



Internal Audit - Impact of Direct Assistance Prohibition on Group Audits

May 2015

Purpose of the Bulletin

The purpose of this Bulletin is to lead auditors to the use of professional judgement on audit engagements when planning, obtaining and assessing the sufficiency and appropriateness of audit evidence that was compiled in a jurisdiction, where there is no prohibition on the use of direct assistance of internal auditors in that jurisdiction.

The Issue

In November 2013, the AUASB revised Auditing Standard ASA 610 *Using the Work of Internal Auditors*. The revised standard reflects developments in the internal auditing environment and provides a more robust framework for the evaluation and, where appropriate, use of the work of the internal audit function by the independent external auditor. The revised standard also prohibits the use of internal auditors to provide direct assistance in an independent audit or review conducted in accordance with the Australian Auditing Standards.

For a group audit, this prohibition extends to the use of internal auditors to provide direct assistance in an audit or review of a component, including an overseas component, conducted in accordance with the Australian Auditing Standards.

The AUASB concluded that a prohibition on direct assistance is justified as it reinforces the principle of auditor independence¹, which is critical to overall audit quality and the integrity of the external audit process. The AUASB considers that internal auditors are not independent of the audit client and are not subject to the same independence requirements as external auditors. The prohibition creates a clearer division of responsibility between internal and external audit teams to safeguard against conflicts of interest and supports stakeholders' expectations that external auditors maintain their independence.

One of the areas of difficulty impacting auditors since the revision of ASA 610 is around the issues that auditors need to consider when using the work of internal

auditors in jurisdictions where there is no prohibition on the use of direct assistance, such as in the United States (US)². This Bulletin seeks to provide two scenarios and the consequences and considerations to assist auditors in complying with the Australian Auditing Standards.

Scenarios, Consequences and Considerations

The table on the following pages summarises two auditor reporting scenarios and the consequences and considerations regarding the impact of the prohibition of the use of direct assistance of internal auditors when undertaking or performing group/component audit engagements. The scenarios below assume that the overseas entity, where direct assistance is permitted, and the matter for which internal audit provided direct assistance is **material** to the audit engagement that is subject to Australian Auditing Standards.

¹ See also APES 110 *Code of Ethics for Professional Accountants* issued by the Accounting Professional and Ethical Standards Board.

² Various other jurisdictions have the same prohibition as Australia. Auditors are reminded that when dealing with these jurisdictions, there would be no additional consequences as a result of the prohibition. These jurisdictions include: Bulgaria, Estonia, Finland, France, Germany, Greece, Lithuania, Luxembourg, Malta, Netherlands, Norway, Portugal, Slovakia, Slovenia, Spain, Sweden and the UK.



Scenario and Consequence

Considerations

1 Scenario:

An Australian group auditor signs an auditor's report under Australian Auditing Standards where the component auditor uses direct assistance (for example in the US where the use of direct assistance is permitted).

Consequence:

Where overseas component auditors provide evidence to Australian auditors signing an Australian Auditor's Report, and the overseas auditor has relied on direct assistance of internal audit in the past, the group auditor may incur additional audit effort and costs to obtain sufficient appropriate audit evidence under Australian Auditing Standards.

Early instructions to the component auditor, as addressed in ASA 600³, regarding the Australian prohibition on direct assistance is essential to allow the component auditor to plan the audit without the use of internal auditors providing direct assistance.

Where there is a change to the extent of audit effort resulting from the prohibition of direct assistance, the auditor may communicate such changes with those charged with governance.

It is ultimately the auditor's responsibility to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. If such evidence is not obtained, this may lead to a modification of the auditor's opinion.

2 Scenario:

An Australian auditor is a subsidiary component auditor signing a statutory auditor's report under Australian Auditing Standards.

The auditor is using work performed by the group auditor in a jurisdiction, where direct assistance by internal audit is permitted. Examples of use of direct assistance include:

- A group's IT systems are centralised, or there is a shared service centre outside of Australia that is audited in a jurisdiction where direct assistance is permitted; or
- A third party service organisation audited in a jurisdiction where direct assistance is permitted provides an ASAE 3402⁴ report on controls prepared by the service organisation's auditors who may have used direct assistance.

