DRAFT INTERNATIONAL STANDARD ON AUDITING 610
USING THE WORK OF THE INTERNAL AUDIT FUNCTION

[CLEAN]

(Effective for audits of financial statements for periods
beginning on or after [ ])

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International Standard on Auditing (ISA) 610, “Using the Work of the Internal Audit Function” should be read in conjunction with ISA 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing.”
Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the external auditor’s responsibilities relating to using the work of the internal audit function when the external auditor has determined, in accordance with ISA 315,\(^1\) that the internal audit function is likely to be relevant to the overall audit strategy and audit plan. It also addresses the external auditor’s responsibilities when using internal auditors to provide direct assistance under the direction and supervision of the external auditor. (Ref: Para. A1-A2)

Relationship between the Internal Audit Function and the External Auditor

3. The objectives of the internal audit function are determined by management and, where applicable, those charged with governance and may include assurance and consulting activities within an entity aimed at evaluating and improving the effectiveness of the entity’s risk management, internal control, and governance processes. Frequently, an entity’s internal audit function performs audit procedures similar to those performed by the external auditor in an audit of financial statements. For example, the internal audit function might plan and perform tests or other procedures to provide assurance regarding the design, implementation and operating effectiveness of internal control relevant to the external audit. External auditors may be able to use such work rather than perform that work themselves in obtaining sufficient appropriate audit evidence on which to base the auditor’s opinion. Internal auditors may also provide direct assistance on the engagement by performing audit procedures under the direction and supervision of the external auditor. (Ref: Para. A2a-A3)

4. Irrespective of the degree of objectivity of the internal audit function, such function is not independent of the entity as is required of the external auditor in an audit of financial statements in accordance with ISA 200.\(^2\) The external auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the external auditor’s use of the work of the internal audit function. For this reason, even if some of the internal audit function’s activities appear relevant to the external audit, the external auditor may conclude that it is either not appropriate in the circumstances, or not efficient, to use the work of the internal audit function. This ISA addresses how the external auditor determines whether and to what extent to use the work of the internal audit function and the external auditor’s evaluation of the adequacy of the work of the internal audit function for purposes of the audit. It also addresses relevant considerations when contemplating whether to use internal auditors to provide direct assistance, including the types of procedures needed in recognition of the fact that work performed by internal auditors is presumed to provide less reliable evidence.

4a. In some jurisdictions, the external auditor may be prohibited, or restricted to some extent, by law or regulation from using the work of the internal audit function, from obtaining direct assistance from internal auditors, or from communicating with the internal audit function to

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\(^1\) ISA 315, “Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment,” paragraph 23.

\(^2\) ISA 200, paragraph 14.
the extent contemplated in this ISA. The ISAs do not override laws or regulations that govern an audit of financial statements. As this ISA does not require the auditor to use the work of the internal audit function or to obtain direct assistance from internal auditors, such prohibitions or restrictions will not prevent the external auditor from complying with the ISAs.

4b. Activities similar to those performed by an internal audit function may be conducted by functions within an entity with other titles. Some or all of the activities of an internal audit function may also be outsourced to a third-party service provider. Neither the title of the function, nor whether it is performed by the entity or a third-party service provider, are determinants of whether or not the external auditor can use the work of the internal audit function. Rather it is the nature of the activities, and the objectivity and competence of the function that are relevant.

4c. There may be individuals within an entity that perform ad hoc procedures similar to those performed within an internal audit function. However, unless performed within an objective and competent function that applies a systematic and disciplined approach, including quality control, such procedures would be considered control activities and obtaining evidence regarding the effectiveness of such controls would be part of the auditor’s responses to assessed risks in accordance with ISA 330.

Effective Date

5. This ISA is effective for audits of financial statements for periods beginning on or after [ ].

Objectives

6. The objectives of the external auditor, where the entity has an internal audit function that the external auditor has determined is likely to be relevant to the overall audit strategy and audit plan, are:

(a) To determine whether, and to what extent, to use the work of the internal audit function; and

(b) If using the work of the internal audit function or obtaining direct assistance from internal auditors, to determine whether that work is adequate for the purposes of the audit.

