

REVISION OF INTERNATIONAL STANDARD ON AUDITING (ISA) 500, AUDIT EVIDENCE

Note to IAASG CAG Representatives:

This IAASB Audit Evidence Project Proposal is an initial draft that has been prepared by the Audit Evidence Working Group, which may be further adapted based on the feedback from the CAG Representatives; as well as the Audit Evidence Working Group's further work in progressing the issues in Q4 and the Board's deliberations in December 2020.

[This document was developed and approved by the International Auditing and Assurance Standards Board (IAASB)] – Text subject to IAASB approval of project proposal in December 2020.

The IAASB develops auditing and assurance standards and guidance for use by all professional accountants under a shared standard-setting process involving the Public Interest Oversight Board, which oversees the activities of the IAASB, and the IAASB Consultative Advisory Group, which provides public interest input into the development of the standards and guidance.

The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

I. Subject

1. This project proposal addresses the revision of ISA 500.

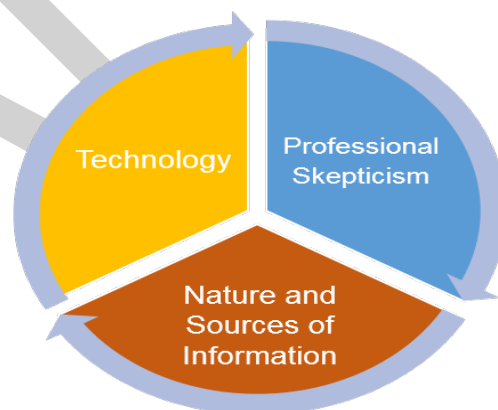
II. Background

2. ISA 500 deals with the auditor's responsibilities to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion. ISA 500 was issued in December 2008 as part of the IAASB's revisions to improve the clarity of its International Standards. Conforming and consequential amendments were made to the standard in 2018 as part of the project to revise ISA 540¹ (i.e. to include material addressing external information sources, as defined). No other updates have been made to ISA 500 during a period where the world has evolved with rapid changes in technology and the types of information sources available to auditors.
3. Given the evolving use of technology by auditors, the IAASB released the [Request for Input, Exploring the Growing Use of Technology in the Audit, With a Focus on Data Analytics](#) in December 2016. The paper identified and explored various issues and challenges associated with the use of data analytics and other technology in the performance of audits. Simultaneously, the purpose of the publication was to obtain stakeholder input and perspectives on the issues identified, including whether all of the issues relevant to the use of data analytics and other technology in a financial statement audit had been identified.

¹ ISA 540, *Auditing Accounting Estimates*, Including Fair Value Accounting Estimates, and Related Disclosures

4. To provide an overview of the key messages from the responses to the Request for Input, the IAASB issued a [Feedback Statement](#), *Exploring the Growing Use of Technology in the Audit, With a Focus on Data Analytics* in January 2018. Key messages included that the ISAs aren't broken and should remain principle-based, but need to reflect the digital era. Moreover, specific views were expressed in relation to the topic of audit evidence, including:
 - Emphasizing the need to exercise professional skepticism when using data analytics.
 - Clarifying how the use of data analytics contributes to the audit evidence model.
 - Highlighting the importance of the source and quality of the data used and challenges in considering the relevance and reliability of both internal and external data.
5. Given these matters and recognizing the evolution of technology more broadly, the IAASB established the Audit Evidence Working Group (AEWG) in January 2019. The preliminary purpose of the AEWG was twofold:
 - Identify and explore possible issues related to audit evidence and technology in the context of ISAs, and in particular, ISA 500; and
 - Develop recommendations for possible further actions, such as guidance or standard setting, if it was identified that further action was necessary.
6. The AEWG developed an initial listing of possible issues categorized into the following topics related to the auditor's consideration of audit evidence:
 - Changes in the source of information and how the information is processed, communicated and used;
 - Continual developments in technology; and
 - Professional skepticism.
7. The AEWG presented the initial listing of issues and possible actions to address the identified issues to the Board in June 2019.² In determining whether ISA 500 and possibly other standards needed to be revised, the Board was of the view that further information-gathering and targeted outreach activities were necessary to understand:
 - The extent to which the issues identified or other issues (if any) are creating challenges in practice, including the reasons or causes of those issues; and
 - How the issues may be best addressed.

