

## **Using the Work of Internal Auditors— Significant Issues Raised by Respondents on Exposure**

### **Background**

1. Extant ISA 610 was last revised in March 1994.<sup>1</sup> As part of the Clarity project, ISA 610 was redrafted, but not revised, for conformity with the Clarity drafting conventions. Some respondents to the Clarity ED of ISA 610 encouraged the IAASB to consider a more comprehensive revision of the ISA, a view shared by the Representatives of the Consultative Advisory Group (CAG) and the National Auditing Standard Setters. Using the work of internal auditors can be important particularly in audits of financial institutions and other larger entities. There were concerns that the extant ISA failed to reflect developments in the internal auditing environment and national audit practices. The IAASB was also encouraged to remove the current ambiguity in the scope of the extant ISA 610 regarding direct assistance.
2. At the time this revision project was commenced, the IAASB had not received indications that the overall structure and requirements of extant ISA 610 no longer remained sound. Accordingly, it did not anticipate the need for a major overhaul of the ISA. Rather, its aim was to enhance the performance of external auditors by:
  - (a) Enabling better consideration and leveraging, as appropriate, the knowledge and findings of the internal audit function in making risk assessments; and
  - (b) Strengthening the framework for the evaluation and, where appropriate, use of the work of internal auditors in obtaining audit evidence.
3. In July 2010, the IAASB issued an ED proposing revisions to ISAs 315 and 610. The 120-day comment period ended on November 15, 2010. Comment letters have been received from 57 respondents belonging broadly to the groups as shown in **Figure A** on the next page.<sup>2</sup>

### **Main Proposals in the Exposure Draft**

4. The IAASB aimed for a strengthened principles-based approach to using internal audit work. While the objectives of internal audit functions vary, the IAASB recognized that such functions often perform audit procedures—either or both tests of controls or substantive procedures—that are similar to those performed in the external audit. Notwithstanding this, internal auditors are not independent of the entity as is required of the external auditor. Therefore, to be able to use work of the internal audit function in lieu of performing procedures directly, the external auditor needs to have a robust basis for evaluating the structures and mechanisms within the entity that support the internal auditors' objectivity, competence, and quality of work.

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<sup>1</sup> Conforming amendments were made when the IAASB issued the audit risk standards in October 2003.

<sup>2</sup> A list of respondents to the ED is provided in the Appendix to this Issues paper.

**Figure A: Respondents to the Exposure Draft (by main groupings)**

<b>Regulators and Oversight Authorities<sup>3</sup></b>	<b>9</b>
National Auditing Standard Setters	3
Public Sector Organizations	8
Accounting Firms	8
IFAC Member Bodies & Other Professional Bodies	21
Others (including individuals)	8
<b>Total Responses</b>	<b>57</b>

5. On this basis, the ED proposed enhancements to strengthen the basis on which the external auditor leverages the knowledge and findings of the internal audit function as input to the external auditor’s risk assessments, and in making judgments regarding whether and, if so, to what extent to use the work of the internal audit function and the direct assistance of internal auditors. Key proposals are described below:
- Requiring the external auditor to make inquiries of the internal audit function about information of which they are aware that is relevant to identifying and assessing the risks of material misstatement. This is to enable the external auditor to more fully leverage the internal auditor’s understanding of the entity and its environment.
  - Strengthening the requirements to ensure they establish a robust framework for the external auditor’s judgments regarding whether and, if so, the nature and extent of the work of the internal audit function that can justifiably be used on the engagement:
    - First, by evaluating the internal audit function’s objectivity and competence, and determining whether it applies a systematic and disciplined approach;
    - Based on the evaluation, determining the areas where it might be acceptable to use such work, taking into account the degree of objectivity and level of competence of the internal audit function but also, importantly, the extent to which judgment is involved in planning, performing and evaluating that work; and
    - Finally, performing audit procedures to determine the adequacy of the function’s work for purposes of the external audit.
  - Introducing certain baseline requirements to guard against undue or overuse of the work of the internal audit function. In particular, prohibiting the use of such work if the internal

