



**INTERNATIONAL FEDERATION  
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## **Agenda Item**

# **E**

**Committee** IESBA Consultative Advisory Group

**Meeting Location:** Hotel Arts, Barcelona, Spain

**Meeting Date:** March 3, 2010

### **Internal Audit**

#### **Objectives of Agenda Item**

1. To discuss and comment on IESBA view that no modification is required to the Code

#### **Background**

The International Auditing and Assurance Standards Board (IAASB) has a project to revise ISA 610 *Using the Work Of Internal Auditors*. The objective of the project is to “revise [the clarified] ISA 610 to reflect developments in the internal audit environment and changes in practice regarding the interactions between external and internal auditors.”

The Task Force is proposing to expand the scope of ISA 610 to address instances of internal audit staff providing direct assistance to the auditor. Given the linkage with the Code of Ethics, the IAASB extended an invitation to the IESBA to appoint a task force member. The IESBA accepted the invitation and Bob Franchini is a correspondent member on Task Force.

#### **Discussion**

The IAASB Task Force approach with respect to direct assistance is broadly as follows:

- If the external auditor plans to use internal auditors to provide direct assistance, require an evaluation of the level of competence and degree of objectivity of the internal auditors;
- If obtaining direct assistance from internal audits, require the external auditor to direct, supervise and review the work, recognizing that internal auditors are not independent and therefore their work is presumed to provide less reliable evidence.

The Code addresses management responsibilities and states that a firm shall not assume a management responsibility for an audit client (the complete text of the section is contained in the appendix to this agenda paper).

The relevant extracts are as follows:

“It is not possible to specify every activity that is a management responsibility. However, management responsibilities involve leading and directing an entity, including making significant decisions regarding the acquisition, deployment and control of human, financial, physical and intangible resources. Whether an activity is a management responsibility depends on the circumstances and requires the exercise of judgment. Examples of activities that would generally be considered a management responsibility include ... [d]irecting and taking responsibility for the actions of the entity’s employees.”

At its meeting on February 17-18, 2010 the IESBA considered whether the above guidance in the Code is consistent with the proposed revised ISA 620 which would require an external auditor, when obtaining direct assistance from internal auditors, to “direct, supervise and review the work performed by internal auditors on the engagement in accordance with ISA 220” and whether any clarification to the Code was necessary.

The IESBA considered the following factors in forming a view as to whether the Code needs to be clarified to indicate that internal audit direct assistance on the audit is not a management responsibility.

*Points indicating no need for clarification*

- The Code does not state that directing and taking responsibility for the actions of an entity’s employees would always be considered a management responsibility. It states that an assessment of whether an activity is a management responsibility depends upon the circumstances and requires the exercise of judgment;
- The external auditor is responsible for the audit, and planning to use internal auditors to provide direct assistance on the engagement does not relieve the external auditor from this responsibility; and
- The external audit is the responsibility of the external auditor - provision of direct assistance by an internal auditor is therefore part of the external audit and cannot be viewed as a management responsibility.

*Points indicating a need for clarification*

- The Code states that directing and taking responsibility for the actions of an entity’s employees would “generally be considered a management responsibility” – without clarification, some readers of the Code might inappropriately interpret this as including situations where the external auditor is obtaining direct assistance from internal audit.

The IESBA concluded that no clarification to the Code was necessary. IESBA members felt that it would be clear to readers of the Code that the directing and supervising internal auditors when providing direct assistance to the external audit would not be considered to be a management responsibility.

**Action requested**

CAG members are asked to consider the description of a management responsibility and its interaction with the provision of direct assistance by an internal auditor.

**Material Presented**

Agenda Paper E

This Agenda Paper

**Action Requested**

1. CAG members are asked to consider the questions posed.

## **Appendix Management Responsibilities**

### *Management Responsibilities*

290.162 Management of an entity performs many activities in managing the entity in the best interests of stakeholders of the entity. It is not possible to specify every activity that is a management responsibility. However, management responsibilities involve leading and directing an entity, including making significant decisions regarding the acquisition, deployment and control of human, financial, physical and intangible resources.

290.163 Whether an activity is a management responsibility depends on the circumstances and requires the exercise of judgment. Examples of activities that would generally be considered a management responsibility include:

- Setting policies and strategic direction;
- Directing and taking responsibility for the actions of the entity's employees;
- Authorizing transactions;
- Deciding which recommendations of the firm or other third parties to implement;
- Taking responsibility for the preparation and fair presentation of the financial statements in accordance with the applicable financial reporting framework; and
- Taking responsibility for designing, implementing and maintaining internal control.

290.164 Activities that are routine and administrative, or involve matters that are insignificant, generally are deemed not to be a management responsibility. For example, executing an insignificant transaction that has been authorized by management or monitoring the dates for filing statutory returns and advising an audit client of those dates is deemed not to be a management responsibility. Further, providing advice and recommendations to assist management in discharging its responsibilities is not assuming a management responsibility.

290.165 If a firm were to assume a management responsibility for an audit client, the threats created would be so significant that no safeguards could reduce the threats to an acceptable level. For example, deciding which recommendations of the firm to implement will create self-review and self-interest threats. Further, assuming a management responsibility creates a familiarity threat because the firm becomes too closely aligned with the views and interests of management. Therefore, the firm shall not assume a management responsibility for an audit client.

290.166 To avoid the risk of assuming a management responsibility when providing non-assurance services to an audit client, the firm shall be satisfied that a member of management is responsible for making the significant judgments and decisions that are the proper responsibility of management, evaluating the results of the service and accepting responsibility for the actions to be taken arising from the results of the service. This reduces the risk of the firm inadvertently making any significant judgments or decisions on behalf of management. The risk is further reduced when the firm gives the client the opportunity to make judgments and decisions based on an objective and transparent analysis and presentation of the issues.