

# State of the Internal Auditing Profession

*Presented by:*

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# Agenda

- What should Internal Auditors do?
- How can we Assess Internal Auditing Performance?
- How can The IIA help?



## Definition of Internal Auditing:

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 by bringing a *systematic and disciplined approach to evaluate and improve* the effectiveness of the *risk management, control and governance processes*.

(Approved by the Board of Directors 6/26/99)

# What do Internal Auditors Do?

- Help solve problems
- Confirm accuracy of information
- Ensure assets are properly safeguarded
- Confirm compliance to laws and regulations
- Help improve the effectiveness and efficiency of processes
- Investigate fraud situations
- Provide a resource for skills

# What are our Constituents saying about us?

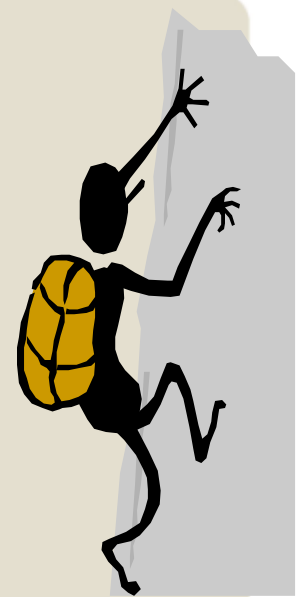
- Communication needs improvement (AC, Mgt, EA)
- Focus needs better alignment
- Resources/skills need assessment
- Top areas for attention: control, risk, fraud, IT
- Assessment of results presentation

# Emerging Trends

- IAD involvement in ERM implementation
- Forensic Auditing
- Fraud prevention & detection
- Ethics hot lines
- Financial statement control assessment
- Total control assessment (operational, financial, & compliance)

# Emerging Trends

- Longer term audit plans
- IAD Quality Assurance reviews
- Customer focus and involvement
- Entity – wide control component assessments (COSO framework)
- Enhanced staff qualifications



# Emerging Trends

- Governance involvement
- Assisting audit committee with their changing responsibilities
- “Balance” of IAD Work
- Auditors as consultants
- Use of Risk Assessment in audits
- Use of third party providers



# Emerging Trends

- Strategic plans for IAD
- Meeting results expectations  
(KPI's & performance goals)
- Technology auditing and use by IAD
- Compliance programs

# Role of IA Today

- **Risk**
- Control
- Governance

So what are you doing?

# Risk

- Knowledge
- Use
- Reporting
- Audit Committee and risk
- ERM and IA

# Core Roles for IA on ERM

- Giving assurance on risk management processes.
- Giving assurance that risks are correctly evaluated.
- Evaluating risk management processes.
- Evaluating the reporting of key risks.
- Reviewing the management of key risks.

Per IIA position paper 2004

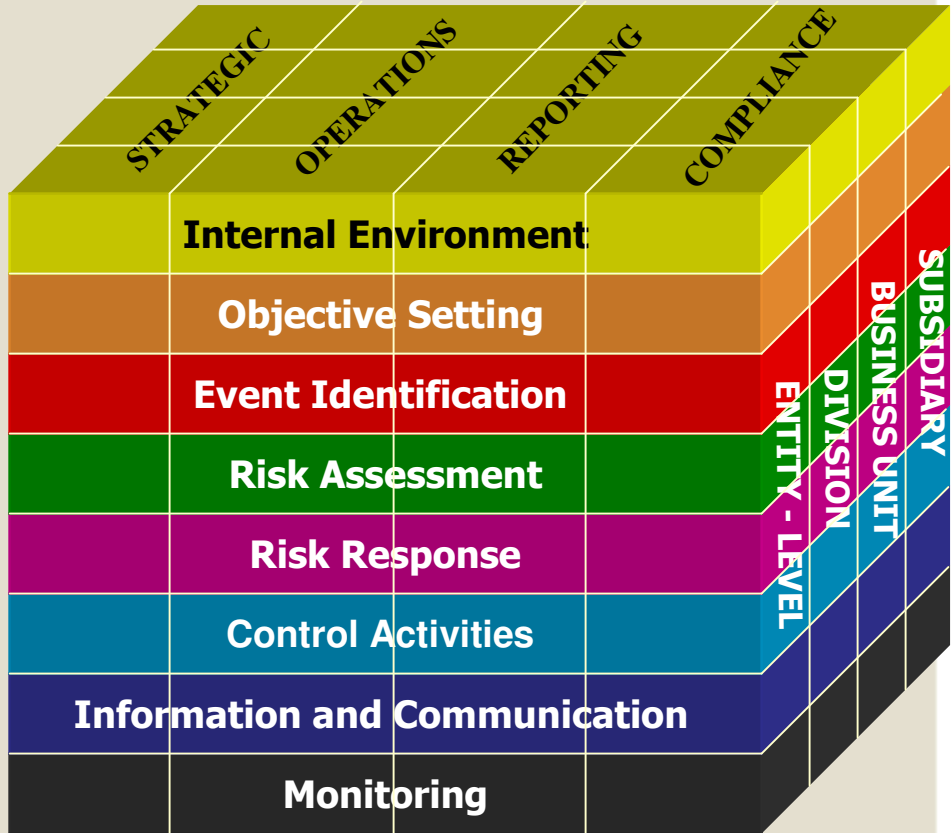
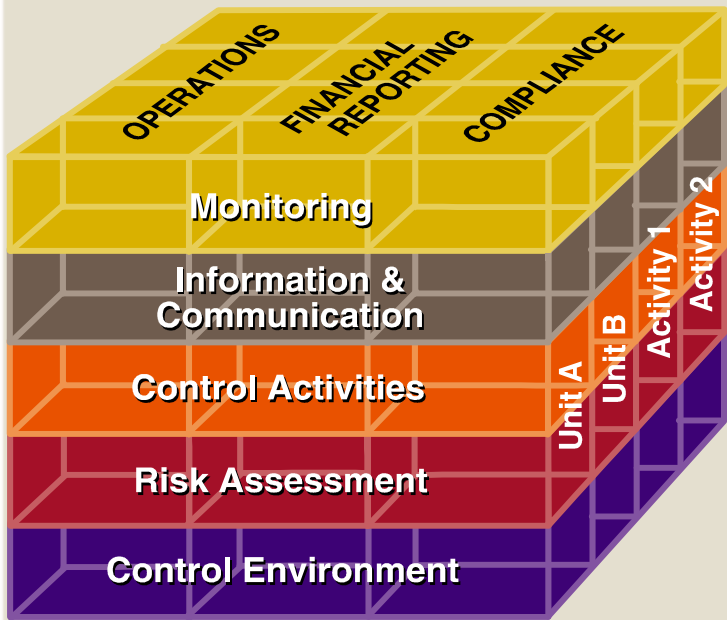
# Roles IA Can Do

