

EXPOSURE DRAFT

ED 21/05
(October 2005)

Proposed Auditing Standard: Using the Work of an Expert (Re-issuance of AUS 606)

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



Australian Government

Auditing and Assurance Standards Board

Commenting on this Exposure Draft

Comments on this Exposure Draft should be forwarded so as to arrive by 15 December 2005. Comments should be addressed to:

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A copy of all non-confidential submissions will be placed on public record on the AUASB website: www.auasb.gov.au.

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PREFACE

Reasons for Issuing ED 21/05

The Auditing and Assurance Standards Board (AUASB) is proposing to re-issue Auditing Standard (AUS 606) *Using the Work of an Expert* due to the requirements of the legislative provisions explained below.

The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (the CLERP 9 Act) established the AUASB as an independent statutory body under section 227A of the *Australian Securities and Investments Commission Act 2001*, as from 1 July 2004. Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards will be legislative instruments under the *Legislative Instruments Act 2003*.

Main Proposals

This proposed Auditing Standard establishes mandatory requirements and provides explanatory guidance on using the work of an expert as audit evidence.

Proposed Operative Date

It is intended that this proposed Auditing Standard will be operative for financial reporting periods commencing on or after 1 July 2006.

Main changes from existing AUS 606 (July 2002)

The main differences between this proposed Auditing Standard and the Auditing Standard issued by the former Auditing & Assurance Standards Board of the Australian Accounting Research Foundation that it supersedes, AUS 606 (July 2002), is that in this proposed Auditing Standard:

1. the word 'shall', in the **bold-type** paragraphs, is the terminology used to describe an auditor's mandatory requirements, whereas an auditor's degree of responsibility was previously described by the word 'should';
2. the explanatory paragraphs provide guidance and illustrative examples to assist the auditor in fulfilling the mandatory requirements, whereas previously some obligations were implied within certain explanatory paragraphs. Accordingly, such

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paragraphs have been redrafted to clarify that the matter forms part of the explanatory guidance;

3. the terminology and overall concepts have been aligned to the Audit Risk Standards and the Quality Control Standard. The issue and re-issue of the Audit Risk Standards in February 2004 and the Quality Control Standard in June 2004, comprising:
- AUS 402 “Understanding the Entity and Its Environment and Assessing the Risks of Misstatement”;
 - AUS 406 “The Auditor’s Procedures in Response to Assessed Risks”;
 - AUS 502 “Audit Evidence”; and
 - AUS 206 “Quality Control for Audits of Historical Financial Information”

gave rise to necessary conforming amendments to certain existing AUSs, including AUS 606; and

4. includes as an expert a person employed by the auditor, whereas previously in AUS 606, a person employed by the auditor was not an expert.

A Table of Proposed Changes is provided as an attachment to the Exposure Draft.

Request for Comments

Comments are invited on this Exposure Draft of the proposed re-issuance of Auditing Standard (AUS 606) *Using the Work of an Expert* by 15 December 2005. The AUASB would prefer that respondents express a clear overall opinion on whether the proposed Auditing Standard, as a whole, is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on any matter. The AUASB regards both critical and supportive comments as essential to a balanced review of the proposed Auditing Standard.

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes Auditing Standard << >> *Using the Work of an Expert* as set out in paragraphs 1 to 28, pursuant to section 227B of the *Australian Securities and Investment Commission Act 2001* and section 336 of the *Corporations Act 2001*.

This Auditing Standard is to be read in conjunction with the *Preamble to AUASB Standards*, which sets out the intentions of the AUASB on how the Auditing Standards are to be understood, interpreted and applied.

The mandatory requirements of this Auditing Standard are set out in **bold-type** paragraphs.

AUDITING STANDARD

Using the Work of an Expert

Application

- 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 Part 2M.3 of the *Corporations Act 2001*; and**
 - (b) **an audit of a financial report for any other purpose.**
- 2 This Auditing Standard also applies, as appropriate, to an audit of other financial information.

