

April 24, 2023

IFAC Small and Medium Practices Advisory Group Response to the IAASB's Exposure Draft of proposed International Standard on Auditing 500 (Revised), Audit Evidence

INTRODUCTION

The IFAC SMP Advisory Group (SMPAG) is pleased to respond to the IAASB (the Board) Exposure Draft of proposed International Standard on Auditing 500 (Revised) Audit Evidence (the ED). The SMPAG is charged with identifying and representing the needs of its constituents and, where applicable, to consider relevant issues pertaining to small- and medium-sized entities (SMEs). The constituents of the SMPAG are small- and medium-sized practices (SMPs) who provide accounting, auditing, assurance, and business advisory services principally, but not exclusively, to clients who are SMEs. Members and Technical Advisers serving the SMPAG are drawn from IFAC member organizations representing 25 countries from all regions of the world.

GENERAL COMMENTS

The SMPAG supports the IAASB's principles-based approach and limited number of requirements. We recognize the importance of the IAASB reacting to changes in the environment, including with advancements in different technologies being used both by auditors and entities they are auditing. This trend has accelerated with the Covid-19 pandemic, as auditors are generally using more automated tools and techniques, although it is also likely that such changes will be taking place more in large entities and large firms in the immediate future, not in the SME and SMP space.

We support the fact that ISA 500 (Revised) should apply to all information intended to be used as audit evidence, irrespective of its source. We also agree with the clarification that not all information is itself audit evidence. It is therefore important that the auditor's working papers make clear which information recorded by the auditor is intended to be used as audit evidence and has been subject to audit procedures, but it should not lead to additional documentation than would already be expected to be the case.

We are concerned about the number of changes proposed, the volume and nature of some of the application material and the numerous cross references to other ISAs. We believe that there could have been stronger evidence presented on what specific problems the Board is aiming to solve (i.e., what is going wrong in practice) and how the changes will have an impact on auditors' behavior, including clarity on documentation. Once the proposals are finalized, we recommend that the Board prepare a short summary and explanation of the changes, which includes the practical implications for SMPs and what they are expected to do differently in practice. This would also be extremely useful to Professional Accountancy Organizations and their members, as well as other stakeholders.

DETAILED COMMENTS

We have outlined our responses to the questions (in bold) below.

1. Is the purpose and scope of ED-500 clear? In this regard:

(a) Does ED-500 provide an appropriate principles-based reference framework for auditors when making judgments about audit evidence throughout the audit?

(b) Are the relationships to, or linkages with, other ISAs clear and appropriate?

The SMPAG believes a principles-based approach is appropriate and very important as an underpinning for auditors making judgements about audit evidence throughout the audit.

However, we are concerned that the scope and purpose could be unclear because ED-500 is viewed as a “reference framework” (paras. 14 and 32 of the explanatory memorandum). This may explain the numerous references to other standards, but it may not be clear to practitioners. We noted an extensive use of cross references, which could be distracting and not necessarily helpful. Extant ISA 500 could be compared to ISA 230, *Audit Documentation* because they both focus on matters that are pervasive through the entire audit process. These standards should be more general in scope and complemented by more specific requirements in other standards. This structure remains in ISA 230 but is now not clear for ED-500 because it is a “reference framework”, includes multiple references to other standards and has a high volume of “independent” application material.

In addition, it is difficult to assess the sufficiency and appropriateness of the proposals in ED-500 as the basis for a framework standard until the proposed revisions have been made to other relevant ISAs that underpin ISA 500.

The objective of ED-500 (para 6 (b)) includes to “evaluate information intended to be used audit evidence, and the audit evidence obtained, to provide a basis for the auditor to conclude whether sufficient appropriate audit evidence has been obtained”, which overlaps with the requirements in ISA 330, *The Auditors Responses to Assessed Risks* (ISA 330) to evaluate and “conclude whether sufficient appropriate audit evidence has been obtained” (para.26). Further distinction between ED-500 and ISA 330 on this matter could be considered to avoid duplicated work effort.

We also note that ISA 315 (Revised 2019) para.13 may need to be subject to a conforming amendment. As it is a currently worded there is a disconnect between “audit evidence that provides an appropriate basis” required by ISA 315 (Revised 2019) para.13 for “(a) the identification and assessment of risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels; and (b) the design of further audit procedures in accordance with ISA 330” and the concepts of “sufficient appropriate audit evidence” and “relevance and reliability” of information intended to be used as audit evidence in ED ISA 500 (Revised) paras. 8 and 9, respectively. The issue that needs clarification is what makes audit evidence sufficient and appropriate to “qualify” as an appropriate basis.

