



Agenda Item 2

Audit Evidence

Objective of Agenda Item

To discuss revisions to the proposed Statement on Auditing Standards, *Audit Evidence* (proposed SAS) after considering the comment letters received in connection with the exposure draft.

Task Force

Task Force members are:

- Jay Brodish, PwC, Chair (supported by Kathy Healy)
- 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 (supported by Sally Ann Bailey)
- Eric Turner, CPA Canada and IAASB Member
- Alan Young, EY and IAASB AEWG Correspondent Member

Bob Dohrer, Chief Auditor, AICPA and Vanessa Teitelbaum, CAQ Technical Director, serve as observers of the task force.

Background

The overall objective of the revisions to the proposed SAS is to address the evolving nature of business and audit services, specifically 1) use of emerging technologies by both preparers and auditors, 2) audit data analytics (ADA), 3) the application of professional skepticism, 4) the expanding use of external information sources as audit evidence, and 5) more broadly, the accuracy, completeness, and reliability of audit evidence.

On June 20, 2019, the Auditing Standards Board (ASB) issued the Exposure Draft related to the proposed SAS. The Exposure Draft period ended September 18, 2019.

At the October 2019 ASB meeting, the ASB discussed the significant issues arising from the comment letters received in response to the Exposure Draft related to the proposed SAS and

provided direction to the Task Force based on the responses received from the comments. Significant comments or observations by the ASB members were as follows:

1. The attributes and factors that the auditor would be required to consider in making the evaluation of whether sufficient appropriate audit evidence has been obtained and whether the diagram included in the proposed SAS should be retained. After discussion, the ASB agreed to remove the diagram from the proposed SAS, but the diagram (with some revisions to address the comments by responders) could be used in an exhibit to AU-C 500 or as other guidance material.
2. The revised definitions, in particular 1) audit evidence, 2) appropriateness, and 3) sufficiency. After discussion, the ASB agreed to restore the extant definitions of appropriateness and sufficiency. The ASB also agreed to add application material to more fully explain the terms *persuasiveness*, *quantity* and *quality* and how they relate to and interact with each other.
3. The flow of the requirements. In the Issues Paper, the Task Force provided indicative drafting to address feedback in the comment letters. The ASB was supportive of the direction of the indicative drafting and provided some suggestions for improvement.
4. The guidance related to automated tools and techniques. The ASB supported the Task Force views on this matter and supported exploration of adding examples and/or guidance.
5. External confirmations. After discussion, the ASB agreed to no longer consider the proposed conforming amendments that would have permitted oral confirmations. However, the ASB directed the Task Force to consider adding application material that would address the use of electronic means to obtain external written confirmations and address the use of inquiry as an audit procedure.
6. Audit documentation. The ASB supported the Task Force suggestions to make clear in the application material that the proposed SAS is not intended to create incremental documentation requirements.
7. Linkage to other standards. The ASB supported the Task Force views and approach on this matter.
8. Professional skepticism. The ASB supported the Task Force views and approach on this matter.
9. Relocation of Management's Specialists content. The ASB supported the Task Force recommendation to relocate the content regarding use of management's specialists currently in AU-C section 500. After discussion, the ASB agreed to relocate this content to a separate standard.

On December 6, 2019, the ASB held a conference call to discuss proposed changes made in response to the comment letters to the introduction, definitions, objective, requirements, and certain specific elements of the application material related to the proposed SAS. The discussion in January 2020 is aimed at substantially finalizing the scope, definitions and the requirements and a further discussion of the application material. The ASB current Project Plan is targeting approval of the final SAS at its May 2020 meeting.

Matters for the ASB Consideration

Flow of Requirements

At its December 6 teleconference, the ASB discussed the flow of requirements in paragraphs 7 and 8 of the proposed SAS. The ASB provided suggestions to revise the flow of the requirements. In particular, the ASB suggested improvements to paragraph 8 that addresses whether the information is sufficiently precise and detailed for the auditor's purposes (paragraph 9a) and obtaining audit evidence about the accuracy and completeness of the information (paragraph 9b). The Task Force believes the requirement to evaluate whether the information is sufficiently precise and detailed for the auditor's purposes should apply in all cases. However, the Task Force acknowledges the auditor may not be able to obtain evidence about the accuracy and completeness of information to be used as audit evidence, for example, in situations in which the auditor obtains information from certain external information sources. Accordingly, the clause "as necessary" has been relocated to paragraph 7b.

