Proposed Statement on Auditing Standards, Audit Evidence

Introduction

Scope of This Proposed SAS

1. This proposed Statement on Auditing Standards (SAS) explains what constitutes audit evidence in an audit of financial statements and addresses how an auditor evaluates attributes of information that are taken into account by the auditor when evaluating information to be used as audit evidence, by setting out attributes of information. Taking these attributes into account assists the auditor in maintaining professional skepticism. (Ref: par. A1)

2. The application of this proposed SAS assists the auditor in fulfilling the auditor’s responsibilities in other AU-C sections. This proposed SAS is to be read in conjunction with other AU-C sections, including those that address the auditor’s responsibilities to identify and assess the risks of material misstatement, design and implement responses to the risks of material misstatement identified and assessed by the auditor, and form an opinion on the financial statements. In particular, AU-C section 330, Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained, requires the auditor to conclude whether sufficient appropriate audit evidence has been obtained and thereby provides a basis for the auditor’s opinion. (Ref: par. A2)

3. The auditor’s overall conclusion in accordance with AU-C section 330 about whether sufficient appropriate audit evidence has been obtained is a matter of professional judgment and includes evaluating the following: Evaluating information to be used as audit evidence in accordance with this SAS assists the auditor in making that conclusion. (Ref: par. A2)

Commented [KKH1]: Edits made to respond to a comment to provide greater consistency with the requirements.

Commented [KKH2]: Board feedback about streamlining the language.

Issue 1 - Since the main point of this paragraph was to explain the interaction between AU-C section 330 and this SAS, this has been simplified.
Whether the assessment of the risks of material misstatement at the financial statement and at the relevant assertion levels remains appropriate

The information to be used as audit evidence in accordance with this proposed SAS

Effective Date

4. This proposed SAS is effective for audits of financial statements for periods ending on or after December 15, 2021.

Objective

5. The objective of the auditor is to evaluate information to be used as audit evidence, including the results of audit procedures, to inform the auditor’s overall conclusion about whether sufficient appropriate audit evidence has been obtained.

Definitions

6. For purposes of generally accepted auditing standards (GAAS), the following terms have the meanings attributed as follows:

**Appropriateness (of audit evidence).** The measure of the quality of audit evidence, that is, its relevance and reliability in providing support for the conclusions on which the auditor’s opinion is based. (Ref: par. A10)

**Audit evidence.** Information used by the auditor in arriving at the conclusions on which the auditor’s opinion is based. Audit evidence is information to which audit procedures have been applied, that is, the results of audit procedures. Audit evidence consists of information that corroborates or contradicts assertions in the financial statements. (Ref: par. A5A6–A11A9)

**External information source.** An external individual or organization external to the entity that provides information that is used by the entity in preparing the financial statements or that has been obtained by the auditor as audit evidence, when such information is suitable for use by a broad range of users. When information has been provided by an individual or organization acting in the capacity of management’s specialist, service organization, or auditor’s specialist, the individual or organization is not considered an external information source with respect to that particular information.

**Sufficiency (of audit evidence).** The measure of the quantity of audit evidence. The quantity of audit evidence necessary is affected by the auditor’s assessment of the risks of material

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Commented [JDB3]: Based on Board feedback.

Commented [KKH4]: Change made to go back to IAASB wording in the amendments to ISA 500 and avoid differences

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4 See AU-C section 402, Audit Considerations Relating to an Entity Using a Service Organization.

5 See AU-C section 620, Using the Work of an Auditor’s Specialist.
misstatement and the quality of the audit evidence obtained (that is, its appropriateness). (Ref: par. A10-A5, A9-A11-A12)

Requirements

Evaluating Information to Be Used as Audit Evidence

7. The auditor should evaluate information to be used as audit evidence by taking into account: (Ref: par. A12-A43)
   a. the relevance and reliability of the information, including its source and (Ref: par. A13-A14-A36-A39)
   b. whether such information corroborates or contradicts assertions in the financial statements. (Ref: par. A37-A40-A43-A43)

8. The auditor’s evaluation of the information to be used as audit evidence in accordance with paragraph 7 should include
   a. evaluating whether the information is sufficiently precise and detailed for the auditor’s purposes and (Ref: par. A42-A31-A44-A45-A44-A44)
   b. as necessary, obtaining audit evidence about the accuracy and completeness of the information as necessary. (Ref: par. A45-A31-A44-A45-A44-A44)

Audit Procedures as a Basis for Obtaining Concluding on the Sufficiency and Appropriateness of Audit Evidence

9. In evaluating information to be used as audit evidence, the auditor should consider whether the results of audit procedures provide a basis for concluding on the sufficiency and appropriateness of audit evidence obtained. (Ref: par. A45-A45-A46-A66-A66-A67)

Inconsistency in, or Doubts About the Reliability of Information to be Used as Audit Evidence or Inconsistencies in, Audit Evidence

10. The auditor should determine whether modifications or additions to audit procedures are necessary to resolve inconsistencies in, or doubts about the reliability of, information to be used as audit evidence or inconsistencies in audit evidence, including when:
   a. Information to be used as audit evidence obtained from one source is inconsistent with that obtained from another source
   b. The results of an audit procedure are inconsistent with the results of another audit procedure.
   (Ref: par. A67-A67-A68-A68-A68-A69)

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Application and Other Explanatory Material

Scope of This Proposed SAS (Ref: par. 1-31-3)

A1. AU-C section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards, defines professional skepticism and professional judgment. AU-C section 200 and AU-C section 330 provide application material about exercising professional skepticism and professional judgment.5 Paragraphs A18, A32, A35, A36, A40, A43, A62, and A64 are examples of paragraphs that describe ways in which the auditor can maintain professional skepticism.

A2. Paragraph 2 states that this proposed SAS should be read in conjunction with other AU-C sections, for example, AU-C section 330, which. For example, the objective of AU-C section 330 is for the auditor to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement through designing and implementing appropriate responses to those risks.10 AU-C section 330 also states that the auditor is required to do the following:

- Design and perform further audit procedures whose nature, timing, and extent are based on, and are responsive to, the assessed risks of material misstatement at the relevant assertion level.11
- Obtain more persuasive audit evidence the higher the auditor’s assessment of risk.12
- Conclude whether sufficient appropriate audit evidence has been obtained.13

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6 Paragraph .14 of AU-C section 200.
7 Paragraphs .A22 – .A31 of AU-C section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards.
8 Paragraphs .A22 – .A31 of AU-C section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards.
9 Paragraph A27 of AU-C section 200.
10 Paragraph .03 of AU-C section 330.
11 Paragraph .06 of AU-C section 330.
12 Paragraph .07b of AU-C section 330.
13 Paragraph .28 of AU-C section 330.
• Attempt to obtain further audit evidence if the auditor has not obtained sufficient appropriate audit evidence about a relevant assertion.\textsuperscript{14}

In addition, AU-C section 700, \textit{Forming an Opinion and Reporting on Financial Statements}, requires the auditor to conclude whether reasonable assurance has been obtained about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. The conclusions required by AU-C section 700 take into account, among other things, whether sufficient appropriate audit evidence has been obtained in accordance with AU-C section 330.\textsuperscript{15}

A3. The auditor’s evaluation of information to be used as audit evidence is not a formulaic exercise but rather is multidimensional and is dependent on the degree to which the attributes of information to be used as audit evidence influence the auditor’s evaluation.

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 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.

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\textbf{Definitions (Ref: par. 6)}
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\textbf{A5.} The quantity of audit evidence, in and of itself, is not determinative of its sufficiency when considering the persuasiveness of audit evidence. As the quality of evidence increases, the need for additional evidence decreases. However, obtaining more audit evidence may not compensate for its lack of appropriateness. Depending on the auditor’s consideration of relevance and reliability, information obtained from a single source may provide persuasive evidence.

\textbf{Audit Evidence}

\textbf{A6. A5.} Audit evidence is information to which audit procedures have been applied, that is, the results of audit procedures. The nature of the audit procedures that the auditor performs in order to use information as audit evidence may depend on the source of the information and may range from simple to more-extensive audit procedures. For example, when using information from an external information source, obtaining the information may be relatively easy and the auditor’s consideration of procedures to evaluate that information would be largely focused on considering the

\textsuperscript{14} Paragraph .29 of AU-C section 330.

\textsuperscript{15} Paragraph .14 of AU-C section 700.
source and reliability of that information. On the other hand, more extensive procedures, including audit procedures to obtain evidence about the accuracy and completeness of the information, such as tests of controls, may be necessary when the auditor intends to use information generated internally from the entity’s financial reporting process as audit evidence.

A7. Audit evidence may be obtained by the auditor

   a. By applying audit procedures during the course of the current year audit.
   b. From other sources, such as previous audits, provided that the auditor has determined whether changes have occurred since the previous audits that may affect its relevance to the current audit.
   c. Based on other sources, such as the results of applying the firm’s quality control procedures for client acceptance and continuance to the engagement.

A8. As explained in AU-C section 200, the sufficiency and appropriateness of audit evidence are interrelated. Together they affect the persuasiveness of audit evidence. The auditor’s conclusion about whether sufficient appropriate audit evidence has been obtained in accordance with AU-C section 200 is both at the financial statement level as well as the relevant assertion level. The evidence that is needed is affected by the risk of material misstatement. For example, ordinarily more persuasive evidence is needed to respond to significant risks.

