ISA 540 (Revised) Implementation –
Simple and Complex Illustrative Examples
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ISA 540 (Revised) Implementation – Illustrative Examples

This publication has been prepared by a Working Group of the International Auditing and Assurance Standards Board (IAASB) following the approval of International Standard on Auditing (ISA) 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*. Reading this publication is not a substitute for reading the International Standards on Auditing (ISAs) nor does it amend or override the ISAs, the texts of which alone are authoritative. The illustrative examples include explanations of how certain requirements of ISA 540 (Revised) may be applied but do not represent the audit documentation that would be prepared.

Introduction

The following illustrative examples are designed to illustrate how an auditor could address certain requirements of ISA 540 (Revised), and have been developed to assist the auditor in understanding how ISA 540 (Revised) may be applied:

1. Simple Accounting Estimate – Provision on Inventory Impairment	Example 1 illustrates how an auditor may address selected requirements of ISA 540 (Revised) in the context of the audit of the financial statements of an entity with relatively simple accounting estimates.
2. Complex Accounting Estimate – Provision on Property, Plant and Equipment Impairment	Example 2 illustrates how an auditor may address selected requirements of ISA 540 (Revised) in the context of the audit of the financial statements of an entity that include more complex accounting estimates.

The examples illustrate accounting estimates with varying characteristics and degrees of complexity. Each example illustrates a selection of requirements from ISA 540 (Revised). Not all requirements are addressed in each example, nor do they cover all parts of those requirements that have been selected. The requirements selected across each example vary to illustrate different aspects of ISA 540 (Revised) and to focus on those requirements that are most relevant to the example.

These examples use the following format:

Selection of ISA 540 (Revised) Requirements	Auditor's Understanding and Approach
This column contains extracts from the requirements of ISA 540 (Revised). It is not a substitute for reading the standard and does not contain the objectives, definitions and application material that are necessary to apply the requirements properly.	This column provides examples of how the auditor may have responded to the requirements, including describing procedures that were performed and possible outcomes. It is not intended to: • Cover other possible outcomes; • Describe every procedure that may be possible to comply with the relevant requirement; or • Address all the relevant considerations in the second column.

These examples are intended to be read together to demonstrate how an auditor's work effort to comply with the requirements of ISA 540 (Revised) may be scaled down and scaled up when auditing simple and complex accounting estimates, respectively. For example, an auditor's work effort in obtaining an understanding of the entity and its environment, including the entity's internal control, may be relatively scaled down when auditing simple versus complex accounting estimates. In addition, the auditor may determine that specialized skills are not required, or that there are fewer significant assumptions, or that the applicable method does not involve modelling, when auditing simple accounting estimates.

Illustrative Examples Not Covered in this Publication

Additional illustrative examples are being developed to illustrate how an auditor may address the requirements of ISA 540 (Revised) in the context of more complex accounting estimates such as those relating to expected credit losses.

Example 1 – Application of Select Aspects of ISA 540 (Revised) to Provision on Inventory Impairment

Background

The entity sells cameras of three types: professional, enthusiast and consumer. Professional camera items are expensive, and the entity holds small amounts of inventory. Enthusiast camera items are mid-priced, and the entity holds comparatively large amounts of inventory. Consumer camera items are relatively cheap, and the entity holds large amounts of inventory. Due to the fast-moving nature of the enthusiast and consumer photographic goods industry, the introduction of new models may make selling older models more difficult. In addition, improvements in built-in cameras in mobile phones are reducing sales of consumer cameras. When sales of particular models slow down, the audited entity's management reduces the selling price to try to sell slow moving inventories. These discounts may be increased over time if considered necessary to achieve sales. At the year-end, management assesses and provides for inventory impairment based on changes in customer demand, technology developments or other economic factors.

For this example, the applicable financial reporting framework requires that inventory is measured at the lower of cost and net realizable value.[2] The amount of any write-down of inventories to net realizable value and all losses of inventories is recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, is recognized as a reduction in expense in the period in which the reversal occurs.[3] The applicable financial reporting framework requires disclosure of the accounting policies adopted in measuring inventories, including the cost formula used, the amount of any write-down of inventories recognized as an expense in the period, and the amount of any reversal of any write-down that is recognized as a reduction in the amount of inventories recognized as an expense in the period, among others.[4]

The entity is not operating in a regulated sector.

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[2] For example, International Accounting Standard (IAS) 2, *Inventories*, paragraph 9.

[3] For example, IAS 2, paragraph 34.

[4] For example, IAS 2, paragraph 36.

Application of ISA 540 (Revised)

The table below gives illustrative examples of an auditor's understanding and approach that may be followed in relation to selected requirements of ISA 540 (Revised). It does not address all the requirements of the standard. There may also be other factors that are relevant in the specific circumstances of an audit engagement of a similar entity (e.g., pricing rebates from suppliers and / or the effects of foreign exchange movements on the prices of imported goods).

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
Risk Assessment Procedures and Related Activities	
13. When obtaining an understanding of the entity and its environment, including the entity's internal control, as required by ISA 315 (Revised),[7] the auditor shall obtain an understanding of the following matters related to the entity's accounting estimates. The auditor's procedures to obtain the understanding shall be performed to the extent necessary to provide an appropriate basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. (Ref: Para. A19–A22)	The auditor performed risk assessment procedures to obtain an understanding of the entity and its environment, including the following on the entity's accounting estimates as a whole: • Read prior period audit working papers and prior period financial statements; • Examined minutes of board and committee meetings; • Inquired of management with appropriate responsibilities for the financial statements; and • Performed simple walk-throughs of management's process for making the estimate of the provision.
The Entity and Its Environment (a) The entity's transactions and other events and conditions that may give rise to the need for, or changes in, accounting estimates to be recognized or disclosed in the financial statements. (Ref: Para. A23)	The auditor identified that the value of some cameras held by the entity may become impaired. As a result, there may be a need for, or changes in, a provision for inventory impairment (i.e., an accounting estimate) to record impaired inventories at the lower of cost and net realizable value.