2. What are your views about whether the proposed revisions in ED-500, when considered collectively as explained in paragraph 10 above, will lead to enhanced auditor judgments when obtaining and evaluating audit evidence?

We acknowledge the need for the IAASB to address the public interest issues raised, in particular modernizing the standard to recognize the evolution in technology. However, there are concerns that it will ultimately just lead to more documentation and not substantially change or enhance SMP auditor behavior when obtaining and evaluating audit evidence. This is because many SMPs audit relatively straightforward and uncomplicated SMEs – those which are selling goods or services, that have simple accounting policies and are unlikely to push the boundaries on accounting treatments.

We are concerned about the volume of changes and number of cross references, as well as the level of examples, which in some instances could be considered as too basic and just reflecting common sense. For example, the bullets in A24 and A41 (except the second bullet that includes remote observations). We

would encourage the Board to consider including more useful examples, such as how technology is used as part of obtaining audit evidence.

There is also application material that either just duplicates the content in other ISAs (e.g., A26) or replicates what is in a requirement or in other application material paragraphs (e.g., A46 refers to and duplicates A12 and A65 refers back to A37 and A67 back to A48). We suggest the Board reconsider this textbook approach to focus ISA 500 (Revised) on key matters.

In our opinion, once the proposals are finalized, the Board should prepare a summary and explanation of the changes and clearly include the problems the Board is seeking to address, the practical implications for auditors and what they are expected to do differently. This will be very useful to assist with communicating the impact to SMPs.

3. What are your views about whether ED-500 has an appropriate balance of requirements and application material (see paragraph 11 above)?

Overall, the volume of application material to the requirements seems disproportionate with 93 paragraphs (up from 68 in the extant standard) for 7 requirements. The requirements are short and easily digestible, but we would strongly encourage the Board to consider whether some of the application material could be re-packaged as separate guidance outside of the standard (e.g., the examples) or shortened and made more concise. Duplication of material in other ISAs should also be avoided, as we observe some repetitiveness, long introductions to some paragraphs, as well as explanations for what is in other standards. In addition, some of the application material reads more like an audit theory textbook, which is useful, but may not be necessary to include in the standard (for example, what observation and confirmation means in the Appendix). We are concerned that it will be difficult for practitioners to focus on what is important and the application material may not meet the intended purpose because of the high volume.

Note, we do not consider that there is application material that should be elevated to requirements.

4. Do you agree that ED-500 is appropriately balanced with respect to technology by reinforcing a principles-based approach that is not prescriptive but accommodates the use of technology by the entity and the auditor, including the use of automated tools and techniques?

We agree with the IAASB's principles-based approach that accommodates the use of technology, including automated tools and techniques. We recognize the pace of change with technology developments and believe the Board has struck the right balance with the proposals, keeping to the principles-based approach and not being too prescriptive because of the range in entities being audited and technologies available for different audit firms. We support the inclusion of automation bias, the need for auditors to rely on specialists and emphasis on professional skepticism.

We welcome the IAASB expanding the information that could constitute audit evidence to include "digital information" (A41). However, there are concerns that "digital information" is not clearly articulated in the ED. Digital information could be broadly categorised to include:

- Digital data – information that is developed and/or stored within an IT system or obtained electronically from an external source.
- Digital documents – information, which is obtained in electronic format, for example an electronic confirmation.

- Information that has been transformed from its original medium into an electronic format, for example, a scanned version of an executed contract.

Using different categories of digital information may require the auditor to perform different audit procedures to evaluate its reliability. For example, for digital data, the auditor may design audit procedures to test the effectiveness of controls over their accuracy and completeness. Whereas, inspecting underlying original documents to validate the authenticity of information in electronic form will be more appropriate as an audit procedure when evaluating the reliability of information that has been transformed from its original medium into an electronic format. We recommend the IAASB to provide the distinction of, and clarity around different audit procedures that may be required to evaluate the reliability of the different categories of “digital information”.

Feedback indicated that it could be useful for the Board to develop examples of what is sufficient and appropriate audit evidence when using technology, but this should be published outside of the standard and not included in application material.

