



NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

EXPLANATORY GUIDE Au7

References to Practical Guidance on Professional Scepticism in an Audit of Financial Statements

Issued February 2013

This Explanatory Guide provides references to papers that contain guidance on how professional scepticism can be enhanced in an audit of financial statements, and reflected in audit documentation.

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REFERENCES TO PRACTICAL GUIDANCE ON PROFESSIONAL SCEPTICISM IN AN
AUDIT OF FINANCIAL STATEMENTS

Issued by the New Zealand Auditing and Assurance Standards Board

Professional Scepticism in an Audit of Financial Statements

- 1 Professional scepticism has an important role to play in the audit of financial statements. Being sceptical is a key element of every ISA (NZ) audit. Rather than approaching work in an unthinking box-ticking way, the auditor should challenge information and the evidence obtained.
- 2 Scepticism is a behavioural issue or attitude of mind for the entire audit team rather than an issue that can be addressed solely through specific requirements in standards. The ISAs (NZ) should be brought to life by ensuring that all auditor behaviour and actions flow from, and are informed by a sceptical mindset. It includes walking the floors, communicating effectively with the client's staff and challenging what you are being told if it doesn't make sense.
- 3 The public places high value on the independent financial audit because it enhances the degree of confidence of intended users on the financial statements. The International Auditing and Assurance Standards Board (IAASB) and a number of national standard setters have issued papers on the subject of auditor scepticism. These papers provide auditors with guidance on how professional scepticism can be enhanced in an audit of financial statements, and reflected in audit documentation.

**Sources of practical guidance on professional scepticism in an audit of
Financial Statements**

- 4 The papers noted below provide guidance on how professional scepticism can be applied and evidenced in practice.

International Auditing and Assurance Standards Board**[IAASB: Staff Questions and Answers – Professional Skepticism in an audit of Financial Statements \(2012\)](#)**

- 5 This is a question-and-answer (Q&A) publication that re-emphasises to auditors the importance of an attitude of professional scepticism when performing their role.
- 6 The Q&A publication focuses on the requirements and application material in the ISAs and the IAASB's quality control standard that are of particular relevance to the proper understanding and application of professional scepticism during an audit of financial statements. In addition, answers are provided regarding what audit firms and

auditors can do to enhance awareness of the importance of professional scepticism, identify aspects of an audit where professional scepticism may be particularly important, and how professional scepticism can be evidenced.

Auditing Practices Board (APB)

Professional Scepticism, Establishing a Common Understanding and Reaffirming its Central Role in Delivering Audit Quality (March 2012)

- 7 The paper sets out the APB's considered views on the nature of auditor scepticism and its role in the audit. The document builds on the APB Discussion Paper published in August 2010 'Auditor Scepticism: Raising the Bar' and the subsequent feedback Paper published in March 2011. The overarching message is that the relationship between the auditor and the client should not be close, and that auditors work for the stakeholder and should reflect their cynical sentiment on financial reports accordingly. The paper has seven sections:
- The first section explains that the paper is a guide the APB hopes all auditors will consider, and includes background information.
 - The second section goes into philosophy, looking at the history of the word scepticism and its Greek origin. It pushes auditors to return to their roots and think of the state of mind needed to produce a sceptical opinion, if necessary, on financial statements
 - The third section looks more deeply at developing an audit strategy and how other professions such as scientists have created a sceptical approach.
 - The fourth section looks at the relationship between the auditor and the business' management:
 - The idea of working independently from management is carried through to section five.
 - Section six showcased the challenges faced by auditors. It outlines what audit firms, teams and individuals need to do to enhance scepticism.
 - Section seven looks at how the APB will push this issue forward.

Australian Auditing and Assurance Standards Board (AUASB) Bulletin

Professional Scepticism in an Audit of a Financial Report (August 2012)

- 8 The AUASB bulletin is presented in Question and Answer form and seeks to encourage auditors to bring "professional scepticism" to front-of mind in the conduct of audit engagements.
- 9 It addresses the following questions:
- What is professional scepticism?
 - How is professional scepticism applied?

- How does professional scepticism relate to the auditor's responsibilities with respect to fraud?
- Why is professional scepticism important?
- How is professional scepticism evidenced?
- How can awareness of the importance of professional scepticism be maintained?

Public Company Accounting Oversight Board (PCAOB)

Staff Audit Practice Alert No. 10 – Maintaining and Applying Professional Scepticism in Audits (December 2012)

- 10 The PCAOB continues to observe instances in which circumstances suggest that auditors did not appropriately apply professional scepticism in their audits. This is a Staff Audit Practice Alert to remind auditors of their requirement to exercise professional scepticism throughout their audits.
- 11 The alert focuses on:
- the importance of professional scepticism and due professional care;
 - factors that impair an auditor's scepticism;
 - certain important considerations to promote professional scepticism using audit firms' quality control systems;
 - steps that firms and auditors can take to enhance their application of professional scepticism; and
 - the appropriate application of professional scepticism in audits.

Institute of Chartered Accountants Australia (ICAA)

Preserving capital market confidence through audit quality (Feb 2013)

- 12 The ICAA presents quantitative data research of auditors from five major accounting firms in Australia to assess the importance of the main drivers of audit quality in those firms. The value of exercising professional skepticism in auditing is front and foremost for auditors in practice, yet more work can be done to build capability in this area.
- 13 The publication highlights key messages resulting from the research:
- The sustainability of the profession;
 - Professional skepticism;
 - Communication;
 - The audit committee;
 - Influencing the profession.