5 Refer to the relevant application material.

6 These are intended to illustrate possible outcomes for this example - these do not illustrate all possible outcomes.

7 ISA 315 (Revised), paragraphs 3, 5–6, 9, 11–12, 15–17, and 20–21

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(b) The requirements of the applicable financial reporting framework related to accounting estimates (including the recognition criteria, measurement bases, and the related presentation and disclosure requirements); and how they apply in the context of the nature and circumstances of the entity and its environment, including how transactions and other events or conditions are subject to, or affected by, inherent risk factors. (Ref: Para. A24–A25)	In relation to inventories and impairment, the auditor obtained the understanding of the applicable financial reporting framework through reading the applicable accounting standards. In relation to how the framework's requirements apply in the context of the audited entity and are affected by inherent risk factors, the auditor: • Obtained an understanding of the retail sector for cameras and trading conditions from the start of the period being audited to the current time by researching trade publications; • Made inquiries of management with responsibility for the preparation of the financial statements, inventory control, product purchasing and marketing; and • Performed simple walk-throughs of management's process for making the estimate of the provision. The auditor determined that application of the requirements of the applicable financial reporting framework relevant to the entity's provision for inventory impairment should be straightforward. The nature and circumstances of the business mean that making the estimate of the provision and related disclosures for inventory impairment does not require complex methods or modelling. Relevant inherent risk factors include estimation uncertainty related to market conditions and the possible impact on camera pricing, and the subjectivity of management's assumptions in making the estimate of the provision in accordance with the requirements of the financial reporting framework. *[Note: The assessment of inherent risk is addressed in paragraph 16 of ISA 540 (Revised) below.]*
(c) Regulatory factors relevant to the entity's accounting estimates, including, when applicable,	Having considered their own knowledge, available industry guidance and their discussions with management, the auditor determined there are no regulatory factors relevant to the entity's provision for inventory impairment.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
regulatory frameworks related to prudential supervision. (Ref: Para. A26)	
(d) The nature of the accounting estimates and related disclosures that the auditor expects to be included in the entity's financial statements, based on the auditor's understanding of the matters in 13(a)–(c) above. (Ref: Para. A27)	The auditor obtained this understanding based on the results of the procedures performed in response to paragraph 13(a)–(c) above, identifying that a provision for inventory impairment would be needed. The auditor determined the expected nature of the accounting estimate and related disclosures to be included in the entity's financial statements in accordance with the requirements for the provision of inventory impairment set out in the applicable financial reporting framework (i.e., determining the lower of cost and net realizable value under IAS 2). An understanding of prior period financial statements disclosures with respect to the entity's provision for inventory impairment also assisted in forming this expectation.
The Entity's Internal Control (e) The nature and extent of oversight and governance that the entity has in place over management's financial reporting process relevant to accounting estimates. (Ref: Para. A28–A30)	The auditor determined through observation and inquiries that the owner of the business is involved in the day-to-day operations and exercises oversight over employees responsible for inventory and the bookkeeper, who estimates the provision for inventory impairment.
(f) How management identifies the need for, and applies, specialized skills or knowledge related to accounting estimates, including with respect to the use of a management's expert. (Ref: Para. A31)	The auditor determined through inquiries that management concluded there is no need for specialized skills or expertise beyond their own as they have an in-depth knowledge of the products they deal in and monitor market developments.
(g) How the entity's risk assessment process identifies and addresses risks relating to accounting estimates. (Ref: Para. A32–A33)	The auditor determined that management does not have a formal risk assessment process and considers that this is not unusual for a business of this size and nature.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(h) The entity's information system as it relates to accounting estimates, including: (i) The classes of transactions, events and conditions that are significant to the financial statements and that give rise to the need for, or changes in, accounting estimates and related disclosures; and (Ref: Para. A34–A35) (ii) For such accounting estimates and related disclosures, how management: a. Identifies the relevant methods, assumptions or sources of data, and the need for changes in them, that are appropriate in the context of the applicable financial reporting framework, including how management: (Ref: Para. A36–A37) i. Selects or designs, and applies, the methods used, including the use of models; (Ref: Para. A38–A39) ii. Selects the assumptions to be used, including consideration of alternatives, and identifies significant assumptions; and (Ref: Para. A40–A43)	The auditor determined that each camera has a serial number and can be traced back to a purchase invoice. The cost can be specifically identified for each camera. This cost is recorded by the accounting system when the goods are received. In determining the valuation of the provision for inventory impairment, management uses its judgment and experience of the industry, as well as current trading conditions of its own business and knowledge of its competitors' prices and discounts, to identify the camera categories and models that may have slow-moving inventory and to establish an appropriate estimated realizable value for these cameras. A junior member of staff, overseen by management, maintains a spreadsheet, updated weekly, to record the prices its competitors are setting for the different camera models. These include other retailers with premises within a radius of 20 miles and a selection of websites for other retailers that will be offering the cameras for sale with official warranties from the manufacturers' local agents. (Cameras can be obtained online without official warranties. However, management recognize that they cannot compete on a price basis with those and do not include them in the data collected.) In relation to estimation uncertainty, the auditor determined that management considers the amounts of discounts to be offered and whether these may need to be increased in stages over time to eventually sell all inventories held at year-end and not have to scrap any. Management's judgment of how much to discount the camera models is informed by their experience of which camera models are currently selling well or poorly, and their experience of deep discounting of previous slow-moving items by themselves and by their competitors. Decisions about discounts are agreed with the owner of the business and recorded on the spreadsheet. Impairments of inventory are recognized when camera models are discounted such that the net realizable value is reduced to less than cost. Management does not need or use models to estimate values.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
iii. Selects the data to be used; (Ref: Para. A44) b. Understands the degree of estimation uncertainty, including through considering the range of possible measurement outcomes; and (Ref: Para. A45) c. Addresses the estimation uncertainty, including selecting a point estimate and related disclosures for inclusion in the financial statements. (Ref: Para. A46–A49)	
(i) Control activities relevant to the audit over management's process for making accounting estimates as described in paragraph 13(h)(ii). (Ref: Para. A50–A54)	Control activities exist but are relatively limited in nature. Competitor price data for the spreadsheet is collected by a junior member of staff. This is reviewed for 'reasonableness' by management (based on their own knowledge and experience) who also check a sample of prices themselves, including all prices that appear out of line with the general pattern they expect. The owner is closely involved in, and signs off, determining the levels of discounts to be offered on selling prices and the preparation of the provision where the estimated resale value falls below cost. The bookkeeper uses the inventory records, including the quantities and prices paid for items held, and the discounts agreed by management to calculate the inventory amounts for the financial statements. These are reviewed by the owner for accuracy and completeness.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(j) How management reviews the outcome(s) of previous accounting estimates and responds to the results of that review.	Management does not formally review the outcome of their previous accounting estimates. They have an ongoing process for reviewing discounts that they believe are needed, seeking to apply the minimum discount and increasing it over time if needed to achieve sales.
14. The auditor shall review the outcome of previous accounting estimates, or, where applicable, their subsequent re-estimation to assist in identifying and assessing the risks of material misstatement in the current period. The auditor shall take into account the characteristics of the accounting estimates in determining the nature and extent of that review. The review is not intended to call into question judgments about previous period accounting estimates that were appropriate based on the information available at the time they were made. (Ref: Para. A55–A60)	Based on a review of sale prices actually achieved compared to those that had been estimated at previous year-ends, the auditor identified that the difference between the established provision and the sales prices achieved is usually within materiality.
15. With respect to accounting estimates, the auditor shall determine whether the engagement team requires specialized skills or knowledge to perform the risk assessment procedures, to identify and assess the risks of material misstatement, to design and perform audit procedures to respond to those risks, or to evaluate the audit evidence obtained. (Ref: Para. A61–A63)	The auditor determined that specialized skills were not required.
Identifying and Assessing the Risks of Material Misstatement	
16. In identifying and assessing the risks of material misstatement relating to an accounting estimate and related disclosures at the assertion level, as required by	The auditor assessed that the inherent risk of material misstatement of the valuation of the provision is moderate, taking into account assessments that:

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
ISA 315 (Revised),[8] the auditor shall separately assess inherent risk and control risk. The auditor shall take the following into account in identifying the risks of material misstatement and in assessing inherent risk: (Ref: Para. A64–A71) (a) The degree to which the accounting estimate is subject to estimation uncertainty; and (Ref: Para. A72–A75) (b) The degree to which the following are affected by complexity, subjectivity, or other inherent risk factors: (Ref: Para. A76–A79) (i) The selection and application of the method, assumptions and data in making the accounting estimate; or (ii) The selection of management's point estimate and related disclosures for inclusion in the financial statements.	• The estimate of the provision is subject to moderate estimation uncertainty. This assessment is based on the relatively short forecast period, and the inventory balance with most year-end inventory expected to be sold within 6 months; • The impact of management's subjectivity and possible changes in market conditions that do not reflect management's assumptions could have a moderate effect; • There are independent sources of data for pricing that management uses as part of the method; • The application of the method used by management to calculate a point estimate for the provision is relatively simple; and • The required related disclosures are limited and easy to determine from the application of the method. The auditor assessed control risk to be high as the entity's controls are limited and not designed to address the risk of material misstatement resulting from making assumptions about the future that turn out to be invalid. Taking account of the relative simplicity of the method used by management, the nature and availability of the data used, and the limited nature of the other controls applied by the entity, the auditor determined that a wholly substantive approach is most appropriate.
17. The auditor shall determine whether any of the risks of material misstatement identified and assessed in accordance with paragraph 16 are, in the auditor's judgment, a significant risk.[9] If the auditor has determined that a significant risk exists, the auditor shall	Taking account of the understanding obtained of the business and current market conditions, the auditor did not consider the risk of material misstatement of the valuation of the provision for inventory impairment to be a significant risk.

8 ISA 315 (Revised), paragraphs 25 and 26

9 ISA 315 (Revised), paragraph 27

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
obtain an understanding of the entity's controls, including control activities, relevant to that risk.[10] (Ref: Para. A80)	
Responses to the Assessed Risks of Material Misstatement	
18. As required by ISA 330,[11] the auditor's further audit procedures shall be responsive to the assessed risks of material misstatement at the assertion level,[12] considering the reasons for the assessment given to those risks. The auditor's further audit procedures shall include one or more of the following approaches: (a) Obtaining audit evidence from events occurring up to the date of the auditor's report (see paragraph 21); (b) Testing how management made the accounting estimate (see paragraphs 22–27); or (c) Developing an auditor's point estimate or range (see paragraphs 28–29). The auditor's further audit procedures shall take into account that the higher the assessed risk of material misstatement, the more persuasive the audit evidence needs to be.[13] The auditor shall design and perform further audit procedures in a manner that is not biased	The auditor determined that the most appropriate further audit procedures were primarily testing how management made the accounting estimate, as well as through obtaining audit evidence from events occurring up to the date of the auditor's report. The auditor concluded that it was not necessary to develop an auditor's point estimate or range, subject to the outcome of the further audit procedures in relation to paragraph 18(b).

