

**Using the Work of Internal Auditors—
IAASB Task Force Recommendations in Response to IAASB’s Consideration
of Significant Comments on Exposure****Background**

1. In September 2011, the Task Force received comments from the IAASB, the IAASB Consultative Advisory Group (CAG) and the International Federation of Accountants (IFAC) Small and Medium Practices Committee on the Task Force’s proposed amendments to draft revised ISAs 315 and 610¹ in response to the remaining significant matters raised by the IAASB in relation to respondents’ comments on the Exposure Draft (ED).
2. The IAASB expressed support for draft revised ISA 315 as presented and did not raise further comments. While also expressing broad support for draft revised ISA 610, the IAASB pointed out some areas in the draft ISA which needed to be further clarified or the placement of certain requirements or application guidance needed to be revisited. These matters and the Task Force’s proposals in response are described in the remainder of this issues paper.
3. The IAASB also discussed input provided by the International Ethics Standards Board for Accountants (IESBA) Task Force² regarding their views on the adequacy of the requirements on direct assistance as safeguards to the threats to objectivity that arise when internal auditors provide direct assistance. In view of continued concern amongst some stakeholders about the perceived conflict of direct assistance with independence requirements of external auditors, the IESBA’s decision regarding whether to explicitly permit direct assistance in the IESBA Code³ depends on whether the safeguards in revised ISA 610 are adequate. The outcomes of this discussion were communicated to the IESBA at its October 2011 meeting to input into the IESBA’s consideration of whether and if so, what changes needed to be made to the IESBA Code. Matters discussed by the IESBA and the Task Force’s proposals in response are described in the remainder of this issues paper.

Significant Issues and Task Force Recommendations**Communication with Those Charged With Governance**

4. The ED included application material explaining that, when communicating the overview of the planned scope and timing of the audit with those charged with governance in accordance with ISA 260,⁴ the external auditor would be able to discuss the planned use of

¹ Proposed ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment* and proposed ISA 610 (Revised), *Using the Work of Internal Auditors*

² In June 2011, the IESBA agreed to set up a task force (“IESBA Task Force”) to consider respondents’ comments relating to ethical matters received on the IAASB’s ISA 610 ED. Chair of the ISA 610 Task Force has been invited to participate as a correspondent member on this task force.

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

⁴ ISA 260, *Communication with Those Charged with Governance*, paragraph 15

the work of the internal audit function and direct assistance. In September 2011, the IAASB discussed the IESBA Task Force’s proposal that external auditors should be *required* to communicate their planned use of direct assistance from internal auditors when communicating with those charged with governance an overview of the planned scope and timing of the audit and, in particular, *to seek the concurrence* of those charged with governance prior to engaging the direct assistance of internal auditors.

5. Reflecting on experiences in practice, members of the IAASB had mixed views on whether this would be as robust a safeguard as suggested – a view shared by some of the regulators who had observed evidence of pressure on fees coming from audit committees.⁵ Accordingly, the IAASB did not support a requirement for external auditors to seek pre-approval of those charged with governance, but believed that communication of planned use, consistent with the overarching concepts in ISA 260, would facilitate the appropriate dialogue and supported elevating the current application material to the requirements.
6. In October 2011, the IESBA discussed the IAASB’s reservations but continued to believe that mandating external auditors to communicate with those charged with governance how they have planned to use internal auditors to provide direct assistance in order to agree the approach is an important safeguard that needs to be built into proposed revised ISA 610. The IESBA argued that, whilst interested in audit fees, if required to provide their approval to the planned use of direct assistance, those charged with governance would focus on the possible threat to users’ perceptions of the independence of the external audit that could arise from over or undue use of direct assistance.

Task Force Recommendations

7. The Task Force considers it pertinent to dispel, to the extent possible, any perception that the external auditor’s independence might be compromised by direct assistance even when external auditors engaged internal auditors to perform procedures under the appropriate circumstances and taking adequate measures. Accordingly, the Task Force proposes the following in response to the IESBA’s recommendation:
 - (a) Requiring the external auditor to communicate with those charged with governance how the external auditor has planned to use the work of the internal audit function in communicating an overview of the planned scope and timing of the audit in accordance with ISA 260;⁶ and **[See paragraph 22 in Agenda Item 4-B.]**
 - (b) Requiring 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, communicate the nature and extent of the planned use of internal auditors to provide direct assistance so as to agree that the proposed nature and extent of the use is not excessive. **[See paragraph 32 in Agenda Item 4-B.]**

⁵ Comment made at the EAIG meeting attended by IAASB leadership in September 2011.