Operative Date

- 3 **This Auditing Standard is operative for financial reporting periods commencing on or after 1 July 2006.**

Introduction

- 4 The purpose of this Auditing Standard is to establish mandatory requirements and provide explanatory guidance on using the work of an expert as audit evidence.
- 5 **When using the work performed by an expert, the auditor shall obtain sufficient appropriate audit evidence that such work is adequate for the purposes of the audit.**
- 6 “Expert” means a person or firm possessing special skill, knowledge and experience in a particular field other than accounting and auditing.
- 7 The auditor’s education and experience enable the auditor to be knowledgeable about business matters in general, but the auditor is not expected to have the expertise of a person trained for or qualified to engage in the practice of another profession or occupation, such as an actuary or engineer.
- 8 An expert may be:
 - (a) contracted by the entity;

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- (b) contracted by the auditor;
- (c) employed by the entity; or
- (d) employed by the auditor.

When the auditor uses the work of an expert employed by the audit firm, the auditor will be able to rely on the firm's systems for recruitment and training that determine that expert's capabilities and competence, as explained in AUS 206, "Quality Control for Audits of a Financial Report", instead of needing to evaluate them for each audit engagement.

- 9 Although the auditor may use the work of an expert as audit evidence, the auditor retains full responsibility for the audit opinion on the financial report.

Determining the Need to Use the Work of an Expert

- 10 In obtaining an understanding of the entity and performing further procedures in response to assessed risks, the auditor may need to obtain, in conjunction with the entity or independently, audit evidence in the form of reports, opinions, valuations and statements of an expert. Examples include the following:
- (a) valuations of certain types of assets, for example land and buildings, plant and machinery, works of art and precious stones;
 - (b) determination of quantities or physical condition of assets, for example minerals stored in stockpiles, underground mineral and petroleum reserves and the remaining useful life of plant and machinery;
 - (c) determination of amounts using specialised techniques or methods, for example an actuarial valuation;
 - (d) the measurement of work completed and to be completed on contracts in progress; and
 - (e) legal opinions concerning interpretations of agreements, statutes and regulations.

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- 11 When determining the need to use the work of an expert, the auditor would ordinarily consider:
- (a) the engagement team's knowledge and previous experience of the matter being considered;
 - (b) the risk of material misstatement based on the nature, complexity, and materiality of the matter being considered; and
 - (c) the quantity and quality of other audit evidence expected to be obtained.

Competence and Objectivity of the Expert

- 12 **When planning to use the work of an expert, the auditor shall evaluate the professional competence of the expert.**
- 13 Pursuant to paragraph 12 of this Auditing Standard, this will involve considering the expert's:
- (a) professional certification or licensing by, or membership in, an appropriate professional body; and
 - (b) experience and reputation in the field in which the auditor is seeking audit evidence.
- 14 **The auditor shall evaluate the objectivity of the expert.**
- 15 The risk that an expert's objectivity will be impaired increases when the expert is:
- (a) employed by the entity; or
 - (b) related in some other manner to the entity, for example by being financially dependent upon or having an investment in the entity.

If the auditor is concerned regarding the competence or objectivity of the expert, the auditor needs to discuss any reservations with management and consider whether sufficient appropriate audit evidence can be obtained concerning the work of an expert. The auditor may need to undertake additional audit procedures or seek audit evidence from another expert (after taking into account the factors in paragraph 11 of this Auditing Standard).

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- 16 Where an expert is employed by or related to the entity, the auditor would ordinarily consider whether there are any mitigating factors such as professional and/or statutory obligations governing the work of an expert, that would impact on the objectivity of the expert. For example it is common practice for the actuary of a life insurance company to be an employee.

