

## **External confirmations (Lecture A837 – 7.59 minutes)**

ISA (UK) 505 *External Confirmations* provides guidance to auditors on obtaining external confirmations for use as audit evidence.

An external confirmation is audit evidence obtained in written form by the auditor in response to a request from the auditor. ISA (UK) 505 acknowledges that the response can be in paper form or by electronic or other medium.

There are a couple of points that are worthy of consideration where ISA (UK) 505 is concerned.

### **1.1 Proposed revisions to ISA (UK) 505**

The FRC has recently carried out a consultation to revise ISA (UK) 505 to reflect recent enforcement findings and to ensure that the ISA (UK) is reflective of modern approaches to obtaining confirmations. Comments on this consultation closed on 1 September 2023. A summary of the proposed changes are as follows:

#### **Additional clarification on electronic external confirmations**

ISA (UK) 505 currently acknowledges that external confirmations can be obtained electronically. However, the FRC is proposing to include additional wording that clarifies that external confirmations can be obtained through directly accessing information held by third parties through web portals or software interfaces.

#### **Prohibition of negative confirmations**

A 'negative confirmation request' is a request where the confirming party responds to the auditor only if the confirming party disagrees with the information provided in the request. The FRC is proposing to prohibit the use of negative confirmation requests.

The FRC has come across instances where auditors have inappropriately relied on negative confirmations, for example where a response was unlikely ever to be received even if there were relevant matters. This calls into question the suitability of negative confirmation requests. In addition, the FRC considers them a less persuasive form of audit evidence compared to positive confirmation requests.

#### **Designing confirmation requests to provide assertion-based audit evidence**

Additional material is proposed to be included in ISA (UK) 505 to ensure that auditors design confirmations to obtain sufficient appropriate audit evidence in relation to all assertions identified in respect of ISA (UK) 330 *The Auditor's Responses to Assessed Risks*.

## Enhanced requirements to investigating exceptions

The FRC is proposing to include enhanced requirements to the auditor's responsibilities when investigating exceptions. The FRC have come across instances where auditors are not appropriately considering risk when confirmations are not as expected.

The enhanced requirements will direct auditors to consider if exceptions are indicative of fraud or a deficiency in the entity's system of internal control and how follow-up procedures will allow the auditor to obtain sufficient appropriate audit evidence.

### Effective date

The proposed effective date of the revised ISA (UK) 505 will be for audits of financial statements for periods beginning on or after 15 December 2024.

## 1.2 Bank confirmation requests

An issue that has seemingly come to the surface relates to obtaining sufficient appropriate audit evidence over the **completeness** of bank balances at the year end.

ISA (UK) 505 does not make it mandatory for an auditor to obtain a bank confirmation letter (often referred to as a 'bank audit letter' or 'bank certificate'). This is now based on the auditor's risk assessment.

Nowadays, clients will often keep a copy of the year-end bank statement that has been downloaded from the online banking system on file and many auditors take a copy of this bank statement and use it as audit evidence to support the balance per the bank statement on the client's year-end bank reconciliation.

Many banks tend not to send out paper bank statements in the post anymore and so an original bank statement may not be available. Where the auditor has not obtained a bank confirmation letter, the completeness of the year-end bank balances still needs to be adequately verified.

There is a risk that the copy of the bank statement downloaded from the online banking system may have been 'doctored' (remember, original documents are more reliable audit evidence than copies). To address this risk, it is advisable to ask the audit client to logon to the online banking system to prove the balances of each bank account at the year end. The auditor should then document that they have done this on the audit file so that the reviewer can see that the completeness assertion has been adequately covered.

While ISA (UK) 505 does not mandate the auditor to obtain a bank confirmation letter, they can still provide the necessary audit evidence, particularly where the auditor may consider the risk of material misstatement of the year-end bank balances to be higher.