

Auditing Standard

AUS 502
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Audit Evidence

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Auditing Standards contain the basic principles and essential procedures identified in bold-type (black lettering) which are mandatory, together with related guidance. For further information about the responsibility of members for compliance with AUSs refer Miscellaneous Professional Statement APS 1.1 "Conformity with Auditing Standards".

Copies of this Standard are available for purchase from the offices of the Australian Accounting Research Foundation, 211 Hawthorn Road, Caulfield, Victoria 3162, Australia.

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AUDITING STANDARD

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Introduction

- .01 The purpose of this Auditing Standard (AUS) is to establish standards and provide guidance on the quantity and quality of audit evidence to be obtained when auditing a financial report, and the procedures for obtaining that evidence.
- .02 *The auditor should obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion.*
- .03 Audit evidence is obtained during all phases of the audit process which includes an appropriate mix of tests of control and substantive procedures. The auditor will use professional judgement to determine the appropriate mix of audit procedures. In some circumstances, sufficient appropriate audit evidence may be obtained entirely from substantive procedures.
- .04 "Audit evidence" means the information obtained by the auditor in arriving at the conclusions on which the audit opinion is based. Audit evidence will comprise source documents and accounting records underlying the financial report, and corroborating information from other sources.
- .05 "Tests of control" means tests performed to obtain audit evidence about the suitability of design and effective operation of the internal control structure.
- .06 "Substantive procedures" means tests performed to obtain audit evidence to detect material misstatements in the financial report, and are of the following types:
- (a) tests of details of:
 - (i) transactions; and
 - (ii) balances; and
 - (b) analytical procedures.

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Sufficient Appropriate Audit Evidence

- .07 Sufficiency and appropriateness are interrelated and apply to audit evidence obtained from both tests of control and substantive procedures. Sufficiency is the measure of the quantity of audit evidence; appropriateness is the measure of the quality of audit evidence, its relevance to particular assertions and its reliability. Ordinarily, the auditor finds it necessary to rely on audit evidence that is persuasive rather than conclusive, and will often seek audit evidence from different sources or of a different nature to support the same assertion.
- .08 In forming the audit opinion, the auditor does not ordinarily examine all of the information available because conclusions can be reached about an account balance, class of transactions or control using judgemental or statistical sampling procedures.
- .09 The auditor's judgement as to what is sufficient appropriate audit evidence is influenced by such factors as the:
- (a) auditor's assessment of the nature and level of inherent risk at both the financial report level and the account balance or class of transactions level;
 - (b) nature of the internal control structure and the assessment of control risk;
 - (c) materiality of the item being examined;
 - (d) experience gained during previous audits;
 - (e) results of audit procedures, including fraud, other illegal acts and error which may have been found; and
 - (f) source and reliability of information available.
- .10 ***When obtaining audit evidence from tests of control, the auditor should consider the sufficiency and appropriateness of the audit evidence to support the assessed level of control risk.***
- .11 The aspects of the internal control structure about which the auditor would obtain audit evidence are:
- (a) *design*: the internal control structure is suitably designed to prevent and/or detect and correct material misstatements; and

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- (b) *operation*: the internal control structure exists and has operated effectively throughout the relevant period.
- .12 ***When obtaining audit evidence from substantive procedures, the auditor should consider the sufficiency and appropriateness of audit evidence from such procedures, together with any evidence from tests of control to support financial report assertions.***
- .13 Financial report assertions are assertions by management, explicit or otherwise, that are embodied in the financial report. They can be categorised as follows:
- (a) *existence*: an asset or a liability exists at a given date;
- (b) *rights and obligations*: an asset or liability pertains to the entity at a given date;
- (c) *occurrence*: a transaction or other event took place which pertains to the entity during the relevant period;
- (d) *completeness*: there are no unrecorded assets, liabilities, transactions or other events, or undisclosed items;
- (e) *valuation*: an asset or liability is recorded at an appropriate carrying value;
- (f) *measurement*: a transaction or other event is recorded at the proper amount and revenue or expense is allocated to the proper period; and
- (g) *disclosure*: an item is disclosed, classified, and described in accordance with the applicable financial reporting framework.
- .14 Ordinarily, audit evidence is obtained regarding each financial report assertion. Audit evidence regarding one assertion, for example existence of inventory, will not compensate for failure to obtain audit evidence regarding another, for example valuation. The nature, timing and extent of substantive procedures will vary depending on the assertions. Tests can provide audit evidence about more than one assertion, for example collection of receivables may provide audit evidence regarding both existence and valuation.
- .15 The reliability of audit evidence is influenced by its source: internal or external, and by its nature: visual, documentary or oral. While the reliability of audit evidence is dependent on individual