<sup>3</sup> Responses included: (i) Audit Inspection Unit (Financial Reporting Council, UK) & Auditing Practices Board, UK; (ii) Basel Committee on Banking Supervision; (iii) Committee of European Banking Supervisors; (iv) Committee of European Securities Regulators; (v) Canadian Public Accountability Board; (vi) Federal Audit Oversight Authority, Switzerland; (vii) International Organization of Securities Commissions; (viii) Independent Regulatory Board for Auditors, South Africa; and (ix) 14 independent European audit regulators/oversight bodies: Bulgaria, Estonia, Finland, Greece, Lithuania, Luxembourg, Malta, the Netherlands, Norway, Portugal, Slovakia, Slovenia, Spain and Sweden (referred to as 14 AR).

audit function has a low degree of objectivity or low level of competence; and requiring the external auditor to make all significant judgments. In addition, the principle was established that, overall, the external auditor needs to perform sufficient procedures directly to be able to draw reasonable conclusions on which to base the external auditor's opinion on the financial statements.

- Introducing requirements and guidance to acknowledge the use of direct assistance, but at the same time establishing boundaries to limit such use to acceptable circumstances (similar to those when it would be acceptable to use the work of the internal audit function). The ED also, however, explicitly acknowledged that such practice is prohibited by local law or regulation in some jurisdictions. Finally, more rigorous direction, supervision, and review by the external auditor are required in recognition of the fact that internal auditors are not independent of the entity.

## **Overview of Responses**

6. Based on the number of responses alone, there was substantial support for the ED, although some significant issues were also raised. There is significant and widespread support for the requirements and guidance proposed in ISA 315 that were aimed at providing a basis to better leverage the knowledge and understanding of the internal audit function.
7. However, although there was substantial support for the proposals on how external auditors determine whether and to what extent to use the work of an internal audit function, regulators and oversight bodies felt that the requirements in certain areas needed strengthening to varying degrees. There were also mixed views on the desirability of direct assistance. The concerns raised by this stakeholder group on both using the work of the internal audit function and direct assistance are further discussed below.

## **Significant Issues**

### **Using the Work of the Internal Audit Function**

#### *Matters Raised by Respondents*

8. On the whole, there was a substantial amount of support for the ED proposals regarding whether, and if so how, the external auditor might use the work of the internal audit function. However, some respondents in particular, as noted above regulators and oversight bodies, sought to strengthen the proposals in a number of ways.
9. Table 1 (at the end of this section) summarizes the relevant requirements and key premises on which they are based. Although broadly following a similar structure to the extant ISA, the ED introduced both baseline requirements to guard against over or undue use of work of the internal audit function, as well as more robust requirements. In developing the ED, the IAASB did not aim to increase or decrease the use of the work of internal audit functions by external auditors as it was not aware of evidence of widespread problems in practice. The strengthened requirements were intended, however, to ensure more informed judgments were made regarding the use of work of the internal audit function. This in turn could decrease use of such work. Responses from auditors and member bodies generally reflected this view.

### Strengthening Proposals in the ED

10. Regulators and oversight bodies expressed concern, however, that the ED would allow for *significantly* greater use of work of the internal audit function. Some were also concerned that it could result in pressure on external auditors to use more of such work for efficiency reasons. This was seen as problematical. Some cited cases where the extent of use of the work of the internal audit function observed in inspections is not justified in the respondents' view. Concern was also expressed because extensive use of such work could impair the external auditor's independence, or at least the perception of it. A key point for debate is therefore whether the requirements are sufficient to ensure that the use of such work is within acceptable levels.
11. Many regulators and oversight bodies recommended that some of the application material be elevated to requirements. In particular, many thought that doing so would more explicitly limit, if not prohibit, the use of work of the internal audit function in relation to significant risks. Suggestions were varied:
  - (a) Including the assessed risk of material misstatement as a factor to be considered when making judgments regarding where it would be appropriate to use the work of the internal audit function.
  - (b) Elevating to requirements the fact that the higher the assessed risk, the less reliance that can be placed on work of the internal audit function.
  - (c) Introducing the safeguard in the requirements that, where the risk of material misstatement is high (particularly for significant risks), tests must be performed directly by the external auditor, as consideration of work of the internal audit function alone cannot reduce audit risk to an acceptably low level.
  - (d) Prohibiting using the work of the internal audit function in relation to significant risks.
12. Some regulators also asked for greater prescription of the audit procedures the external auditor needs to perform in order to have a sufficiently robust basis to use the internal audit work. Suggestions also involved elevating some of the application material to requirements, or mandating a certain level of reperformance.
13. One of the responses<sup>4</sup> went further. This response expressed the view that because the internal audit function is internal to the entity, by definition, it is an internal control. The response argued that, as a result, the work of internal audit could only be considered, under the audit risk model (as defined in the Glossary and described in ISA 200<sup>5</sup>), to reduce control risk.

