

*Proposed Revised and Redrafted International
Standard on Auditing*

ISA 505, External Confirmations

Conforming Amendments

**Proposed ISA 500, Considering the
Relevance and Reliability of Audit
Evidence**



REQUEST FOR COMMENTS

The International Auditing and Assurance Standards Board (IAASB), an independent standard-setting body within the International Federation of Accountants (IFAC), approved the exposure draft of proposed International Standard on Auditing (ISA) 505 (Revised and Redrafted), “External Confirmations” in September 2007 for publication. The proposed ISA may be modified in light of comments received before being issued in final form.

Please submit your comments, preferably by e-mail, so that they will be received by **February 15, 2008**. All comments will be considered a matter of public record. Comments should be addressed to:

International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, New York 10017 USA

Comments should be emailed to Edcomments@ifac.org. They may also be faxed to +1-212-286-9570 or mailed to the above address.

Copies of the exposure draft may be downloaded free-of-charge from the IFAC website at <http://www.ifac.org>.

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EXPLANATORY MEMORANDUM

Introduction

This memorandum provides background to, and an explanation of, proposed International Standard on Auditing (ISA) 505 (Revised and Redrafted), “External Confirmations.” The International Auditing and Assurance Standards Board (IAASB) approved the proposed ISA in September 2007 for exposure.

Background

Recent experience has indicated that external confirmations may not always be as reliable as expected as audit evidence. As a result, some stakeholders believe that more rigorous requirements governing the use of external confirmations by the auditor are required. At the same time, others have questioned whether external confirmations are in fact an effective audit technique in obtaining relevance and reliable audit evidence.

In December 2005, the IAASB commenced a project to revise the standards and guidance in extant ISA 505 addressing the auditor’s use of external confirmations, within the context of the audit risk model.

Significant Matters

Mandating External Confirmation Requests

The IAASB considered whether external confirmation requests should be mandated in particular circumstances in order to improve audit quality and enhance the persuasiveness of audit evidence obtained by the auditor.

The IAASB concluded that making external confirmation requests mandatory would conflict with the audit risk model, may not improve audit quality, and would suffer from significant operational disadvantages having regard to the international context in which the ISAs are applied. In particular, the IAASB noted that to mandate the use of external confirmation requests in particular circumstances would:

- Require the presumption that external confirmations requests would always provide relevant and reliable audit evidence, and that such evidence would always be used. Research and experience have shown, however, that there is no basis for such a presumption. As stated in proposed ISA 500 (Redrafted), “Considering the Relevance and Reliability of Audit Evidence,” 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.
- Introduce inconsistency with ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks.” That ISA requires that the auditor design and perform audit procedures whose nature, timing, and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level, and explains that the auditor’s assessment of the identified risks at the assertion level provides a basis for considering the appropriate audit approach for designing and performing audit procedures

- Disregard the fact that an effective confirmation request is dependent on the confirming party being engaged in the process. Whether the confirming party is so engaged is beyond the auditor's control.
- Result in the use of external confirmation requests even in circumstances where the auditor has reason to believe that responses would not be obtained or would be unreliable.
- Require exceptions to be provided for, in light of jurisdictional differences and practical considerations.

Accordingly, the proposed ISA does not mandate the use of external confirmation requests in any particular circumstance or in response to any particular risk of material misstatement.

Determining When to Use External Confirmation Procedures

Extant ISA 505 requires that the auditor determine whether the use of external confirmations is necessary to obtain sufficient appropriate audit evidence at the assertion level. In revising the extant ISA, the IAASB deliberated whether that requirement is in fact necessary and relevant in the context of the proposed ISA.