- Facilitating identification and evaluation of risks
- Coaching management in responding to risks
- Coordinating ERM activities
- Consolidating the reporting on risks
- Maintaining and developing the ERM framework
- Championing establishment of ERM
- Developing risk management strategy for board approval

# Roles IA should NOT do

- Setting the risk appetite
- Imposing risk management processes
- Management assurance on risks
- Taking decisions on risk responses
- Implementing risk responses on management's behalf
- Accountability for risk management

# ERM Framework – What's New?



**MARKET/EXTERNAL RISK**

<b>Competitor</b>	<b>Sensitivity</b>	<b>Investor</b>	<b>Capital Availability</b>	<b>Sovereign/Political</b>
<b>Legal</b>	<b>Regulatory</b>	<b>Industry</b>	<b>Financial Markets</b>	<b>Business Interruption</b>
<b>Catastrophic Loss</b>	<b>Sourcing</b>	<b>Interest Rate</b>	<b>Currency</b>	<b>Commodity</b>
				<b>Collateral Equity</b>

**BUSINESS PROCESS RISK**

- Cash Flow
- Concentration (Liquidity)
- Concentration (Credit)
- Efficiency
- Customer Satisfaction
- Performance Gap
- Cycle Time
- Dispatch
- Pension Fund
- Compliance
- Planning
- Product/Service Failure
- Opportunity Costs
- Environmental Scan
- Pricing
- Product Development
- Regulatory Reporting (Operating)
- Regulatory Reporting (Financial)
- Resource Allocation
- Taxation
- Collective Bargaining

**MANAGEMENT REPORTING RISK**

- Accounting Information
- Contract Commitment
- Financial Reporting Evaluation
- Relevance
- Treasury Reporting

**FACILITIES & EQUIPMENT RISK**

- Capacity
- Environmental
- Health & Safety
- Obsolescence/Shrinkage

**MODEL & ASSUMPTION RISK**

- Budget & Planning
- Financial Instrument
- Investment
- Evaluation
- Performance
- Measurement (Process)
- Valuation

**ORGANIZATION, MANAGEMENT & STRUCTURE RISK**

- Authority/Limit
- Change Readiness
- Communications
- Employee Fraud
- Human Resources
- Illegal Acts
- Leadership
- Management Fraud
- Organization Structure
- Performance Incentives
- Unauthorized Use

**BUSINESS STRATEGY AND POLICY RISK**

- Alignment
- Business Portfolio
- Credit Policy
- Life Cycle
- Performance Measurement
- Reputation
- Trademark/Brand Name Erosion

