



Meeting: IAASB Consultative Advisory Group
Meeting Location: Brussels
Meeting Date: March 6–7, 2012

Agenda Item E.2

Using the Work of Internal Auditors—ISA 610—Report Back

Objective of Agenda Item

1. The objective of this Agenda Item is to provide a report back on proposals of the Representatives on this project as discussed at the September 2011 CAG Meeting.

Papers to Be Referred to during Discussion

2. The discussion on this topic will follow the structure of this CAG Paper.

Project Status and Timeline

3. The IAASB approved ISA 610 (Revised)¹ and ISA 315 (Revised)² at its December 2011 meeting. For reference only, the relevant updated meeting papers for the December 2011 IAASB meeting are included as CAG Reference Papers.
4. The IAASB agreed and finalized the technical content of both ISA 315 (Revised) and ISA 610 (Revised). It approved both ISA 315 and the section of ISA 610 on using the internal audit function for review by the Public Interest Oversight Board (PIOB) and release thereafter.
5. However, regarding the material on direct assistance, the IAASB was cognizant of the need to allow time for the IESBA to further consider the definition of the “engagement team” in the IESBA Code.³ The IESBA intends to propose changes to the IESBA Code's definition of engagement team to resolve any ambiguity that may be seen relative to the internal auditor providing direct assistance.⁴ Accordingly, the IAASB decided to delay request for PIOB approval and release of that section of standard that relates to direct assistance. The IAASB's approval of the technical content of ISA 610 is based on the understanding that the IESBA supports the adequacy of the revised requirements in the section on direct assistance.
6. The IAASB recognizes that it is important to know the IESBA's final changes to the IESBA Code, hence why the IAASB has not requested PIOB approval of due process on the direct assistance

¹ ISA 610 (Revised), *Using the Work of Internal Auditors*

² ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

³ The IESBA's *Code of Ethics for Professional Accountants* (IESBA Code)

⁴ See press release on potential changes to the IESBA Code at <http://www.ifac.org/news-events/2012-02/iesba-proposes-changes-code-ethics-definition-engagement-team>

part of ISA 610 at this time. Equally, the IAASB recognizes that the IESBA needs to know the IAASB's position on direct assistance so that it can consult effectively on proposed changes to the IESBA Code—therefore the IAASB has concluded its debate on the topic and placed the material in a “close-off” format on the IAASB website ISA 610 [Approved and awaiting PIOB approval of due process].⁵ By “closing-off” the direct assistance material, the intent of the IAASB is that there would be no further deliberation of, or changes to, the section. That is, the IAASB is comfortable with its position on direct assistance having developed it following due process but subject to learning of the IESBA's changes to the Code. Having said that, it is not inconceivable that new information could come to light from the IESBA's consultation on the Code that warrants further IAASB consideration relative to its “closed off” document. The IAASB however does not anticipate this will be the case given its own consultations to date.

7. The Appendix to this paper provides a project history, including links to the relevant CAG documentation.

September 12-13, 2011 CAG Discussion

8. Below are extracts from the draft minutes of the September 2011 CAG meeting,⁶ and an indication of how the project Task Force or IAASB has responded to the Representatives' comments.

Representatives' Comments	Task Force/IAASB Response
Ms. Bastolla noted that the proposals seemed very clear and are more indicative of actual practice. She supported the inclusion in the application material of more comprehensive information about the role of internal audit, particularly in supporting the governance function. She noted some challenges with regulators regarding direct assistance, but believed that the controls over use of direct assistance are appropriate. She also noted that the Institute of Internal Auditors (IIA) has no evidence that direct assistance is prevalent in practice.	Support noted.
Mr. Attolini noted that the SMP committee had not submitted a comment letter to the ED. He asked that the requirements in the ISA be examined to ensure that there is no unnecessary burden imposed on SMPs. He suggested the ISA should include a clear statement that there is no further obligation for the external auditor if he is not using internal audit. Mr. Diomeda and Ms. Blomme supported Mr.	Point accepted. A statement is added in ISA 610 (Revised) that clearly states that the ISA does not apply if the entity does not have an internal audit function. [See paragraph 2 of ISA 610 (Approved and awaiting PIOB approval of due process)]

⁵ Available at www.ifac.org/sites/default/files/meetings/files/20111209-IAASB-Updated_Agenda%20Item%204-D-ISA_610_Revised-final_0.pdf

⁶ The minutes will be approved at the March 2011 IAASB CAG meeting.