10 ISA 315 (Revised), paragraph 29

11 ISA 330, paragraphs 6–15 and 18

12 ISA 330, paragraphs 6–7 and 21

13 ISA 330, paragraph 7(b)

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory. (Ref: Para. A81–A84)	
Obtaining Audit Evidence from Events Occurring up to the Date of the Auditor's Report 21. When the auditor's further audit procedures include obtaining audit evidence from events occurring up to the date of the auditor's report, the auditor shall evaluate whether such audit evidence is sufficient and appropriate to address the risks of material misstatement relating to the accounting estimate, taking into account that changes in circumstances and other relevant conditions between the event and the measurement date may affect the relevance of such audit evidence in the context of the applicable financial reporting framework. (Ref: Para. A91–A93)	For the professional, enthusiast and consumer camera ranges, the auditor analyzed each camera model to identify any that may have slow-moving inventory, taking into account: • Sales for the year of each camera; • Inventory at year-end; • Sales between year-end and the date of the test, including the levels of any discounts; and • Inventory at the date of the test. Sufficient appropriate audit evidence about sales during the year and the inventory levels at the year-end was obtained in other elements of the audit. The auditor designed and performed further substantive procedures to obtain sufficient appropriate audit evidence about sales and discounts after the year-end. This provided evidence that the impairment provision for cameras sold since the year-end was not materially misstated. The auditor also determined that the entity still holds cameras that were in inventory at the year- end and for which the related impairment provision is material.
Testing How Management Made the Accounting Estimate 22. When testing how management made the accounting estimate, the auditor's further audit procedures shall include procedures, designed and performed in accordance with paragraphs 23–26, to obtain sufficient appropriate audit evidence regarding the risks of material misstatement relating to: (Ref: Para. A94)	Through discussions with management about their approach, the auditor established that management: • Attends trade fairs to keep informed about new products that may be launched. • Reviews competitors' advertising to understand which camera models their competitors are offering at discounted prices. • Uses their experience of the industry to identify how much to provide against the carrying value of slow-moving items.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(a) The selection and application of the methods, significant assumptions and the data used by management in making the accounting estimate; and (b) How management selected the point estimate and developed related disclosures about estimation uncertainty.	These discussions identified the camera models against which management had established a provision, as well as those camera models which were reviewed by management but against which management did not establish a provision. The discussions were informed and corroborated by the audit evidence from events occurring up to the date of testing, including post-balance sheet sales to identify slow-moving and already discounted camera models, and announcements of major new product developments that may impact the attractiveness of cameras in inventory at the year-end.
Methods 23. In applying the requirements of paragraph 22, with respect to methods, the auditor's further audit procedures shall address: (a) Whether the method selected is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from the method used in prior periods are appropriate; (Ref: Para. A95, A97) (b) Whether judgments made in selecting the method give rise to indicators of possible management bias; (Ref: Para. A96) (c) Whether the calculations are applied in accordance with the method and are mathematically accurate; (d) When management's application of the method involves complex modelling, whether judgments have been applied consistently and whether, when applicable: (Ref: Para. A98– A100)	The auditor concluded that management's method is appropriate to determining whether net realizable value is lower than cost and, in respect of which camera models it is making a provision in accordance with the requirements of the applicable financial reporting framework. The auditor also concluded that management's judgments in selecting the method did not indicate possible management bias as management's method is common industry practice and the auditor agreed it was appropriate in the circumstances. Substantive procedures were designed and performed that provided evidence that calculations applied in the method were mathematically accurate. The method does not involve modelling. Substantive procedures were designed and performed that provided evidence that the integrity of management's assumptions and the data used had been maintained in applying the method.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(i) The design of the model meets the measurement objective of the applicable financial reporting framework, is appropriate in the circumstances, and, if applicable, changes from the prior period's model are appropriate in the circumstances; and (ii) Adjustments to the output of the model are consistent with the measurement objective of the applicable financial reporting framework and are appropriate in the circumstances; and (e) Whether the integrity of the significant assumptions and the data has been maintained in applying the method. (Ref: Para. A101)	
Significant Assumptions 24. In applying the requirements of paragraph 22, with respect to significant assumptions, the auditor's further audit procedures shall address: (a) Whether the significant assumptions are appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate; (Ref: Para. A95, A102–A103) (b) Whether judgments made in selecting the significant assumptions give rise to indicators of possible management bias; (Ref: Para. A96)	The auditor identified that the significant assumptions made by management and the owner are that the discount levels already applied, or that will apply in the future, will enable them to sell inventory over time at the planned prices; known new product releases will not prevent them selling the inventory with the discounts levels they have or plan to apply; and that there will not be other, unknown, new product releases, or changes in the market conditions that may significantly affect sales of year-end inventory. Taking account of the results of the procedures performed to obtain evidence from events occurring up to the date of the auditor's report (see above) and further procedures designed and performed to obtain evidence about: • Comparisons to trends in prior years; and • Review of photography magazines and websites for information relevant to the camera models, the auditor determined that:

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(c) Whether the significant assumptions are consistent with each other and with those used in other accounting estimates, or with related assumptions used in other areas of the entity's business activities, based on the auditor's knowledge obtained in the audit; and (Ref: Para. A104) (d) When applicable, whether management has the intent to carry out specific courses of action and has the ability to do so. (Ref: Para. A105)	○ The assumptions are appropriate in the context of the applicable financial reporting framework and are consistent with the basis for assumptions made in prior years. They are also consistent with the assumptions used for the next year budget. ○ Management's reasons for different planned discounts for different camera models (or camera models that have a variety of characteristics, such as different colours) appear reasonable. ○ There was evidence of possible management bias towards understatement of the provision in relation to two camera models which was followed up in further testing (see below). ○ For the camera models that comprise the provision for inventory impairment, there is evidence that management is both seeking to and managing to sell those cameras at the reduced price and, for those camera models, further price reductions beyond those planned do not appear necessary.
Data 25. In applying the requirements of paragraph 22, with respect to data, the auditor's further audit procedures shall address: (a) Whether the data is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate (Ref: Para. A95, A106); (b) Whether judgments made in selecting the data give rise to indicators of possible management bias; (Ref: Para. A96)	The auditor assessed that the data used by management are appropriate in the context of the financial reporting framework. Procedures designed and performed provided evidence that the data are relevant, reliable and appropriately understood by management, including that: • The figures for sales and inventory agree to the entity's records, about which sufficient appropriate audit evidence has been obtained from other procedures performed. • Original price data agrees to the amounts invoiced by and paid to suppliers. • Competitor pricing information in the spreadsheet used by management in making assumptions and planning discounts, agrees to magazine and website adverts.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
(c) Whether the data is relevant and reliable in the circumstances; and (Ref: Para. A107) (d) Whether the data has been appropriately understood or interpreted by management, including with respect to contractual terms. (Ref: Para. A108)	• Management's knowledge of planned new camera models coming to market is supported by manufacturer originated information. • There is no evidence of possible management bias in the selection of sources of data.
Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty 26. In applying the requirements of paragraph 22, the auditor's further audit procedures shall address whether, in the context of the applicable financial reporting framework, management has taken appropriate steps to: (a) Understand estimation uncertainty; and (Ref: Para. A109) (b) Address estimation uncertainty by selecting an appropriate point estimate and by developing related disclosures about estimation uncertainty. (Ref: Para. A110–A114)	The auditor understood that the applicable financial reporting framework requires disclosure of the accounting policy but, for a business of this size and nature, does not require disclosure of estimation uncertainty or factors affecting it. The auditor concluded that, for most camera models for which a provision is required, the inventory is held at the lower of cost and net realizable value on the basis of the method used by management. Management has not produced a range of possible outcomes to cover possible variations in the discounts that may ultimately be applied as they believe that such variations, if any, will be limited and not have a significant impact. The auditor determined that, with two exceptions, management did consistently take into account competitor's prices in understanding estimation uncertainty. The auditor performed sensitivity analysis on the prices for a sample camera models and concluded that management's belief that such variations, if any, will be limited and not have a significant impact was reasonable.
27. When, in the auditor's judgment based on the audit evidence obtained, management has not taken appropriate steps to understand or address estimation uncertainty, the auditor shall: (Ref: Para. A115–A117) (a) Request management to perform additional procedures to understand estimation uncertainty or to address it by reconsidering the selection of	The auditor identified, and confirmed with management, two camera models which were being sold by competitors at a lower price than management's reduced price and which were not included in management's provision for inventory impairment. For these models, the auditor concluded that management's valuation was overly optimistic as none of these particular models had been sold in over a month and further discounting seemed likely to be necessary.

Selection of ISA 540 (Revised) Requirements[5]	Auditor's Understanding and Approach[6]
management's point estimate or considering providing additional disclosures relating to the estimation uncertainty, and evaluate management's response(s) in accordance with paragraph 26; (b) If the auditor determines that management's response to the auditor's request does not sufficiently address estimation uncertainty, to the extent practicable, develop an auditor's point estimate or range in accordance with paragraphs 28–29; and (c) Evaluate whether a deficiency in internal control exists and, if so, communicate in accordance with ISA 265.[14]	In respect of these two camera models, the auditor discussed with management the reasons for the provision and the auditor's findings. As a result, management agreed to make provisions against these camera models. Taking account of the auditor's sensitivity analysis for the pricing of a sample of other cameras (see above), the auditor concluded that the finding does not constitute a significant deficiency in internal control and that management did not need to perform additional procedures.

[14] ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

Example 2 – Application of Select Aspects of ISA 540 (Revised) to Provision on Property, Plant and Equipment Impairment

Background

The entity manufactures and sells, globally, low to moderately priced consumer cameras. The entity's manufacturing operations are based in a single territory, but sales are made to customers and distributors overseas. Significant changes with an adverse effect on the entity continued to take place during the period as improvements to built-in cameras in mobile devices are reducing sales volumes and prices of consumer cameras, placing pressure on the revenue and profitability of the entity. Management identified the adverse market conditions as an indicator that the carrying value of the entity's property, plant and equipment used to manufacture consumer cameras may be impaired and, as a result, at the period-end management has estimated the recoverable amount of the property, plant and equipment items.

The applicable financial reporting framework is based on international accounting standards and requires that the entity estimate the recoverable amount of an asset with a finite useful life, when there is an indication that the asset may be impaired at the period end.[15] An asset's recoverable amount is measured at the higher of its fair value less costs of disposal and its value in use.[16] If the asset's recoverable amount is lower than its carrying amount, the asset's carrying amount is reduced with the reduction recognized as an impairment loss.[17] IAS 36 requires a range of disclosures, including information about the events and circumstances that led to the impairment, and elements of the methods used to estimate recoverable amount, amongst others.

The entity is not operating in a regulated sector.

