



International Federation of Accountants

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Agenda Item C.3.2

Committee: IAASB Consultative Advisory Group

Meeting Location: Basel

Meeting Date: March 3-4, 2008

IAASB Clarity Project – Issues on Exposure of Proposed ISA 500 (Redrafted) and ISA 530 (Redrafted)

Objective of Agenda Item

1. The objective of this Agenda Item is to obtain the views of Representatives on the proposed resolution of key issues arising from respondents' comments on the exposure drafts of the following proposed clarified ISAs to be considered by the IAASB at its March 2008 meeting:
 - Proposed ISA 500 (Redrafted), "Obtaining Sufficient Appropriate Audit Evidence;" and
 - Proposed ISA 530 (Redrafted), "Audit Sampling."

Approval of the final ISAs is planned for the June IAASB meeting.

Matters for CAG Consideration

A. PROPOSED ISA 500 (REDRAFTED), "OBTAINING SUFFICIENT APPROPRIATE AUDIT EVIDENCE"

Dealing with Sufficiency as well as Appropriateness of Audit Evidence

2. As a result of the proposed repositioning of the overarching bold type requirement in paragraph 2 of extant ISA 500¹ for the auditor to obtain sufficient appropriate audit evidence to proposed ISA 200 (Revised and Redrafted)², the scope of ED-ISA 500 (Redrafted) was changed to focus on the auditor's responsibility to design and perform audit procedures to obtain relevant and reliable audit evidence, and the ISA re-titled accordingly³.
3. The majority of respondents to ED-ISA 500 (Redrafted) disagreed with this change. They were of the view that ISA 500 (Redrafted) should cover both the sufficiency and the appropriateness of audit evidence, despite the repetition that may arise with ISA 200 (Revised and Redrafted). The Task Force has accepted this view and has, therefore, amended the title and scope of the ISA and the objective of the auditor, and introduced a new requirement that includes consideration of sufficiency. **(Refer to paragraphs B2-B4 of March 2008 IAASB Agenda Item 9-A, and paragraphs 1-2, 9 and 11.1 of March 2008 IAASB Agenda Item 9-B)**

¹ ISA 500, "Audit Evidence."

² 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."

³ Proposed ISA 500 (Redrafted), "Considering the Relevance and Reliability of Audit Evidence."

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Clarity—Proposed ISAs 500 and 530 (Redrafted)

Matters for Consideration by the IAASB CAG:

Q1. The Representatives are asked for their views on:

- (a) Whether the proposed amendments to the scope, objective and relevant requirement in the ISA to deal with obtaining both sufficient and appropriate audit evidence are appropriate; and
- (b) Whether there are appropriate linkages made between proposed ISAs 200 (Revised and Redrafted) and 500 (Redrafted) and ISA 330 (Redrafted)⁴, each of which deal directly with the sufficiency and appropriateness of audit evidence.

Q2. While the above is the issue that the Task Force believes may most usefully be discussed at the CAG meeting, the Representatives are welcome to express their views on any matter discussed in the IAASB Issue Paper for which further consideration may be needed by the IAASB. **(Refer to March 2008 IAASB Agenda Item 9-A)**

Proposed ISA 500 (Redrafted) Material Presented – IAASB CAG REFERENCE PAPERS

Available at
<http://www.ifac.org/IAASB/Meeting-BGPapers.php?MID=0141&ViewCat=0915>

Proposed ISA 500 (Redrafted) – Issue Paper
(March 2008 IAASB Agenda Item 9-A)

Available at
<http://www.ifac.org/IAASB/Meeting-BGPapers.php?MID=0141&ViewCat=0915>

Proposed ISA 500 (Redrafted) (March 2008
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⁴ ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks.”

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B. PROPOSED ISA 530 (REDRAFTED), “AUDIT SAMPLING”

Limited Revisions to Extant ISA 530 Regarding the Projection and Evaluation of Sample Results

4. In developing proposed ISA 530 (Redrafted), the IAASB agreed to introduce some limited revisions to the extant ISA. These limited revisions aimed to provide greater clarity on certain aspect of audit sampling which were viewed as being of particular importance and which may be subject to differing interpretations.
5. Whilst a number of respondents indicated that the proposed revisions helped to clarify the auditor’s responsibility, others expressed concerns that the extent and nature of some of the proposed changes go beyond the scope of the IAASB’s clarity project for an ISA intended to be subject to redrafting only. Concern was expressed that the draft had not been subject to the full due process that would normally be expected of a revised ISA. In addition, concern was expressed that some useful guidance had been lost in the redrafting.
6. In response to these concerns, the Task Force proposes a number of changes to the following, to bring the redrafted ISA more in line with the extant ISA while retaining clarity of the auditor’s responsibilities:
 - The responsibilities of the auditor with respect to the projection and evaluation of sample results. **(Refer to paragraphs 23-31 of March 2008 IAASB Agenda Item 8-A, and paragraphs 14-15 and A17-A21 of March IAASB Agenda Item 8-B)**

The relevant paragraphs of the revised draft of ISA 530 (Redrafted) and extant ISA 530 are as follows:

Revised Draft of Proposed ISA 530 (Redrafted)	Extant ISA 530
<p><u>Requirement</u></p> <p>Projecting Misstatements</p> <p>14. For tests of details, the auditor shall project misstatements found in the sample to the population. (Ref: Para. A17-A19)</p> <p><u>Application Material</u></p> <p>Projecting Misstatements (Ref: Para. 14)</p> <p>A17. The auditor is required to project misstatements for the population to obtain a broad view of the scale of misstatement.</p> <p>A18. When a misstatement has been established as an anomaly, it may be excluded when projecting misstatements in samples to the population. However, the effect of any such misstatement, if uncorrected, still needs to be considered in</p>	<p>Projecting Errors</p> <p>51. For tests of details, the auditor should project monetary errors found in the sample to the population, and should consider the effect of the projected error on the particular audit objective and on other areas of the audit. The auditor projects the total error for the population to obtain a broad view of the scale of errors, and to compare this to the tolerable error. For tests of details, tolerable error is the tolerable misstatement, and will be an amount less than or equal to the auditor’s materiality used for the individual class of transactions or account balances being audited.</p>

