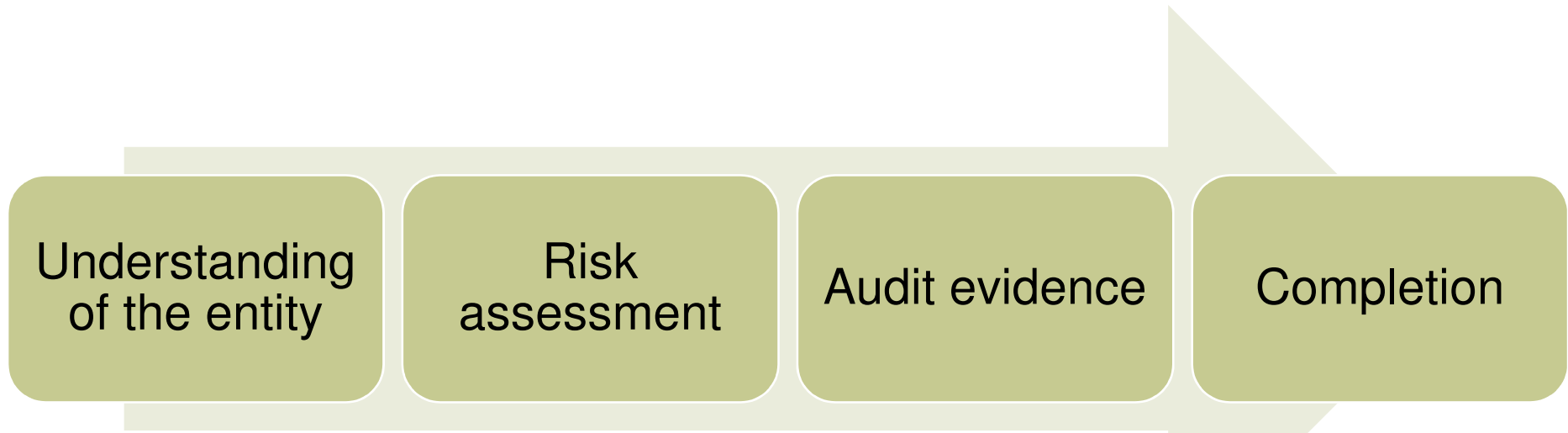
Verbal representations

Contradictory evidence?

Review estimates as a whole for bias

Report to TGWG

Is there a more holistic way?



Could all work on accounting estimates be documented separately 'cradle to grave'?

Auditing estimates and related disclosures – ISA 540 (Revised)

PRACTICAL EXAMPLES

Example 1 - depreciation



Haulage company – large fleet

- HGV tractor units have a life of 4 years
- Residual value £55,000 for additions in year

Example - depreciation

Understand
the entity

Business strategy

GAAP – FRS 102

Internal controls?

Prior
periods
review

At what age are vehicles
disposed of?

How does RV compare to
that estimated?

Example - depreciation

SEPARATE
risk
assessments

Inherent risk

Lower end of spectrum
–, subjectivity,
complexity, bias, fraud

Estimation uncertainty
not as low?

Control risk

No testing of controls
planned

Risk cannot be low

Note: ISA is specific on the nature of audit procedures



The auditor's further audit procedures **shall** include one or more of the following approaches:

- Obtaining audit evidence from events occurring up to the date of the auditor's report
- Testing how management made the accounting estimate
- Developing an auditor's point estimate or range

Example - depreciation

Approach Testing of how management made the accounting estimate

Useful life Regulatory issues?

Test age of vehicles sold

Residual value How did management arrive at £55,000?

Look at current market prices for 4 year old vehicles

Example 2 - depreciation



Airline

- Components have 3 to 30 year useful life.
- Risks might be on the other end of the spectrum!

Example 3 – contingent liability



Disputed construction contract

- A construction company is being sued for £5m for completing a project to the wrong spec – the building was 25m² smaller than the plans
- The directors believe the case will fail and have disclosed it as a contingent liability – the directors don't believe that is significant

Example – contingent liability

Understand
the entity

Understand the nature of the contracts and
the industry

GAAP – FRS 102 – provisions/contingent
liability

Internal controls?

Prior
periods
review

Look at similar ongoing cases or cases in the
past

There may not be any

Example – contingent liability

Inherent risk	Estimation uncertainty	Higher on the scale
	Complexity	Less high
	Subjectivity	Higher on the scale
	Management bias	Much higher on the scale
	Significant risk	Yes – is it a provision? Are disclosures reasonable?

Note: Management bias might make it more important than ever to challenge hard



**A LOOK
AT
SKEPTICISM**

More questioning and challenge
Not just seeking corroboration
Looking for contradictory
evidence

Example – contingent liability

Audit approach –
Test how management made the accounting estimate

Review legal advice and discuss with legal team

Also, review the details of the case

Documentation!

Challenge
management on assumptions in their legal defense

Look for similar cases to back management's' view

Documentation!

Are disclosures reasonable?

Is disclosure suitably robust?

Are prejudicial disclosure exemptions reasonable?

Auditing estimates and related disclosures – ISA 540 (Revised)

***WHAT IS THE AUDIT AND
ASSURANCE FACULTY DOING?***

Implementation support

Online
guides

Snapshot
examples

Webinars
and events

Future events

For details, please visit [icaew.com/aafevents](https://www.icaew.com/aafevents)



Webinar

04 September - A Practical Guide to Auditing Related Party Transactions



Audit Conference

04 October 2019

Thank you for attending

Please take the time to fill out our short survey.

Contact the Audit & Assurance Faculty

 +44 (0)20 7920 8493

 tdaf@icaew.com

 icaew.com/aaf

ICAEW and the presenters will not be liable for any reliance you place on the information in this presentation. You should seek independent advice.



icaew.com