

TCASP

INTERNAL AUDIT

CMAs' Role in INTERNAL AUDITING

by
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INTERNAL AUDIT



PURPOSE & PROCESS


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INTERNAL AUDIT

The Purpose of Internal Auditing?

- "Eyes and Ears"
- "Policeman"
- "Watchdog"
- "Consultant"
- "Catalyst"



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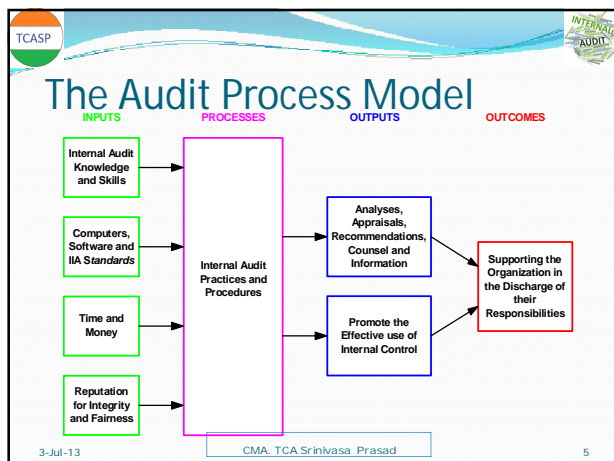
INTERNAL AUDIT

IIA Statement of Responsibilities

Purpose:

- Internal auditing is an **independent appraisal** function established within an organization to examine and evaluate its activities **as a service** to the organization.
- The objective of internal auditing is **to assist members of the organization** in the effective discharge of their responsibilities.
- The audit objective includes **promoting control at a reasonable cost**.

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IIA Statement of Responsibilities

Scope:

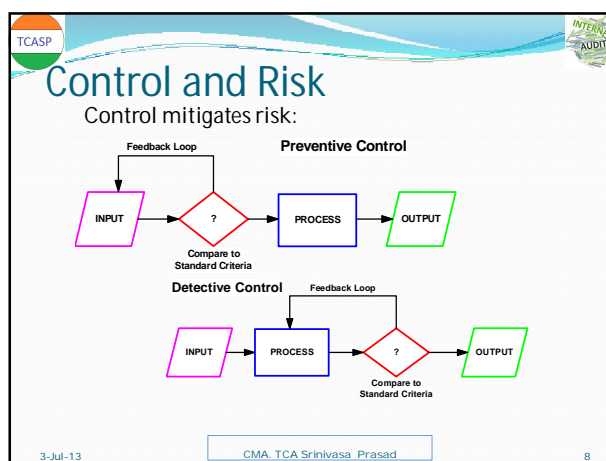
- The scope of internal auditing should encompass the examination of the **adequacy and effectiveness** of the organization's system of internal control **and the quality of performance** in carrying out assigned responsibilities.
- Assessment** (adequacy and effectiveness).
- Enhancement** (measuring performance quality improvement).

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The Nature of Business Risk

Risk is a concept used by auditors and managers to express concerns about the probable effects of an uncertain environment.

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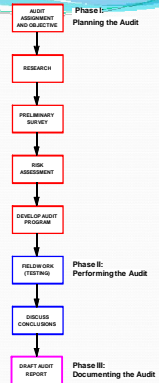
PLANNING PERFORMING & REPORTING

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Internal Audit Framework

- Planning
- Performing
- Reporting




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Establishing Audit Objective and Scope

- Ensure a positive link between the audit objective and the entity's goals.
- Ensure the audit program will produce the evidence as required.
- Ensure that each test will provide the evidence required by the audit program.

Linking the Audit to the Business Plan



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Planning the Audit

- Research
- Risk Assessment
- Audit Strategy
- Preliminary Survey
 - Policies and Procedures
 - Inputs and Outputs
 - Control Steps
 - People





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Audit Plans

1. Scope and objectives.
2. Auditors.
3. Activity schedule.
4. Relevant Standard's sections.
5. Past audits and other documents

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Planning Step #1

Perform Research on Area under Audit

Research is important for understanding, but we must be able to recognize when "enough is enough"

Research tells us define the historical issues, current issues, marketing issues, pervasive risks, personnel issues, and future issues.

