

**International Standard on  
Auditing (Ireland) 265  
Updated October 2022**

**Communicating Deficiencies in  
Internal Control to  
those Charged with Governance  
and Management**

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To contribute to Ireland having a strong regulatory environment in which to do business by supervising and promoting high quality financial reporting, auditing and effective regulation of the accounting profession in the public interest.

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**INTERNATIONAL STANDARD ON AUDITING (IRELAND) 265**  
**COMMUNICATING DEFICIENCIES IN INTERNAL CONTROL TO**  
**THOSE CHARGED WITH GOVERNANCE AND MANAGEMENT**  
**(UPDATED OCTOBER 2022)**

(Effective for audits of financial statements for periods commencing on or after 17 June 2016, for which opinions are issued on or after 1 February 2017)

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International Standard on Auditing (Ireland) (ISA (Ireland)) 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* should be read in conjunction with ISA (Ireland) 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (Ireland)*.

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## Introduction

### Scope of this ISA (Ireland)

1. This International Standard on Auditing (Ireland) (ISA (Ireland)) deals with the auditor's responsibility to communicate appropriately to those charged with governance and management deficiencies in internal control<sup>1</sup> that the auditor has identified in an audit of financial statements. This ISA (Ireland) does not impose additional responsibilities on the auditor regarding obtaining an understanding of the entity's system of internal control and designing and performing tests of controls over and above the requirements of ISA (Ireland) 315 (Revised October 2020) and ISA (Ireland) 330.<sup>2</sup> ISA (Ireland) 260<sup>3</sup> establishes further requirements and provides guidance regarding the auditor's responsibility to communicate with those charged with governance in relation to the audit.
2. The auditor is required to obtain an understanding of the entity's system of internal control when identifying and assessing the risks of material misstatement.<sup>4</sup> In making those risk assessments, the auditor considers the entity's system of internal control in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The auditor may identify control deficiencies in entity's system of internal control not only during this risk assessment process but also at any other stage of the audit. This ISA (Ireland) specifies which identified deficiencies the auditor is required to communicate to those charged with governance and management.
3. Nothing in this ISA (Ireland) precludes the auditor from communicating to those charged with governance and management other internal control matters that the auditor has identified during the audit.

### Effective Date

4. This ISA (Ireland) is effective for the audits of financial statements for periods commencing on or after 17 June 2016, for which opinions are issued on or after 1 February 2017.

### Objective

5. The objective of the auditor is to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditor has identified during the audit and that, in the auditor's professional judgment, are of sufficient importance to merit their respective attentions.

### Definitions

6. For purposes of the ISAs (Ireland), the following terms have the meanings attributed below:
  - (a) Deficiency in internal control – This exists when:

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<sup>1</sup> ISA (Ireland) 315 (Revised October 2020), *Identifying and Assessing the Risks of Material Misstatement*, paragraphs 12(c) and (m), and paragraphs 21 to 27.

<sup>2</sup> ISA (Ireland) 330, *The Auditor's Responses to Assessed Risks*.

<sup>3</sup> ISA (Ireland) 260, *Communication with Those Charged with Governance*.

<sup>4</sup> ISA (Ireland) 315 (Revised October 2020), paragraphs 21-26.

- (i) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis; or
- (ii) A control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing.

(b) Significant deficiency in internal control – A deficiency or combination of deficiencies in internal control that, in the auditor's professional judgment, is of sufficient importance to merit the attention of those charged with governance. (Ref: Para. A5)

## Requirements

7. The auditor shall determine whether, on the basis of the audit work performed, the auditor has identified one or more deficiencies in internal control. (Ref: Para. A1-A4)
8. If the auditor has identified one or more deficiencies in internal control, the auditor shall determine, on the basis of the audit work performed, whether, individually or in combination, they constitute significant deficiencies. (Ref: Para. A5-A11)
9. The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis. (Ref: Para. A12-A18, A27)
10. The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis: (Ref: Para. A19, A27)
  - (a) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and (Ref: Para. A14, A20-A21)
  - (b) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention. (Ref: Para. A22-A26)
11. The auditor shall include in the written communication of significant deficiencies in internal control:
  - (a) A description of the deficiencies and an explanation of their potential effects; and (Ref: Para. A28)
  - (b) Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor shall explain that: (Ref: Para. A29-A30)
    - (i) The purpose of the audit was for the auditor to express an opinion on the financial statements;
    - (ii) The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and

(iii) The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.

