



MALAYSIAN INSTITUTE
OF ACCOUNTANTS
ACCOUNTANTS: MANAGERS OF VALUE

ISA 610 (Revised)
September 2012

International Standards on Auditing

ISA 610 (Revised), Using the
Work of Internal Auditors

Conforming Amendments to
Other ISAs

INTERNATIONAL STANDARD ON AUDITING 610 (REVISED)

Using the Work of Internal Auditors

Explanatory Foreword

The Council of the Malaysian Institute of Accountants has approved this standard in September 2012 for publication. This standard should be read in conjunction with the Preface to Malaysian Approved Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements; Preface to the International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements; Glossary of Terms and International Framework for Assurance Engagements.

The status of International Standards on Auditing is set out in the Preface to Malaysian Approved Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements.

Applicability

International Standards on Auditing (ISAs) are to be applied in the audit of financial statements under all reporting frameworks. Reporting frameworks are determined by legislation, regulations and promulgations of the Malaysian Institute of Accountants and where appropriate mutually agreed upon terms of reporting.

ISAs are to be applied in the audit of historical financial information.

Notes and Exceptions

The Council wishes to highlight that reference made in the Standard to the *Code of Ethics for Professional Accountants* issued by the International Ethics Standards Board for Accountants should be deemed as reference to the *By-Laws (on Professional Ethics, Conduct and Practice)* of the Malaysian Institute of Accountants.

Effective Date in Malaysia

This standard is effective for audits of financial statements for periods ending on or after December 15, 2013.

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INTERNATIONAL STANDARD ON AUDITING 610 (REVISED)

USING THE WORK OF INTERNAL AUDITORS

(Effective for audits of financial statements for periods ending on or after December 15, 2013)

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International Standard on Auditing (ISA) 610 (Revised), *Using the Work of Internal Auditors*, should be read in conjunction with ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the external auditor's responsibilities if using the work of the internal audit function in obtaining audit evidence.
2. This ISA does not apply if the entity does not have an internal audit function. (Ref: Para. A2)
3. If the entity has an internal audit function, the requirements in this ISA do not apply if:
 - (a) The responsibilities and activities of the function are not relevant to the audit; or
 - (b) Based on the auditor's preliminary understanding of the function obtained as a result of procedures performed under ISA 315 (Revised),¹ the external auditor does not expect to use the work of the function in obtaining audit evidence.

Nothing in this ISA requires the external auditor to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed directly by the external auditor; it remains a decision of the external auditor in establishing the overall audit strategy.

4. In some jurisdictions, the external auditor may be prohibited, or restricted to some extent, by law or regulation from using the work of the internal audit function. The ISAs do not override laws or regulations that govern an audit of financial statements.² Such prohibitions or restrictions will therefore not prevent the external auditor from complying with the ISAs.

Relationship between ISA 315 (Revised) and ISA 610 (Revised)

5. Many entities establish internal audit functions as part of their internal control and governance structures. The objectives and scope of an internal audit function, the nature of its responsibilities and its organizational status, including the function's authority and accountability, vary widely and depend on the size and structure of the entity and the requirements of management and, where applicable, those charged with governance.
6. ISA 315 (Revised) addresses how the knowledge and experience of the internal audit function can inform the external auditor's understanding of the entity and its environment and identification and assessment of risks of material misstatement. ISA 315 (Revised)³ also explains how effective communication between the internal and external auditors also creates an environment in which the external auditor can be informed of significant matters that may affect the external auditor's work.
7. Depending on whether the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors, the level of competency of the internal audit function, and whether the function applies a systematic and disciplined approach, the external auditor may also be able to use the work of the internal audit function in a constructive and complementary manner. This ISA addresses the external auditor's responsibilities when, based on the external auditor's preliminary understanding of the internal audit function obtained as a result of procedures performed

¹ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

² ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph A55

³ ISA 315 (Revised), paragraph A116

under ISA 315 (Revised), the external auditor expects to use the work of the internal audit function as part of the audit evidence obtained.⁴ Such use of that work modifies the nature or timing, or reduces the extent, of audit procedures to be performed directly by the external auditor.

8. There may be individuals in an entity that perform procedures similar to those performed by an internal audit function. However, unless performed by an objective and competent function that applies a systematic and disciplined approach, including quality control, such procedures would be considered internal controls and obtaining evidence regarding the effectiveness of such controls would be part of the auditor's responses to assessed risks in accordance with ISA 330.⁵

The External Auditor's Responsibility for the Audit

9. 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 audit function on the engagement. Although the function may perform audit procedures similar to those performed by the external auditor, neither the internal audit function nor the internal auditors are independent of the entity as is required of the external auditor in an audit of financial statements in accordance with ISA 200.⁶ This ISA, therefore, defines the conditions that are necessary for the external auditor to be able to use the work of internal auditors. It also defines the necessary work effort to obtain sufficient appropriate evidence that the work of the internal audit function is adequate for the purposes of the audit. The requirements are designed to provide a framework for the external auditor's judgments regarding the use of the work of the internal audit function to prevent over or undue use of such work.

