

AU-C Section 450

Evaluation of Misstatements Identified During the Audit

Source: SAS No. 122; SAS No. 134; SAS No. 135; SAS No. 136; SAS No. 137; SAS No. 138.

Effective for audits of financial statements for periods ending on or after December 15, 2012, unless otherwise indicated.

Introduction

Scope of This Section

.01 This section addresses the auditor's responsibility to evaluate the effect of identified misstatements on the audit and the effect of uncorrected misstatements, if any, on the financial statements. Section 700, *Forming an Opinion and Reporting on Financial Statements*, and section 703, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*, address the auditor's responsibility in forming an opinion on the financial statements based on the evaluation of the audit evidence obtained. The auditor's conclusion, required by section 700 or section 703, takes into account the auditor's evaluation of uncorrected misstatements, if any, on the financial statements, in accordance with this section. Section 320, *Materiality in Planning and Performing an Audit*, addresses the auditor's responsibility to appropriately apply the concept of materiality in planning and performing an audit of financial statements. [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 136.]

Effective Date

.02 This section is effective for audits of financial statements for periods ending on or after December 15, 2012.

Objective

- .03 The objective of the auditor is to evaluate the effect of
- a. identified misstatements on the audit and
 - b. uncorrected misstatements, if any, on the financial statements.

Definitions

.04 For purposes of generally accepted auditing standards, the following terms have the meanings attributed as follows:

Misstatement. A difference between the reported amount, classification, presentation, or disclosure of a financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be presented fairly in accordance with

the applicable financial reporting framework. Misstatements can arise from fraud or error. (Ref: par. .A1)

Misstatements also include those adjustments of amounts, classifications, presentations, or disclosures that, in the auditor's professional judgment, are necessary for the financial statements to be presented fairly, in all material respects.

Uncorrected misstatements. Misstatements that the auditor has accumulated during the audit and that have not been corrected.

[As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

Requirements

Accumulation of Identified Misstatements

.05 The auditor should accumulate misstatements identified during the audit, other than those that are clearly trivial. (Ref: par. .A2–.A3)

Consideration of Identified Misstatements as the Audit Progresses

.06 The auditor should determine whether the overall audit strategy and audit plan need to be revised if

- a. the nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements may exist that, when aggregated with misstatements accumulated during the audit, could be material or (Ref: par. .A7)
- b. the aggregate of misstatements accumulated during the audit approaches materiality determined in accordance with section 320.¹ (Ref: par. .A8)

Communication and Correction of Misstatements

.07 The auditor should communicate on a timely basis with the appropriate level of management all misstatements accumulated during the audit. The auditor should request management to correct those misstatements. (Ref: par. .A9–.A11)

.08 If, at the auditor's request, management has examined a class of transactions, account balance, or disclosure and corrected misstatements that were detected, the auditor should perform additional audit procedures to determine whether misstatements remain. (Ref: par. .A12–.A14)

.09 If management refuses to correct some or all of the misstatements communicated by the auditor, the auditor should obtain an understanding of management's reasons for not making the corrections and should take that understanding into account when evaluating whether the financial statements as a whole are free from material misstatement.² (Ref: par. .A15–.A18)

¹ Paragraph .10 of section 320, *Materiality in Planning and Performing an Audit*.

² Paragraph .13 of section 700, *Forming an Opinion and Reporting on Financial Statements*, or paragraph .38 of section 703, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*. [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 136.]