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## **Application and Other Explanatory Material**

### **Determination of Whether Deficiencies in Internal Control Have Been Identified** (Ref: Para. 7)

A1. In determining whether the auditor has identified one or more deficiencies in internal control, the auditor may discuss the relevant facts and circumstances of the auditor's findings with the appropriate level of management. This discussion provides an opportunity for the auditor to alert management on a timely basis to the existence of deficiencies of which management may not have been previously aware. The level of management with whom it is appropriate to discuss the findings is one that is familiar with the internal control area concerned and that has the authority to take remedial action on any identified deficiencies in internal control. In some circumstances, it may not be appropriate for the auditor to discuss the auditor's findings directly with management, for example, if the findings appear to call management's integrity or competence into question (see paragraph A20).

A2. In discussing the facts and circumstances of the auditor's findings with management, the auditor may obtain other relevant information for further consideration, such as:

- Management's understanding of the actual or suspected causes of the deficiencies.
- Exceptions arising from the deficiencies that management may have noted, for example, misstatements that were not prevented by the relevant information technology (IT) controls.
- A preliminary indication from management of its response to the findings.

### *Considerations Specific to Smaller Entities*

A3. While the concepts underlying controls in the control activities component in smaller entities are likely to be similar to those in larger entities, the formality with which they operate will vary. Further, smaller entities may find that certain types of controls are not necessary because of controls applied by management. For example, management's sole authority for granting credit to customers and approving significant purchases can provide effective control over important account balances and transactions, lessening or removing the need for more detailed controls.

A4. Also, smaller entities often have fewer employees which may limit the extent to which segregation of duties is practicable. However, in a small owner-managed entity, the owner-manager may be able to exercise more effective oversight than in a larger entity. This higher level of management oversight needs to be balanced against the greater potential for management override of controls.

### **Significant Deficiencies in Internal Control** (Ref: Para. 6(b), 8)

A5. The significance of a deficiency or a combination of deficiencies in internal control depends not only on whether a misstatement has actually occurred, but also on the

likelihood that a misstatement could occur and the potential magnitude of the misstatement. Significant deficiencies may therefore exist even though the auditor has not identified misstatements during the audit.

A6. Examples of matters that the auditor may consider in determining whether a deficiency or combination of deficiencies in internal control constitutes a significant deficiency include:

- The likelihood of the deficiencies leading to material misstatements in the financial statements in the future.
- The susceptibility to loss or fraud of the related asset or liability.
- The subjectivity and complexity of determining estimated amounts, such as fair value accounting estimates.
- The financial statement amounts exposed to the deficiencies.
- The volume of activity that has occurred or could occur in the account balance or class of transactions exposed to the deficiency or deficiencies.
- The importance of the controls to the financial reporting process; for example:
  - General monitoring controls (such as oversight of management).
  - Controls over the prevention and detection of fraud.
  - Controls over the selection and application of significant accounting policies.
  - Controls over significant transactions with related parties.
  - Controls over significant transactions outside the entity's normal course of business.
  - Controls over the period-end financial reporting process (such as controls over non-recurring journal entries).
- The cause and frequency of the exceptions detected as a result of the deficiencies in the controls.
- The interaction of the deficiency with other deficiencies in internal control.

A7. Indicators of significant deficiencies in internal control include, for example:

- Evidence of ineffective aspects of the control environment, such as:
  - Indications that significant transactions in which management is financially interested are not being appropriately scrutinized by those charged with governance.
  - Identification of management fraud, whether or not material, that was not prevented by the entity's internal control.
  - Management's failure to implement appropriate remedial action on significant deficiencies previously communicated.
- Absence of a risk assessment process within the entity where such a process would ordinarily be expected to have been established.