Representatives' Comments	Task Force/IAASB Response
<p>Attolini's comment and suggested that the ED was clearer.</p> <p>Ms. Hillier noted that the Task Force would consider the paragraph again, but also noted that the IAASB had previously commented that it was overcomplicated.</p>	
<p>Mr. Attolini noted that there was a suggestion that the requirements for using work of internal audit are more stringent than for the use of direct assistance. Ms. Blomme noted that the auditor's obligations may be more explicit for direct assistance than for use of internal audit.</p>	<p>Ms. Hillier responded by noting that that this was not intended. In fact, although the ED had been premised on the principle that the work of the function and direct assistance could be used in the same circumstances, the revisions made in response to comments restricted the use of direct assistance further.</p>
<p>Mr. Hallqvist noted that, as chair of several audit committees, he always requires internal audit to report to the audit committee, and invited external auditors to participate in some meetings that the audit committee has with internal auditors. He noted that the internal audit function is often the secretary to audit committee, which fosters good synchronization between auditors.</p>	<p>Point noted.</p> <p>ISA 610 (Revised) includes a requirement for the external auditor, in communicating with those charged with governance an overview of the planned scope and timing of the audit in accordance with ISA 260, to communicate how the external auditor has planned to use the work of the internal audit function. [See paragraph 18 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p>
<p>Mr. Fleck suggested structuring the ISA in such a way that jurisdictions that prohibit direct assistance can do so and will continue to comply with the ISAs. He noted that the U.K. had not particularly considered the issue prior to the revision of ISA 610 and may choose to prohibit it.</p>	<p>Amendments were made to both the Introductory section in ISA 610, and in the introductory paragraph in the section on direct assistance to clarify this point. However, Ms. Hillier noted that it was nevertheless important that group auditors were aware that it exists so they can instruct component auditors and application material has been added to make that point. [See paragraphs 5, 27 and A31 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p>
<p>Ms. Blomme supported the inclusion of direct assistance, as this was used in many jurisdictions, and noted that the revised draft standard is balanced and responsive to the comments received.</p>	<p>Support noted.</p>
<p>Mr. Hansen expressed the view that the final ISA should require the external auditor to consider internal audit</p>	<p>ISA 315 (Revised) requires the auditor to make inquiries of appropriate individuals within the</p>

Representatives' Comments	Task Force/IAASB Response
<p>reports, as these may indicate material weaknesses in internal control.</p> <p>He asked about the use of direct assistance by internal auditors on significant risks, and whether a reporting obligation on the extent of reliance placed on internal audit would change any conclusions regarding the use of internal audit.</p>	<p>internal audit function (if the function exists). The application material indicates that this may include internal audit reports if they are relevant to financial reporting and the audit. [See paragraphs 6(a) and A10 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p> <p>ISA 610 now prohibits the use of direct assistance for procedures related to higher risks of material misstatement (a category that is larger than significant risks) where the judgment required in performing the relevant audit procedures or evaluating the audit evidence gathered is more than limited. The IAASB decided not to prohibit direct assistance in relation to significant risks because there are circumstances where some of the work involves little or no judgment and prohibiting use in those circumstances seemed unduly restrictive. [See paragraphs 29-30 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p>
<p>Ms. Bastolla was unsure about prohibiting the auditor to use the work of internal audit when the function had already performed specific work. She questioned whether this applied to the entire function or just the individuals involved.</p>	<p>Ms. Hillier responded that this relates to individuals providing assistance only, to avoid self-review threats.</p>
<p>Ms. Bastolla noted that judgments were always involved in internal audit work.</p>	<p>Ms. Hillier agreed, and noted that this was recognized in the proposals. [See paragraphs 16 and 22 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p>
<p>Mr. Roussey supported ISA 610, noting that information systems auditors are a part of internal audit and that it is important to have these people available to the external auditor.</p>	<p>Support noted.</p>
<p>Mr. Pannier supported the Task Force's approach. He noted that this reinforced the importance of internal audit, was in the public interest and reinforced audit quality. He also supported the inclusion of direct assistance.</p>	<p>Support noted.</p>
<p>In relation to the limitations regarding direct assistance, Ms. Sucher preferred the language prohibiting internal auditors</p>	<p>Points partly accepted. The IAASB agreed that the use of direct assistance should not be</p>