The nature and extent of the further information gathering and targeted outreach activities were captured in the [Audit Evidence Workstream Plan](#).
8. The Board also noted the importance and need to address audit evidence issues related to technology, and specifically for issues where there was an opportunity for a timely response through developing and



² [Agenda Item 7](#) of the June 2019 IAASB Audit Evidence issues paper

issuing of non-authoritative support material. The Data Analytics Working Group was renamed the Technology Working Group (TWG) and was tasked to develop and issue such non-authoritative support material. The Board also recommended establishing a [Technology Workstream Plan](#), setting out a process for the identification, development and issuance of non-authoritative support materials. With the establishment of the Audit Evidence and Technology Workstream Plans, and the related allocation of responsibility to the AEWG and TWG, the differentiation between the activities of these two working groups was clarified.

9. At its June 2020 meeting, the IAASB discussed the outcome of the AEWG's information gathering and targeted outreach activities, which included an updated listing of audit evidence related issues.³ Key overall messages communicated to the Board included that:
- Issues creating the most difficulties in practice were generally closely related to the information to be used as audit evidence, the evaluation of whether sufficient appropriate audit evidence has been obtained and the definitions of "sufficiency" and "appropriateness." Further, the evolution of technology has created additional challenges in relation to the evaluation of whether sufficient appropriate audit evidence has been obtained.
 - Notwithstanding the evolution in technology, the relevance of many of the audit evidence issues identified were further emphasized in light of the COVID-19 pandemic.
 - A project to revise ISA 500, including conforming and consequential amendments to other ISAs, was broadly noted as the desired approach by stakeholders to address the identified audit evidence issues. Accordingly, the AEWG recommended, and the Board supported, prioritizing those issues that were directly related to a project to revise ISA 500, and only making conforming and consequential amendments to related standards.

Basis of Project Proposal

10. This project proposal has been formed on the basis of:
- (a) Information gathering activities which included analyzing the results of the:
- [Post-implementation review](#) of the clarified ISAs.
 - Request for Input, *Exploring the Growing Use of Technology in the Audit, with a Focus on Data Analytics*.
 - Feedback statement, *Exploring the Growing Use of Technology in the Audit with a Focus on Data Analytics*.
- (b) Targeted outreach with stakeholders, including:
- Regulators and audit oversight bodies; including representatives from regulator inspection teams;
 - National Standard Setters;
 - Accounting firms, including members of the Global Public Policy Committee and other members of the Forum of Firms;
 - Public Sector Organizations;

³ See [Agenda Item 7](#) of the June 2020 IAASB meeting

- International Federation of Accountants' (IFAC) Professional Accountancy Organization Members; including the IFAC Small and Medium Practices Committee; and
 - Preparers of financial statements.
- (c) Analysis of the Audit Evidence Project of the American Institute of Certified Public Accountants (AICPA);
- (d) Review of academic research on the topic of audit evidence;
- (e) Consideration of the IAASB's [Strategy for 2020-2023](#) and [Work Plan for 2020-2021](#);
- (f) Consideration of the activities of the Professional Skepticism Working Group (PSWG), in particular its work in relation to the IAASB's [Invitation to Comment, Enhancing Audit Quality in the Public Interest](#) (ITC); and
- (g) The Working Group's and Board's discussions to date.

Coordination with Other Working Groups to Date

Technology Working Group

11. In preparing the listing of audit evidence related issues, some issues were identified by the AEWG and the TWG as being more suited to be addressed by non-authoritative support material focused on the effect of technology when applying certain aspects of the ISAs. Therefore, where the TWG included any of these issues in the Technology Workstream Plan for the development of non-authoritative support material, the issue was excluded from the current itemization of issues to be covered through the audit evidence project proposal.

Professional Skepticism Working Group

12. In June 2015 the IAASB established the PSWG to commence a project on professional skepticism.⁴ The objective of the project was to formulate views on whether and how the IAASB could further contribute to strengthening the understanding and application of the concept of professional skepticism as it applies to an audit.
13. To solicit input, among other matters, on how to reinforce the fundamental concept of professional skepticism throughout the audit, the IAASB included a section on professional skepticism in the ITC. In the spirit of the IAASB's efforts to improve the exercise of professional skepticism throughout the audit, the AEWG considered the work of the PSWG in relation to the ITC in the context of audit evidence.