- Evidence of an ineffective entity risk assessment process, such as management's failure to identify a risk of material misstatement that the auditor would expect the entity's risk assessment process to have identified.
- Evidence of an ineffective response to identified significant risks (for example, absence of controls over such a risk).
- Misstatements detected by the auditor's procedures that were not prevented, or detected and corrected, by the entity's internal control.
- Restatement of previously issued financial statements to reflect the correction of a material misstatement due to error or fraud.
- Evidence of management's inability to oversee the preparation of the financial statements.

A8. Controls may be designed to operate individually or in combination to effectively prevent, or detect and correct, misstatements.<sup>5</sup> For example, controls over accounts receivable may consist of both automated and manual controls designed to operate together to prevent, or detect and correct, misstatements in the account balance. A deficiency in internal control on its own may not be sufficiently important to constitute a significant deficiency. However, a combination of deficiencies affecting the same account balance or disclosure, assertion, or component of the entity's system of internal control may increase the risks of misstatement to such an extent as to give rise to a significant deficiency.

A9. Law or regulation in some jurisdictions may establish a requirement (particularly for audits of listed entities) for the auditor to communicate to those charged with governance or to other relevant parties (such as regulators) one or more specific types of deficiency in internal control that the auditor has identified during the audit. Where law or regulation has established specific terms and definitions for these types of deficiency and requires the auditor to use these terms and definitions for the purpose of the communication, the auditor uses such terms and definitions when communicating in accordance with the legal or regulatory requirement.

A10. Where the jurisdiction has established specific terms for the types of deficiency in internal control to be communicated but has not defined such terms, it may be necessary for the auditor to use judgment to determine the matters to be communicated further to the legal or regulatory requirement. In doing so, the auditor may consider it appropriate to have regard to the requirements and guidance in this ISA (Ireland). For example, if the purpose of the legal or regulatory requirement is to bring to the attention of those charged with governance certain internal control matters of which they should be aware, it may be appropriate to regard such matters as being generally equivalent to the significant deficiencies required by this ISA (Ireland) to be communicated to those charged with governance.

A11. The requirements of this ISA (Ireland) remain applicable notwithstanding that law or regulation may require the auditor to use specific terms or definitions.

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<sup>5</sup> ISA (Ireland) 315 (Revised October 2020), paragraph A175.

## Communication of Deficiencies in Internal Control

### *Communication of Significant Deficiencies in Internal Control to Those Charged with Governance* (Ref: Para. 9)

A12. Communicating significant deficiencies in writing to those charged with governance reflects the importance of these matters, and assists those charged with governance in fulfilling their oversight responsibilities. ISA (Ireland) 260 establishes relevant considerations regarding communication with those charged with governance when all of them are involved in managing the entity.<sup>6</sup>

A12-1. In Ireland, where applicable, timely communication of significant deficiencies, in writing, to directors of listed entities can assist them to comply with the provisions of the UK Corporate Governance Code relating to internal control and reporting to shareholders.

A13. In determining when to issue the written communication, the auditor may consider whether receipt of such communication would be an important factor in enabling those charged with governance to discharge their oversight responsibilities. In addition, for listed entities in certain jurisdictions, those charged with governance may need to receive the auditor's written communication before the date of approval of the financial statements in order to discharge specific responsibilities in relation to internal control for regulatory or other purposes. For other entities, the auditor may issue the written communication at a later date. Nevertheless, in the latter case, as the auditor's written communication of significant deficiencies forms part of the final audit file, the written communication is subject to the overriding requirement<sup>7</sup> for the auditor to complete the assembly of the final audit file on a timely basis. ISA (Ireland) 230 states that an appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report.<sup>8</sup>

A13-1. For audits of financial statements of public interest entities, ISA (Ireland) 260<sup>8a</sup> requires the auditor to communicate in the additional report to the audit committee any significant deficiencies in the entity's internal financial control system or in the accounting system, and whether or not the deficiencies reported have been resolved by management.