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[15] IAS 36, *Impairment of Assets*, paragraph 9

[16] IAS 36, paragraph 18

[17] IAS 36, paragraph 59

Application of ISA 540 (Revised)

The table below gives illustrative examples of the auditor's understanding and approach that may be followed in relation to selected requirements of ISA 540 (Revised). The example does not address all the requirements of the standard. In addition, other events, conditions or factors may be relevant in the specific circumstances of an engagement that may also need to be considered.

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
Risk Assessment Procedures and Related Activities	
13. When obtaining an understanding of the entity and its environment, including the entity's internal control, as required by ISA 315 (Revised),[20] the auditor shall obtain an understanding of the following matters related to the entity's accounting estimates. The auditor's procedures to obtain the understanding shall be performed to the extent necessary to provide an appropriate basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. (Ref: Para. A19–A22)	The auditor performed the following risk assessment procedures to obtain an understanding of the entity and its environment, including the following on the entity's accounting estimates as a whole: • Read prior period audit working papers and prior period financial statements; • Examined minutes of board and committee meetings; • Inquired of management with appropriate responsibilities for the financial statements; • Performed risk assessment analytics; • Performed walkthroughs of management's processes for identifying the need for and making accounting estimates; and • Utilized the auditor's knowledge of the industry in which the entity operates, including that obtained through auditing other entities in the camera manufacturing industry and through review of trade publications and public information issued by other manufacturers.

18 Refer to the relevant application material.

19 These are intended to illustrate possible outcomes for this example - these do not illustrate all possible outcomes.

20 ISA 315 (Revised), paragraphs 3, 5–6, 9, 11–12, 15–17, and 20–21

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
The Entity and Its Environment (a) The entity's transactions and other events and conditions that may give rise to the need for, or changes in, accounting estimates to be recognized or disclosed in the financial statements. (Ref: Para. A23)	As a result of performing the risk assessment procedures, the auditor identified that the adverse market conditions have accelerated during the current period due mainly to the increasing penetration of affordable mobile devices with improving camera capabilities. As a result, the entity's revenues and earnings have failed to meet budgetary targets, despite a budgeted reduction from the prior period levels, which affected several estimates including the valuation of property, plant and equipment.
(b) The requirements of the applicable financial reporting framework related to accounting estimates (including the recognition criteria, measurement bases, and the related presentation and disclosure requirements); and how they apply in the context of the nature and circumstances of the entity and its environment, including how transactions and other events or conditions are subject to, or affected by, inherent risk factors. (Ref: Para. A24–A25)	The auditor obtained an understanding of the detailed requirements of the applicable financial reporting framework by reviewing IAS 36 and associated guidance and practice aids developed by the auditor's firm. IAS 36 requires the entity to assess, at the end of each reporting period, whether there is any indication that property, plant and equipment assets may be impaired and, if any such indication exists, to estimate the recoverable amount of the assets and to determine whether the carrying amount exceeds the estimated recoverable amount. IAS 36 defines recoverable amount as the higher of an asset's or cash-generating unit's fair value less costs of disposal and its value in use. A number of related disclosures are also required by IAS 36 when an impairment loss is recognized, including the judgments and estimates involved in the impairment calculations. In addition, IAS 1[21] requires disclosure of information about the assumptions management makes regarding the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. IAS 36 includes some explicit requirements as to how to calculate recoverable amount (e.g., what specific elements are to be included in a value in use calculation), which can limit the degree of subjectivity involved in selecting and applying a method in the development of the estimate.

[21] IAS 1, *Presentation of Financial Statements*

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
	In this instance, management has used a value in use model to estimate recoverable amount. Such models can typically involve multiple assumptions and the need for complex modelling. This gives rise to subjectivity and susceptibility to management bias in the selection of appropriate assumptions, and complexity in the development and application of an appropriate model. The auditor assessed that the disclosures required by IAS 36 and IAS 1, as relevant to the estimate of recoverable amount of property, plant and equipment for the entity, are not themselves especially complex, nor do they give rise to increased levels of subjectivity or potential for management bias.
(c) Regulatory factors relevant to the entity's accounting estimates, including, when applicable, regulatory frameworks related to prudential supervision. (Ref: Para. A26)	Having considered their knowledge of the camera manufacturing industry, available industry guidance and their discussions with management, the auditor determined there are no regulatory factors relevant to the entity's accounting estimate of the valuation of property, plant and equipment.
(d) The nature of the accounting estimates and related disclosures that the auditor expects to be included in the entity's financial statements, based on the auditor's understanding of the matters in 13(a)–(c) above. (Ref: Para. A27)	The auditor obtained this understanding based on the results of the procedures performed in response to paragraph 13(a)–(c) above. The auditor determined the expected nature of the accounting estimate (valuation and impairment of property, plant and equipment) and related disclosures to be included in the entity's financial statements in accordance with the applicable financial reporting framework (i.e., determining recoverable amount under IAS 36) by: • Reviewing a practice aid developed by the auditor's firm that includes best practice illustrative presentation and disclosure examples for IAS 1 and IAS 36; and • Reviewing the entity's prior period financial statements disclosures regarding its determination of the recoverable amount of property, plant and equipment.
The Entity's Internal Control	The auditor performed risk assessment procedures to obtain an understanding of whether those charged with governance:

Selection of ISA 540 (Revised) Requirements [18]	Auditor's Understanding and Approach [19]
(e) The nature and extent of oversight and governance that the entity has in place over management's financial reporting process relevant to accounting estimates. (Ref: Para. A28–A30).	• Have the skills or knowledge to understand the characteristics of a particular method or model to make accounting estimates and the risks related to accounting estimates – this included assessing the experience of the entity's Audit Committee, relevant to assessing impairment of property, plant and equipment; • Have the skills or knowledge to understand whether management made the entity's accounting estimates in accordance with the applicable financial reporting framework – this included understanding the relevant qualifications of the Audit Committee, including whether it has sufficient knowledge of IAS 36 to understand how management's estimates complied with the requirements of the standard; • Are independent from management, have the information required to evaluate on a timely basis how management made the entity's accounting estimates, and the authority to call into question management's actions when those actions appear to be inadequate or inappropriate – this included inspecting periodic reporting packages submitted to the Audit Committee by management and assessing whether they contained the information necessary to evaluate management's estimates, and evaluating recent interactions between the Audit Committee and management to assess whether the Audit Committee had asked relevant questions about management's estimates; • Oversee management's process for making the entity's accounting estimates, including the use of models – this included corroborating through inspection of minutes and other communications that management submits periodic reporting packages to the Audit Committee and that those submissions are challenged, discussed and approved by the Audit Committee; and • Oversee the monitoring activities undertaken by management – this included evaluating the Audit Committee's involvement in overseeing management's supervision and review procedures to detect and correct deficiencies in the design or operating effectiveness of controls.

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
(f) How management identifies the need for, and applies, specialized skills or knowledge related to accounting estimates, including with respect to the use of a management's expert. (Ref: Para. A31)	Management concluded that, for the purposes of testing the recoverable amount of property, plant and equipment, it had sufficient skills and knowledge to select and apply appropriate methods, assumptions and data without the need to involve an expert. The auditor performed risk assessment procedures to obtain an understanding of whether management: • Considered the specialized nature of the matter requiring estimation (impairment indicators); • Considered the complex nature of the models required to apply the requirements of IAS 36; and • Assessed whether the nature of the condition, transaction or event requiring an accounting estimate (impairment) is unusual or infrequent. The auditor noted that management did take these matters into consideration when performing its own risk assessment of accounting estimates and concluded that management had appropriately applied specialized skills or knowledge.
(g) How the entity's risk assessment process identifies and addresses risks relating to accounting estimates. (Ref: Para. A32–A33)	The auditor performed risk assessment procedures to obtain an understanding of management's risk assessment process overall, and whether, and if so how, management: • Pays particular attention to selecting or applying the methods, assumptions and data used in making accounting estimates – this included understanding management's process around the selection of appropriate methods, assumptions and data and evaluating review controls and other control activities relevant to the impairment process regarding consumer cameras. • Monitors key performance indicators (KPIs) that may indicate unexpected or inconsistent performance compared with historical or budgeted performance or with other known factors (e.g., changes in events or conditions) – this included inspecting evidence of periodic meetings held by management to analyze the

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
	entity's performance against its KPIs and to evaluate the implication of that performance on the entity's accounting estimates, and in particular those developed using forecast information; • Identifies financial or other incentives that may be a motivation for bias – this included understanding what remuneration and other incentives were linked to the output of accounting estimates, and what controls management had implemented to detect potential misstatements arising in estimates as a result of bias; • Monitors the need for changes in the methods, significant assumptions or the data used in making accounting estimates – this included reading minutes of board and committee meetings to assess whether the financial reporting implications of events and conditions arising during the period and after the period end had been taken into consideration by management and what actions had been taken; • Establishes appropriate oversight and review of models used in making accounting estimates – this included understanding and evaluating management's review controls over the development of accounting estimates, including how those controls address the use of models; • Implements a process requiring documentation of the rationale for, or an independent review of, significant judgments made in making accounting estimate – this included understanding and evaluating management's review controls, and management's interactions with the Audit Committee, including any relevant materials submitted for Audit Committee review; • Implements a process of periodic model validation procedures – this included understanding the change controls management has implemented over changes or adjustments to its models, and inspecting minutes of periodic meetings where the need for model changes and enhancements are discussed; and • Takes steps to implement adequate segregation of duties between those responsible for risk assessment activities and those responsible for developing