Evaluating the Effect of Uncorrected Misstatements

.10 Prior to evaluating the effect of uncorrected misstatements, the auditor should reassess materiality³ to confirm whether it remains appropriate in the context of the entity's actual financial results. (Ref: par. .A19–.A21)

.11 The auditor should determine whether uncorrected misstatements are material, individually or in the aggregate. In making this determination, the auditor should consider

- a. the size and nature of the misstatements, both in relation to particular classes of transactions, account balances, or disclosures and the financial statements as a whole, and the particular circumstances of their occurrence and (Ref: par. .A22–.A29 and .A31–.A32)
- b. the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances, or disclosures and the financial statements as a whole. (Ref: par. .A30)

Documentation

.12 The auditor should include in the audit documentation⁴ (Ref: par. .A33)

- a. the amount below which misstatements would be regarded as clearly trivial; (See paragraph .05)
- b. all misstatements accumulated during the audit and whether they have been corrected; and (See paragraphs .05–.07)
- c. the auditor's conclusion about whether uncorrected misstatements are material, individually or in the aggregate, and the basis for that conclusion. (See paragraph .11)

Application and Other Explanatory Material

Definitions

Misstatement (Ref: par. .04)

.A1 Misstatements may result from fraud or error, such as

- a. an inaccuracy in gathering or processing data from which the financial statements are prepared;
- b. an omission of an amount or disclosure, including inadequate or incomplete disclosures and omission of those disclosures required to meet disclosure objectives of certain financial reporting frameworks as applicable;
- c. a financial statement disclosure that is not presented in accordance with the applicable financial reporting framework;
- d. an incorrect accounting estimate arising from overlooking or clear misinterpretation of facts;

³ Paragraph .12 of section 320.

⁴ Paragraphs .08–.12 and .A8 of section 230, *Audit Documentation*.

- e. judgments of management concerning accounting estimates that the auditor considers unreasonable or the selection or application of accounting policies that the auditor considers inappropriate;
- f. an inappropriate classification, aggregation, or disaggregation of information; and
- g. the omission of a disclosure necessary for the financial statements to achieve fair presentation beyond disclosures specifically required by the framework.

Other examples of misstatements arising from fraud are provided in section 240, *Consideration of Fraud in a Financial Statement Audit*.⁵ [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

Accumulation of Identified Misstatements (Ref: par. .05)

"Clearly Trivial"

.A2 Paragraph .05 requires the auditor to accumulate misstatements identified during the audit other than those that are clearly trivial. "Clearly trivial" is not another expression for "not material." Misstatements that are clearly trivial will be of a wholly different (smaller) order of magnitude, or of a wholly different nature, than those that would be determined to be material and will be misstatements that are clearly inconsequential, whether taken individually or in the aggregate and whether judged by any criteria of size, nature, or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the misstatement is considered not to be clearly trivial. [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

Misstatements in Individual Statements

.A3 The auditor may designate an amount below which misstatements of amounts in the individual statements would be clearly trivial and would not need to be accumulated because the auditor expects that the accumulation of such amounts clearly would not have a material effect on the financial statements. However, misstatements of amounts that are above the designated amount would be accumulated as required by paragraph .05. In addition, misstatements relating to amounts may not be clearly trivial based on their nature or circumstances and, if not clearly trivial, would be accumulated as required by paragraph .05 of this section. [Paragraph added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

Misstatements in Disclosures

.A4 Misstatements in disclosures may also be clearly trivial whether taken individually or in the aggregate and whether judged based on size, nature, or circumstances. Misstatements in disclosures that are not clearly trivial are also accumulated to assist the auditor in evaluating the effect of such misstatements on the relevant disclosures and the financial statements as a whole. Paragraph .A23 provides examples of when misstatements in qualitative disclosures may be material. [Paragraph added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

⁵ Paragraphs .A1–.A8 of section 240, *Consideration of Fraud in a Financial Statement Audit*.

Accumulation of Misstatements

.A5 Misstatements by nature or circumstances, accumulated as described in paragraphs .A3–.A4, cannot be added together as is possible in the case of misstatements of amounts. Nevertheless, the auditor is required by paragraph .11 to evaluate those misstatements individually and in the aggregate (that is, collectively with other misstatements) to determine whether they are material. [Paragraph added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

.A6 To assist the auditor in evaluating the effect of misstatements accumulated during the audit and in communicating misstatements to management and those charged with governance, the auditor may find it useful to distinguish between factual misstatements, judgmental misstatements, and projected misstatements, described as follows:

