



Agenda Item 3B

PROPOSED AMENDMENTS TO MANAGEMENT SPECIALISTS CONTENT IN GAAS

The following is the material in extant AU-C section 500, *Audit Evidence*, related to management specialists that was moved to AU-C section 501 by SAS No. 142, *Audit Evidence*. Proposed further amendments are shown in bold italics and strikethrough.

Definitions

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

...

Management's specialist. An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.

Requirements

Information to Be Used as Audit Evidence

.08 If information to be used as audit evidence has been prepared using the work of a management's specialist, the auditor should, to the extent necessary, taking into account the significance of that specialist's work for the auditor's purposes, (Ref: [par. .A35-.A37](#))

- a. evaluate the competence, capabilities, and objectivity of that specialist; (Ref: [par. .A38-.A44](#))
- b. obtain an understanding of the work of that specialist; and (Ref: [par. .A45-.A48](#))
- c. evaluate the appropriateness of that specialist's work as audit evidence for the relevant assertion. (Ref: [par. .A49](#))

Application and Other Explanatory Material

Reliability of Information Produced by a Management's Specialist (Ref: [par. .08](#))

- .A35** The preparation of an entity's financial statements may require expertise in a field other than accounting or auditing, such as actuarial calculations, valuations, or engineering data. The entity uses a management's specialist in these fields to obtain the needed expertise to prepare the financial statements. Failure to do so when such expertise is necessary increases the risks of material misstatement and may be a significant deficiency or material weakness.^{fn 12}
- .A36** When information to be used as audit evidence has been prepared using the work of a management's specialist, the requirement in [paragraph .08](#) applies. For example, an individual or organization may possess expertise in the application of models to estimate the fair value of securities for which no observable market exists. If the individual or organization applies that expertise in making an estimate which the entity uses in preparing its financial statements, the individual or organization is a management's specialist and [paragraph .08](#) applies. If, on the other hand, that individual or organization merely provides price data regarding private transactions not otherwise available to the entity which the entity uses in its own estimation methods, such information, if used as audit evidence, is subject to [paragraph .07](#), but it is not the use of a management's specialist by the entity.
- .A37** The nature, timing, and extent of audit procedures with regard to the requirement in [paragraph .08](#) may be affected by such matters as the following:
- The nature and complexity of the matter to which the management's specialist relates
 - The risks of material misstatement of the matter
 - The availability of alternative sources of audit evidence
 - The nature, scope, and objectives of the work of the management's specialist
 - Whether the management's specialist is employed by the entity or is a party engaged by it to provide relevant services
 - The extent to which management can exercise control or influence over the work of the management's specialist
 - Whether the management's specialist is subject to technical performance standards or other professional or industry requirements

^{fn 12} See section 265, *Communicating Internal Control Related Matters Identified in an Audit*, for further guidance

- The nature and extent of any controls within the entity over the work of the management's specialist
- The auditor's knowledge and experience of the field of expertise management's specialist
- The auditor's previous experience of the work of that specialist

The need for more persuasive evidence with regard to the requirement in paragraph .08 increases as the significance of the specialist's work, the risk of material misstatement, or the ability of management to affect the specialist's judgments increases, or as the competence, capabilities, and objectivity possessed by the specialist in the particular field decreases.

Commented [AG1]: See Exhibit B, AS 1105 Appendix B, note to par. A7

The Competence, Capabilities, and Objectivity of a Management's Specialist (Ref: [par. .08a](#))

- .A38** Competence relates to the nature and level of expertise of the management's specialist. Capability relates to the ability of the management's specialist to exercise that competence in the circumstances. Factors that influence capability may include, for example, geographic location and the availability of time and resources. Objectivity relates to the possible effects that bias, conflict of interest, or the influence of others may have on the professional or business judgment of the management's specialist. The competence, capabilities, and objectivity of a management's specialist, and any controls within the entity over that specialist's work, are important factors with regard to the reliability of any information produced by a management's specialist.
- .A39** Information regarding the competence, capabilities, and objectivity of a management's specialist may come from a variety of sources, such as the following:
- Personal experience with previous work of that specialist
 - Discussions with that specialist
 - Discussions with others who are familiar with that specialist's work
 - Knowledge of that specialist's qualifications, membership in a professional body or industry association, license to practice, or other forms of external recognition
 - Published papers or books written by that specialist
 - An auditor's specialist, if any, that assists the auditor in obtaining sufficient appropriate audit evidence with respect to information produced by the management's specialist
- .A40** Matters relevant to evaluating the competence, capabilities, and objectivity of a management's specialist include whether that specialist's work is subject to technical performance standards or other professional or industry requirements, for example, ethical standards and other membership requirements of a professional body or industry

association, accreditation standards of a licensing body, or requirements imposed by law or regulation.

.A41 Other matters that may be relevant include

- the relevance of the capabilities and competence of the management's specialist to the matter for which that specialist's work will be used, including any areas of specialty within that specialist's field. For example, a particular actuary may specialize in property and casualty insurance but have limited expertise regarding pension calculations.
- the competence of the management's specialist with respect to relevant accounting requirements, for example, knowledge of assumptions and methods, including models, when applicable, that are consistent with the applicable financial reporting framework.
- whether unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures indicate that it may be necessary to reconsider the initial evaluation of the competence, capabilities, and objectivity of the management's specialist as the audit progresses.

.A42 A broad range of circumstances may threaten objectivity, for example, self-interest threats, advocacy threats, familiarity threats, self-review threats, and intimidation threats. Safeguards may reduce such threats and may be created either by external structures (for example, the profession, legislation, or regulation of the management's specialist) or by the work of the management's specialist environment (for example, quality control policies and procedures).