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<sup>4</sup> 14 AR

<sup>5</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraphs 13(c) and A32

14. ISA 200 states that audit risk<sup>6</sup> is a function of:
- Inherent risk—the susceptibility to misstatement before considering any controls;
  - Control risk—the risk that a misstatement will not be prevented, or detected and corrected, by the entity’s internal control; and
  - Detection risk—the risk that the auditor’s procedures will not detect a material misstatement that exists.
15. The response noted that the definition of detection risk, as currently drafted, would suggest only the external auditor can reduce detection risk. The implications of this interpretation of how internal audit should be considered within the audit risk model are:
- (a) It would not be appropriate for the external auditor to use the results of any substantive procedures performed by the internal audit function.
  - (b) The external auditor should not leverage the work of the internal audit function when obtaining an understanding of the entity. An example of such work includes walk-throughs of internal controls.
  - (c) Each piece of the function’s work (for example, testing of a particular control activity) must be tested (including reperformance) by the external auditor in order to obtain sufficient appropriate audit evidence regarding the appropriateness to use such work. Some testing directly by the external auditor is also needed.
16. In comparison, the ED reflected a view that, although part of the entity’s monitoring controls, the objective of an entity’s internal audit function is to provide assurance to those charged with governance. It is, therefore, different from other monitoring controls that are designed to detect and correct misstatements, and more akin to the work of another auditor than an internal control. The fact that the function is not independent makes internal audit different from other external auditors, however, and therefore additional safeguards are needed (which the requirements in the ED were intended to provide).
17. With the exception of this response, the comments summarized in paragraphs 10–12, while seeking to strengthen the requirements, did not appear to be challenging the premises underlying the ED (as are described in Table 1). These respondents might be characterized as supporting a threats and safeguards approach to addressing risks arising from the fact that the internal audit function, although objective, is not independent (as defined in the IESBA Code<sup>7</sup>). While the Task Force will continue to deliberate the various views put forward, it nevertheless notes that the approach described in paragraphs 13–16, if adopted, would result in the ISA permitting less use of the work of internal audit, and requiring more work effort by the external auditor to support the use of such work, when compared to any other equivalent national auditing standards. It would result in significant changes to practice and, in some cases, result in a significant increase in audit effort. It is unclear at

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<sup>6</sup> Risk that the auditor expresses an inappropriate audit opinion when the financial statements are material misstated.

<sup>7</sup> International Ethics Standards Board for Accountants *Code of Ethics for Professional Accountants* (IESBA Code)

this stage whether the advantages of doing so would outweigh other possible implications and the IAASB's views on this would be useful to the Task Force's deliberations.