A9. In some cases, the absence of information is used by the auditor and, therefore, also constitutes audit evidence. For example, when considering information regarding management’s assertions related to the entity’s recorded warranty provision, the absence of sales returns of the product in question may be audit evidence supporting management’s assertion as to the completeness of the warranty provision.

Sufficiency of Audit Evidence

Sufficient Appropriate Audit Evidence

A40. As explained in AU-C section 200, reasonable assurance is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially

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16 Paragraph .10 of AU-C section 315.
17 Paragraph .A32 of AU-C section 200.
18 Paragraph .A33 of this proposed SAS. Paragraph .A33 of AU-C section 200.
misstated) to an acceptably low level.\(^{19}\)

\textbf{A4.9.} The quantity of audit evidence, in and of itself, is not \textit{solely} determinative of its sufficiency when considering the persuasiveness. For example, obtaining more of the same type of audit evidence—\textit{As may not compensate for its lack of appropriateness. However, as the quality of audit evidence increases, the need for additional corroborating audit evidence decreases. However, obtaining more audit evidence may not compensate for its lack of appropriateness. Depending on the auditor’s consideration of relevance and reliability, information obtained from a single source may provide persuasive audit evidence.}

\textbf{A10.} \textit{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.}\(^{20}\) 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 contemplate\textit{[A]} explained in \textit{AU-C section 200}, the sufficiency and appropriateness of audit evidence are interrelated.\(^{21}\) Together they affect the persuasiveness of audit evidence. The auditor’s conclusion about whether sufficient appropriate audit evidence has been obtained in accordance with AU-C section 330 is both at the financial statement level as well as the relevant assertion level. The evidence that is needed is affected by the risk of material misstatement.

\textbf{A12/A11.} \textit{AU-C section 330 requires the auditor to obtain more persuasive audit evidence the higher the assessment of risk.}\(^{22}\) For example, ordinarily more persuasive audit evidence is needed to respond to significant risks. Persuasiveness therefore relates to 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 to be responsive to the audit objectives.

\textbf{Evaluating Information to Be Used as Audit Evidence}

\textit{Exercising Professional Skepticism (Ref: par. 7–8)}

\textbf{A13.} \textit{The auditor’s evaluation of information to be used as audit evidence in accordance with this proposed SAS involves exercising professional skepticism, including the consideration of whether unconscious or conscious auditor’s bias may affect the auditor’s professional judgments.}

\textit{Relevance and Reliability (Ref: par. 7a)}

\textbf{A14/A11.} \textit{The reliability of evidence depends on the nature and source of the evidence and}

\footnotesize{\textsuperscript{19} Paragraph .06 of AU-C section 200.}

\footnotesize{\textsuperscript{20} See paragraph 7a of AU-C section 330.}

\footnotesize{\textsuperscript{21} See paragraph A27A\textsuperscript{99} of this proposed SAS. Paragraph A27A\textsuperscript{100} of AU-C section 200.}

\footnotesize{\textsuperscript{22} See paragraph 7b of AU-C section 330.}
the circumstances under which it is obtained. Generally, the reliability of audit evidence increases when it is obtained from external parties because the information is less susceptible to management bias. Consideration of the sources of information to be used as audit evidence includes the possibility that the information source may not be reliable.

A15-A12. Information to be used as audit evidence may take different forms, which influences the nature of audit procedures that may be necessary to evaluate reliability of the information. Different forms, individually or in combination, of information include:

- Oral – information obtained through a verbal response to an inquiry of management or external information sources (for example, oral inquiries made during the course of the audit).
- Visual – information obtained through observation (for example, a message that appears on-screen for a control restricting access to an information technology (IT) system information observed by the auditor using remote observation tools).
- Paper documents – information obtained in documentary form (for example, an original executed sales contract or a written confirmation).
- Electronic information:
  - documents – information obtained in electronic documentary form (for example, a scanned version of an executed sales contract or an electronic confirmation).
  - Electronic data – data stored in the entity’s IT system or obtained electronically from an external information source. Such data may be manually input into the system or may be electronically generated (for example, an electronic data interface between the entity and a service organization).

**Relevance and Reliability of the Information, Including Its Source (Ref: par. 7ab)**

*External confirmation* procedures may provide relevant information when addressing assertions associated with certain account balances and their elements. However, external confirmations need not be restricted to classes of transactions, account balances, or disclosures. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, the relevant details. External confirmation procedures are also used to obtain audit evidence about the absence of certain conditions (for example, the absence of a side agreement that may influence revenue recognition).

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Commented [KKH19]: Suggestion to keep electronic as one category, but break into sub-bullets

Commented [HH20]: Added this subtitle to align structure with the requirement

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See AU-C section 505, *External Confirmations*. 
Sources of Information to be Used as Audit Evidence

A17. The source of the information to be used as audit evidence often affects the consideration of its relevance and reliability. Information to be used as audit evidence may be obtained directly or derived individually or in combination from different sources, including the following:

a. **Management.** Management may provide the auditor with information that is generated internally obtained from the financial reporting process used to prepare the financial statements, including disclosures (for example, the entity’s accounting records) as well as information obtained from outside the financial reporting process of the general and subsidiary ledgers (for example, from the entity’s risk management system or sales functions). This information may be stored by the entity within its IT systems or in a network of remote servers. Management may also employ or engage a specialist who may provide information that cannot be used as audit evidence.

b. **External parties, including external information sources and other external parties.** Management or the auditor may use information obtained from external sources, including external information sources and other external parties (for example, information used as inputs to forecasts or models used to prepare accounting estimates). The auditor may obtain external confirmations or may make inquiries of external parties to corroborate management’s assertions.

c. **Auditor.** The auditor may develop information to be used as audit evidence. For example, an auditor may accumulate and analyze industry trends to be used in the audits of entities in that industry. The auditor may also employ or engage a specialist to assist the auditor in developing audit evidence, which could include developing an independent expectation to evaluate the reasonableness of an accounting estimate. The auditor may also use automated tools and techniques to analyze information provided by management or external parties, resulting in audit evidence.

A14. **Accounting records are an example of information provided by management that is obtained from the financial reporting process and may include the following:**

- The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers; and journal entries.

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24 See AU-C section 501, Audit Evidence—Specific Considerations for Selected Items
• Records, such as spreadsheets, cost allocations, computations, reconciliations, and disclosures

A15. An example of information provided by management that is obtained from outside the financial reporting process is internal marketing information developed by the entity’s sales function as an assumption in making an accounting estimate for a warranty provision.

A16. External confirmation procedures may provide relevant information to be used as audit evidence when addressing assertions associated with certain account balances and their elements. However, external confirmations need not be restricted to classes of transactions, account balances, or disclosures. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, the relevant details. External confirmation procedures are also used to obtain audit evidence about the absence of certain conditions (for example, the absence of a side agreement that may influence revenue recognition).

A17. As indicated in paragraph A16, information to be used as audit evidence by the auditor may be obtained directly or derived individually or in combination from different sources. For example, in making an accounting estimate for an accumulated pension obligation, management may use information that is generated internally obtained from the financial reporting process; information obtained from outside the financial reporting process; and information obtained from a management’s specialist. Similarly, an auditor may obtain information to be used as audit evidence from multiple sources. For example, in performing a regression analysis to test revenue recorded, the auditor may obtain information about square footage of retail space and sales prices (both management generated) and changes in an index published by a government agency (an external information source).

A18. As indicated in paragraph A16, information to be used as audit evidence by the auditor may be obtained directly or derived individually or in combination from different sources. For example, in making an accounting estimate for an accumulated pension obligation, management may use information that is generated internally obtained from the financial reporting process; information obtained from outside the financial reporting process; and information obtained from a management’s specialist. Similarly, an auditor may obtain information to be used as audit evidence from multiple sources. For example, in performing a regression analysis to test revenue recorded, the auditor may obtain information about square footage of retail space and sales prices (both management generated) and changes in an index published by a government agency (an external information source).

A19. Accounting records are an example of information provided by management that is generated internally from the financial reporting process and may include the following:

- The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers; and journal entries
- Records, such as spreadsheets, cost allocations, computations, reconciliations, and disclosures

A20. An example of information provided by management that is generated from outside the financial reporting process is internal marketing information used as an assumption in making an accounting estimate for a warranty provision.

A21. Information provided by management may be as follows:

25 See AU-C section 505, External Confirmations.
a. in electronic or paper form. Examples of internal information in electronic form are electronic records of sales made through an entity’s website.

b. stored by the entity locally within its IT systems or in a network of remote servers.

A22. Evaluating certain attributes related to the relevance and reliability of information obtained from external information sources used by the auditor may not be practicable. For example, the auditor may not be able to evaluate the completeness and accuracy of information obtained from an external source to the same degree as the auditor would evaluate the completeness and accuracy of internal information obtained from management.