⁶ ISA 260, *Communication with Those Charged with Governance*, paragraph 15

Matter for IAASB Consideration

1. The IAASB is asked whether it agrees with requiring 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; and
 - The nature and extent of the external auditor’s planned use of internal auditors to provide direct assistance so as to agree that the proposed nature and extent of the use is not excessive.

Responses to the IESBA Task Force’s Other Inputs

8. In September 2011, the IAASB discussed and agreed the following inputs provided by the IESBA Task Force:
 - (a) Aligning wordings in proposed revised ISA 610 with the IESBA Code:
 - Replacing the phrase “evaluation of threats to the objectivity of an internal auditor” with “evaluation of *the existence and significance* of any threats to the objectivity of an internal auditor.” **[See for example, paragraphs 28, 30(a) and 37(a) in Agenda Item 4-B.]**
 - Replacing the phrase “*compromise* professional judgment” with “*override* professional judgment.” **[See paragraphs A8 and A35 in Agenda Item 4-B.]**
 - The examples of factors that may be relevant in evaluating the existence and significance of threats to an internal auditor’s objectivity in proposed revised ISA 610 refers to the internal auditor’s association with the division in the entity to which the work relates. This should be extended this to include the department in the entity. **[See paragraph A35 in Agenda Item 4-B.]**

The Task Force proposes amending proposed revised ISA 610 accordingly;

- (b) Proposed ISA 610 contains a list of examples of activities and tasks that would not be appropriate for external auditors to use internal auditors to provide direct assistance. The reference to “discussion of matters relating to the audit opinion” appears too wide as the external auditor’s discussions during the audit could arguably be linked ultimately to the audit opinion. On reflection, the Task Force proposes to exclude this example as reactions obtained to date has indicated that it creates more confusion than provide helpful guidance; and **[See paragraph A38 in Agenda Item 4-B.]**
- (c) In relation to the external auditor directing internal auditors who are engaged to provide direct assistance, it was noted that the reference to external auditors directing internal auditors to bring all *significant* accounting and auditing issues identified during the audit to the attention of the external auditor appears to set too high a bar. The Task Force proposes that a more appropriate articulation is “to remind the internal auditors to bring accounting and auditing issues identified during the

audit to the attention of the external auditor. **[See paragraph A41 in Agenda Item 4-B.]**

Matter for IAASB Consideration

2. The IAASB is asked whether it agrees with the Task Force’s proposals to:
 - Amend the wordings in proposed revised ISA 610 as indicated in paragraph 8(a) to align with the IESBA Code;
 - Delete the example “discussion of matters relating to the audit opinion” in the sample list of activities and tasks that would not be appropriate for external auditors to use internal auditors to provide direct assistance in paragraph A38 of proposed revised ISA 610; and
 - Clarify that when external auditors are directing internal auditors who are engaged to provide direct assistance, internal auditors should be reminded to bring accounting and auditing issues identified during the audit to the attention of the external auditor.

Reperforming Work of the Internal Audit Function

9. In September 2011, some IAASB members commented that further guidance is needed to explain the concept of reperformance and its application in the context of the relevant requirements in proposed revised ISA 610. In particular, some questioned whether examining similar items not actually examined by the internal audit function would achieve the same objective as examining items already examined by the internal audit function. A similar point was also raised in meetings with regulators.

Task Force Recommendations

10. The Task Force is in agreement with the IAASB that further explanation would be useful. The Task Force notes that both approaches are necessary because, for example, there are some procedures which cannot be reperfomed after the fact (for example, some procedures related to inventory counts). Performing similar procedures can, however, provide a basis for validating the conclusions that internal audit has reached. The Task Force, therefore, proposes that application guidance be added that further explain the purpose of the external auditor’s examination of items already examined by the internal audit function or examination of sufficient other similar items not actually examined by the internal audit function is to validate the conclusions reached by the internal audit function. **[See paragraph A31 in Agenda Item 4-B.]**

Matter for IAASB Consideration

3. The IAASB is asked whether it agrees with the Task Force’s proposal to clarify the purpose of the external auditor’s reperformance procedures.

