

INTERNATIONAL STANDARD ON AUDITING 500

AUDIT EVIDENCE

(Effective for audits of financial statements for periods
beginning on or after December 15, 2004)

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International Standard on Auditing (ISA) 500, “Audit Evidence” should be read in the context of the “Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services,” which sets out the application and authority of ISAs.

Introduction

1. The purpose of this International Standard on Auditing (ISA) is to establish standards and to provide guidance on what constitutes audit evidence in an audit of financial statements, the quantity and quality of audit evidence to be obtained, and the audit procedures that auditors use for obtaining that audit evidence.
2. **The auditor should obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion.**

Concept of Audit Evidence

3. “Audit evidence” is all the information used by the auditor in arriving at the conclusions on which the audit opinion is based, and includes the information contained in the accounting records underlying the financial statements and other information. Auditors are not expected to address all information that may exist.¹ Audit evidence, which is cumulative in nature, includes audit evidence obtained from audit procedures performed during the course of the audit and may include audit evidence obtained from other sources such as previous audits and a firm’s quality control procedures for client acceptance and continuance.
4. Accounting records generally include the records of initial entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in formal journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures. The entries in the accounting records are often initiated, recorded, processed and reported in electronic form. In addition, the accounting records may be part of integrated systems that share data and support all aspects of the entity’s financial reporting, operations and compliance objectives.
5. Management is responsible for the preparation of the financial statements based upon the accounting records of the entity. The auditor obtains some audit evidence by testing the accounting records, for example, through analysis and review, reperforming procedures followed in the financial reporting process, and reconciling related types and applications of the same information. Through the performance of such audit procedures, the auditor may determine that the accounting records are internally consistent and agree to the financial statements. However, because accounting records alone do not provide sufficient audit evidence on which to base an audit opinion on the financial statements, the auditor obtains other audit evidence.

¹ See paragraph 14.

6. Other information that the auditor may use as audit evidence includes minutes of meetings; confirmations from third parties; analysts' reports; comparable data about competitors (benchmarking); controls manuals; information obtained by the auditor from such audit procedures as inquiry, observation, and inspection; and other information developed by, or available to, the auditor that permits the auditor to reach conclusions through valid reasoning.

Sufficient Appropriate Audit Evidence

7. Sufficiency is the measure of the quantity of audit evidence. Appropriateness is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for, or detecting misstatements in, the classes of transactions, account balances, and disclosures and related assertions. The quantity of audit evidence needed is affected by the risk of misstatement (the greater the risk, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Accordingly, the sufficiency and appropriateness of audit evidence are interrelated. However, merely obtaining more audit evidence may not compensate for its poor quality.
8. A given set of audit procedures may provide audit evidence that is relevant to certain assertions, but not others. For example, inspection of records and documents related to the collection of receivables after the period end may provide audit evidence regarding both existence and valuation, although not necessarily the appropriateness of period-end cutoffs. On the other hand, the auditor often obtains audit evidence from different sources or of a different nature that is relevant to the same assertion. For example, the auditor may analyze the aging of accounts receivable and the subsequent collection of receivables to obtain audit evidence relating to the valuation of the allowance for doubtful accounts. Furthermore, obtaining audit evidence relating to a particular assertion, for example, the physical existence of inventory, is not a substitute for obtaining audit evidence regarding another assertion, for example, the valuation of inventory.
9. 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. Generalizations about the reliability of various kinds of audit evidence can be made; however, such generalizations are subject to important exceptions. Even when audit evidence is obtained from sources external to the entity, circumstances may exist that could affect the reliability of the information obtained. For example, audit evidence obtained from an independent external source may not be reliable if the source is not knowledgeable. While recognizing that exceptions may exist, the following generalizations about the reliability of audit evidence may be useful:
 - Audit evidence is more reliable when it is obtained from independent sources outside the entity.

