PROPOSED INTERNATIONAL STANDARD ON AUDITING 505
(REVISED AND REDRAFTED) *(Mark up showing changes from ED)*
EXTERNAL CONFIRMATIONS

(Effective for audits of financial statements for periods beginning on or after \[December 15, 2009\])

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Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) establishes requirements and provides guidance for the auditor’s performing use of external confirmation procedures to obtain audit evidence in accordance with the requirements of ISA 330 (Redrafted)\(^1\) and with [proposed] ISA 500 (Redrafted)\(^2\). It does not address inquiries regarding litigation and claims. Part C: Procedures Regarding Litigation and Claims of [Proposed] ISA 501, (Redrafted)\(^3\) “Audit Evidence—Additional Considerations for Specific Items,” deals with obtaining sufficient appropriate audit evidence establishes requirements and provides guidance on such inquiries. [ISSUE A]

External Confirmation Procedures as a Response to Assessed Risks (Ref: Para. A1-A5)

2. [Proposed] ISA 500 (Redrafted) indicates that the reliability of audit evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained.\(^4\) That ISA also includes the following generalizations applicable to audit evidence that may be relevant to external confirmations:\(^5\) (Ref: Para. A1-A6)

- 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.

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 internally generated evidence generated internally by the entity. This ISA is intended to assist the auditor in designing and performing external confirmation procedures to obtain relevant and reliable audit evidence.

3. Other ISAs recognize the importance of external confirmations as audit evidence, for example:

- ISA 330 (Redrafted) requires that the auditor obtain more persuasive audit evidence the higher the auditor’s assessment of risk.\(^6\) Consequently, as the assessed when

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\(^1\) ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks.”
\(^3\) [Proposed ISA 501 (Redrafted), “Audit Evidence Regarding Specific Financial Statement Account Balances and Disclosures.”
\(^5\) [Proposed] ISA 500 (Redrafted), paragraph A23.
\(^6\) ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks,” paragraph 7(b).
obtaining more persuasive audit evidence because of a higher assessment of risk of material misstatement increases, 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 by placing more emphasis on obtaining third party evidence directly from third parties or by obtaining corroborating evidence from a number of independent sources. ISA 330 (Redrafted) 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.7 [ISSUE A]

- ISA 240 (Redrafted) 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.8
- [Proposed] ISA 500 (Redrafted) indicates that corroborating information obtained from a source independent of the entity, such as external confirmations, may increase the assurance the auditor obtains from evidence existing within the accounting records or from representations made by management.9

Effective Date

4. This ISA is effective for audits of financial statements for periods beginning on or after [December 15, 2009].

Objective

5. The objective of the auditor, when the auditor has determined that using external confirmation procedures is appropriate in the circumstances of the audit, in response to an assessed risk of material misstatement is to design and perform such procedures to obtain relevant and reliable audit evidence. [ISSUE D]

Definitions

6. For purposes of the ISAs, the following terms have the meanings attributed below:

(a) External confirmation – Audit evidence obtained as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.

(b) Positive confirmation request – A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

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7 ISA 330 (Redrafted), paragraph A49.
9 [Proposed] ISA 500 (Redrafted), paragraph A2.
(c) Negative confirmation request – A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.

(d) Non-response – A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered.

(e) 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.

Requirements

External Confirmation Procedures

7. When the auditor decides to use external confirmation procedures in response to an assessed risk of material misstatement, the auditor shall maintain control over the external confirmation requests and responses, including:

(a) Determining the information to be confirmed or requested;

(b) Selecting the appropriate confirming party (Ref: Para. A6);

(c) Designing the confirmation requests, including determining that requests are appropriately addressed and contain return information for responses to be sent directly to the auditor (Ref: Para. A7-A10); and

(d) Communicating with the confirming party, including determining that requests are appropriately addressed and include return information for responses to be sent directly to the auditor, and sending the requests to the confirming party (Ref: Para. A11); and,

8. Evaluating. The auditor shall evaluate the evidence obtained (responses, non-responses and exceptions) from the external confirmation procedures results from individual external confirmation requests. (Ref: Para. A2-A14)

Management’s Refusal to Allow the Auditor to Send a Confirmation Request

89. If management refuses to allow the auditor to send a confirmation request, then the auditor shall:

(a) Evaluate the reasonableness of management’s refusal by challenging the reasons provided by management and seeking evidence about the validity of such reasons. Inquire as to management’s reasons for the refusal, seek evidence about their validity and evaluate them; (Ref: Para. A12-A13)

(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: Para. A13-A14)

(c) Where possible, perform alternative audit procedures designed to obtain relevant and reliable audit evidence. (Ref: Para. A14-A15)
9. If the auditor concludes that management’s refusal to allow the auditor to send a confirmation request is unreasonable, or the auditor is unable to obtain relevant and reliable audit evidence from alternative audit procedures performed in accordance with paragraph 8(e), the auditor shall communicate with those charged with governance in accordance with ISA 260 (Revised and Redrafted) and The auditor also shall consider the possible effect on the auditor’s opinion in accordance with [proposed] ISA 705 (Revised and Redrafted).