Effective Date

10. This ISA is effective for audits of financial statements for periods ending on or after December 15, 2013.

Objectives

11. The objectives of the external auditor, where the entity has an internal audit function and the external auditor expects to use the work of the function to modify the nature or timing, or reduce the extent, of audit procedures to be performed directly by the external auditor are:
 - (a) To determine whether the work of the internal audit function can be used, and if so, in which areas and to what extent;
and having made that determination:
 - (b) If using the work of the internal audit function, to determine whether that work is adequate for purposes of the audit.

Definition

12. For purposes of the ISAs, the following term has the meaning attributed below:

⁴ See paragraphs 13–23.

⁵ ISA 330, *The Auditor's Responses to Assessed Risk*

⁶ ISA 200, paragraph 14

Internal audit function – A function of an entity that performs assurance and consulting activities designed to evaluate and improve the effectiveness of the entity’s governance, risk management and internal control processes. (Ref: Para. A1–A4)

Requirements

Determining Whether, in Which Areas, and to What Extent the Work of the Internal Audit Function Can Be Used

Evaluating the Internal Audit Function

13. The external auditor shall determine whether the work of the internal audit function can be used for purposes of the audit by evaluating the following:
 - (a) The extent to which the internal audit function’s organizational status and relevant policies and procedures support the objectivity of the internal auditors; (Ref: Para. A5–A9)
 - (b) The level of competence of the internal audit function; and (Ref: Para. A5–A9)
 - (c) Whether the internal audit function applies a systematic and disciplined approach, including quality control. (Ref: Para. A10–A11)
14. The external auditor shall not use the work of the internal audit function if the external auditor determines that:
 - (a) The function’s organizational status and relevant policies and procedures do not adequately support the objectivity of internal auditors;
 - (b) The function lacks sufficient competence; or
 - (c) The function does not apply a systematic and disciplined approach, including quality control. (Ref: Para. A12–A14)

Determining the Nature and Extent of Work of the Internal Audit Function that Can Be Used

15. As a basis for determining the areas and the extent to which the work of the internal audit function can be used, the external auditor shall consider the nature and scope of the work that has been performed, or is planned to be performed, by the internal audit function and its relevance to the external auditor’s overall audit strategy and audit plan. (Ref: Para. A15–A17)
16. The external auditor shall make all significant judgments in the audit engagement and, to prevent undue use of the work of the internal audit function, shall plan to use less of the work of the function and perform more of the work directly: (Para Ref: A15–A17)
 - (a) The more judgment is involved in:
 - (i) Planning and performing relevant audit procedures; and
 - (ii) Evaluating the audit evidence gathered; (Ref: Para. A18–A19)
 - (b) The higher the assessed risk of material misstatement at the assertion level, with special consideration given to risks identified as significant; (Para Ref: A20–A22)
 - (c) The less the internal audit function’s organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors; and
 - (d) The lower the level of competence of the internal audit function.

17. The external auditor shall also evaluate whether, in aggregate, using the work of the internal audit function to the extent planned would still result in the external auditor being sufficiently involved in the audit, given the external auditor's sole responsibility for the audit opinion expressed. (Ref: Para. A15–A22)
18. The external auditor shall, in communicating with those charged with governance an overview of the planned scope and timing of the audit in accordance with ISA 260,⁷ communicate how the external auditor has planned to use the work of the internal audit function. (Ref: Para. A23)