**Table 1: Overview of Proposals on Use of Work of Internal Audit Function (IAF)**

<p><i>Using the IAF's Work and the External Auditor's Responsibilities</i></p> <ul style="list-style-type: none"><li>• Where the right conditions exist the IAF, although not independent of the entity as required of external auditors, can perform high quality assurance work (that is, audit procedures such as tests of controls or substantive-testing) with an objective state of mind. External auditors may use such work, within acceptable boundaries, in lieu of performing those procedures directly themselves.</li><li>• To reduce the risk that IAF's work does not provide evidence that is adequate for purposes of the engagement, the external auditor needs a robust framework, supported by evidence, for determining the areas where IAF's work may be used, and for assessing the quality of such work. Further, because the external auditor has sole responsibility for the audit opinion, the external auditor is responsible for:<ul style="list-style-type: none"><li>○ The overall audit strategy and audit plan (including, the risk assessment and design of the responses to assessed risks), and subsequently determining the relevance of IAF's work;</li><li>○ Significant judgments in the audit (for example, risks of material misstatements, sufficiency of tests performed, appropriateness of management's use of the going concern assumption, evaluation of significant accounting estimates, adequacy of disclosures in financial statements and other matters affecting the auditor's report); and</li><li>○ Performing sufficient procedures directly so as to draw reasonable conclusions on which to base the audit opinion (a safeguard on the overall extent of IAF's work used).</li></ul></li></ul> <p><i>Determining Planned Use of IAF's Work</i></p> <ul style="list-style-type: none"><li>• The quality of the IAF determines the external auditor's use of IAF's work:<ul style="list-style-type: none"><li>○ If the function has a low degree of objectivity or low level of competence, the risk that the work will not be adequate for the external auditor's purposes is too high and, therefore, IAF's work should not be used in these circumstances (a baseline intended as a safeguard against undue use).</li><li>○ If the function does not have its own quality control (part of a systematic and disciplined approach), the approach in the ED is not appropriate. The external auditor might be able to use the IAF's work, but as a control activity, and the effective operation of that control need to be tested in accordance with ISA 330.<sup>8</sup></li><li>○ In other circumstances, the degree of objectivity and level of competence influence both where IAF's work can be used, and the nature and extent of audit procedures needed for concluding its adequacy for purposes of the audit.</li></ul></li><li>• The amount of <i>judgment</i> involved in planning and performing the audit procedures, and in evaluating the results, is the other key determinant in making these decisions. The higher the risk of material misstatement, the more judgment involved in planning, performing and evaluating the audit procedures to respond to that risk. Therefore, although IAF's work involving limited judgment can contribute to the body of evidence in relation to significant risks, it is unlikely to constitute a significant portion of the evidence needed, and therefore the extent to which it is acceptable to use IAF's work in relation to significant risks is limited. On the other hand, even in</li></ul>
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<sup>8</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

relation to lower risks, if the procedure involves significant judgment, the external auditor should not use IAF's work.

*Supporting the External Auditor's Use of IAF's Work*

- In order to have a sufficient basis to support the use of IAF's work in lieu of performing that work directly, the external auditor needs to perform audit procedures (which ordinarily include some reperformance) on that work to determine its adequacy for purposes of the audit engagement. Because the IAF operates with its own quality control, the external auditor performs sufficient procedures on the *body* of IAF's work the external auditor plans to use so as to determine whether:
  - Such work was properly planned, performed, supervised, reviewed and documented;
  - Adequate audit evidence has been obtained; and
  - Conclusions reached are appropriate and any IAF reports are consistent with the results of the work performed. The external auditor is required to read the IAF reports related to the work the external auditor plans to use.

These audit procedures provide evidence to support both the external auditor's original evaluation of the function and the quality of the work being used for purposes of the engagement.

**Matters for IAASB's Consideration**

1. The ED had focused on principles intended to guide the external auditor's judgments regarding the use of the work of the internal audit function, with the application material providing guidance on the application of those principles. Based on the Task Force's preliminary analysis of comments, the key issue is whether the ED sufficiently ensures that the use of such work is within acceptable levels. There is a balance to be achieved between an approach designed to ensure that the risk of an excessive use of the work of the internal audit function is minimized, and one that may be perceived as being so restrictive that general use of such work is inadvertently discouraged and appropriate cooperation between external and internal auditors in the interests of audit quality is undermined.

The IAASB is asked to share its reactions to the comments raised by respondents as described, in particular whether clearer bright-lines that narrow the boundaries of the external auditor's judgments should be established (for example, restricting the use of internal audit work to areas of low risk, or prohibiting using work of the internal audit function in relation to significant risks.) In this regard, what are the pros and cons of the various alternatives?

**Direct Assistance**

*Matters Raised by Respondents*

18. Table 2 (at the end of this section) summarizes the requirements relating to direct assistance in the ED and key premises on which they are based. Respondents' views regarding whether the ISAs should address the matter of direct assistance were polarized. This is consistent with the views raised with the IAASB during the development of the ED.

