

## **Exposure Draft**

# **(Revised) Preface to the Standards and Guidance Notes on Internal Audit**

*The Committee on Internal Audit of the Institute of Chartered Accountants of India invites comments on the Exposure Draft of the Revised Preface to the Standards and Guidance Notes on Internal Audit. Comments are most helpful if they indicate the specific paragraph(s) to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.*

*Comments should be submitted in writing to the Secretary, Committee on Internal Audit, The Institute of Chartered Accountants of India, C-1, Sector-1, NOIDA-201 301 so as to be received not later than **November 17, 2006**. Comments can also be sent by e-mail at **[cia@icai.org](mailto:cia@icai.org)**.*

### **1. Formation of the Committee on Internal Audit**

The Institute of Chartered Accountants of India constituted the Committee on Internal Audit (CIA) on 5<sup>th</sup> February 2004.

### **2. Scope and Functions of the Committee on Internal Audit**

2.1 A large number of the members of the Institute are involved in carrying out internal audit engagements. The Institute has, from time to time, issued general and industry specific guidelines on internal audit practices for the guidance of the members. However, till date, no formal standards on internal audit under the authority of the Council have been issued. The main function of the Committee on Internal Audit would be to review the existing internal audit practices in India and to develop Standards on Internal Audit (SIAs). The SIAs would aim to codify the best practices in the area of internal audit and would also serve to provide a benchmark of the performance of the internal audit services. The SIAs would be issued under the authority of the Council.

2.2 While formulating the SIAs, the Committee will take into consideration the applicable

laws, customs, usages and business environment and auditing practices in India. The Committee may also, where it considers appropriate, take into consideration the international practices in the area of internal audit, to the extent they are relevant to the conditions existing in India.

2.3 The Committee on Internal Audit will develop Guidance Notes on internal audit, including those on issues arising from the Standards on Internal Audit. These Guidance Notes will be issued under the authority of the Council of the Institute.

2.4 The Committee on Internal Audit will also formulate Clarifications on issues arising from SIAs. These Clarifications will also be issued under the authority of the Council.

### **3. Scope of the Standards on Internal Audit**

3.1 ~~The Standards on Internal Audit will apply whenever an internal audit is carried out.~~ Internal audit is an independent management function, which involves a continuous and critical appraisal of the functioning of an entity with a view to suggest improvements thereto and add value to and strengthen the overall governance mechanism of the entity,

including the entity's strategic risk management and internal control system.

~~3.2 Any limitation in the applicability of a specific Standard on Internal Audit will be made clear in the introductory paragraph of the Standard.~~

#### 4. Procedure for Issuing the Standards on Internal Audit

Broadly, the following procedure will be adopted for issuing Standards on Internal Audit:

- 4.1 The Committee on Internal Audit will identify the broad areas in which the SIAs need to be formulated and the priority in regard to selection thereof.
- 4.2 In the preparation of the SIAs, the Committee will be assisted by Study Groups constituted to consider specific subjects. In the formation of the Study Groups, provision will be made for participation of a cross section of members of the Institute. In situations considered necessary, the Committee may also consider having an expert on such Study Groups, subject to such terms and conditions, as may be finalised by the Committee. The expert need not necessarily be a member of the Institute of Chartered Accountants of India. The Study Group will be responsible for preparing the draft of the Standard.
- 4.3 The above mentioned draft Standard would be considered by the Committee. On the basis of the deliberations of the Committee on the draft Standard, an Exposure Draft of the proposed Standard will be prepared by the Committee and issued for comments by the members of the Institute. The Exposure Draft will also be open for comments by non-members.
- 4.4 The abovementioned Exposure Draft will be published in the Journal of the Institute and will also be hosted on the website of the Institute under appropriate head.
- 4.5 The Exposure Draft will normally remain open for comments for a period of at least forty five days from the date of issuance.
- 4.6 The above mentioned Exposure Draft will be circulated to all the Council members, Regional Councils, Branches, Outside Chapters and Past Presidents of the Institute for their comments. The Exposure Draft will also be circulated to the following bodies, as may be necessary on a case to case basis, for their comments:
- (i.) The Ministry of Company Affairs
  - ~~(i.)~~(ii.) The Reserve Bank of India
  - ~~(ii.)~~(iii.) The Securities and Exchange Board of India
  - ~~(iii.)~~(iv.) Insurance Regulatory and Development Authority
  - ~~(iv.)~~(v.) The Comptroller & Auditor General of India
  - ~~(v.)~~ ~~The Department of Company Affairs~~
  - (vi.) The Central Board of Direct Taxes
  - (vii.) The Institute of Cost and Works Accountants of India
  - (viii.) The Institute of Company Secretaries of India
  - (ix.) The Associated Chambers of Commerce & Industry
  - (x.) The Federation of Indian Chambers of Commerce & Industry
  - (xi.) The Confederation of Indian Industry
  - (xii.) The Indian Banks' Association
  - (xiii.) The Foreign Exchange Dealers' Association of India
  - (xiv.) The Standing Conference of Public Enterprises
  - (xv.) All recognised Stock Exchanges in India
  - (xvi.) The Competition Commission of India