Questions for the ASB

1. What are the ASB's views on the flow of the requirements in paragraphs 7 and 8 of the proposed SAS as redrafted?

Automated Tools and Techniques

In the Exposure Draft, the ASB included several examples of the use of automated tools and techniques in the application material of the proposed SAS. The intent of these examples was to illustrate how the use of automated tools and techniques may impact the auditor's consideration of information to be used as audit evidence and, recognize more prominently in the proposed SAS the increased use of automated tools and techniques. More specifically, the application material contained several examples that included the use of Audit Data Analytics as a method of obtaining audit evidence. Upon further review of the application material, the Task Force noted that in some of these examples "audit data analytics" was used where reference more broadly to other types of automated tools and techniques would be more appropriate. For example, paragraph A38 of the Exposure Draft contains the following guidance about audit data analytics:

A38. The auditor's evaluation of information to be used as audit evidence may be enhanced by the use of automated tools and techniques *such as audit data analytics* that may enable the auditor to aggregate and consider information obtained from multiple sources. Audit data analytics are described as the analysis of patterns, identification of anomalies, or extraction of other useful information in data underlying or related to the subject matter of an audit through analysis, modeling, or visualization.

A concern was expressed that the use of the term "audit data analytics" may not have been precisely used throughout the application material and in certain examples, referencing use of automated tools and techniques more broadly would be appropriate.

To address these concerns, the Task Force decided to revise the application material to better explain the different forms of automated tools and techniques as follows:

A4. Audit evidence is cumulative in nature and is obtained primarily through the performance of one or more audit procedures on information obtained during the course of the audit. The auditor may also use automated tools and techniques such as audit data analytics, artificial intelligence, machine learning, remote observation tools, or robotic process automation as a means to obtain audit evidence. The auditor's evaluation of information to be used as audit evidence may be enhanced by the use of automated tools and techniques, which may enable the auditor to aggregate or disaggregate information, or consider information obtained from multiple sources. For example, audit data analytics may enhance the auditor's ability to analyze patterns, identify anomalies, or extract other useful information in data underlying or related to the subject matter of an audit through analysis, modeling, or visualization.

The Task Force then deleted the specific references to audit data analytics in some of the examples, thereby making the examples broader than just for audit data analytics and running more generally to use of automated tools and techniques.

Questions for the ASB

2. What are the ASB views about the revisions to the application material to better explain the use of automated tools and techniques?

Sufficiency of Audit Evidence

The Task Force edited paragraph A12 of the proposed SAS to make it clearer that the auditor's evaluation whether sufficient appropriate audit evidence has been obtained in accordance with AU-C section 330 is not solely dependent upon the quantity or measurement of audit evidence; rather it is dependent upon the persuasiveness of the audit evidence. The application material has been amended to note that audit evidence is sufficient when an experienced auditor would be persuaded to draw conclusions for the auditor's purposes. Revised paragraph A11 reads as follows:

A12. AU-C section 330 requires that the higher the assessed risks of material misstatement, the more persuasive the audit evidence required to support the conclusion may need to be. While *sufficiency* is defined as the measure of the quantity of audit evidence, *persuasiveness* may not be dependent solely upon the measurement of the quantity of audit evidence. Rather, *persuasiveness* contemplates the auditor obtaining an amount of appropriate audit evidence that is sufficient for the auditor to draw reasonable conclusions for the intended purposes. Audit evidence is sufficient when an experienced auditor would be persuaded to draw conclusions for the auditor's intended purposes.

Questions for the ASB

3. What are the ASB views about the revisions to paragraph A12 to better explain the concept of when sufficient appropriate audit evidence has been obtained?

Auditor Bias

In the proposed SAS, an attribute of audit evidence that the auditor would consider in evaluating information to be used as audit evidence was susceptibility to bias, including auditor bias. As noted by the Task Force at the October 2019 ASB meeting, comment letter responders raised issues with respect to including the concept of auditor bias as an attribute of audit evidence, questioning whether it was appropriately placed in AU-C section 500.

At its December 6, 2019 teleconference, the ASB decided that guidance with respect to auditor bias is an important notion to incorporate in GAAS but suggested AU-C section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*, would be a more appropriate location for this guidance. In response, the Task Force has drafted the consequential amendment to AU-C section 200 (taken from paragraph A28 of proposed ISA 220. Proposed consequential amendment is shown in ***bold italics***):

Professional Skepticism (Ref: [par. .17](#))

...

.A26 The auditor neither assumes that management is dishonest nor assumes unquestioned honesty. The auditor cannot be expected to disregard past experience of the honesty and integrity of the entity's management and those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the auditor of the need to maintain professional skepticism or allow the auditor to be satisfied with less than persuasive audit evidence when obtaining reasonable assurance.

A26a. Unconscious or conscious auditor biases may affect the auditor's professional skepticism and professional judgment, including for example, in the design and performance of audit procedures, or the evaluation of audit evidence. Examples of unconscious auditor biases that may impede the exercise of professional skepticism, and therefore the reasonableness of the professional judgments made by the auditor in complying with the requirements of this proposed SAS, may include:

- ***Availability bias, which involves considering information that is easily retrievable from memory as being more likely, more relevant and more important for a judgment.***
- ***Confirmation bias, which involves seeking, and treating as more persuasive, information that is consistent with initial beliefs or preferences.***
- ***Overconfidence bias, which involves overestimating one's own abilities to perform tasks or to make accurate assessments of risk or other judgments and decisions.***

- *Anchoring bias, which involves making assessments by starting from an initial numerical value and then adjusting insufficiently away from that initial value in forming a final judgment.*

Questions for the ASB

4. What are the ASB views with respect to the proposed consequential amendment to AU-C section 200 to address the concept of auditor bias?