In considering this matter, the IAASB noted that ISA 315 (Redrafted), "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment" requires that the auditor identify and assess the risks of material misstatement at the assertion level for classes of transactions, account balances, and disclosures. A requirement in proposed ISA 505 (Revised and Redrafted) that the auditor consider whether to use external confirmation procedures may therefore lead the auditor to document that consideration for each assertion associated with material account balances, classes of transactions and disclosures. Alternatively, such consideration may be documented at an engagement level, rendering the activity relatively perfunctory. The IAASB also noted that ISAs 315 (Redrafted) and 330 (Redrafted) provide guidance on the auditor's determination of the nature, timing, and extent of audit procedures, and contain references to when external confirmation procedures may be used.

The IAASB therefore concluded that the auditor's consideration of whether, and to what extent, to use external confirmation procedures when performing an audit of financial statements is inherent in the requirements of ISAs 315 (Redrafted) and 330 (Redrafted), and that those ISAs provide adequate guidance to assist auditors to decide in that regard. It is therefore unnecessary for the proposed ISA to establish a requirement that the auditor do so. Rather, the IAASB believes that the scope and focus of proposed ISA 505 (Revised and Redrafted) should be on setting requirements that will improve auditor performance, with the starting point of the proposed ISA being when the auditor has determined that the use of external confirmation procedures is an appropriate response to an assessed risk of material misstatement.

To assist auditors, proposed ISA 505 (Revised and Redrafted) provides references to other ISAs that recognize the importance of external confirmations as audit evidence and provide guidance regarding when the auditor considers using external confirmation procedures as a response to an assessed risk of material misstatement at the assertion level.

Negative Confirmation Requests

Extant ISA 505 provides for the use of negative confirmations under certain limited circumstances and includes guidance explaining the audit evidence limitations inherent in their use. A number of concerns have been expressed that auditors may be placing undue reliance on negative confirmation requests as a source of audit evidence. Accordingly, the IAASB considered whether use of negative confirmation requests should be prohibited, or limited to specific circumstances.

The IAASB concluded that an ISA should not prevent the auditor from performing a particular audit procedure simply because that procedure would provide only limited audit evidence. Rather, the auditor should understand the limitations of the audit evidence obtained from such a procedure when deciding to use that procedure and in evaluating the audit evidence obtained. Further, the IAASB believes that negative confirmation requests may in fact be a useful audit procedure when performed in conjunction with other substantive audit procedures. However, the IAASB decided to place strict limits on the circumstances in which negative confirmation requests may be used as the only substantive audit procedure to address an assessed risk of material misstatement at the assertion level.

Accordingly, proposed ISA 505 (Revised and Redrafted) does not prohibit the use of negative confirmation requests in an audit of financial statements. However, it includes requirements and application and other explanatory material limiting the extent to which an auditor may use them.

Effective Date

The current IAASB project timetable envisages that all ISAs will have been revised and redrafted, or redrafted only, by late 2008. The IAASB has agreed that the complete set of ISAs will be effective for audits of financial statements for financial periods beginning on or after December 15, 2009. The IAASB believes that it is in the interest of auditors and others who use the ISAs that the standards should be released as soon as they are approved so as to facilitate their implementation.

Guide for Respondents

The IAASB welcomes comments on all matters addressed in the exposure draft. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, where appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this exposure draft (especially those calling for change in current practice), it will be helpful for the IAASB to be made aware of this view.

Request for Specific Comments

The IAASB would welcome views on the following:

1. The proposal that proposed ISA 505 (Revised and Redrafted) should not mandate the use of external confirmation requests in any particular circumstance or in response to any particular risk of material misstatement.
2. The proposal that the scope of proposed ISA 505 (Revised and Redrafted) be directed at the effective performance of external confirmation procedures when the auditor determines that such procedures are an appropriate response to an assessed risk of material misstatement, and that accordingly the ISA should not require that the auditor consider when, or under what

circumstances, it may be appropriate to use external confirmation procedures when performing an audit of financial statements.

If a respondent believes that the ISA should require that the auditor consider whether to use external confirmation procedures, please explain why and indicate at what level (e.g., financial statement assertion) such consideration should be made, and whether and how the auditor should document such consideration.

3. Whether proposed ISA 505 (Revised and Redrafted) appropriately limits the extent to which auditors may use negative confirmation requests.