- *Factual misstatements* are misstatements about which there is no doubt.
- *Judgmental misstatements* are differences arising from the judgments of management including those concerning recognition, measurement, presentation, and disclosure in the financial statements (including the selection or application of accounting policies) that the auditor considers unreasonable or inappropriate.
- *Projected misstatements* are the auditor's best estimate of misstatements in populations, involving the projection of misstatements identified in audit samples to the entire population from which the samples were drawn. Guidance on the determination of projected misstatements and evaluation of the results is set out in section 530, *Audit Sampling*.⁶

[Paragraph renumbered and amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

Consideration of Identified Misstatements as the Audit Progresses (Ref: par. .06)

.A7 A misstatement may not be an isolated occurrence. Evidence that other misstatements may exist include, for example, when the auditor identifies that a misstatement arose from a breakdown in internal control or from inappropriate assumptions or valuation methods that have been widely applied by the entity. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A8 If the aggregate of misstatements accumulated during the audit approaches materiality,⁷ a greater than acceptably low level of risk may exist that possible undetected misstatements, when taken with the aggregate of uncorrected misstatements accumulated during the audit, could exceed materiality. Undetected misstatements could exist because of the presence of sampling risk and nonsampling risk.⁸ [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

⁶ Paragraphs .13–.14 of section 530, *Audit Sampling*.

⁷ Paragraph .12 of section 320.

⁸ Paragraph .05 of section 530.

Communication and Correction of Misstatements (Ref: par. .07–.09)

.A9 Timely communication of misstatements to the appropriate level of management is important because it enables management to evaluate whether the classes of transactions, account balances, and disclosures are misstated, inform the auditor if it disagrees, and take action as necessary. Ordinarily, the appropriate level of management is the one that has responsibility and authority to evaluate the misstatements and take the necessary action. [Paragraph renumbered and amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

.A10 Law or regulation may restrict the auditor's communication of certain misstatements to management or others within the entity. For example, laws or regulations may specifically prohibit a communication or other action that might prejudice an investigation by an appropriate authority into an instance of noncompliance or suspected noncompliance with laws or regulations. In some circumstances, potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex. In such cases, the auditor may consider seeking legal advice. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A11 The correction by management of all misstatements, including those communicated by the auditor, enables management to maintain accurate accounting books and records and reduces the risks of material misstatement of future financial statements because of the cumulative effect of immaterial uncorrected misstatements related to prior periods. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A12 The auditor may request management to examine a class of transactions, account balance, or disclosure in order for management to understand the cause of a misstatement identified by the auditor; perform procedures to determine the amount of the actual misstatement in the class of transactions, account balance, or disclosure; and make appropriate adjustments to the financial statements. Such a request may be made, for example, based on the auditor's projection of misstatements identified in an audit sample to the entire population from which it was drawn. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A13 The auditor may request management to record an adjustment needed to correct all factual misstatements, including the effect of prior period misstatements (see paragraph .08), other than those that the auditor believes are clearly trivial. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A14 When the auditor has identified a judgmental misstatement involving differences in estimates, such as a difference in a fair value estimate, the auditor may request management to review the assumptions and methods used in developing management's estimate. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A15 Sections 700 and 703 require the auditor to evaluate whether the financial statements are presented fairly, in all material respects, in accordance with the requirements of the applicable financial reporting framework.⁹ This

⁹ Paragraph .12 of section 700 and paragraph .37 of section 703, as applicable. [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 136.]

evaluation includes consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments, which may be affected by the auditor's understanding of management's reasons for not making the corrections (see section 700).¹⁰ [Paragraph renumbered by the issuance of SAS No. 134, May 2019. As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 136.]

