# Exploring the Growing Use of Technology in the Audit, with a focus on Data Analytics

A public consultation issued by IAASB

Comments from ACCA to IAASB
15 February 2017
Ref: TECH-CDR-1501

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ACCA welcomes the opportunity to comment on the proposals issued by IAASB. The ACCA Global Forum for Audit and Assurance has considered the matters raised and their views are represented in the following.

# AREAS FOR SPECIFIC COMMENT:

The IAASB's publication 'Exploring the growing use of technology in the audit, with a focus on data analytics' is a helpful contribution to the debate on how technology could be integrated with existing auditing standards. It identifies many of the important factors that impact the use of data analytics in a financial statement audit. In this context, and to deepen the debate, ACCA makes the following points:

## 1.  Definition of data analytics

'Data analytics' is defined in the paper as 'the science and art of discovering and analysing patterns, deviations and inconsistencies, and extracting other useful information in the data underlying or related to the subject matter of an audit through analysis, modelling and visualisation for the purpose of planning or performing the audit'. To the extent that data analytics is a science, it should be possible to articulate it in a way that can be incorporated into auditing standards, as this would imply that data analytics procedures can be replicated by other professional accountants. However, to the extent that it is an art, this process would seem to be more problematic. One motive for describing data analytics as an art might be to avoid precision around how it is to be practised. In these circumstances, this lack of precision could create challenges for explaining how data analytics should interface with auditing standards. ACCA's view is that the IAASB should prioritise connecting the science of data analytics to auditing standards first.

## 2.  The importance of transactions to auditing

Developments in IFRS and accounting standards generally have led to financial statements which rely less upon transactions processed by systems and accounting adjustments than was the case historically. As a result, an ability to test 100% of transactions, were it to be possible, may be less relevant to the audit of a set of modern financial statements than, say, expertise in estimates and valuations. ACCA anticipates that branches of data analytics that use predictive algorithms and pattern analysis to review management's assumptions on estimates or valuations will develop to enhance audit quality in this area. There are some related issues, such as what further work might be necessary to validate the data beyond reviewing its consistency with management's explanations.

ACCA notes that a claim commonly made about blockchain technology is that it may make auditing obsolete, as transactions will have been validated by counterparties prior to being entered onto the ledger. The IAASB should seek to articulate how auditing standards might accommodate both of these possible futures: one where data analytics allows 100% of transactions to be tested and one where it is claimed that blockchain technology means that no transactions need be tested.

## 3.  Testing 100% of a population compared to sampling

The paper identifies, in paragraph 19(g) that there is an issue in relation to the work effort required following the identification of an exception using data analytics. Conceptually, an approach based upon sampling must produce a similar estimate of the level of misstatement as would testing 100% of the population produce. Where it does not, this can only be because the sample was not representative of the complete population, as might be the case if the sample is too small, or because identified exceptions were not followed up appropriately. Data analytics promises to provide better information about whether a sample is representative and the nature and magnitude of identified exceptions. Accordingly, data analytics should be a useful tool in improving practice around audit sampling.

In addition to the issues raised above over the importance of transactions to auditing, references to '100% of the population' make light of the audit procedures that will remain necessary to establish that information provided to the auditor is complete. It is also unclear whether it is appropriate to conclude that manual testing, which may involve retrieving physical documents and performing further follow-up enquiry and testing, will always be equivalent to a procedure supported by data analytics, which may simply match entries in the accounting system. There is also a risk that the availability of computer-assisted procedures may lead to less interaction between the audit team and the client, and hence actually reduce the team's understanding of the entity, eroding audit quality.

Although the paper makes it clear that being able to test 100% of a population does not imply that the auditor is able to provide more than reasonable assurance, it could still affect the public perception of the term. Indeed, this could fuel the traditional expectation gap. For example, it may be difficult for a firm to explain how it failed to identify a fraud in an environment where data analytics allowed it to test 100% of the population.

On the other hand, a better understanding of the entire population should inform better assessments of the risk of material misstatement and therefore help to focus the auditor's work under ISA 315 and ISA 330. ACCA suggests that the IAASB seek to incorporate these concepts into its existing project to revise ISA 315, in particular the circumstances under which it would be appropriate to exclude certain risks of material misstatement on the grounds that they are considered remote.

## 4.  Understanding General IT controls

Audit inspection reports show that auditors' understanding of general IT controls could be improved (IFIAR 2014 and 2015 findings). Incorporating data analytics into the audit process will require a more in-depth understanding of general IT controls to the extent that existing audit procedures are reduced in favour of a more sophisticated analysis of the wider data set. This is particularly pertinent to the acquisition of data from client systems, especially where a number of different systems are used.

Furthermore firms that use off-the-shelf data analytics software may rely upon the software performing effectively without establishing that it is appropriate to do so. Currently, ISAs include guidance how the auditor should test in-scope software

applications used by the client; however there is no equivalent guidance for software applications used by the auditor. The IAASB should consider incorporating what additional support might be needed by auditors, as regulators might reasonably be expected to challenge auditors in this area.

