INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD (IAASB)
REQUEST FOR INPUT – EXPLORING THE GROWING USE OF TECHNOLOGY IN THE AUDIT, WITH A FOCUS ON DATA ANALYTICS

RESPONSE FROM ICAS TO THE IAASB

15 February 2017

Background

ICAS is a professional body for more than 21,000 world class business men and women who work in the UK and in more than 100 countries around the world. Our members have all achieved the internationally recognised and respected CA qualification (Chartered Accountant). We are an educator, examiner, regulator, and thought leader.

Almost two thirds of our working membership work in business; many leading some of the UK's and the world's great companies. The others work in accountancy practices ranging from the Big Four in the City to the small practitioner in rural areas of the country.

We currently have around 3,000 students striving to become the next generation of CAs under the tutelage of our expert staff and members. We regulate our members and their firms. We represent our members on a wide range of issues in accountancy, finance and business and seek to influence policy in the UK and globally, always acting in the public interest.

ICAS was created by Royal Charter in 1854.

General comments

We welcome the IAASB's decision to establish the Data Analytics Working Group (DAWG) to address the issues emerging from the increased use of technology in the audit and the overall objective of responding appropriately and timeously to how these developments in technology might fit into the current risk-based audit model.

We believe that the need for the IAASB to consider such developments is an essential part of its ongoing activities. There is a clear need to ensure that the auditing standards do not act as an unnecessary barrier to technological developments whilst at the same time ensuring that there is a proper understanding of their impact.

We believe that the extent of the application of data analytics in the audit of financial statements could best be described as a spectrum. Many audit firms are somewhere on this spectrum, but all are doing a range of different things, e.g. per the definition used in the paper, the simple extraction by the auditor of data from a client's accounting system to a spreadsheet to allow it to be interrogated is an example of data analytics in its simplest form. Therefore, some form of guidance on best practice in this evolving area would be welcomed by the profession in the short term although, ultimately, there may be a need for a more detailed review of the full suite of International Standards on Auditing (ISAs). Furthermore, at some stage consideration may need to be given as to what an audit is, and what it could be, in the light of technological advances.

Our responses to the specific questions in the request for input publication in relation to the growing use of technology in the audit, with a focus on data analytics, are set out below.

Specific Questions

The DAWG's work in this area is not done and the IAASB has an open mind as to the way forward. In addition to the matters addressed in this publication, the IAASB and the DAWG are requesting your input on the following questions:

Question (a) Have we considered all circumstances and factors that exist in the current business environment that impact the use of data analytics in a financial statement audit?

Response (a)

We believe that the DAWG has considered many of the circumstances and factors that exist in the current business environment that impact the use of data analytics in a financial statement audit but would like to highlight some areas for further consideration or where further investigation might be required.

The publication states that the use of data analytics offers opportunities for the auditor to obtain a more effective and robust understanding of the entity. However, whilst we agree and are supportive of the use, where applicable, of such techniques, one must be cognisant that there are also some potential downsides. For example, we have concerns that an over-reliance on the use of data analytics might lead to less direct interaction and discussion with the client about the entity's operational activities thereby potentially inadvertently reducing the extent of the auditor's understanding of the entity. The lack of face to face interaction has on occasion been flagged as a weakness in the manner in which the modern-day audit is undertaken. There is a potential danger that increased use of audit data analytics could merely compound that problem. Additionally, as highlighted in the DAWG's paper, we have concerns that the use of data analytics could create an expectation gap leading to a false impression that the client's data is 100% correct and to unrealistic expectations being placed on the auditor's responsibility in relation to the detection of fraud.

However, we recognise that the automation of some of the more routine and repetitive audit tasks might free up at least some auditor time. This would allow auditors to place even more focus on the higher risk areas of the audit encouraging greater application of judgement and scepticism. It is often the forensic type of work that is seen as more appealing to junior auditors so the use of data analytics might present an opportunity for such staff (subject to them having appropriate training) to have greater involvement in this type of work making the audit profession more interesting and attractive.