A14. Regardless of the timing of the written communication of significant deficiencies, the auditor may communicate these orally in the first instance to management and, when appropriate, to those charged with governance to assist them in taking timely remedial action to minimize the risks of material misstatement. Doing so, however, does not relieve the auditor of the responsibility to communicate the significant deficiencies in writing, as this ISA (Ireland) requires.

A15. The level of detail at which to communicate significant deficiencies is a matter of the auditor's professional judgment in the circumstances. Factors that the auditor may consider in determining an appropriate level of detail for the communication include, for example:

<sup>6</sup> ISA (Ireland) 260, paragraph 13.

<sup>7</sup> ISA (Ireland) 230, *Audit Documentation*, paragraph 14.

<sup>8</sup> ISA (Ireland) 230, paragraph A21.

<sup>8a</sup> ISA (Ireland) 260, paragraph 16R-2(j).

- The nature of the entity. For instance, the communication required for a public interest entity may be different from that for a non-public interest entity.
- The size and complexity of the entity. For instance, the communication required for a complex entity may be different from that for an entity operating a simple business.
- The nature of significant deficiencies that the auditor has identified.
- The entity's governance composition. For instance, more detail may be needed if those charged with governance include members who do not have significant experience in the entity's industry or in the affected areas.
- Legal or regulatory requirements regarding the communication of specific types of deficiency in internal control.

A16. Management and those charged with governance may already be aware of significant deficiencies that the auditor has identified during the audit and may have chosen not to remedy them because of cost or other considerations. The responsibility for evaluating the costs and benefits of implementing remedial action rests with management and those charged with governance. Accordingly, the requirement in paragraph 9 applies regardless of cost or other considerations that management and those charged with governance may consider relevant in determining whether to remedy such deficiencies.

A17. The fact that the auditor communicated a significant deficiency to those charged with governance and management in a previous audit does not eliminate the need for the auditor to repeat the communication if remedial action has not yet been taken. If a previously communicated significant deficiency remains, the current year's communication may repeat the description from the previous communication, or simply reference the previous communication. The auditor may ask management or, where appropriate, those charged with governance, why the significant deficiency has not yet been remedied. A failure to act, in the absence of a rational explanation, may in itself represent a significant deficiency.

#### Considerations Specific to Smaller Entities

A18. In the case of audits of smaller entities, the auditor may communicate in a less structured manner with those charged with governance than in the case of larger entities.

#### *Communication of Deficiencies in Internal Control to Management (Ref: Para. 10)*

A19. Ordinarily, the appropriate level of management is the one that has responsibility and authority to evaluate the deficiencies in internal control and to take the necessary remedial action. For significant deficiencies, the appropriate level is likely to be the chief executive officer or chief financial officer (or equivalent) as these matters are also required to be communicated to those charged with governance. For other deficiencies in internal control, the appropriate level may be operational management with more direct involvement in the control areas affected and with the authority to take appropriate remedial action.

#### *Communication of Significant Deficiencies in Internal Control to Management (Ref: Para. 10(a))*

A20. Certain identified significant deficiencies in internal control may call into question the integrity or competence of management. For example, there may be evidence of fraud

or intentional non-compliance with laws and regulations by management, or management may exhibit an inability to oversee the preparation of adequate financial statements that may raise doubt about management's competence. Accordingly, it may not be appropriate to communicate such deficiencies directly to management.