Using the Work of the Internal Audit Function

19. If the external auditor plans to use the work of the internal audit function, the external auditor shall discuss the planned use of its work with the function as a basis for coordinating their respective activities. (Ref: Para. A24–A26)
20. The external auditor shall read the reports of the internal audit function relating to the work of the function that the external auditor plans to use to obtain an understanding of the nature and extent of audit procedures it performed and the related findings.
21. The external auditor shall perform sufficient audit procedures on the body of work of the internal audit function as a whole that the external auditor plans to use to determine its adequacy for purposes of the audit, including evaluating whether:
 - (a) The work of the function had been properly planned, performed, supervised, reviewed and documented;
 - (b) Sufficient appropriate evidence had been obtained to enable the function to draw reasonable conclusions; and
 - (c) Conclusions reached are appropriate in the circumstances and the reports prepared by the function are consistent with the results of the work performed. (Ref: Para. A27–A30)
22. The nature and extent of the external auditor's audit procedures shall be responsive to the external auditor's evaluation of:
 - (a) The amount of judgment involved;
 - (b) The assessed risk of material misstatement;
 - (c) The extent to which the internal audit function's organizational status and relevant policies and procedures support the objectivity of the internal auditors; and
 - (d) The level of competence of the function;⁸ (Ref: Para. A27–A29)and shall include reperformance of some of the work. (Ref: Para. A30)
23. The external auditor shall also evaluate whether the external auditor's conclusions regarding the internal audit function in paragraph 13 of this ISA and the determination of the nature and extent of use of the work of the function for purposes of the audit in paragraphs 16–17 of this ISA remain appropriate.

⁷ ISA 260, *Communication with Those Charged with Governance*, paragraph 15

⁸ See paragraph 16.

Documentation

24. If the external auditor uses the work of the internal audit function, the external auditor shall include in the audit documentation:
- (a) The evaluation of:
 - (i) Whether the function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors;
 - (ii) The level of competence of the function; and
 - (iii) Whether the function applies a systematic and disciplined approach, including quality control;
 - (b) The nature and extent of the work used and the basis for that decision; and
 - (c) The audit procedures performed by the external auditor to evaluate the adequacy of the work used.

Application and Other Explanatory Material

Definition of Internal Audit Function (Ref: Para. 2, 12)

- A1. The objectives and scope of internal audit functions typically include assurance and consulting activities designed to evaluate and improve the effectiveness of the entity's governance processes, risk management and internal control such as the following:

Activities Relating to 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 organization and effectiveness of communication among those charged with governance, external and internal auditors, and management.

Activities Relating to Risk Management

- The internal audit function may assist the entity by identifying and evaluating significant exposures to risk and contributing to the improvement of risk management and internal control (including effectiveness of the financial reporting process).
- The internal audit function may perform procedures to assist the entity in the detection of fraud.

Activities Relating to Internal Control

- Evaluation of internal control. The internal audit function may be assigned specific responsibility for reviewing controls, evaluating their operation and recommending improvements thereto. In doing so, the internal audit function provides assurance on the control. For example, the internal audit function might plan and perform tests or other procedures to provide assurance to management and those charged with governance regarding the design, implementation and operating effectiveness of internal control, including those controls that are relevant to the audit.
- Examination of financial and operating information. The internal audit function may be assigned to review the means used to identify, recognize, measure, classify and report

financial and operating information, and to make specific inquiry 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 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.
- A2. Activities similar to those performed by an internal audit function may be conducted by functions with other titles within an entity. Some or all of the activities of an internal audit function may also be outsourced to a third-party service provider. Neither the title of the function, nor whether it is performed by the entity or a third-party service provider, are sole determinants of whether or not the external auditor can use the work of the function. Rather, it is the nature of the activities; the extent to which the internal audit function's organizational status and relevant policies and procedures support the objectivity of the internal auditors; competence; and systematic and disciplined approach of the function that are relevant. References in this ISA to the work of the internal audit function include relevant activities of other functions or third-party providers that have these characteristics.
- A3. In addition, those in the entity with operational and managerial duties and responsibilities outside of the internal audit function would ordinarily face threats to their objectivity that would preclude them from being treated as part of an internal audit function for the purpose of this ISA, although they may perform control activities that can be tested in accordance with ISA 330.⁹ For this reason, monitoring controls performed by an owner-manager would not be considered equivalent to an internal audit function.
- A4. While the objectives of an entity's internal audit function and the external auditor differ, the function may perform audit procedures similar to those performed by the external auditor in an audit of financial statements. If so, the external auditor may make use of the function for purposes of the audit in one or more of the following ways:
- To obtain information that is relevant to the external auditor's assessments of the risks of material misstatement due to error or fraud. In this regard, ISA 315 (Revised)¹⁰ requires the external auditor to obtain an understanding of the nature of the internal audit function's responsibilities, its status within the organization, and the activities performed, or to be performed, and make inquiries of appropriate individuals within the internal audit function (if the entity has such a function); or
 - Unless prohibited, or restricted to some extent, by law or regulation, the external auditor, after appropriate evaluation, may decide to use work that has been performed by the internal audit function during the period in partial substitution for audit evidence to be obtained directly by the external auditor.¹¹

⁹ See paragraph 8.

¹⁰ ISA 315 (Revised), paragraph 6(a)

¹¹ See paragraphs 13–23.

