



INTERNATIONAL STANDARD ON AUDITING (NEW ZEALAND) 505

External Confirmations (ISA (NZ) 505)

Effective for audits of historical financial statements for periods beginning on or after 1 September, 2011.

This Standard was issued by the External Reporting Board pursuant to section 24(1)(b) of the Financial Reporting Act 1993. This Standard is a disallowable instrument for the purposes of the Legislation Act 2012.

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<p>International Standard on Auditing (New Zealand) (ISA (NZ)) 505, “External Confirmations” should be read in conjunction with ISA (NZ) 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (New Zealand).”</p>

History of Amendments

Table of pronouncements – ISA (NZ) 505 *External Confirmations*

This table lists the pronouncements establishing and amending ISA (NZ) 505.

Pronouncements	Date approved	Effective date
International Standard on Auditing (New Zealand) 505	July 2011	This ISA (NZ) is effective for audits of historical financial statements for periods beginning on or after 1 September, 2011.
International Standard on Auditing (New Zealand) 610 (Revised 2013) <i>Using the Work of Internal Auditors</i>	April 2013	Effective for audits of financial statements for periods ending on or after 15 December 2013
Use of management and those charged with governance	December 2013	Effective for audits of financial statements for periods beginning on or after 1 July 2014
Conforming and Consequential Amendments to International Standards (New Zealand) Arising from ISA (NZ) 315 (Revised 2019)	February 2020	Effective for audits of financial statements for periods beginning on or after 15 December 2021

Table of Amended Paragraphs in ISA (NZ) 505		
Paragraph affected	How affected	By...[date]
A9, A17, A19	Amended	ISA (NZ) 610 (Revised 2013) [April 2013]
Various	Amended	Use of management and those charged with governance [Dec 2013]
A9, A17, A19	Amended	Conforming and Consequential Amendments to International Standards (New Zealand) Arising from ISA (NZ) 315 (Revised 2019)

Introduction

Scope of this ISA (NZ)

1. This International Standard on Auditing (New Zealand) (ISA (NZ)) deals with the auditor's use of external confirmation procedures to obtain audit evidence in accordance with the requirements of ISA (NZ) 330¹ and ISA (NZ) 500.² It does not address enquiries regarding litigation and claims which are dealt with in ISA (NZ) 501.³

External Confirmation Procedures to Obtain Audit Evidence

2. ISA (NZ) 500 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.⁴ That ISA (NZ) also includes the following generalisations applicable to audit evidence:⁵
 - 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, depending on the circumstances of the audit, audit evidence in the form of external confirmations received directly by the auditor from confirming parties may be more reliable than evidence generated internally by the entity. This ISA (NZ) is intended to assist the auditor in designing and performing external confirmation procedures to obtain relevant and reliable audit evidence.

3. Other ISAs (NZ) recognise the importance of external confirmations as audit evidence, for example:
 - ISA (NZ) 330 discusses the auditor's responsibility to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level, and to design and perform further audit procedures whose nature, timing and extent are based on, and are responsive to, the assessed risks of material misstatement at the assertion level.⁶ In addition, ISA (NZ) 330 requires that, irrespective of the assessed risks of material misstatement, the auditor designs and performs substantive procedures for each material class of transactions, account balance, and disclosure. The auditor is also required to consider whether external confirmation procedures are to be performed as substantive audit procedures.⁷

¹ ISA 330, *The Auditor's Responses to Assessed Risks*.

² ISA 500, *Audit Evidence*.

³ ISA (NZ) 501, *Audit Evidence—Specific Considerations for Selected Items*.

⁴ ISA (NZ) 500, paragraph A9.

⁵ ISA (NZ) 500, paragraph A35.

⁶ ISA (NZ) 330, paragraphs 5-6.

⁷ ISA (NZ) 330, paragraphs 18-19.

- ISA (NZ) 330 requires that the auditor obtain more persuasive audit evidence the higher the auditor's assessment of risk.⁸ To do this, the auditor may increase the quantity of the evidence or obtain evidence that is more relevant or reliable, or both. For example, the auditor may place more emphasis on obtaining evidence directly from third parties or obtaining corroborating evidence from a number of independent sources. ISA (NZ) 330 also indicates that external confirmation procedures may assist the auditor in obtaining audit evidence with the high level of reliability that the auditor requires to respond to significant risks of material misstatement, whether due to fraud or error.⁹
- ISA (NZ) 240 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.¹⁰
- ISA (NZ) 500 indicates that corroborating information obtained from 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 those charged with governance.¹¹

Effective Date

4. This ISA (NZ) is effective for audits of financial statements for periods beginning on or after 1 September, 2011.

Objective

5. The objective of the auditor, when using external confirmation procedures, is to design and perform such procedures to obtain relevant and reliable audit evidence.