Early communication to the group auditor regarding the Australian prohibition on direct assistance by internal audit is essential so that the Australian auditor can ascertain the extent of use of direct assistance of internal audit and accordingly understand the possible impact on the Australian audit.

It is ultimately the auditor's responsibility to obtain sufficient appropriate audit evidence in accordance with the Australian Auditing Standards to be able to draw reasonable conclusions on which to base the auditor's opinion. If such evidence is not obtained, this may lead to a modification of the auditor's opinion.

Where there is a change in the extent of audit effort resulting from the prohibition of direct assistance, the auditor may communicate such changes with those charged with governance.



³ See ASA 600 *Special Considerations – Audits of a Group Financial Report (Including the Work of Component Auditors)*.

⁴ See ASAE 3402 *Assurance Reports on Controls at a Service Organisation*. References to an ASAE 3402 report throughout this Bulletin apply equally to a report issued under an international equivalent.

Scenario and Consequence

Considerations

2 **Consequence:**

cont.

Where an Australian component auditor signs an Australian Auditor's Report, and the overseas auditor has relied on direct assistance of internal audit in the past, the Australian auditor needs to consider the sufficiency and appropriateness of the audit evidence obtained. If the audit evidence is not deemed sufficient and appropriate to meet Australian Auditing Standards, this may lead to additional audit effort.

Considerations specific to Third Party Service Organisations:

Where the auditor is anticipating using a service organisation report under ASAE 3402 as a piece of audit evidence, it is important for the auditor to communicate upfront with their client at the planning phase when setting up the terms of engagement, that there may be a need for the auditor to communicate with the service organisation's auditor and that the client may need to assist in facilitating these communications.

Where a third party service organisation is audited in a jurisdiction where direct assistance is permitted and where direct assistance may have been used by the service organisation's auditors, the user auditor in Australia needs to consider whether the service organisation report under ASAE 3402 constitutes sufficient appropriate audit evidence in accordance with the Australian Auditing Standards. In determining the sufficiency and appropriateness of the audit evidence obtained from an ASAE 3402 report, the Australian auditor considers:

- the source of the report including the service auditor's professional competence⁵;
- whether the standards⁶ of the jurisdiction under which the report was issued meet Australian Auditing Standards;
- the service auditor's independence from the service organisation as required under ASA 402⁷, including, whether the service auditor meets applicable ethical requirements in Australia. Where direct assistance may have been used by the service auditor, the auditor considers the impact this may have on the reliability and relevance of the service auditor's report (the auditor may need to make enquiries to determine whether direct assistance has been obtained);
- the nature and significance of the work undertaken at the service organisation and the relevance of those services to the entity's controls and the overall audit; and
- complementary user entity controls supporting the ASAE 3402 report.

The results of the above considerations, in relation to the Australian auditor's assessment of the ASAE 3402 report as appropriate audit evidence, including those where direct assistance of internal audit may have been used by the overseas auditor, leads to the following outcomes in relation to the use of the ASAE 3402 report for the user auditor:

- reliance on the ASAE 3402 report as sufficient appropriate audit evidence; or
- a modification to the extent of reliance on the ASAE 3402 report as audit evidence; or
- an inability to rely on the ASAE 3402 report as sufficient appropriate audit evidence.

The auditor exercises professional judgement in making this determination.

As contemplated in ASA 402, if a user auditor is unable to obtain sufficient appropriate audit evidence regarding the services provided by the service organisation relevant to the audit of the user entity's financial report, a limitation of scope of the audit exists⁸. Whether the user auditor expresses a qualified opinion or disclaims the audit opinion depends on the user auditor's conclusion as to whether the possible effects on the financial report are material or both material and pervasive.

⁵ See ASA 402 *Audit Considerations Relating to an Entity Using a Service Organisation*, paragraph 13.

⁶ See ASA 402, paragraph 13.

⁷ See ASA 402, paragraph 13.

⁸ See ASA 402, paragraph A42.



Australian Government

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