Determining Whether, in Which Areas, and to What Extent the Work of the Internal Audit Function Can Be Used

Evaluating the Internal Audit Function

Objectivity and Competence (Ref: Para. 13(a)–(b))

- A5. The external auditor exercises professional judgment in determining whether the work of the internal audit function can be used for purposes of the audit, and the nature and extent to which the work of the internal audit function can be used in the circumstances.
- A6. The extent to which the internal audit function’s organizational status and relevant policies and procedures support the objectivity of the internal auditors and the level of competence of the function are particularly important in determining whether to use and, if so, the nature and extent of the use of the work of the function that is appropriate in the circumstances.
- A7. Objectivity refers to the ability to perform those tasks without allowing bias, conflict of interest or undue influence of others to override professional judgments. Factors that may affect the external auditor’s evaluation include the following:
- Whether the organizational status of the internal audit function, including the function’s authority and accountability, supports the ability of the function to be free from bias, conflict of interest or undue influence of others to override professional judgments. For example, whether the internal audit function reports to those charged with governance or an officer with appropriate authority, or if the function reports to management, whether it has direct access to those charged with governance.
 - Whether the internal audit function is free of any conflicting responsibilities, for example, having managerial or operational duties or responsibilities that are outside of the internal audit function.
 - Whether those charged with governance oversee employment decisions related to the internal audit function, for example, determining the appropriate remuneration policy.
 - Whether there are any constraints or restrictions placed on the internal audit function by management or those charged with governance, for example, in communicating the internal audit function’s findings to the external auditor.
 - Whether the internal auditors are members of relevant professional bodies and their memberships obligate their compliance with relevant professional standards relating to objectivity, or whether their internal policies achieve the same objectives.
- A8. Competence of the internal audit function refers to the attainment and maintenance of knowledge and skills of the function as a whole at the level required to enable assigned tasks to be performed diligently and in accordance with applicable professional standards. Factors that may affect the external auditor’s determination include the following:
- Whether the internal audit function is adequately and appropriately resourced relative to the size of the entity and the nature of its operations.
 - Whether there are established policies for hiring, training and assigning internal auditors to internal audit engagements.
 - Whether the internal auditors have adequate technical training and proficiency in auditing. Relevant criteria that may be considered by the external auditor in making the assessment may include, for example, the internal auditors’ possession of a relevant professional designation and experience.

- Whether the internal auditors possess the required knowledge relating to the entity's financial reporting and the applicable financial reporting framework and whether the internal audit function possesses the necessary skills (for example, industry-specific knowledge) to perform work related to the entity's financial statements.
 - Whether the internal auditors are members of relevant professional bodies that oblige them to comply with the relevant professional standards including continuing professional development requirements.
- A9. Objectivity and competence may be viewed as a continuum. The more the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors and the higher the level of competence of the function, the more likely the external auditor may make use of the work of the function and in more areas. However, an organizational status and relevant policies and procedures that provide strong support for the objectivity of the internal auditors cannot compensate for the lack of sufficient competence of the internal audit function. Equally, a high level of competence of the internal audit function cannot compensate for an organizational status and policies and procedures that do not adequately support the objectivity of the internal auditors.

Application of a Systematic and Disciplined Approach (Ref: Para. 13(c))

- A10. The application of a systematic and disciplined approach to planning, performing, supervising, reviewing and documenting its activities distinguishes the activities of the internal audit function from other monitoring control activities that may be performed within the entity.
- A11. Factors that may affect the external auditor's determination of whether the internal audit function applies a systematic and disciplined approach include the following:
- The existence, adequacy and use of documented internal audit procedures or guidance covering such areas as risk assessments, work programs, documentation and reporting, the nature and extent of which is commensurate with the size and circumstances of an entity.
 - Whether the internal audit function has appropriate quality control policies and procedures, for example, such as those policies and procedures in ISQC 1¹² that would be applicable to an internal audit function (such as those relating to leadership, human resources and engagement performance) or quality control requirements in standards set by the relevant professional bodies for internal auditors. Such bodies may also establish other appropriate requirements such as conducting periodic external quality assessments.

Circumstances When Work of the Internal Audit Function Cannot Be Used (Ref: Para. 14)

- A12. The external auditor's evaluation of whether the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors, the level of competence of the internal audit function, and whether it applies a systematic and disciplined approach may indicate that the risks to the quality of the work of the function are too significant and therefore it is not appropriate to use any of the work of the function as audit evidence.