## 5. Small and Medium-sized Entity audits

Not every audit would necessarily benefit from the use of data analytics. For example, small and medium-sized entities tend to have a lower volume of transactions so the benefits to be gained by implementing data analytics may not outweigh the costs. These costs include the investment necessary to acquire and maintain data analytics software and specialist staff. Such costs are more easily absorbed by larger firms, where economies of scale make them relatively more affordable. On the other hand, small and medium-sized entities tend to have simpler business models that may make it easier to apply data analytics.

While some smaller firms may try to integrate data analytics techniques by using off-the-shelf data analytics software, they may lack expertise or experience, resulting in lower audit quality. An articulation of how small and medium-sized practices can make use of data analytics is important to maintaining the objective for auditing standards to be universally applicable to all entities.

## 6. Client use of data analytics

The IAASB should consider how the auditor should make use of evidence that derive from the client's own use of data analytics. This issue is potentially imminent. For example, an insurer may employ sophisticated, proprietary data analytics to justify reducing its risk ratios. In the UK, one car insurer provides lower insurance premiums to drivers who demonstrate they are safer by reference to a proprietary mobile phone app. Access to such personal data may reasonably be restricted by the client to the auditor due to concerns over data protection. However, without it, it may be difficult to argue that audit evidence obtained is sufficient. If the use of such proprietary analytics were to become widespread, auditors may face barriers in obtaining sufficient appropriate audit evidence over assets and liabilities that are based on personal data.

## 7. Articulating the value in data analytics

Ultimately, it is important to understand where the value in data analytics really lies. Data analytics may contribute to better audit quality either by increasing efficiency or by permitting a greater depth of auditor enquiry. An alternative view is that it may consist of the insights data analytics provide back to the company. If the value of data analytics is largely in the latter, there may be questions for standard-setters and regulators about how to manage issues of auditor independence. Overall, however, it is right for IAASB to be supporting innovation in audit. Data analytics does not indicate that the existing audit methodology is broken, but there is a need for it to develop to accommodate new technologies to remain relevant to users' needs.

**Answers to specific questions**

(a) Have we considered all circumstances and factors that exist in the current business environment that impact the use of data analytics in a financial statement audit?

ACCA believes that the circumstances and factors considered in this paper cover the majority of what exists in the current business environment that impacts the use of data analytics in a financial statement audit, however, ACCA noted above some additional considerations and factors that the DAWG may wish to consider.

(b) Is our list of standard-setting challenges accurate and complete?

Yes.

(c) To assist the DAWG in its on-going work, what are your views on possible solutions to the standard-setting challenges?

ACCA believes the DAWG should prioritise:

- Focusing on data analytics as a science rather than an art in trying to integrate it into auditing standards (see point 1 above).

- Considering using data analytics as a method to support sample-based testing rather than as a replacement for it (see points 2 and 3 above).

- Incorporating data analytics into the auditor's assessment of the risk of material misstatement in accordance with ISA 315 (see point 3 above).

- Supporting the development of some materials to assist the auditor in respect of general IT controls (see point 4 above).

- Accommodating the specific issues that arise from applying data analytics to the audits of small and medium-sized entities (see point 5 above).

- Understanding the nature of audit evidence derived from data analytics procedures (see point 6 above).

- Articulating the value in data analytics (see point 7 above).

(d) Is the DAWG's planned involvement in the IAASB projects currently underway appropriate?

Yes.

(e) Beyond those initiatives noted in the Additional Resources section of this publication, are there other initiatives of which we are not currently aware of that could further inform the DAWG's work?

ACCA is not aware of any other initiatives that could further inform DAWG's work.

(f) In your view, what should the IAASB's and DAWG's next steps be? For example, actions the IAASB and DAWG are currently considering include:

(i) Focusing attention on revisions, where appropriate, to ISAs affected by the IAASB's current projects.

ACCA supports this approach.

(ii) Exploring revisions to ISA 520

ACCA supports the consideration of revisions to ISA 520, as well as any consequential amendments that may be necessary to ISA 500 and other related ISAs, such as ISA 320 ('Materiality in Planning and Performing an Audit').

(iii) Hosting one or more conferences with interested stakeholders to collectively explore issues and possible solutions to the identified challenges.

ACCA supports this proposal and, through the existing work on *Professional Accountants: The Future* and *Generation Next*, is well-placed to assist IAASB in convening stakeholders globally.

(iv) Continuing with outreach and exploration of issues associated with the use of data analytics in a financial statement audit, with a view towards a formal Discussion Paper consultation in advance of any formal standard-setting activities.

ACCA supports continuing outreach and exploration of issues, due to the rate of technological change and innovation in data analytics. There is a need to balance the future flexibility of auditing standards against the practical issues being faced by firms now in using data analytics.