Request for Comments on the Application of the Clarity Drafting Conventions

In addition to the matters referred to above, the IAASB is seeking comments on the application of the clarity drafting conventions. Respondents are asked to consider whether the objective for the proposed ISA is appropriate, and whether the proposed requirements are appropriate responses to that objective.

Comments on Other Matters

Recognizing that the final ISA will apply to audits of all sizes and in all sectors of the economy, the IAASB is also interested in comments on matters set out below.

- *Special Considerations in the Audit of Small Entities*—Respondents are asked to comment whether, in their opinion, considerations in the audit of small entities have been dealt with appropriately in the proposed ISA.
- *Special Considerations in the Audit of Public Sector Entities*—Respondents are asked to comment whether, in their opinion, special considerations in the audit of public sector entities have been dealt with appropriately in the proposed ISA.
- *Developing Nations*—Recognizing that many developing nations have adopted or are in the process of adopting the ISAs, the IAASB invites respondents from these nations to comment, in particular, on any foreseeable difficulties in applying the proposed ISA in a developing nation environment.
- *Translations*—Recognizing that many respondents intend to translate the final ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues noted in reviewing the proposed ISA.

To be considered, responses should be emailed to Edcomments@ifac.org. They may also be faxed to +1-212-286-9570 or mailed to 545 Fifth Avenue, 14th Floor, New York, NY 10017, USA. They should be received by **February 15, 2008**.

PROPOSED INTERNATIONAL STANDARD ON AUDITING 505
(REVISED AND REDRAFTED)
EXTERNAL CONFIRMATIONS

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

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[Proposed] International Standard on Auditing (ISA) 505 (Revised and Redrafted), “External Confirmations” should be read in conjunction with [proposed] ISA 200 (Revised and Redrafted), “The Overall Objective of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing.”

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) establishes requirements and provides guidance for performing external confirmation procedures. It does not address inquiries regarding litigation and claims. Part C: Procedures Regarding Litigation and Claims of ISA 501, “Audit Evidence—Additional Considerations for Specific Items” establishes requirements and provides guidance on such inquiries.

External Confirmation Procedures as a Response to Assessed Risks

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.¹ That ISA also includes the following generalizations applicable to audit evidence that may be relevant to external confirmations:² (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, audit evidence in the form of external confirmations received directly by the auditor from confirming parties may be more reliable than internally generated evidence.

3. Other ISAs recognize the importance of external confirmations as audit evidence, for example:
 - ISA 330 (Redrafted) requires the auditor to obtain more persuasive audit evidence the higher the auditor’s assessment of risk.³ Consequently, as the assessed risk of material misstatement increases, the auditor may increase the quantity of the evidence or obtain evidence that is more relevant or reliable, for example, by placing more emphasis on obtaining third party evidence or by obtaining corroborating evidence from a number of independent sources.
 - 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.⁴
 - [Proposed] ISA 500 (Redrafted) indicates that corroborating information obtained from

¹ [Proposed] ISA 500 (Redrafted), “Considering the Relevance and Reliability of Audit Evidence,” paragraph 6.

² [Proposed] ISA 500 (Redrafted), paragraph A23.

³ ISA 330 (Redrafted), “The Auditor’s Responses to Assessed Risks,” paragraph 7(b).

⁴ ISA 240 (Redrafted), “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements,” paragraph A37.

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.⁵

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 using external confirmation procedures in response to an assessed risk of material misstatement is to design and perform such procedures to obtain relevant and reliable audit evidence.

Definitions

6. For the purpose 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.
 - (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;

⁵ [Proposed] ISA 500 (Redrafted), paragraph A2.