¹² International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

- A13. Consideration of the factors in paragraphs A7, A8 and A11 of this ISA individually and in aggregate is important because an individual factor is often not sufficient to conclude that the work of the internal audit function cannot be used for purposes of the audit. For example, the internal audit function's organizational status is particularly important in evaluating threats to the objectivity of the internal auditors. If the internal audit function reports to management, this would be considered a significant threat to the function's objectivity unless other factors such as those described in paragraph A7 of this ISA collectively provide sufficient safeguards to reduce the threat to an acceptable level.
- A14. In addition, the IESBA Code¹³ states that a self-review threat is created when the external auditor accepts an engagement to provide internal audit services to an audit client, and the results of those services will be used in conducting the audit. This is because of the possibility that the engagement team will use the results of the internal audit service without properly evaluating those results or without exercising the same level of professional skepticism as would be exercised when the internal audit work is performed by individuals who are not members of the firm. The IESBA Code¹⁴ discusses the prohibitions that apply in certain circumstances and the threats and the safeguards that can be applied to reduce the threats to an acceptable level in other circumstances.

Determining the Nature and Extent of Work of the Internal Audit Function that Can Be Used

Factors Affecting the Determination of the Nature and Extent of the Work of the Internal Audit Function that Can Be Used (Ref: Para. 15–17)

- A15. Once the external auditor has determined that the work of the internal audit function can be used for purposes of the audit, a first consideration is whether the planned nature and scope of the work of the internal audit function that has been performed, or is planned to be performed, is relevant to the overall audit strategy and audit plan that the external auditor has established in accordance with ISA 300.¹⁵
- A16. Examples of work of the internal audit function that can be used by the external auditor include the following:
- Testing of the operating effectiveness of controls.
 - Substantive procedures involving limited judgment.
 - Observations of inventory counts.
 - Tracing transactions through the information system relevant to financial reporting.
 - Testing of compliance with regulatory requirements.
 - In some circumstances, audits or reviews of the financial information of subsidiaries that are not significant components to the group (where this does not conflict with the requirements of ISA 600).¹⁶

¹³ The International Ethics Standards Board for Accountants' (IESBA) *Code of Ethics for Professional Accountants* (IESBA Code), Section 290.199

¹⁴ IESBA Code, Section 290.195–290.200

¹⁵ ISA 300, *Planning an Audit of Financial Statements*

¹⁶ ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

A17. The external auditor's determination of the planned nature and extent of use of the work of the internal audit function will be influenced by the external auditor's evaluation of the extent to which the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors and the level of competence of the internal audit function in paragraph 16 of this ISA. In addition, the amount of judgment needed in planning, performing and evaluating such work and the assessed risk of material misstatement at the assertion level are inputs to the external auditor's determination. Further, there are circumstances in which the external auditor cannot use the work of the internal audit function for purpose of the audit as described in paragraph 14 of this ISA.

Judgments in planning and performing audit procedures and evaluating results (Ref: Para. 16(a))

A18. The greater the judgment needed to be exercised in planning and performing the audit procedures and evaluating the audit evidence, the external auditor will need to perform more procedures directly in accordance with paragraph 16 of this ISA, because using the work of the internal audit function alone will not provide the external auditor with sufficient appropriate audit evidence.

A19. Since the external auditor has sole responsibility for the audit opinion expressed, the external auditor needs to make the significant judgments in the audit engagement in accordance with paragraph 16. Significant judgments include the following:

- Assessing the risks of material misstatement;
- Evaluating the sufficiency of tests performed;
- Evaluating the appropriateness of management's use of the going concern assumption;
- Evaluating significant accounting estimates; and
- Evaluating the adequacy of disclosures in the financial statements, and other matters affecting the auditor's report.

Assessed risk of material misstatement (Ref: Para. 16(b))

A20. For a particular account balance, class of transaction or disclosure, the higher an assessed risk of material misstatement at the assertion level, the more judgment is often involved in planning and performing the audit procedures and evaluating the results thereof. In such circumstances, the external auditor will need to perform more procedures directly in accordance with paragraph 16 of this ISA, and accordingly, make less use of the work of the internal audit function in obtaining sufficient appropriate audit evidence. Furthermore, as explained in ISA 200,¹⁷ 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 external auditor will need to perform more of the work directly.

A21. As explained in ISA 315 (Revised),¹⁸ significant risks require special audit consideration and therefore the external auditor's ability to use the work of the internal audit function in relation to significant risks will be restricted to procedures that involve limited judgment. In addition, where the risks of material misstatement is other than low, the use of the work of

¹⁷ ISA 200, paragraph A29

¹⁸ ISA 315 (Revised), paragraph 4(e)

the internal audit function alone is unlikely to reduce audit risk to an acceptably low level and eliminate the need for the external auditor to perform some tests directly.

- A22. Carrying out procedures in accordance with this ISA may cause the external auditor to reevaluate the external auditor's assessment of the risks of material misstatement. Consequently, this may affect the external auditor's determination of whether to use the work of the internal audit function and whether further application of this ISA is necessary.