In this context, we also refer to our comment letter in response to the IAASB’s consultation on its future strategy and work plan in which we expressed our support the Board continuing to monitor and assess developments in technology and its application in an audit.

5. Do the requirements and application material in ED-500 appropriately reinforce the exercise of professional skepticism in obtaining and evaluating audit evidence?

The SMPAG believes that the requirements and application material appropriately reinforce the exercise of professional skepticism in obtaining and evaluating audit evidence.

In our view, para. 10 could be made clearer by changing the position of ‘information’ and ‘audit evidence’ – “...the auditor shall obtain information about the accuracy and completeness of information intended to be used as audit evidence’.

It is in assessing the “persuasiveness” of audit evidence where the auditor will apply professional skepticism, so we believe a definition would be helpful. In addition, the definition of professional skepticism in ISA 200¹ refers to a critical assessment of audit evidence without explaining exactly [we believe it is the persuasiveness] what about the audit evidence is to be critically assessed, so a conforming amendment to ISA 200 would be helpful.

6. Do you support the revised definition of audit evidence? In particular, do you agree with the “input-output model” that information can become audit evidence only after audit procedures are applied to it?

We support the revised definition audit evidence. We agree with the “input-output model” that information can become audit evidence only after audit procedures are applied to it.

7. Does the application material appropriately describe the interrelationship of the sufficiency, appropriateness and persuasiveness of audit evidence?

We acknowledge paragraph A6 in particular, which links persuasiveness to sufficiency and appropriateness. However, the fact that ED ISA 500 contains separate definitions of appropriateness and sufficiency each in the context “of audit evidence” is potentially misleading and misaligned with the

¹ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

statement in paragraph A14. The auditor's evaluation of the sufficiency of audit evidence is interrelated to its appropriateness, because – as explained in the last sentence of A14: obtaining more audit evidence cannot compensate for its poor quality. We suggest the definitions be phrased to be provided in the context of sufficient, appropriate audit evidence.

We refer to our response to question 5 above, and note that the IAASB did not support including a definition of “persuasiveness” in the standard. We suggest that this is given further consideration due to the differences in interpretation of what this word means by practitioners from different countries. In addition, in A13 on the appropriateness of audit evidence, an example could be helpful to explain as there was some confusion about what this means in practice. It is also unclear whether the effectiveness of the design of an audit procedure is expected to be documented (i.e., does this require the auditor to justify e.g., sample sizes or sampling methodology applied?).

8. Will the requirements and application material in ED-500 support an appropriate evaluation of the relevance and reliability of information intended to be used as audit evidence?

We are concerned that the implications of what is included in para. 9 may result in an expectation by regulators that practitioners should explicitly document the relevance and reliability of all information intended to be used as audit evidence. This could be very onerous and not significantly enhance audit quality. The change from ‘consider’ relevance and reliability to ‘evaluate’ implies a different work effort, which will result in practical challenges as auditors may be unsure about the level of work and documentation needed as the attributes may not be applicable every time. There are also concerns that one consequence could be that regulators then question how practitioners made their judgments and evaluations.

An area that could warrant further consideration is whether the wording in para. 11 (c) could have a dilutive effect on the responsibilities of the auditor when evaluating the information prepared by a management's expert. The paragraph requires the auditor to “Obtain an understanding about how the information prepared by that expert has been used by management in the preparation of financial statements”, which could be perceived as a lower-level requirement than what is currently required in the extant ISA 500 to “Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion”.

9. Do you agree with the separate conditional requirement to obtain audit evidence about the accuracy and completeness of information when those attributes are applicable in the circumstances?

We do not see an advantage in having the separate conditional requirement to obtain audit evidence about the accuracy and completeness of information when those attributes are applicable in the circumstances. The relative significance of attributes can vary, and the auditor may need to consider other attributes. The application material (A63-A65) is helpful, but there remains a concern about how much work an auditor needs to do to test the accuracy and completeness before the information can be relied upon as audit evidence.

As drafted, para. 9 and 10 together require the auditor to evaluate the relevance and reliability of information intended to become audit evidence and in so doing consider which attributes are applicable in the circumstances. However, where the attributes accuracy and completeness are applicable para. 10 requires the auditor to obtain audit evidence about these attributes and thus the auditor is required to loop back to para. 9 and evaluate the relevance and reliability of information to perform procedures before this can become audit evidence, potentially considering again that accuracy and completeness of the information

are applicable etc. Therefore, the auditor could potentially be required to obtain audit evidence ad infinitum (infinite regress). In our response to question 5 we suggest changes to the proposed wording of para. 10 that would address these concerns.