**SYSTEM & TOOLS RISK**

- Integrity
- Access
- Availability
- Infrastructure

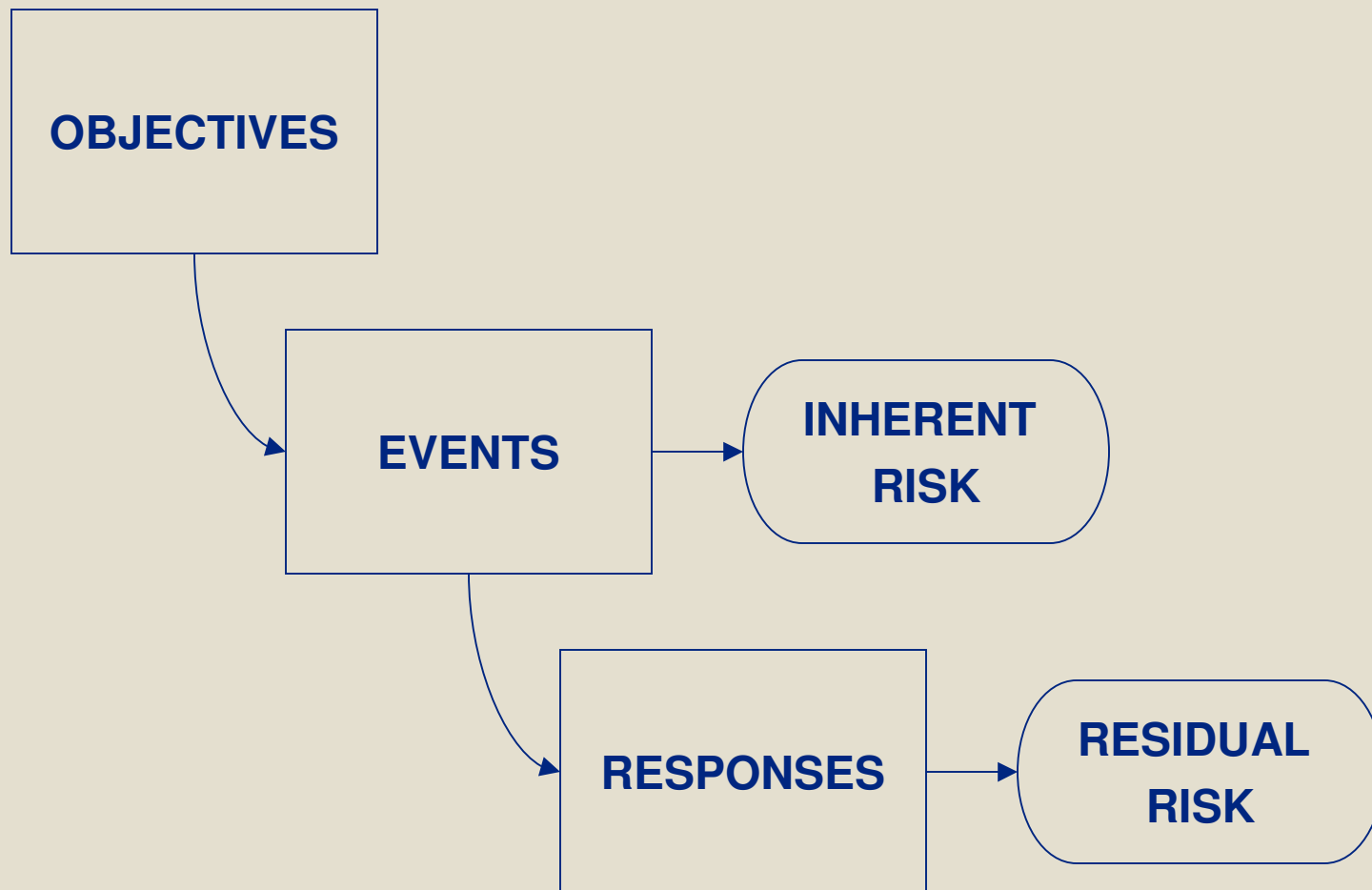
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**COUNTERPARTY RISK**

Default      Outsourcing      Settlement



# Essential – Process



# Essential – The Big Picture

High Impact/ Low Likelihood	High Impact/ High Likelihood
Low Impact/ Low Likelihood	Low Impact/ High Likelihood

# Role of IA Today

- Risk
- **Control**
- Governance

So what are you doing?

# Control Roles for IA

- Defining key controls
- Assessing control effectiveness
- Rendering an opinion

# Control

A **process** effected by an entity's Board of Directors, management and other personnel, designed to provide **reasonable assurance** regarding the **achievement of objectives** in the following categories:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations
- Safeguarding of assets

COSO Definition

## **IIA's Position on IA Role in Control Assessment**

- Project oversight
- Consulting and project support
- Ongoing monitoring and testing
- Project audit

Per IIA position paper 2004

# **IIA's Position on IA Role in Control Assessment**

## **Project Oversight**

- Steering committee member
- Facilitate management and EA

# IIA's Position on IA Role in Control Assessment

## *Consulting & Project Support*

- Provide IA documentation of processes
- Advise on tools, documentation, & testing
- Training on internal control & risk
- QA of documentation



# **IIA's Position on IA Role in Control Assessment**

## **Ongoing Monitoring and Testing**

- Advise management on testing design, scope, and frequency
- Independent assessor
- Perform tests
- Gap analysis and corrective action
- Follow-up on gaps
- Disclosure committee participation