- (xvii.) The National Bank for Agricultural and Rural Development
- (xviii.) The Controller General of Accounts
- (xix.) The Ministry of Finance – Insurance and Banking Divisions
- (xx.) The Indian Institute of Management, Ahmedabad, Bangalore, Kolkata, Indore, Kochi and Lucknow
- (xxi.) The Central Registrar of Cooperative Societies, Ministry of Agriculture, Government of India
- (xxii.) The Bombay Mercantile Association

The Committee may, however, in addition to the bodies listed above, circulate the Exposure Draft for comments to such other bodies also, as considered appropriate by it.

- 4.7 After taking into consideration the comments received on the Exposure Draft, the draft of the proposed Standard will be finalised by the Committee and submitted for the consideration of the Council of the Institute.
- 4.8 The Council of the Institute will consider the final draft of the proposed Standard on Internal Audit and if necessary, modify the same in consultation with the Committee on Internal Audit. The SIA will then be issued under the authority of the Council.
- 4.9 For a substantive revision of a Standard on Internal Audit, the procedure followed for formulation of a new Standard on Internal Audit, as detailed in paragraphs 4.1 through 4.8 will be followed.
- 4.10 Subsequent to the issuance of a Standard on Internal Audit, some aspect(s) may require revision which are not substantive in nature. For this purpose, the Institute of Chartered Accountants of India may make limited revision to a Standard on Internal Audit. The procedure followed for the limited revision will substantially be the same as that to be followed for formulation of a Standards on Internal Audit, ensuring that

sufficient opportunity is given to various interest groups and general public to react to the proposal for limited revision.

## 5. Procedure for Issuing the Guidance Notes on Internal Audit

Broadly, the following procedure will be adopted for issuing Guidance Notes on internal audit:

- 5.1 The Committee will identify the issues on which Guidance Notes need to be formulated and the priority in regard to selection thereof.
- 5.2 In the preparation of the Guidance Notes, the Committee will be assisted by Study Groups constituted to consider specific subjects. In the formation of the Study Groups, provision will be made for participation of a cross section of members of the Institute. In situations considered necessary, the Committee may also consider having an expert on such Study Groups, subject to such terms and conditions, as may be finalised by the Committee. Such expert need not necessarily be a member of the Institute of Chartered Accountants of India. The Study Group will be responsible for preparing the draft of the Guidance Note.
- 5.3 The above mentioned draft Guidance Note would be considered by the Committee. On the basis of the deliberations of the Committee on the draft Guidance Note, the draft of the proposed Guidance Note will be finalised by the Committee and submitted for the consideration of the Council of the Institute.

Unlike Standards on Internal Audit, ordinarily, no proposed Guidance Note will be required to be exposed for comments of the members and others. However, in situations considered necessary by the Committee, an Exposure Draft of a Guidance Note may as well be issued for comments. In case an Exposure Draft of a Guidance Note is issued, the same procedures as required for an Exposure Draft of an SIA

(listed in paragraphs 4.3 through 4.8 above) will be required to be followed.

5.4 The Council of the Institute will consider the final draft of the proposed Guidance Note and, if necessary, modify the same in consultation with the Committee on Internal Audit. The Guidance Note will then be issued under the authority of the Council.