.A43 Although safeguards cannot eliminate all threats to the objectivity of a management's specialist, threats such as intimidation threats may be of less significance to a specialist engaged by the entity than to a specialist employed by the entity, and the effectiveness of safeguards such as quality control policies and procedures may be greater. Because the threat to objectivity created by being an employee of the entity will always be present, a specialist employed by the entity cannot ordinarily be regarded as being more likely to be objective than other employees of the entity.

.A44 When evaluating the objectivity of a specialist engaged by the entity, it may be relevant to discuss with management and that specialist any interests and relationships that may create threats to the specialist's objectivity and any applicable safeguards, including any professional requirements that apply to the specialist, and to evaluate whether the safeguards are adequate. Interests and relationships creating threats may include the following:

- Financial interests
- Business and personal relationships

- Provision of other services

Obtaining an Understanding of the Work of the Management's Specialist (Ref: [par. .08b](#))

- .A45** An understanding of the work of the management's specialist includes an understanding of the relevant field of expertise. An understanding of the relevant field of expertise may be obtained in conjunction with the auditor's determination of whether the auditor has the expertise to evaluate the work of the management's specialist, or whether the auditor needs an auditor's specialist for this purpose.^{fn 13}
- .A46** Aspects of the field of the management's specialist relevant to the auditor's understanding may include
- whether that specialist's field has areas of specialty within it that are relevant to the audit.
 - whether any professional or other standards and regulatory or legal requirements apply.
 - what assumptions and methods are used by the management's specialist and whether they are generally accepted within that specialist's field and ~~appropriate~~ *appropriately applied under the applicable financial reporting framework for financial reporting purposes.*
 - the nature of internal and external data or information the management's specialist uses.
- .A47** In the case of a management's specialist engaged by the entity, there will ordinarily be an engagement letter or other written form of agreement between the entity and that specialist. Evaluating that agreement when obtaining an understanding of the work of the management's specialist may assist the auditor in determining for the auditor's purposes the appropriateness of
- the nature, scope, and objectives of that specialist's work;
 - the respective roles and responsibilities of management and that specialist; and
 - the nature, timing, and extent of communication between management and that specialist, including the form of any report to be provided by that specialist.
- .A48** In the case of a management's specialist employed by the entity, it is less likely that there will be a written agreement of this kind. Inquiry of the specialist and other members of

Commented [AG2]: See Exhibit B, AS 1105 Appendix A, Note above par. A9

^{fn 13} Paragraph .07 of section 620, *Using the Work of an Auditor's Specialist*.

management may be the most appropriate way for the auditor to obtain the necessary understanding.

Evaluating the Appropriateness of the Work of the Management's Specialist (Ref: [par. .08c](#))

.A49 Considerations when evaluating the appropriateness of the work of the management's specialist as audit evidence for the relevant assertion may include

- if that specialist's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods, taking into account the consistency of those assumptions with relevant information; and
- the relevance and reasonableness of that specialist's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial statements;
- ~~if that specialist's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods; and~~
- if that specialist's work involves significant use of source data, the relevance, completeness, and accuracy of that source data.

.A50 Examples of information that, if relevant, should be taken into account when evaluating significant assumptions developed by the specialist include:

- assumptions generally accepted within the specialist's field;
- supporting information provided by the specialist;
- industry, regulatory, and other external factors, including economic conditions;
- the company's objectives, strategies, and related business risks;
- existing market information;
- historical or recent experience, along with changes in conditions and events affecting the company; and
- significant assumptions used in other estimates tested in the company's financial statements.

.A51 Factors that affect the relevance and reliability of the specialist's work include:

- The results of the auditor's procedures over data, significant assumptions, and methods;
- The nature of any restrictions, disclaimers, or limitations in the specialist's report or equivalent communication; and
- The consistency of the specialist's work with other evidence obtained by the auditor and the auditor's understanding of the company and its environment.

Commented [AG3]: See Exhibit B, AS 1105 Appendix A, Note below par. A8(b)(1).

Commented [AG4]: See Exhibit B, AS 1105 Appendix A, par. A9

A51A If the specialist's method includes the use of a model, the auditor's procedures may include, for example:

- Obtaining an understanding of the model, including the source of the inputs
- Reviewing descriptions of the model in the specialist's report or equivalent communication
- Testing controls over the company's evaluation of the specialist's work
- Testing mathematical accuracy of the calculations under the model
- Assessing the inputs to and output from the model, which may involve using an alternative model for comparison

The extent of such procedures will depend on the type of model used (for example, commercially available versus internally-developed) and the applicability of the factors described in paragraph .A51.

A52 Examples of situations in which additional procedures may be necessary include:

- the specialist's findings and conclusions are inconsistent with (i) other information, if any, in the specialist's report, or equivalent communication, (ii) other evidence obtained by the auditor, or (iii) the auditor's understanding of the company and its environment;
- the specialist's report, or equivalent communication, contains restrictions, disclaimers, or limitations regarding the auditor's use of the report or communication;
- exceptions were identified in performing procedures related to data, significant assumptions, or methods;
- the auditor has doubt about the specialist's knowledge, skill, and ability, or about the company's effect on the specialist's judgments; or
- the specialist has a conflict of interest relevant to the specialist's work.

Commented [AG5]: Adapted from example provided on Pages A3-20-21 of PCAOB Release No. 2018-006

Commented [AG6]: See Exhibit B, AS 1105 Appendix A, note below par. A10