**SA 265 — Communicating Deficiencies in Internal Control to Those with Governance and Management** — Effective since April 1, 2010

The SA 265 deals with the auditor's responsibility to communicate appropriately the deficiencies in internal control to those charged with governance and management, in the backdrop of SA 315 and SA 330 on *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment* and *The Auditor's Responses to Assessed Risks* respectively.

This Standard is designed with the underlined objective to assist the auditor in achieving his objective —

> 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.

The Standard requires the auditor to —

(a) determine whether, on the basis of the audit work performed, the auditor has identified one or more deficiencies in internal control

(b) If yes, whether such deficiencies – either individually or in combination, constitute significant deficiency/ies.

Whether a deficiency is significant depends upon various factors, and not necessarily whether a misstatement has actually occurred, but including the likelihood that a misstatement could occur. Examples of matters that an auditor may consider in determining whether a deficiency is significant include – 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, volume of activity that has occurred or could occur in the account balance or class of transactions exposed to the deficiency or deficiencies.

Where, e.g. a small business managed by its single owner, and there is no one else assigned with the specific role of governance, the matters required by the Standard are communicated with the person(s) with the management responsibilities, and such person(s) also have a governance role, the auditor need not communicate the matters again with the same person(s) in their governance role.

(c) communicate, in writing, such significant deficiency/ies in internal control to those charged with governance on timely basis

(d) communicate also to management at the appropriately level of responsibility on a timely basis —

   (i) 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 [e.g. evidence of fraud or intentional non-compliance with laws by management, deficiencies calling into question the integrity or competence of management].

   Putting it differently, generally all deficiencies communicated to those charged with governance are also required to be communicated to management

   (ii) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties [e.g. internal auditors, regulators] and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention.

   However, where such deficiencies have been communicated in the prior period, and the management has chosen not to remedy them for cost or other reasons, the same need no communication in the current period, but in circumstances, such as, a change in management, it may be appropriate to re-communication.

(e) include in the written communication of significant deficiencies —

   (i) a description of the deficiencies and an explanation of their potential effects, and

   (ii) sufficient information to enable those charged with governance and management to understand the context of the communication, explaining, in particular, that —

   - the purpose of the audit was for the auditor to express an opinion on financial statements
   - the audit included consideration of internal control relevant to the preparation of the financial statements in order to design appropriate audit procedures, but not for the purpose of expressing an opinion on the effectiveness of internal control
   - the matter being reported are limited to those deficiencies that the auditor has identified during the audit and concluded to be of sufficient importance to merit, also reported/being reported to those charged with governance.