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
	estimates – this included obtaining an understanding of roles and responsibilities in the estimation process and assessing whether these are allocated in such a way that those preparing the estimate are independent of those individuals responsible for risk assessment, including controls that ensure that the development of estimates is subject to independent review.
(h) The entity's information system as it relates to accounting estimates, including: (i) The classes of transactions, events and conditions that are significant to the financial statements and that give rise to the need for, or changes in, accounting estimates and related disclosures; and (Ref: Para. A34–A35)	The auditor obtained a thorough understanding of the entity's information system when they performed risk assessment procedures in accordance with ISA 315 (Revised).[22] This included understanding which systems and reports are used by management in developing its estimates of recoverable amount for the entity's property, plant and equipment.
(ii) For such accounting estimates and related disclosures, how management: a. Identifies the relevant methods, assumptions or sources of data, and the need for changes in them, that are appropriate in the context of the applicable financial reporting framework, including how management: (Ref: Para. A36–A37) i. Selects or designs, and applies, the methods used, including the	Management concluded that it was unable to determine the fair value less costs of disposal of the assets because they did not believe they could make a reliable estimate of the price at which an orderly transaction to sell the assets would take place between market participants. Therefore, management estimated the recoverable amount of the entity's property, plant and equipment used to produce cameras based on its value in use. Management used the income approach to develop its value in use estimates. The entity has developed a discounted cash flow ("DCF") model. Management made some changes to the model in the current year to take into account some changes in the entity's products and markets.

22 ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment*

Selection of ISA 540 (Revised) Requirements[18]		Auditor's Understanding and Approach[19]
	use of models; (Ref: Para. A38–A39)	
ii.	Selects the assumptions to be used, including consideration of alternatives, and identifies significant assumptions; and (Ref: Para. A40–A43)	The auditor determined the assumptions applied by management in determining recoverable amount to include: • Projected future cash flows, including revenues and assumed revenue growth rates, operating margins, capital expenditures (considered necessary for continued use of the assets) and working capital requirements. • Discount rates determined on a pre-tax basis. In considering alternative cash flow assumptions, the auditor determined that management considered a range of different market sources and historical financial results and market trends. In order to determine the discount rate, having considered alternative methods, management determined that weighted average cost of capital (WACC) was the method most reflective of the entity's financial structure. The auditor observed that management's approach to determining which assumptions are significant assumptions is to perform sensitivity analysis to assess the impact that reasonable variations in assumptions would have on the calculation of the point estimate. As a result, management identified that the estimated value in use had material sensitivity to reasonable variations in revenue forecasts, projected operating margins, capital expenditures, working capital requirements, and discount rate assumptions. As such, these assumptions were identified by management as significant. The auditor considered management's determination of significant assumptions to be appropriate given the nature and circumstances of the entity.
iii.	Selects the data to be used; (Ref: Para. A44)	The auditor determined that the following data was selected by management for use in determining the recoverable amounts of the entity's property, plant and equipment: • Historical cash flows and historical cost asset book values for periods prior to the income approach projection period, selected as it is factual information.

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
	• Data used in budgets approved by those charged with governance, such as approved revenue contracts and internal production capacity and order backlog data, selected to be consistent with the data used in other parts of the business. • Camera industry trend analysis from reputable sources, selected on the basis of agreed industry standards. • Independent external data: Interest rates, beta measures and risk-free rates from reputable sources (e.g., governmental agencies, international financial data providers), selected based on sources management have identified to be reliable in the past.
b. Understands the degree of estimation uncertainty, including through considering the range of possible measurement outcomes; and (Ref: Para. A45)	The auditor determined that management has assessed estimation uncertainty to be high because the estimate of recoverable amount depends on forecasts over a long assessment period and has a range of possible outcomes. Management also performed sensitivity analysis to identify the range of reasonably possible measurement outcomes, which further demonstrates the high degree of estimation uncertainty.
c. Addresses the estimation uncertainty, including selecting a point estimate and related disclosures for inclusion in the financial statements. (Ref: Para. A46–A49)	The auditor determined that management developed a range of possible measurement outcomes for the value in use of the assets using a DCF model. Management selected a point estimate that was at the mid-point of this range, based on its knowledge of the business, its industry and relevant markets. In addition to disclosures to meet the requirements of IAS 36, management also developed disclosures that describe key sources of estimation uncertainty and include the range of possible outcomes and the assumptions used in developing that range, specific information about the significance of the estimate to the entity's financial position and performance and other qualitative and quantitative disclosures regarding the exposure to and management of related risks.

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
(i) Control activities relevant to the audit over management's process for making accounting estimates as described in paragraph 13(h)(ii). (Ref: Para. A50–A54)	The auditor determined that management designed and implemented a number of controls relevant to this accounting estimate, including the following controls: • Management performs a quarterly review of property, plant and equipment to assess for possible indicators of impairment. • Management reviews and approves estimates related to the recoverable amount of property, plant and equipment used to manufacture consumer cameras, including judgments over selection of appropriate methods, assumptions and data. • Management compares revenue forecasts with actual results and investigates variances. The auditor obtained an understanding of the nature of these control activities, evaluated the design effectiveness of the controls and determined whether the controls have been implemented during the period, as required by ISA 315 (Revised).
(j) How management reviews the outcome(s) of previous accounting estimates and responds to the results of that review.	The auditor determined that management reviews the outcome of its previous estimates of recoverable amount by reviewing the realization / outcome of the assumptions applied in its DCF model for measuring the value in use on which cash flow projections are based. The auditor noted that management considers making adjustments to its process if significant variances are identified.
14. The auditor shall review the outcome of previous accounting estimates, or, where applicable, their subsequent re-estimation to assist in identifying and assessing the risks of material misstatement in the current period. The auditor shall take into account the characteristics of the accounting estimates in determining the nature and extent of that review. The review is not intended to call into question judgments about previous period accounting estimates that were appropriate based	The auditor performed a retrospective review of management's estimate of the recoverable amount at the previous period-end, reviewing the realization / outcome of the significant assumptions on which cash flow projections at the previous period-end were based, including comparing the significant assumptions used in management's current DCF model to those used at the prior year-end and investigating any significant changes in assumptions. In performing this retrospective review, the auditor considered whether there were any indicators of management bias in the prior period estimate.

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on the information available at the time they were made. (Ref: Para. A55–A60)	No significant variations in assumptions were noted, nor indicators of bias identified. Management's previous estimates were found to be reasonable.
15. With respect to accounting estimates, the auditor shall determine whether the engagement team requires specialized skills or knowledge to perform the risk assessment procedures, to identify and assess the risks of material misstatement, to design and perform audit procedures to respond to those risks, or to evaluate the audit evidence obtained. (Ref: Para. A61–A63)	The auditor determined that it was necessary to involve the firm's valuation specialists in evaluating the discount rate used by management in the DCF model including through comparison to industry data points.
Identifying and Assessing the Risks of Material Misstatement	
16. In identifying and assessing the risks of material misstatement relating to an accounting estimate and related disclosures at the assertion level, as required by ISA 315 (Revised),[23] the auditor shall separately assess inherent risk and control risk. The auditor shall take the following into account in identifying the risks of material misstatement and in assessing inherent risk: (Ref: Para. A64–A71) (a) The degree to which the accounting estimate is subject to estimation uncertainty; and (Ref: Para. A72–A75)	The auditor assessed that the risk of material misstatement of the valuation of the provision is moderate, taking into account the auditor's assessments of the matters covered by paragraphs 16(a)–(b). The auditor assessed control risk to be low as the entity's controls are well designed and expected to address the risk of material misstatement based on previous testing and an evaluation of changes made during the year. The auditor assessed the **estimation uncertainty** associated with the accounting estimate to be **high**, as the estimated recoverable amount depends on cash flow forecasts over a long period, with a range of potential outcomes, and is therefore difficult to measure with a high degree of precision.
(b) The degree to which the following are affected by complexity, subjectivity, or other inherent risk factors: (Ref: Para. A76–A79)	In terms of complexity, subjectivity and other inherent risk factors, the auditor's considerations were as follows:

[23] ISA 315 (Revised), paragraphs 25 and 26

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
(i) The selection and application of the method, assumptions and data in making the accounting estimate; or (ii) The selection of management's point estimate and related disclosures for inclusion in the financial statements.	With respect to the selection of the method, assumptions and data: • The level of **complexity** was assessed as **high** as management's DCF calculations include numerous judgmental assumptions and use complex modelling (complex method). • The level of **subjectivity** was assessed as **high** because, owing to the high level of estimation uncertainty, management needs to exercise significant judgment in measuring the estimated recoverable amount. In particular, there is a high degree of judgment in selecting appropriate revenue forecasts and in developing an appropriate discount rate for use in the cash flow calculation. • **Other inherent risk factors** were assessed. The high level of subjectivity in assumptions underlying the revenue projection makes the recoverable amount highly susceptible to management bias, meaning the risk of management bias is assessed as **high**. Susceptibility to misstatement due to fraud was assessed as **low** as the auditor did not identify specific fraud risk factors relating to this estimate. The effect of change was assessed as **moderate**, as there was risk introduced to the estimate by changes in the entity's products and markets that led to a need for management to make changes to its assumptions in the DCF model. There were no other significant changes in the financial reporting framework or the nature of the financial statement line item leading to a need for changes in the estimate. With respect to the selection of management's point estimate and related disclosures for inclusion in the financial statements: • The auditor assessed that the selection of the point estimate and disclosures to be made, in accordance with the requirements of IAS 36, are explicit and non-complex. As such, the auditor determined that the degree to which selection of management's point estimate and related disclosures was affected by inherent risk factors was **low**.

