

ISSUES PAPER**Proposed ISA 500 (Redrafted) – Audit Evidence****A. Overview**

A1. In most respects, respondents were generally supportive of the redraft. The most significant issues raised were with respect to the following topics, each of which is discussed in more detail below:

- (a) **Dealing with Sufficiency as well as Appropriateness:** The vast majority of respondents who provided detailed comment on this matter were in favor of ISA 500 covering both the sufficiency and the appropriateness of audit evidence. The task force agrees with this approach and has, therefore, amended the title and the objective of the ISA, and introduced a new requirement that includes consideration of sufficiency.
- (b) **Repetition of text from ISA 200:** The introductory section to ED-ISA 500 included a discussion of key points regarding sufficiency and appropriateness drawn from ED-ISA 200. The Explanatory Memorandum noted the IAASB's view that the repetition of this text was appropriate to provide context for the requirements of ISA 500. A large number of respondents who provided detailed comment on this matter accepted that some duplication is necessary. The repetition has been retained, but the text has been moved from the Introduction to the Application Material, and unnecessary differences from ISA 200 have been eliminated.
- (c) **Mandating Procedures:** Some respondents suggested that the ISA should mandate the list of procedures included the Application Material (inspection, observation, confirmation, etc). The task force does not agree with this suggestion, but notes that the introduction of the new requirement that includes consideration of sufficiency (mentioned in para (a) above), requires the auditor to "design and perform audit procedures that are appropriate in the circumstances."
- (d) **Selecting Items for Testing:** ED-ISA 500 included material, previously included in ISA 530,¹ that deals with the selection of items for testing by means other than sampling. Mixed views on the placement of this material were expressed by respondents. The task force is of the view that the material suits the flow of ISA 500 and should remain.

B. Dealing with Sufficiency as well as Appropriateness

B1. The Explanatory Memorandum accompanying ED-ISA 500 noted that:

The IAASB is of the view that the overarching bold type requirement in paragraph 2 of extant ISA 500, "Audit Evidence" for the auditor to obtain sufficient appropriate audit evidence is a fundamental audit requirement, appropriate for inclusion as a requirement in proposed ISA 200 (Revised and Redrafted), "Overall Objective of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing." Further, the IAASB believes that including this requirement in

¹ ISA 530 (Redrafted), "Audit Sampling and Other Means of Testing."

proposed ISA 200 (Revised and Redrafted) provides the appropriate context for the requirement of that ISA that the auditor use objectives to consider whether sufficient appropriate audit evidence has been obtained.

Accordingly, the requirement for the auditor to obtain sufficient appropriate audit evidence has been moved from extant ISA 500 to proposed ISA 200 (Revised and Redrafted) along with supporting Application and Other Explanatory Material. As a result of the repositioning of this requirement, proposed ISA 500 (Redrafted) focuses on the auditor’s responsibility to design and perform audit procedures to obtain relevant and reliable audit evidence; it has been re-titled accordingly.

B2. While agreeing that the fundamental requirement to obtain sufficient appropriate audit evidence should be in ISA 200, the vast majority of respondents who provided detailed comment on this matter were in favor of ISA 500 covering both the sufficiency and the appropriateness of audit evidence.² Reasons given for why ISA 500 should not focus solely on appropriateness included that doing so:

- Gives rise to a risk that auditors might fail to fully appreciate the importance of the relationship between sufficiency and appropriateness.
- Results in an ISA that is imbalanced, and lacks substance and clarity.
- Creates a danger of inconsistency with the other ISAs as sufficiency and appropriateness are generally considered together in the other ISAs.
- Necessitates introducing the term “relevant and reliable audit evidence,” which causes confusion regarding the auditor’s responsibilities.

Some of these respondents also noted that ED-ISA 500 already includes coverage of various aspects of sufficiency but is incomplete, and the rationale as to what has been included and what has been excluded is not clear.