III. How the Project Serves the Public Interest

Responding to Changes in the Information that is Being Used by Auditors, Including the Nature and Source of the Information

14. The world of information is transforming at a rapid pace, largely as a result of the evolution of technology. Changes because of the use of big data and social media for example, have affected the sources, diversity and volume of information available to entities and auditors. This has impacted the manner in which entities obtain, process, manage, use, communicate and report information, and has also influenced how,

⁴ The IAASB has a project looking at professional skepticism more broadly. For details, see [Project Page](#)

and from where, auditors obtain audit evidence. As a result, the IAASB has determined that consideration is needed about whether ISA 500, and the extent to which it relates to other ISAs, remains fit for purpose.

15. Given the expansion of the sources and volume of information, it is in the public interest to explore how the source of information influences the nature and extent of the consideration of its relevance and reliability.

Modernizing and Supporting a Principle Based Standard that Recognizes the Evolution in Technology

16. The availability of more information and the ability of the auditor to use innovative audit techniques to obtain, prepare or analyze such information, allows the auditor to process and consider increasing volumes of information and data. This raises questions about how the use of automated tools and techniques fit within ISA 500, including:
 - How the use of automated data analytics contributes to issues such as the categorization of audit procedures. For example, where audit procedures are performed using automated tools and techniques, questions have arisen about the categorization or nature of such procedures (e.g., risk assessment, tests of controls, tests of details); and
 - The importance of the source and quality of the data used and challenges in considering the relevance and reliability of both internal and external data.
17. In today's changing environment, auditors are more commonly using automated tools and techniques, including, for example data analytics, robotic process automation, drone technology, machine learning and other artificial intelligence applications. However, ISA 500 does not specifically address the potential benefits and implications when such tools and techniques are used in obtaining, preparing or analyzing information to be used as audit evidence. The IAASB therefore believes it is in the public interest, to enhance or clarify ISA 500 to address the increasing use of technology.

Fostering the Maintenance of Professional Skepticism when Making Judgments About Sufficient Appropriate Audit Evidence

18. Professional skepticism is a fundamental concept and core to audit quality, and it is therefore in the public interest to explore what should be done to reinforce the exercise of professional skepticism when evaluating the sufficiency and appropriateness of audit evidence. Some corporate failures have resulted in questions being raised about the role of the auditor, including highlighting concerns about the appropriateness of professional skepticism exercised by auditors when making professional judgments about information to be used as audit evidence and whether sufficient appropriate audit evidence has been obtained.
19. Notwithstanding the evolution in technology, the relevance of many of the audit evidence issues identified were further emphasized in light of the COVID-19 pandemic. These developments underline the importance and need for the auditor to exercise professional skepticism when making judgements about the relevance and reliability of information to be used as audit evidence.
20. The importance of professional skepticism to the public interest is underscored by the increasing complexity of business and financial reporting, including the greater use of accounting estimates and related management judgments, business model changes due to technological developments, and the reliance of the public on dependable financial reporting.

IV. Project Objectives

21. Given the public interest issues identified, the IAASB believes it will be necessary to enhance its International Standards taking into account the following objectives:

Sources of Information

- (a) Explain the scope of ISA 500 and its relationship with other standards.
- (b) Evaluate, and if considered appropriate, affect changes to the extant definitions in ISA 500.
- (c) Clarify the auditor's responsibilities in relation to different sources of information, including the distinction between information produced by the entity and external information.
- (d) Develop an enhanced set of factors or attributes of information that must be considered by the auditor in evaluating and concluding whether sufficient appropriate audit evidence has been obtained.

Technology

- (e) Update ISA 500 to be sufficiently adaptable to the current business and audit environment, and to better reflect the digital era.

Professional Skepticism

- (f) Emphasize the role of professional skepticism in relation to information to be used as audit evidence and evaluating audit evidence obtained.

22. The IAASB will also consider whether improvements in the structure of the standard are necessary to facilitate improvements in effectively and efficiently applying ISA 500 in evaluating the sufficiency and appropriateness of audit evidence.

