Internal Auditing

(Basics and Best Practices)

The Purpose of Internal Auditing?

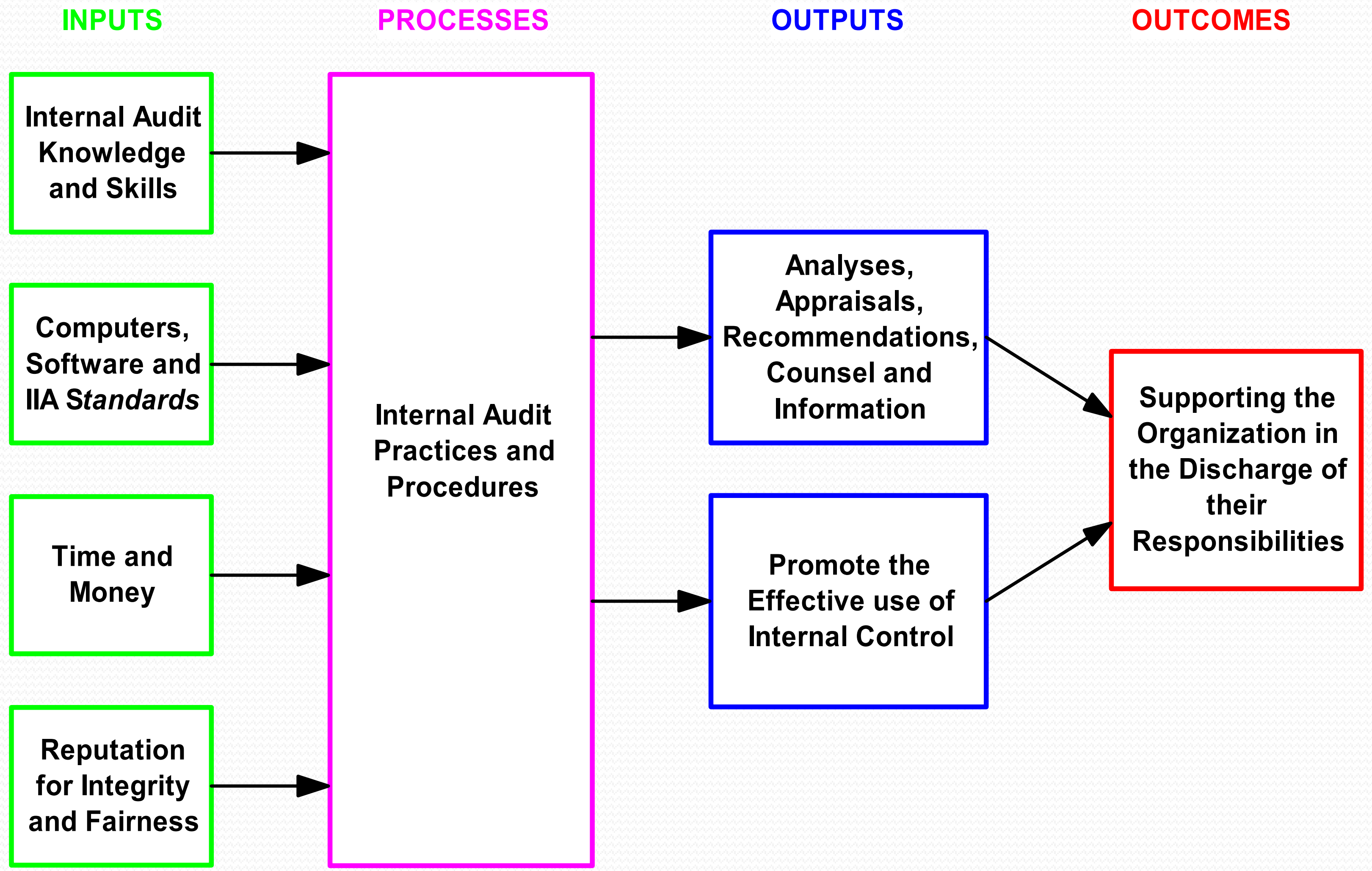
- “Eyes and Ears”
- “Policeman”
- “Watchdog”
- “Consultant”
- “Catalyst”