A21. ISA (Ireland) 250 establishes requirements and provides guidance on the reporting of identified or suspected non-compliance with laws and regulations, including when those charged with governance are themselves involved in such non-compliance.<sup>9</sup> ISA (Ireland) 240 establishes requirements and provides guidance regarding communication to those charged with governance when the auditor has identified fraud or suspected fraud involving management.<sup>10</sup>

Communication of Other Deficiencies in Internal Control to Management (Ref: Para. 10(b))

A22. During the audit, the auditor may identify other deficiencies in internal control that are not significant deficiencies but that may be of sufficient importance to merit management's attention. The determination as to which other deficiencies in internal control merit management's attention is a matter of professional judgment in the circumstances, taking into account the likelihood and potential magnitude of misstatements that may arise in the financial statements as a result of those deficiencies.

A23. The communication of other deficiencies in internal control that merit management's attention need not be in writing but may be oral. Where the auditor has discussed the facts and circumstances of the auditor's findings with management, the auditor may consider an oral communication of the other deficiencies to have been made to management at the time of these discussions. Accordingly, a formal communication need not be made subsequently.

A24. If the auditor has communicated deficiencies in internal control other than significant deficiencies to management in a prior period and management has chosen not to remedy them for cost or other reasons, the auditor need not repeat the communication in the current period. The auditor is also not required to repeat information about such deficiencies if it has been previously communicated to management by other parties, such as the internal audit function or regulators. It may, however, be appropriate for the auditor to re-communicate these other deficiencies if there has been a change of management, or if new information has come to the auditor's attention that alters the prior understanding of the auditor and management regarding the deficiencies. Nevertheless, the failure of management to remedy other deficiencies in internal control that were previously communicated may become a significant deficiency requiring communication with those charged with governance. Whether this is the case depends on the auditor's judgment in the circumstances.

A25. In some circumstances, those charged with governance may wish to be made aware of the details of other deficiencies in internal control the auditor has communicated to management, or be briefly informed of the nature of the other deficiencies. Alternatively, the auditor may consider it appropriate to inform those charged with

<sup>9</sup> ISA (Ireland) 250, *Section A - Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraphs 22-28.

<sup>10</sup> ISA (Ireland) 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraph 41.

governance of the communication of the other deficiencies to management. In either case, the auditor may report orally or in writing to those charged with governance as appropriate.

A26. ISA (Ireland) 260 establishes relevant considerations regarding communication with those charged with governance when all of them are involved in managing the entity.<sup>11</sup>

*Considerations Specific to Public Sector Entities* (Ref: Para. 9-10)

A27. Public sector auditors may have additional responsibilities to communicate deficiencies in internal control that the auditor has identified during the audit, in ways, at a level of detail and to parties not envisaged in this ISA (Ireland). For example, significant deficiencies may have to be communicated to the legislature or other governing body. Law, regulation or other authority may also mandate that public sector auditors report deficiencies in internal control, irrespective of the significance of the potential effects of those deficiencies. Further, legislation may require public sector auditors to report on broader internal control-related matters than the deficiencies in internal control required to be communicated by this ISA (Ireland), for example, controls related to compliance with legislative authorities, regulations, or provisions of contracts or grant agreements.

*Content of Written Communication of Significant Deficiencies in Internal Control* (Ref: Para. 11)

A28. In explaining the potential effects of the significant deficiencies, the auditor need not quantify those effects. The significant deficiencies may be grouped together for reporting purposes where it is appropriate to do so. The auditor may also include in the written communication suggestions for remedial action on the deficiencies, management's actual or proposed responses, and a statement as to whether or not the auditor has undertaken any steps to verify whether management's responses have been implemented.

A29. The auditor may consider it appropriate to include the following information as additional context for the communication:

- An indication that if the auditor had performed more extensive procedures on internal control, the auditor might have identified more deficiencies to be reported, or concluded that some of the reported deficiencies need not, in fact, have been reported.
- An indication that such communication has been provided for the purposes of those charged with governance, and that it may not be suitable for other purposes.

A30. Law or regulation may require the auditor or management to furnish a copy of the auditor's written communication on significant deficiencies to appropriate regulatory authorities. Where this is the case, the auditor's written communication may identify such regulatory authorities.

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<sup>11</sup> ISA (Ireland) 260, paragraph 13.



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