.A16 Section 580, *Written Representations*, addresses management representations, including representations with respect to uncorrected misstatements.¹¹ [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A17 In accordance with section 265, *Communicating Internal Control Related Matters Identified in an Audit*, identification by the auditor of a material misstatement of the financial statements under audit in circumstances that indicate that the misstatement would not have been detected by the entity's internal control is an indicator of a material weakness.¹² [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A18 Section 260, *The Auditor's Communication With Those Charged With Governance*, addresses matters to be communicated by the auditor to those charged with governance, including uncorrected misstatements. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

Evaluating the Effect of Uncorrected Misstatements (Ref: par. .10-.11)

.A19 The auditor's determination of materiality in accordance with section 320 often is based on estimates of the entity's financial results because the actual financial results may not yet be known.¹³ Therefore, prior to the auditor's evaluation of the effect of uncorrected misstatements, it may be necessary to revise materiality determined in accordance with section 320 based on the actual financial results. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A20 Section 320 explains that, as the audit progresses, materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances, or disclosures) is revised in the event of the auditor becoming aware of information during the audit that would have caused the auditor to have determined a different amount (or amounts) initially.¹⁴ Thus, any significant revision is likely to have been made before the auditor evaluates the effect of uncorrected misstatements. However, if the auditor's reassessment of materiality determined in accordance with section 320 (see paragraph .10 of this section) gives rise to a lower amount (or amounts), then performance materiality and the appropriateness of the nature, timing, and extent of the further audit procedures are reconsidered in order to

¹⁰ Paragraph .14 of section 700 and paragraph .39 of section 703, as applicable. [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 136.]

¹¹ Paragraph .14 of section 580, *Written Representations*.

¹² Paragraph .A11 of section 265, *Communicating Internal Control Related Matters Identified in an Audit*.

¹³ Paragraph .10 of section 320.

¹⁴ Paragraph .12 of section 320.

obtain sufficient appropriate audit evidence on which to base the audit opinion. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A21 Materiality is determined based on the auditor's understanding of the user needs and expectations (see section 320).¹⁵ Although user expectations may differ based on inherent uncertainty associated with the measurement of particular items in the financial statements, these expectations have already been considered in the auditor's determination of materiality. For example, the fact that the financial statements include very large provisions with a high degree of estimation uncertainty (for example, provisions for insurance claims in the case of an insurance company; oil rig decommissioning costs in the case of an oil company; or, more generally, legal claims against an entity) may influence the auditor's assessment of what users might consider material. However, after materiality is reassessed, this section requires the auditor to evaluate any misstatements in accordance with that level of materiality, regardless of the degree of inherent uncertainty associated with the measurement of particular items in the financial statements. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A22 Each individual misstatement of an amount is considered to evaluate its effect on the relevant classes of transactions, account balances, or disclosures, including whether the materiality level for that particular class of transactions, account balance, or disclosure, if any, has been exceeded. [Paragraph renumbered and amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

.A23 In addition, each individual misstatement of a qualitative disclosure is considered to evaluate its effect on the relevant disclosures, as well as its overall effect on the financial statements as a whole. The determination of whether a misstatement in a qualitative disclosure is material, in the context of the applicable financial reporting framework and the specific circumstances of the entity, is a matter that involves the exercise of professional judgment. Examples of misstatements that may be material include the following:

- Inaccurate or incomplete descriptions of information about the objectives, policies, and processes for managing capital
- The omission of information about the events or circumstances that have led to an impairment loss (for example, a significant long-term decline in the demand for a metal or commodity)
- An incorrect description of an accounting policy relating to a significant item in any of the statements that the financial statements comprise
- An inadequate description of the sensitivity of an exchange rate

[Paragraph added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

.A24 In determining whether uncorrected misstatements by nature are material as required by paragraph .11, the auditor considers uncorrected misstatements in amounts and disclosures. Such misstatements may be considered material either individually or in combination with other misstatements. For example, depending on the misstatements identified in disclosures, the auditor may consider the following:

- Whether identified errors are recurring or pervasive

¹⁵ Paragraph .10 of section 320.