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.*

The Audit Process Model



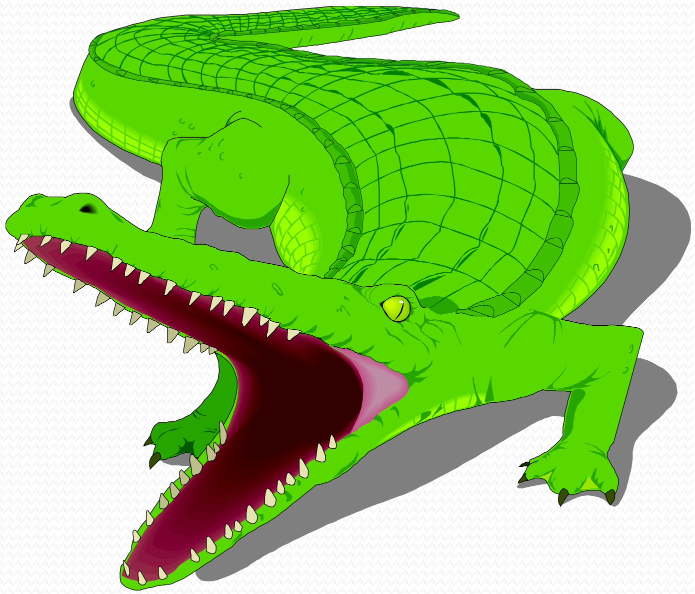
IIA *Statement of Responsibilities*

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).