A23. A18. In some situations, there may be only one source of certain information external to the entity, for example, information from a central bank or government, such as an inflation rate, or single recognized industry body. In such cases, the auditor’s consideration of assessing the reliability of such information is influenced by the nature and credibility of the source of the external information, the assessed risks of material misstatement to which that external information is relevant, and the degree to which the use of that external information is relevant to the reasons for the assessed risk of material misstatement. For example, when the information is from a credible authoritative source, the extent of the auditor’s further audit procedures may be less extensive, such as corroborating the information with the source’s website or published information. In other cases, when information is from a source not assessed as credible, the auditor may determine that more extensive audit procedures are appropriate. In the absence of an alternative independent information source against which to compare, the auditor may consider whether performing additional audit procedures to obtain information from the external information source is appropriate in order to obtain sufficient appropriate audit evidence (see paragraph 9 in appendix A).

A24. Some sources of electronic information may provide a central location from which the auditor may obtain audit evidence. For example, a record maintained in a distributed ledger, such as a blockchain, may include information that is internal or external to the entity, which, among other factors, may affect the auditor’s consideration of the reliability of the information in a blockchain.

A25. A19. In certain circumstances, the source of information may be a combination of management and external parties. For example, if an entity develops a distributed ledger to capture transactions, there may be few or many other external parties also participating in the transactions and contributing to the information included in the distributed ledger— including the entity. Therefore, when considering the source of the information included in the distributed ledger, the source is not solely management (that is, the information provided by management), but also includes information from external parties. In such circumstances, professional judgment is used by the auditor to assess the relevance and reliability of the information obtained from the distributed ledger to be used as audit evidence.

External Information Sources

Relevance and Reliability

Relevance

A27. A21. The relevance of the information to be used as audit evidence relates to the logical connection with, or bearing upon, the auditor’s purposes. Such information may be relevant when applying multiple audit procedures. Information from one source may be relevant when performing one or more audit procedures (for example, sales information provided by management may be used to perform procedures related to both warranty provision and evaluation of management’s cash flow forecast). The following are factors that, individually or in combination, may affect the relevance of information to be used as audit evidence:

- The classes of transactions, account balances, or disclosures or assertions to which the information relates. Information to be used as audit evidence may be relevant to multiple classes of transactions, account balances or disclosures, or assertions.

- The period of time to which the information relates.

A28. A22. The following examples illustrate the relevance of information to be used as audit evidence:

- If the objective of an audit procedure is to test the existence or valuation of accounts payable, testing information related to the recorded accounts payable may provide relevant audit evidence when the objective of the audit procedures is to test the existence or valuation pertaining to accounts payable.

- Information related to employee salaries may provide relevant audit evidence regarding an accounting estimate for a bonus accrual.

- Information related to the collection of receivables after the period-end may provide relevant audit evidence regarding existence and valuation of receivables and occurrence and accuracy of revenue, but not necessarily completeness of receivables and revenue.

- Information related to the commodity pricing data may be used to perform the performance of an audit data analytic to test evaluate recorded revenue. The period of time used for the commodity pricing data will need to be relevant to the time period revenue was recorded.

A29. A23. Certain information to be used as audit evidence may have direct relevance the existence of an asset to one financial statement assertion, but not be relevant to all assertions:

- Inspection of a document constituting a financial instrument such as a stock, bond, or a digital copy a mortgage may provide relevant audit evidence about existence but may not necessarily provide audit evidence about ownership or value.
of tangible assets may provide relevant audit evidence with respect to their existence but not necessarily about the entity’s rights and obligations.

**Reliability**

A24. The reliability of audit evidence depends on the nature and source of the audit evidence and the circumstances under which it is obtained. Generally, the reliability of audit evidence increases when it is obtained from external parties because the information is less susceptible to management bias. Consideration of the sources of information to be used as audit evidence includes the possibility that the information source may not be reliable.

A30. A1. The reliability of information to be used as audit evidence is affected to varying degrees by the following attributes, individually or in combination:

- **Accuracy**
- **Completeness**
- **Authenticity**
- **Susceptibility to management bias**

A31. Determining whether controls are effectively designed and implemented may help the auditor design appropriate audit procedures to evaluate the reliability of information. In some cases, the reliability of such information may only be established when the related controls (whether manual or automated), including those over the preparation and maintenance of the information, have been tested and determined to be operating effectively.

A32. A25. Information obtained directly by the auditor (for example, observation of the application of a control) may be more reliable than information obtained indirectly or by inference (for example, inquiry about the application of a control). In the latter circumstances, when information has been obtained indirectly or by inference, the auditor may perform additional audit procedures to evaluate the reliability of the information obtained indirectly or by inference, such as by reperforming the control activity.

A33. A26. Information in documentary form, whether written, paper or electronic, or other medium, may be more reliable than evidence obtained orally through oral inquiries (for example,

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26. See paragraph 9 of this proposed SAS

27. See also paragraph .05b of AU-C section 520, Analytical Procedures.
a contemporaneously written record of a meeting may be more reliable than a subsequent oral representation of the matters discussed.

A27. Determining whether controls are effectively designed and implemented may help the auditor design appropriate audit procedures to evaluate the reliability of information.28 In some cases, the reliability of such information may only be established when the related controls whether manual or automated, and including those over the preparation and maintenance of the information, have been tested and determined to be operating effectively.29

A28. Using information in electronic documents may require the auditor to perform additional audit procedures to establish its reliability. For example, when using a scanned version of an executed sales contract provided by the sales department, additional audit procedures, such as confirmation of the key terms with a third party, may be necessary if the auditor has not tested the operating effectiveness of the controls around execution of the original contract and the maintenance of the scanned version.

A29. The reliability of information to be used as audit evidence is affected to varying degrees by the following attributes, individually or in combination:

- Accuracy
- Completeness
- Authenticity
- Susceptibility to management bias

These attributes are also relevant when automated tools and techniques are used to obtain audit evidence.

Testing Controls over Information to Be Used as Audit Evidence

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. Authenticity:

A30. 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 information.
maintenance of the information. In other situations, the auditor may determine that additional audit procedures are needed to address reliability (for example, inspecting underlying original documents to validate the authenticity of information in electronic form). In other situations, the auditor may determine that it is necessary to test controls over the transformation and maintenance of information.

A31. Similarly, when a significant amount of information is electronically initiated, recorded, processed, or reported, information to be used as audit evidence may be available only in electronic form. In such cases, the sufficiency and appropriateness of the audit evidence usually depends on the effectiveness of controls over their accuracy and completeness. Furthermore, the potential for improper initiation or alteration of information to occur and not be detected may be greater if information is initiated, recorded, processed, or reported only in electronic form and appropriate controls are not operating effectively.

Authenticity

A35. A32. 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 procedures to evaluate authenticity. Such audit procedures may include

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

Susceptibility to Management Bias

A36. A33. Information with a higher susceptibility to management bias is considered less reliable than information for which the susceptibility to management bias is lower unless audit procedures have been performed to address the higher susceptibility to management bias.

A37. A34. A susceptibility to management bias may exist in the development of information itself or may exist due to interpretation of the information by the entity. A greater susceptibility to management bias may exist when information is generated from internal sources.

A38. A35. Professional judgment may be required in accordance with AU-C section 200, the auditor is required to exercise professional judgment. This includes determining the impact of management bias in evaluating the reliability of information from external information sources.

Commented [HH41]: This paragraph was moved from the Authenticity section to here.

Commented [KKH42]: Suggestion to clarify and link more closely to AU-C section 200.
to be used as audit evidence. Determining the effect of management bias involves considering the following:

a. The ability of the entity to influence the external information source

b. Management’s selection of information from an external source known to be favorably biased toward corroborating management’s assertions or information

External information is more likely to be suitable for use by a broad range of users and less likely to be subject to influence by any particular user if the external individual or organization provides it to the public for free or makes it available to a wide range of users in return for payment of a fee.

Corroborative or Contradictory Information (Ref: par. 7b)

AU-C section 330 states that, in forming a conclusion about whether sufficient appropriate audit evidence has been obtained, the auditor should consider all relevant audit evidence, regardless of whether it appears to corroborate or contradict the assertions being tested by the auditor or the amounts recorded in the financial statements.32

Evaluating information to be used as audit evidence involves taking into account information that corroborates assertions or contradicts assertions in the financial statements. For example, audit evidence obtained through the inspection of an original document may corroborate a financial statement assertion, while audit evidence obtained from confirmation with an external party may contradict that financial statement assertion. In this example, additional audit evidence may be necessary to enable the auditor to conclude on the relevant assertion.

Information may be relevant and therefore used as audit evidence even when the source of that contradictory information is less reliable than the source of corroborative information. For example, in the audit of a depository institution, the auditor may obtain press reports of property value declines in a particular geography that contradicted the report of an external appraisal provided by management to support its estimate of the values of collateral for a loan portfolio. In this case, given that contradictory information has been obtained, the auditor may determine that it is necessary to perform additional audit procedures to obtain audit evidence about the value of the property to evaluate the reliability of the appraisal received.

The auditor does not consider contradictory information to be used as audit evidence in isolation but rather as part of the auditor’s consideration of the information obtained with respect to that management assertion taken as a whole. In such cases, professional skepticism and judgment is necessary to evaluate the persuasiveness of the totality of the audit evidence taken as a whole rather than focusing on a single source of individual piece of audit evidence. For example, the auditor may be aware of

32 Paragraph .28 of AU-C section 330.
information on social media suggesting a company’s product has major quality issues and that all buyers will be returning the product. The auditor may have obtained external confirmations regarding product sales and outstanding accounts receivable that do not indicate quality or return issues; and may have scanned the sales returns subsidiary ledger, which contained only an immaterial amount of returns subsequent to year end. In light of that, the auditor will likely conclude that the contradictory information does not suggest a reasonably possible risk of material misstatement and will not perform further audit procedures.

