

July 12, 2013

American Institute of Certified Public Accountants  
1211 Avenue of the Americas  
New York, New York 10036-8775 USA

Response e-mailed to shazel@aicpa.org

RE: Response to the Exposure Draft Proposed Statement of Auditing Standards  
SAS No. 122 Using the Work of Internal Auditors

Dear Sir/Madam:

The Institute of Internal Auditors (The IIA) appreciates the opportunity to respond to the subject exposure draft. Our comments are based on a thorough analysis and discussion, utilizing a core team of governance, compliance and audit experts who serve on The IIA's Professional Issues Committee (PIC). These individuals consist of Certified Internal Auditors, Certified Public Accountants, Chartered Accountants, audit executives and professional services firm representatives who have worked in both public accounting and management positions in small, medium and large multinational organizations.

The following are our principal comments regarding the exposure draft. Detailed responses to the questions posed are summarized in Appendix A – Significant Matters and Requests for Specific Comments.

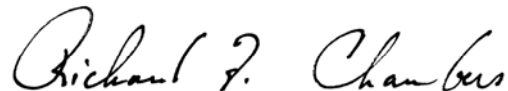
1. The exposure draft seeks to define levels of competence in evaluating the internal audit function. Although several examples are provided in the exposure draft, we suggest that external auditors be required to confirm that an independent Quality Assessment (QA) has been completed as mandated by The IIA's *Standards* to demonstrate the degree and level of competence of the internal audit function. The IIA International Standards for the Professional Practice of Internal Auditing (*Standards*) represents the only internationally recognized standards for internal audit practitioners. Such an assessment would provide the external auditor an independent level of confidence that the work of the internal audit function conforms to such standards.
2. We understand the external audit function must independently perform their work activity, but it does seem the proposed standard overly constricts the work product that can be accepted by the external auditors. In many situations, it can be demonstrated that the internal audit function does have a high degree of independence and therefore, it would seem the external auditors could provide a

higher level of reliance and accept more of the internal audit function's work product.

3. Although the document discusses coordination of external and internal audit activities, it would seem beneficial and more efficient to conduct yearly planning meetings to ensure the most efficient use of both resources. Such planning should occur prior to the internal audit function completing and submitting their annual audit plan to the board audit committee (or other relevant board governance body).
4. The exposure draft does, in our view, require clarification in certain aspects as we outline in our detailed comments in Appendix A. However, notably, clarification seems specifically warranted in the areas of defining evaluation of competency, as well as terminology such as "direct assistance" and "work of the internal auditors."

The IIA is well-equipped to support those AICPA projects that are related to the core competencies of internal auditing: governance, risk management and control. We welcome further discussion on any of our recommendations and offer our assistance in the continued development of SAS No. 122.

Best Regards,

A handwritten signature in cursive script that reads "Richard F. Chambers".

Richard F. Chambers, CIA, CGAP, CCSA, CRMA  
President and Chief Executive Officer

**About The Institute of Internal Auditors**

The IIA is the global voice, acknowledged leader, principal educator, and recognized authority of the internal audit profession and maintains the International Standards for the Professional Practice of Internal Auditing (*Standards*). These principles-based standards are recognized globally and are available in 29 languages. The IIA represents more than 180,000 members across the globe and has 109 affiliates in 190 countries that serve members at the local level.

**Q1. Are the objectives to be achieved by the auditor, stated in the proposed SAS appropriate?**

Yes, however, the phrases “work of internal auditors” and “direct assistance” seem to be used interchangeably in the objectives and throughout the document. We believe the users would have a better understanding if the terminology was consistent. If both terms remain, the SAS should provide a definition of “work of internal auditors” and possibly elaborate on the term “direct assistance.”

**Q2. Are revisions from the existing standards to converge with ISA 610 (Revised 2013) appropriate?**

The objectives require evaluation of the internal audit function to determine level of competency and therefore, reliance on the function. The exposure draft provides tactics to evaluate competence; we offer an additional suggestion. The auditor should consider whether the internal audit function is in compliance with The IIA’s *Standards*. The IIA’s International Professional Practices Framework (IPPF) represents the internationally recognized standards for professional internal auditors. Further, those standards require a QA by a competent, independent evaluator every 5 years, with a report as to whether the internal audit function is in compliance with the *Standards*. We suggest that external auditors request and consider this evidence. Therefore, we propose that the SAS consider including the evaluation of the external assessment required by the *Standards* in paragraphs 7, 14, 15, 22 and 32.

The SAS should make clear what documentation and communications with those charged with governance (TCWG) are required following the evaluation by the external auditor in paragraphs 14 and 15, particularly, when significant deficiencies are found when assessing an internal audit function, as a whole.

**Q3. Are the differences between the proposed SAS and ISA 610 (Revised 2013) identified in the exhibit, and other language changes, appropriate?**

Per the disclosure draft “...The ASB decided to revise paragraph 31 of ISA 610 (Revised 2013) to improve the clarity of the requirement and to eliminate the requirement to explicitly **obtain the agreement** of those charged .....” However, ISA 610 states “reach a mutual understanding” which is not the same as “obtain the agreement.” While external auditors do not generally make agreements with the entity, they should communicate responsibly to obtain a mutual understanding in order to avoid inefficient use of resources.

We suggest incorporating statements in the standard regarding the deleted paragraph 33 to safeguard the impacts to the internal audit function when working for the external auditors for an extended period. Impacts could directly affect the function’s performance evaluation activities such as pay increases, promotions and training.