- Audit evidence that is generated internally is more reliable when the related controls imposed by the entity are effective.
 - Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example, inquiry about the application of a control).
 - Audit evidence is more reliable when it exists in documentary form, whether paper, electronic, or other medium (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed).
 - Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles.
10. An audit rarely involves the authentication of documentation, nor is the auditor trained as or expected to be an expert in such authentication. However, the auditor considers the reliability of the information to be used as audit evidence, for example, photocopies, facsimiles, filmed, digitized or other electronic documents, including consideration of controls over their preparation and maintenance where relevant.
11. **When information produced by the entity is used by the auditor to perform audit procedures, the auditor should obtain audit evidence about the accuracy and completeness of the information.** In order for the auditor to obtain reliable audit evidence, the information upon which the audit procedures are based needs to be sufficiently complete and accurate. For example, in auditing revenue by applying standard prices to records of sales volume, the auditor considers the accuracy of the price information and the completeness and accuracy of the sales volume data. Obtaining audit evidence about the completeness and accuracy of the information produced by the entity's information system may be performed concurrently with the actual audit procedure applied to the information when obtaining such audit evidence is an integral part of the audit procedure itself. In other situations, the auditor may have obtained audit evidence of the accuracy and completeness of such information by testing controls over the production and maintenance of the information. However, in some situations the auditor may determine that additional audit procedures are needed. For example, these additional procedures may include using computer-assisted audit techniques (CAATs) to recalculate the information.
12. The auditor ordinarily obtains more assurance from consistent audit evidence obtained from different sources or of a different nature than from items of audit evidence considered individually. In addition, obtaining audit evidence from different sources or of a different nature may indicate that an individual item of audit evidence is not reliable. For example, corroborating information obtained from a source independent of the entity may increase the assurance the auditor

obtains from a management representation. Conversely, when audit evidence obtained from one source is inconsistent with that obtained from another, the auditor determines what additional audit procedures are necessary to resolve the inconsistency.

13. The auditor considers the relationship between the cost of obtaining audit evidence and the usefulness of the information obtained. However, the matter of difficulty or expense involved is not in itself a valid basis for omitting an audit procedure for which there is no alternative.
14. In forming the audit opinion the auditor does not examine all the information available because conclusions ordinarily can be reached by using sampling approaches and other means of selecting items for testing. Also, the auditor ordinarily finds it necessary to rely on audit evidence that is persuasive rather than conclusive; however, to obtain reasonable assurance,² the auditor is not satisfied with audit evidence that is less than persuasive. The auditor uses professional judgment and exercises professional skepticism in evaluating the quantity and quality of audit evidence, and thus its sufficiency and appropriateness, to support the audit opinion.

The Use of Assertions in Obtaining Audit Evidence

15. Management is responsible for the fair presentation of financial statements that reflect the nature and operations of the entity. In representing that the financial statements give a true and fair view (or are presented fairly, in all material respects) in accordance with the applicable financial reporting framework, management implicitly or explicitly makes assertions regarding the recognition, measurement, presentation and disclosure of the various elements of financial statements and related disclosures.
16. **The auditor should use assertions for classes of transactions, account balances, and presentation and disclosures in sufficient detail to form a basis for the assessment of risks of material misstatement and the design and performance of further audit procedures.** The auditor uses assertions in assessing risks by considering the different types of potential misstatements that may occur, and thereby designing audit procedures that are responsive to the assessed risks. Other ISAs discuss specific situations where the auditor is required to obtain audit evidence at the assertion level.
17. Assertions used by the auditor fall into the following categories:
 - (a) Assertions about classes of transactions and events for the period under audit:

² ISA 200, “Objective and General Principles Governing an Audit of Financial Statements” provides discussion of reasonable assurance as it relates to an audit of financial statements.