19. Whether supporting or not supporting the use of direct assistance, most respondents agreed that it is necessary to address this matter in the ISAs so as to remove ambiguity regarding whether or not the external auditor can use direct assistance provided by internal auditors, and to provide appropriate direction on circumstances when it is appropriate to use that work and the audit procedures that should be performed. These respondents were of the view that remaining silent on this matter in the ISAs is contrary to promoting consistent audit practices globally and therefore detrimental to audit quality.
20. Many respondents supported the ability for the external auditor to obtain direct assistance of internal auditors. They argued that use of the work of the internal audit function is not inherently different from direct assistance, therefore, there is no conceptual difference for permitting one but not the other. Of these, most agreed that the ED provided a robust judgment-based framework for ensuring direct assistance of internal auditors is only obtained under appropriate circumstances, and that external auditors can appropriately tailor the level of direction, supervision and review.
21. Other respondents disagreed. This is mostly because they fundamentally disagree that such practices should be permitted. The respondents were of the view that, if direct assistance is addressed in the ISAs, it may inadvertently be perceived as a positive signal about the desirability of such practices in all circumstances. They were concerned the external auditor may be subject to undue pressure from management to obtain the direct assistance of internal auditors with the objective of lowering audit fees. These respondents noted the following:
  - Direct assistance blurs the distinction between the external and the internal auditors. Since internal auditors are employees of the entity, such assistance could be viewed as compromising the external auditor's independence, at least in appearance. The IESBA Code requires the external auditor to be independent. Internal auditors providing direct assistance on the engagement seems incompatible with this requirement. In particular, some respondents noted that internal auditors providing direct assistance on the engagement would be, in effect, acting as members of the engagement team. If so, this is inconsistent with the definition of engagement team in the IESBA Code and its requirement for members of the engagement team to be independent. Many noted that if this is not the case, clarification is needed in the IESBA Code and the rationale for the conclusion explained.
  - Because internal auditors are employees of the entity, some felt they are ultimately accountable to management or those charged with governance even in the case where they are "seconded" to the external auditor to provide direct assistance on the engagement. Thus, confidentiality could be at risk, which could threaten the effectiveness of the external audit.
22. A number of respondents, while accepting that the possibility of using direct assistance should be allowed (if only because it is accepted practice in some countries), thought that additional safeguards need to be put in place to address some of the risks identified above. Some commented, for example, that direct assistance should only be obtained under a limited range of circumstances and that boundaries should be clearly outlined. For example, some felt that direct assistance should be prohibited in areas of significant/high

risks, while others were of the view that such practices should only be permitted in areas of low risk. Respondents added that, in any case, the measures to guard against undue use of internal auditors need to be strengthened. For example, some suggested the extent of the external auditor's involvement should be greater where the assessed risk is higher. The Task Force noted that the issues raised by respondents have implications for both proposed revised ISA 610 and the IESBA Code.

**Table 2: Overview of Proposals on Direct Assistance**

<p><i>Obtaining Direct Assistance from Internal Auditors and the External Auditor's Responsibilities</i></p> <ul style="list-style-type: none"><li>• With appropriate direction, supervision and review of the external auditor, internal auditors, although not independent of the entity as required of external auditors, can, in defined limited circumstances and if sufficiently competent and objective, provide assistance directly to external auditors by carrying out audit procedures on the engagement.</li><li>• The decisions of whether and if so, to what extent to obtain direct assistance from internal auditors, if permitted at all, remain <i>solely</i> those of the external auditor. In some jurisdictions, the external auditor may be prohibited by law or regulation from obtaining direct assistance.</li><li>• There is a spectrum between direct assistance and using the work of the internal audit function, and drawing lines between seen as somewhat arbitrary. As a result, to a large extent, the boundaries defining the circumstances when it would be appropriate to use direct assistance are similar to those for using the work of the internal audit function, as described in Table 1. However, the consideration of objectivity and competence is at the level of the individual, rather than the function as a whole, and any self-review threat must also be taken into account.</li></ul> <p><i>Determining Work to be Assigned to Individual Internal Auditors</i></p> <ul style="list-style-type: none"><li>• The level of competence and degree of objectivity of the internal auditor influences the external auditor's decision to obtain the direct assistance from internal auditors:<ul style="list-style-type: none"><li>○ If an internal auditor has a low degree of objectivity or low level of competence, the risk that it is inappropriate to obtain the direct assistance of the internal auditor is too high and, therefore, direct assistance should not be obtained from the internal auditor in these circumstances (a baseline intended as a safeguard against undue use).</li><li>○ In other circumstances, the degree of objectivity and level of competence influence both the work that may be assigned to internal auditors and the amount of direction, supervision and review that is appropriate in the circumstances.</li></ul></li><li>• The amount of <i>judgment</i> involved in planning and performing the audit procedures, and in evaluating the results, is the other key determinant in making these decisions. The higher the risk of material misstatement, the more judgment involved in planning, performing and evaluating the audit procedures to respond to that risk. Therefore, although internal auditors may perform procedures involving limited judgment and such work can contribute to the body of evidence in relation to significant risks, it is unlikely to constitute a significant portion of the evidence needed, and therefore the extent to which it is acceptable to obtain the direct assistance of internal auditors in relation to significant risks is limited. On the other hand, even in relation to lower risks, if the procedure involves significant judgment, the external auditor should not obtain the direct assistance of internal auditors.</li><li>• Additional safeguards on using direct assistance in inappropriate areas include that assistance from internal auditors should not be obtained:<ul style="list-style-type: none"><li>○ Whereby the internal auditors make significant judgments in the audit engagement; or</li></ul></li></ul>
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- To perform procedures to determine whether the work of the internal audit function can be used for purposes of the audit or to provide a sufficient basis to support the external auditor's use of the work of the internal audit function, as this would create a self-review threat for the internal auditors.

