



Agenda Item 2

Audit Evidence

Objective of Agenda Item

To approve the proposed revised AU-C section 500, *Audit Evidence* (AU-C section 500) as an exposure draft.

Task Force

Because of the mutual interest of the AICPA's Auditing Standards Board (ASB) and Assurance Services Executive Committee (ASEC), the Audit Evidence Task Force (the "Task Force") is comprised of members from both bodies, as well as representatives from the AICPA's Technical Issues Committee (TIC). In addition, the International Auditing and Assurance Standards Board (IAASB) has an interest in this project, and consequently, IAASB representatives participate as observers on the Task Force. Task Force members are:

- Bob Dohrer, Chief Auditor, AICPA, Chair
- Jay Brodish, PwC
- Jim Burton, GT
- David Finkelstein, SingerLewak (TIC)
- Audrey Gramling, Oklahoma State University
- Kristen Kociolek, GAO
- Susan Jones, KPMG and IAASB Technical Advisor
- Jeff Schaberg, Deloitte
- Eric Turner, CPA Canada and IAASB Member
- Alan Young, EY and IAASB AEWG Correspondent Member

Background

The overall objective of the project is to assess whether revisions of AU-C section 500 are appropriate and necessary to address the evolving nature of business, including the use of emerging technologies by both preparers and auditors, the expanding use of externally generated information as audit evidence, and more broadly the accuracy, completeness, and reliability of such audit evidence. The application of professional skepticism by auditors in evaluating audit evidence is

also being emphasized. Appendix 1 to this Issues Paper contains a more detailed explanation of the issues that have been presented to the ASB in prior meetings. The revisions in the proposed AU-C section 500 are intended to address these matters.

Prior discussions between the Task Force and the ASB are summarized as follows:

- January 2018—at the joint meeting between ASB and ASEC, the chair of the Task Force provided a high-level overview of the background of the project and a high-level discussion of possible issues identified by the Task Force.
- May 2018—
 - The Task Force provided an overview of the preliminary issues identified. These preliminary issues were: 1) definitions, 2) audit procedures, 3) key concepts, and 4) changing the focus of the standard.
 - The Task Force explained that it had been exploring possibly developing additional application material that would assist the auditor in assessing whether sufficient appropriate audit evidence had been obtained. The intent of such additional application material or framework would be to change the focus of AU-C 500 from focusing on the performance of audit procedures to obtain audit evidence to a focus in which the auditor’s main objective would be to evaluate whether sufficient appropriate audit evidence had been obtained. The ASB expressed support for such a framework and agreed that it would be helpful to provide application material. But, it noted that a procedures-based approach and a framework approach are not mutually exclusive, that is, the procedures-based approach should complement the framework being suggested by the Task Force rather than replace it.
- October 2018—
 - The ASB discussed a first draft of the proposed SAS, Audit Evidence, which would supersede AU-C section 500, Audit Evidence. In presenting the draft of the proposed SAS, the Task Force discussed with the ASB the following matters:
 - a. The project timeline, including coordination with the international standard setting activities,
 - b. expanded guidance to evaluate sufficient appropriate audit evidence, including how the relevance of audit evidence interrelates with the proposed framework,
 - c. whether management’s specialists content should be relocated out of the proposed SAS,
 - d. changes to the definitions,

- e. how to deal with the content addressing external information sources taken from the IAASB’s conforming amendments from ISA 540,
 - f. changes to guidance dealing with audit procedures, and
 - g. disposition of the Interpretations in extant AU-C 500.
- Significant feedback provided by the ASB to the Task Force were as follows:
 - Revise objective to sharpen the focus on evaluating sufficient appropriate audit evidence.
 - Retain, with some refinements, the requirements and application material added to provide the auditor with a framework for evaluating whether sufficient appropriate audit evidence has been obtained.
 - Relocate content related to management’s specialists to either AU-C section 620, Using the Work of an Auditor’s Specialist, or a new standard.
 - Incorporate in the proposed SAS conforming amendments to ISA 500, Audit Evidence, arising from the final ISA 540, Auditing Accounting Estimates as those amendments relate to *External Information Sources*.
 - Retain the Interpretations to AU-C section 500 attached to this standard.
- January 2019—
 - The ASB was supportive of the direction of the project. However, the ASB expressed the view that the proposed standard needs further editing and refinements.
 - Some ASB members expressed the view that the proposed effective date of years ending on or after December 15, 2020 may be challenging given the timeline of the project.
 - The ASB was supportive of the graphic illustration of the proposed attributes and factors that would assist the auditor in making the conclusion whether sufficient appropriate audit evidence (the “Cube”). However, the ASB found the term “relationship to management assertions” to describe the notion of corroborative or contradictory information confusing. After discussion, the ASB decided to retain the Cube but suggested that the Cube should be more prominently featured throughout the proposed standard so that it can better illustrate the proposed attributes and factors that would assist the auditor in concluding whether sufficient appropriate audit evidence has been obtained.

