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Auditing Standard ASA 610

Using the Work of Internal Auditors

Issued by the **Auditing and Assurance Standards Board**

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Auditing and Assurance Standards Board

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Contact Details

Auditing and Assurance Standards Board Phone: (03) 8080 7400
Level 7 Fax: (03) 8080 7450
600 Bourke Street E-mail: enquiries@auasb.gov.au
Melbourne Victoria 3000
AUSTRALIA

Postal Address:
PO Box 204
Collins Street West
Melbourne Victoria 8007
AUSTRALIA

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PREFACE

Reasons for Issuing Auditing Standard ASA 610 *Using the Work of Internal Auditors*

The Auditing and Assurance Standards Board (AUASB) issues Auditing Standard ASA 610 *Using the Work of Internal Auditors* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Australian Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the International Auditing and Assurance Standards Board (IAASB) for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

Main Features

This Auditing Standard establishes Requirements and provides Application and Other Explanatory Material regarding the auditor's responsibilities regarding the work of internal auditors when it is relevant to the external auditor.

This Auditing Standard:

- (a) establishes the relationship between internal audit function and external audit;
- (b) requires the external auditor to assess the internal audit function, and to determine the extent of planned reliance on the work performed; and
- (c) requires the external auditor to document the conclusions reached on the work of internal audit, and the audit procedures performed by the external auditor on that work.

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AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 610 *Using the Work of Internal Auditors* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

This Auditing Standard is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing, on or after 1 January 2010, are to be understood, interpreted and applied. This Auditing Standard is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of the Audit in Accordance with Australian Auditing Standards*.

Dated: 27 October 2009

M H Kelsall
Chairman - AUASB

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Application

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
 - (b) an audit of a financial report or a complete set of financial statements, for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

Operative Date

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 1 January 2010.

Introduction

Scope of this Auditing Standard

1. This Auditing Standard deals with the auditor's responsibilities relating to the work of internal auditors when the external auditor has determined, in accordance with ASA 315,¹ that the internal audit function is likely to be relevant to the audit. (Ref: Para. A1-A2)
2. This Auditing Standard does not deal with instances when individual internal auditors provide direct assistance to the external auditor in carrying out audit procedures.

¹ See ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 23.

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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. While the objectives of the internal audit function and the external auditor are different, some of the ways in which the internal audit function and the external auditor achieve their respective objectives may be similar. (Ref: Para. A3)
4. Irrespective of the degree of autonomy and objectivity of the internal audit function, such function is not independent of the entity as is required of the external auditor when expressing an opinion on the financial report. 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 auditors.

Effective Date

5. [Deleted by the AUASB. Refer Aus 0.3]

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 audit are:
 - (a) To determine whether, and to what extent, to use specific work of the internal auditors; and
 - (b) If using the specific work of the internal auditors, to determine whether that work is adequate for the purposes of the audit.

Definitions

7. For purposes of the Australian Auditing Standards, the following terms have the meanings attributed below:
 - (a) Internal audit function means an appraisal activity established or provided as a service to the entity. Its functions include, amongst other things, examining, evaluating and monitoring the adequacy and effectiveness of internal control.

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- (b) Internal auditors means those individuals who perform the activities of the internal audit function. Internal auditors may belong to an internal audit department or equivalent function.

Requirements

Determining Whether and to What Extent to Use the Work of the Internal Auditors

- 8. The external auditor shall determine:
 - (a) Whether the work of the internal auditors is likely to be adequate for purposes of the audit; and
 - (b) If so, the planned effect of the work of the internal auditors on the nature, timing or extent of the external auditor's procedures.
- 9. In determining whether the work of the internal auditors is likely to be adequate for purposes of the audit, the external auditor shall evaluate:
 - (a) The objectivity of the internal audit function;
 - (b) The technical competence of the internal auditors;
 - (c) Whether the work of the internal auditors is likely to be carried out with due professional care; and
 - (d) Whether there is likely to be effective communication between the internal auditors and the external auditor.
(Ref: Para. A4)
- 10. In determining the planned effect of the work of the internal auditors on the nature, timing or extent of the external auditor's procedures, the external auditor shall consider:
 - (a) The nature and scope of specific work performed, or to be performed, by the internal auditors;
 - (b) The assessed risks of material misstatement at the assertion level for particular classes of transactions, account balances, and disclosures; and

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- (c) The degree of subjectivity involved in the evaluation of the audit evidence gathered by the internal auditors in support of the relevant assertions. (Ref: Para. A5)

Using Specific Work of the Internal Auditors

- 11. In order for the external auditor to use specific work of the internal auditors, the external auditor shall evaluate and perform audit procedures on that work to determine its adequacy for the external auditor's purposes. (Ref: Para. A6)
- 12. To determine the adequacy of specific work performed by the internal auditors for the external auditor's purposes, the external auditor shall evaluate whether:
 - (a) The work was performed by internal auditors having adequate technical training and proficiency;
 - (b) The work was properly supervised, reviewed and documented;
 - (c) Adequate audit evidence has been obtained to enable the internal auditors to draw reasonable conclusions;
 - (d) Conclusions reached are appropriate in the circumstances and any reports prepared by the internal auditors are consistent with the results of the work performed; and
 - (e) Any exceptions or unusual matters disclosed by the internal auditors are properly resolved.