**Q4. Have considerations for audits of smaller, less complex entities and governmental entities been dealt with appropriately?**

The disclosure draft appears to be written in sufficiently general terms to allow for interpretation for less complex entities and governmental units.

**Q5. Other Comments:**

| Paragraph No. | Comments   |
|---------------|--|
| 6             | More clarification is needed as to who would inform the external auditor? If not the internal auditor, then who else does this imply?  |
| 14            | We would suggest adding evaluation of the QA performed on the internal audit function to the list of external auditor considerations.  |
| 17            | We suggest adding the word “timing” to precede the clause “...nature and scope.”   |
| 18a           | While agreeing the external auditor needs to employ its own judgment, there would seem to be areas of judgment which IA assistance would be warranted, so long as the external auditor has enough information to make its own judgments. Therefore, the concept of “judgment” might be more clearly stated as effective supervision or lack of susceptibility of effective direction, supervision and evaluation, or simply that there is sufficient, competent information/evidence so the external auditor can come to the same conclusion as the internal auditor. Further, the concepts of residual risk or detection risk would enhance paragraph 18.   |
| 18c           | We suggest the following: “The internal audit function does not have sufficient organizational status or policies and procedures to provide for its objectivity.”  |
| 21<br>22      | We suggest adding with whom “...the external audit should discuss the planned...”<br>We suggest the language “review the most recent Quality Assessment as required by The IIA’s <i>Standards</i> ” be added.  |
| 23 and 26     | We propose that the AICPA consider the impact of a competent QA on this paragraph. If the internal audit function has obtained a QA from a competent evaluator and is in compliance with the <i>Standards</i> , these results should be factored into the external auditors’ considerations.<br><br>We believe the terminology “the body of work” is unclear. For example, does it include just the audit documentation or also how the audit was conducted? Does it mean the internal audit function itself or an instance of workpapers? Or, is it broader and refer to the standards the internal audit function uses such as The IIA’s <i>Standards</i> ? Or, does it mean those standards used by the external auditors?<br><br>Also, it seems unclear in the paragraph whether the audit referred to is the internal audit function that is being evaluated or the internal auditor’s work as related to external audit being planned. |
| 24a           | We suggest improving the phrase “the amount of judgment” to clarify whose judgment is being referred to (e.g., external auditor, management, internal auditor).  |

| Paragraph No.                                     | Comments   |
|---|--|
| 30a   | The word “responsive” usually implies someone else to whom the response is directed. In this case, there is no second part: the external auditor evaluates the factors and then plans the nature, timing and extent. The external auditor is responsive to himself? We suggest replacing “responsive” with another word like adequate, commensurate, or aligned.   |
| 32ai  | We suggest the SAS add as 32ai (and subordinate the current I, ii and iii) “the auditor should evaluate the most recent QA.”   |
| 32aiii  | We suggest defining “disciplined approach” in more detail.   |
| <b>Application and Other Explanatory Material</b> |  |
| A7 last bullet                                    | The IIA is the dominant professional body for internal auditors. For the IIA, membership alone does not obligate compliance with the <i>Standards</i> . Internal auditors claiming to be in compliance with the <i>Standards</i> in performing their work are required to comply with the <i>Standards</i> .   |
| A8  | The Certified Internal Auditor and Certification in Risk Management Assurance designations are global professional standards for indicating mastery of the fundamentals of the profession of internal auditing. We recommend adding determination of internal auditor’s competency include consideration of relevant internal auditing certifications.   |
| A8 last bullet                                    | Membership in the professional body of internal auditors does not require continuing professional development. This is required by internal auditing certifications, not membership.   |
| A18   | Where the paragraph discusses “nature and extent”, should timing also be mentioned?  |
| A20   | <p>There seems to be a disconnect between the requirement for seemingly higher level of competence by the internal audit function as a whole and a lower level of competence by those internal auditors who can adequately perform work for the external audit without their significant judgments. We suggest that clarification is needed.</p> <p>Also, it seems there are many concepts stated in one sentence. Examples include: Who assesses the risk of material misstatement at the assertion level? Who plans and evaluates the IA’s work? Who is the owner of the detection risk for testing performed by the IA? We suggest breaking up this sentence into separate parts.</p> |
| A22   | The phrase “the external auditor will need to perform more procedures” implies re-doing work. To improve effectiveness of the external auditor’s use of the internal audit function, there is a need for the mechanism that controls or eliminates duplication of planning effort, resolves disagreements in assessment of materiality at the assertion level, and establishes agreed-upon restrictions on the internal auditor’s judgments.   |

| <b>Paragraph No.</b> | <b>Comments</b>  |
|----------------------|--|
|                      | <p>Also, the phrase “therefore, the external auditor will need to perform more of the work directly” is unclear as to the manner in which the conclusion is made. The external auditor may simply need to increase sample sizes in the testing plan to achieve higher precision. The internal audit function may have to provide more resources to test larger samples designed by the external auditor.</p> <p>Both of the above should be clarified further.</p> |
| A27                  | Clarify the phrase “may affect the function”, as relating to the internal audit function.  |
| <b>Appendix A</b>    |  |
| A9                   | The findings previously reported by the internal audit function are more likely to have been resolved by the time of the external auditor’s inquiry. Accordingly, the external auditor should consider the current status of findings.   |
| .A13                 | Does the phrase “risk of deficiencies” mean the risk of material misstatement due to significant deficiencies? If so, then we suggest clarifying.  |
| .A96                 | The risk assessments by the group auditors are typically not provided to the component auditor, so this requirement may be unreasonable without the requirement to supply the component auditor with the group risk assessment information.  |