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Planning Step #2

Prepare Your Hypothesis

1. The activity is operating normally
What is = What should Be
2. The activity is not operating as it should in some significant way
What is does not = What should be
3. Some value in between
There are minor differences between What is and What should be

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Planning Step #3

Send Engagement Memo

1. To executive management
2. Include the name of the audit effort and the initiation date
3. Request the name of a contact person

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Designing Audit Tests

- Evidence is created from tests or questions.
- The creation of the right test or question to ask is a process of working backwards from the audit objective.

A Logical Sequence: From Tests to Objective

```

graph LR
    A[Tests: What creates the evidence (y/n)?] --> B[Evidence: What proves the hypothesis?]
    B --> C[Hypothesis: What do you want to prove?]
    C --> D[Audit Objective]
  
```

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Documenting the Audit

Automated Work Papers provide

- A framework to guide the audit process.
- Support for the conclusions reached by the audit.
- A record of the audit process and its conformance to standards.

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Work Papers – Good Practices

- Use electronic templates to capture data:
 - * Background & Scope Document
 - * Risk
 - * Control
 - * Test
 - * Audit Point Sheet
- Structure your work paper documents as carefully as you would the final audit report.

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A Framework for the Audit

1. Audit Strategy/ Audit Scope & Objective.
2. Creation of Risk Based Work Papers
3. Collection of basic reference materials (flow charts, etc.)
4. Determination of tests needed
5. Sample Design
6. Preparation of meeting agendas
7. Follow-up on information gleaned/re-direction
8. Documentation of test results and conclusions.
9. Creation of Audit Point Sheets.
10. Audit Report

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Writing Up Conclusions

Best practices include:

- Test description or question.
- Results (clearly stated).
- Conclusion reached as a result of that test.

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Best Practices (cont)

- Discussion of the conclusion with management.
 - To avoid misunderstandings.
 - To give management a 'heads-up' about issues.
 - To encourage corrective action as soon as possible.
- Cross-reference the audit point sheets to the conclusions in the audit work papers (and back-reference the conclusions to the report).

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Summarizing and Evaluating Results

- The audit process creates evidence.

The Logical Results: From Tests to Findings

```


graph LR
    Test[Test: Creates the evidence.] --> Evidence[Evidence: Provides factual information.]
    Evidence --> Conclusion[Conclusion: Puts the facts in context (impact).]
    Conclusion --> Finding[FINDING]
  
```

- Evidence is summarized into conclusions.
- Evidence (facts) + Context (impact) = Finding

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The Audit Point Sheet

- Ensures all aspects of problems (findings) are captured.
- Useful as ready documentation.
- Serves as a basis for discussion.
- Aids the summarization and report writing.



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Writing Effective Audit Reports

Reports are important because they:

- Provide documented communication and assurance to senior management.
- Provide operating management with assessments of operations and corrective action.
- Provide the auditor with records for follow-up of audit results.
- Provide the audit group with marketing opportunities to demonstrate added value.

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Audit Report Structure

1. Audit purpose, objective, & scope
2. Auditors, dates, auditee.
3. Observations & supporting evidence
4. Recommendations for improvements.
5. Recommendations for follow-up audit of corrective actions.

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Principles of Audit Reporting

- Don't overstate facts.
- Performance vs. documentation.
- Avoid generalities.
- Communicate exception specifics.
- Avoid extreme language.
- Spell things out.
- Don't focus on individuals.
- Provide policy references.

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FOLLOW UP & INTERACTIONS

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Following Up – Corrective Actions

The control aspect of auditing is not complete until corrective action is taken (or the risk formally assumed by senior management).

Effective statements of corrective action include:

- The specific steps to be taken,
- The completion date and
- The person responsible for completion.

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Audit Interaction with Auditee

The diagram illustrates three models of audit interaction with an auditee (Internal Audit):

- Competition:** Shows an Auditor and a Manager with red arrows pointing away from each other, indicating a competitive relationship. The Internal Audit box is below the Manager.
- Cooperation:** Shows an Auditor and a Manager with blue arrows pointing towards each other, indicating a cooperative relationship. The Internal Audit box is below the Manager.
- Collaboration:** Shows an Auditor and a Manager with a pink arrow pointing from the Auditor to the Manager, indicating a collaborative relationship. The Internal Audit box is below the Manager.

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Building Trust with Auditee

- The slow way- Making and keeping commitments
- The faster way - Collaboration.

