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United States Government Accountability Office
Washington, DC 20548

November 1, 2010

International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, New York 10017 USA

Subject: International Auditing and Assurance Standards Board (IAASB) July 2010 Exposure Draft on Proposed International Standards on Auditing (ISA) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment* and ISA 610 (Revised), *Using the Work of Internal Auditors*.

This letter provides the U.S. Government Accountability Office's (GAO) comments on the IAASB's proposed revisions to the ISAs on identifying and assessing the risk of material misstatement and using the work of internal auditors. We agree with the changes made by the Board and we support the proposed standards.

ISA 315

We believe that the proposed revisions to ISA 315 will help clarify the auditor's responsibility with regard to identifying and assessing risks of material misstatements through understanding the entity and its environment. We especially support the IAASB's position of requiring that the auditor inquire of appropriate individuals within the internal audit function as part of the risk assessment process. This will further inform the external auditor's understanding of the entity and its environment, which forms the basis of the risk assessment. Also, it encourages effective communication between the internal auditors and the external auditors which supports an environment in which internal auditors can bring significant matters that may affect the work of the external auditor to the external auditor's attention.

While we support the revisions to ISA 315, we suggest including a section in ISA 315 that addresses special considerations for the audit of public sector entities. This consideration for governmental entities would be referenced to paragraph 6(a) of ISA 315 and would provide important guidance on the broader audit objectives in audits of government entities that use the work of internal auditors. We suggest wording this government consideration as follows:

Considerations Specific to Audits in the Public Sector (Ref: par 6(a))

Auditors of public sector entities often have additional responsibilities with regard to internal control and compliance with applicable laws and regulations. Inquires of appropriate individuals in the internal audit function can assist the auditors in identifying the risk of material noncompliance with applicable laws and regulations and the risk of material deficiencies in internal control over financial reporting.

ISA 610

We support the IAASB's efforts to improve the requirements and guidance on using the work of internal auditors. We believe that internal auditors can assist the external auditors by bringing an objective, systematic, and disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. We also support providing a framework for determining whether and to what extent the internal audit function can be leveraged by the external auditors in assessing audit risk and in obtaining audit evidence. To further improve ISA 610, we offer the following suggestions:

- Paragraphs 2 and 3 state that the ISA does not apply if the external auditor does not plan to use the work of the internal audit function. We suggest modifying paragraphs 2 and 3 to remove the reference to planning to use the work of the internal audit function as opposed to actually using it, since the applicability of the ISA is determined by the auditor's actual use of the work of the internal audit function, regardless of planned actions. Similarly, paragraph 12 discusses the objectives where the external auditor expects to use the work of the internal audit function; this also should be revised to discuss the auditor's actual, rather than expected, use of the internal audit function. The following outlines our suggested changes:

2. ISA 315 addresses the understanding the external auditor obtains of an entity's internal audit function (if the function exists) and inquiries the external auditor makes of internal auditors to obtain information relevant to the external auditor's risk assessment. This ISA addresses the use of the work of the internal audit function when 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. This ISA does not apply if an internal audit function does not exist or the function's responsibilities and activities are not related to the entity's financial reporting. In addition, the external auditor need not apply this ISA if the external auditor does not ~~expect 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.

3. This ISA also addresses the external auditor's responsibilities when using internal auditors to provide direct assistance under the direction and supervision of the external auditor. The requirements relating to

direct assistance do not apply if the external auditor does not ~~plan to~~ obtain the direct assistance of internal auditors. (Ref: Para. A1)

Objectives

12. The objectives of the external auditor, where the entity has an internal audit function and the external auditor ~~expects to~~ uses the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed, are ...

- In addition, we suggest defining applicable terms in the definition section of the ISA instead of in the application material. Specifically, ISA 610 defines objectivity and competence in the application material paragraph A5. To make it easier for the reader to find the definitions of these terms, we suggest moving the definitions to the definitions section of the ISA. This also will ensure that the definitions will be included in the glossary section of the *Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*.

We support the Board in its efforts to revise the ISAs to better reflect the current internal auditing environment and believe that the proposed revisions to ISA 315 and ISA 610 will help improve audit effectiveness by leveraging the work of the internal audit function.

We thank you for considering our comments on these important issues.

Sincerely yours,



James R. Dalkin

Director

Financial Management and Assurance