# IIA's Position on IA Role in Control Assessment

## *Project Audit*

- Ensure project is well managed
- Use risk-based techniques to select project assessment activities

# IIA's Position on IA Role in Control Assessment

## **Objectivity Impairment**

- Involvement in running project
- Making management assertion
- Performing the testing that leads to management assertion
- Drafting procedures
- Making decisions on remedial actions
- Devotion of resources

# Issues

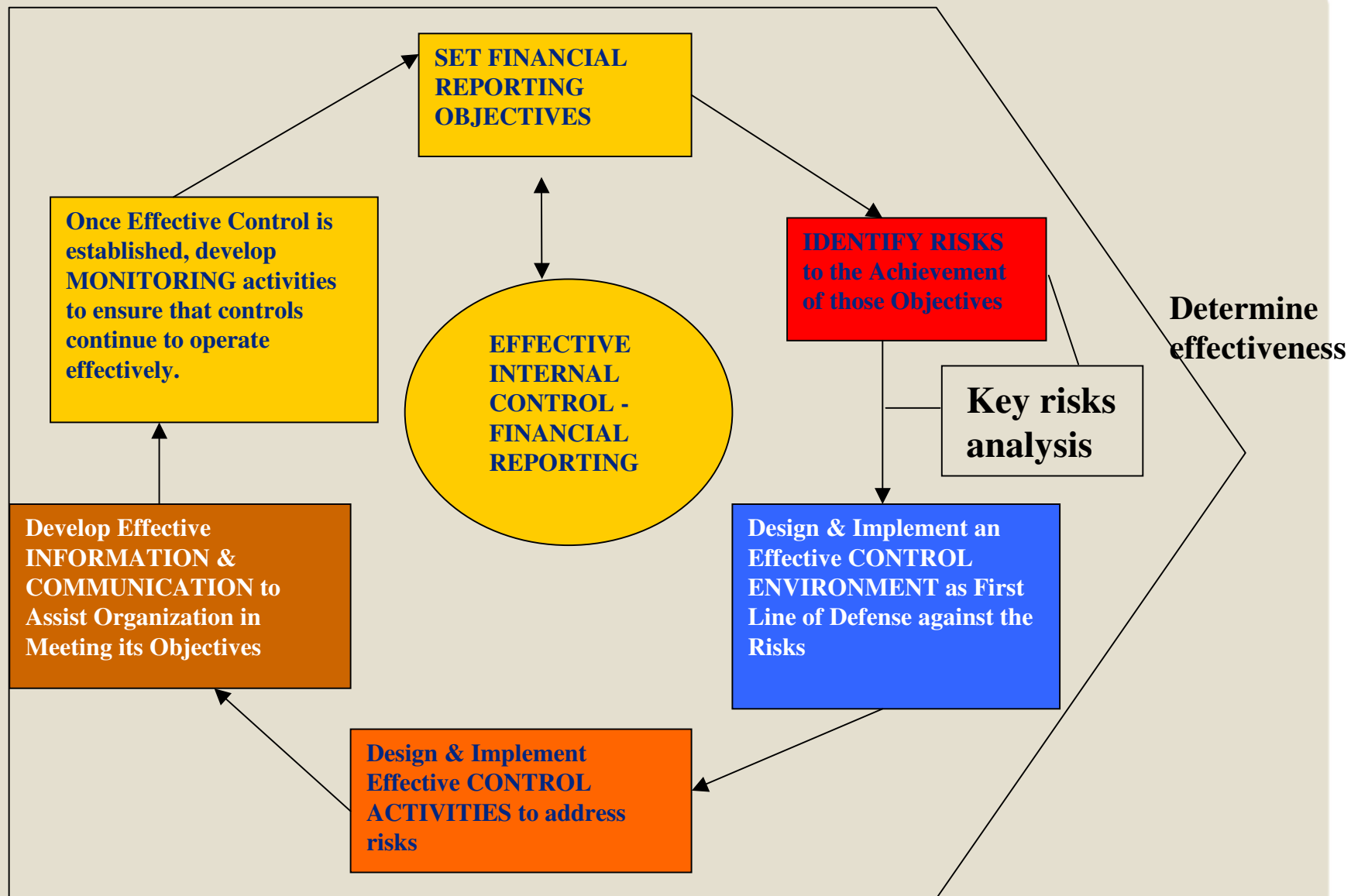
- Estimates
- Closing process
- Journal entries
- Reconciliations
- Assignment of responsibilities
- Accountability
- Ethics
- Risk assessment
- Governance (principles)
- IT controls
- Analysis and monitoring