Communication with Those Charged with Governance (Ref: Para. 18)

- A23. In accordance with ISA 260,¹⁹ the external auditor is required to communicate with those charged with governance an overview of the planned scope and timing of the audit. The planned use of the work of the internal audit function is an integral part of the external auditor's overall audit strategy and is therefore relevant to those charged with governance for their understanding of the proposed audit approach.

Using the Work of the Internal Audit Function

Discussion and Coordination with the Internal Audit Function (Ref: Para. 19)

- A24. In discussing the planned use of their work with the internal audit function as a basis for coordinating the respective activities, it may be useful to address the following:

- The timing of such work.
- The nature of the work performed.
- The extent of audit coverage.
- Materiality for the financial statements 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 and sample sizes.
- Documentation of the work performed.
- Review and reporting procedures.

- A25. Coordination between the external auditor and the internal audit function is effective when, for example:

- Discussions take place at appropriate intervals throughout the period.
- The external auditor informs the internal audit function of significant matters that may affect the function.
- The external auditor is advised of and has access to relevant reports of the internal audit function and is informed of any significant matters that come to the attention of the function when such matters may affect the work of the external auditor so that the external auditor is able to consider the implications of such matters for the audit engagement.

- A26. ISA 200²⁰ discusses the importance of the auditor planning and performing the audit with professional skepticism, including being alert to information that brings into question the

¹⁹ ISA 260, paragraph 15

²⁰ ISA 200, paragraphs 15 and A18

reliability of documents and responses to inquiries to be used as audit evidence. Accordingly, communication with the internal audit function throughout the engagement may provide opportunities for internal auditors to bring matters that may affect the work of the external auditor to the external auditor's attention.²¹ The external auditor is then able to take such information into account in the external auditor's identification and assessment of risks of material misstatement. In addition, if such information may be indicative of a heightened risk of a material misstatement of the financial statements or may be regarding any actual, suspected or alleged fraud, the external auditor can take this into account in the external auditor's identification of risk of material misstatement due to fraud in accordance with ISA 240.²²

Procedures to Determine the Adequacy of Work of the Internal Audit Function (Ref: Para. 21–22)

- A27. The external auditor's audit procedures on the body of work of the internal audit function as a whole that the external auditor plans to use provide a basis for evaluating the overall quality of the function's work and the objectivity with which it has been performed.
- A28. The procedures the external auditor may perform to evaluate the quality of the work performed and the conclusions reached by the internal audit function, in addition to reperformance in accordance with paragraph 22, include the following:
- Making inquiries of appropriate individuals within the internal audit function.
 - Observing procedures performed by the internal audit function.
 - Reviewing the internal audit function's work program and working papers.
- A29. The more judgment involved, the higher the assessed risk of material misstatement, the less the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors, or the lower the level of competence of the internal audit function, the more audit procedures are needed to be performed by the external auditor on the overall body of work of the function to support the decision to use the work of the function in obtaining sufficient appropriate audit evidence on which to base the audit opinion.

Reperformance (Ref: Para. 22)

- A30. For purposes of this ISA, reperformance involves the external auditor's independent execution of procedures to validate the conclusions reached by the internal audit function. This objective may be accomplished by examining items already examined by the internal audit function, or where it is not possible to do so, the same objective may also be accomplished by examining sufficient other similar items not actually examined by the internal audit function. Reperformance provides more persuasive evidence regarding the adequacy of the work of the internal audit function compared to other procedures the external auditor may perform in paragraph A28. While it is not necessary for the external auditor to do reperformance in each area of work of the internal audit function that is being used, some reperformance is required on the body of work of the internal audit function as a whole that the external auditor plans to use in accordance with paragraph 22. The external auditor is more likely to focus reperformance in those areas where more judgment

²¹ ISA 315 (Revised), paragraph A116

²² ISA 315 (Revised), paragraph A11 in relation to ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

was exercised by the internal audit function in planning, performing and evaluating the results of the audit procedures and in areas of higher risk of material misstatement.

CONFORMING AMENDMENTS TO OTHER ISAs

Note: The following are conforming amendments to other ISAs as a result of ISA 610 (Revised), *Using the Work of Internal Auditors*. These amendments are effective for audits of financial statements for periods ending on or after December 15, 2013. The footnote numbers within these amendments do not align with the ISAs that will be amended, and reference should be made to those ISAs.

ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

A72. In some cases, an ISA (and therefore all of its requirements) may not be relevant in the circumstances. For example, if an entity does not have an internal audit function, nothing in ISA 610 (Revised)¹ is relevant.