Definitions

6. For purposes of the ISAs (NZ), 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.

⁸ ISA (NZ) 330, paragraph 7(b)

⁹ ISA (NZ) 330, paragraph A55

¹⁰ ISA (NZ) 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraph A38

¹¹ ISA (NZ) 500, paragraph A12-A13

- (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 using external confirmation procedures, the auditor shall maintain control over external confirmation requests, including:
 - (a) Determining the information to be confirmed or requested; (Ref: Para. A1)
 - (b) Selecting the appropriate confirming party; (Ref: Para. A2)
 - (c) Designing the confirmation requests, including determining that requests are properly addressed and contain return information for responses to be sent directly to the auditor; and (Ref: Para. A3-A6)
 - (d) Sending the requests, including follow-up requests when applicable, to the confirming party. (Ref: Para. A7)

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, the auditor shall:
 - (a) Enquire as to management’s reasons for the refusal, and seek audit evidence as to their validity and reasonableness; (Ref: Para. A8)
 - (b) Evaluate the implications of management’s refusal on the auditor’s 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. A9)
 - (c) Perform alternative audit procedures designed to obtain relevant and reliable audit evidence. (Ref: Para. A10)
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 relevant and reliable audit evidence from alternative audit procedures, the auditor shall communicate with those charged with governance in accordance with ISA (NZ) 260 (Revised).¹² The auditor also shall determine the implications for the audit and the auditor’s opinion in accordance with ISA (NZ) 705 (Revised).¹³

Results of the External Confirmation Procedures

Reliability of Responses to Confirmation Requests

10. If the auditor identifies factors that give rise to doubts about the reliability of the response to a confirmation request, the auditor shall obtain further audit evidence to resolve those doubts. (Ref: Para. A11-A16)
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

¹² ISA (NZ) 260 (Revised), *Communication with Those Charged with Governance*, paragraph 16

¹³ ISA (NZ) 705 (Revised), *Modifications to the Opinion in the Independent Auditor’s Report*

misstatement, including the risk of fraud, and on the related nature, timing and extent of other audit procedures. (Ref: Para. A17)

Non-Responses

12. In the case of each non-response, the auditor shall perform alternative audit procedures to obtain relevant and reliable audit evidence. (Ref: Para A18-A19)

When a Response to a Positive Confirmation Request Is Necessary to Obtain Sufficient Appropriate Audit Evidence

13. If the auditor has determined that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence, alternative audit procedures will not provide the audit evidence the auditor requires. If the auditor does not obtain such confirmation, the auditor shall determine the implications for the audit and the auditor's opinion in accordance with ISA (NZ) 705 (Revised). (Ref: Para A20)

Exceptions

14. The auditor shall investigate exceptions to determine whether or not they are indicative of misstatements. (Ref: Para. A21-A22)

Negative Confirmations

15. Negative confirmations provide less persuasive audit evidence than positive confirmations. Accordingly, the auditor shall not use negative confirmation requests as the sole substantive audit procedure to address an assessed risk of material misstatement at the assertion level unless all of the following are present: (Ref: Para. A23)
- (a) The auditor has assessed the risk of material misstatement as low and has obtained sufficient appropriate audit evidence regarding the operating effectiveness of controls relevant to the assertion;
 - (b) The population of items subject to negative confirmation procedures comprises a large number of small, homogeneous, account balances, transactions or conditions;
 - (c) A very low exception rate is expected; and
 - (d) The auditor is not aware of circumstances or conditions that would cause recipients of negative confirmation requests to disregard such requests.

Evaluating the Evidence Obtained

16. The auditor shall evaluate whether the results of the external confirmation procedures provide relevant and reliable audit evidence, or whether further audit evidence is necessary. (Ref: Para A24-A25)

Application and Other Explanatory Material

External Confirmation Procedures

Determining the Information to Be Confirmed or Requested (Ref: Para. 7(a))

- A1. External confirmation procedures frequently are performed to confirm or request

information regarding account balances and their elements. They may also be used to confirm terms of agreements, contracts, or transactions between an entity and other parties, or to confirm the absence of certain conditions, such as a “side agreement.”

Selecting the Appropriate Confirming Party (Ref: Para. 7(b))

A2. 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 financial institution from whom to request confirmation.

Designing Confirmation Requests (Ref: Para. 7(c))

A3. 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.

A4. Factors to consider when designing confirmation requests 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 authorisation 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 authorisation.
- The ability of the intended confirming party to confirm or provide the requested information (for example, individual invoice amount versus total balance).