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
17. The auditor shall determine whether any of the risks of material misstatement identified and assessed in accordance with paragraph 16 are, in the auditor's judgment, a significant risk.[24] If the auditor has determined that a significant risk exists, the auditor shall obtain an understanding of the entity's controls, including control activities, relevant to that risk.[25] (Ref: Para. A80)	The auditor assessed that there is a **significant risk** of material misstatement in the valuation of property, plant and equipment, relating to the determination of the recoverable amount of assets used to manufacture cameras. This was due to the auditor's assessment of estimation uncertainty, subjectivity, complexity and susceptibility to management bias as high, which increases the likelihood of misstatement. In addition, the carrying value of property, plant and equipment is five times materiality such that a material misstatement is reasonably possible. As noted above in response to the requirement of paragraph 13(i), the auditor understood and evaluated the controls implemented by the entity in response to the risk of misstatement related to the recoverable amount.
Responses to the Assessed Risks of Material Misstatement	
18. As required by ISA 330,[26] the auditor's further audit procedures shall be responsive to the assessed risks of material misstatement at the assertion level,[27] considering the reasons for the assessment given to those risks. The auditor's further audit procedures shall include one or more of the following approaches: (a) Obtaining audit evidence from events occurring up to the date of the auditor's report (see paragraph 21);	The auditor determined that the further audit procedures to respond to the assessed risks of material misstatement should include testing management's process for making the estimate by performing tests of details. The auditor's decision to select this approach was based on a number of factors including: • Evidence from events occurring up to the date of the auditor's report is not expected to provide sufficient appropriate audit evidence for this estimate; • The auditor's review of the DCF used by the entity for purposes of this estimate in prior periods suggests that management's process is appropriate;

24 ISA 315 (Revised), paragraph 27

25 ISA 315 (Revised), paragraph 29

26 ISA 330, paragraphs 6–15 and 18

27 ISA 330, paragraphs 6–7 and 21

Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
(b) Testing how management made the accounting estimate (see paragraphs 22–27); or (c) Developing an auditor's point estimate or range (see paragraphs 28–29). The auditor's further audit procedures shall take into account that the higher the assessed risk of material misstatement, the more persuasive the audit evidence needs to be.[28] The auditor shall design and perform further audit procedures in a manner that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory. (Ref: Para. A81–A84)	• The applicable financial reporting framework specifies how management is expected to make the accounting estimate; and • The approach is expected to be more effective / practicable than developing an auditor's independent point estimate or range. In designing testing procedures to be performed, the auditor took into account the higher level of subjectivity and susceptibility to management bias determined to be associated with the significant assumptions used in making the estimate of recoverable amount.
19. As required by ISA 330,[29] the auditor shall design and perform tests to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls, if: (a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively, or (b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.	The auditor's response was based on an expectation of being able to obtain evidence from testing the operating effectiveness of controls. Regarding management's review control (Control title – *"Management reviews and approves estimates related to the recoverable amount of property, plant and equipment used to manufacture consumer cameras, including judgments over selection of appropriate methods, assumptions and data"*), the auditor anticipated that this would reduce the level of substantive testing necessary over the judgments taken in selecting relevant sources of data to develop significant assumptions, which is one of the principal objectives of management's review control. The auditor determined that testing of another relevant control activity (Control title – "*Property, plant and equipment accounts are reviewed for possible impairment*") would not be efficient as the auditor expects to be able to obtain sufficient evidence over the

28 ISA 330, paragraph 7(b)

29 ISA 330, paragraph 8

	Selection of ISA 540 (Revised) Requirements[18]	Auditor's Understanding and Approach[19]
	In relation to accounting estimates, the auditor's tests of such controls shall be responsive to the reasons for the assessment given to the risks of material misstatement. In designing and performing tests of controls, the auditor shall obtain more persuasive audit evidence the greater the reliance the auditor places on the effectiveness of a control.[30] (Ref: Para. A85-A89)	valuation assertion by performing substantive procedures. As a result, the operating effectiveness of this control was not tested by the auditor.
20.	For a significant risk relating to an accounting estimate, the auditor's further audit procedures shall include tests of controls in the current period if the auditor plans to rely on those controls. When the approach to a significant risk consists only of substantive procedures, those procedures shall include tests of details.[31] (Ref: Para. A90)	As noted above, the operating effectiveness of a single control was tested by the auditor during the period, but the auditor also performed tests of details when testing how management made the accounting estimate. No exceptions were noted with respect to the operating effectiveness of the control throughout the period.

[30] ISA 330, paragraph 9

[31] ISA 330, paragraphs 15 and 21

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Testing How Management Made the Accounting Estimate 22. When testing how management made the accounting estimate, the auditor's further audit procedures shall include procedures, designed and performed in accordance with paragraphs 23–26, to obtain sufficient appropriate audit evidence regarding the risks of material misstatement relating to: (Ref: Para. A94) (a) The selection and application of the methods, significant assumptions and the data used by management in making the accounting estimate; and (b) How management selected the point estimate and developed related disclosures about estimation uncertainty.	See responses to requirements in paragraphs 23–25 below.
Methods 23. In applying the requirements of paragraph 22, with respect to methods, the auditor's further audit procedures shall address: (a) Whether the method selected is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from the method used in prior periods are appropriate; (Ref: Para. A95, A97)	The auditor performed a detailed evaluation of the DCF model used to estimate value in use to determine that the model was selected, designed and applied in accordance with the applicable financial reporting framework. The auditor determined that the model had appropriately incorporated the specific requirements of IAS 36 related to DCF models, such as: • Basing cash flow projections on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset and giving greater weight to external evidence. • Limiting the cash flow projections based on most recent financial budgets / forecasts approved by management (excluding impact of matters such as

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	restructuring or improving or enhancing the assets' performance) to a maximum of five years. • Using extrapolated forecast revenues that do not exceed the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market in which the asset is used, unless a higher rate can be justified, and extrapolating cash flows over a future period that does not exceed the useful life of the assets. • Developing future cash flow estimates that include: ○ Projections of cash inflows from the continuing use of the assets; ○ Projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and ○ Net cash flows, if any, to be received (or paid) for the disposal of the asset at the end of its useful life. • Excluding cash flows that relate to financing activities or income tax receipts or payments. • Incorporating discount rates that are pre-tax rate and that reflect(s) current market assessments of: ○ The time value of money; and ○ The risks specific to the asset for which the future cash flow estimates have not been adjusted. The auditor compared management's DCF model to the model prepared by management in the prior year and observed that management made changes to assumptions used in the DCF model but did not change the method used. Upon further investigation this was

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	deemed to be appropriate, and the auditor determined that the method used by management to make the accounting estimate was appropriate in the context of the financial reporting framework.
(b) Whether judgments made in selecting the method give rise to indicators of possible management bias; (Ref: Para. A96)	Based on the work performed in paragraph 23(a), the auditor did not identify any judgments made by management in selecting the method that gave rise to indicators of possible management bias.
(c) Whether the calculations are applied in accordance with the method and are mathematically accurate;	The auditor determined that the model calculations were mathematically accurate by checking and verifying the formulae used in the spreadsheet used to apply management's method.
(d) When management's application of the method involves complex modelling, whether judgments have been applied consistently and whether, when applicable: (Ref: Para. A98– A100) (i) The design of the model meets the measurement objective of the applicable financial reporting framework, is appropriate in the circumstances, and, if applicable, changes from the prior period's model are appropriate in the circumstances; and (ii) Adjustments to the output of the model are consistent with the measurement objective of the applicable financial reporting framework and are appropriate in the circumstances; and	The auditor determined that the model used to apply management's method was complex due principally to the fact that it can be difficult to maintain the integrity (e.g., accuracy, consistency, or completeness) of the data and assumptions in using the model due to multiple valuation attributes (i.e., the range of assumptions used in the DCF model), multiple relationships between them and multiple iterations of the calculation. For example, the model incorporates cash flows arising from multiple camera products and revenue projections relating to sales across different markets and geographies in a number of different currencies. The auditor evaluated the design of the model and determined that it met the measurement objective of the applicable financial reporting framework and was appropriate as a means of calculating the recoverable amount. This included substantive testing over the completeness and accuracy of significant assumptions and data used in the model. The auditor determined that assumptions, and judgments thereon, were being applied consistently. The auditor determined, through inquiry of management and inspection of current period model documentation and calculations, that management made no adjustments to the output of the model, which was deemed appropriate.