Results of the External Confirmation Procedures (Ref: Para. A15)

Reliability of Responses to Confirmation Requests

4. If the auditor identifies factors that give rise to doubts about the reliability of information included in the response to a confirmation request, the auditor shall obtain further audit evidence to resolve those doubts. (Ref: Para. A16-A19)

12. If the auditor determines that information included in a response to a confirmation request is not reliable, the auditor shall evaluate the implications on the assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures. (Ref: Para. A20)

Non-Responses

13. In the case of non-responses, the auditor shall perform alternative audit procedures to obtain relevant and reliable audit evidence. (Ref: Para A21-A22)

When a Response to a Positive Confirmation Request is Necessary to Obtain Sufficient Appropriate Audit Evidence [ISSUE F]

14. If the auditor determines that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence to respond to assessed risks of material misstatement, alternative audit procedures will not provide the audit evidence the auditor requires, and If the auditor does not obtain such confirmation, the auditor shall determine the implications for the audit and the auditor’s opinion in accordance with [proposed] ISA 705 (Revised and Redrafted). (Ref: Para A21-A23)

Exceptions

15. The auditor shall investigate exceptions to determine whether or not they represent misstatements. (Ref: Para. A24-A25)

Negative Confirmations [ISSUE C]

16. Negative confirmations provide less persuasive audit evidence than positive confirmations. Accordingly, the auditor shall only use negative confirmation requests as the
sole substantive audit procedure to address an assessed risk of material misstatement at the assertion level when:

(a) The auditor has obtained sufficient appropriate audit evidence regarding the operating effectiveness of controls relevant to the assertion; and

(b) The auditor has concluded that the risk of material misstatement is low, and:

(a) The population of items subject to negative confirmation procedures comprises a large number of small, homogeneous, account balances, transactions or conditions;

(b) A very few or no exceptions are expected; and

(e) The auditor has no reason to believe that recipients of negative confirmation requests will disregard such confirmation requests. (Ref: Para. A26)

Evaluating the Evidence Obtained

The auditor shall evaluate whether the results of the external confirmation procedures provide relevant and reliable audit evidence, or whether performing further audit procedures is necessary. (Ref: Para A27)

Application and Other Explanatory Material

External Confirmation Procedures as a Response to Assessed Risks (Ref: Para. 2-3)

A1. ISA 330 (Redrafted) deals with the auditor’s responsibility to design and implement responses to the risks of material misstatement that the auditor has identified and assessed in accordance with ISA 315 (Redrafted). Such responses are designed to enable the auditor to obtain sufficient appropriate audit evidence. External confirmation procedures can provide relevant and reliable audit evidence that assists the auditor, either alone or together with other audit procedures, in obtaining sufficient appropriate audit evidence.

Relevance of External Confirmations

A2. External confirmation procedures frequently are relevant when addressing assertions associated with account balances and their constituent parts, but need not be restricted to these items. For example, the auditor may request 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 confirmation request may specifically address the absence of a “side agreement” that may be relevant to an entity’s cut-off assertion. Other situations where external confirmation procedures may provide relevant audit evidence in responding to assessed risks of material misstatement include:

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• Bank balances and other information relevant to banking relationships.
• Accounts receivable balances and terms.
• 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.

A3. Although external confirmations may provide relevant evidence relating to certain assertions, there are some assertions for which external confirmations provide less relevant evidence. For example, external confirmations provide less relevant evidence relating to the recoverability of accounts receivable balances, than they do of their existence.

A4. The auditor may determine that external confirmation procedures prepared performed for one purpose provide an opportunity to obtain audit evidence about other matters. For example, confirmation requests for bank balances often include requests for other information relevant to other assertions in the financial statements. Such considerations may influence the auditor’s decision about whether to use perform external confirmation procedures.