Evaluating Whether the Information Is Sufficiently Precise and Detailed for the Auditor’s Purposes (Ref: par. 8a)

A43. In some cases, the auditor may intend to use information obtained from management for other audit purposes. For example, the auditor may intend to use the entity’s performance measures for the purpose of analytical procedures or use the entity’s information produced for monitoring activities such as reports of the internal audit function. In such cases, the appropriateness of this information to be used as audit evidence is affected by whether the information is sufficiently precise or detailed for the auditor’s purposes. For example, performance measures used by management may not be precise enough to detect material misstatements.

Accuracy and Completeness (Ref: par. 8b)

A42. In accordance with paragraph 8, the auditor is required to determine whether it is necessary to obtain audit evidence about the accuracy and completeness of information to be used as audit evidence. For example, the reliability of:

- the price and sales volume data produced by the entity used to develop an expectation of revenue is affected by the accuracy and completeness of the information being used.

A43. The auditor may obtain audit evidence about the accuracy or completeness of information to be used as audit evidence through the performance of an audit procedure that was not primarily intended for that purpose, other audit procedures. For example, in testing investment transactions, the auditor may reconcile the listing of investment purchases in testing for completeness before selecting a sample. In other situations, the auditor may consider it necessary to obtain audit evidence about the accuracy and completeness of information by testing controls over the preparation and maintenance of the information (for example, in light of the nature, frequency, and volume of transactions), a population being tested for a certain characteristic, such as payment authorization, is affected by the completeness of the population from which items are selected.

A44. On the other hand, evaluating certain attributes related to the relevance and reliability of information obtained from external information sources used by the auditor may not be practicable. For example, Procedures regarding the reliability of external information may be dependent on how the external information will be used in the execution of an audit procedure, because the auditor may not be able to evaluate the completeness and accuracy of information obtained from an external source to the same degree as the auditor would evaluate the completeness and accuracy
of internal information obtained from management. For example, when using information from external information sources to perform an audit data analytic, the auditor’s evaluation may focus more on the quality of that information (for example, that the information was from a reputable source) rather than its completeness.

**Accuracy and Completeness (Ref: par. 8b)**

A44. In accordance with paragraph 8, the auditor is required to determine whether it is necessary to obtain audit evidence about the accuracy and completeness of information to be used as audit evidence. For example, the reliability of the price and sales volume data produced by the entity used to develop an expectation of revenue is affected by the accuracy and completeness of the information being used. Similarly, if the auditor intends to test a population (for example, payments) for a certain characteristic, such as authorization, the results of the test will be less reliable if the population from which items are selected for testing is not complete.

A45. The auditor may obtain audit evidence about the accuracy or completeness of information to be used as audit evidence through the performance of an audit procedure that was not primarily intended for that purpose. For example, in testing investment transactions, the auditor may reconcile the listing of investment purchases in testing for completeness before selecting a sample. In other situations, the auditor may consider it necessary to obtain audit evidence about the accuracy and completeness of information by testing controls over the preparation and maintenance of the information (for example, in light of the nature, frequency, and volume of transactions).

**Audit Procedures for Obtaining Audit Evidence (Ref: par. 9)**

A46. Audit procedures performed on information may include inspection, observation, confirmation, recalculation, reperformance, and analytical procedures, often in some combination, in addition to inquiry. These audit procedures may be performed either manually or using automated tools and techniques. The nature, timing, and extent of audit procedures performed on information influences the persuasiveness of the audit evidence obtained. For example, inspection or observation may provide more persuasive audit evidence than inquiry about existence.

A47. As explained further in AU-C section 315 and AU-C section 330, to draw reasonable conclusions on which to base the auditor’s opinion, audit evidence is obtained by performing the following:

33 Paragraphs .05–.06 of AU-C section 315.
34 Paragraphs .06–.07 of AU-C section 330.

a. Risk assessment procedures

b. Further audit procedures, which comprise

i. tests of controls, when required by the AU-C sections or when the auditor has

Commented [HH48]: This paragraph was moved here to show all the completeness and accuracy together.
chosen to do so, and

ii. substantive procedures, which include tests of details and substantive analytical procedures

An audit procedure may have characteristics of one or more than one category of substantive procedures. The auditor’s focus is on evaluating the results of the audit procedures performed (that is, the information to be used as audit evidence).

A48-A47. The auditor may use automated tools and techniques to process, organize, structure, or present data in a given context in order to generate useful information that can be used as audit evidence.

Electronic Information

A48. An auditor may use automated tools and techniques to perform both a risk assessment procedure and a substantive procedure concurrently. As illustrated in Exhibit A, a properly designed audit data analytic may be used to perform risk assessment procedures and may also provide sufficient appropriate audit evidence to address a risk of material misstatement related to a population or class of transactions.

A49. Some information may be available only in electronic form or only at certain points or periods in time, which may affect the nature and timing of the audit procedures to be performed.

A50. Certain electronic information may be destroyed or deleted after a specified period of time (for example, if files are changed and backup files do not exist). Accordingly, as a result of the entity’s data retention policies, the auditor may find it necessary to request retention of some information for the performance of audit procedures at a later point in time or to perform audit procedures at a time when the information is available.

A51. Some electronic information (for example, records maintained on a distributed ledger, such as a blockchain) is available on a continuous basis during the audit. In such cases, auditors may develop audit procedures using automated tools and techniques to obtain information about transactions on a real-time basis.

Inspection

A52. Inspection involves a physical examination (being physically present or using remote observation tools) of an asset or an examination of records or documents, whether internal or external or in paper form, electronic form, or other media. An example of inspection used as a test of controls is inspection of records, using manual or automated techniques, for evidence of authorization. An example of an automated technique for inspection is the use of text-recognition programs to examine large populations of documents, such as contracts, to identify items for further audit consideration.

Observation

A53. Observation includes looking at a process or procedure being performed by others (for
example, the auditor’s observation of inventory counting by the entity’s personnel or the performance of control activities).

A54. Automated tools and techniques such as remote observation tools (for example, a camera mounted on a drone or a video transmission) may aid the auditor in performing an inspection or an observation procedure, such as management’s physical inventory count.

A55. Audit evidence obtained through observation procedures is limited to the point in time at which the observation takes place and by the fact that the act of being observed may affect how the process or procedure is performed.

Confirmation

A56. An external confirmation is defined as audit evidence obtained as a direct written response to the auditor from a third party (the confirming party), either in paper form or by electronic or other medium (for example, through the auditor’s direct access to information held by a third party). See AU-C section 505, External Confirmations, for further guidance.

Recalculation

A57. Recalculation consists of testing the mathematical accuracy of information. Recalculation may be performed manually or using automated tools and techniques.

A58. By using automated tools and techniques, auditors may be able to perform recalculation procedures on 100 percent of a population, for example, recalculating the gross margin for each product sold for an entity’s product line.

Reperformance

A59. Reperformance involves the independent execution of procedures or controls by the auditor that were originally performed as part of the entity’s internal control.

Analytical Procedures

A60. Analytical procedures consist of evaluations of financial information through analysis of plausible relationships among both financial and nonfinancial data. Analytical procedures also encompass necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount. Audit data analytics are a technique that the auditor may use to perform risk assessment procedures or substantive procedures.35

A61. As a risk assessment procedure, the use of audit data analytics may enable auditors to

35 Paragraph _ of AU-C section 520.
identify areas that might represent specific risks relevant to the audit, including the existence of unusual transactions and events, and amounts, ratios, and trends that warrant investigation. An analytical procedure performed using audit data analytics may be used to produce a visualization of transactional detail, to assist the auditor in performing risk assessment procedures. For example, a visualization depicting the composition of a population may be prepared to illustrate the volume and dollar value of items in the population. Although the auditor may find this technique useful in obtaining information in order to identify and assess the risks of material misstatement, the information provided may not be sufficiently precise for the auditor’s purpose of obtaining information to respond to the assessed risks of material misstatement at the assertion level.

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 considers 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 produces a risk score for each transaction. The transactions are then grouped based on risk scores. For those transactions that have a low risk score, no additional substantive procedures may be warranted for that population if the auditor determined the audit data analytic is sufficiently precise for the auditor to conclude the population does not warrant further investigation. For the low risk grouping, the audit data analytic may be used to simultaneously achieve the objective of both a risk assessment procedure and a substantive procedure.

A61.

A63. The auditor may use automated tools and techniques to obtain audit evidence about the effectiveness of the entity’s internal control. For example, if management has controls over the sequential numbering of sales invoices, the auditor may be able to obtain corroborating information about the effectiveness of sequential numbering of sales invoices for the year by using automated tools and techniques to determine whether any gaps in numbering or duplicates exist, which provides information about the controls over the completeness of invoices issued during the period and evidence regarding the effectiveness of management’s monitoring of the control.