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<p>addition to the projection of the non-anomalous misstatements.</p> <p>A19. For tests of controls, no explicit projection of deviations is necessary since the sample deviation rate is also the projected deviation rate for the population as a whole. ISA 330, “The Auditor’s Responses to Assessed Risks”⁵ provides guidance when deviations from controls upon which the auditor intends to rely are detected.</p> <p><u>Requirement</u></p> <p>Evaluating Sample Results</p> <p>15. The auditor shall evaluate the sample results to determine whether, in the case of tests of controls, the rate of deviation is less than tolerable rate of deviation, and in the case of tests of details, the projected misstatement is less than tolerable misstatement. (Ref: Para. A20-A21)</p> <p><u>Application Material</u></p> <p>Evaluating Sample Results (Ref: Para. 15-16)</p> <p>A20. For tests of controls, an unexpectedly high sample deviation rate may lead to an increase in the assessed risk of material misstatement, unless further audit evidence substantiating the initial assessment is obtained. For tests of details, an unexpectedly high misstatement amount in a sample may cause the auditor to believe that a class of transactions or account balance is materially misstated, in the absence of further audit evidence that no material misstatement exists.</p>	<p>52. When an error has been established as an anomalous error, it may be excluded when projecting sample errors to the population. The effect of any such error, if uncorrected, still needs to be considered in addition to the projection of the non-anomalous errors. If a class of transactions or account balance has been divided into strata, the error is projected for each stratum separately. Projected errors plus anomalous errors for each stratum are then combined when considering the possible effect of errors on the total class of transactions or account balance.</p> <p>53. For tests of controls, no explicit projection of errors is necessary since the sample error rate is also the projected rate of error for the population as a whole.</p> <p>Evaluating the Sample Results</p> <p>54. The auditor should evaluate the sample results to determine whether the assessment of the relevant characteristic of the population is confirmed or needs to be revised. In the case of tests of controls, an unexpectedly high sample error rate may lead to an increase in the assessed risk of material misstatement, unless further audit evidence substantiating the initial assessment is obtained. In the case of tests of details, an unexpectedly high error amount in a sample may cause the auditor to believe that a class of transactions or account balance is materially misstated, in the absence of further audit evidence that no material misstatement exists.</p> <p>55. If the total amount of projected error plus anomalous error is less than but close to that which the auditor deems tolerable, the</p>
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⁵ ISA 330 paragraphs 17 and A41.

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A21. In the case of tests of details, the projected misstatement plus anomalous misstatement, if any, is the auditor's best estimate of misstatement in the population. When the projected misstatement plus anomalous misstatement, if any, exceeds tolerable misstatement, the sample does not provide an appropriate basis for conclusions about the population that has been tested. The closer the projected misstatement plus anomalous misstatement is to tolerable misstatement, the more likely that actual misstatement in the population may exceed tolerable misstatement. Also if the projected misstatement is greater than the auditor's expectations of misstatement used to determine the sample size, the auditor may conclude that there is an unacceptable sampling risk that the actual misstatement in the population exceeds the tolerable misstatement. Considering the results of other audit procedures helps the auditor to assess the risk that actual misstatement in the population exceeds tolerable misstatement, and the risk may be reduced if additional audit evidence is obtained.

auditor considers the persuasiveness of the sample results in the light of other audit procedures, and may consider it appropriate to obtain additional audit evidence. The total of projected error plus anomalous error is the auditor's best estimate of error in the population. However, sampling results are affected by sampling risk. Thus when the best estimate of error is close to the tolerable error, the auditor recognizes the risk that a different sample would result in a different best estimate that could exceed the tolerable error. Considering the results of other audit procedures helps the auditor to assess this risk, while the risk is reduced if additional audit evidence is obtained.

- The definitions of, and related guidance on, estimated maximum misstatements and estimated maximum rate of deviation. *(Refer to paragraphs 32-33 of March 2008 IAASB Agenda Item 8-A, and old paragraphs 5(j) and (k) and A20 and Appendix 5 of March IAASB Agenda Item 8-B)*

Matters for Consideration by the IAASB CAG:

- Q3. The Representatives are asked for their views on whether, in light of the scope of the project to only redraft extant ISA 530, the changes proposed to ISA 530 (Redrafted) make clear the auditor's responsibilities with respect to the projection and evaluation of sample results.
- Q4. While the above is the issue that the Task Force believes may most usefully be discussed at the CAG meeting, the Representatives are welcome to express their views on any matter discussed in the IAASB Issue Paper for which further consideration may be needed by the IAASB. *(Refer to March 2008 IAASB Agenda Item 8-A)*

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*Proposed ISA 530 (Redrafted) Material Presented – **IAASB CAG REFERENCE PAPERS***

Available at

<http://www.ifac.org/IAASB/Meeting-BGPapers.php?MID=0141&ViewCat=0911>

Proposed ISA 530 (Redrafted) – Issue Paper
(March 2008 IAASB Agenda Item 8-A)

Available at

<http://www.ifac.org/IAASB/Meeting-BGPapers.php?MID=0141&ViewCat=0911>

Proposed ISA 530 (Redrafted) (March 2008
IAASB Agenda Item 8-B)