- (i) Occurrence—transactions and events that have been recorded have occurred and pertain to the entity.
 - (ii) Completeness—all transactions and events that should have been recorded have been recorded.
 - (iii) Accuracy—amounts and other data relating to recorded transactions and events have been recorded appropriately.
 - (iv) Cutoff—transactions and events have been recorded in the correct accounting period.
 - (v) Classification—transactions and events have been recorded in the proper accounts.
- (b) Assertions about account balances at the period end:
- (i) Existence—assets, liabilities, and equity interests exist.
 - (ii) Rights and obligations—the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
 - (iii) Completeness—all assets, liabilities and equity interests that should have been recorded have been recorded.
 - (iv) Valuation and allocation—assets, liabilities, and equity interests are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.
- (c) Assertions about presentation and disclosure:
- (i) Occurrence and rights and obligations—disclosed events, transactions, and other matters have occurred and pertain to the entity.
 - (ii) Completeness—all disclosures that should have been included in the financial statements have been included.
 - (iii) Classification and understandability—financial information is appropriately presented and described, and disclosures are clearly expressed.
 - (iv) Accuracy and valuation—financial and other information are disclosed fairly and at appropriate amounts.
18. The auditor may use the assertions as described above or may express them differently provided all aspects described above have been covered. For example, the auditor may choose to combine the assertions about transactions and events with the assertions about account balances. As another example, there may not be a separate assertion related to cutoff of transactions and

events when the occurrence and completeness assertions include appropriate consideration of recording transactions in the correct accounting period.

Audit Procedures for Obtaining Audit Evidence

19. The auditor obtains audit evidence to draw reasonable conclusions on which to base the audit opinion by performing audit procedures to:
 - (a) Obtain an understanding of the entity and its environment, including its internal control, to assess the risks of material misstatement at the financial statement and assertion levels (audit procedures performed for this purpose are referred to in the ISAs as “risk assessment procedures”);
 - (b) When necessary or when the auditor has determined to do so, test the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level (audit procedures performed for this purpose are referred to in the ISAs as “tests of controls”); and
 - (c) Detect material misstatements at the assertion level (audit procedures performed for this purpose are referred to in the ISAs as “substantive procedures” and include tests of details of classes of transactions, account balances, and disclosures and substantive analytical procedures).
20. The auditor always performs risk assessment procedures to provide a satisfactory basis for the assessment of risks at the financial statement and assertion levels. Risk assessment procedures by themselves do not provide sufficient appropriate audit evidence on which to base the audit opinion, however, and are supplemented by further audit procedures in the form of tests of controls, when necessary, and substantive procedures.
21. Tests of controls are necessary in two circumstances. When the auditor’s risk assessment includes an expectation of the operating effectiveness of controls, the auditor is required to test those controls to support the risk assessment. In addition, when substantive procedures alone do not provide sufficient appropriate audit evidence, the auditor is required to perform tests of controls to obtain audit evidence about their operating effectiveness.
22. The auditor plans and performs substantive procedures to be responsive to the related assessment of the risks of material misstatement, which includes the results of tests of controls, if any. The auditor’s risk assessment is judgmental, however, and may not be sufficiently precise to identify all risks of material misstatement. Further, there are inherent limitations to internal control, including the risk of management override, the possibility of human error and the effect of systems changes. Therefore, substantive procedures for material

classes of transactions, account balances, and disclosures are always required to obtain sufficient appropriate audit evidence.

23. The auditor uses one or more types of audit procedures described in paragraphs 26-38 below. These audit procedures, or combinations thereof, may be used as risk assessment procedures, tests of controls or substantive procedures, depending on the context in which they are applied by the auditor. In certain circumstances, audit evidence obtained from previous audits may provide audit evidence where the auditor performs audit procedures to establish its continuing relevance.
24. The nature and timing of the audit procedures to be used may be affected by the fact that some of the accounting data and other information may be available only in electronic form or only at certain points or periods in time. Source documents, such as purchase orders, bills of lading, invoices, and checks, may be replaced with electronic messages. For example, entities may use electronic commerce or image processing systems. In electronic commerce, the entity and its customers or suppliers use connected computers over a public network, such as the Internet, to transact business electronically. Purchase, shipping, billing, cash receipt, and cash disbursement transactions are often consummated entirely by the exchange of electronic messages between the parties. In image processing systems, documents are scanned and converted into electronic images to facilitate storage and reference, and the source documents may not be retained after conversion. Certain electronic information may exist at a certain point in time. However, such information may not be retrievable after a specified period of time if files are changed and if backup files do not exist. An entity's data retention policies may require the auditor to request retention of some information for the auditor's review or to perform audit procedures at a time when the information is available.
25. When the information is in electronic form, the auditor may carry out certain of the audit procedures described below through CAATs.