## Internal Control over Financial Reporting - Guidance for Smaller Public Companies

Volume I : Executive Summary





# Components of Internal Control

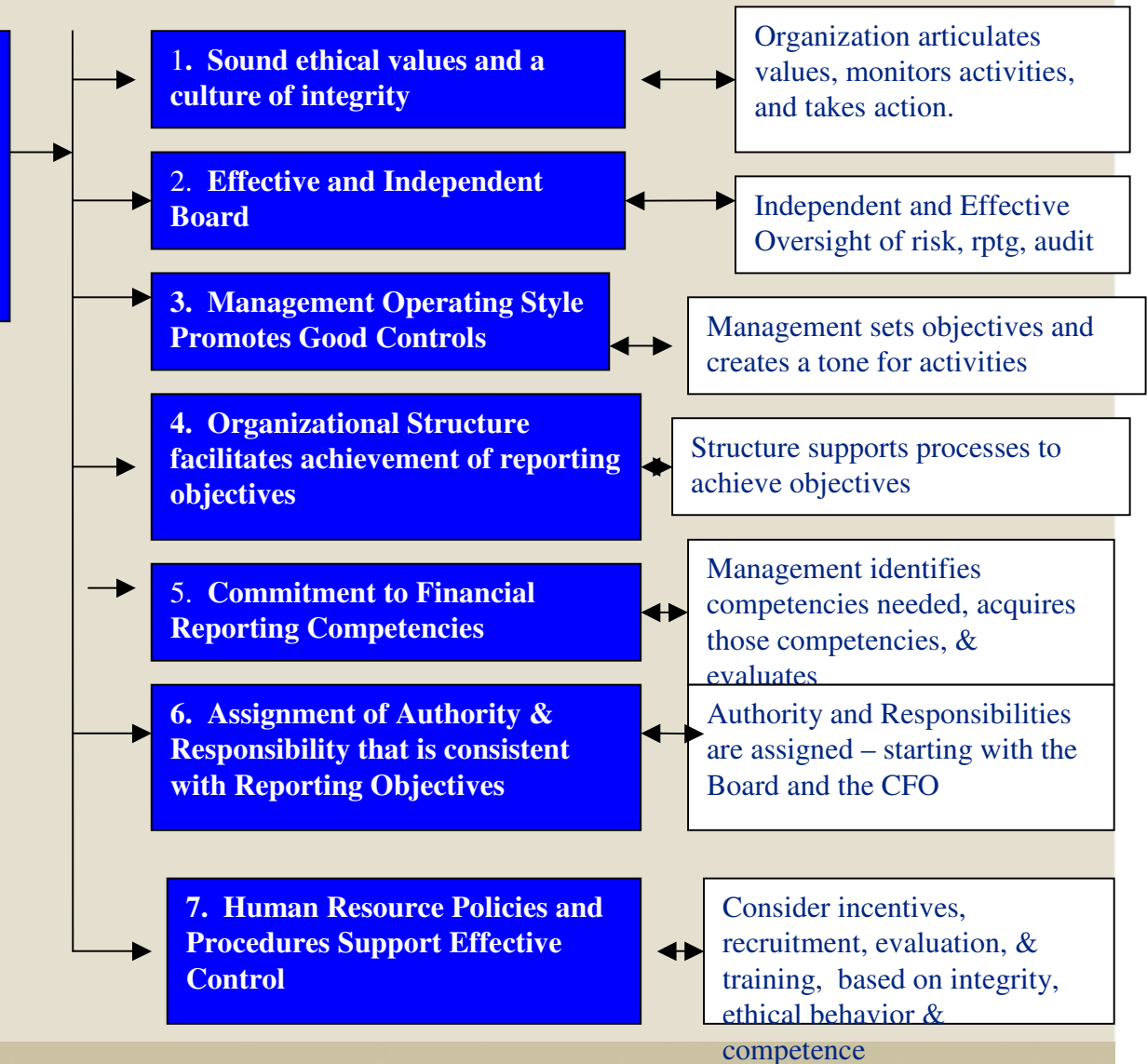
1. Control environment
2. Risk assessment
3. Control activities
4. Information and communication
5. Monitoring

# Organization of Guidance

- 5 Components of internal control
  - Principles = Fundamental concepts
    - Attributes = Characteristics
      - Approach = ways to accomplish principles
        - » Examples = real life cases
        - » Tools = sample documents



**CONTROL ENVIRONMENT:** *The control environment sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure.*



**RISK ASSESSMENT** - *Every entity faces a variety of risks from external and internal sources that must be assessed. Risk assessment is the identification and analysis of relevant risks to achievement of the objectives, forming a basis for determining how the risks should be managed.*

**8. Identify Financial Reporting Objectives**

Complies with achievement of GAAP, full disclosure, assertions, & materiality

**9. Identify Risks that threaten the achievement of the objectives**

Consider processes, personnel, incentives, internal & external factors & technology likelihood & impact

**10. Identify and assess the Risk of Fraud as it affects the company**

Consider incentives, opportunities, & likelihood to commit fraud plus assigns responsibility

## CONTROL ACTIVITIES:

*Control activities are the policies and procedures that help ensure that management directives are carried out. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties.*

11. Controls chosen to mitigate risks identified

Consider all sources of entry into the books; information technology, and personnel

12. Controls chosen based on assessment of effectiveness and cost

Apply a combination of preventive and detective controls plus cost/benefits to mitigate risks

13. Policies and Procedures established and communicated to accomplish objectives.

Implement consistently in a timely fashion across the organization, investigates exceptions & periodically reassesses

14. Information Technology is utilized to accomplish objectives

Includes application controls, considers general computer controls, and end-user computing.