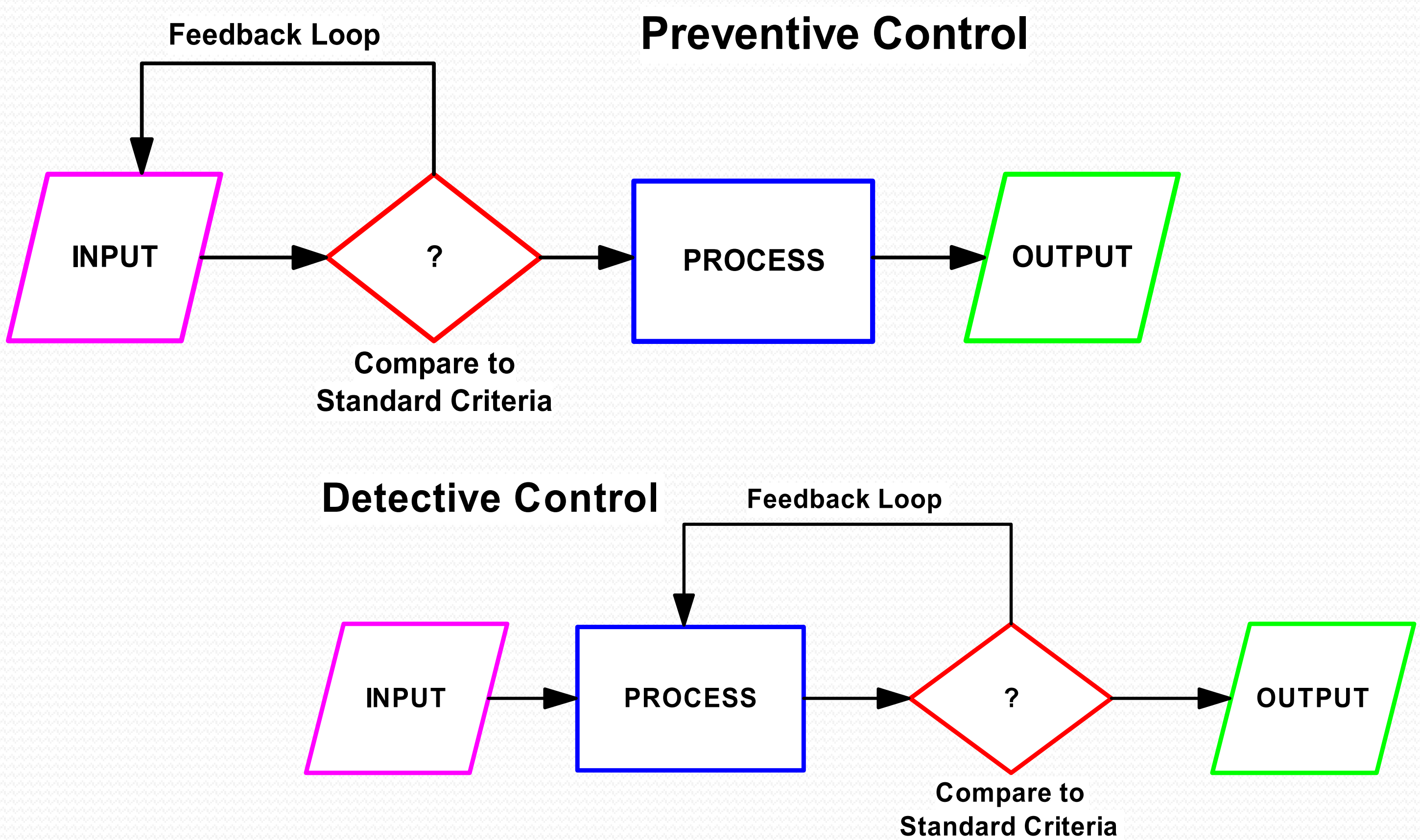
The Nature of Business Risk

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



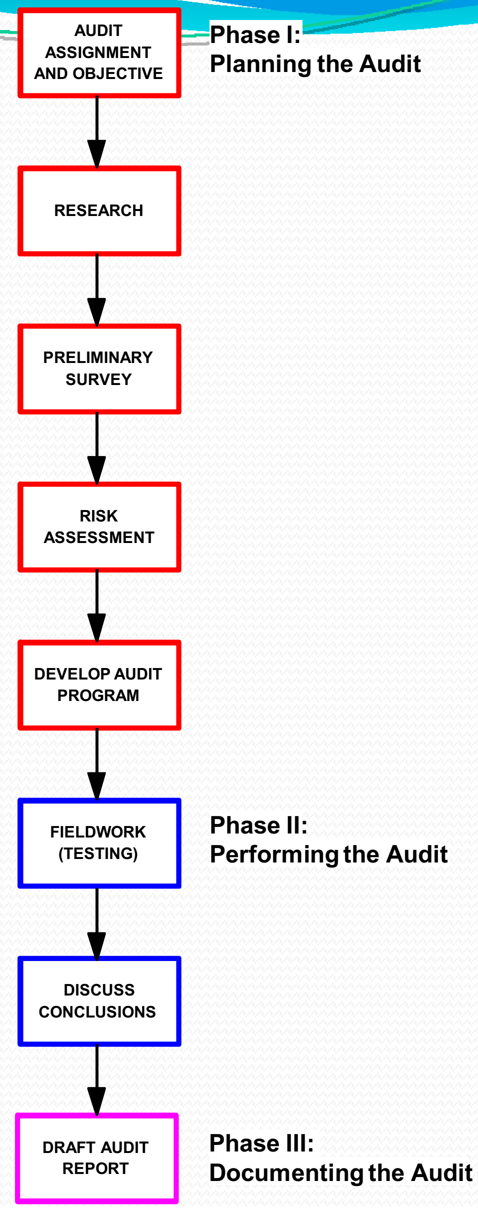
Control and Risk

Control mitigates risk:



Internal Audit Framework

- Planning
- Performing
- Reporting



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.

Planning the Audit

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

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.

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*

Planning Step #3

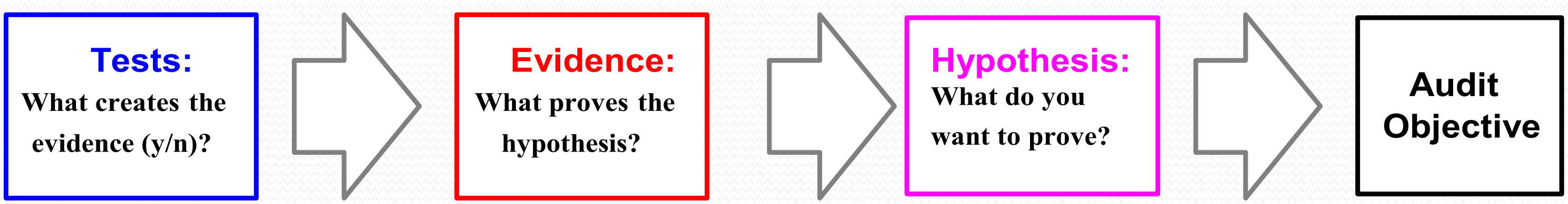
Send Engagement Memo

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

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



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.

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.

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

Writing Up Conclusions

Best practices include:

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

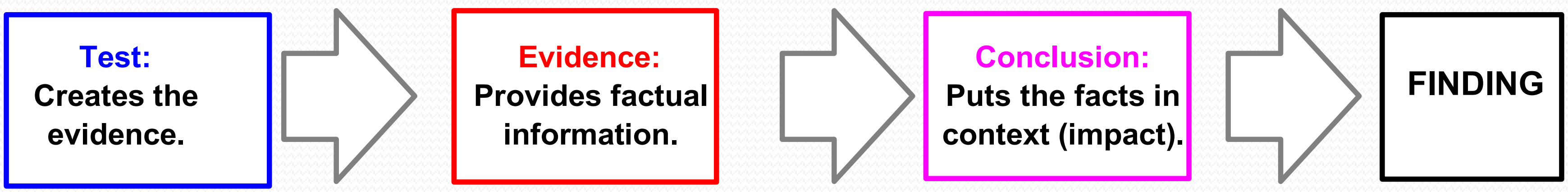
Best Practices (cont)

- 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).