A64. Analytical procedures involve the auditor’s exercise of professional judgment and may be performed manually or by using automated tools and techniques. For example, the auditor may scan data to identify significant or unusual items to test, which may include the identification of unusual individual items within account balances or other data through the reading or analysis of entries in transaction listings, subsidiary ledgers, general ledger control accounts, adjusting entries, suspense accounts, reconciliations, and other detailed reports for indications of misstatements that have occurred. The auditor also might use automated tools and techniques to scan an entire population of transactions and identify those transactions meeting the auditor’s criteria for a transaction being unusual. The identification of items that exhibit characteristics of risk of material misstatement through analytical procedures provides the auditor with audit evidence about those items. Analytical procedures also provide audit evidence about the items not exhibiting characteristics of risks of material misstatements because the auditor has determined,
using exercising professional judgment, that the items not selected for further audit procedures are less likely to be materially misstated.

Inquiry

A65. Inquiry consists of seeking information, both financial and nonfinancial, from knowledgeable persons within the entity or outside the entity. Inquiry is used extensively throughout the audit, in addition to other audit procedures.

A66. Evaluating responses to inquiries is an integral part of the inquiry process. Responses to inquiries may provide the auditor with corroborative information that corroborates other information or with new information. Alternatively, responses might provide information that contradicts other information that the auditor has obtained (for example, audit evidence regarding the possibility of management override of controls). Responses to inquiries may provide a basis for the auditor to modify or perform additional audit procedures.

A67. While inquiries of knowledgeable persons outside the entity do not meet the definition of external confirmations in accordance with AU-C section 505, such responses to inquiries of persons outside of the entity are considered in accordance with this proposed SAS and may constitute reliable information to be used as audit evidence.

Inconsistency in, or Doubts About the Reliability of Information to be Used as Audit Evidence or Inconsistencies in Audit Evidence (Ref: par. 10)

A68. Information obtained from different sources that differs in nature may indicate that an individual item of audit evidence is not reliable, such as when audit evidence obtained from one source is inconsistent with that obtained from another. This may be the case when, for example, an external confirmation is inconsistent with the terms of a debt obligation. AU-C section 230, Audit Documentation, includes a specific documentation requirement if the auditor identifies information that is inconsistent with the auditor’s final conclusion regarding a significant finding or issue.36

A69. In the case of inquiries about management’s intent, the information available to support management’s intent may be limited.37 AU-C section 580, Written Representations, provides guidance about obtaining written representations that address management’s intent. The exercise of maintaining professional skepticism is particularly important when corroborative audit evidence is limited to inquiry. In such circumstances, it may be helpful to consider the consistency, or lack thereof, between the information obtained through inquiry and management’s history of carrying out its stated intentions, management’s stated reasons for choosing a course of action, and

36 Paragraph .12 of AU-C section 230, Audit Documentation.
37 Paragraph .A13 of AU-C section 580, Written Representations.
management’s ability to pursue a specific course of action.
Appendix A — Considerations Regarding the Use of External Information Sources (Ref: par. A20)

1. As defined in paragraph 76, an external information source is an external individual or organization that is external to the entity that provides information used by the entity in preparing the financial statements or used by the auditor as audit evidence, when such information is suitable for use by a broad range of users.

2. External information sources may include pricing services, governmental organizations, central banks, recognized stock exchanges, media, or academic journals. Examples of information that may be obtained from external information sources include the following:
   - Prices and pricing-related data
   - Macroeconomic data, such as historical and forecast unemployment rates and economic growth rates, or census data
   - Credit history data
   - Industry-specific data, such as an index of reclamation costs for certain extractive industries or viewership information or ratings used to determine advertising revenue in the entertainment industry
   - Mortality tables used to determine liabilities in the life insurance and pension sectors
   - Documents or records on websites or in databases or distributed ledgers

3. As set forth in GAAS, an external individual or organization external to the entity cannot, in respect of any particular set of information, be both an external information source and
   - a management’s specialist,
   - a service organization, or
   - an auditor’s specialist.

4. However, an external individual or organization external to the entity may, for example, be acting as a management’s specialist when providing a particular set of information but acting as an external information source when providing a different set of information. Professional judgment may be needed to determine whether an external individual or organization is acting as an external information source or as a management’s specialist with respect to a particular set of information. The following examples illustrate some of the considerations that may be used. Each situation may be influenced by individual facts and circumstances:
   - An external individual or organization may be providing information about real estate prices that is suitable for use by a broad range of users, for example, information made generally available pertaining to a geographical region, and be determined to be an
external information source with respect to that set of information. The same external organization may also be acting as a management’s or auditor’s specialist in providing commissioned valuations, with respect to the entity’s real estate portfolio specifically tailored for the entity’s facts and circumstances.

- Some actuarial organizations publish mortality tables for general use that, when used by an entity, would generally be considered to be information from an external information source. The same actuarial organization may also be a management’s specialist with respect to different information tailored to the specific circumstances of the entity to help management determine the pension liability for several of the entity’s pension plans.

- An external individual or organization may possess expertise in the application of models to estimate the fair value of securities for which there is no observable market. If the external individual or organization applies that expertise in making an estimate specifically for the entity and that work is used by management in preparing its financial statements, the external individual or organization is likely to be a management’s specialist with respect to that information. If, on the other hand, that external individual or organization merely provides, to the public, prices or pricing-related data regarding private transactions, and the entity uses that information in its own estimation methods, the external individual or organization is likely to be an external information source with respect to such information.

- An external individual or organization may publish information, suitable for a broad range of users, about risks or conditions in an industry. If used by an entity in preparing its risk disclosures (for example in compliance with FASB Accounting Standards Codification 275, Risk and Uncertainties), such information would ordinarily be considered to be information from an external information source. However, if the same type of information has been specifically commissioned by the entity to use its expertise to develop information about those risks, tailored to the entity’s circumstances, the external individual or organization is likely to be acting as a management’s specialist.

- An external individual or organization may apply its expertise in providing information about current and future market trends, which it makes available to, and is suitable for use by, a broad range of users. If used by the entity to help make decisions about assumptions to be used in making accounting estimates, such information is likely to be considered to be information from an external information source. If the same type of information has been commissioned by the entity to address current and future trends relevant to the entity’s specific facts and circumstances, the external individual or organization is likely to be acting as a management’s specialist.

5. The auditor is required by paragraph 8 of this proposed SAS to take into account the relevance and reliability of information to be used as audit evidence regardless of whether that information has been used by the entity in preparing the financial statements or was
obtained by the auditor. For information obtained from an external information source, that consideration may, in certain cases, include

- information about the external information source
- details about the preparation of the information by the external information source, or
- audit evidence obtained through designing and performing further audit procedures in accordance with AU-C section 330 or, where applicable, AU-C section 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures.

6. Obtaining an understanding of why management or, when applicable, a management’s specialist uses an external information source, and how the relevance and reliability of the information was considered (including its accuracy and completeness), may help inform the auditor’s consideration of relevance and reliability of that information.

7. The following factors may be important when taking into account the relevance and reliability of information obtained from an external information source, including its accuracy and completeness. Some of these factors may only be relevant when the information has been used by management in preparing the financial statements or has been obtained by the auditor:

- The nature and authority of the external information source (For example, a central bank or government statistics office with a legislative mandate to provide industry information to the public may be considered a reliable external information source for certain types of information.)
- The ability of management to influence the information obtained, through relationships between the entity and the external information source
- The competence and reputation of the external information source with respect to the information, including whether, in the auditor’s professional judgment, the information is routinely provided by an external information source with a track record of providing reliable information
- Past experience of the auditor with the reliability of the information provided by the external information source
- Evidence of general market acceptance by users of the relevance or reliability of information from an external information source for a similar purpose to that for which the information has been used by management or the auditor
- Whether the entity has in place controls to address the relevance and reliability of the information obtained and used
- Whether the external information source accumulates overall market information or engages directly in “setting” market transactions
• Whether the information is suitable for use in the manner in which it is being used and, if applicable, was developed taking into account the applicable financial reporting framework
• Alternative information that may contradict the information used
• The nature and extent of disclaimers or other restrictive language relating to the information obtained
• Information about the methods used in preparing the information; how the methods are being applied including, where applicable, how models have been used in such application; and the controls over the methods
• When available, information relevant to considering the appropriateness of assumptions and other data applied by the external information sources in developing the information obtained

8. The nature and extent of the auditor’s consideration takes into account the assessed risks of material misstatement at the assertion level to which the use of the external information is relevant, the degree to which the use of that information is relevant to the reasons for the assessed risks of material misstatement, and the possibility that the information from the external information source may not be reliable (for example, whether it is from a credible source). Based on the auditor’s consideration of the matters described in paragraph 5, the auditor may determine that further understanding of the entity and its environment, including its internal control, is needed, in accordance with AU-C section 315, Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement, or that further audit procedures, in accordance with AU-C section 330 and AU-C section 540, when applicable, are appropriate in the circumstances, to respond to the assessed risks of material misstatement at the assertion level related to the use of information from an external information source. Such audit procedures may include the following:

• Performing a comparison of information obtained from the external information source with information obtained from an alternative independent information source
• When relevant to considering management’s use of an external information source, obtaining an understanding of controls management has in place to consider the

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1 Paragraphs .A56–.A62 of AU-C section 501, Audit Evidence—Specific Considerations for Selected Items.
2 Paragraph .06 of AU-C section 330, Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained.
3 Paragraphs .12–.14 of AU-C section 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures.
reliability of the information from external information sources, and potentially testing the operating effectiveness of such controls

- Performing procedures to obtain information from the external information source to understand its processes, techniques, and assumptions, for the purposes of identifying, understanding, and when relevant, testing the operating effectiveness of its controls

9. When the auditor does not have a sufficient basis upon which to consider the relevance and reliability of information from an external information source, the auditor may have a limitation on scope if sufficient appropriate audit evidence cannot be obtained through alternative procedures. Any imposed limitation on scope is evaluated in accordance with the requirements of AU-C section 705, *Modifications to the Opinion in the Independent Auditor’s Report*. 
Appendix B — Amendments to Various Sections in Statement on Auditing Standards No. 122, Statements on Auditing Standards: Clarification and Recodification, as Amended

(Boldface italics denote new language. Deleted text is shown in strikethrough.)