Other Matters

11. In September 2011, the IAASB highlighted a number of other areas in draft revised ISA 610 that could be further clarified. These and the Task Force’s proposals are described below:
- (a) It was raised that the circumstances, as set out as in the scope of proposed revised ISA 610, in which the requirements of the ISA would not apply needed to be further clarified. The Task Force accepts this suggestion. It proposes that the following the circumstances—in which the requirements of proposed revised ISA 610 need not be applied—be clearly distinguished:
- (i) If the entity does not have an internal audit function;
- (ii) If the entity has an internal audit function:
- The requirements in proposed revised ISA 610 relating to using the work of the internal audit function do not apply if: (a) the responsibilities and activities of the function are not relevant to the audit; or (b) the external auditor does not expect to use the work of the function in obtaining audit evidence; and
 - The requirements in proposed revised ISA 610 relating to direct assistance do not apply if the external auditor does not plan to use internal auditors to provide direct assistance **[See paragraphs 2–4 in Agenda Item 4-B.]**
- (b) A number of IAASB members noted that the reference to “overall body of work of the internal audit function that the external auditor plans to use” still requires clarification. The Task Force accepts this suggestion and proposes the following:
- To refer to “the work of the internal audit function in aggregate”⁷ when considering whether the extent of use planned would still result in the external auditor being sufficiently involved in the audit **[See paragraph 20 in Agenda Item 4-B.]**
 - To refer to “the body of work of the internal audit function as a whole that the external auditor plans to use” when referring to the nature and extent of audit procedures external auditor needs to perform to determine the adequacy of that work for purposes of the external audit. **[See paragraphs 24, A27 and A31 in Agenda Item 4-B.]**
- (c) It was raised that prohibiting the external auditor from using internal auditors to provide direct assistance to perform procedures that *require judgment* in performing the relevant audit procedure or evaluating the audit evidence is overly stringent. This is because such a requirement would result in the exclusion of using internal auditors to provide direct assistance on almost all audit procedures since most procedures would require some form of judgment to be exercised. The Task Force is in agreement and proposes replacing the phrase with “require *more than limited judgment*” **[See for example, paragraph 31(b) in Agenda Item 4-B.]**

⁷ Description adapted as necessary accordingly to the sentence structure in the relevant paragraphs.

- (d) It was commented that guidance should be included to serve as a reminder that even in jurisdictions where the external auditor is prohibited by law or regulation from obtaining direct assistance from internal auditors, it is relevant for group auditors in those jurisdictions to be aware that component auditors may be in jurisdictions where such practices are allowed and if so, the group auditor may need to address the prohibition in their group engagement team’s letter of engagement. The Task Force is in agreement and proposes guidance accordingly. **[See paragraph A32 in Agenda Item 4-B.]**

Matter for IAASB Consideration

4. The IAASB is asked whether it agrees with the Task Force’s proposals to:
- Clearly distinguish in the scope section of proposed revised ISA 610 the circumstances in which the revised ISA need not be applied;
 - Replacing the term “overall body of work of the internal audit function that the external auditor plans to use” with “the body of work of the internal audit function that the external auditor plans to use in aggregate”; and
 - Clarifying that the external auditor is prohibited from using internal auditors to provide direct assistance to perform procedures that *require more than limited judgment*.
 - Including guidance on direct assistance relevant to the context of a group audit.
12. The Task Force also conducted a consistency check of proposed revised ISA 610 and proposes amendments in certain areas to align the wordings with the remainder of the standard. For example, it is proposed that in the section on using the work of the internal audit function, the phrase “the external auditor’s evaluation of the objectivity of the internal auditors” be updated to “evaluation of the extent to which the internal audit function’s organizational status and relevant policies and procedures support the objectivity of the internal auditors.” **[See for example, paragraphs 19(c), 25(a) and 36 in Agenda Item 4-B.]**

Other Considerations

Effective Date

13. The explanatory memorandum to the ED proposed that revised ISAs 315 and 610 become effective for audits of financial statements for periods ending on or after December 15, 2013. The overwhelming majority of respondents who commented on the proposed effective date expressed that this is appropriate for supporting effective adoption and implementation of the proposed revised ISAs at the national level.⁸ Early application of the revised ISAs would be permitted as provided for under the IAASB’s Preface.