There is also a danger of auditors straying into more of a business advisory role through the implementation and use of data analysis techniques and the interpretation of some of the outputs/reports that these techniques generate. This could have implications for auditor independence. Furthermore, it could lead to some SMPs withdrawing from the audit market and to them providing more of a business advisory service, particularly for those entities who have elected for an audit voluntarily. We are aware that the largest audit firms have invested heavily in technology to enable them to incorporate the use of data analytics in the audit process for their largest clients and this raises concerns that, because audit firms operating at the SME end of the audit market may not be able to invest in such technology, a two-tier audit system might emerge.

Whilst we agree with the statement in paragraph 20 of the DAWG paper concerning the increased access that SMEs should have to such technology, we would like to highlight that in the SME market, it is not only the cost of the investment in the technology itself, but also the cost of the related training and/or specialised staff, that has restricted the use of Data Analytics during the audit process for this sector.

Larger organisations themselves are also starting to increase their own use of data analytics. This will potentially include an entity's internal audit team. Practical issues might start to be encountered where auditors have to assess to what, if any, use they can make of particular work that has been undertaken by the entity's internal audit staff. Whilst we accept this is not a new issue we do believe this issue will be exacerbated by the client's use of data analysis techniques.

The training and skillsets required by auditors to effectively incorporate the use of data analysis techniques within the audit process is an area which should also be considered. Audit teams of the future might also need to be composed of different types of individuals from more diverse backgrounds with a broader range of skills and experience. This will rely on auditors who possess pure data analysis skills as well as an understanding of the purpose and objective of the test being undertaken.

ICAS and the Financial Reporting Council (FRC) recently commissioned two pieces of research on the skills and competencies required for the auditor of the future and published a Steering Committee Report which set out a series of recommendations for the future of the profession as a whole. These publications would be a valuable source of reference for the DAWG as part of their ongoing work in this area.

Regardless of the extent to which data analytics is applied in the audit process, we do not believe that it will completely remove the requirement for the auditor to exercise professional judgement and professional scepticism over the way the evidence that is generated by these techniques is interpreted and the extent to which it is judged to represent sufficient and appropriate audit evidence.

Finally, there may be issues around client confidentiality/data protection issues in relation to the extent to which the auditor is granted access to confidential and sensitive information and the level of security and anti-corruption measures that have been implemented to protect the integrity of the information. There may also be jurisdictional specific issues in relation to the ability for the auditor to gain access to the relevant data.

Question (b) Is our list of standard-setting challenges accurate and complete?

Response (b)
We believe that the discussion paper lists many of the standard-setting challenges but we have some further points of detail for consideration. Practical application of data analytics techniques in the audit process presents a significant challenge with regards to satisfying the regulatory requirement for sufficient, appropriate audit evidence and interaction with current auditing standards. At the moment, data analytics are being used in practice however, the auditing standards have not been updated to reflect the complexities of the modern business environment and auditors are faced with the challenge of trying to determine to what extent their data analysis techniques can be relied upon during the audit process.

The DAWG paper discusses the issue above and whether the use of data analytics should be classified as risk assessment procedures, substantive tests or tests of control. Greater clarity in this area would be welcome.

The reliability of the data being produced is likely to be a challenge and might still require some controls testing to ensure that sufficient, reliable and appropriate audit evidence is being produced, which reinforces the uncertainty around how the use of data analytics interacts with, and satisfies, the current ISA requirements. For example, the discussion paper asks, in paragraph 19 (e): What is the role of controls testing when auditors analyse 100% of the transactions in a particular area of the audit?

This statement assumes that all transactions that should have related to a population have been properly recorded – it does not necessarily take account of transactions that may not have been reflected in the accounting records i.e. it does not appropriately consider the issue of completeness. We do accept that certain audit data analytic techniques may offer the opportunity of testing other data sources to help to address the possibility of such transactions not being recorded.

Question (c) To assist the DAWG in its ongoing work, what are your views on possible solutions to the standard-setting challenges?

Response (c)
We support the need for auditing standards to remain principles-based and sufficiently flexible and adaptable in order that they are relevant in a changing business environment.