V. Project Scope

23. To address the project objectives, the project scope is to:

- (a) Develop revisions to ISA 500 to establish more robust requirements and appropriate application material. It is intended that these revisions will achieve greater consistency in auditor judgements, as well as better explain the scope of the standard and its relationship with other standards, such as ISA 200⁵ and ISA 330.⁶
- (b) Propose conforming and consequential amendments to other ISAs that may be necessary as a result of revisions to ISA 500.
- (c) To determine whether non-authoritative materials should be developed by the IAASB, or others, to supplement revisions to ISA 500 and thereby aid its effective implementation. First-time implementation support activities or non-authoritative support materials may include, for example, fact sheets, questions and answers, webinars, or presentations, flow charts, diagrams or illustrations.

⁵ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

⁶ ISA 330, *The Auditors Responses to Assessed Risks*

VI. Outline of the Project

Major Issues that Will Be Addressed

24. As noted, the IAASB discussed the outcome of the information gathering and targeted outreach activities of the AEWG at its June 2020 meeting. The discussion included the Board's consideration of an updated listing of audit evidence related issues.⁷ In developing this project proposal, the IAASB has taken into account these issues.
25. In the overall context that all identified issues will form the basis of the IAASB's work in progressing the revision of ISA 500, and considering the Project Objectives (see Section IV), the preliminary assessment of the major issues that will be addressed can be summarized by theme, as presented in paragraphs 26 to 38.

Clarifying the Objective of the Standard

26. ISA 500 sets out a principle-based approach in relation to the requirements that are appropriate to achieve the auditor's objective to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. Questions have arisen about the purpose of ISA 500 in the context of the other ISAs, and in particular whether:
- ISA 500 is intended to be a performance standard;⁸ and
 - The objective of the standard is sufficiently distinct from ISA 330.
27. In addition to the consideration of the objective, the IAASB will also consider whether existing application material adequately explains the distinction between ISA 500 and ISA 330.⁹

The Concept and Evaluation of Sufficient Appropriate Audit Evidence

28. Many of the audit evidence issues creating the most difficulties in practice are closely related to the concept and evaluation of sufficient appropriate audit evidence. The evolution in the nature and sources (as well as volume) of information and the use of technology in designing and performing audit procedures have raised questions about the factors that are considered by the auditor in concluding whether sufficient appropriate audit evidence has been obtained. The IAASB will explore which changes are needed to address these matters, including:
- (a) Whether the definitions of appropriateness of audit evidence and sufficiency of audit evidence¹⁰ are appropriate.
 - (b) What factors are considered by the auditor in concluding whether sufficient appropriate audit evidence has been obtained.

⁷ The listing of issues was included in appendix 4 of the June 2020 [IAASB Audit Evidence Issues Paper](#)

⁸ For example, the objective of ISA 500 indicates that "the objective of the auditor is to design and perform audit procedures," and paragraph 6 requires the auditor to "design and perform audit procedures."

⁹ ISA 500, paragraph A6

¹⁰ Paragraph 5(e) of ISA 500 describes the sufficiency of audit evidence as the measure of the quantity of audit evidence.

29. The IAASB will explore whether the definition of sufficiency should have a broader focus than quantity alone (e.g., the 'strength' of audit evidence), given the significant changes in the nature and sources (as well as volume) of information.
30. The IAASB will also explore the relevancy of the notion of the 'persuasiveness' of audit evidence, given the auditor's responsibility to obtain more persuasive audit evidence the higher the auditor's assessment of risk.¹¹
31. In relation to the concept of sufficient appropriate audit evidence, the IAASB intends to explore whether the development of a set of relevant factors with respect to the nature and the source of audit evidence is useful. A framework may achieve greater consistency in auditor judgements about the concept and evaluation of sufficient appropriate audit evidence.

Sources of Information – Clarifying the Auditor's Responsibility When Considering the Relevance and Reliability of Information to be Used as Audit Evidence, Including External Information

32. In dealing with the auditor's consideration of information to be used as audit evidence, ISA 500 addresses specific characteristics of the reliability of information produced by the entity that the auditor is required to evaluate. This additional work effort required is not specifically addressed for external information. The IAASB will explore whether such distinction remains appropriate.
33. The IAASB will also explore whether changes to ISA 500 are needed related to:
 - The notion that information from any source may be susceptible to different biases, including auditor bias in considering information to be used as audit evidence.
 - The distinction between internal and external information, and the complexities about gaining access to certain types of information, such as service organization auditor reports, blockchain, cloud-based services or hosting, etc.
 - Whether all information to be used as audit evidence should be subject to the same rigor when considering the relevance and reliability of such information. For example, should information to be used in risk assessment procedures be subject to the same level of consideration as information to be used in a substantive analytical procedure?