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circumstances, the following generalisations will help in assessing the reliability of audit evidence:

- (a) audit evidence from external sources, for example confirmation received from a third party is more reliable than that generated internally;
- (b) audit evidence generated internally is more reliable when the related internal control is effective;
- (c) audit evidence obtained directly by the auditor is more reliable than that obtained from the entity; and
- (d) audit evidence in the form of documents and written representations is more reliable than oral representations.

- .16 Audit evidence is more persuasive when items of evidence from different sources or of a different nature are consistent. In these circumstances, the auditor may obtain a cumulative degree of confidence higher than would be obtained from items of audit evidence when considered individually. Conversely, when audit evidence obtained from one source is inconsistent with that obtained from another, the auditor determines what additional procedures are necessary to resolve the inconsistency.
- .17 The auditor needs to consider the relationship between the cost of obtaining audit evidence and the usefulness of the information obtained. However, the matters of difficulty and expense involved are not in themselves valid bases for omitting a necessary procedure.
- .18 When in substantial doubt as to a material financial report assertion, the auditor would attempt to obtain sufficient appropriate audit evidence to remove such doubt. ***If unable to obtain sufficient appropriate audit evidence, a scope limitation exists, and the auditor should, in accordance with AUS 702 "The Audit Report on a General Purpose Financial Report", express a qualified opinion.***

Procedures for Obtaining Audit Evidence

- .19 The auditor obtains audit evidence by one or more of the following procedures: inspection, observation, inquiry and confirmation, computation and analytical procedures. The timing of such procedures will be dependent, in part, upon the periods of time during which the audit evidence sought is available.

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Inspection

- .20 Inspection consists of examining records, documents, or tangible assets. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and the effectiveness of internal controls over their processing. Three major categories of documentary audit evidence, which provide different degrees of reliability to the auditor, are:
- (a) documentary audit evidence created and held by third parties;
 - (b) documentary audit evidence created by third parties and held by the entity; and
 - (c) documentary audit evidence created and held by the entity.
- Inspection of tangible assets provides reliable audit evidence with respect to their existence but not necessarily as to future economic benefits or measurement.

Observation

- .21 Observation consists of looking at a process or procedure being performed by others. For example, the auditor may observe the counting of inventories by entity personnel or the performance of control procedures that leave no audit trail.

Inquiry and Confirmation

- .22 Inquiry consists of seeking appropriate information of knowledgeable persons inside or outside the entity. Inquiries may range from formal written inquiries addressed to third parties, to informal oral inquiries addressed to persons inside the entity. Responses to inquiries may provide the auditor with information not previously possessed, or with corroborative audit evidence.
- .23 Confirmation consists of the response to an inquiry to corroborate information contained in the accounting records. For example, the auditor ordinarily seeks direct confirmation of receivables by communication with debtors.

Computation

- .24 Computation consists of checking the arithmetical accuracy of source documents and accounting records, or of performing independent calculations.

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Analytical Procedures

- .25 Analytical procedures consist of the investigation and analysis of fluctuations and relationships to determine whether there are inconsistencies with other relevant information, or deviations from predicted amounts.

Operative Date

- .26 This AUS is operative in relation to the first financial reporting period commencing on or after 1 July, 1996 and later reporting periods, although earlier application is encouraged. This AUS supersedes Statement of Auditing Practice AUP 14 "Audit Evidence" as issued in January 1983.

Compatibility with International Standards on Auditing

- .27 The basic principles and essential procedures of this AUS and of International Standard on Auditing ISA 500, Audit Evidence, are consistent in all material respects.