There might also be a case for a move towards more outcome/objective based auditing standards to ensure that the standards remain relevant and do not lag behind technological developments and changes in the business environment. We are therefore very supportive of the comments made at paragraph 17 of the discussion paper: *"At the same time, auditing standards should also be able to accommodate developments (such as technology advancements) that occur in the future, without needing to be in a continual state of change. While significant technological developments have occurred to date, including in the area of data analytics, further development and analysis (such as academic research) is anticipated in the near future."*

Question (d) Is the DAWG's planned involvement in the IAASB projects currently underway appropriate?

Response (d)
We agree that the DAWG's planned involvement in the IAASB projects currently underway is appropriate. Whilst we believe that ultimately a review of the current ISAs may be necessary, in the short term there is a more pressing need for guidance in the use of audit data analytics as part of the audit process and therefore the issue of staff guidance notes or international auditing practice notes (IAPNs) would appear more appropriate at this stage.

Question (e) Beyond those initiatives noted in the Additional Resources section of this publication, are there other initiatives of which we are not currently aware of that could further inform the DAWG's work?

Response (e)
The Financial Reporting Council, FRC, in the UK has just published a Thematic Review on the use of Data Analytics in the Audit of Financial Statements [1]which could help to inform the DAWG's work.

Question (f) In your view, what should the IAASB's and DAWG's next steps be? For example, actions the IAASB and DAWG are currently considering include:
(i) **Focusing attention on revisions, where appropriate, to ISAs affected by the IAASB's current projects.**
(ii) **Exploring revisions to ISA 520.**
(iii) **Hosting one or more conferences with interested stakeholders to collectively explore issues and possible solutions to the identified challenges.**
(iv) **Continuing with outreach and exploration of issues associated with the use of data analytics in a financial statement audit, with a view towards a formal Discussion Paper consultation in advance of any formal standard-setting activities**

Response (f)
We believe that the IAASB and DAWG have to consider all of the above possible activities. IAASB should undoubtedly continue its programme of outreach with all interested stakeholders to explore possibilities for the use of, and application of, audit data analytics and potentially other technological advancements to improve the audit process and help improve the appeal of audit as a career destination. In particular, we believe it would be useful to seek the views of those charged with governance (TCWG) of entities where the auditors have applied audit data analytics techniques. This would provide an additional perspective as to the benefits of applying such techniques as well as addressing any concerns such as data security which might exist from an audited entity's perspective. This may help to better get an understanding on the extent of the conceptual challenge highlighted in the discussion paper i.e. "when performing an audit that involves data analytics, the engagement team may be requesting data from the entity and asking questions about that data that have not been asked in the past. The approach to certain areas of the audit where data analytics is utilized is also quite different to what the entity may be used to seeing, and the entity may be hesitant to provide all of the data being requested." It may also tackle the legal and regulatory challenges in relation to the access, and storage of client data. This interaction with TCWG might also provide some insight into whether the use of data analytics during the audit has made the process of communicating key audit findings any easier. We do accept that there will be jurisdictional differences, however, we do believe that there would be value in adopting such an approach.

We very much view proposal (iii) as merely being a subset of this outreach programme and one win which targeting key individuals such as TGWC would be of benefit.

---

[1] https://www.frc.org.uk/Our-Work/Publications/Audit-Quality-Review/Audit-Quality-Thematic-Review-The-Use-of-Data-Ana.pdf

Whilst we appreciate that short-term revisions to ISAs may ultimately be required we would rather that this was undertaken following the process described in proposal (iv) above. Such an approach should provide greater certainty to the extent of revisions that would be required to the ISAs. We also would again highlight our response to (d) above i.e. Whilst we believe that ultimately a review of the current ISAs may be necessary, in the short term there is a more pressing need for guidance in the use of audit data analytics as part of the audit process and therefore the issue of staff guidance notes or international auditing practice notes (IAPNs) might be more appropriate at this stage.

A further fact-finding exercise could also be undertaken to take stock of all the initiatives and guidance currently underway, or available, in this area which might inform and identify the IAASB's and DAWG's next steps. Regardless of one's views there is little doubt that consideration does need to be given to the fundamental question noted in the discussion paper i.e. "what the audit could or should be, including exploring whether there is a need to possibly start with a blank sheet of paper as attempting to retrofit data analytics into the ISAs today is likely not an effective approach."