<table>
<tr><th>Selection of ISA 540 (Revised) Requirements[18]</th><th>Auditor's Understanding and Approach[19]</th></tr>
<tr><td>(e) Whether the integrity of the significant assumptions and the data has been maintained in applying the method. (Ref: Para. A101)</td><td>The auditor assessed whether the integrity of the significant assumptions and data had been maintained by management in applying its method to determine the value in use of the property, plant and equipment. The auditor performed this assessment through detailed testing of the model, including testing that data and assumptions had been transferred completely and accurately through each stage of the estimation process, noting no issues.</td></tr>
<tr><td>Significant Assumptions

24. In applying the requirements of paragraph 22, with respect to significant assumptions, the auditor's further audit procedures shall address:

(a) Whether the significant assumptions are appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate; (Ref: Para. A95, A102–A103)</td><td>In addition to inquiry and sensitivity analysis, the auditor performed tests of details over revenue forecasts, projected operating margins, capital expenditures, working capital requirements and the discount rate to obtain sufficient appropriate audit evidence as to whether the significant assumptions underlying the DCF models were appropriate in the context of IAS 36. The auditor's procedures included the following:

<table><tr><th>Significant assumption</th><th>Procedures performed</th></tr><tr><td>Revenue forecasts</td><td>● Given the high level of subjectivity around this assumption and the high susceptibility to management bias, the auditor focused on management's rationale for selecting the revenue forecasts used in the model. This included challenging management as to why the selected rate was more appropriate than available alternatives and considering whether the selection of the assumption was consistent with (or whether it should not have been consistent with) previous periods, publicly available market data from reliable sources and</td></tr></table></td></tr>
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		similar assumptions used in other estimates. ● Analyzed actual historical movements in revenue and whether these remain a good indicator of likely future revenues, given the significant market-related changes and the industry-wide decline in consumer camera sales. ● Evaluated whether the entity's forecasts are in line with industry or market data and trade publications and the reliability of this evidence by taking into account the reliability and reputation of the source of the data. ● Evaluated the accuracy of management's past forecasts.
	Projected operating margins	● Compared projected operating margins to historical results, prior forecasts and industry / market data and evaluated whether the actual historical margin remains a good indicator of the likely future margin rate, given the significant market-related changes, the industry-wide decline in consumer camera sales and the resulting implications for operating margins.

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		• Considered whether cost forecasts appropriately reflect the impacts of contractual rate increases from leases, vendor or employment agreements, or other contracts.
	Capital expenditure (considered necessary for continued use of the assets)	• The auditor identified that the entity's future business plans are predicated on the introduction of a new product. Management intends to manufacture the new product using its existing plant, investing in the capital improvements necessary to ensure the plant can be used to manufacture the new product and thereby continue to produce volumes at a level commensurate with current capacity. • The auditor evaluated whether projected capital expenditures included in the model were at reasonable levels for the improvement and continued maintenance of the existing plant, and whether projected revenue volumes reflected current capacity.
	Working capital requirements	• The auditor evaluated the level of increase in net working capital and found it to be

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		consistent with the projected increase in revenue and margins.
	Discount rate	• Given the high level of subjectivity inherent in determining the discount rate, and its high susceptibility to management bias, the auditor focused on judgments made by management in the development and selection of an appropriate discount rate, in particular the selection of an appropriate beta for calculation of the cost of equity. • The auditor assessed whether selections made were consistent with prior periods and other assumptions made by management, and challenged management to justify that key inputs selected were more appropriate than available alternatives. • The auditor also compared the discount rate with the rate used by unrelated entities in the same industry and determined that the discount rate is pre-tax and reflects current market assessments of the time value of money and any risks specific to the asset not already adjusted for in the forecasted cash flows.

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	In addition to these procedures, the auditor reviewed the results memorandum prepared by the firm's valuation specialist with respect to the discount rate (see paragraph 15), evaluating the relevance and reasonableness of the specialist's findings, performed follow-up actions required on outstanding issues raised by the specialist and determined that final versions of the agreed deliverables (e.g., memoranda and any supporting schedules prepared by specialists) were included within the audit workpapers. In performing the procedures above, the auditor identified that management's selection of revenue forecast assumptions appeared optimistic when compared to published industry forecast data. The auditor determined that, on the basis of procedures performed, the other significant assumptions were appropriate in the context of the financial reporting framework. *[Note: The auditor's response with respect to the revenue forecast assumption is addressed later in this example.]*
(b) Whether judgments made in selecting the significant assumptions give rise to indicators of possible management bias; (Ref: Para. A96)	Having performed procedures over management's selection of significant assumptions, in particular challenging the appropriateness of the discount rate and revenue forecasts used in the DCF model, the auditor identified an indicator of possible management bias in management's selection of revenue forecast assumptions, which appeared optimistic when compared to published industry forecast data. The auditor did not identify any other indicators of possible management bias. *[Note: The auditor's response to this indicator of possible management bias is addressed later in this example.]*
(c) Whether the significant assumptions are consistent with each other and with those used in other accounting estimates, or with related assumptions used in other areas of the entity's business	In addition to the auditor's procedures in response to paragraph 24(a) above, the auditor assessed whether the revenue forecast assumptions and projected operating margins in the DCF model were consistent with each other, given the direct relationship between these assumptions.

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activities, based on the auditor's knowledge obtained in the audit; and (Ref: Para. A104)	The auditor also compared assumptions used in the model to approved budgets and other approved forecasts, including those prepared by management as part of its going concern assessment. On the basis of these procedures, and other procedures addressing the other significant assumptions, the auditor determined that management's significant assumptions were consistent with other significant assumptions used in the estimate of recoverable amount, and assumptions used in other accounting estimates.
(d) When applicable, whether management has the intent to carry out specific courses of action and has the ability to do so. (Ref: Para. A105)	The auditor identified that the entity's revenue projection incorporated into management's DCF included cash flows from the introduction of a new lower cost, high quality camera which it plans to manufacture using the existing camera production facility. The new camera is still in a research and development phase with introduction planned for 18 months after the current year-end. The auditor determined that management had the intent and ability to deliver the new product through performance of the following procedures: • Review of management's historical success with developing and introducing new cameras and the timeline for doing so. • Interview of the lead research and development and manufacturing executives to assess their views of the assumptions about the expected introduction date and whether use of the existing manufacturing facility would require any significant modifications. • Inspection of written plans and other documentation, including, when applicable, formally approved budgets, authorizations or minutes. • Inquiry of management about its reasons for manufacturing the new product using existing machinery and equipment, rather than investing in new machinery and equipment.

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	• Consideration of events occurring subsequent to the date of the financial statements and up to the date of the auditor's report, including whether management's research and development of the new product has remained on schedule and whether management has made the level of investment in capital equipment projected in the DCF model.
Data 25. In applying the requirements of paragraph 22, with respect to data, the auditor's further audit procedures shall address: (a) Whether the data is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate (Ref: Para. A95, A106);	The auditor performed tests of details over the data used, agreeing it to appropriate supporting documentation and determined that the data used in the model was appropriate in the context of the applicable financial reporting framework, was relevant and reliable and that changes in the data used from the prior period were appropriate. The data tested included, among others: • Historical cash flows, including historical revenues and operating margins. • Historical asset book values. • Risk-free interest rates used in the development of the discount rate assumptions. • Contractual terms. • Independent external data (e.g., market or industry metrics) relevant to management's assumptions. On the basis of these procedures, the auditor determined that data used in making the accounting estimate was appropriate in the context of the financial reporting framework.
(b) Whether judgments made in selecting the data give rise to indicators of possible management bias; (Ref: Para. A96)	The auditor did not identify any judgments made by management in selecting the data that indicated possible management bias.
(c) Whether the data is relevant and reliable in the circumstances; and (Ref: Para. A107)	See procedures performed by the auditor with respect to paragraph 25(a) above which covered consideration of whether the data used was relevant and reliable in the circumstances.

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(d) Whether the data has been appropriately understood or interpreted by management, including with respect to contractual terms. (Ref: Para. A108)	Based on the procedures performed in paragraph 25(a), the auditor determined that the data used had been appropriately understood and interpreted by management, including with respect to contractual terms.
Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty 26. In applying the requirements of paragraph 22, the auditor's further audit procedures shall address whether, in the context of the applicable financial reporting framework, management has taken appropriate steps to: (a) Understand estimation uncertainty; and (Ref: Para. A109) (b) Address estimation uncertainty by selecting an appropriate point estimate and by developing related disclosures about estimation uncertainty. (Ref: Para. A110–A114)	Based on the testing performed over methods, significant assumptions and data, the auditor determined that management had taken appropriate steps to understand and address estimation uncertainty. As management included specific financial statement disclosures describing the estimation uncertainty associated with its impairment evaluation process (e.g., disclosure of the range of possible outcomes and the assumptions used in determining the range), the auditor also evaluated that the disclosures demonstrated that management had appropriately understood, and that the disclosures adequately described, the estimation uncertainty. The auditor determined that, although management possessed an understanding of the estimation uncertainty associated with the accounting estimate, a concern was identified with one of the significant assumptions selected and applied by management in developing its point estimate of the recoverable amount. The specific concern related to an element of the revenue forecasts assumptions selected by management which appeared optimistic when compared to published industry forecast data and the recent financial performance of the entity.
27. When, in the auditor's judgment based on the audit evidence obtained, management has not taken appropriate steps to understand or address estimation uncertainty, the auditor shall: (Ref: Para. A115–A117) (a) Request management to perform additional procedures to understand estimation uncertainty or to address it by reconsidering the selection of management's point estimate or considering	As a concern was identified by the auditor related to a specific significant assumption selected and applied by management in developing its point estimate of the recoverable amount, the auditor requested that management perform additional procedures to re-evaluate the appropriateness of the assumptions used in the DCF model, including requesting that management provide additional rationale and supporting documentation to address the apparent misalignment of the revenue forecast with other available audit evidence.