*Supporting the External Auditor's Use of Direct Assistance from Internal Auditors*

- To recognize that internal auditors are not independent of the entity, the direction, supervision or review by the external auditor of the audit procedures performed by the internal auditors is ordinarily more extensive than if members of the engagement team had performed the work. In making such determinations, the external auditor takes into consideration the external auditor's evaluation of the degree of objectivity and level of competence of, and the nature and extent of audit procedures to be performed by, the internal auditors. In reviewing the work performed by internal auditors, the external auditor also considers whether the evidence obtained is sufficient and appropriate in the circumstances, and that it supports the conclusions reached.

**Matters for IAASB's Consideration**

2. The IAASB is asked for its reactions to the issues raised by respondents as described, in particular, does the IAASB think that direct assistance: (a) should be prohibited; (b) allowed within the boundaries proposed in the ED; or (c) allowed but with further restrictions as to when it would be appropriate to obtain direct assistance?
3. Does the IAASB think that the requirements regarding the external auditor's work effort in relation to work performed by internal auditors need to be strengthened?

**Balance between Requirements and Application and Other Explanatory Material**

*Matters Raised by Respondents*

23. A common theme evident in a number of responses is that the respondents felt certain application material should either be elevated to requirements, or further specific criteria or necessary conditions needed to be introduced so as to narrow the boundaries within which the external auditor forms judgments and makes decisions regarding the use of the work of internal auditors. For example, a few respondents raised certain examples of procedures in the application material that should be stated as requirements. Table 3 (at the end of this section) provides a summary of the key areas noted by respondents.
24. The Clarity Project saw the application of new drafting conventions to all ISAs to reflect the new conventions and matters of clarity generally. The proposed revised ISA 610 conforms to these drafting conventions. In particular, ISA 200 explains that the requirements of the ISAs are designed to enable the auditor to achieve the objectives specified in the ISAs. Auditors are expected to comply with the requirements unless the entire ISA is not relevant, or the requirement is not relevant because it is conditional and the condition does not exist.
25. As part of the Clarity Project, the IAASB agreed that it would determine the requirements of a Standard as follows:
  - The requirement is necessary to achieve the objective stated in the Standard;

- The requirement is expected to be applicable in virtually all engagements to which the Standard is relevant; and
- The objective stated in the Standard is unlikely to have been met by the requirements of other Standards.

In determining the requirements of a Standard, the IAASB considered whether the requirements are proportionate to the importance of the subject matter of the Standard in relation to the overall objective of the engagement.<sup>9</sup>

26. On the other hand, the authority of application and other explanatory material is outlined in ISA 200 as follows:<sup>10</sup>

Paragraph 19: The auditor shall have an understanding of the entire text of an ISA, including its application and other explanatory material, to understand its objectives and to apply its requirements properly.

Paragraph A59: Where necessary, the application and other explanatory material provides further explanation of the requirements of an ISA and guidance for carrying them out. In particular, it may:

- Explain more precisely what a requirement means or is intended to cover.
- Include examples of procedures that may be appropriate in the circumstances.