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<p>to perform procedures that “are designed to respond to a significant risk of material misstatement” (former paragraph 28(a) of the proposed ISA) rather than those that “relate to higher assessed risks of material misstatement and require judgment in performing the relevant audit procedures or evaluating the audit evidence gathered” (paragraph 28(b)). Also, she was of the view that the reference to judgment was not needed, and it was also unclear how “judgment” could be measured in this case as judgment was relevant in so many audit procedures.</p>	<p>permitted when it would involve:</p> <ul style="list-style-type: none"> - making significant judgments, - higher assessed risks of material misstatement and where the judgment required in performing the relevant audit procedures or evaluating the audit evidence gathered is more than limited, - work with which the internal auditors have been involved and which has already been, or will be, reported to management or those charged with governance by the internal audit function; or - decisions the external auditor makes in accordance with this ISA regarding the internal audit function and the use of its work or direct assistance. <p>The IAASB concluded, in response to ED comments, that the threshold should be areas of higher assessed risks of material misstatement rather than significant risks (a subset of higher risks) where more than limited judgment is required. To illustrate the interaction of risk and judgment, an example has been added to the application material.</p> <p>In relation to the limitation of using internal audit to provide direct assistance when the procedure involved any judgment at all, the IAASB agreed that this appeared overly stringent, in that it could result in the external auditor not being able to use internal auditors to provide direct assistance on almost all audit procedures, due to the prevalence of judgment in auditing. [See paragraphs 29-30 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p>
<p>Mr. Baumann noted that direct assistance is specifically mentioned and permitted in the U.S. He also noted that it was not a topic under review, but that it may be put under review based on the outcome in the ISAs. He noted that the comments questioning the use of direct assistance calls into question the use of internal audit in its entirety, as it was difficult to conclude that the auditor could use internal</p>	<p>The IAASB noted these divergent views, and has agreed to provide guidance on direct assistance, noting that some jurisdictions prohibit it while other jurisdictions permit it. The IAASB noted that ISA 610 does not override such decisions at the national level, but does provide requirements and guidance for when it is used. The IAASB's debate</p>

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<p>audit if direct supervision of their work is not sufficient. He gave the example of two identical companies, in one the auditor is unable to use internal audit to provide direct assistance, in the second internal audit has performed their own work (without direct supervision by the external auditor), that the auditor is able to rely on and hence reduce the extent of the external audit procedures. Ms. Sucher noted that she understood Mr. Baumann's perspective, but that the auditor is considering the robustness of the function rather than individual. She also noted that there was some anecdotal evidence about boards trying to get external audit to rely more on internal audit to cut costs. Mr. Fleck disagreed with Mr. Baumann, and expressed the view that the auditor is not relying on internal audit, but instead taking it as one piece of evidence that is considered by the auditor in determining how much other work to do.</p>	<p>benefited from continued input from IESBA on necessary safeguards. See paragraphs 4-6 above with respect to the approval of the material regarding direct assistance in a "close off" document.</p>
<p>Ms. Sucher asked if ISA 610 would be re-exposed.</p>	<p>The IAASB concluded at its December 2011 that there is no need for re-exposure.</p>
<p>Ms. Bastolla noted that what distinguished internal audit from other monitoring controls is the set of internal audit standards and a disciplined approach.</p> <p>Mr. James noted that there was no definition for a "systematic and disciplined approach."</p>	<p>Ms. Hillier noted that the application material contains considerations relevant to the auditor's assessment of whether internal audit had a systematic and discipline approach. [See paragraphs A10-A11 of ISA 610 (Approved and awaiting PIOB approval of due process)]</p>