AU-C Section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards

[No amendments to paragraphs .01–.13.]

Definitions

.14 For purposes of GAAS, the following terms have the meanings attributed as follows:

... Audit evidence. Information used by the auditor in arriving at the conclusions on which the auditor’s opinion is based. Audit evidence is information to which audit procedures have been applied, that is, the results of audit procedures. Audit evidence consists of information that corroborates or contradicts assertions in the financial statements. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information. Sufficiency of audit evidence is the measure of the persuasiveness of audit evidence. The persuasiveness of audit evidence necessary needed is affected by the auditor’s assessment of the risks of material misstatement, and also by the quality of such audit evidence. Appropriateness of audit evidence is the measure of the relevance and reliability of audit evidence, that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based...

... [No amendments to paragraphs .15–.26.]

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 maintenance 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 is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not.

- **Confirmation bias**, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief.

- **Groupthink**, which is a tendency to think or make decisions as a group that discourages creativity or individual responsibility.

- **Overconfidence bias**, which is a tendency to overestimate one’s own ability to make accurate assessments of risk or other judgments or decisions.

- **Anchoring bias**, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed.

- **Automation bias**, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions as to whether such output is reliable or fit for purpose.

[A27–A74. No amendments to paragraphs A27–A74.]

A33 The sufficiency and appropriateness of audit evidence are interrelated. Audit evidence is sufficient (that is, persuasive) when an auditor would be persuaded to reach conclusions for the auditor’s purposes based on consideration of the 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.

[A34–A75. No amendments to paragraphs A34–A75.]

[Commented [HH54]: Source: AU-C 200. Included for contextual purposes only (no changes are proposed to this paragraph).]

[Commented [HH55]: Source: proposed SAS 220 (March 2020).]

[Commented [HH56]: This is a deletion from the ED to this version. It is not a conforming amendment.]
.A76 The auditor is required by paragraph .23b to use the objectives stated in the relevant AU-C sections to evaluate whether sufficient appropriate audit evidence has been obtained in the context of the overall objectives of the auditor. If, as a result, the auditor concludes that sufficient appropriate audit evidence has not been obtained is not sufficient and appropriate, then the auditor may follow one or more of the following approaches to meeting the requirement of paragraph .23b:

- Evaluate whether further relevant audit evidence has been, or will be, obtained as a result of complying with other AU-C sections, in particular, AU-C section 330.
- Extend the work performed in applying one or more requirements.
- Perform other procedures judged by the auditor to be necessary in the circumstances.

When none of the preceding is expected to be practical or possible in the circumstances, the auditor will not be able to obtain sufficient appropriate audit evidence and is required by GAAS to determine the effect on the auditor’s report or on the auditor’s ability to complete the engagement.

[No further amendments to AU-C section 200.]

AU-C Section 230, Audit Documentation

[No amendments to paragraphs .01–.05.]

.06 For purposes of GAAS, the following terms have the meanings attributed as follows:

Audit documentation. The record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached (terms such as working papers or workpapers are also sometimes used)…

[No further amendments to AU-C section 230.]

AU-C Section 315, Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement

[No amendments to paragraphs .01–A79.]
.A80 Audit evidence for elements of the control environment. Relevant audit evidence related to elements of the control environment may be obtained through a combination of inquiries and other risk assessment procedures, such as corroborating inquiries through observation or inspection of documents. For example, through inquiries of management and employees, the auditor may obtain an understanding of how management communicates to employees management’s views on business practices and ethical behavior. The auditor may then determine whether relevant controls have been implemented by considering, for example, whether management has a written code of conduct and whether it acts in a manner that supports the code.

[No further amendments to AU-C section 315.]

AU-C Section 330, Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained

[No amendments to paragraphs .01–.2705.]

.06 The auditor should design and perform further audit procedures whose nature, timing, and extent are based on, and are responsive to, the assessed risks of material misstatement at the assertion level. The auditor should do so in a manner that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory. The auditor’s responses to the assessed risks of material misstatement should involve the application of professional skepticism in developing an effective approach to obtaining and evaluating audit evidence, including consideration of information that may be used as audit evidence and what procedures would be appropriate in the circumstances.

[No amendments to paragraphs .05–.27.]

.28 The auditor should conclude whether sufficient appropriate audit evidence has been obtained. In forming a conclusion, the auditor should consider all relevant audit evidence, regardless of whether it appears to corroborate or contradict the assertions in the financial statements.

[No amendments to paragraphs .29–.A47.]

.A48 The nature of the risk and assertion is relevant to the design of tests of details. For example, tests of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining relevant audit evidence. On the other hand, tests of details related to the completeness assertion may involve selecting from items that are expected to be included in the relevant
External confirmation procedures frequently may be relevant when addressing assertions associated with account balances and their elements but need not be restricted to these items. For example, the auditor may request external confirmation of the terms of agreements, contracts, or transactions between an entity and other parties. External confirmation procedures also may be performed to obtain audit evidence about the absence of certain conditions. For example, a request may specifically seek confirmation that no "side agreement" exists that may be relevant to an entity’s revenue cut-off assertion. Other situations in which external confirmation procedures may provide relevant audit evidence in responding to assessed risks of material misstatement include the following:

- Bank balances and other information relevant to banking relationships
- Inventories held by third parties at bonded warehouses for processing or on consignment
- Property title deeds held by lawyers or financiers for safe custody or as security
- Investments held for safekeeping by third parties or purchased from stockbrokers but not delivered at the balance sheet date
- Amounts due to lenders, including relevant terms of repayment and restrictive covenants
- Accounts payable balances and terms

Although external confirmations may provide relevant audit evidence relating to certain assertions, some assertions exist for which external confirmations may not provide less audit evidence, for example, external confirmations provide less audit evidence relating to the recoverability of accounts receivable balances than they do of their existence.
high level of reliability that the auditor requires to respond to significant risks of material misstatement, whether due to fraud or error. For example, if the auditor identifies that management is under pressure to meet earnings expectations, a risk may exist that management is inflating sales by improperly recognizing revenue related to sales agreements with terms that preclude revenue recognition or by invoicing sales before shipment. In these circumstances, the auditor may, for example, design external confirmation procedures not only to confirm outstanding amounts but also to confirm the details of the sales agreements, including date, any rights of return, and delivery terms. In addition, the auditor may find it effective to supplement such external confirmation procedures with inquiries of nonfinancial personnel in the entity regarding any changes in sales agreements and delivery terms.

[No amendments to paragraphs .A59--.A64.]

.A65 An effective test provides appropriate audit evidence to the extent that it will be sufficient for the auditor’s purpose when taken with other audit evidence obtained or to be obtained. In selecting items for testing, the auditor is required by AU-C section 500 to consider the relevance and reliability of information to be used as audit evidence; fn 12 the other aspect of effectiveness (sufficiency extent) is an important consideration in selecting items to test. The means available to the auditor for selecting items for testing are

a. selecting all items (100 percent examination),
b. selecting specific items, and
c. audit sampling.

fn 12 [Footnote omitted for purposes of this proposed SAS.]

[No amendments to paragraphs .A66--.A73.]

.A74 By performing audit procedures, the auditor may determine that the accounting records are internally consistent and agree to the financial statements. However, accounting records alone do not provide sufficient appropriate audit evidence on which to base an audit opinion on the financial statements.

[Paragraph .A74 is renumbered as .A75.]

.A78A76 The auditor’s conclusion of whether sufficient appropriate audit evidence has been obtained is both at the relevant assertion level as well as the financial statement level. AU-C section 500 enables the auditor to evaluate the results of audit procedures and other information to be used as audit evidence to inform the auditor’s
overall conclusion about whether sufficient appropriate audit evidence has been obtained as required by paragraph .28 explains the considerations involved in evaluating whether information is appropriate audit evidence. The auditor’s professional judgment about what constitutes sufficient appropriate audit evidence is influenced by the following additional such factors: as the

- Significance of the potential misstatement in the relevant assertion and the likelihood of its having a material effect, individually or aggregated with other potential misstatements, on the financial statements (see section 450, Evaluation of Misstatements Identified During the Audit).

- Effectiveness of management’s responses and controls to address the risks.

- Experience gained during previous audits with respect to similar potential misstatements.

- Results of audit procedures performed, including whether such the audit procedures identified specific instances of fraud or errors.

- Source and reliability of the available information.

- Persuasiveness of the audit evidence.

- Understanding of the entity and its environment, including its internal control.

Paragraph .A76 is renumbered as .A77.

[No further amendments to AU-C section 330.]