Requirements

Determining Whether and to What Extent to Use the Work of the Internal Audit Function

Whether the Work of the Internal Audit Function Is Likely to Be Adequate for Purposes of the Audit

9. The external auditor shall determine whether the work of the internal audit function is likely to be adequate for purposes of the audit by evaluating the following:

(a) The degree of objectivity of the internal audit function;

4 ISA 330, “The Auditor’s Responses to Assessed Risks.”
(b) The level of competence of the internal audit function; and
(c) Whether the internal audit function applies a systematic and disciplined approach, including quality control. (Ref: Para. A3a-A4c)

9a. The external auditor shall not use the work of the internal audit function if it has:
   (a) a low degree of objectivity, regardless of its level of competence; or
   (b) a low level of competence, regardless of its degree of objectivity. (Ref: Para. A4a)

Planned Effect of the Work of the Internal Audit Function on the Nature, Timing or Extent of the External Auditor’s Procedures

10. In determining the planned effect of the work of the internal audit function on the nature, timing or extent of the external auditor’s procedures, the external auditor shall consider:
   (a) The auditor’s evaluation of the degree of objectivity and level of competence of the internal audit function;
   (b) The nature and scope of work performed, or to be performed, by the internal audit function and its relevance to the external auditor’s overall audit strategy and audit plan; and
   (c) The amount of judgment involved in:
      (i) Planning and performing relevant audit procedures for particular classes of transactions, account balances and disclosures; and
      (ii) Evaluating the audit evidence gathered by the internal audit function in support of the relevant assertions. (Ref: Para. A4d-A4f)

10a. Since the external auditor has sole responsibility for the audit opinion expressed, the external auditor shall plan to directly perform sufficient procedures to be able to conclude on the key audit judgments regardless of the external auditor’s decision to use the work of the internal audit function. (Ref: Para. A4g)

10b. If the external auditor intends to use the work of the internal audit function, the external auditor shall discuss the planned use of their work with the internal audit function as a basis for coordinating the respective activities. (Ref: Para. A5-A5a)

Using the Work of the Internal Audit Function

11. In order for the external auditor to use the work of the internal audit function, the external auditor shall evaluate and perform audit procedures on that work to determine its adequacy for the external auditor’s purposes. (Ref: Para. A5b-A6a)

12. To determine the adequacy of the work performed by the internal audit function for the external auditor’s purposes, the external auditor shall evaluate whether:
   (a) The work was properly planned, performed, supervised, reviewed and documented;
   (b) Adequate audit evidence has been obtained to enable the internal audit function to draw reasonable conclusions; and
Conclusions reached are appropriate in the circumstances and any reports prepared by the internal audit function are consistent with the results of the work performed. (Ref: Para. A6b)

**Obtaining Direct Assistance from Internal Auditors** (Ref: Para. A7)

12a. If the external auditor plans to use internal auditors to provide direct assistance on the engagement, the external auditor shall evaluate the level of competence and degree of objectivity of the internal auditors who will be providing such assistance.

12b. The external auditor shall direct, supervise and review the work performed by internal auditors on the engagement in accordance with ISA 220. The level of direction, supervision and review shall recognize that internal auditors are not independent of the entity and therefore their work is presumed to provide less reliable evidence than work performed directly by the external auditor.

**Documentation** (Ref: Para. A10-A11)

13. If the external auditor uses the work of the internal audit function, the external auditor shall include in the audit documentation:

(a) The evaluation of the objectivity and competence of the internal audit function, and whether it applies a systematic and disciplined approach, including quality control;

(b) The nature and extent of the work used and the basis for that decision; and

(c) The audit procedures performed by the external auditor to evaluate the adequacy of the work used

14. The working papers prepared by the internal auditors who provided direct assistance on the engagement shall be included in the audit documentation.

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**Application and Other Explanatory Material**

**Scope of this ISA** (Ref: Para. 1)

A1. As described in ISA 315, the entity’s internal audit function is likely to be relevant to the audit if the nature of the internal audit function’s responsibilities and activities are related to the entity’s financial reporting, and the auditor expects to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed.

A2. Carrying out procedures in accordance with this ISA may cause the external auditor to re-evaluate the external auditor’s assessment of the risks of material misstatement. Consequently, this may affect the external auditor’s determination of the relevance of the internal audit function to the audit and whether further application of this ISA is necessary. Similarly, the external auditor may decide not to otherwise use the work of the internal audit function to affect the nature, timing or extent of the external auditor’s procedures, or to receive direct

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5 ISA 220, “Quality Control for an Audit of Financial Statements.”
6 ISA 315, paragraph A102a.
assistance from internal auditors. In those circumstances, the external auditor’s further application of this ISA is not necessary.