A5. A positive external confirmation request asks the confirming party to reply to the auditor in all cases, either by indicating the confirming party’s agreement with the given information, or by asking the confirming party to provide information. A response to a positive confirmation request ordinarily is expected to provide reliable audit evidence. There is a risk, however, that a confirming party may reply to the confirmation request without verifying that the information is correct. The auditor may reduce this risk by using positive confirmation requests that do not state the amount (or other information) on the confirmation request, and ask the confirming party to fill in the amount or furnish other information. On the other hand, use of this type of “blank” confirmation request may result in lower response rates because additional effort is required of the confirming parties.

A6. Determining that requests are properly addressed includes testing the validity of some or all of the addresses on confirmation requests before they are sent out.

Follow-Up on Confirmation Requests (Ref: Para. 7(d))

A7. The auditor may send an additional confirmation request when a reply to a previous request has not been received within a reasonable time. For example, the auditor may,

having re-verified the accuracy of the original address, send an additional or follow-up request.

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

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

A8. 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 enquire as to 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 seek audit evidence as to the validity and reasonableness of the reasons because of the risk that management may be attempting to deny the auditor access to audit evidence that may reveal fraud or error.

Implications for the Assessment of Risks of Material Misstatement (Ref: Para. 8(b))

A9. The auditor may conclude from the evaluation in paragraph 8(b) that it would be appropriate to revise the assessment of the risks of material misstatement at the assertion level and modify planned audit procedures in accordance with ISA (NZ) 315 (Revised 2019).¹⁴ For example, if management’s request to not confirm is unreasonable, this may indicate a fraud risk factor that requires evaluation in accordance with ISA (NZ) 240.¹⁵

Alternative Audit Procedures (Ref: Para. 8(c))

A10. The alternative audit procedures performed may be similar to those appropriate for a non-response as set out in paragraphs A18-A19 of this ISA (NZ). Such procedures also would take account of the results of the auditor’s evaluation in paragraph 8(b) of this ISA (NZ).

Results of the External Confirmation Procedures

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

A11. ISA (NZ) 500 indicates that even when audit evidence is obtained from sources external to the entity, circumstances may exist that affect its reliability.¹⁶ All responses carry some risk of interception, alteration or fraud. Such risk exists regardless of whether a response is obtained in paper form, or by electronic or other medium. Factors that may indicate doubts about the reliability of a response include that it:

- Was received by the auditor indirectly; or
- Appeared not to come from the originally intended confirming party.

A12. Responses received electronically, for example by facsimile or electronic mail, involve risks as to reliability because proof of origin and authority of the respondent may be difficult to establish, and alterations may be difficult to detect. A process used by the auditor and the respondent that creates a secure environment for responses received electronically may mitigate these risks. If the auditor is satisfied that such a process is secure and properly controlled, the reliability of the related responses is enhanced. An

¹⁴ ISA (NZ) 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*, paragraph 37

¹⁵ ISA (NZ) 240, paragraph 25

¹⁶ ISA (NZ) 500, paragraph A35

electronic confirmation process might incorporate various techniques for validating the identity of a sender of information in electronic form, for example, through the use of encryption, electronic digital signatures, and procedures to verify web site authenticity.

- A13. If a confirming party uses a third party to coordinate and provide responses to confirmation requests, the auditor may perform procedures to address the risks that:
- (a) The response may not be from the proper source;
 - (b) A respondent may not be authorised to respond; and
 - (c) The integrity of the transmission may have been compromised.
- A14. The auditor is required by ISA (NZ) 500 to determine whether to modify or add procedures to resolve doubts over the reliability of information to be used as audit evidence.¹⁷ The auditor may choose to verify the source and contents of a response to a confirmation request by contacting the confirming party. For example, when a confirming party responds by electronic mail, the auditor may telephone the confirming party to determine whether the confirming party did, in fact, send the response. 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 confirming party to respond in writing directly to the auditor.
- A15. On its own, 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 circumstances, request the confirming party to respond in writing directly to the auditor. If no such response is received, in accordance with paragraph 12, the auditor seeks other audit evidence to support the information in the oral response.
- A16. A response to a confirmation request may contain restrictive language regarding its use. Such restrictions do not necessarily invalidate the reliability of the response as audit evidence.

Unreliable Responses (Ref: Para. 11)

- A17. When the auditor concludes that a response is unreliable, the auditor may need to revise the assessment of the risks of material misstatement at the assertion level and modify planned audit procedures accordingly, in accordance with ISA (NZ) 315 (Revised 2019)¹⁸. For example, an unreliable response may indicate a fraud risk factor that requires evaluation in accordance with ISA (NZ) 240.¹⁹

Non-Responses (Ref: Para. 12)

- A18. Examples of alternative audit procedures the auditor may perform include:
- For accounts receivable balances – examining specific subsequent cash receipts, shipping documentation, and sales near the period-end.
 - For accounts payable balances – examining subsequent cash disbursements or correspondence from third parties, and other records, such as goods received notes.