ISA 230, *Audit Documentation*

A19. The documentation requirement applies only to requirements that are relevant in the circumstances. A requirement is not relevant² only in the cases where:

- (a) The entire ISA is not relevant (for example, if an entity does not have an internal audit function, nothing in ISA 610 (Revised)³ is relevant); or
- (b) The requirement is conditional and the condition does not exist (for example, the requirement to modify the auditor's opinion where there is an inability to obtain sufficient appropriate audit evidence, and there is no such inability).

ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

19. For those entities that have an internal audit function, the auditor shall make inquiries of appropriate individuals within the function ~~internal audit~~ to determine whether ~~it~~ they ~~have~~ knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risks of fraud. (Ref: Para. A18)

Inquiries of the Internal Audit Function (Ref: Para. 19)

A18. ISA 315 (Revised) and ISA 610 (Revised) establish requirements and provide guidance relevant to ~~in~~ audits of those entities that have an internal audit function.⁴ In carrying out the requirements of those ISAs in the context of fraud, the auditor may inquire about specific activities of the function ~~internal audit activities~~ including, for example:

- The procedures performed, if any, by the internal auditors function during the year to detect fraud.
- Whether management has satisfactorily responded to any findings resulting from those procedures.

¹ ISA 610 (Revised), *Using the Work of Internal Auditors*, paragraph 2

² ISA 200, paragraph 22

³ ISA 610 (Revised), *Using the Work of Internal Auditors*, paragraph 2

⁴ ISA 315 (Revised), paragraphs 6(a) and 23, and ISA 610 (Revised), *Using the Work of Internal Auditors*

Appendix 1

Examples of Fraud Risk Factors

Internal control components are deficient as a result of the following:

- Inadequate monitoring of controls, including automated controls and controls over interim financial reporting (where external reporting is required).
- High turnover rates or employment of staff in accounting, internal audit, or information technology, or the internal audit function staff that are not effective.

ISA 260, *Communication with Those Charged with Governance*

A14. Other planning matters that it may be appropriate to discuss with those charged with governance include:

- Where the entity has an internal audit function, the extent to which how the external auditor will use the work of internal audit, and how the external and internal auditors can best work together in a constructive and complementary manner, including any planned use of the work of the internal audit function.⁵
- ...

A33. Before communicating matters with those charged with governance, the auditor may discuss them with management, unless that is inappropriate. For example, it may not be appropriate to discuss questions of management's competence or integrity with management. In addition to recognizing management's executive responsibility, these initial discussions may clarify facts and issues, and give management an opportunity to provide further information and explanations. Similarly, when the entity has an internal audit function, the auditor may discuss matters with the appropriate individuals within the function ~~internal auditor~~ before communicating with those charged with governance.

A43. As noted in paragraph 4, effective two-way communication assists both the auditor and those charged with governance. Further, ISA 315 (Revised) identifies participation by those charged with governance, including their interaction with the internal audit function, if any, and external auditors, as an element of the entity's control environment.⁶ Inadequate two-way communication may indicate an unsatisfactory control environment and influence the auditor's assessment of the risks of material misstatements. There is also a risk that the auditor may not have obtained sufficient appropriate audit evidence to form an opinion on the financial statements.

ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

A24. If the auditor has communicated deficiencies in internal control other than significant deficiencies to management in a prior period and management has chosen not to remedy them for cost or other reasons, the auditor need not repeat the communication in the current period. The auditor is also not required to repeat information about such deficiencies if it has been previously communicated to management by other parties, such as the internal auditors function or regulators. It may, however, be appropriate for the

⁵ ISA 610 (Revised), paragraph 18

⁶ ISA 315 (Revised), paragraph A7770

auditor to re-communicate these other deficiencies if there has been a change of management, or if new information has come to the auditor's attention that alters the prior understanding of the auditor and management regarding the deficiencies. ...

ISA 300, *Planning an Audit of Financial Statements*

Appendix

Characteristics of the Engagement

...

- The need for a statutory audit of standalone financial statements in addition to an audit for consolidation purposes.
- ~~The availability of the work of internal auditors and the extent of the auditor's potential reliance on such work~~ Whether the entity has an internal audit function and if so, whether, in which areas and to what extent, the work of the function can be used for purposes of the audit.

...

ISA 402, *Audit Considerations Relating to an Entity Using a Service Organization*

A1. Information on the nature of the services provided by a service organization may be available from a wide variety of sources, such as:

- User manuals.
- System overviews.
- Technical manuals.
- The contract or service level agreement between the user entity and the service organization.
- Reports by service organizations, the internal auditors function or regulatory authorities on controls at the service organization.
- Reports by the service auditor, including management letters, if available.