Matters for the ASB’s Consideration

Audit Evidence
ASB Meeting, May 20-23, 2019

<i>ASB Comment</i>	<i>Task Force Disposition</i>
<i>January 2019 ASB Meeting</i>	
1. Augment the scope section to better articulate the interrelationship of the proposed SAS to other standards such as AU-C section 315 and 330. The ASB also requested the Task Force to make it clearer that information obtained by the auditor only becomes audit evidence after audit procedures are applied to the information.	The Task Force made the edits as suggested (see paragraphs 1-4).
2. Make it explicit that the requirements in the proposed SAS do not establish incremental audit documentation requirements beyond those already required in other standards.	The Task Force added the paragraph as suggested (see paragraph 6).
3. Revise the objective to make it more explicit that the auditor evaluates information as a basis to conclude whether sufficient appropriate audit evidence has been obtained.	The Task Force made the edits as suggested (see paragraph 8).
4. Add guidance to better explain the concept of “sufficient appropriate audit evidence” by explaining separately the concepts of “sufficiency” and “appropriateness” and how “sufficiency” is assessed based on the persuasiveness of audit evidence.	The Task Force reinstated revised definitions of sufficiency and appropriateness. The revised definition of sufficiency is now focused on the persuasiveness of audit evidence.
5. Clarify the intended work effort of the requirements dealing with the factors and attributes to be used for evaluating whether the information obtained is audit evidence. Specifically, some ASB members expressed the view that the requirement “should consider” might be too weak especially as it relates to relevance and reliability of the information.	See disposition below under “March 8, 2019 ASB Conference Call” (Item 7).
6. Relocate significant portions of the application material related to external information sources (EIS) to an appendix. Reconsider the	The Task Force relocated the content to an appendix and added an application material paragraph to highlight the difference in testing

Audit Evidence
ASB Meeting, May 20-23, 2019

<i>ASB Comment</i>	<i>Task Force Disposition</i>
application material dealing with the accuracy and completeness of external information sources.	the completeness and accuracy of external information (see paragraph A43).
<i>March 8, 2019 ASB Conference Call</i>	
<p>7. Discussion involved the use of words to describe the work effort contemplated for the requirements of the proposed SAS. In prior ASB discussions, requests had been made of the Task Force to replace the words “should consider” with words such as “evaluate” or “assess” to better describe and strengthen the expected work effort in various requirements of the proposed SAS. After further discussion, the ASB requested the Task Force to reconsider the terms used to describe expected work effort related to the requirements of the proposed SAS, taking into account how various terms such as “should consider,” “assess” and “evaluate” are used in other AU-C sections and use descriptors appropriate for each individual requirement.</p>	<p>The Task Force reconsidered the words used to describe the “work effort” in paragraphs 10-14. The Task Force concluded that the requirement representing the auditor’s overarching work effort to conclude whether sufficient appropriate audit evidence has been obtained should remain as stated at extant AU-C 330.28. The Task Force also concluded that the work effort related to determining whether information to which audit procedures have been applied is actually audit evidence should be articulated as “should evaluate.” In doing so, the auditor then “considers” relevance and reliability in the context of its sources and whether the information corroborates or contradicts the assertions in the financial statements. The bases for these conclusions are as follows:</p> <ul style="list-style-type: none"> • “Evaluate” is used throughout GAAS (e.g., in AU-C 315 to evaluate whether...) to indicate a conclusion needs to be drawn. • “Assess” is used particularly again in AU-C 315 to indicate the auditor is to identify and quantify something (as in risk assessment and assessing ROMMs). • “Should consider” is identified as a presumptively mandatory requirement in AU-C 200.25 and .A79. Therefore, the auditor cannot just “blow by” this consideration (a concern of some ASB members).
<p>8. With respect to the proposed definitions of “appropriateness” and “sufficiency,” the ASB requested the task force to consider how these proposed definitions are aligned with the</p>	<p>The Task Force has proposed conforming amendments to AU-C 200 to align the definitions of appropriateness and sufficiency in</p>