## 6. Compliance with the Standards and Guidance Notes on Internal Audit

6.1 The Standards on Internal Audit shall apply whenever an internal audit, whether in house or outsourced, is carried out. The SIA(s) will be mandatory from the respective dates(s) mentioned in the SIA(s). However, any limitation in the applicability of a specific Standard shall be made clear in the Standard. The mandatory status of a Standard on Internal Audit implies that ~~While~~ carrying out an internal audit, it will be the duty of the members of the Institute to ensure that the SIAs are followed. If, for any reason, a member has not been able

to perform all or any of such activities, as mentioned before, in accordance with the SIAs, his report should draw attention to the material departures therefrom.

6.2 Guidance Notes on internal audit are primarily designed to provide guidance to the members on matters which may arise in the course of their professional work and on which they may desire assistance in resolving issues which may pose difficulty. The Guidance Notes on internal audit will be recommendatory in nature. A member should, ordinarily, follow recommendations in a Guidance Note on internal audit except where he is satisfied that in the circumstances of the case, it may not be necessary to do so.

## 7. Effective Date

~~The Standards on Internal Audit shall be effective in respect of the internal audits commencing on or after the date specified in the respective Standards. Members will be expected to follow SIAs in the internal audits commencing on or after the date(s) specified in the Standard.~~

## Exposure Draft

# Standard on Internal Audit (SIA) Documentation

*The Committee on Internal Audit of the Institute of Chartered Accountants of India invites comments on the Exposure Draft of the Standard on Internal Audit (SIA). Comments are most helpful if they indicate the specific paragraph(s) to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.*

*Comments should be submitted in writing to the Secretary, Committee on Internal Audit, The Institute of Chartered Accountants of India, C-1, Sector-1, NOIDA-201 301 so as to be received not later than **November 17, 2006**. Comments can also be sent by e-mail at [cia@icai.org](mailto:cia@icai.org).*

## Introduction

1. The purpose of this Standard on Internal Audit (SIA) is to establish Standards and provide guidance on the documentation requirements in an internal audit.
2. Paragraph 10 of the Standard on Internal Audit (SIA) 2, states as follows:

***“10. The internal auditor should document matters, which are important in providing evidence that the audit was carried out in accordance with the Standards on Internal Audit and support his findings or the report submitted by him. In addition, the working papers also help in properly planning and performing the internal audit, review and***

*supervise the work and most importantly, provide evidence of the work performed to support his opinion or findings."*

## Definitions

3. "Audit documentation" means the record of audit procedures performed, including audit planning as discussed in the Standard on Internal Audit (SIA) 1, Planning an Internal Audit, relevant audit evidence obtained, and conclusions the auditor reached (terms such as "working papers" or "workpapers" are also sometimes used). Thus, documentation refers to the working papers prepared or obtained by the internal auditor and retained by him in connection with the performance of his audit.

*"Experienced internal auditor"* means an individual (whether internal or external to the entity) who has a reasonable understanding of (i) internal audit processes, (ii) SIAs, other relevant pronouncements of the Institute and applicable legal and regulatory requirements, (iii) the business environment in which the entity operates, and (iv) internal audit issues relevant to the entity's industry.

4. Working papers:
  - ❖ Aid in planning and performing the internal audit.
  - ❖ Aid in supervision and review of the internal audit work.
  - ❖ Provide evidence of the internal audit work performed to support the internal auditor's findings and opinion.
  - ❖ Aids in third party reviews, where so done
  - ❖ Provide evidence of the fact that the internal audit was performed in accordance with the SIAs and other relevant pronouncements issued by the Institute of Chartered Accountants of India.

## Form and Content

5. Audit documentation may be recorded

on paper or on electronic or other media. It includes, for example, audit programmes, analyses, issues memoranda, summaries of significant matters, letters of confirmation and representation, checklists and correspondence (including e-mail) concerning significant matters. Abstracts or copies of the entity's records, for example, significant and specific contracts and agreements, may be included as part of audit documentation if considered appropriate. Audit documentation, however, is not a substitute for the entity's accounting records. The audit documentation for a specific audit engagement is assembled in an audit file.