Considerations in Determining the Appropriateness of External Confirmations

A5. Factors that may assist the auditor in determining whether external confirmation procedures are an appropriate response to an assessed risk of material misstatement include:

• The confirming party’s knowledge of the subject matter – if the subject matter of external confirmation procedures is complex or highly subjective, responses may be more reliable if provided by a person at the confirming party who is more knowledgeable has the requisite knowledge about the information being confirmed.
• The ability or willingness of the intended confirming party to respond – for example, the confirming party:
  o May not accept responsibility for responding to a confirmation request.
  o May consider responding too costly or time consuming.
  o May have concerns about the potential legal liability resulting from responding.
  o May account for transactions in different currencies.
  o May operate in an environment where responding to confirmation requests is not a significant aspect of day-to-day operations.
In such situations, confirming parties may not respond, may respond in a casual manner or may attempt to restrict the reliance placed on the response.

- The objectivity of the intended confirming party – if the confirming party is a related party of the entity, responses to confirmation requests may be less reliable.

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

A6. In certain circumstances, the auditor may determine that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence to address an assessed risk of material misstatement. Examples of such circumstances include where:

- The information available to corroborate management’s assertion(s) is only available outside the entity;
- The entity’s information systems and internal controls are unreliable or ineffective;
- Specific fraud risk factors, such as the risk of management override of internal controls, prevent the auditor from relying on evidence from the entity.

External Confirmation Procedures (Ref: Para. 7)

Control Over External Confirmation Requests and Responses

A7. Controlling communications between the intended confirming parties and the auditor reduces the risk of unreliable results of the external confirmation procedures.

Selecting the Appropriate Confirming Party (Ref: Para. 7(b))

A6. Responses to confirmation requests provide more relevant and reliable audit evidence when confirmation requests are sent to a confirming party the auditor believes is knowledgeable about the information to be confirmed. For example, a financial institution official who is knowledgeable about the transactions or arrangements for which confirmation is requested may be the most appropriate person at the entity from whom to request confirmation. [ISSUE F]

Designing Confirmation Requests (Ref: Para. 7(c))

A7. The design of a confirmation request may directly affect the confirmation response rate, and the reliability and the nature of the audit evidence obtained from responses.

A8. Factors to consider when designing confirmation requests may include:

- The assertions being addressed.
- Specific identified risks of material misstatement, including fraud risks.
- The layout and presentation of the confirmation request.
- Prior experience on the audit or similar engagements.
- The method of communication (for example, in paper form, or by electronic or other medium).
Management’s authorization or encouragement to the confirming parties to respond to the auditor. Confirming parties may only be willing to respond to a confirmation request containing management’s authorization.

The ability of the intended confirming party to confirm or provide the requested information (for example, individual invoice amount versus total balance).

A9. A positive external confirmation request asks the confirming party to reply to the auditor in all cases, either by indicating the confirming party’s agreement with the given information, or by asking the confirming party to provide information. A response to a positive confirmation request ordinarily is expected to provide reliable audit evidence. There is a risk, however, that a confirming party may reply to the confirmation request without verifying that the information is correct. The auditor may not be able to detect whether this has occurred. The auditor may reduce this risk by using positive confirmation requests that do not state the amount (or other information) on the confirmation request, and ask the confirming party to fill in the amount or furnish other information. On the other hand, use of this type of “blank” confirmation request may result in lower response rates because additional effort is required of the confirming parties. [ISSUE H]

Identifying the Appropriate Confirming Party

A10. Responses to confirmation requests provide more relevant and reliable audit evidence when confirmation requests are sent to a confirming party the auditor believes is knowledgeable about the information to be confirmed. For example, a financial institution official who is knowledgeable about the transactions or arrangements for which confirmation is requested may be the most appropriate person at the intended confirming party from which to request confirmation. The auditor may consider evaluating the validity of some or all of the addresses on confirmation requests before these are sent out.

Follow-Up on Confirmation Requests (Ref: Para. 7(d))

A11. The auditor may perform procedures to obtain external confirmations for non-responses. Send an additional confirmation request when a reply to a previous request has not been received within a reasonable time. For example, the auditor may, having re-verified the accuracy of the original address, and then send an additional or follow-up requests.

Evaluating the Results from Individual External Confirmation Requests (Ref: Para. 8)

A12. When evaluating the results from individual external confirmation requests, the auditor may categorize results as follows:

(a) A response by the appropriate confirming party indicating agreement with the information provided in the confirmation request, or providing requested information without exception;

(b) A response deemed unreliable;

(c) A non-response; or
(d) A response indicating an exception.