Summarizing and Evaluating Results

- The audit process creates evidence.

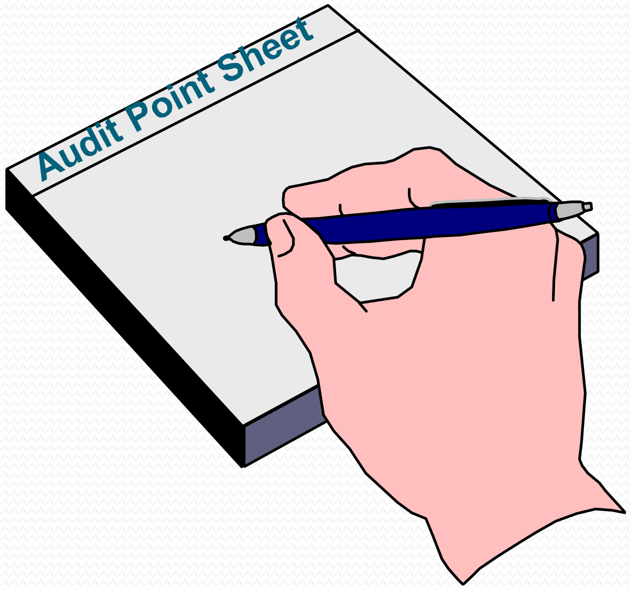
The Logical Results: From Tests to Findings



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

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.



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.

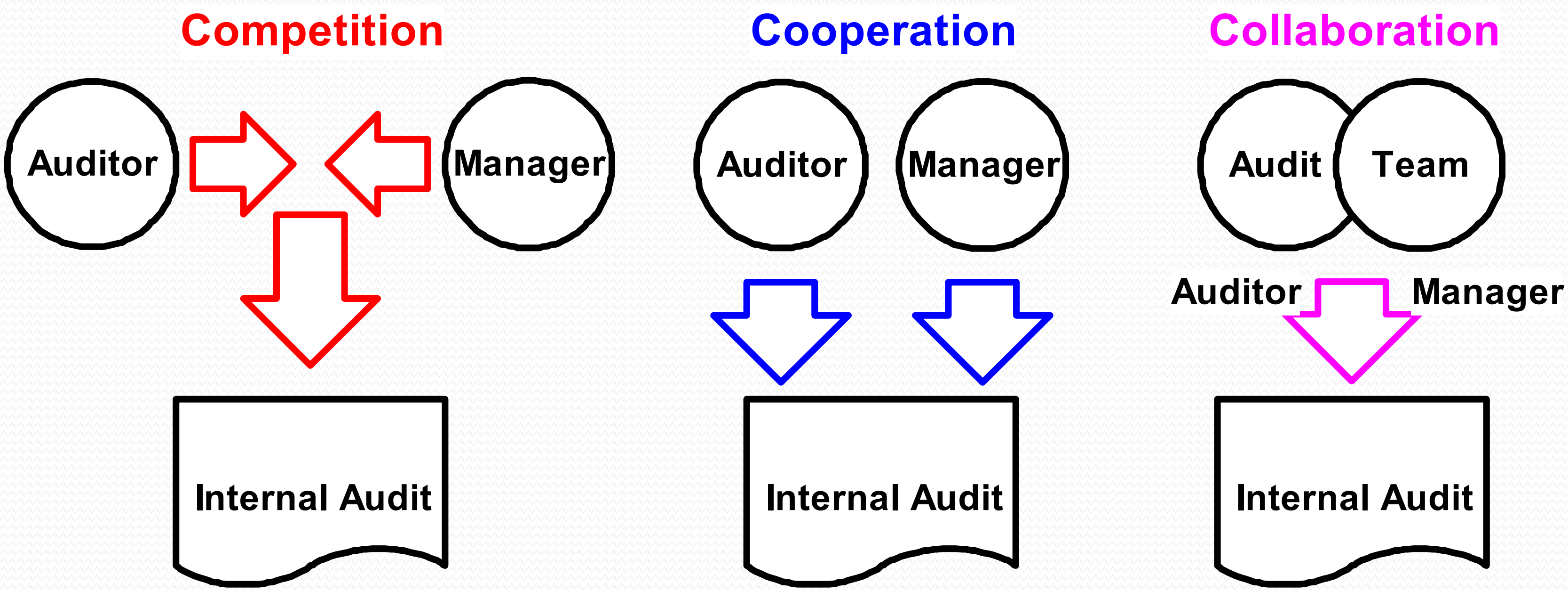
Following Up – Corrective Actions

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.

Audit Interaction with Auditee



Building Trust with Auditee

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