**Relationship between the Internal Audit Function and the External Auditor** (Ref: Para. 3-4c)

A2a. As set out in ISA 315, internal auditing refers to assurance and consulting activities within an entity aimed at evaluating and improving the effectiveness of the entity’s risk management, internal control, and governance processes.

A3. The objectives of internal audit functions vary widely and depend on the size and structure of the entity and the requirements of management and, where applicable, those charged with governance. The activities of the internal audit function may include one or more of the following:

**Activities relating to risk management**

- The internal audit function may assist the organization by identifying and evaluating significant exposures to risk and contributing to the improvement of risk management and internal control.

**Activities relating to internal control**

- Evaluation of internal control. The internal audit function may be assigned specific responsibility for reviewing controls, evaluating their operation and recommending improvements thereto. In doing so, the internal audit function provides assurance on the operating effectiveness of the entity’s internal control.

- Examination of financial and operating information. The internal audit function may be assigned to review the means used to identify, measure, classify and report financial and operating information, and to make specific inquiry into individual items, including detailed testing of transactions, balances and procedures.

- Review of operating activities. The internal audit function may be assigned to review the economy, efficiency and effectiveness of operating activities, including non-financial activities of an entity.

- Review of compliance with laws and regulations. The internal audit function may be assigned to review compliance with laws, regulations and other external requirements, and with management policies and directives and other internal requirements.

**Activities relating to governance**

- The internal audit function may assess the governance process in its accomplishment of objectives on ethics and values, performance management and accountability, communicating risk and control information to appropriate areas of the organization and effectiveness of communication among those charged with governance, external and internal auditors, and management.

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7 ISA 315, paragraph A101.
Determining Whether and to What Extent to Use the Work of the Internal Audit Function

Whether the Work of the Internal Audit Function Is Likely to Be Adequate for Purposes of the Audit (Ref: Para. 9)

A3a. The external auditor exercises professional judgment in determining whether the work of the internal audit function is likely to be adequate for the purposes of the audit, and the nature and extent to which it may be appropriate to use work of the internal audit function in the circumstances.

A3b. The objectivity and competence of the internal audit function are particularly important in determining the nature and extent of the use of the work of the internal audit function that is appropriate in the circumstances. Objectivity refers to the ability to perform those tasks without allowing bias, conflict of interest or undue influence of others to override professional or business judgments. Competence refers to the attainment and maintenance of knowledge and skills at the level required to enable assigned tasks to be performed diligently and in accordance with applicable professional standards.

A4. Factors that may affect the external auditor’s determination include the following:

Objectivity

- The status of the internal audit function within the entity and the effect such status has on the ability of the internal audit function to be objective.
- Whether the internal audit function reports to those charged with governance or an officer with appropriate authority, and whether the internal audit function has direct access to those charged with governance.
- Whether the internal audit function is free of any conflicting responsibilities.
- Whether those charged with governance oversee employment decisions related to the internal audit function.
- Whether there are any constraints or restrictions placed on the internal audit function by management or those charged with governance for example, in communicating internal audit findings to the external auditor.

Competence

- Whether there are established policies for hiring, training and assigning internal auditors to internal audit engagements.
- Whether the internal auditors have adequate technical training and proficiency as internal auditors. Relevant criteria which may be considered by the external auditor in making the assessment may include for example, the internal auditors’ possession of a relevant professional designation.
- Whether the internal auditors are members of relevant professional bodies and are obligated to comply with the relevant professional standards and continuing professional development requirements.
A4a. Objectivity and competence may be viewed on a sliding scale. The higher the degree of objectivity and level of competence, the more appropriate it would be for the external auditor to use the work of the internal audit function and in more areas. However, a high degree of objectivity cannot compensate for a low level of competence, and equally, a high level of competence cannot compensate for a lack of objectivity. If the external auditor evaluates the objectivity or competence of the internal audit function as low, it is not appropriate to use their work. (Ref: Para. 9a)

A4b. The application of a systematic and disciplined approach is an important characteristic that distinguishes the activities of the internal audit function from other monitoring control activities that may be performed within the entity.

A4c. Factors that may affect the external auditor’s determination of whether the internal audit function applies a systematic and disciplined approach include the following:

- The existence and adequacy of internal audit manuals or other similar documents, work programs, and documentation and reports prepared by the internal audit function for determining whether its activities are properly planned, supervised, reviewed and documented.
- Whether the internal audit function has appropriate quality control policies and procedures.