Management’s Refusal to Allow the Auditor to Send a Confirmation Request

**Reasonableness of Management’s Refusal** (Ref: Para 89(a))

A12A13. A refusal by management to allow the auditor to send a confirmation request is a limitation on the audit evidence the auditor may wish to obtain. The auditor is therefore required to challenge inquire as to the reasons for the limitation. A common reason advanced is the existence of a legal dispute or ongoing negotiation with the intended confirming party, the resolution of which may be affected by an untimely confirmation request. The auditor is required to evaluate such reasons and to seek audit evidence about their validity because of the risk that management may be attempting to deny the auditor access to audit evidence that may reveal fraud or error.

**Implications on for the Assessment of Relevant Risks of Material Misstatement** (Ref: Para 89(b))

A13A14. The auditor may conclude from the evaluation in paragraph 89(b) that it would be appropriate to revise the assessment of the relevant risks of material misstatement at the assertion level and modify planned audit procedures accordingly, in accordance with ISA 315 (Redrafted).13 For example, if management’s request to not confirm is unreasonable, this may indicate a fraud risk factor that requires further evaluation in accordance with ISA 240 (Redrafted).14

**Alternative Audit Procedures** (Ref: Para 89(c))

A14A15. The alternative audit procedures performed may be similar to those appropriate for a non-response as set out in paragraphs A21-A23-A22 of this ISA. Such procedures also would take account of the results of the auditor’s evaluation as discussed in paragraph 89(b) of this ISA.

**Results of the External Confirmation Procedures** (Ref: Para. 10-13)

A15. When considering responses to confirmation requests and whether they provide audit evidence that addresses an assessed risk of material misstatement, the auditor may categorize responses as follows:

(a) A response by the appropriate confirming party indicating agreement with the information provided in the confirmation request, or providing requested information;

(b) A response deemed unreliable;

(c) A non-response; or

(d) A response indicating an exception.

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13 ISA 315 (Redrafted), paragraph 30.
14 ISA 240 (Redrafted), paragraph 24.
Reliability of Responses to Confirmation Requests (Ref: Para. 111)

A16. [Proposed] ISA 500 (Redrafted) indicates that even when audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability. No response is without some risks of interception, alteration or fraud. Such risks exist regardless of whether the response is in paper form, or by electronic or other medium. Accordingly, the auditor may assess the reliability of a response by evaluating factors that may indicate doubts about the reliability of a response include whether that it:

- Was received directly by the auditor indirectly;
- Appeared not to come from the originally intended confirming party; and/or
- Was received by a means that does not provide sufficient evidence as to the identity of the originating party.

A17. The auditor is required to determine what modifications to, or additional, procedures are necessary to resolve doubts over the reliability of information to be used as audit evidence. The auditor may choose to verify the source and contents of a response to a confirmation request by contacting the purported confirming party. When a response has been returned to the auditor indirectly (for example, because the confirming party incorrectly addressed it to the entity rather than to the auditor), the auditor may request the purported confirming party to respond in writing directly to the auditor.

A18. 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. However, upon obtaining an oral response to a confirmation request, the auditor may, depending on the circumstances, request the confirming party to respond in writing directly to the auditor, or seek other audit evidence to support the information in the oral response.

A19. A response to a confirmation request may contain restrictive language regarding its use. Such restrictions do not, in themselves, necessarily invalidate the reliability of the response as audit evidence.

Unreliable Responses (Ref: Para. 12)

A20. When the auditor concludes that a response is unreliable, the auditor may need to revise the assessment of the relevant risks of material misstatement at the assertion level and modify planned audit procedures accordingly, in accordance with ISA 315 (Redrafted). For example, an unreliable response may indicate a fraud risk factor that requires further evaluation in accordance with ISA 240 (Redrafted).

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15 [Proposed] ISA 500 (Redrafted), paragraph A23.
16 [Proposed] ISA 500 (Redrafted), paragraph 14.
Non-Responses (Ref: Para. 4213)

A21. Examples of alternative audit procedures the auditor may perform when a response to a positive confirmation request is not considered necessary to obtain sufficient appropriate audit evidence include:

- For accounts receivable balances – examining specific subsequent cash receipts, shipping documentation, and sales near the period-end, to provide audit evidence for the cut-off assertion.
- For accounts payable balances – examining subsequent cash disbursements or correspondence from third parties, and other records, such as goods received notes.
- For bank balances – directly accessing information held by a third party concerning the client’s-entity’s account.

A22. The nature and extent of alternative audit procedures are affected by the assessed risk of material misstatement at the assertion level. A non-response to a confirmation request may indicate a previously unidentified risk of material misstatement. In such a situation, the auditor may need to revise the assessed risk of material misstatement at the assertion level, and modify planned audit procedures, in accordance with ISA 315 (Redrafted). For example, a non-response to a confirmation request may indicate a previously unidentified fraud risk factor that requires further evaluation in accordance with ISA 240 (Redrafted).