¹⁷ ISA (NZ) 500, paragraph 11

¹⁸ ISA (NZ) 315 (Revised 2019), paragraph 37

¹⁹ ISA (NZ) 240, paragraph 25

A19. The nature and extent of alternative audit procedures are affected by the account and assertion in question. A non-response to a confirmation request may indicate a previously unidentified risk of material misstatement. In such situations, 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 (NZ) 315 (Revised 2019).²⁰ For example, fewer responses to confirmation requests than anticipated, or a greater number of responses than anticipated, may indicate a previously unidentified fraud risk factor that requires evaluation in accordance with ISA (NZ) 240.²¹

When a Response to a Positive Confirmation Request Is Necessary to Obtain Sufficient Appropriate Audit Evidence (Ref. Para. 13)

A20. In certain circumstances, the auditor may identify an assessed risk of material misstatement at the assertion level for which a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence. Such circumstances may include where:

- The information available to corroborate management's assertion(s) is only available outside the entity.
- Specific fraud risk factors, such as the risk of management override of controls, or the risk of collusion which can involve employee(s) and/or management, prevent the auditor from relying on evidence from the entity.

Exceptions (Ref: Para. 14)

A21. Exceptions noted in responses to confirmation requests may indicate misstatements or potential misstatements in the financial statements. When a misstatement is identified, the auditor is required by ISA (NZ) 240 to evaluate whether such misstatement is indicative of fraud.²² Exceptions may provide a guide to the quality of responses from similar confirming parties or for similar accounts. Exceptions also may indicate a deficiency, or deficiencies, in the entity's internal control over financial reporting.

A22. 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. 15)

A23. 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 or verification of the accuracy of the information contained in the request. Accordingly, a failure of a confirming party to respond to a negative confirmation request provides significantly less persuasive audit evidence than does a response to a positive confirmation request. Confirming parties also may be more likely to respond indicating their disagreement with a confirmation request when the information in the request is not in their favour, and less likely to respond otherwise. For example, holders of bank deposit accounts may be more likely to respond if they believe that the balance in their account is understated in the

²⁰ ISA (NZ) 315 (Revised 2019), paragraph 37

²¹ ISA (NZ) 240, paragraph 25

²² ISA (NZ) 240, paragraph 36

confirmation request, but may be less likely to respond when they believe the balance is overstated. Therefore, sending negative confirmation requests to holders of bank deposit accounts may be a useful procedure in considering whether such balances may be understated, but is unlikely to be effective if the auditor is seeking evidence regarding overstatement.

Evaluating the Evidence Obtained (Ref: Para. 16)

A24. When evaluating the results of individual external confirmation requests, the auditor may categorise such results as follows:

- (a) A response by the appropriate confirming party indicating agreement with the information provided in the confirmation request, or providing requested information without exception;
- (b) A response deemed unreliable;
- (c) A non-response; or
- (d) A response indicating an exception.

A25. The auditor's evaluation, when taken into account with other audit procedures the auditor may have performed, may assist the auditor in concluding whether sufficient appropriate audit evidence has been obtained or whether further audit evidence is necessary, as required by ISA (NZ) 330.²³

²³ ISA (NZ) 330, paragraphs 26-27

ACCOMPANYING ATTACHMENT: CONFORMITY TO THE INTERNATIONAL STANDARDS ON AUDITING

This conformity statement accompanies but is not part of ISA (NZ) 505.

Conformity with International Standards on Auditing

This International Standard on Auditing (New Zealand) (ISA (NZ)) conforms to International Standard on Auditing ISA 505 *External Confirmations*, issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this ISA (NZ) (and do not appear in the text of the equivalent ISA) are identified with the prefix “NZ”.

References to “management” and “those charged with governance” have been amended in the ISAs (NZ) because the statutory responsibility for the preparation of the financial statements rests with those charged with governance. The ISAs require the auditor to obtain written representations from management. The ISAs (NZ) require written representations from those charged with governance. Paragraphs where references to “management” have been amended have been labelled as NZ paragraphs.

This ISA (NZ) incorporates terminology and definitions used in New Zealand.

Compliance with this ISA (NZ) enables compliance with ISA 505.

Comparison with Australian Auditing Standards

In Australia the Australian Auditing and Assurance Standards Board (AUASB) has issued Australian Auditing Standard ASA 505 *External Confirmations*.

ASA 505 conforms to ISA 505.