While such guidance does not in itself impose a requirement, it is relevant to the proper application of the requirements of an ISA. The application and other explanatory material may also provide background information on matters addressed in an ISA.

27. Table 3 shows the range of suggestions from respondents to move application material to requirements. While each suggestion would be considered on its own merits as part of due process, the Task Force reflected on the extent to which respondents collectively suggested elevating application material to requirements. The Task Force envisages if this was to be the case the application material remaining is likely to be minimal.
28. The Task Force is cognizant that IAASB was mindful of the need to keep the ISAs principles-based while also ensuring their clarity, completeness and enforceability. As ISA 610 is the first clarified ISA to be revised, the Task Force anticipates that decisions taken henceforth will likely be reference points for future revisions. Attaining the right balance is therefore of crucial importance in this case.

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<sup>9</sup> These guidelines, which are intended only to assist the IAASB in appropriately and consistently determining requirements, may be refined as further experience is gained.

<sup>10</sup> Further in the Basis for Conclusion for clarified ISA 200, the following explanations are relevant:

- The IAASB is of the view that ISA 200 (Revised and Redrafted) must make clear the authority of the application and other explanatory material in the ISAs and dispel any notion that consideration of such material is entirely optional; and
- The application material may explain more precisely what a requirement means or is intended to cover, and may include examples of procedures that may be appropriate in the circumstances. This is an important clarification in terms of those circumstances where application material elaborates on a requirement but such material is not placed as part of a requirement itself in order to maintain its clarity.

**Table 3: Application Material that Respondents Felt Should Be Elevated to Requirements**

<i>Determining Whether to Use IAF's Work</i>	
¶A6	It was suggested that some of the factors to be considered by the external auditor when determining the IAF's degree of objectivity (for example, organizational status and reporting relationship in the entity) and level of competence (for example, technical training and proficiency, and professional memberships) are necessary criteria and, therefore, should be specified as requirements.
¶A7	It was suggested that the principle in the application material – the higher the degree of objectivity and level of competence [of the IAF], the more likely the external auditor may make use of the work of the IAF and in more areas – needs to be strengthened. These respondents felt specific criteria and minimum conditions are required to guide the external auditor's consideration of the IAF's objectivity and competence.
<i>Determining Planned Use of IAF's Work</i>	
¶A12– ¶A13	It was suggested that the factor described in the application material – the external auditor's assessments of the risk of material misstatement – should be a necessary consideration in the external auditor's decisions regarding use of the IAF's work. In particular, some suggested that the principle, “the higher the assessed risks of material misstatement, the more persuasive the audit evidence required by the external auditor will need to be, and, therefore, the more likely it will be that the external auditor will need to perform more of the work directly,” should be mandatory.  Further, some respondents also noted that the external auditor should be required to perform procedures directly in areas of significant risks.
<i>Using Work of the IAF</i>	
¶A17	It was suggested that inclusion in the application material of examples of IAF's work that may be used by the external auditor is inappropriate because it may be perceived that such IAF's work is appropriately used by the external auditor <i>in all circumstances</i> without further consideration.
¶A18	It was suggested that it be mandatory for the external auditor to perform one or more of the procedures listed as examples in the application material for purposes of appraising the quality of the work of and conclusions reached by the IAF.
¶A20	It was suggested that the principle in the application material regarding the external auditor's determination of whether and the extent to reperform the IAF's work should be elevated to a requirement (that is, the external auditor should be required to test the IAF's work, including through reperformance, in all cases regardless of circumstances).
¶A21	It was suggested that in determining adequacy of the IAF's work, the external auditor should be required to evaluate processes and systems used for tracking and following up on IAF's findings.
<i>Direct Assistance</i>	
¶A22– ¶A28	Overall it was suggested that the application material needs to be strengthened by inclusion of specific criteria, and minimum conditions and procedures to prevent undue use of direct assistance of internal auditors by the external auditor. For example, it was suggested that direct assistance should be prohibited in areas of high/significant risks while some felt it should be restricted to areas of lower risk.  Some also felt the principle regarding the external auditor's direction, supervision and

	review of the audit procedures performed by internal auditors being more extensive than if members of the engagement team performed the work should apply <i>in all circumstances</i> .
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**Matter for IAASB's Consideration**

4. The IAASB is asked for its views regarding the advantages and drawbacks of elevating application material to requirements.

