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Basis for Conclusions: ISA 230 (Redrafted), Audit Documentation

*Prepared by the Staff of the International Auditing and
Assurance Standards Board*



**International Federation
of Accountants**

**BASIS FOR CONCLUSIONS:
ISA 230 (REDRAFTED), AUDIT DOCUMENTATION**

This Basis for Conclusions has been prepared by staff of the International Auditing and Assurance Standards Board (IAASB). It relates to, but does not form part of, ISA 230 (Redrafted), “Audit Documentation,” which was unanimously approved by the IAASB in September 2007.

Background

1. In September 2006, the IAASB agreed the conventions to be used in drafting future International Standards on Auditing (ISAs). These conventions are commonly referred to as the IAASB’s Clarity conventions.¹
2. The IAASB has undertaken to redraft all of its ISAs in accordance with the Clarity conventions. This approach responds to the desire for all ISAs to be consistently drafted, and subject to a single statement of their authority and effect. The IAASB has agreed, in response to the general call for the Clarity project to be completed within a reasonable time, that while a significant number of the ISAs are under substantive revision as well as redrafting to reflect the new conventions, others will be subject to a limited redrafting to reflect only the conventions and matters of clarity generally. ISA 230 is in the latter category.
3. The IAASB issued an exposure draft of proposed ISA 230 (Redrafted) (“ED-ISA 230”) in December 2006, with a comment date of March 31, 2007. The exposure draft represented:
 - (a) The amendment of extant ISA 230 to reflect required changes as a result of the amendment to the Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services (Preface) that the IAASB approved in September 2006 (“amended extant ISA 230”); and
 - (b) The redrafting of amended extant ISA 230 in accordance with the Clarity conventions.

The IAASB received forty-five comment letters from a variety of respondents, including regulators, IFAC member bodies, and firms. Input was also received from the IFAC Small and Medium Practices Committee. The IAASB made changes to ED-ISA 230 in response to these comments.

¹ The IAASB’s Clarity conventions, and the authority and obligation attaching to them, are established in the amended Preface to International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services. (Preface.) The amended Preface can be accessed at http://www.ifac.org/download/IAASB_Preface.pdf. Elements of the authority and obligation attaching to the Clarity conventions are currently being exposed as part of proposed ISA 200 (Revised and Redrafted), “Overall Objective of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing.”

4. This Basis for Conclusions explains the more significant issues raised by respondents on ED-ISA 230, and how the IAASB addressed them. In general, ED-ISA 230 received strong support from respondents. No one issue discussed below was raised by more than six respondents.

Scope of the ISA

5. The effective date paragraph in the extant ISA indicates that the ISA is effective for audits of financial information for periods beginning on or after June 15, 2006. One respondent suggested that this paragraph should be reworded to focus on financial *statements* as opposed to financial *information*. Another respondent noted that the wording in paragraph A23 of ED-ISA 230 was inconsistent with wording used in the exposure draft of proposed ISA 560 (Redrafted)² because the former used the phrase “after the financial *information* has been issued” whereas the latter used the phrase “after the financial *statements* have been issued.”
6. The IAASB acknowledged the need to be consistent with the approach taken in other ISAs that are being redrafted under the Clarity project. Accordingly, the IAASB decided that ISA 230 (Redrafted) should focus on the audit of *financial statements*, with appropriate wording about the application of the ISA to audits of other historical financial information (see paragraph 1 of the ISA). The IAASB agreed to consequential changes to the effective date paragraph (paragraph 4), and paragraph A20 of the ISA.

Definitions

Experienced Auditor

7. Three respondents noted that the definition of “experienced auditor” in ED-ISA 230 did not specify the need for that individual to have relevant experience in performing audits. They commented that it would be unrealistic to expect an individual lacking relevant *audit* experience in relation to the entity to perform reviews of the audit working papers satisfactorily. They noted that a graduate or postgraduate could have a reasonable understanding of the matters listed in the definition, but little or no practical experience of performing audits in relevant industries. Accordingly, they suggested that the definition be clarified to indicate that it includes an expectation of relevant audit experience.
8. The IAASB noted that the extant definition did not include any specific reference to practical audit experience because the term “*experienced* auditor” in itself implied a need for that individual to have had practical experience of participating in audits. The IAASB did not agree to the criterion that the individual have relevant experience of audits in the entity’s specific industry because this would have been a substantive change to an ISA that was simply being redrafted, and could have been read as implying a significant limit to the universe of individuals who would be deemed competent to perform reviews of the working papers.