B3. In the light of the strong opposition to the approach of the ED, the task force accepts that ISA 500 should cover both sufficiency and appropriateness of audit evidence, and has, therefore:

- (a) Amended the title of the ISA, from “Considering the Relevance and Reliability of Audit Evidence,” to “Obtaining Sufficient Appropriate Audit Evidence;”
- (b) Amended the objective to read: “The objective of the auditor is to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion;” and
- (c) Introduced a new requirement at paragraph 11.1, under the heading Sufficient Appropriate Audit Evidence: “The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.”

² APB; BDO; Baker Tilly; Basel; CEBS; CIPFA; CNCC-CSOEC; DTT (2nd preference); EYG; FEE; ICAEW; ICAS; ICJCE; IdW; Mazars; and NAO.

- B4. The task force believes the revised objective and new paragraph 11.1 create an appropriate linkage between the three ISAs that deal directly with the sufficiency and appropriateness of audit evidence:
- (a) ISA 200, which contains an overarching requirement to obtain sufficient appropriate audit evidence,³ and includes high-level discussion of sufficiency and appropriateness, and of such matters as the nature of audit procedures, and the timeliness of financial reporting and the balance between benefit and cost.⁴
 - (b) ISA 500, which focuses on designing and performing procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence; and
 - (c) ISA 330, which considers audit evidence in the context of further audit procedures to respond to assessed risks, and includes a requirement to conclude whether sufficient appropriate audit evidence has been obtained.⁵

Matters for IAASB Consideration

- Q1. Does the IAASB agree that ISA 500 should cover both sufficiency and appropriateness of audit evidence?
- Q2. Does the IAASB agree with revising the title of the ISA?
- Q3. Does the IAASB agree with the wording of the revised objective (para 9) and the new requirement in paragraph 11.1 of the draft?

C. Repetition of text from ISA 200

- C1. The Explanatory Memorandum accompanying ED-ISA 500 noted that:

... to provide the appropriate context for the requirements of proposed ISA 500 (Redrafted), a discussion of the sufficiency and appropriateness of audit evidence, consistent with that in the Application and Other Explanatory Material of proposed ISA 200 (Revised and Redrafted), has been retained in the Introduction to proposed ISA 500 (Redrafted). Because the concept of sufficiency and appropriateness of audit evidence is fundamental to the conduct of an audit in accordance with ISAs, the IAASB believes that the benefits of emphasizing it in both the context of proposed ISA 500 (Redrafted) and proposed ISA 200 (Revised and Redrafted) outweigh the disadvantages of repetition.

- C2. A large number of respondents who provided detailed comment on this matter accepted that some duplication is necessary.⁶ In fact, most of these respondents advocated covering both sufficiency and appropriateness in ISA 500 as well as ISA 200, and while acknowledging that this may lead to further duplication, believed that it was still desirable.

³ “The auditor shall obtain sufficient appropriate audit evidence in order to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion” – March 2008 draft of ISA 200 (Revised and Redrafted),” Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing,” paragraph 17.

⁴ March 2008 draft of ISA 200 (Revised and Redrafted), paragraph A22-A25, and A41-A47.

⁵ “The auditor shall conclude whether sufficient appropriate audit evidence has been obtained.” -- ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks,” paragraph 27 “

⁶ APB; Baker Tilly; CEBS; CIPFA; CNCC-CSOEC; FEE; ICAEW; ICAS; IdW; NAO; and PwC.

- C3. Some respondents would prefer to delete some or all of the duplicated text.⁷ In some cases, the problem of duplication was offered as part of an argument that ISA 500 should be entirely subsumed in to other ISAs.⁸ In one case⁹ there was a preference for moving ISA 200's coverage of sufficiency and appropriateness into ISA 500.
- C4. Some respondents thought that, if retained, some or all of the duplicated text, should be moved out of the Introduction section and into either the Application Material or the Requirements (see Section D of this memo "Mandating Procedures").¹⁰
- C5. The task force agrees with the majority of respondents that the benefits of emphasizing this material in the context of both ISA 500 and ISA 200 outweigh the disadvantages of repetition. The task force has, however, moved relevant text (old paragraphs 3-7) from the Introduction section of ED-ISA 500, to the beginning of the Application Material (paragraphs Aa-Af), where it is cross-referenced to the new paragraph 11.1. The task force has also eliminated unnecessary differences between the text as it appears in ISA 500 and ISA 200 (see appendix to this memo for a comparison). It is also noted that, if this text changes as a result of discussions on ISA 200, it will also need to change in ISA 500.