Authenticity

Authenticity is another attribute of auditor evidence that the auditor would consider in evaluating information to be used as audit evidence. The Exposure Draft contained the following guidance to explain authenticity as an attribute of audit evidence [footnote omitted]:

A26. AU-C section 240, *Consideration of Fraud in a Financial Statement Audit*, addresses circumstances in which the auditor has reason to believe that a document (that is, information) may not be authentic or may have been modified without that modification having been disclosed to the auditor. AU-C section 240 further explains that an audit performed in accordance with GAAS rarely involves the authentication of documents, nor is the auditor trained as, or expected to be, an expert in such authentication.

A27. When information has been transformed from its original medium (for example, documents that have been scanned or otherwise transformed to electronic form), the reliability of that information may depend on the controls over the information's transformation and maintenance. In some situations, the auditor may obtain audit evidence about the authenticity of electronic information by testing controls over the transformation and maintenance of the information. In other situations, the auditor may determine that additional substantive procedures to address the authenticity are needed (for example, inspecting underlying original documents to validate the authenticity of information in electronic form).

Some responders to the Exposure Draft expressed the view that this guidance is not clear because the paragraphs seem to be contradictory, for example, paragraph A26 explains that an auditor in accordance with GAAS rarely involves the authentication of documents... However, paragraph A27 explains that in some situations, the auditor may need to perform additional procedures to obtain audit evidence about the authenticity of information... To address these comments, the Task Force edited paragraphs A26 and A27 as follows [footnote omitted]:

A35. When information has been transformed from its original medium (for example, documents that have been filmed, digitized, or otherwise transformed to electronic form), the reliability of that information may depend on the controls over the information's transformation and maintenance. In some situations, the auditor may test controls over the transformation and maintenance of the information. In other situations, the auditor may determine that additional procedures are needed to address reliability (for example, inspecting underlying original documents to validate the authenticity of information in electronic form). However, an audit performed in accordance with GAAS rarely involves

the authentication of documents, nor is the auditor trained as, or expected to be, an expert in such authentication. When the auditor identifies conditions that cause the auditor to believe that a document may not be authentic, that terms in a document may have been modified but not disclosed to the auditor, or that undisclosed side agreements may exist, the auditor may need to perform additional procedures, including procedures to evaluate authenticity. Such procedures may include

- confirming directly with the third party.
- using the work of a specialist to assess the document's authenticity.

Questions for the ASB

5. Does the ASB agree with the revisions to paragraph A35 to better explain authenticity as an attribute of audit evidence?

Automated Tools and Techniques Examples

At its December 6, 2019 teleconference, the ASB discussed an example provided by a comment letter responder on the use of audit data analytics to illustrate the level of specificity in examples that might be included in the proposed SAS. The ASB decided that while the proposed example provided very useful guidance, the example was too detailed to be included in the application material. That example could be better included in a separate document as a practice aid or other guidance material to the proposed SAS. The Task Force continues to believe that a detailed example within the application material would be useful to illustrate how the use of data analytics could meet more than one objective but agrees with the ASB feedback that the example could be more high-level. Accordingly, the Task Force drafted a different example with less detailed guidance as follows:

A62. An auditor may use automated tools and techniques to perform both a risk assessment procedure and a substantive procedure concurrently. For example, an audit data analytic was used to analyze a population to identify transactions that meet certain characteristics in order to identify and assess risks of material misstatement. The audit data analytic considered multiple attributes of the population (for example customers with significant fluctuation in volume, and transactions for which the invoice does not match the shipping document) and produced a risk score for each transaction. The transactions were then grouped based on risk scores. For those transactions that had a low risk score, no additional substantive procedures were necessary for that population if the auditor determined the audit data analytic was sufficiently precise for the auditor to conclude the population did not warrant further investigation. For the low risk grouping, the audit data analytic was used to simultaneously achieve the objective of both a risk assessment procedure and a substantive procedure.

Questions for the ASB

6. What are the ASB views about the revised example and its level of specificity?

Other Matters

At the October 2019 ASB meeting, the Task Force acknowledged that additional attributes of audit evidence such as the notions of direct and indirect audit evidence and timeliness of providing information to be used as audit evidence, had been suggested by the comment letter responders. These suggestions remain open items that the Task Force still needs to address and may be concepts better placed in AU-C sections other than AU-C section 500.

Items Presented

Agenda Item 2 – Issues Paper

Agenda Item 2A – Proposed SAS, marked from ED

Agenda Item 2B – Proposed SAS, clean

Agenda Item 2C – Forepart Only_marked from the December 6 ASB teleconference

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