² Proposed ISA 560 (Redrafted), “Subsequent Events,” paragraph 1.

9. The IAASB, however, decided that as a point of clarification, the definition of an experienced auditor should specify that the individual should have practical audit experience (see paragraph 6(c) of the ISA). The IAASB believes that no change in substance results from this clarification.

Audit Documentation

10. One respondent was of the view that the definition of the term “audit documentation” should be revised to clarify that risk assessment and planning are also intended to be covered by the general documentation requirements in the ISA. The respondent argued that it would be important for the definition to mention these aspects of the audit along with “the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached” because the documentation of the basis for planning the audit should also be done in a way that “would enable an experienced auditor, having no previous connection with the audit, to understand ... [what was done].”
11. The IAASB noted that audit procedures include planning and risk assessment procedures. The IAASB believes that, for the purposes of a definition of audit documentation, it would be inappropriate to single out those two aspects of the audit as this would downplay the importance of other areas for documentation. Accordingly, the IAASB determined that the definition of audit documentation should not be changed.
12. However, as a point of emphasis, the IAASB agreed to clarify that audit documentation needs to provide evidence that the audit was *planned* and performed in accordance with ISAs and applicable legal and regulatory requirements (see paragraphs 2(b) and 5(b) of the ISA).

“Negative Requirements”

13. A number of respondents noted that the application and other explanatory material in ED-ISA 230 contained guidance that described restrictions or limitations on the scope of application of specific requirements. Some of them argued that these restrictions were in effect “negative requirements,” and that separating the actual requirements from material circumscribing their scope was contrary to the clarity principles and would not promote consistency of performance. They suggested that incorporating these “negative requirements” into the relevant places in the Requirements section would better help avoid excessive documentation.
14. The respondents singled out, in particular, the following statements in the application and other explanatory material of ED-ISA 230 as being fundamental to the proper application of the related requirements:
 - Paragraph A4: The auditor *need not* include in audit documentation superseded drafts of working papers and financial statements, notes that reflect incomplete or preliminary thinking, previous copies of documents corrected for typographical or other errors, and duplicates of documents.
 - Paragraph A5: Oral explanations by the auditor, on their own, *do not* represent adequate support for the work the auditor performed or conclusions the auditor

reached, but may be used to explain or clarify information contained in the audit documentation.

- Paragraph A7: ... it is *neither* necessary *nor* practicable for the auditor to document every matter considered in an audit. Further, it is *unnecessary* for the auditor to document separately compliance with matters for which compliance is self-evident within the audit file. ...
 - Paragraph A13: The documentation of how the auditor addressed inconsistencies in information *does not* imply that the auditor needs to retain documentation that is incorrect or superseded.
 - Paragraph A17: The documentation requirement applies *only* to requirements that are relevant in the circumstances. ...
 - Paragraph A19: The requirement to document who reviewed the audit work performed *does not* imply a need for each specific working paper to include evidence of review. ...
 - Paragraph A21: The completion of the assembly of the final audit file after the date of the auditor's report is an administrative process that *does not* involve the performance of new audit procedures or the drawing of new conclusions.
15. Further, some of the respondents noted that, because certain jurisdictions may adopt the ISAs into law and give the requirements a higher level of legal authority than the application and other explanatory material, there was ground for considering whether these “negative requirements” should be elevated to essential guidance to the relevant requirements to make clear the particular limitations attaching to those requirements.
16. The IAASB noted that the purpose of these negative statements is to *explain* the scope and application of the requirements. The statements do not by themselves impose additional obligations on the auditor. The IAASB believes that incorporating these statements into the Requirements section may initiate a practice that would undermine the requirements in the ISAs. In particular, the more these negative clauses are incorporated into the requirements, the more doubt may be cast on the proper limitations of requirements to which no limiting language is attached. Further, such practice would detract from the specific documentation obligations the IAASB intends the auditor to fulfill. It would also devalue the role of the application and other explanatory material. The IAASB was of the view that there should be no doubt that the requirements of each ISA should be read in light of the application and other explanatory material.³ Accordingly, the IAASB determined that the negative statements listed above should remain in the application and other explanatory material.