Documentation

- 13. If the external auditor uses specific work of the internal auditors, the external auditor shall include in the audit documentation the conclusions reached regarding the evaluation of the adequacy of the work of the internal auditors, and the audit procedures performed by the external auditor on that work, in accordance with paragraph 11 of this Auditing Standard.²

* * *

² See ASA 230 *Audit Documentation*, paragraphs 8-11 and paragraph A6.

Application and Other Explanatory Material

Scope of this Auditing Standard (Ref: Para. 1)

- A1. As described in ASA 315,³ 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 auditors to modify the nature or timing, or reduce the extent, of audit procedures to be performed.
- A2. Carrying out procedures in accordance with this Auditing Standard 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. Similarly, the external auditor may decide not to otherwise use the work of the internal auditors to affect the nature, timing or extent of the external auditor's procedures. In such circumstances, the external auditor's further application of this Auditing Standard may not be necessary.

Objectives of the Internal Audit Function (Ref: Para. 3)

- 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:
- Monitoring of internal control. The internal audit function may be assigned specific responsibility for reviewing controls, monitoring their operation and recommending improvements thereto.
 - 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 enquiry 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

³ See ASA 315, paragraph A101.

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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.
- Risk management. The internal audit function may assist the organisation by identifying and evaluating significant exposures to risk and contributing to the improvement of risk management and control systems.
- 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 organisation and effectiveness of communication among those charged with governance, external and internal auditors, and management.

Determining Whether and to What Extent to Use the Work of the Internal Auditors

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

- A4. Factors that may affect the external auditor's determination of whether the work of the internal auditors is likely to be adequate for the purposes of the audit include:

Objectivity

- The status of the internal audit function within the entity and the effect such status has on the ability of the internal auditors to be objective.
- Whether the internal audit function reports to those charged with governance or an officer with appropriate authority, and whether the internal auditors have direct access to those charged with governance.
- Whether the internal auditors are free of any conflicting responsibilities.

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- 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.
- Whether, and to what extent, management acts on the recommendations of the internal audit function, and how such action is evidenced.

Technical competence

- Whether the internal auditors are members of relevant professional bodies.
- Whether the internal auditors have adequate technical training and proficiency as internal auditors.
- Whether there are established policies for hiring and training internal auditors.

Due professional care

- Whether activities of the internal audit function are properly planned, supervised, reviewed and documented.
- The existence and adequacy of audit manuals or other similar documents, work programs and internal audit documentation.

Communication

Communication between the external auditor and the internal auditors may be most effective when the internal auditors are free to communicate openly with the external auditors, and:

- Meetings are held 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 auditors when such matters may affect the work of the external auditor; and

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- The external auditor informs the internal auditors of any significant matters that may affect the internal audit function.

Aus A4.1 An illustrative example questionnaire to assist in obtaining an understanding and making a preliminary assessment of the internal audit function is included in Appendix 1.

Planned Effect of the Work of the Internal Auditors on the Nature, Timing or Extent of the External Auditor's Procedures (Ref: Para. 10)

A5. Where the work of the internal auditors is to be a factor in determining the nature, timing or extent of the external auditor's procedures, it may be useful to agree in advance the following matters with the internal auditors:

- The timing of such work;
- The extent of audit coverage;
- Materiality for the financial report 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.

Using Specific Work of the Internal Auditors (Ref: Para. 11)

A6. The nature, timing and extent of the audit procedures performed on specific work of the internal auditors will depend on the external auditor's assessment of the risk of material misstatement, the evaluation of the internal audit function, and the evaluation of the specific work of the internal auditors. Such audit procedures may include:

- Examination of items already examined by the internal auditors;
- Examination of other similar items; and

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- Observation of procedures performed by the internal auditors.

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Conformity with International Standards on Auditing

This Auditing Standard conforms with International Standard on Auditing ISA 610 *Using the Work of Internal Auditors*, issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this Auditing Standard (and do not appear in the text of the equivalent ISA) are identified with the prefix “Aus”.

Compliance with this Auditing Standard enables compliance with ISA 610.