Inspection of Records or Documents

26. Inspection consists of examining records or documents, whether internal or external, in paper form, electronic form, or other media. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production. An example of inspection used as a test of controls is inspection of records or documents for evidence of authorization.
27. Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as a stock or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value. In addition, inspecting an executed

contract may provide audit evidence relevant to the entity's application of accounting policies, such as revenue recognition.

Inspection of Tangible Assets

28. Inspection of tangible assets consists of physical examination of the assets. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets. Inspection of individual inventory items ordinarily accompanies the observation of inventory counting.

Observation

29. Observation consists of looking at a process or procedure being performed by others. Examples include observation of the counting of inventories by the entity's personnel and observation of the performance of control activities. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place and by the fact that the act of being observed may affect how the process or procedure is performed. See ISA 501, "Audit Evidence—Additional Considerations for Specific Items" for further guidance on observation of the counting of inventory.

Inquiry

30. Inquiry consists of seeking information of knowledgeable persons, both financial and non-financial, throughout the entity or outside the entity. Inquiry is an audit procedure that is used extensively throughout the audit and often is complementary to performing other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.
31. Responses to inquiries may provide the auditor with information not previously possessed or with corroborative audit evidence. Alternatively, responses might provide information that differs significantly from other information that the auditor has obtained, for example, information regarding the possibility of management override of controls. In some cases, responses to inquiries provide a basis for the auditor to modify or perform additional audit procedures.
32. The auditor performs audit procedures in addition to the use of inquiry to obtain sufficient appropriate audit evidence. Inquiry alone ordinarily does not provide sufficient audit evidence to detect a material misstatement at the assertion level. Moreover, inquiry alone is not sufficient to test the operating effectiveness of controls.
33. Although corroboration of evidence obtained through inquiry is often of particular importance, in the case of inquiries about management intent, the

information available to support management's intent may be limited. In these cases, understanding management's past history of carrying out its stated intentions with respect to assets or liabilities, management's stated reasons for choosing a particular course of action, and management's ability to pursue a specific course of action may provide relevant information about management's intent.

34. In respect of some matters, the auditor obtains written representations from management to confirm responses to oral inquiries. For example, the auditor ordinarily obtains written representations from management on material matters when other sufficient appropriate audit evidence cannot reasonably be expected to exist or when the other audit evidence obtained is of a lower quality. See ISA 580, "Management Representations" for further guidance on written representations.

Confirmation

35. Confirmation, which is a specific type of inquiry, is the process of obtaining a representation of information or of an existing condition directly from a third party. For example, the auditor may seek direct confirmation of receivables by communication with debtors. Confirmations are frequently used in relation to account balances and their components, but 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. Confirmations also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a "side agreement" that may influence revenue recognition. See ISA 505, "External Confirmations" for further guidance on confirmations.

Recalculation

36. Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation can be performed through the use of information technology, for example, by obtaining an electronic file from the entity and using CAATs to check the accuracy of the summarization of the file.

Reperformance

37. Reperformance is the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control, either manually or through the use of CAATs, for example, reperforming the aging of accounts receivable.

Analytical Procedures

38. Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial and non-financial data.

Analytical procedures also encompass the investigation of identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts. See ISA 520, “Analytical Procedures” for further guidance on analytical procedures.

Effective Date

39. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2004.

Public Sector Perspective

1. *When carrying out audits of public sector entities, the auditor takes into account the legislative framework and any other relevant regulations, ordinances or ministerial directives that affect the audit mandate and any other special auditing requirements. In making assertions about the financial statements, management asserts that transactions and events have been in accordance with legislation or proper authority in addition to the assertions in paragraph 15 of this ISA.*