November 25, 2020

Via e-mail: CommentLetters@aicpa-cima.com

Auditing Standards Board
American Institute of Certified Public Accountants
1345 Avenue of the Americas, 27th Floor
New York, NY 10105

Re: Proposed Statement on Auditing Standards Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement

To the Auditing Standards Board:

BDO USA, LLP ("our" or "we") appreciates the opportunity to provide our comments on the Auditing Standards Board’s ("ASB" or the "Board") proposed Statement on Auditing Standards (SAS), Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement ("proposed SAS").

We support of the ASB’s overall strategy to converge its standards with those of the International Auditing and Assurance Standards Board (IAASB), particularly in regard to its risk assessment standard, which is foundational to the audit.

Our comments with respect to the specific questions posed in the exposure draft are set out below.

1. Are the requirements and application material of the proposed SAS sufficiently scalable, that is, is the proposed SAS capable of being applied to the audits of entities with a wide range of sizes, complexities, and circumstances?

   Yes, we believe that the requirements and the application material of the proposed SAS are capable of being proportionately applied to entities with a wide range of sizes, complexities and circumstances.

   Specifically, we find the presentation of the "what" in the requirements paragraphs from the "why" and "how" in the application material paragraphs to be helpful in focusing a reader’s attention on the requirements first, followed by the application material, which includes a separately highlighted scalability paragraph, where appropriate.

   We also appreciate the added emphasis on complexity of an entity over size. We agree that while the size of entity may be indicative of its complexity, many smaller entities may be more complex than larger entities.
2. Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks of material misstatement? Specifically:

a. Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?

   Yes, we believe the requirements have been appropriately enhanced and clarified.

b. Have the requirements related to the auditor’s identification of controls that address the risks of material misstatement been appropriately enhanced and clarified? Is it clear how controls that addressed the risks of material misstatement are identified, particularly for audits of smaller and less complex entities?

   Yes, we believe the requirements have been appropriately enhanced and clarified.

c. Given that COSO’s 2013 Internal Control—Integrated Framework (COSO framework) is often used by entities subject to the AICPA’s generally accepted auditing standards, is the terminology in paragraphs 21–27 and related application material of the proposed SAS clear and capable of consistent interpretation for audits of entities that use the COSO framework?

   Yes, the terminology used is sufficiently clear.

3. Are the enhanced requirements and application material related to the auditor’s understanding of the IT environment, the identification of the risks arising from the entity’s use of IT, and the identification of general IT controls clear to support the auditor’s consideration of the effects of the entity’s use of IT on the identification and assessment of the risks of material misstatement?

   Yes, we find the requirements and application material to be sufficiently clear. We are supportive of the enhanced requirements and related application material relating to obtaining and understanding of the IT environment and the requirements to identify and assess risks arising from the use of IT related to the IT applications and other aspects of the IT environment. We believe that these elements are essential to the risk assessment process due to the significant role of IT in most audits.
4. Do you support the introduction in the proposed SAS of the new concepts and related definitions of significant classes of transactions, account balances, and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (that is, that an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion), and how they assist the auditor in identifying where risks of material misstatement exist?

Yes, we are supportive of the new concepts and related definitions of significant classes of transactions, account balances and disclosures and their relevant assertions and believe they assist the auditor in identifying where the risks of material misstatement exist. We find the guidance on this topic to be sufficient and clear in the proposed SAS.

5. Do you support the introduction of the spectrum of inherent risk into the proposed SAS?

We are supportive of the introduction of the concept of spectrum of inherent risk into the proposed SAS. In particular, we believe that the spectrum of inherent risk is a helpful concept in recognizing that ‘inherent risk is higher for some assertions and related classes of transactions, account balances and disclosures than for others’, and that the spectrum will assist auditors in making their assessments of inherent risk. Additionally, the spectrum of risk concept supports the concept of scalability in the auditor’s risk assessment and designed audit response.

6. Do you support the separate assessments of inherent and control risk in relation to all risks of material misstatement at the assertion level?

Yes, we support the separate assessments of inherent and control risk in relation to all risks of material misstatement.

7. What are your views regarding the clarity of the requirement to assess the control risk, in particular, when the auditor does not plan to test the operating effectiveness of controls?

We find the requirement in paragraph 34 and the related application material with respect to assessing control risk to be sufficiently clear in the proposed SAS.

8. What are your views regarding the clarity of the requirement in paragraph 26d of the proposed SAS to evaluate design and determine implementation of certain control activities (including, specifically, the requirement related to controls over journal entries)?

We find the requirements in paragraph 26d of the proposed SAS to be sufficiently clear. Particularly, the application material in paragraph A175 is helpful in
highlighting the possible controls over journal entries that may affect the routine processing of transactions in the entity’s information system for significant classes of transactions account balances and disclosures from controls over non-standard journal entries relevant to adjustments to significant classes of transactions, account balances, and disclosures.

9. **Do you support the revised definition, and related material, on the determination of significant risks? What are your views on the matters previously presented relating to how significant risks are determined based on the spectrum of inherent risk?**

   Yes, we are supportive of the revised definition, and related material, on the determination of significant risks. In particular, we find the revised definition of significant risks and its linkage to both the concept of spectrum of inherent risk and the related assessment of likelihood of occurrence and magnitude of possible misstatement to be helpful, especially in comparison to the current definition, which focuses on the auditor’s response to the risk as opposed to the assessment of the risk itself.

10. **What are your views about the proposed stand-back requirement in paragraph 36 of the proposed SAS and the conforming amendments proposed to paragraph .18 of AU-C section 330?**

    We are supportive of the proposed stand-back requirements in paragraph 36 of the proposed SAS and the conforming amendments proposed to paragraph .18 of AU-C section 330.

    In particular, we are in favor of the proposed amendments to paragraph .18 of AU-C Section 330, which requires the auditor to perform substantive procedures for each relevant assertion of each significant class of transactions. We find the Board’s conforming amendments to paragraph .18 of AU-C 330 to be more intuitive and aligned with the proposed SAS in comparison to the corresponding conforming amendments made by the IAASB to paragraph 18 of ISA 330 in conjunction with its revisions to ISA 315 Revised, which, irrespective of the assessed risks of material misstatement, requires the auditor to perform substantive procedures for each material class of transaction, account balance, and disclosure.

11. **What are your views with respect to the clarity and appropriateness of the documentation requirements?**

    In general, the documentation requirements are clear; however, we continue to evaluate how best to provide practical application guidance to engagement teams that is scalable to audits of smaller and less complex entities. We encourage the ASB to develop further implementation guidance in the form of examples or case studies in this area to further illustrate the scalability considerations.
For example, paragraph A21 in the application material describes situations where entities may establish processes and systems with limited documentation or a lack of consistency in how they are undertaken. When such systems and processes lack formality, the auditor may still be able to perform risk assessment procedures through observation and inquiry. We welcome more detailed examples to demonstrate (a) the nature and extent of audit evidence that would be appropriate to demonstrate the auditor’s direct observation of specific procedures, and (b) the extent of audit documentation that would be appropriate support the auditor’s basis for the identification and assessment of risks of material misstatement.

We appreciate the opportunity to comment on this proposed SAS. Please contact Phillip Austin (312) 259-0357 or Ashwin Chandran (214) 689-5667 for any inquiries or questions regarding our submission.

Sincerely,

/s/ BDO USA, LLP