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ASSUMPTIONS & RESPONSIBILITIES



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Basic Auditing Assumptions

1. Auditors are qualified
2. Quality system exists.
3. Adequate resources and support.
4. Evidential material.
5. Formally reported results .
6. Follow-up audits.
7. Audit's Quality assurance.


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Audit Definitions

Assessment
Audit
Auditee
Auditor
Exception
Finding
Observation
Verification



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Auditor Responsibilities

1. Comply with audit standards.
2. Implement audit effectively & efficiently.
3. Report observations to Auditee A.S.A.P.
4. Maintain independence.
5. Assist with the audit report.



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Auditee Responsibilities

1. Appoint person to accompany auditor.
2. Access to facilities and evidence
3. Adequate working area.
4. Attend meetings.
5. Review report.
6. Take corrective action A.S.A.P.

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Audit Quality Assurance

1. Validity
2. Correctness
3. Absence of bias
4. Report's information usefulness.



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Auditor Qualification

- Knowledge
- Skill
- Personality
- Experience
- Examination & Certification
- Independence



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Audit Working Papers

1. What you did
2. What you found.
3. What you concluded.

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Suggested Working Paper Techniques

- New topics on a new page.
- 2 in. margin from the top & left sides.
- Copies of documents.
- Initial, date and number each page.
- Cross reference to procedure.
- Interim conclusions.
- List of findings, observations, and exceptions.



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Lead Auditor Responsibilities

- Select & assign team members.
- Distribute background data.
- Audit notification.
- Conduct audit planning meeting.
- Lead audit opening meeting.
- Review audit status & findings with team.
- Periodic feedback to auditee.
- Prepare & issue report.

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Audit Interview Tips

1. Organize your thoughts.
2. General sequence of questions.
3. Right setting.
4. Interviewee does most of the talking.
5. Take discrete notes.
6. Summarize your understanding.



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Techniques for Understanding Quality Management Systems

- Interviews
- Document Review
- Observation
- Limited Verification Testing

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Auditor Attributes

- Skills
- Traits
 - Good communicator
 - Tactful
 - Flexible
 - Persistent
 - Objective
 - Integrity



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Inquiry Categories

- Definition of responsibilities
- Delegation of responsibilities & authorities
- Personnel training and experience
- Documentation
- Protective measures
- Internal verification



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Interview Considerations

- Attitude and approach
- Setting
- Non-verbal communication
- Types of questions


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Interview Don'ts

- Debate with interviewee.
- Be insensitive.
- Criticise people.
- Ask leading, tricky questions.
- Be nit-picky.
- Divulge thoughts about audit outcome
- Fail to test conclusions.



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Cast of Characters

1. External Standards' Organizations
2. Divisional HQ
3. Local Management Team
4. Audit Committee
5. Department Managers
6. Supervisors
7. Employees



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Process Requirements

- Business Process
 - Objectives & Targets
 - With what?
 - With whom?
 - Inputs
 - Outputs
 - How many?
 - How?
 - Linked to what other processes?



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Process Audit

- Plan (what do we want to accomplish?)
- Do (are we implementing our plans?)
- Check (do we evaluate our progress?)
- Act (do we take action based on the results?)



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Sampling

- Take the appropriate amount
 - Don't enlarge sample when nothing found
 - Enlarge sample if something found
 - To enable clear & complete reporting



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Gathering Information

- Stay on track
- Agree on the facts
- Remain objective
- Select samples randomly



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Non-conformities

- Failure to meet specified requirement
 - ISO 9001-2000
 - Customer's contracts, specs, etc.
 - Company SOP's or Work Instructions
 - Some more serious than others
 - Risk of occurrence
 - Impact of occurrence



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Reporting's 5 C's

- Clear
- Correct
- Complete
- Concise
- Checked


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Reporting Non-conformities

1. Source of the requirement
2. Requirement summary
3. Source of the evidence
4. Summary of the evidence



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Audit Evolution



<ul style="list-style-type: none"> • Old Way evaluates <ul style="list-style-type: none"> • Organization • SOP's • Manuals • Documentation • Compliance 	<ul style="list-style-type: none"> • New Way evaluates <ul style="list-style-type: none"> • Availability of process data • Training efforts • Teamwork • Customer awareness • Quality cost analysis • Customer & Supplier involvement
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Case Study



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VISION

Best practice Internal Audit Department in the Public Service that adds value to achievement of goals

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STRUCTURE

- The department operates administratively under CEO and reports functionally to the Board through the Audit Committee.