- Whether a number of identified misstatements are relevant to the same matter and, considered collectively, may affect the users' understanding of that matter

This consideration of accumulated misstatements is also helpful when evaluating the financial statements as discussed in paragraph .A15 of section 700, *Forming an Opinion and Reporting on Financial Statements*,¹⁶ or paragraph .A70 of section 703, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*,¹⁷ which states that evaluating whether the financial statements achieve fair presentation may include discussions with management about whether the presentation of amounts or disclosures obscures useful information or results in misleading information. [Paragraph added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

.A25 The auditor is required by section 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, to evaluate the effect on the group audit opinion of any uncorrected misstatement identified by the group engagement team or communicated by the component auditors.¹⁸ [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A26 If an individual misstatement is judged to be material, it is unlikely that it can be offset by other misstatements. For example, if revenue has been materially overstated, the financial statements as a whole will be materially misstated, even if the effect of the misstatement on earnings is completely offset by an equivalent overstatement of expenses. It may be appropriate to offset misstatements within the same account balance or class of transactions; however, the risk that further undetected misstatements may exist is considered before concluding that offsetting even immaterial misstatements is appropriate. The auditor may need to reassess the risks of material misstatement for a specific account balance or class of transactions upon identification of a number of immaterial misstatements within that account balance or class of transactions. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A27 Determining whether a classification misstatement is material involves the evaluation of qualitative considerations, such as the effect of the classification misstatement on debt or other contractual covenants, the effect on individual line items or subtotals, or the effect on key ratios. Circumstances may exist in which the auditor concludes that a classification misstatement is not material in the context of the financial statements as a whole, even though it may exceed the materiality level or levels applied in evaluating other misstatements. For example, a misclassification between balance sheet line items may not be considered material in the context of the financial statements as a whole when the amount of the misclassification is small in relation to the size of the related balance sheet line items and the misclassification does not affect the income statement or any key ratios. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

¹⁶ Paragraph .16 of section 700, *Forming an Opinion and Reporting on Financial Statements*. [Footnote added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

¹⁷ Paragraph .41 of section 703, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*. [Footnote added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

¹⁸ Paragraph .44 of section 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*. [Footnote renumbered by the issuance of SAS No. 134, May 2019.]

.A28 The circumstances related to some misstatements may cause the auditor to evaluate them as material, individually or when considered together with other misstatements accumulated during the audit, even if they are lower than materiality for the financial statements as a whole. Circumstances that may affect the evaluation include the extent to which the misstatement

- affects compliance with regulatory requirements.
- affects compliance with debt covenants or other contractual requirements.
- relates to the incorrect selection or application of an accounting policy that has an immaterial effect on the current period's financial statements but is likely to have a material effect on future periods' financial statements.
- masks a change in earnings or other trends, especially in the context of general economic and industry conditions.
- affects ratios used to evaluate the entity's financial position, results of operations, or cash flows.
- affects segment information presented in the financial statements (for example, the significance of the matter to a segment or other portion of the entity's business that has been identified as playing a significant role in the entity's operations or profitability).
- has the effect of increasing management compensation (for example, by ensuring that the requirements for the award of bonuses or other incentives are satisfied).
- is significant with regard to the auditor's understanding of known previous communications to users (for example, regarding forecast earnings).
- relates to items involving particular parties (for example, whether external parties to the transaction are related to members of the entity's management).
- is an omission of information not specifically required by the applicable financial reporting framework but that, in the professional judgment of the auditor, is important to the users' understanding of the financial position, financial performance, or cash flows of the entity.
- affects other information that will be communicated in documents containing the audited financial statements (for example, information to be included in a "Management Discussion and Analysis" or an "Operating and Financial Review") when there is substantial likelihood that the other information would influence the judgment made by a reasonable user based on the financial statements. Section 720, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports*, addresses the auditor's responsibilities relating to other information, whether financial or nonfinancial information (other than the financial statements and the auditor's report thereon), included in an entity's annual report.
- is a misclassification between certain account balances affecting items disclosed separately in the financial statements (for example, misclassification between operating and nonoperating income or recurring and nonrecurring income items or a misclassification

between restricted and unrestricted resources in a not-for-profit entity).