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providing additional disclosures relating to the estimation uncertainty, and evaluate management's response(s) in accordance with paragraph 26;	Management agreed to perform the additional procedures and subsequently concluded that it agreed with the concerns raised by the auditor and consequently applied a more conservative revenue forecasts assumption to its model that was aligned with published industry forecast data and the recent financial performance of the entity. This resulted in a material change in the estimated recoverable amount applied in management's impairment assessment. The revised impairment assessment resulted in a material increase in the entity's previously recognized impairment provision which was corrected by management.
(b) If the auditor determines that management's response to the auditor's request does not sufficiently address estimation uncertainty, to the extent practicable, develop an auditor's point estimate or range in accordance with paragraphs 28–29; and	The auditor determined that management's response to the auditor's request sufficiently addressed the associated estimation uncertainty and, as a result, it was not considered necessary to develop an auditor's point estimate or range.
(c) Evaluate whether a deficiency in internal control exists and, if so, communicate in accordance with ISA 265.[32]	The auditor concluded that the selection of an inappropriate revenue growth rate was indicative of a control deficiency and, on the basis that the matter led to a material adjustment to the financial statements, considered it to be a significant deficiency in management's review control which is to be communicated to those charged with governance on a timely basis. *[Note: The auditor's response to this significant deficiency is addressed later in this example.]*
Other Considerations Relating to Audit Evidence 30. In obtaining audit evidence regarding the risks of material misstatement relating to accounting estimates,	The auditor gave careful consideration to the sources of information used as audit evidence when auditing the recoverable amount estimate. In preparing its DCF assumptions, management had obtained data concerning relevant industry metrics from a

32 ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

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irrespective of the sources of information to be used as audit evidence, the auditor shall comply with the relevant requirements in ISA 500. When using the work of a management's expert, the requirements in paragraphs 21–29 of this ISA may assist the auditor in evaluating the appropriateness of the expert's work as audit evidence for a relevant assertion in accordance with paragraph 8(c) of ISA 500. In evaluating the work of the management's expert, the nature, timing and extent of the further audit procedures are affected by the auditor's evaluation of the expert's competence, capabilities and objectivity, the auditor's understanding of the nature of the work performed by the expert, and the auditor's familiarity with the expert's field of expertise. (Ref: Para. A126–A132)	reputable third-party source specializing in analysis of the industry. The auditor compared this data with information from an alternative independent source specializing in similar industry analysis, in order to assess its reliability. The auditor determined that data from the alternative source was consistent with that used by management. The auditor also performed additional procedures over the reliability (e.g., completeness and accuracy) of information used by the entity in preparing the DCF model. Management did not use the work of any management experts in making the recoverable amount estimate.
Disclosures Related to Accounting Estimates	
31. The auditor shall design and perform further audit procedures to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement at the assertion level for disclosures related to an accounting estimate, other than those related to estimation uncertainty addressed in paragraphs 26(b) and 29(b).	The auditor performed tests of details over the disclosures related to impairment required by the applicable financial reporting framework, including the following procedures: • Testing that the recoverable amount of each asset or cash-generating unit for which an impairment loss was recognized or reversed during the period had been disclosed; • Testing that each recoverable amount disclosed is the higher of the related asset's fair value less costs of disposal and its value in use; and • Agreeing the disclosures to appropriate supporting documentation.

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Indicators of Possible Management Bias	
32. The auditor shall evaluate whether judgments and decisions made by management in making the accounting estimates included in the financial statements, even if they are individually reasonable, are indicators of possible management bias. When indicators of possible management bias are identified, the auditor shall evaluate the implications for the audit. Where there is intention to mislead, management bias is fraudulent in nature. (Ref: Para. A133–A136)	The auditor performed an evaluation of the judgments and decisions made by management in making the recoverable amount estimate and other estimates made in preparing the financial statements. The auditor identified that management's selection of revenue forecasts appeared optimistic, and this indicated possible management bias. The auditor evaluated the reason for this selection and determined that it was due to the release of an updated market report subsequent to management's selection of assumptions that indicated a higher rate of decline for the market. Based on this evaluation and acknowledging management's openness to revising the selection estimate when challenged, the auditor concluded that this was not an instance of management bias nor was there an intention to mislead. As such, this was not deemed to be an indication of an increased risk of fraud. While management's revision of the selection of a revenue forecast assumption addressed the auditor's concerns for the purposes of this estimate, the auditor also considered whether other fair value estimates prepared by management contained optimistic assumptions and did not identify any other unduly optimistic assumptions indicating possible management bias.
Overall Evaluation Based on Audit Procedures Performed	
33. In applying ISA 330 to accounting estimates,[33] the auditor shall evaluate, based on the audit procedures performed and audit evidence obtained, whether: (Ref: Para. A137–A138) (a) The assessments of the risks of material misstatement at the assertion level remain	The auditor reflected on the audit procedures performed and the audit evidence obtained in respect of management's estimate of the recoverable amount of property, plant and equipment at the period-end. Management's selection of revenue forecasts was deemed to be indicative of a deficiency in the review control upon which the auditor sought to place reliance through testing its operating effectiveness. As such, the auditor considered the impact of this on the audit plan and concluded that no reliance could be placed on the

[33] ISA 330, paragraphs 25–26

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appropriate, including when indicators of possible management bias have been identified; (b) Management's decisions relating to the recognition, measurement, presentation and disclosure of these accounting estimates in the financial statements are in accordance with the applicable financial reporting framework; and (c) Sufficient appropriate audit evidence has been obtained.	review control, and a higher level of substantive evidence was necessary. This was obtained through the auditor's additional audit procedures over the revised revenue forecast assumptions selected by management and the evidence the auditor obtained over the revised assumptions. The auditor's assessment of inherent risk (namely that there was a significant risk of material misstatement, and high levels of subjectivity and susceptibility to management bias) remained unchanged. The auditor also considered the impact of this significant deficiency on the audit plan by evaluating its impact in other areas of management's process (including the identification and selection of methods, significant assumptions and data), as well as any other review controls relied upon in the audit. The auditor planned to obtain evidence from the control over judgments taken in selection of data sources to develop significant assumptions. Given that this evidence could not be obtained from reliance on the review control, the auditor performed additional substantive procedures over management's selection of data sources relevant to the revenue forecast, including evaluating whether they were consistent with judgments made in prior periods and in other estimates. After revision of the assumption by management, the auditor was satisfied with management's decisions regarding recognition, measurement, presentation and disclosure, and that sufficient appropriate audit evidence had been obtained.
34. In making the evaluation required by paragraph 33(c), the auditor shall take into account all relevant audit evidence obtained, whether corroborative or contradictory.[34] If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall evaluate the implications for the audit or the auditor's opinion on the	In performing the evaluation above, the auditor took into account all relevant evidence obtained. In addition to the corroborative evidence obtained, specific consideration was given to whether any potentially contradictory audit evidence had been identified. The auditor determined that management's original selection of a revenue forecast was inconsistent with the latest available published market data. Management's revision of its selected revenue forecast assumptions, at the request of the auditor, was deemed to appropriately resolve this matter. The auditor identified no other evidence that

[34] ISA 500, paragraph 11

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financial statements in accordance with ISA 705 (Revised).[35]	contradicted the audit evidence obtained while assessing management's recoverable amount estimate.
Determining Whether the Accounting Estimates are Reasonable or Misstated 35. The auditor shall determine whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated. ISA 450[36] provides guidance on how the auditor may distinguish misstatements (whether factual, judgmental, or projected) for the auditor's evaluation of the effect of uncorrected misstatements on the financial statements. (Ref: Para. A12–A13, A139–A144)	The auditor determined that, following the recognition of the audit adjustment recognized by management referred to in response to paragraph 27(a) above, management's estimate of recoverable amount was reasonable in the context of the applicable financial reporting framework. In addition, the related disclosures made by management, for example as required by IAS 36 and the estimation uncertainty disclosures made under IAS 1, were considered by the auditor to be reasonable in the context of the applicable financial reporting framework.
36. In relation to accounting estimates, the auditor shall evaluate: (a) In the case of a fair presentation framework, whether management has included disclosures, beyond those specifically required by the framework, that are necessary to achieve the fair presentation of the financial statements as a whole;[37] or	The entity determined that it did not consider it necessary to include any additional disclosures beyond those required by IAS 36 and other relevant standards, such as IAS 1, in order to achieve a fair presentation of the financial statements as a whole. The auditor evaluated and was in agreement with management's conclusions on this matter.

[35] ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

[36] ISA 450, paragraph A6

[37] See also ISA 700 (Revised), paragraph 14.

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(b) In the case of a compliance framework, whether the disclosures are those that are necessary for the financial statements not to be misleading.[38]	This requirement is not applicable as the applicable financial reporting framework is not considered to be a compliance framework.

38 See also ISA 700 (Revised), paragraph 19.

About the IAASB

The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

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