It has two major sections

- Risk Management and
- Internal Audit.

Two subsections under Internal audit

- Finance and Operations Audit and
- Information Technology Audit

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DEFINITION OF INTERNAL AUDIT

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations.

- It helps an organization accomplish its objectives through a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.



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OVERALL ROLE IN THE ORGANISATION

- Internal Audit Department assists the Board in its oversight responsibility and works with management to provide assurance in three key areas:
- Risk Management
- Internal Control Systems,
- Governance.



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INTERNAL AUDIT GUIDES

- Audit Committee Charter
- Audit Department Charter
- Risk Management Policy Framework
- Internal Audit Manual
- Public Audit Act 2003
- Treasury circulars on audit committees
- Treasury Circular on Risk Management



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PURPOSE

- The main objective of the internal audit activity is to determine whether the Organisation's network of risk management, control, and governance processes, as designed and represented by the management, is adequate and functioning in a manner to ensure:
- Risks are appropriately identified and managed
- Interaction between various governance processes occurs as needed
- Accurate, reliable and timely financial and managerial information.
- Compliance with policies, standards, procedures, laws and regulations
- Resources are acquired economically, used efficiently, and are adequately protected (safeguarded)
- Objectives are achieved
- Requirements and agreements with funding partners are met
- Legislative or regulatory issues impacting on the Organisation are recognized and addressed properly



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SCOPE OF INTERNAL AUDIT

- Monitoring risk management framework
- Review governance processes
- Policies, plans, procedures, laws and regulations for compliance
- Confirm Reliability and integrity of financial and operating information
- Systems established to ensure proper design & compliance
- Safeguarding assets include existence, ownership, protection, use
- Value for money - economy, efficiency and effectiveness
- Operations and programs for achievement of objectives



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RESPONSIBILITIES OF INTERNAL AUDIT

- Conduct work in accordance with the Standards for the Professional Practice of Internal Auditing and Code of Ethics.
- Develop and execute an annual workplan
- Hold audit entry meetings
- Execute the annual workplan
- Hold exit meetings
- Provide management with a preliminary written report
- Provide management with a final written report
- Follow up on management's responses and actions
- Share efforts with external auditors and regulatory agencies where requested
- Follow up on all external auditors' or regulatory reports and recommendations.
- Investigate known or suspected acts of fraud
- Conduct special reviews or studies as requested by the Board or the Audit Committee.
- Meet with the Audit Committee at least quarterly



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RESPONSIBILITIES OF MANAGEMENT

- The internal audit review and appraisal of processes does not in any way relieve other persons in the organization of the responsibilities assigned to them.
- Responsibility for designing, complying with policies and procedures as well as correcting deficiencies rests with the respective administrators and management.



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SPECIFIC MANAGEMENT RESPONSIBILITIES

- Provide the Internal Audit staff with full support and cooperation at all levels of operations.
- Provide the Internal Audit staff complete access to all records, property and personnel relative to the performance of their duties and responsibilities.
- Ensure the Internal Audit Department has an adequate budget and staffing to perform its responsibilities.
- Provide a written response to all Internal Audit reports submitted.
- Put in place a mechanism for tracking implementation of actions stated in the responses.
- Promptly inform the Internal Audit staff of known or suspected cases of a criminal nature involving Organization funds, property and employees.
- Annually review and revise the Internal Audit Charter as necessary.

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AUTHORITY AUDITORS HAVE



- Unrestricted access to all functions, records, property, and personnel with stringent regard for safekeeping and confidentiality.
- Access to records of all partners as well as third parties to KNBS
- Access to contracted third parties as per contractual terms.
- Full and free access to the Audit Committee.
- Allocate resources applicable to Internal Audit Department, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish audit objectives.
- Obtain the necessary assistance of personnel in units of the organization where they perform audits, as well as other specialized services from within or outside the organization.

NOTE

- Documents and information given to Internal Audit will be handled in the same prudent manner as by those employees normally accountable for them.

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AUTHORITY AUDITORS DON'T HAVE

- Perform any operational duties for the organization or its partners.
- Initiate or approve accounting transactions external to the internal auditing department.
- Direct the activities of any organization employee not employed by the internal audit unit, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.

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THANK YOU

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