A23. If a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence to address an assessed risk of material misstatement, and the auditor does not receive an external confirmation, an inability to obtain sufficient appropriate audit evidence results. [Proposed] ISA 705 (Revised and Redrafted) establishes requirements and provides guidance when there is an inability to obtain sufficient appropriate audit evidence. [ISSUE F]

When a Response to a Positive Confirmation Request is Necessary to Obtain Sufficient Appropriate Audit Evidence (Ref. Para. 14)

A23. In certain circumstances, the auditor may determine that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence to address an assessed risk of misstatement. Examples of such circumstances include where:

- The information available to corroborate management’s assertion(s) is only available outside the entity.
- The entity’s information systems and controls are unreliable or ineffective.
- Specific fraud risk factors, such as the risk of management override of controls, or the risk of collusion which can involve employee(s) and/or management, prevent the auditor from relying on evidence from the entity.

Exceptions (Ref: Para. 4315)

A24. Exceptions noted in responses to confirmation requests may assist the auditor in determining the extent of misstatements and potential misstatements. When the auditor
identifies a misstatement, the auditor is required by ISA 240 (Redrafted) to evaluate whether such misstatement is indicative of fraud. Exceptions may provide a guide to the quality of responses from similar confirming parties or for similar accounts. Exceptions also may indicate a weakness in the entity’s internal control over financial reporting.

A25. Some exceptions do not represent misstatements. For example, the auditor may conclude that differences in responses to confirmation requests are due to timing, measurement, or clerical errors in the external confirmation procedures.

**Negative Confirmations** (Ref: Para. 14)

A26. The failure to receive a response to a negative confirmation request does not explicitly indicate receipt by the intended confirming party of the confirmation request and-or verification of the accuracy of the information contained in the request. Accordingly, a non-response failure of a confirming party to respond to a negative confirmation request provides significantly less persuasive audit evidence than does a response to a positive confirmation request. Confirming parties also are more likely to respond indicating their disagreement with a negative confirmation request when the information in the request is not in their favor, and less likely to respond otherwise, unless the information is material to them. For example, holders of bank deposit accounts are more likely to respond if they believe that the balance in their account is understated in the confirmation request, but are less likely to respond when they believe the balance is overstated or accurate. Therefore, sending negative confirmation requests to holders of bank deposit accounts may be a useful procedure in considering whether such balances may be understated, but is unlikely to be effective if the auditor is seeking evidence regarding overstatement. [ISSUE C]

**Evaluating the Evidence Obtained** (Ref: Para 17)

A27. The auditor’s evaluation, when taken into account with other audit procedures the auditor may have performed in response to assessed risks of misstatement, may assist the auditor in concluding whether sufficient appropriate audit evidence has been obtained or whether performing further audit procedures is necessary, as required by ISA 330 (Redrafted).  

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17 Refer to ISA 240 (Redrafted), paragraph 35.

18 ISA 330 (Redrafted), paragraphs 27 and 28.
CONFORMING AMENDMENTS TO OTHER ISAS

[Proposed] ISA 500 (Redrafted), “Audit Evidence”

A16. Confirmation is a specific type of inquiry that is the process of obtaining a representation of information or of an existing condition directly from a third party. Confirmations are frequently used in relation to account balances and their components. An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. External confirmation procedures frequently are used in relation to account balances and their constituent parts. For example, the auditor may seek direct confirmation of receivables by communication with debtors. However, external confirmations need not be restricted to these items. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request is designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are. External confirmations also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a “side agreement” that may influence revenue recognition. See [proposed] ISA 505 (Revised and Redrafted), “External Confirmations” for further guidance.

ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks” [ISSUE A]

Substantive Procedures Responsive to Significant Risks (Ref: Para. 22)

A49. Paragraph 22 of this ISA requires the auditor to perform substantive procedures that are specifically responsive to risks the auditor has determined to be significant risks. Substantive procedures related to significant risks ordinarily are designed to obtain audit evidence with high reliability, for example, by placing more emphasis on obtaining third party evidence or by obtaining corroborating evidence from a number of independent sources. Audit evidence in the form of external confirmations received directly by the auditor from confirming parties 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.

For example, if the auditor identifies that management is under pressure to meet earnings expectations, there may be a risk 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 non-financial personnel in the entity regarding any changes in sales agreements and delivery terms. Substantive procedures related to significant risks are most often designed to obtain audit evidence with high reliability.