## Appendix

### List of Respondents to the Exposure Draft

#	Abbreviation	Respondent (Total)
<b>Regulators and Oversight Authorities (9)</b>		
1.	14 AR	14 Independent European Regulators
2.	AIU & APB	Audit Inspection Unit (Financial Reporting Council, United Kingdom) & Auditing Practices Board, United Kingdom
3.	BCBS	Basel Committee on Banking Supervision
4.	CEBS	Committee of European Banking Supervisors
5.	CESR	Committee of European Securities Regulators
6.	CPAB	Canadian Public Accountability Board
7.	FAOA	Federal Audit Oversight Authority (Switzerland)
8.	IOSCO	International Organization of Securities Commissions
9.	IRBA	Independent Regulatory Board for Auditors (South Africa)
<b>National Auditing Standard Setters (3)<sup>11</sup></b>		
10.	AuAASB	Australian Auditing and Assurance Standards Board
11.	CAASB	Canadian Auditing and Assurance Standards Board
12.	NZICA	New Zealand Institute of Chartered Accountants (Professional Standards Board)
<b>Public Sector Organizations (8)</b>		
13.	AAA	American Accounting Association (Auditing Standards Committee)
14.	ACAG	Australasian Council of Auditors-General
15.	DGRV	Deutscher Genossenschafts- und Raiffeisenverband e. V. (German Cooperative and Raiffeisen Confederation)
16.	GAO	United States Government Accountability Office
17.	MOFBC	Ministry of Finance British Columbia
18.	PAS	Provincial Auditor Saskatchewan
19.	SNAO	Swedish National Audit Office
20.	WAO	Wales Audit Office
<b>Accounting Firms (8)</b>		
21.	BDO	BDO Global Coordination B.V.
22.	DTT	Deloitte Touche Tohmatsu
23.	EYG	Ernst & Young Global
24.	GT	Grant Thornton International
25.	KPMG	KPMG
26.	LS	Levi & Sinclair
27.	PwC	PricewaterhouseCoopers
28.	RSM	RSM International Limited

<sup>11</sup> For the purpose of this table only, the joint response letter from the AIU & APB has been listed only once under the “Regulators and Oversight Authorities” category.

<b>IFAC Member Bodies &amp; Other Professional Bodies (21)</b>		
29.	ACCA	Association of Chartered Certified Accountants
30.	AICPA	American Institute of Certified Public Accountants
31.	CIPFA	Chartered Institute of Public Finance and Accountancy
32.	CNCC & CSOEC	Compagnie Nationale des Commissaires aux Comptes & Conseil Supérieur de l'Ordre des Experts-Comptables
33.	DnR	Norwegian Institute of Public Accountants (Revisorforeningen)
34.	FARSRS	Svenska Revisorsamfundet SRS
35.	FEE	Federation des Experts Comptables Europeens
36.	FSR	Foreningen af Statsautoriserede Revisorer
37.	HKICPA	Hong Kong Institute of Certified Public Accountants
38.	ICAEW	Institute of Chartered Accountants in England and Wales
39.	ICAI	Institute of Chartered Accountants in Ireland
40.	ICPAK	Institute of Certified Public Accountants of Kenya
41.	ICPAS	Institute of Certified Public Accountants of Singapore
42.	IDW	Institut der Wirtschaftsprüfer
43.	IIA	Institute of Internal Auditors
44.	ISACA	Information Systems Audit and Control Association
45.	JICPA	Japanese Institute of Certified Public Accountants
46.	MIA	Malaysian Institute of Accountants
47.	NIVRA	Koninklijk Nederlands Instituut van Registeraccountants
48.	NYSSCPA	New York State Society of Certified Public Accountants
49.	SAICA	South African Institute of Chartered Accountants
<b>Others (including individuals) (8)</b>		
50.	C. Barnard	Chris Barnard
51.	D. Juvenal	Denise Silva Ferreira Juvenal
52.	H. Jaegtnes	Harald Jaegtnes
53.	HC	Hunter College
54.	J. Maresca	Joseph Maresca
55.	P. Angulo	Paulino Angulo
56.	R. Ramchurun	Rajnish Ramchurun
57.	R. Mahadevan	Ramachandran Mahadevan