- offsets effects of individually significant but different misstatements.
- is currently immaterial and likely to have a material effect in future periods because of a cumulative effect, for example, that builds over several periods.
- is too costly to correct. It may not be cost beneficial for the client to develop a system to calculate a basis to record the effect of an immaterial misstatement. On the other hand, if management appears to have developed a system to calculate an amount that represents an immaterial misstatement, it may reflect a motivation of management.
- represents a risk that possible additional undetected misstatements would affect the auditor's evaluation.
- changes a loss into income or vice versa.
- heightens the sensitivity of the circumstances surrounding the misstatement (for example, the implications of misstatements involving fraud and possible instances of noncompliance with laws or regulations, violations of contractual provisions, and conflicts of interest).
- has a significant effect relative to reasonable user needs (for example,
 - earnings to investors and the equity amounts to creditors,
 - the magnifying effects of a misstatement on the calculation of purchase price in a transfer of interests [buy-sell agreement], and
 - the effect of misstatements of earnings when contrasted with expectations).
- relates to the definitive character of the misstatement (for example, the precision of an error that is objectively determinable as contrasted with a misstatement that unavoidably involves a degree of subjectivity through estimation, allocation, or uncertainty).
- indicates the motivation of management (for example, [i] an indication of a possible pattern of bias by management when developing and accumulating accounting estimates, [ii] a misstatement precipitated by management's continued unwillingness to correct weaknesses in the financial reporting process, or [iii] an intentional decision not to follow the applicable financial reporting framework).

These circumstances are only examples — not all are likely to be present in all audits nor is the list necessarily complete. The existence of any circumstances such as these does not necessarily lead to a conclusion that the misstatement is material. [Paragraph renumbered by the issuance of SAS No. 134, May 2019. As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 137. As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 138.]

.A29 Section 240 explains how the implications of a misstatement that is, or may be, the result of fraud are required to be considered with regard to other aspects of the audit, even if the size of the misstatement is not material in relation to the financial statements.¹⁹ Depending on the circumstances, misstatements in disclosures could also be indicative of fraud and, for example, may arise from the following:

- Misleading disclosures that have resulted from bias in management's judgments
- Extensive duplicative or uninformative disclosures that are intended to obscure a proper understanding of matters in the financial statements

When considering the implications of misstatements in classes of transactions, account balances, and disclosures, the auditor exercises professional skepticism in accordance with section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*.²⁰ [Paragraph renumbered and amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

.A30 The cumulative effect of immaterial uncorrected misstatements related to prior periods may have a material effect on the current period's financial statements. Different acceptable approaches to the auditor's evaluation of such uncorrected misstatements on the current period's financial statements are available. Using the same evaluation approach provides consistency from period to period. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

Considerations Specific to Governmental Entities

.A31 In the case of an audit of a governmental entity, the evaluation of whether a misstatement is material also may be affected by the auditor's responsibilities established by law or regulation to report specific matters, including, for example, fraud. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

.A32 Furthermore, issues such as public interest, accountability, integrity, and ensuring effective legislative oversight, in particular, may affect the assessment of whether an item is material by virtue of its nature. This is particularly so for items that relate to compliance with law or regulation. [Paragraph renumbered by the issuance of SAS No. 134, May 2019.]

Documentation (Ref: par. .12)

.A33 The auditor's documentation of uncorrected misstatements may take into account the following:

- a. The consideration of the aggregate effect of uncorrected misstatements
- b. The evaluation of whether the materiality level or levels for particular classes of transactions, account balances, or disclosures, if any, have been exceeded

¹⁹ Paragraph .35 of section 240. [Footnote renumbered by the issuance of SAS No. 134, May 2019.]

²⁰ Paragraph .17 of section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*. [Footnote added, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

- c. The evaluation of the effect of uncorrected misstatements on key ratios or trends and compliance with legal, regulatory, and contractual requirements (for example, debt covenants)

[Paragraph renumbered by the issuance of SAS No. 134, May 2019.]