## **INFORMATION & COMMUNICATION.**

*Pertinent information must be identified, captured and communicated in a form and timeframe that enables people to carry out their responsibilities.*

*Organizational personnel must receive a clear message from top management that control responsibilities must be taken seriously. They must understand their own role in the internal control system, as well as how their individual activities relate to the work of others. They must have a means of communicating significant information upstream.*

15. Pertinent information is gathered at all levels in the organization to support the achievement of the financial reporting objectives.

Data is captured at its source; technology is utilized to ensure consistency and accuracy, and is designed to maintain quality.

16. Information is gathered to support personnel and systems in carrying out their control responsibilities.

Information is gathered to ensure compliance with policies and regulations facilitates a quick identification and understanding of the root causes of control failures, and facilitates maintaining quality.

17. Internal communication facilitates personnel understanding sufficient to accomplish the control objectives.

Includes effective communication with the Board, across personnel, and a “whistle blowing” process.

18. Matters affecting achievement of the control objectives, where applicable, are communicated to outside parties

Includes open communication with vendors, suppliers, and customers, as well as with important stakeholders

## **MONITORING:**

*Internal control systems need to be monitored - a process that assesses the quality of the system's performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of the two. Internal control deficiencies should be reported upstream, with serious matters reported to top management and the board.*

19. On-Going or Separate Evaluations are designed to provide information on whether internal control over financial reporting remains effective. Design is such that monitoring facilitates timely identification of control failures and remediation

On-going evaluations are designed to provide continuous monitoring of the controls. Separate evaluations need to be carried out by knowledgeable personnel with sufficient frequency and scope to manage the risks associated with control failures.

20. Deficiencies are reported to the proper personnel (and level) within the organization that facilitates timely, corrective action of the control deficiencies.

Findings and deficiencies are reported to those with the ability to correct the root causes of the failures in a timely fashion. Important deficiencies are reported to management and the board to facilitate accomplishment of their responsibilities to ensure appropriate corrections are made.

# Guidance – Volume II: Principles, Attributes, Approaches, and Examples

## **Principle 1**

Sound integrity and ethical values, particularly of top management, are developed and understood and set the standard of conduct for financial reporting.

## **Three Attributes**

- **Articulates Values**
- Monitors Adherence
- Addresses Deviation

## **Three Approaches**

- Articulating and Demonstrating Integrity and Ethics
- Informing Employees about Integrity and Ethics
- Demonstrating Commitment to Integrity and Ethics

## **Six Examples**

- Company Newsletter Reinforcing Integrity and Ethics
- Promoting Awareness of Ethical Behavior
- Etc...

# Role of IA Today

- Risk
- Control
- **Governance**

So what are you doing?

# Governance

- Defining
  - Leadership - Tone
  - Employees – Carry out mission
  - Constituents – Interest in success
- IA Role
- Governance model
- Governance principles



# Governance Principles

1. Organization and functioning board
2. Qualifications of board members
3. Board authority, funding, and resources
4. Transparency
5. Articulate strategy
6. Organizational structure
7. Establish policies
8. Clear lines of responsibility and accountability

Per IIA Position Paper June 2006

# Governance Principles

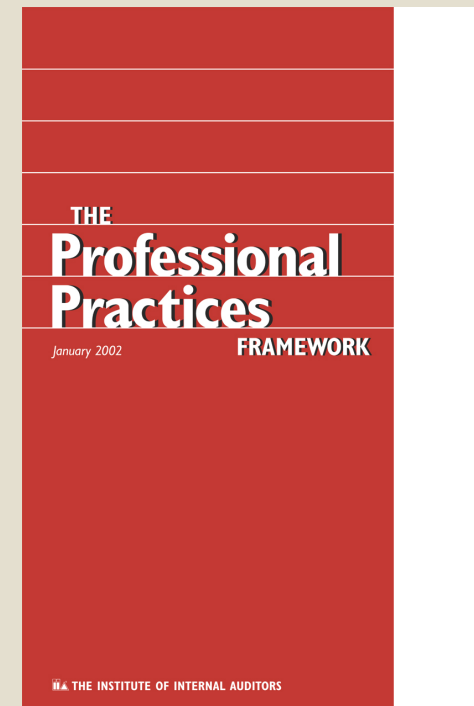
9. Interactions (board, mgt, EA, IA)
10. Strong internal controls
11. Compensation policies and practices
12. Ethical culture, values, tone at top
13. Use of internal auditors
14. Define and implement risk mgt policies
15. Effectively use EA
16. Appropriate disclosures of key information
17. Governance process disclosure
18. Related party transaction oversight