Assembly of the Final Audit File and Definition of Audit File

17. One respondent noted that there were a number of assumptions throughout ED-ISA 230 that audit documentation will be maintained in an audit file but there was no clear

³ Proposed ISA 200 (Revised and Redrafted), paragraph 21, requires the auditor to consider the entire text of an ISA to understand its requirements.

requirement that this should be the case. The respondent also noted that, although the term “audit file” was used throughout ED-ISA 230, it was undefined. Another respondent suggested that the statement in the application and other explanatory material to the effect that “audit documentation for a specific audit engagement is assembled in an audit file” should be reconsidered as the present tense seemed to suggest an obligation on the auditor.

18. The IAASB decided that it would be appropriate for the term “audit file” to be defined given that it is used in several places in the ISA. This definition is set out in paragraph 6(b) of the ISA. The definition allows for electronic files.
19. The IAASB also determined that it would be appropriate to elevate the particular occurrence of the present tense noted above to a requirement to make clear the expectation that audit documentation be assembled in an audit file. Accordingly, a requirement to that effect has been added in paragraph 14 of the ISA.

Changes to Audit Documentation after the Date of the Auditor’s Report

20. Paragraph 14 of ED-ISA 230 established a requirement for the auditor to document changes to audit documentation after the completion of the assembly of the final audit file, whereas paragraph 15 of ED-ISA 230 established a requirement for the auditor to document changes to audit documentation arising in exceptional circumstances after the date of the auditor’s report. One respondent noted that these two requirements overlapped to some extent given that they would both cover changes made to the audit file after the date of the auditor’s report.
21. The IAASB acknowledged the element of overlap. It therefore re-ordered the two requirements so that changes of substance to the audit documentation in exceptional circumstances after the date of the auditor’s report would first be dealt with in the section addressing the auditor’s documentation of the audit procedures performed and audit evidence obtained (see paragraph 13 of the ISA). Any other necessary changes to the audit documentation after assembly of the final audit file has been completed would then be dealt with in the section addressing assembly of the final audit file (see paragraph 16 of the ISA).
22. Two respondents questioned why the requirement to review the changes to audit documentation was qualified with the words “where applicable.” They argued that changes to audit documentation should always be reviewed to ensure an element of quality control. The IAASB accepted this suggestion because with the stringent requirement for completion of file assembly on a timely basis (ordinarily 60 days after the date of the auditor’s report), there is no longer an expectation that changes to audit documentation after that date would occur as a matter of routine. The IAASB therefore deleted the qualifying words “where applicable” from the requirements in paragraphs 13 and 16 of the ISA.
23. In addition, with regard to paragraph 16 of the ISA, the IAASB deleted the requirement for the auditor to document why the changes to the audit documentation have no effect on the auditor’s conclusions and the auditor’s report. This is because such changes would not be expected to be substantive unlike those that affect the auditor’s conclusions and the auditor’s report addressed in the requirement of paragraph 13. As indicated above, all changes will be reviewed.

24. The IAASB believes that the changes to these two paragraphs improve the distinction between the two requirements.

Documentation of Compliance with ISAs

Documentation of Compliance with Every Relevant Requirement

25. Many respondents welcomed the addition of guidance in the exposure draft to clarify the requirement that documentation provide evidence that the audit was performed in accordance with ISAs (paragraph A6-A7 of ED-ISA 230). Several of them, however, suggested that the guidance further stress that it is neither necessary nor practicable for the auditor to document how the auditor has complied with every requirement in the ISAs.
26. The IAASB noted that, although this suggestion is intended to emphasize that the auditor need not document compliance with each and every relevant requirement in the ISAs, it could have the unintended effect of implying that compliance with relevant requirements for which documentation is necessary *sometimes* need not be demonstrated in the audit documentation. The IAASB believes that the negative consequences of this potential outcome would far outweigh the perceived benefits of making the suggested emphasis. Further, the IAASB believes that such an emphasis is unnecessary given that paragraph A7 of the ISA already makes clear that:
- It is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit; and
 - It is unnecessary for the auditor to document separately compliance with matters for which compliance is demonstrated by documents included within the audit file.