Scope of the Expert's Work

- 17 **The auditor shall obtain sufficient appropriate audit evidence that the scope of the expert's work is adequate for the purposes of the audit.**
- 18 Audit evidence may be obtained through a review of the terms of reference which are often set out in written instructions from the entity to the expert. Such instructions to the expert may cover such matters as the following:
- (a) the objectives and scope of the expert's work;
 - (b) a general outline as to the specific matters the auditor expects the expert's report to cover;
 - (c) the intended use by the auditor of the expert's work, including the possible communication to third parties of the expert's identity and extent of involvement;
 - (d) the extent of the expert's access to appropriate records and files;
 - (e) clarification of the expert's relationship with the entity, if any;
 - (f) confidentiality of the entity's information; and
 - (g) information regarding the assumptions and methods intended to be used by the expert and their consistency with those used in prior periods.

In the event that these matters are not clearly set out in written instructions to the expert, the auditor may need to communicate with the expert directly to obtain audit evidence in this regard. In obtaining an understanding of the entity, the auditor also ordinarily considers whether to include the expert during the engagement team's discussion of the susceptibility of the entity's financial report to material misstatement.

Evaluating the Work of the Expert

- 19 **The auditor shall evaluate the appropriateness of the expert's work as audit evidence regarding the assertion being considered.**
- 20 Pursuant to paragraph 19 of this Auditing Standard, the auditor is required to evaluate whether the substance of the expert's findings is properly reflected in the financial report or supports the assertions, and consideration of:
- (a) source data used;
 - (b) assumptions and methods used and their consistency with prior periods; and
 - (c) results of the expert's work in the light of the auditor's overall knowledge of the business and the results of other audit procedures.
- 21 When considering whether the expert has used source data which is appropriate in the circumstances, the auditor would ordinarily consider the following procedures:
- (a) making inquiries regarding any procedures undertaken by the expert to establish whether the source data is relevant and reliable; and
 - (b) reviewing or testing the data used by the expert.
- 22 The appropriateness and reasonableness of assumptions and methods used and their application are the responsibility of the expert. The auditor does not have the same expertise and, therefore, cannot always challenge the expert's assumptions and methods. However, the auditor will ordinarily need to obtain an understanding of the assumptions and methods used and to consider whether they are appropriate and reasonable, based on the auditor's knowledge of the business and the results of other audit procedures.
- 23 **If the results of the expert's work do not provide sufficient appropriate audit evidence, or if the results are not consistent with other audit evidence, the auditor shall resolve the matter.**
- 24 This may involve discussions with the entity and the expert, applying additional audit procedures, including possibly engaging another expert, or modifying the auditor's report.

Reference to an Expert in the Auditor's Report

- 25 **When issuing an unmodified auditor's report, the auditor shall not refer to the work of an expert.**
- 26 Such a reference might be misunderstood to be a qualification of the auditor's opinion or a division of responsibility, neither of which is intended.
- 27 If, as a result of the work of an expert, the auditor decides to issue a modified auditor's report, in some circumstances it may be appropriate in explaining the nature of the modification, to refer to or describe the work of the expert (including the identity of the expert and the extent of the expert's involvement). In these circumstances, the auditor would ordinarily obtain the permission of the expert before making such a reference. If permission is refused and the auditor believes a reference is necessary, the auditor ordinarily may need to seek legal advice.

Conformity with International Standards on Auditing

- 28 Except as noted below, this Auditing Standard conforms with International Standard on Auditing ISA 620, "Using the Work of an Expert", issued by the International Auditing and Assurance Standards Board of the International Federation of Accountants. The differences between this Auditing Standard and ISA 620 are:

- There is no corresponding paragraph 9 or 16 in ISA 620.

Compliance with this Auditing Standard enables compliance with ISA 620.

Table of Proposed Changes from AUS 606 <i>Using The Work Of An Expert</i>
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Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
1, 2	Requirement	New Application paragraphs.
3	Requirement	Re-position Operative Date paragraph.
5, 12, 14, 17, 19, 23, 25	Requirement	Replace “should” with “shall”.
8, 10, 11, 12, 14, 18, 19, 20, 21, 22, 24, 26	Requirement / Grey	Change to conform to ISA 620.
11, 16, 18, 21, 22	Guidance	Insert “ordinarily” to clarify implied obligations.
13, 20	Guidance	Insert “pursuant to paragraph xx of this Auditing Standard...” to clarify implied obligations.