- (b) Selecting the appropriate confirming party;
- (c) Designing the confirmation requests;
- (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; and
- (e) Evaluating the evidence obtained (responses, non-responses and exceptions) from the external confirmation procedures. (Ref: Para. A7-A11)

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

8. 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; (Ref: Para. A12)
 - (b) Evaluate the implications of management’s refusal 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; and (Ref: Para. A13)
 - (c) Where possible, perform alternative procedures designed to obtain relevant and reliable audit evidence. (Ref: Para. A14)
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 appropriate audit evidence from alternative procedures performed in accordance with paragraph 8(c), the auditor shall communicate with those charged with governance, and consider the possible effect on the auditor’s opinion in accordance with [proposed] ISA 705 (Revised and Redrafted).⁶

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

Reliability of Responses to Confirmation Requests

10. If the auditor has doubts about the reliability of the response to a confirmation request, the auditor shall obtain further audit evidence to resolve those doubts. (Ref: Para. A16-A19)
11. If the auditor determines that 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)

⁶ [Proposed] ISA 705 (Revised and Redrafted), “Modifications to the Opinion in the Independent Auditor’s Report.”

Non-Responses

12. In the case of non-responses, the auditor shall perform alternative audit procedures to obtain relevant and reliable audit evidence. 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, and 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

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

Negative Confirmations

14. Negative confirmations provide less persuasive audit evidence than positive confirmations. Accordingly, the auditor shall only use negative confirmation requests as the sole substantive procedure to address an assessed risk of material misstatement at the assertion level when the auditor has obtained sufficient appropriate audit evidence regarding the operating effectiveness of controls relevant to the assertion and 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;
 - (b) Very few or no exceptions are expected; and
 - (c) 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

15. 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.

Application and Other Explanatory Material

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

- 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).⁷

⁷ ISA 315 (Redrafted), "Identifying and Assessing Risks of Material Misstatement Through Understanding the Entity and Its Environment."

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:
- 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 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 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 about the information being confirmed.

- The ability or willingness of the intended confirming party to respond – for example, the confirming party:
 - May not accept responsibility for responding to a confirmation request.
 - May consider responding too costly or time consuming.
 - May have concerns about the potential legal liability resulting from responding.
 - May account for transactions in different currencies.
 - 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.

Designing Confirmation Requests

- A8. 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.
- A9. 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).

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.

Follow-Up on Confirmation Requests

A11. The auditor may perform procedures to obtain external confirmations for non-responses. For example, the auditor may verify the accuracy of the original address, and then send additional or follow-up requests.

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

Reasonableness of Management’s Refusal (Ref: Para 8(a))

A12. 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 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 the Assessment of Relevant Risks of Material Misstatement (Ref: Para 8(b))

A13. The auditor may conclude from the evaluation in paragraph 8(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). 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).

Alternative Procedures (Ref: Para 8(c))

- A14. The alternative procedures performed may be similar to those appropriate for a non-response as set out in paragraphs A21-A23 of this ISA. Such procedures also would take account of the results of the auditor's evaluation as discussed in paragraph 8(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.

Reliability of Responses to Confirmation Requests (Ref: Para. 10)

- A16. Even when audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability.⁸ 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 whether it:
- Was received directly by the auditor;
 - Appeared to come from the originally intended confirming party; and
 - Was received by a means that provides 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.⁹ 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

⁸ [Proposed] ISA 500 (Redrafted), paragraph A23.

⁹ [Proposed] ISA 500 (Redrafted), paragraph 14.

circumstances, request the confirming party to respond in writing directly to the auditor, or seek 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, invalidate the reliability of the response as audit evidence.

Unreliable Responses (Ref: Para. 11)

- 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).

Non-Responses (Ref: Para. 12)

- 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 a client’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.

Exceptions (Ref: Para. 13)

- 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 to evaluate whether such misstatement is

indicative of fraud.¹⁰ 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 verification of the accuracy of the information contained in the request. Accordingly, a non-response to a negative confirmation request provides 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.

¹⁰ Refer to ISA 240 (Redrafted), paragraph 35.

CONFORMING AMENDMENTS TO OTHER ISAS

[Proposed] ISA 500 (Redrafted), “Considering the Relevance and Reliability of 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 procedures 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.~~



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