Matters for IAASB Consideration

- Q4. Does the IAASB agree with retaining an element of repetition between the guidance in ISA 200 and in ISA 500 discussing the sufficiency and appropriateness of audit evidence?
- Q5. Does the IAASB agree with moving this text to the Application Material (paragraphs A-Af)?

D. Mandating Procedures

- D1. Some respondents suggested that the ISA should mandate the list of procedures currently in paragraph Ae.¹¹ For example:

Audit procedures to obtain audit evidence shall include inspection, observation, confirmation, recalculation, reperformance and analytical procedures, in some combination, in addition to inquiry.

Or

When obtaining and evaluating audit evidence to form the audit opinion, the auditor shall consider procedures such as inspection, observation, confirmation, recalculation, reperformance and analytical procedures and inquiry."

- D2. The task force thinks that elevating this material to a requirement is not necessary, and would yield a requirement that was set at too low, or too procedural, a level. The appropriate principle is expressed in new paragraph 11.1, which requires the auditor to "design and perform audit procedures that are appropriate in the circumstances for the

⁷ CICA, DTT, EYG, GTI; and ICAIre.

⁸ CICA; and DTT (although a fallback position included acceptance of duplication).

⁹ EYG.

¹⁰ Basel, CEBS, EC, IRBA; and Mazars.

¹¹ Basel, CEBS, EC, IRBA; and Mazars.

purpose of obtaining sufficient appropriate audit evidence”. To obtain that evidence, the auditor will necessarily use a selection of the procedures in paragraph Ae. The exact procedures to be used will vary considerably from one aspect of an engagement to another, and from year to year, and so it would seem to serve little purpose to include in the requirement a list of procedures for consideration when these are all the classes of procedure available to the auditor, as explained in the application material..

Matter for IAASB Consideration

Q6. Does the IAASB agree that it is unnecessary to spell out that the procedures to be considered are inspection, observation, etc?

E. Selecting Items for Testing

E1. The Explanatory Memorandum accompanying ED-ISA 500 noted that:

As well as dealing with audit sampling, extant ISA 530, “Audit Sampling and Other Means of Testing” includes material dealing with the selection of items for testing by means other than sampling, i.e., selecting all items and selecting specific items. The IAASB is of the view that this material is better placed in proposed ISA 500 (Redrafted) in order to provide a clear focus on sampling in ISA 530.

The IAASB has therefore moved the material regarding selecting all items and selecting specific items from extant ISA 530 to proposed ISA 500 (Redrafted).

E2. This material is in paragraphs 13 and A31-A34. One respondent¹² explicitly supported retaining this text in ISA 500, and a number of others¹³ tacitly indicated support by commenting on the relevant paragraphs without mentioning that they should be moved to ISA 530 (or elsewhere). Two commentators¹⁴ suggested that the material should be moved back to ISA 530, one suggested it should be moved to ISA 330,¹⁵ and one expressed ambivalence about its placement.¹⁶

E3. The task force is of the view that the material suits the flow of ISA 500 and should remain.

Matter for IAASB Consideration

Q7. Does the IAASB agree with retaining the section on Selecting Items for Testing (paragraphs 13, and A31-A34) in ISA 500?

¹² CPAA.

¹³ CEBS; CNCC-CSOEC; EYG; FEE; IBR-IRE; IRBA; and KPMG.

¹⁴ IdW; and KPMG Sth Af. IdW argue that “the selection of items for testing – as opposed to deciding what should be tested about the item – is a “sufficiency” issue – not an appropriateness one per se that is closely linked to audit sampling (which relates to selection of items to obtain representative samples, as opposed to selecting items without considering their representativeness).” To an extent, changing the focus of ISA 500 to include “sufficiency” serves to detract from this argument.

¹⁵ AICPA.

¹⁶ Mazars.