Audit Evidence
ASB Meeting, May 20-23, 2019

<i>ASB Comment</i>	<i>Task Force Disposition</i>
auditor's overall objectives and related definitions in AU-C 200.	the proposed standard to those definitions in AU-C 200.
9. A member noted that the auditor forms numerous conclusions in performing an audit. As the proposed SAS currently indicates that sufficient appropriate audit evidence has been obtained when the auditor is persuaded to draw a conclusion, the question was raised as to whether the auditor then needs to obtain sufficient appropriate audit evidence for every conclusion reached during an audit. The task force was requested to clarify how requirements apply to various conclusions reached during an audit.	The Task Force has added application material to paragraph A15 to indicate that the auditor's draws many conclusions during an audit and while each conclusion reached should be supported by audit evidence, the more significant the conclusion being reached the more persuasive the audit evidence should be (analogizing to AU-C 330.07.b.)
10. A member expressed the view that the scope section of the proposed SAS should include guidance regarding how the proposed requirements of the proposed SAS interact with the requirement in paragraph 28 of AU-C section 330 which states the auditor is required to conclude whether sufficient appropriate audit evidence has been obtained.	The Task Force made the edits as suggested (see paragraph 3).

Questions for the ASB

1. Does the ASB agree with the Task Force's disposition of the issues summarized above?

External Confirmations

Extant AU-C section 505 addresses the auditor's use of confirmation procedures to obtain audit evidence, in accordance with the requirements of AU-C section 330. In the conforming amendments to the proposed SAS, the Task Force has included an amendment that would eliminate the requirement that a confirmation be written, that is, an oral confirmation would be permissible under AU-C section 505. In response to comments received from ASB members, the Task Force discussed whether an oral confirmation is as reliable as a written confirmation. The Task Force concluded that an oral confirmation is as reliable as a written confirmation provided that the oral request is made to an appropriate individual and is documented by the auditor. As part of this discussion, the Task Force considered the following PCAOB requirement (paragraph 29 of AS 2310).

...In addition, the auditor should consider requesting the purported sender to mail the *original* confirmation directly to the auditor. Oral confirmations should be documented in the workpapers. ***If the information in the oral confirmations is significant, the auditor should***

request the parties involved to submit written confirmation of the specific information directly to the auditor. [Emphasis added]

The above PCAOB requirement raises the issue whether in certain situations (for example, when the information in the confirmation is significant), the confirmation should be written. The Task Force believes that this issue is addressed by:

- a. Paragraph 7*b.* of extant AU-C section 330 which requires that in designing the further auditor procedures to be performed, the auditor should obtain more persuasive audit evidence the higher the auditor's assessment of risk, and
- b. the attributes and factors being introduced in the proposed SAS that the auditor would consider in evaluating whether the information is sufficient appropriate audit evidence would address this situation. More specifically, if an auditor obtains an oral confirmation and by applying the proposed SAS, the auditor concludes that the audit evidence obtained does not sufficiently address the risk of material misstatement for a particular assertion, the auditor would be required to modify his or her procedures, for example, obtaining a written information. This position is supported by Paragraph 29 of extant AU-C 330.

Questions for the ASB

2. Does the ASB agree with the Task Force's conclusion that an oral confirmation can be as reliable as a written confirmation? Does the ASB agree that extant AU-C section 330 combined with the attributes and factors in the proposed SAS would assist the auditor in concluding whether an oral confirmation is appropriate or concluding that an oral confirmation should be supplemented by a written confirmation?

Items Presented

Agenda Item 2 – Issues Paper

Agenda Item 2A – AU-C section 500 Exposure Draft_marked from March ASB call

Agenda Item 2B – AU-C 500 Table_Proposed Standard – clean

Agenda Item 2C – AU-C 500 Table_Proposed Standard – marked from extant

Agenda Item 2D – AU-C 500 Traditional Format

Mr. Dohrer will refer to the Agenda Items 2 and 2A in leading the discussion.

Appendix 1

Emerging Techniques and Technologies

Emerging audit techniques, such as ADA, and emerging technologies such as, Artificial Intelligence (AI) and Blockchain, offer both challenges and opportunities that will affect audits of financial and nonfinancial information into the foreseeable future. For the purposes of this paper, the phrase “emerging techniques and technologies” will be used to refer to both emerging audit techniques and emerging technologies. Much activity has been ongoing in the US and internationally regarding how the profession should respond to such emerging techniques and technologies, including consideration of whether changes need to be made to the professional standards. In 2015, the IAASB organized a Data Analytics Working Group (DAWG), chaired by this Task Force’s chair, to inform the IAASB about how and when to respond to developments in technology in the most effective way. Since then, the DAWG has undertaken a comprehensive outreach campaign with various stakeholders that include accounting firms, national standard setters, audit regulators, investors and preparers, among others. In addition, the topic has been presented and discussed with the IAASB at various meetings. These outreach activities and IAASB discussions led to the release in September 2016 of Request for Input, *Exploring the Growing Use of Technology in the Audit, With a Focus on Data Analytics*. The Request for Input sought feedback from stakeholders about various aspects of the use of emerging techniques and technologies. In response to the Request for Input, the DAWG received over 55 comment letters. In January 2018, the DAWG published a Feedback Statement which summarizes the input received from Responders. The key messages were as follows:

- Responders expressed support for the direction of the project.
- The ISAs aren’t “broken” and should remain principles-based but need to reflect the digital era in application guidance. Responders overwhelmingly described a strong desire for practical guidance on the use of data analytics technology. Most responders believe that the principles in the extant ISAs are still appropriate and accommodate the use of data analytics and cautioned against prematurely rushing to change requirements in the standards.
- In connection with standard-setting activity, the IAASB should first consider a project to amend ISA 500, *Audit Evidence*.
- Applying Professional Skepticism when using data analytics is important.

The DAWG continued to advance the project by contributing proposed material to IAASB task forces working on IAASB projects involving risk assessment and quality control, continuing its outreach activities, and providing periodic updates at the IAASB meetings. The IAASB has not moved to a formal standard setting phase because the IAASB is devoting its resources to other standard setting priorities. However in March 2019, the IAASB established an Audit Evidence Working Group (AEWG), chaired by the AICPA Audit Evidence Task Force’s Chair, to conduct research and develop a project proposal for standard setting. The AICPA proposed revisions to AU-C section 500 form a significant input to the AEWG.

In the US, the AICPA has undertaken many activities and projects related to the use of ADA and emerging techniques and technologies. In late 2017, in response to work performed by a working group comprised of members from the ASB and the ASEC, the AICPA released a nonauthoritative guide, *Guide to Audit Data Analytics* (ADA Guide), which discusses the use of ADA in audit engagements.

In March 2018, the AICPA coordinated with CPA Canada to co-publish a [white paper on the implications of Blockchain to the audit and assurance profession](#).

Professional Skepticism

In recent years, the IAASB has had a working group considering the topic of Professional Skepticism. The projects on Quality Control and Group Audits, and Professional Skepticism represented the three areas for which the IAASB sought input from responders in its Invitation to Comment (ITC), *Enhancing Audit Quality in the Public Interest*, issued in January 2016.

As explained in the ITC, the ISAs explicitly recognize the fundamental importance of Professional Skepticism.¹ Professional Skepticism includes being alert to, for example, audit evidence that contradicts other audit evidence obtained, or information that brings into question the reliability of documents or responses to inquiries to be used as audit evidence. The auditor may accept records and documents as genuine unless the auditor has reason to believe the contrary. Nevertheless, the auditor is required to consider the reliability of information to be used as audit evidence.

The key issues identified with respect to Professional Skepticism are as follows:

- Questions have been raised about how auditors can more clearly demonstrate the application of Professional Skepticism, how to better describe the basis for the auditor's professional judgments and how the auditor's mindset has affected the nature, timing and extent of audit procedures performed as well as the critical evaluation of audit evidence.
- Concern about instances in which auditors did not appropriately apply Professional Skepticism in their audits is a recurring theme in audit inspection findings globally and has been a key issue in discussions about audit quality. Regulatory bodies have suggested that enhanced Professional Skepticism by auditors will contribute significantly to improving the quality of audits and that firms should prioritize efforts in this area.
- The existence of many ways to describe the application of Professional Skepticism indicates that the concept of Professional Skepticism, and the expectations of how auditors should appropriately apply it, may need to be more clearly articulated in our standards.

Given this background and the issues related to Professional Skepticism identified above, the Task Force has preliminarily taken an approach to 1) accept the definition of Professional Skepticism

¹ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With International Standards on Auditing*, defines Professional Skepticism as An attitude that includes a questioning mind, being alert to conditions that may indicate possible misstatement due to fraud or error, and a critical assessment of audit evidence.

as set out in AU-C 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*, 2) address these issues by proposing to interweave the concepts surrounding Professional Skepticism throughout AU-C section 500 and 3) attempting to explain auditor performance that would demonstrate the application of Professional Skepticism when obtaining and assessing the sufficiency and appropriateness of audit evidence. Simply having a separate section of a standard labeled “Professional Skepticism” or simply sprinkling the words “Professional Skepticism” throughout the standard is not sufficient to achieve the objectives outlined above.