⁸ Some respondents expressed a preference for an earlier effective date, mainly arguing that they do not anticipate the proposals to necessitate a significant change to current practices and therefore earlier implementation is desirable.

14. Accordingly, subject to the IAASB's approval of proposed revised ISAs 315 and 610 at its December 2011 meeting, the Task Force proposes that the final revised standards be effective for audits of financial statements for periods ending on or after December 15, 2013.

Matter for IAASB Consideration

5. The IAASB is asked whether it agrees with the proposed effective date.

Significant Matters Identified by the Task Force

15. In the Task Force’s view, the significant matters the Task Force has identified as a result of its deliberations since the beginning of this project, and the Task Force’s considerations thereon, have all been reflected in the issues papers presented to the IAASB at its meetings. In the Task Force’s view, there are no significant matters discussed within the Task Force on this project that have not been brought to the IAASB’s attention.

Approval, Re-Exposure and Issuance of Final ISA 610 (Revised)

Considerations Relating to the Approval of Propose Revised ISA 610

16. The IESBA is slated to continue its consideration of the matter of direct assistance and the need to amend the IESBA Code at its next meeting in February 2012. As a change to the definition of the “engagement team” seems likely to avoid the perception of a conflict between the ISAs and the IESBA Code regarding the ability of use direct assistance, the IESBA will have to observe due process and in doing so expose the proposed amendment to the definition. The IESBA deliberations are unlikely, therefore, to be completed until later in 2012 at the earliest. The Task Force has engaged with the IESBA throughout the development of proposed revised ISA 610 in particular regarding the matter of direct assistance. IESBA Member and Chair of the IESBA Task Force Robert Franchini has also been an active member on the Task Force since inception. More recently, the IESBA Task Force has provided input to the IAASB on draft revised ISA 610, to which **Agenda Item 4-B** presents responses. The IESBA has also considered these responses at its October 2011 meeting as described in this Issues Paper. Subject to the IAASB’s adoption of the proposal in paragraph 7, the IESBA has expressed that it would be satisfied the safeguards in revised proposed ISA 610 are sound.
17. A further consideration on timing is that direct assistance is being used in practice to varying degrees across jurisdictions (where not prohibited by local law or regulation) without any requirements in the ISAs to guard against over or undue use, nor to require the proposed safeguards to address the threats to objectivity of the internal auditors providing direct assistance . On this basis, there is some urgency to providing external auditors with the appropriate framework on which to base their decisions and procedures relating to engaging internal auditors to provide direct assistance to guide practice today..
18. With consideration for the above factors, the Task Force is of the view that, on balance, it is desirable for the IAASB to consider approving proposed revised ISA 610 in its entirety, even if the issuance of the section on direct assistance is considered to be subject to the

finalization of IESBA’s deliberations and due process. The matter of the manner and timing of issuance of final ISA 610 (Revised) is further considered below.

Matter for IAASB Consideration

6. The IAASB is asked whether it agrees with the Task Force’s recommendation to consider approving proposed revised ISA 610 in its entirety (that is, all proposed requirements and guidance relating to both using the work of the internal audit function and using internal auditors to provide direct assistance.)

Considerations Relating to the Matter of Re-Exposure

19. A summary of the changes made, and a table showing a comparison of requirements and other key paragraphs between the ED and proposed revised ISA 610 is provided in **Agenda Item 4-E**, **Agenda Item 4-F** and **Agenda Item 4-G** present marked-up versions of proposed revised ISAs 315 and 610 showing changes from the ED. In response to comments received on exposure, proposed revised ISA 315 has been strengthened and clarified for the matters raised by respondents. In numerous areas pointed out by respondents, proposed revised ISA 610 has also been strengthened to varying degrees by elevating application material to requirements, or introducing further specific boundaries or necessary conditions and safeguards so as to appropriate frame the external auditor’s judgments and decisions regarding the use of the work of internal auditors and prevent undue or overuse. Additional application guidance has also been introduced in a number of areas in the proposed standard. The IAASB expressed broad support for the September 2011 drafts of revised ISAs 315 and 610.
20. The Task Force is of the view that overall the changes reflected in proposed revised ISAs 315 and 610 are in response to matters raised by respondents to the ED, and do not fundamentally change the principles in the ED or represent other changes of substance.
21. IAASB leadership has had the opportunity for dialogue with regulators and audit inspection bodies regarding draft revised ISA 610 in September 2011.⁹ The general view was that the IAASB had been responsive to the concerns expressed by regulators on the ED and there was broad support for the September 2011 draft of revised ISA 610. Notwithstanding this, some expressed residual unease about the risk that, in the current economic environment, there would be increased pressure on external auditors to use direct assistance to reduce audit fees. Whilst there was a worry about possible misuse and some continue to be concerned about the perceived conflict of direct assistance with independence requirements, it was commented that the safeguards now reflected in the requirements in proposed revised ISA 610 appeared sound.
22. With consideration for the above developments since receiving respondents’ comments on the ED, the Task Force believes that re-exposure of proposed revised ISAs 315 and 610 is not necessary.