10. Do you agree with the new “stand back” requirement for the auditor to evaluate audit evidence obtained from the audit procedures performed as a basis for concluding in accordance with ISA 330 that sufficient appropriate audit evidence has been obtained?

We do not agree that the new “stand back” requirement is needed in ISA 500 (Revised) given the stand back in para. 26 of ISA 330, *The Auditor’s Responses to Assessed Risks*, which could be duly amended instead. There has been a trend in the latest ISA projects to include stand-back requirements. We are concerned that practitioners may be challenged when taking a holistic approach to all of them and trying to understand how they are supposed to work together in practice. We believe there should be a maximum of two stand backs – one on whether the auditor has obtained sufficient appropriate audit evidence and one on whether the financial statements are prepared in all material respects in accordance with the requirements of the applicable financial reporting framework (as required by para.12 ISA 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*).

There are significant concerns about the increased level of documentation that will be required by practice inspectors. We suggest that the IAASB to be clear on what amount of documentation is expected, so that inspectors are not expecting extensive documentation notes to support how it has been considered.

Further, there are a lot of cross-references to other standards. For example, in A84-A88 there are references to five other ISAs and these are mentioned eleven times. When the Board considers the clarity, understandability and practicality of application of the requirements and application material it may want to consider whether the current approach has the right balance and whether all are needed, particularly given the use of ‘evaluate’ in para. 13, as there could be challenges for practitioners understanding how much work effort and documentation is required.

11. Are there any other matters you would like to raise regarding ED-500? If so, please clearly indicate the requirement(s) or application material, or the theme or topic, to which your comment(s) relate.

There is a lack of consistency in use of terms “consistency/ inconsistency” and “corroboratory/ contradictory” evidence. It seems that consistency is being used in some cases to imply it includes corroboration, whereas the two are not the same.

Proposed A32 is unclear in its purpose. The addition of this paragraph appears to condone full population testing in automated tools and techniques, but its location and its wording makes it unclear. As it is under the heading of ‘Selecting specific items’ and therefore is not subject to sampling risk (as it is not a sample) makes sense. However, in A31 the use of selecting specific items is in effect impermissible to make conclusions related to the entire population. In a situation of full population testing, it is possible to obtain evidence regarding the entire population without the sampling risk (as it is not a sample). If the purpose of A32 is to allow to full population auditing techniques and to select items for testing based on the risk or other attribute permissible in A30, then there is an unintended consequence embedded in A31 that is impermissible as audit evidence on the population assessed.

In the recent IAASB [Non-Authoritative Support Material Related to Technology](#), Note 2, Note 6, and Note 7 could be in jeopardy of being impermissible viewpoints if it is impermissible to draw conclusions related to an entire population from a selection of the entire population. This could discourage the use of full

population testing concepts as the standards are unclear on the permissibility to draw conclusions related to the population.

Given the challenges we have highlighted about what all the changes to ISA 500 (Revised) would mean in practice, we would encourage the Board to give greater consideration to projects with narrow-scope amendments going forward, rather than opening up and changing all aspects of each ISA. This would make it easier to communicate the changes, explain the reasons and also help in managing the IAASB's resource constraints.

12. The IAASB is also seeking comments on the matters set out below:

(a) Translations—Recognizing that many respondents may intend to translate the final ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents note in reviewing ED-500.

(b) Effective Date—Recognizing that ED-500 is a substantive revision, and given the need for national due process and translation, as applicable, the IAASB believes that an appropriate effective date for the standard would be for financial reporting periods beginning approximately 18 months after approval of a final ISA. Earlier application would be permitted and encouraged. The IAASB welcomes comments on whether this would provide a sufficient period to support effective implementation of the ISA.

In line with our earlier comments, we are concerned with the pace of change and recommend the Board considers a longer period (perhaps 24 months) after the approval of the final ISA. In some countries, translating the standard can take a significant amount of time, which substantially reduces the actual implementation period.

CONCLUDING COMMENTS

We hope that the IAASB finds this letter useful. We are committed to helping the Board in whatever way we can as it finalizes this project.

Please do not hesitate to contact me should you wish to discuss matters raised in this submission.

Sincerely,



Monica Foerster

Chair, SMPAG