Planned Effect of the Work of the Internal Audit Function on the Nature, Timing or Extent of the External Auditor’s Procedures

A4d. Once the external auditor has determined that it is appropriate to use the work of the internal audit function, the determination of the nature and extent of the use of the work of the internal audit function that is appropriate in the circumstances will be influenced by whether the work of the internal audit function is relevant to the overall audit strategy and audit plan and the amount of judgment needed in planning, performing and evaluating such work. (Ref: Para. 10)

A4e. The greater the amount of judgment that is needed to be exercised in designing the audit procedures and evaluating the results thereof, the greater the likelihood that the work of the internal audit function may not be adequate for the purposes of the audit. In such circumstances, it is more likely that the external auditor may need to perform some procedures directly because consideration of the work of the internal audit function alone is unlikely to provide the external auditor with sufficient appropriate audit evidence. (Ref: Para. 10)

A4f. In determining the nature and extent of using the work of the internal audit function in specific areas, and overall in the engagement, other factors, such as the assessed risks of material misstatement at the assertion level for particular classes of transactions, account balances and disclosures, may also be relevant in determining the external auditor’s overall audit strategy and audit plan. (Ref: Para. 10)

A4g. Key audit judgments include assessments of inherent and control risks, materiality of misstatements, sufficiency of tests performed, appropriateness of management’s use of the going-concern assumption, evaluation of significant accounting estimates, adequacy of disclosures in the financial statements, and other matters affecting the auditor’s report. (Ref: Para. 10a)
A5. In discussing the planned use of their work with the internal audit function as a basis for coordinating the respective activities, it may be useful to address the following:

- The timing of such work;
- The extent of audit coverage;
- Materiality for the financial statements as a whole (and, if applicable, materiality level or levels for particular classes of transactions, account balances or disclosures), and performance materiality;
- Proposed methods of item selection;
- Documentation of the work performed; and
- Review and reporting procedures. (Ref: Para. 10b)

A5a. Coordination between the external auditor and the internal audit function is effective when:

- Discussions take place at appropriate intervals throughout the period;
- The external auditor is advised of and has access to relevant internal audit reports and is informed of any significant matters that come to the attention of the internal audit function when such matters may affect the work of the external auditor so that the external auditor may consider the implications of such matters for the external audit; and
- The external auditor informs the internal audit function of any significant matters that may affect the internal audit function. (Ref: Para. 10b)

Using the Work of the Internal Audit Function (Ref: Para. 11)

A5b. Examples of work of the internal audit function that may be used by the external auditor include the following:

- Testing of the operating effectiveness of controls
- Substantive procedures (for example, checking reconciliations)
- Observations of inventory counts
- Tracing transactions through the information system relevant to financial reporting
- Audits or reviews of the financial information, or specified procedures on the financial information of subsidiaries (for example, components that are not significant components to the group)

A6. The nature, timing and extent of the audit procedures that the external auditor performs on the work of the internal audit function will depend on the external auditor’s evaluation of the degree of objectivity and level of competence of the internal audit function, and the amount of judgment exercised by the function in planning and performing relevant audit procedures for particular classes of transactions, account balances and disclosures. Such audit procedures may include the following:

- Reperformance by examining items already examined by the internal audit function
- Examination of other similar items
• Observation of procedures performed by the internal audit function

• Review of the internal audit function’s work program and working papers

A6a. While it is not necessary for the external auditor to do some reperformance of each individual piece of work of the internal audit function, reperformance of some of such work provides a strong form of evidence regarding the adequacy of the work of the internal audit function for purposes of the audit.

A6b. In determining the adequacy of the work performed by the internal audit function, the external auditor may consider whether any exceptions or unusual matters disclosed by the function such as misstatements or control deficiencies are properly addressed by the entity and in the event they are not, whether the internal audit function follow-up on these matters.

**Obtaining Direct Assistance from Internal Auditors** (Ref: Para. 12a-12b)

A7. In addition to using the work of the internal audit function, the external auditor may receive direct assistance from the internal auditors in carrying out audit procedures. As individuals in the internal audit function are not independent of the entity as is required of the external auditor when expressing an opinion on financial statements, audit procedures performed by internal auditors in connection with the external audit are presumed to provide less reliable evidence than work performed directly by the external auditor themselves. Therefore, the direction, supervision or review of the audit procedures performed by the internal auditors will ordinarily be more extensive than if members of the engagement team had performed the work.