AU-C Section 505, External Confirmations

No amendments to paragraph .01.

.02 Section 500 indicates that the reliability of audit evidence is influenced by its source and nature and is dependent on the individual circumstances under which it is obtained. Section 500 also includes the following generalizations applicable to audit evidence:

- Audit evidence is more reliable when it is obtained from independent sources outside the entity.

- Audit evidence obtained directly by the auditor is more reliable than audit evidence obtained indirectly or by inference.

- Audit evidence is more reliable when it exists in documentary form, whether paper, electronic, or other medium.

Commented [KKH58]: For previous discussion with the ASB and in response to comment letter feedback, no conforming amendments will be made to AU-C section 505.
Accordingly, depending on the circumstances of the audit, audit evidence in the form of external confirmations received directly by the auditor from confirming parties may be more reliable than evidence generated internally by the entity. This section is intended to assist the auditor in designing and performing external confirmation procedures to obtain relevant and reliable audit evidence. Section 500 provides requirements and application material to assist the auditor in evaluating whether information to be used as audit evidence to which external confirmation procedures are performed is appropriate audit evidence.

Paragraph .A5 of section 500, Audit Evidence.

Paragraph .A32 of section 500.

[Subsequent footnotes are renumbered.]

.03 Other AU-C sections recognize the importance of external confirmations as audit evidence; for example,

- section 330 discusses the auditor’s responsibility (a) to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level and (b) to design and perform further audit procedures whose nature, timing, and extent are based on, and are responsive to, the assessed risks of material misstatement at the relevant assertion level. In addition, section 330 requires that, irrespective of the assessed risks of material misstatement, the auditor design and perform substantive procedures for all relevant assertions related to each material class of transactions, account balance, and disclosure. In addition, section 330 requires that, irrespective of the assessed risks of material misstatement, the auditor design and perform substantive procedures for all relevant assertions related to each material class of transactions, account balance, and disclosure. The auditor is required to consider whether external confirmation procedures are to be performed as substantive audit procedures and is required to use external confirmation procedures for accounts receivable unless:
  - the overall account balance is immaterial,
  - external confirmation procedures would be ineffective, or
  - the auditor’s assessed level of risk of material misstatement at the relevant assertion level is low, and the other planned substantive procedures address the assessed risk.

- section 330 requires that the auditor obtain more persuasive audit evidence the higher the auditor’s assessment of risk. To do this, the auditor may increase the quantity of the evidence or obtain evidence that is more relevant or reliable, or both. For example, the auditor may place more emphasis on obtaining evidence directly from third parties or obtaining corroborating evidence from a number of independent sources. Section 330 also indicates that external confirmation procedures may assist the auditor in obtaining audit evidence with the high level of reliability that the auditor requires to respond to significant risks of material misstatement, whether due to fraud or error.

- section 240, Consideration of Fraud in a Financial Statement Audit, indicates that the auditor may design confirmation requests to obtain additional...
corroborative information as a response to address the assessed risks of material misstatement due to fraud at the assertion level. fn 6

• section .500 indicates that corroborating information obtained from a source independent of the entity (such as external confirmations) may increase the assurance the auditor obtains from information evidence existing within the accounting records or representations made by management. fn 7

[Footnotes omitted for purposes of this proposed SAS.]

Paragraph .A3 of proposed section .500.

[No amendments to paragraph .04.]

.05 The objective of the auditor, when using external confirmation procedures, is to design and perform such procedures to obtain relevant and reliable audit evidence.

.06 For purposes of generally accepted auditing standards, the following terms have the meanings attributed as follows:

Exception. A response that indicates a difference between information requested to be confirmed, or contained in the entity’s records, and information provided by the confirming party.

External confirmation. Audit evidence obtained as a direct written response to the auditor from a third party (the confirming party). (Ref: par. .A1)

[No amendments to paragraph .07.]

When a Written Response to a Positive Confirmation Request Is Necessary to Obtain Audit Evidence

.08 If management refuses to allow the auditor to perform external confirmation procedures, the auditor should

a. inquire about management’s reasons for the refusal and seek audit evidence about their validity and reasonableness; (Ref: par. .A9)

b. evaluate the implications of management’s refusal on the auditor’s assessment of the relevant risks of material misstatement, including the risk of fraud, and
on the nature, timing, and extent of other audit procedures; and (Ref: par. A10)

e— perform alternative audit procedures designed to obtain relevant and reliable audit evidence. (Ref: par. A11)

[No amendments to paragraphs .09–.A11.]

When a Written Response to a Positive Confirmation Request Is Necessary to Obtain Sufficient Appropriate Audit Evidence

.13 If the auditor has determined that a written response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence, alternative audit procedures will not provide the audit evidence the auditor requires. If the auditor does not obtain such confirmation, the auditor should determine the implications for the audit and the auditor’s opinion, in accordance with section 705.

[Paragraph .13 included for contextual information only.]

.A12 Section 500 indicates that even when audit evidence is obtained from sources external to the entity, circumstances may exist that affect its reliability.\[fn^13\] All written or electronic confirmation responses usually carry some risk of interception or alteration. Written, electronic, or oral confirmation responses also carry some risk of fraud. Factors that may indicate doubts about the reliability of a response include whether it

- was received by the auditor indirectly or
- appeared not to come from the originally intended confirming party.

\[fn^13\] Paragraph .A12 of section 500

[No amendments to paragraphs .A13–.A15.]

[All subsequent footnotes renumbered.]

.A16 The auditor is required by section 500 to determine whether to modify or add procedures to resolve doubts over the reliability of information to be used as audit evidence.\[fn^14\] The auditor may choose to verify the source and contents of a response to a confirmation request by contacting the confirming party (for example, as described in paragraph .A14). When a response has been returned to the auditor indirectly (for example, because the confirming party incorrectly addressed it to the entity rather than the auditor), the auditor may request the confirming party to respond in writing directly to the auditor.
Paragraph .10.11 of section 500.

[No amendments to paragraphs .A17–.A26.]

A27—An oral response to a confirmation request does not meet the definition of an external confirmation because it is not a direct written response to the auditor. Provided that the auditor has not concluded that a direct written response to a positive confirmation is necessary to obtain sufficient appropriate audit evidence, the auditor may take the receipt of an oral response to a confirmation request into consideration when determining the nature and extent of alternative audit procedures required to be performed for nonresponses, in accordance with paragraph .12. The auditor may perform additional procedures to address the reliability of the evidence provided by the oral response, such as initiating a call to the respondent using a telephone number that the auditor has independently verified as being associated with the entity. For example, the auditor might call the main telephone number obtained from a reliable source and ask to be directed to the named respondent instead of calling a direct extension provided by the client or included in the statement or other correspondence received by the entity. The auditor may determine that the additional evidence provided by contacting the respondent directly, together with the evidence upon which the original confirmation request is based (for example, a statement or other correspondence received by the entity), is sufficient appropriate audit evidence. In appropriately documenting the oral response, the auditor may include specific details, such as the identity of the person from whom the response was received, his or her position, and the date and time of the conversation.

When a Written Response to a Positive Confirmation Request Is Necessary to Obtain Sufficient Appropriate Audit Evidence (Ref: par. .13)

A28. A27 In certain circumstances, the auditor may identify an assessed risk of material misstatement at the assertion level for which a written response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence. Such circumstances may include the following:

- The information available to corroborate management’s assertion(s) is only available outside the entity.
- Specific fraud risk factors, such as the risk of management override of controls or the risk of collusion, which can involve employee(s) or management, or both, prevent the auditor from relying on evidence from the entity.
- A higher risk of material misstatement exists at the assertion level.

[Paragraphs .A29–.A34 are renumbered as .A28–.A33.]
[No further amendments to AU-C section 330.]
AU-C Section 530, Audit Sampling

[No amendments to paragraph .01. Footnote intentionally omitted.]

.02 This section complements section 500, Audit Evidence, which addresses the auditor’s responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence and addresses how an auditor evaluates information to be used as audit evidence to be able to draw reasonable conclusions as a basis for forming the auditor’s opinion. Section 330, Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained, provides guidance on the means available to the auditor for selecting items for testing, one of which is audit sampling.

[No further amendments to AU-C section 530.]

AU-C Section 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures

[No amendments to paragraphs .01–.A27. Paragraph .A28 shown for contextual purposes.]

Management’s Use of Specialists

.A28 Management may have, or the entity may employ individuals with, the experience and competence necessary to make estimates. In some cases, however, management may need to engage a specialist to make estimates or assist in making them. This need may arise because of, for example,

- the specialized nature of the matter requiring estimation (for example, the measurement of mineral or hydrocarbon reserves in extractive industries).
- the technical nature of the models required to meet the relevant requirements of the applicable financial reporting framework, as may be the case in certain measurements at fair value.
the unusual or infrequent nature of the condition, transaction, or event requiring an accounting estimate.

\(^{fn11}\) See AU-C section 501, *Audit Evidence*—Specific Considerations for Selected Items See Paragraph .08 of section 500, *Audit Evidence*, which addresses management’s specialists.