Appendix

Comparison of guidance regarding sufficiency and appropriateness of audit evidence

ISA 200 (as at March 2008)	ISA 500 (as at March 2008)
<p>A22. Audit evidence is necessary to support the auditor’s opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit) and a firm’s quality control procedures for client acceptance and continuance. Audit evidence comprises both information that supports and corroborates management’s assertions, and any information that contradicts such assertions. In addition, in some cases the existence of a lack of evidence (e.g., management’s failure to provide a requested representation) also represents information used by the auditor and therefore also constitutes audit evidence. Most of the auditor’s work in forming the auditor’s opinion consists of obtaining and evaluating audit evidence.</p>	<p>Aa. Audit evidence is necessary to support the auditor’s opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit) and a firm’s quality control procedures for client acceptance and continuance. <u>In addition to other sources inside and outside the entity, the entity’s accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared by an expert employed or engaged by the entity.</u> Audit evidence comprises both information that supports and corroborates management’s assertions, and any information that contradicts such assertions. In addition, in some cases the existence of a lack of evidence (e.g., management’s failure to provide a requested representation) also represents information used by the auditor and therefore also constitutes audit evidence. <i>[The final sentence of ISA 200.A22 (i.e. “Most of the auditor’s work ...”) appears as the first sentence in ISA 500.Ab]</i></p>
<p><i>[The first sentence of ISA 200.A22 (i.e. “Most of the auditor’s work ...”) appears as the last sentence in ISA 220.22]</i></p>	<p>Ab. Most of the auditor’s work in forming the auditor’s opinion consists of obtaining and evaluating audit evidence. <u>Audit procedures to obtain audit evidence can include inspection, observation, confirmation, recalculation, reperformance and analytical procedures, often in some combination, in addition to inquiry. Although inquiry may provide important audit evidence, inquiry alone ordinarily does not provide sufficient audit evidence to detect a material misstatement at the assertion level, nor of the operating effectiveness of controls.</u></p>
	<p>Ac. <u>As explained in [proposed] ISA 200 (Revised and Redrafted), “Overall Objective of the Independent Auditor, and Concepts Relevant to an Audit of Financial</u></p>

	<p><u>Statements,” reasonable assurance is obtained when the auditor has reduced audit risk to an acceptably low level by obtaining sufficient appropriate audit evidence.</u></p>
<p>A23. Sufficiency is the measure of the quantity of audit evidence. The quantity of audit evidence needed is affected by the auditor’s assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality.</p>	<p>Ad. Sufficiency is the measure of the quantity of audit evidence. The quantity of audit evidence needed is affected by the auditor’s assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality.</p>
<p>A24. Appropriateness is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based. The reliability of evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained.</p>	<p>Ae. Appropriateness is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based. The reliability of evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained.</p>
<p>A25. The sufficiency and appropriateness of audit evidence are interrelated. Whether sufficient appropriate audit evidence has been obtained to reduce audit risk to an acceptably low level, and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion, is a matter for the auditor to determine using professional judgment. [Proposed] ISA 500 (Redrafted) and other relevant ISAs establish additional requirements and provide further guidance applicable throughout the audit regarding the auditor’s considerations in obtaining sufficient appropriate audit evidence.</p>	<p>Af. <u>ISA 330 requires the auditor to conclude whether sufficient appropriate audit evidence has been obtained.</u> The sufficiency and appropriateness of audit evidence are interrelated. Whether sufficient appropriate audit evidence has been obtained to reduce audit risk to an acceptably low level, and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion, is a matter for the auditor to determine using of professional judgment. <u>ISA 200 (Redrafted) contains discussion of such matters as the nature of audit procedures, and the timeliness of financial reporting and the balance between benefit and cost, which are relevant factors when the auditor exercises professional judgment regarding whether sufficient appropriate audit evidence has been obtained.</u> [Proposed] ISA 500 (Redrafted) and other relevant ISAs establish additional requirements and provide further guidance applicable throughout the audit regarding the auditor’s considerations in obtaining sufficient appropriate audit evidence.</p>

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