⁹ The European Audit Inspection Group (EAIG) and the International Forum of Independent Audit Regulators (IFIAR)

Matter for IAASB Consideration

7. Subject to IAASB’s approval of propose revised ISAs 315 and 610, does the IAASB agree that re-exposure is not necessary?

Considerations Relating to the Issuance of Final ISA 610 (Revised)

23. Subject to the IAASB’s approval of proposed revised ISA 610 in its entirety, following are possible options for the issuance of the final ISA:

Option A: Approve ISA 610 (Revised) in its entirety but defer issuance of the entire ISA while pending for a resolution from the IESBA on direct assistance.

Option B: Issue the parts of ISA 610 (Revised) that relate to using the work of the internal audit function. Hold the ‘closed-off’ parts of ISA 610 (Revised) that relate to direct assistance while pending for a resolution from the IESBA.

24. Under **Option A**, all the requirements and guidance of final ISA 610 (Revised) as approved by the IAASB would be approved but not issued until the IESBA has completed its due process. This option has the benefit of completing the IAASB’s consideration of the revision to ISA 610, which would have the advantage of having approved up-to-date requirements and guidance relating to *both* areas of using the work of the internal audit function and using internal auditors to provide direct assistance, even if not issued publicly.
25. Under **Option B**, the requirements and guidance of final ISA 610 (Revised) as approved by the IAASB relating to using the work of the internal audit function will be submitted to the Public Interest Oversight Board (PIOB) for approval of due process and thereafter issued as final. Those requirements and guidance of the final ISA relating to using internal auditors to provide direct assistance will be ‘closed-off’ but their final issuance held off while pending for a resolution from the IESBA on the matter of direct assistance. **Agenda Item 4-H** presents proposed revised ISA 610 with those parts relating to direct assistance shaded in gray. This option is likely to be considered desirable by some stakeholders, given regulators’ and others’, views that there is a need for greater rigor in the external auditors’ use of the work of the internal auditors in practice.
26. There may be advantages in making the ‘closed-off’ version available on the IAASB website as an unofficial source of reference in the interim. The Task Force also felt that there is merit in sharing the ‘close-off’ document (relating to direct assistance) with the IESBA. This is to inform the IESBA of the IAASB’s position on the matter of direct assistance so that the IESBA has context for its future deliberations and proposals.
27. **Option B** has the benefit of allowing the IAASB to ‘close-off’ on the part of ISA 610 (Revised) relating to direct assistance for issuance after the IESBA has reached a resolution. The Task Force is of the view that this is the more desirable option as it avoids the potential for doubt regarding the validity of the IAASB’s proposals relating to direct assistance as the IESBA continues its deliberation of the topic.

Matters for IAASB Consideration

8. Subject to the IAASB’s approval of propose revised ISA 610, the IAASB is asked whether it agrees with the Task Force’s recommendation to:
- Issue the requirements and guidance of final ISA 610 (Revised) relating to using the work of the internal audit function after approval by the PIOB of due process;
 - ‘Close-off’ the requirements and guidance of final ISA 610 (Revised) relating to using internal auditors to provide direct assistance and hold issuance while pending for a resolution from the IESBA on the matter of direct assistance; and
 - Making the “closed-off” version available on the IAASB website as an unofficial source of reference in the interim and sharing the ‘close-off’ document (relating to direct assistance) with the IESBA.