Continual Developments in Technology – Providing Clarity about the Categorization of Audit Procedures When Using Automated Tools and Techniques

34. New technologies have raised questions about where audit procedures performed using automated tools and techniques fit within:
 - The categories of audit procedures (i.e., inspection, observation, inquiry etc.); and
 - The nature of audit procedures (i.e., risk assessment, tests of controls, tests of details).

Challenges about the classification of the nature of such audit procedures also brings into question whether a procedure could be both a risk assessment procedure and a substantive procedure at the same time. This question is particularly relevant, but not limited, to circumstances where the auditor uses automated tools and techniques to assist the auditor in performing audit procedures.

¹¹ ISA 330, paragraph 6(b)

35. Although the question about ‘dual purpose’¹² is not dependent on the use of automated tools and techniques, the IAASB recognizes that the capabilities of modern automated tools and techniques (such as data analytics) may allow the auditor to perform risk assessment procedures that go beyond traditional risk assessment procedures as the information is analyzed at a significantly more granular level. It was therefore questioned, for example:

- Under which conditions (if any) do risk assessment procedures reduce risks of material misstatement to an acceptably low level; and
- Can data analytics be designed in such a way to simultaneously serve the purpose of identifying and assessing risks of material misstatement and detecting material misstatements at the assertion level (and if so, when and how).

Aspects of these questions have been addressed by the IAASB’s TWG through the issuance of non-authoritative support material. The IAASB will consider the work of the TWG in exploring whether, and if so, how, ISA 500 could more robustly address the categorization of audit procedures, in particular when using automated tools and techniques.

36. The IAASB will also consider the classification of substantive procedures in accordance with the procedures recognized and the context of testing, as presented in ISA 500, ISA 520¹³ and ISA 530.¹⁴ For example, where an automated tool performs a recalculation or reconciliation of 100 percent of a population, there was uncertainty as to whether or when this was a substantive analytical procedure or a substantive test of details, or both.

Professional Skepticism

37. Based on its information gathering activities, the IAASB concluded that ISA 500 could more robustly address the need for professional skepticism when making judgments about whether sufficient appropriate audit evidence has been obtained. In particular, it was suggested that the IAASB needs to focus on elaborating what the phrase “a critical assessment of evidence” in the definition of professional skepticism entails (e.g., by seeking to enhance ISA 500 and other ISAs).
38. As noted, ISA 500 does not specifically address the potential benefits and implications when using automated tools and techniques in obtaining, preparing or analyzing information to be used as audit evidence. The IAASB will explore whether it is appropriate for ISA 500 to highlight the need for the auditor to exercise professional skepticism when using automated tools and techniques to obtain, prepare or analyze information to be used as audit evidence.

Coordination with Other Working Groups

Technology Working Group

39. Paragraph 11 provides information regarding coordination with the TWG to date. The AEWG will continue to coordinate with the TWG in relation to technology related aspects of audit evidence.

¹² Dual purpose in this context refers to whether a procedure could be both a risk assessment and a substantive procedure at the same time. The question posed does not address the design of a test of controls to be performed concurrently with a test of detail on the same transaction, as addressed by ISA 330 paragraph A23.

¹³ ISA 520, *Analytical Procedures*

¹⁴ ISA 530, *Audit Sampling*

40. As the IAASB progresses its work, audit evidence matters may be identified for which there is an opportunity for a more timely response in the form of non-authoritative support material. To the extent that such issues relate to technology, the AEWG will continue to coordinate with the TWG to consider such matters.

Professional Skepticism Working Group

41. Paragraphs 12 and 13 provide information regarding coordination with the PSWG to date.
42. The AEWG, in conjunction with the PSWG, will further explore what should be done to re-emphasize how ISA 500 could more robustly address the need for professional skepticism when making judgments about information to be used as audit evidence.