# Governance – Key Words

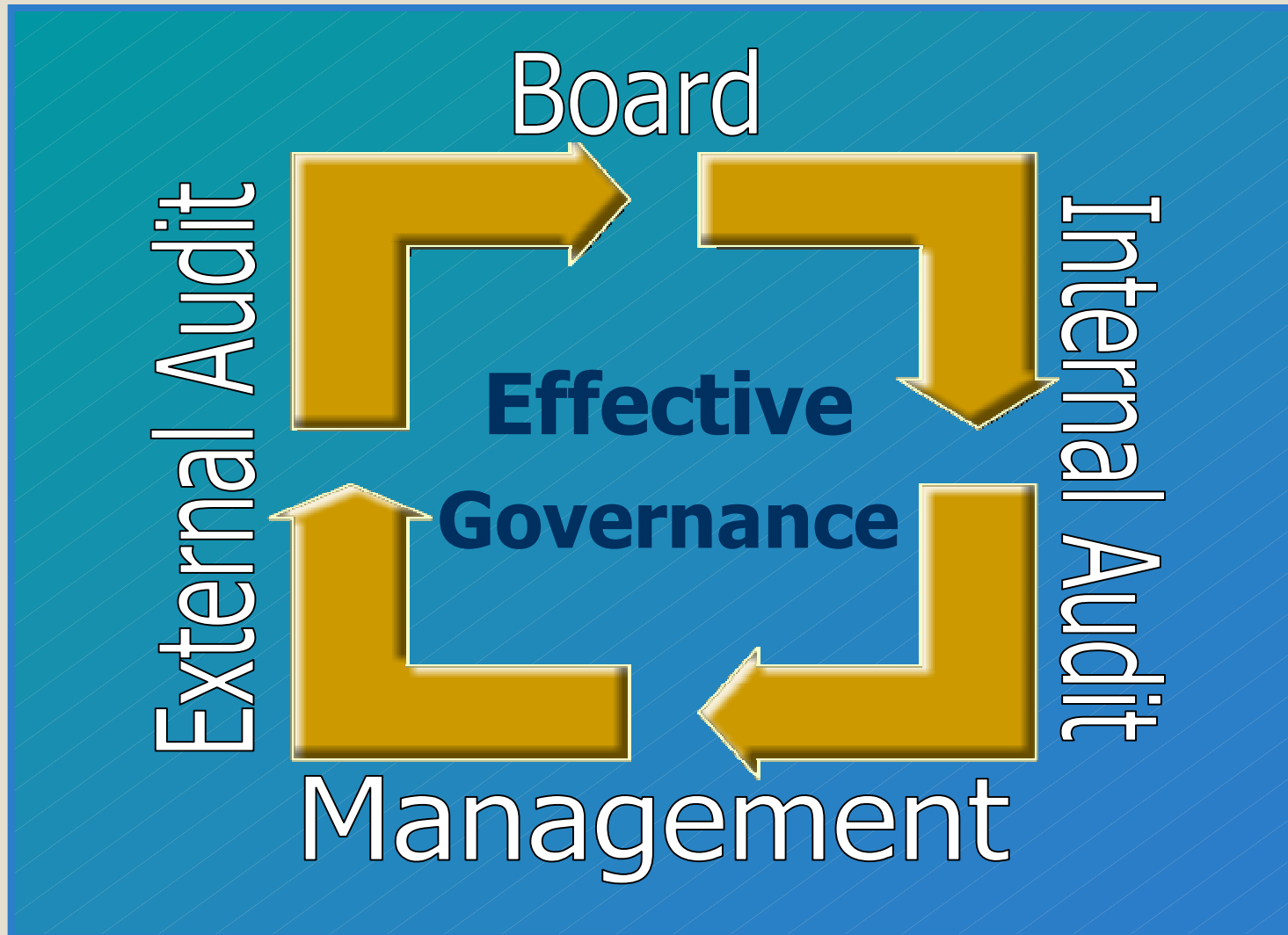
- Expectations
  - What is needed for success:
    - Policies, procedures, guidance, organization, assignment of responsibilities
- Communications
  - Informing and training
- Accountability
  - Holding people accountable for meeting expectations

# IIA Standards-Governance

- **2130-Governance**
- **The internal audit activity should contribute to the organization's governance process by evaluating and improving the process through which (1) values and goals are established and communicated, (2) the accomplishment of goals is monitored, (3) accountability is ensured, and (4) values are preserved**



# The IIA Corporate Governance Model



# Allocation of IA Effort



Per IIA position paper 2006

# What Should IA Do?

## Setting Expectations:

IA should:

- Help drafting of policies, procedures, processes, guidance to utilize their
  - Knowledge
  - Expertise
- Ensuring controls are built into processes not added on

# What Should IA Do?

## Communicate:

IA should:

- Assist in training programs on
  - Ethics
  - Risk identification
  - Control options
  - Fraud awareness
- Design programs
- Participation in training sessions



# What Should IA Do?

## Accountability:

IA should:

- Perform objective assessments using systematic, disciplined approach that incorporates an evaluation of evidence
- Ensure compliance to management directives by comparison of actual to criteria
- Assist in evaluation of processes to ensure efficient operations and effective accomplishment of objectives

# Agenda

- What should internal auditors do?
- *How can we assess internal auditing performance?*
- How can The IIA help?