[No amendments to paragraphs .A29–.A69.]

\[^A70\] In accordance with AU-C section 500, *Audit Evidence*, the auditor is required to evaluate information to be used as audit evidence by taking into account, among other things, the relevance and reliability of the information, including its source. The auditor’s evaluation of such information to be used as audit evidence is required to include evaluating whether the information is sufficiently precise and detailed for the auditor’s purposes and obtaining audit evidence about the accuracy and completeness of the information, as necessary.

evaluate whether the data on which the estimate is based is sufficiently reliable for the auditor’s purposes, including, as necessary.\(^{fn18}\)

\(^a\) obtaining audit evidence about the accuracy and completeness of the data.

\(^b\) evaluating whether the data is sufficiently precise and detailed for the auditor’s purposes.

\(^{fn18}\) Paragraphs .09, .07 and .08 of section 500.

[No further amendments to AU-C section 540.]

\[^A70\] In accordance with section 500, *Audit Evidence*, the auditor is required to consider the relevance and reliability of the information to be used as audit evidence, which includes data on which the estimate is based. Section 500 explains that the reliability of the audit evidence is affected to varying degrees, by the following attributes, individually or in combination:

- Accuracy
- Completeness
- Authenticity
- Risk of bias

evaluate whether the data on which the estimate is based is sufficiently reliable for the auditor’s purposes, including, as necessary.\(^{fn18}\)
a. obtaining audit evidence about the accuracy and completeness of the data.

b. evaluating whether the data is sufficiently precise and detailed for the auditor’s purposes.

fn 18 Paragraph .09 .07 of section 500.

[No further amendments to AU-C section 540.]
A72.A71.

Exhibit A — Using ADAs to Simultaneously Accomplish Multiple Audit Procedures (Ref: par. A48)

This Exhibit illustrates use of an audit data analytic (ADA) that simultaneously accomplishes the objectives of both risk assessment and substantive audit procedures.

Background

The fact pattern in this example, where the auditor uses a revenue transaction scoring model, will focus on the audit of an entity that recognizes revenue when control of the product (or satisfaction of the performance obligation) transfers at a specific point in time, such as a manufacturer of external data storage devices.

For purposes of this example, assume the following:

- Revenue was determined to be a material account during initial planning and scoping with the occurrence (including cut-off) and accuracy assertions being more susceptible to misstatement,
- The ADA was performed after initial planning, scoping, and controls testing as part of the ongoing and iterative risk assessment process,
- All transactions within the account were subject to the same processes and controls,
- The purpose of the ADA was to design the nature, timing, and extent of the audit procedures and to obtain audit evidence,
- Based on the understanding of controls, the auditor has concluded that the controls over revenue were effectively designed and have been implemented, the auditor has tested certain key controls and determined they are operating effectively, and the auditor is otherwise satisfied the entity has appropriately applied the requirements of the applicable financial reporting framework (e.g., ASC 606),
- Data used in the ADA is relevant and reliable and has been tested for accuracy and completeness,
- Customers tend to purchase consistent quantities throughout the year, with the

4 ASC 606-10-25-30
exception of purchases just prior to major retail holidays, such as Memorial Day, Black Friday, and Christmas,

- Some customers only purchase in bulk a few times a year, but most customers consistently purchase quantities one to two times a month,
- The customer base does not fluctuate significantly from period to period,
- Revenue is recognized when control transfers at FOB shipping point,
- Invoicing occurs the day the product ships from the entity’s warehouse,
- Warehouse personnel typically do not work weekends, and
- The company does not sell product to any related parties.

All items that are determined to be individually material were excluded from the ADA and substantively tested separately. The remaining population that was subject to the ADA was comprised of routine, non-complex transactions with third parties. The processing and recording of transactions are highly automated and less likely to be susceptible to management override.

**Description of the Audit Data Analytic**

ADA Scoring Model - A complete population of transactions (at the individual item level) for one material account (excluding individually significant items) was subjected to an ADA designed to identify and assess risk and obtain audit evidence specific to a relevant assertion. The routines were as follows:
<table>
<thead>
<tr>
<th>Routine</th>
<th>Description</th>
<th>Characteristic</th>
<th>Transaction Scoring Model</th>
<th>Risk Score</th>
<th>Relevant Fact Pattern</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Identify customers with infrequent revenue activity (less than X transactions)</td>
<td>Volume</td>
<td>Less than 6 transactions</td>
<td>2</td>
<td>Some customers only purchase in bulk a few times a year, but most customers consistently purchase quantities one to two times a month</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>6-12 transactions</td>
<td>1</td>
<td>Some customers only purchase in bulk a few times a year, whereas others purchase smaller quantities one to two times a month</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>More than 12 transactions</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Identify customers with a significant fluctuation in volume of products purchased (item level) on a period over period basis</td>
<td>Volume</td>
<td>Greater than 70% variance</td>
<td>2</td>
<td>Customers tend to purchase consistent quantities throughout the year, with the exception of purchases just prior to major retail holidays, such as Memorial Day, Black Friday, and Christmas</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>30-70% variance</td>
<td>1</td>
<td>Some customers only purchase in bulk a few times a year, but most customers consistently purchase quantities one to two times a month</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less than 30% variance</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Identify activity for new customers</td>
<td>Volume</td>
<td>Customer for 6 months or less</td>
<td>1</td>
<td>The customer base does not fluctuate significantly from period to period</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Customer for greater than 6 months</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Identify all transactions recorded within X days of quarter-end.</td>
<td>Timing</td>
<td>3 days of quarter end</td>
<td>1</td>
<td>Revenue is recognized when control transfers at FOB shipping point</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Greater than 3 days of quarter end</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>Identify revenue transactions with an invoice date on</td>
<td>Timing</td>
<td>Transaction on a</td>
<td>2</td>
<td>Invoicing occurs the day the product ships from the company’s warehouse</td>
</tr>
<tr>
<td>Routine</td>
<td>Description</td>
<td>Characteristic</td>
<td>Transaction Scoring Model</td>
<td>Risk Score</td>
<td>Relevant Fact Pattern</td>
</tr>
<tr>
<td>---------</td>
<td>-------------</td>
<td>----------------</td>
<td>---------------------------</td>
<td>------------</td>
<td>-----------------------</td>
</tr>
<tr>
<td>6</td>
<td>Identify instances where the shipping document and invoice don’t match.</td>
<td>Timing</td>
<td>Invoice and shipping document don’t match and invoice date is before shipping date</td>
<td>2</td>
<td>Revenue is recognized when control transfers at FOB shipping point</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Invoice and shipping document don’t match and shipping date is before invoice date</td>
<td>1</td>
<td>Invoicing occurs the day the product ships from the company’s warehouse</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Invoice and shipping document match</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>an unusual date (e.g., weekend or holiday)</td>
<td>Weekend/Holiday</td>
<td>Warehouse personnel typically do not work weekends</td>
<td>Transaction on a Weekday</td>
<td>0</td>
<td></td>
</tr>
</tbody>
</table>

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Running the revenue transaction level detail through the ADA routines produces a total score for each transaction. The auditor then groups each transaction into a sub-population based on the individual transaction score. The number of sub-populations may differ depending upon the type of ADA developed, the scores produced by the ADA, and the auditor’s assessment of those scores. For purposes of this example, the auditor grouped the population of the account into sub-populations as follows:

<table>
<thead>
<tr>
<th>Assessed Risk</th>
<th>Total Risk Score</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>High Risk</td>
<td>8 to 10</td>
<td>A</td>
</tr>
<tr>
<td>Moderate Risk</td>
<td>4 to 7</td>
<td>B</td>
</tr>
<tr>
<td>Low Risk</td>
<td>0 to 3</td>
<td>C</td>
</tr>
</tbody>
</table>

- **Group A – High Risk** - Comprised of items with characteristics deemed to present a higher risk of material misstatement.

  Approach - The auditor would perform additional substantive procedures to provide more persuasive audit evidence for the items identified by the ADA. For example, the nature of the substantive procedure may be confirmation as opposed to inspection; the extent of testing may be greater (larger proportionate sample size); or the timing of the procedure may be at or near the financial statement date as opposed to earlier in the period.

- **Group B – Moderate Risk** - Comprised of items that warrant further procedures but do not have characteristics of those in the higher risk group.

  Approach - The auditor would perform substantive procedures appropriate for the items identified by the ADA, in less depth relative to the higher risk population. For example, the nature of the substantive procedure may be limited to inspection of documents and records, the extent of testing may be less (smaller proportionate sample size), and the timing of the procedure may be earlier in the period.
Group C – Low risk - Comprised of items that demonstrate no unusual characteristics based on the procedure performed using the ADA.

Approach - The results of other audit procedures performed throughout the audit would be evaluated for contradictory information regarding the assessed risk of material misstatement. In the absence of contradictory information, no additional substantive procedures may be warranted for any reason other than to incorporate an element of unpredictability in the selection of auditing procedures to be performed from year to year.

As a result of the procedures performed above, the auditor concluded:

Groups A, B, and C comprise a material account in the aggregate for which each Group has differing risks.

For Group C, the audit evidence provided over the transactions within the population analyzed by the ADA in combination with the audit evidence provided by testing of certain key controls over revenue as determined by the auditor and the absence of contradictory audit evidence from the testing of related accounts, was sufficiently persuasive for the auditor to conclude that the risk of material misstatement was addressed; and

For Groups A and B, the audit evidence provided by the ADA was not sufficiently persuasive and further substantive procedures were required to address the risk of material misstatement.