Coordination with the International Ethics Standards Board for Accountants (IESBA)

43. The AEWG notes that the IESBA established a Technology Working Group (IESBA TWG) in 2018, with the objective to identify potential ethical implications of technology developments on the robustness and relevance of the fundamental principles and independence standards in the IESBA Code of Ethics for Professional Accountants. The AEWG will coordinate with the IESBA TWG or liaise with the IAASB TWG in terms of its coordination with the IESBA TWG in relation to technology related aspects of audit evidence. In addition, the AEWG will engage with IESBA representatives and staff more broadly to identify any ethics considerations or matters of relevance in terms of the audit evidence related issues that are within the scope of this project.

Other

44. ISA 500 includes one explicit reference to fraud or ISA 240.¹⁵ The application material explains that ISA 240 deals with circumstances where the auditor has reason to believe that a document may not be authentic, or may have been modified without that modification having been disclosed to the auditor. In progressing the project, the AEWG will consider whether fraud considerations are appropriately addressed in ISA 500 in the context of audit evidence.

VII. Impact Analysis Considerations

45. The primary expected benefit of this project is to further reinforce audit quality through more robust requirements and application material. This will assist auditors, and achieve greater consistency, when making judgements about the concept and evaluation of sufficient appropriate audit evidence.
46. Regardless of whether the outcome of this project results in new or revised requirements or application material or other guidance, there will be cost and benefit implications for audits of financial statements. It is anticipated that the impact on individual audits would vary depending on the size and complexity of the entity. The impact at firm level will also vary depending on the methodologies currently in place, including the extent of the firm's reliance and use of automated tools and techniques in audits of financial statements.
47. In summary, establishing robust principles within the standard to assist the auditor in considering the relevance and reliability of information to be used audit evidence, is expected to enhance auditor judgements about whether sufficient appropriate audit evidence has been obtained. As the auditor is

¹⁵ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraph A33

required to obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level, such changes are expected to result in higher audit quality, which is in the public interest.

Implications for Any Specific Persons or Groups

48. The project has implications for all participants in the financial reporting supply chain, in particular for auditors who perform audits of financial statements and as a result will also have an impact on entities that provide information to auditors. As the ISAs apply to all entities, the risk of unintended consequences to audits of less complex entities needs to be considered. In addition to other outreach, IFAC's Small and Medium Practices Committee and the IAASB's Less Complex Entities Task Force will be kept informed of developments to ensure appropriate input is received at key stages of the project.

VIII. Development Process, Project Timetable and Project Output

Development Process and Project Timetable

49. The project will be conducted in accordance with the Public Interest Activity Committees' Due Process and Working Procedures.¹⁶
50. Below is a preliminary timetable, noting that specific project milestones and outputs may change as the project develops. The IAASB Consultative Advisory Group's input will be obtained throughout the project.

Timing	Action
December 2020	Approval of project proposal and deliberation of issues
January – November 2021	Development of the exposure draft – progressing issues and drafting the proposed revisions to ISA 500
	Dialogue with stakeholders on key issues and proposals
December 2021	IAASB approval of exposure draft, with a 120-day comment period, including proposed conforming and consequential amendments to other ISAs
June 2022 – February 2023	Analysis of responses and resulting revisions to the exposure draft in developing the final standard
	Dialogue with stakeholders on key issues and proposals
March 2023	IAASB approval of ISA 500 (Revised)

Project Output

51. The expected output of the project is a revised ISA 500, with conforming and consequential amendments to other ISAs. The ISA 500 Task Force will, throughout the revision of the standard,

¹⁶ [PIAC Due Process and Working Procedures](#)

consider and advise the IAASB as to the need for, and potential timing of, development of other non-authoritative guidance. First-time implementation support activities or non-authoritative support materials may include, for example, fact sheets, questions and answers, webinars or presentations, flow charts, diagrams or illustrations.

IX. Resources Required

52. A project Task Force will be responsible for the project to revise ISA 500, and will be comprised of IAASB members, technical advisors, and external experts, as appropriate, with diverse backgrounds. For this purpose, and to appropriately leverage the work performed by other national standard setters, the IAASB intends to include IAASB members or technical advisors who participated in the development of the AICPA's Audit Evidence Project. IAASB Staff will provide support to the ISA 500 Task Force.