Accordingly, the IAASB determined that it would not be appropriate to accept the respondents' suggestion.

Extent of Evidence to Demonstrate Compliance

27. In illustrating the statement that it is unnecessary for the auditor to document separately compliance with matters for which compliance is self-evident within the audit file, paragraph A7 in ED-ISA 230 indicated, amongst other things, that:
- Documentation of specific procedures performed to corroborate management's responses to the auditor's inquiries provides *some* evidence that the auditor has maintained appropriate professional skepticism in compliance with the ISAs; and
 - Documentation of the engagement partner's timely involvement in the audit, such as participation in the team discussions required by ISA 315 (Redrafted),⁴ provides *some* evidence that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the ISAs.

⁴ ISA 315 (Redrafted), "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment," paragraph 10.

28. Two respondents questioned the use of the expression “some evidence” in these illustrations. They suggested that this terminology implied that additional documentation would be necessary to demonstrate full compliance with the ISAs.
29. The IAASB agreed that this was not the intention, and that clarification was warranted in these circumstances. The IAASB therefore reworded these specific examples to state more clearly in paragraph A7 of the ISA that:

“In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:

- For example, there may be no single way in which the auditor’s professional skepticism is documented. But the audit documentation may nevertheless provide evidence of the auditor’s exercise of professional skepticism in accordance with the ISAs. Such evidence may include specific procedures performed to corroborate management’s responses to the auditor’s inquiries.
- Similarly, that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the ISAs may be evidenced in a number of ways within the audit documentation. This may include documentation of the engagement partner’s timely involvement in aspects of the audit, such as participation in the team discussions required by ISA 315 (Redrafted).⁵”

Documentation of Significant Professional Judgments

Use of “Would” Terminology

30. Paragraph A10 of ED-ISA 230 listed “examples of circumstances in which it *would* be appropriate for the auditor to prepare audit documentation relating to the use of professional judgment, where the matters and judgments are significant.” A number of respondents expressed concerns about the use of the verb “would” in this context. They were of the view that the use of “would” could create confusion as to whether the examples listed were intended to be requirements or not. One of the respondents suggested that it would be more appropriate to use the word “may” in place of “would” in this case.
31. The IAASB had discussed this issue when finalizing ED-ISA 230 and had concluded that using “would” in this context was appropriate. This is because the examples are so drafted as to represent cases where a specific requirement applies, and not as examples of what might be done out of a number of possibilities to fulfill a specific requirement. Consequently, in the circumstances set out in those examples, documentation *is* required by the ISA.

⁵ ISA 315 (Redrafted), “Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment,” paragraph 10.

32. However, the IAASB acknowledged that it was possible to redraft the introduction to the paragraph to avoid any possible misunderstanding. Accordingly, the IAASB rephrased this guidance to state in paragraph A10 of the ISA that:

“Some examples of circumstances in which, in accordance with paragraph 8, it is appropriate to prepare audit documentation relating to the use of professional judgment include, where the matters and judgments are significant, ...”

This makes it clear that the illustrations represent cases where the specific requirement in paragraph 8 of the ISA applies.

33. The IAASB did not accept the suggestion that the use of “would” in this instance should be replaced with “may,” as this would incorrectly suggest that documentation might not be mandatory in the circumstances.