# Assessing IA

- Standards
  - Planning
  - Organization
  - Execution
- Benchmarks / Comparison
  - Statistical data
  - Size organization, industry, IA org. size
- Independent Assessment
  - Comparison to Standards
  - Access to best practice suggestions

# Standards

- Planning = Audit Plan
  - Risk Assessment – key business risks
  - Audit universe – rotation
  - Control Assessment
  - Governance – Ethics & values
- Organization
  - Independence – reporting relationship
  - Objectivity – scope of internal audit
- Execution
  - Engagement objectives and scope
  - Work program and workpapers
  - Reporting

# Benchmarks

- Process
  - Customer Satisfaction
  - Efficiency
- Results
  - Values
  - Savings (CM)
- Cost
  - Resources
  - Products

# Independent Assessment

- Self-assessment using externally developed assessment guide
- Independent validation of self-assessment
- External to organization QAR team
- Process:
  - Common standards for comparison
  - Evaluation process
  - Criteria for determining opinion
  - Qualifications of evaluators

# Assessment Criteria

- Scope of the overall internal audit plan
- Individual audit performance
- Policies and procedures
- Audit committee and management support and opinion
- Documentation of audit results
- Ongoing communication and reporting
- Charter content
- Human resource management
- Training

# On-going Quality

## 1300 - Quality Assurance and Improvement Program

- The chief audit executive should develop and maintain a quality assurance and improvement program that covers **all aspects** of the internal audit activity and **continuously monitors** its effectiveness. The program should be designed to help the internal auditing activity **add value** and **improve the organization's operations** and to provide assurance that the internal audit activity is in conformity with the *Standards* and the *Code of Ethics*.



# Quality Assurance & Improvement Program

- Quality standards – audit projects  
Customer meetings; project planning, audit agreement, program, report, work papers, and follow-up
- Personal Quality Standards  
Customer focus, training, preparation, timeliness, presentations, respect, and objectivity
- Quality Assessment process (on-going)
- Quality measurement
- External assessments – continuous improvement effort

# Agenda

- What should internal auditors do?
- How can we assess internal auditing performance?
- **How can The IIA help?**

# The IIA Vision

The **global voice** of the internal auditing profession: **advocating** its value, promoting best practice, and providing **exceptional service** to its members.

# The IIA Mission Statement

The mission of The Institute of Internal Auditors is to provide dynamic leadership for the global profession of internal auditing.

Activities in support of this mission will include but will not be limited to:

1. Advocating and promoting the value that internal audit professionals add to their organizations;
2. Providing comprehensive professional growth opportunities; standards and other professional practice guidance; and certification programs;

# The IIA Mission Statement

## (Continued)

3. Researching, disseminating, and promoting to practitioners and stakeholders knowledge concerning internal auditing and its appropriate role in control, risk management, and governance;
4. Educating practitioners and other relevant audiences on best practices in internal auditing; and
5. Bringing together internal auditors from all countries to share information and experiences.

# **IIA Mission is to provide:**

- Guidance and Standards
- Certification program
- Research
- Promotion of the profession
- Forum for interchange
- Training

# IIA Top Needs

- Advocacy
- Globalization
- Service to Members

# Advocacy

- Position papers
- Key constituent groups
- Linking IIA with advocate target
- Advocacy specific plan for each group
  - Objective
  - Approach
  - Measures of success



# Global Initiatives

- Guidance planning
- Academic relations
- Government auditors
- SOA / control assessment
- Technology Based Learning
- Service providers relationship
- Knowledge management
- Customer service

# Global Initiatives

- Branding
- Certification (CBT)
- Translations on Website
- Webcasts
- Common Body of Knowledge (CBOK)
- Global Seminars
- IT – GTAG and GAIT

# Global Initiatives

- International Conference model
- GAIN
- Flash surveys
- Capacity development
- Website redesign
- CIA training course

# Operations - Service

- Website information
- Affiliate relations (restructure)
- Membership (growth & retention)
- New computer systems (customer service)
- Bookstore – global reach
- Quality Assessment (SAWIV, tools, QA Manual)
- Publications – on line delivery
- E-commerce

The Internal Auditing activity is a key element in an on-going monitoring and oversight program within an organization.

It demonstrates management and board commitment to ensuring accuracy, efficiency, and effectiveness of operations and reporting.