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Appendix 1

(Ref: Para. Aus A4.1)

[Aus] Illustrative Example Questionnaire – Obtaining an understanding of and making a preliminary assessment of the internal audit function

The following illustrative questionnaire provides a broad range of questions related to obtaining an understanding of, and making a preliminary assessment of, the internal audit function. Not all questions are necessarily relevant to every audit or review engagement, and the questionnaire is not intended to be exhaustive.

The answers to the following questions may assist in obtaining an understanding and making a preliminary assessment of the internal audit function.

Questionnaire		Yes	No	N/A
<i>Organisational Status</i>				
1.	Who does the head of internal audit report to, and is this appropriate?			
2.	Do those charged with governance and/or management's view of internal audit appear not to limit internal audit?			
3.	Is the head of internal audit free from:			
	(a) The influences of operational management which would impact on the head of internal audit's objectivity?			
	(b) Any operating responsibility?			

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	Questionnaire	Yes	No	N/A
4.	Does the head of internal audit have:			
	(a) Direct access (as required) to:			
	(i) The governing body?			
	(ii) The chairman of the governing body?			
	(iii) The chief executive?			
	(iv) The audit committee (if applicable)?			
	(b) Freedom/flexibility from direct instruction from those charged with governance as to the scope and direction of audit activity?			
	(c) Freedom to communicate with the external auditor on relevant matters on a regular basis?			

(If the answer to any of questions 3(a) or (b) or 4(a) to (c) is negative, describe how objectivity is achieved and maintained).

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Questionnaire		Yes	No	N/A
<i>Scope of Function</i>				
5.	(a)	Does internal audit regularly examine the controls over all significant accounting operations which affect the financial report? (If not, describe the areas not covered by internal audit).		
	(b)	Does the head of internal audit have flexibility to act using discretion on suggestions made by the external auditor as to areas to be included in the internal audit program?		
	(c)	Do internal audit reports and working papers indicate that internal audit applies a professional approach to audit assignments?		
	(d)	Has past experience shown that internal audit has been able to complete previous internal audit programs?		
6.	(a)	(i)	Do internal audit reports identify weaknesses/problems and contain recommendations for improvements?	
		(ii)	Are such reports addressed to the appropriate level of those charged with governance who are capable and able to achieve satisfactory audit results?	

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	Questionnaire	Yes	No	N/A
	(iii) Are copies of all reports forwarded to: <ul style="list-style-type: none">• the chairman of the governing body or chief executive? and/or• the audit committee (if applicable)?			
	(b) Are copies of all reports relating to accounting and associated records available to the external auditor? (If 6(a) or (b) are answered in the negative, describe the method of reporting).			
7.	(a) Is there evidence, for example in the minutes of governing body and/or audit committee meetings, that internal audit reports have been considered?			
	(b) Is there evidence that a person of senior authority, for example the chief executive, has taken action to see that internal audit recommendations are properly considered? (If the answer to 7(a) or (b) is negative, describe the process for ensuring that consideration is given to internal audit reports and recommendations).			

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Questionnaire		Yes	No	N/A
<i>Technical Competence</i>				
8.	Is the head of internal audit a professionally trained auditor? (If not, describe qualifications by training and by experience for the position held).			
9.	(a) Do the entity's hiring and/or internal promotion/transfer policies for internal audit require: (i) Tertiary qualifications? (ii) Formal professional qualifications? (iii) Previous internal audit experience?			
	(b) Does the entity provide internal audit staff with the opportunity to maintain professional competence, for example by encouraging: (i) Internal staff training? (ii) Attendance at external training and professional courses?			
10.	Do assignments undertaken reflect that those charged with governance have confidence in internal audit, and provide experience in audit related work?			
11.	Do the reports prepared by internal audit reflect a clear understanding of the audit task undertaken and the expression of valid conclusions?			

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Questionnaire		Yes	No	N/A
12.	If the entity has a large internal audit function, does it contain an adequate proportion of professionally trained/experienced auditors?			
<i>Due Professional Care</i>				
13.	(a) Does internal audit have a procedures manual clearly describing staff responsibilities and audit procedures concerning documentation?			
	(b) Is the work of internal audit controlled and supervised through managers or supervisors responsible to the head of the department, each of whom supervises the work of staff allocated?			
14.	(a) Does internal audit use written audit programs prepared in conformity with appropriate professional standards and practice?			
	(b) Are comprehensive audit programs prepared for all internal audit engagements?			
15.	(a) Does internal audit prepare working papers to record work done and conclusions drawn?			
	(b) Are the working papers reviewed by appropriate internal audit staff?			

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Questionnaire

Yes No N/A

16. Where the internal audit activity is co-sourced or fully outsourced, is the relationship between the entity and the third party provider appropriate and well managed?

(If the answer to any of questions 13 to 16 is negative describe the process used for planning, supervising, reviewing and documenting internal audit work).

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