Documentation of the Application of ‘Shall Consider’ Requirements

34. The first example in paragraph A10 of ED-ISA 230 indicated that the auditor would document “the *information or factors* considered that were important in forming the relevant professional judgment, when a requirement provides that the auditor ‘shall consider’ certain information or factors.” Several respondents found this to be unclear. Two of them, in particular, were of the view that the reference to documenting *information or factors* considered in relation to a ‘shall consider’ requirement could be misinterpreted to mean *all* information and factors considered, which they argued would be impracticable. They suggested that, rather than information or factors, what should be documented in this circumstance should be the rationale for the auditor’s conclusions.
35. Other respondents noted that this example was insufficiently clear as to whether the auditor is required to document the application of *all* ‘shall consider’ requirements or only those that are significant in the context of the particular engagements. They argued that compliance with the former would be impracticable and suggested that the guidance be clarified in this respect.
36. The IAASB acknowledged that there was scope for misunderstanding the meaning of the words “information or factors,” particularly given that the respondents appear to have interpreted these words to mean *all* information or factors rather than simply those that were *important* in forming the relevant professional judgment. The IAASB therefore agreed that the example should be clarified to focus on the rationale for the auditor’s conclusion regarding a significant consideration required in the engagement circumstances.
37. With respect to the respondents’ concern regarding whether the ISA required documentation of all ‘shall consider’ requirements, the IAASB noted that the qualifying words “where the matters and judgments are significant” in the introductory part of the paragraph appeared to have been overlooked by the respondents. Nevertheless, for the avoidance of doubt, the IAASB further emphasized in the illustrative guidance that the documentation requirement is intended to apply only where the consideration is *significant in the context of the particular engagement*. (See paragraph A10 of the ISA.)

Documentation of Further Audit Procedures Deemed Necessary

38. Paragraph A10 of ED-ISA 230 listed as a second example the documentation of “the basis for the auditor’s conclusions where the auditor considered it necessary to obtain further audit evidence by performing significant further audit procedures in addition to those necessary to meet the requirements of an ISA.” Two respondents noted that in most circumstances, the ISAs are written to require the auditor to design further audit procedures to respond to assessed risks. They therefore questioned whether it would be easy to identify when the auditor has performed procedures beyond those necessary to meet the requirements of an ISA. They were of the view that documentation requirements in other ISAs already ensure that documentation will be prepared to demonstrate how further audit procedures performed are sufficient to appropriately respond to the assessed risks. Accordingly, they suggested that this example be deleted.
39. The IAASB agreed that there was potential for confusion and that this example might suggest a need to document decisions to do further work beyond that clearly flowing from the requirements of the ISAs. Such an outcome could provide a disincentive to auditors to do what they believe is necessary, and if it were to have this effect it would be against the public interest. The IAASB therefore deleted the example.

Quality Control Reviews and Inspections

40. One respondent noted that in describing some of the purposes of audit documentation, paragraph 2 of ED-ISA 230 referred to audit documentation as enabling “experienced auditors” to conduct quality control reviews and inspections in accordance with proposed ISQC 1 (Redrafted).⁶ The respondent observed that proposed ISQC 1 (Redrafted) does not currently use the term “experienced auditor” in connection with periodic inspections, and that the only condition it imposes in respect of the person carrying out the inspection is that they not be involved in the engagement. The respondent suggested that consideration be given to amending the Monitoring section of proposed ISQC 1 (Redrafted) to ensure that inspections are only undertaken by experienced auditors.
41. The IAASB noted that this paragraph was not intended to impose any requirement, but was simply a list of other possible purposes served by audit documentation. The qualifications required of a person carrying out a quality control inspection could depend upon the specific purposes of the inspection. Because quality control inspections fall under the firm’s control, certain types of inspections might not necessarily always require experienced auditors. The IAASB was of the view that there was no basis for proposing an amendment to proposed ISQC 1 (Redrafted), and that it would be more appropriate to amend the fifth bullet in the paragraph so that no reference is made to who might conduct internal quality control reviews and inspections. This change makes this bullet consistent with the last bullet in the paragraph which deals with external inspections, which had been similarly amended prior to exposure to respond to regulatory concern that the original

⁶ Proposed ISQC 1 (Redrafted), “Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements,” paragraphs [41, 43-45, and 55-56].

BASIS FOR CONCLUSIONS:
ISA 230 (REDRAFTED)

drafting implied a bias in favor of peer review (which the IAASB had never intended to imply). (See paragraph 3 of the ISA.)



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