ISA 500, *Audit Evidence*

A51. In some cases, the auditor may intend to use information produced by the entity for other audit purposes. For example, the auditor may intend to make use of the entity's performance measures for the purpose of analytical procedures, or to make use of the entity's information produced for monitoring activities, such as ~~internal auditor's reports of the internal audit function~~. In such cases, the appropriateness of the audit evidence obtained is affected by whether the information is sufficiently precise or detailed for the auditor's purposes. For example, performance measures used by management may not be precise enough to detect material misstatements.

Inconsistency in, or Doubts over Reliability of, Audit Evidence (Ref: Para. 11)

A57. Obtaining audit evidence from different sources or of a different nature may indicate that an individual item of audit evidence is not reliable, such as when audit evidence obtained from one source is inconsistent with that obtained from another. This may be the case

when, for example, responses to inquiries of management, internal auditors, and others are inconsistent, or when responses to inquiries of those charged with governance made to corroborate the responses to inquiries of management are inconsistent with the response by management. ISA 230 includes a specific documentation requirement if the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter.⁷

ISA 550, Related Parties

A15. Others within the entity are those considered likely to have knowledge of the entity's related party relationships and transactions, and the entity's controls over such relationships and transactions. These may include, to the extent that they do not form part of management:

- Those charged with governance;
- Personnel in a position to initiate, process, or record transactions that are both significant and outside the entity's normal course of business, and those who supervise or monitor such personnel;
- The internal auditors function;
- In-house legal counsel; and
- The chief ethics officer or equivalent person.

A17. In meeting the ISA 315 (Revised) requirement to obtain an understanding of the control environment,⁸ the auditor may consider features of the control environment relevant to mitigating the risks of material misstatement associated with related party relationships and transactions, such as:

- Internal ethical codes, appropriately communicated to the entity's personnel and enforced, governing the circumstances in which the entity may enter into specific types of related party transactions.

...

- Periodic reviews by the internal auditors function, where applicable.

...

A22. During the audit, the auditor may inspect records or documents that may provide information about related party relationships and transactions, for example:

- Third-party confirmations obtained by the auditor (in addition to bank and legal confirmations).

...

- ~~Internal auditors' r~~ Reports of the internal audit function.

...

ISA 600, Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)

A27. The auditor is required to identify and assess the risks of material misstatement of the financial statements due to fraud, and to design and implement appropriate responses to

⁷ ISA 230, *Audit Documentation*, paragraph 11

⁸ ISA 315 *(Revised)*, paragraph 14

the assessed risks.⁹ Information used to identify the risks of material misstatement of the group financial statements due to fraud may include the following:

- ...
- Responses of those charged with governance of the group, group management, appropriate individuals within the internal audit function (and if considered appropriate, component management, the component auditors, and others) to the group engagement team's *inquiry* whether they have knowledge of any actual, suspected, or alleged fraud affecting a component or the group.
- ...

A51. The group engagement team's decision as to how many components to select in accordance with paragraph 29, which components to select, and the type of work to be performed on the financial information of the individual components selected may be affected by factors such as the following:

- ...
- Whether the internal audit function has performed work at the component and any effect of that work on the group audit.
- ...

Appendix 2

Examples of Matters about Which the Group Engagement Team Obtains an Understanding

The examples provided cover a broad range of matters; however, not all matters are relevant to every group audit engagement and the list of examples is not necessarily complete.

Group-Wide Controls

1. Group-wide controls may include a combination of the following:
 - ...
 - Monitoring of controls, including activities of the internal audit function and self-assessment programs.
 - ...
2. The internal audit function may be regarded as part of group-wide controls, for example, when the ~~internal audit function~~ is centralized. ISA 610 (Revised)¹⁰ deals with the group engagement team's evaluation of the whether the internal audit function's organizational status and relevant policies and procedures adequately supports the competence and objectivity of the internal auditors, the level of competence of the internal audit function, and whether the function applies a systematic and disciplined approach where the group engagement team expects it plans to use their the function's work.

Appendix 5

Required and Additional Matters Included in the Group Engagement Team's Letter of Instruction

Matters that are relevant to the conduct of the work of the component auditor:

- ...

⁹ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

¹⁰ ISA 610 (Revised), *Using the Work of Internal Auditors*, paragraphs 16-17+9

CONFORMING AMENDMENTS TO OTHER ISAs

- The findings of the internal audit function, based on work performed on controls at or relevant to components...

Note: All references to ISA 315 and ISA 610 in other ISAs will be replaced with reference to ISA 315 (Revised) and ISA 610 (Revised) when those standards become effective.



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