6. **Working papers should record the internal audit charter, the internal audit plan, the nature, timing and extent of auditing procedures performed, and the conclusions drawn from the evidence obtained.**
7. **Working papers should be designed and properly organised to meet the circumstances of each audit and the internal auditor's needs in respect thereof. The internal auditor should formulate policies that help in standardization of the internal auditor's working papers.** The standardization may be in the form of checklists, specimen letters, questionnaires, etc.
8. **Working papers should be sufficiently complete and detailed for an internal auditor to obtain an overall understanding of the audit.** The extent of documentation is a matter of professional judgment since it is neither practical nor possible to document every observation, finding or conclusion in the working papers. **All significant matter which require exercise of judgment, together with the internal auditor's conclusion thereon should be included in the working papers. However, the documentation prepared by the internal auditor should be such that enables an experienced internal auditor,**

having no previous connection with the internal audit to understand:

- (a) the nature, timing, and extent of the audit procedures performed to comply with ISAs and applicable legal and regulatory requirements;
- (b) the results of the audit procedures and the audit evidence obtained; and
- (c) significant matters arising during the audit and the conclusions reached thereon.

9. The form, extent and contents of the documentation would also be affected by the nature and terms of the engagement, and any statutory or regulatory requirements in that regard. The form, content and extent of audit documentation depend on factors such as:

- The nature of the audit procedures to be performed;
- The identified risks of material misstatement;
- The extent of judgment required in performing the work and evaluating the results;
- The significance of the audit evidence obtained;
- The nature and extent of exceptions identified;
- The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained; and
- The audit methodology and tools used.

It is, however, neither necessary nor practicable to document every matter the auditor considers during the audit.

10. **The working papers should cover all the important aspects of an engagement viz., engagement acceptance, engage-**

**ment planning, risk assessment and assessment of internal controls, evidence obtained and examination/ evaluation carried out, review of the findings, communication and reporting and follow up.**

The working papers would, therefore, generally, include:

- Engagement letter
- Internal audit plan and programme
- Papers relating to the staff requirement and allocation
- Papers relating to requirements for technical experts, if any
- Time and cost budgets
- Copies of significant contracts and agreements or management representations on terms and conditions of those contracts
- Internal review reports
- Evaluation questionnaires, checklists, flowcharts, etc.
- Papers relating to discussions/ interviews with the various personnel, etc.
- Chart of the organizational structure and job profile of the persons listed in the chart
- Reconciliation statements
- Communication with the client personnel and third parties, if any
- Results of risk and internal control assessments
- Analytical procedures performed and results thereof
- Final report issued
- Records as to the follow up on the recommendations/ findings contained in the report

### Identification of the Preparer and the Reviewer

11. It is also essential that the working papers

identify the following:

- (i) who performed that task and the date such work was completed;
- (ii) who reviewed the task performed and the date and extent of such review;
- (iii) reasons for creating that working paper;
- (iv) source of the information contained in the working paper; and
- (v) any cross referencing to any other working paper(s).

The preparers and reviewers of the working papers should also sign them.

12. **The internal audit file should be assembled within sixty days after the signing of the report.** Since assembly of the working papers file is only an administrative process and does not involve performance of any new audit procedures or formulation of new conclusions. Changes may be made to the audit documentation file only if such changes are administrative in nature. For example:

- deleting or discarding superceded documentation
- sorting, collating and cross referencing working papers
- signing off on completion checklists relating to file assembly process
- documenting audit evidence that the internal auditor has obtained, discussed and agreed with the relevant members of the internal audit team before the date of the internal auditor's report

After the assembly of the audit file, the internal auditor should not delete or discard audit documentation before the end of the retention period.

13. **When exceptional circumstances arise after the date of the submission of**

**the internal audit report that require the internal auditor to perform new or additional audit procedures or that lead the internal auditor to reach new conclusions, the auditor should document:**

- (i) **the circumstances encountered;**
- (ii) **the new or additional audit procedures performed, audit evidence obtained, and conclusions reached; and**
- (iii) **when and by whom the resulting changes to the audit documentation were made, and (where applicable) reviewed.**

### Document Retention and Access

14. **The internal auditor should formulate policies as to the custody and retention of the working papers within the framework of the overall policy of the entity in relation to the retention of documents.**

While formulating the documentation retention policy, any legal or regulatory requirements in this regard should also be taken into consideration. Management and other designated personnel may seek access to the working papers of the internal audit department subject to the approval of the internal auditor.

15. Where the internal audit or any part thereof is outsourced to a firm of chartered accountants, such firm retains the ownership of the working papers. The firm may provide copies of the working papers to the client or such other third party if there is any legal or regulatory requirement or as may be permitted by the client.

### Effective Date

16. This Standard on Internal Audit will apply to all internal audits commencing on or after .....