# What is Internal Audit ?

Internal Audit is an independent & objective assurance and consulting activity that is guided by a philosophy of **adding value** to improve the operations of the organization. It assists organization in accomplishing its objectives by bringing a systematic & disciplined approach to evaluate & improve the effectiveness of the organization's **governance, risk management, internal control**.-**The Institute of Internal Auditors, Florida, USA**

# Who are responsible for Internal Audit ?

Board of directors assign responsibilities to Audit Committee to oversee the internal audit activity of the organization. Audit committee normally consists of 3 to 5 members from Board of Directors. One of whom act as a chairman(independent director) of the Audit committee. Meets after every three months to discuss & review the audit findings & action to be taken to mitigate the risk as reported in the internal audit report. Class of companies to appoint internal auditor is defined in Rule 13 of Companies (Accounts) Rules, 2014.

# Steps to create internal audit function….contd

1) Appoint the Chief Audit executive(Head Internal Audit), responsible for conducting the internal audit as per audit plan & submit the report to Audit Committee.
2) Establish the scope of internal audit function(to be stated in Internal Audit charter) in consultation with the Audit committee & senior management.

# Steps to create internal audit function

3) Develop an Internal Audit charter(It is a formal written document that defines the activity's purpose, authority and responsibility. The charter should (a)establish the internal audit activity's position within the organization; (b)authorize access to records, personnel and physical properties relevant to the performance of engagements; and © define scope of internal audit activities.

4) Assess risk & develop an Audit Plan.

# Roles of Chief Audit Executive/Head Internal Audit

1) Responsible for preparing an annual audit plan & conducting audit as per audit plan & should effectively manage the internal audit activity to ensure it adds value to the organization. Provide training to the audit staff.
2) Responsible for conducting a preliminary assessment of the risks relevant to the activity under review.
3) Responsible for reporting periodically to the board & senior management on the internal audit activity's purpose, authority, responsibility and performance relative to its plan.
4) Keep the audit committee informed of emerging trends and successful practices in internal auditing.
5) Assist in the investigation of significant suspected fraudulent activities within the organization and notify management and the audit committee of the results.

# Internal Audit Department charter(Every Internal Audit department within an organization needs to have an Internal Audit Charter which contains the following elements & approved by the chairman audit committee)

1) Mission:-

The Internal audit department's mission is to provide independent, objective assurance and consulting services designed to add value and improve the organization's operations. Also helping the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance process.

# Internal Audit Department Charter……contd..

2) Scope of work of internal audit department:-It includes ensuring the following:

a) Risks are appropriately identified and managed.
b) Interaction with the various governance groups occurs as needed.
c) Significant financial, managerial and operating information is accurate, reliable & timely.
d) To ensure that the organizational policies, procedures, standards and applicable laws and regulations are complied with.
e) To ensure that resources are acquired economically, used efficiently and adequately protected.
f) To ensure programs, plans and objectives of the organization are achieved.

# Internal Audit Department Charter…….contd..

g) To ensure that quality and continuous improvement are fostered in the organization's control process.

h) Significant legislative or regulatory issues impacting the organization are recognized and addressed appropriately.

# Internal Audit Department Charter……contd..

3) Accountability of Chief Audit Executive/Head Internal Audit to management & the Audit Committee:-

a) To provide an annual assessment on the adequacy & effectiveness of the organizations processes for controlling its activities and managing its risks in the areas set forth under the mission and scope of work.
b) Report significant issues related to the processes for controlling the activities of the organization, potential improvements.
c) Report significant issues related to the processes for controlling the activities of the organization, potential improvements.
d) Coordinate with and provide oversight about the risk management, compliance, security, legal, ethics.
e) Periodically provide the information on the status of annual Audit plan.

# Internal Audit Department Charter……contd..

4) Independence of Chief Audit Executive/Head Internal audit:

a) To maintain the independence of the internal auditing department.

b) To provide a regular report to the Audit committee on Internal Audit personnel.

c) They are not to be involved in routine job of the organization. Functional accountability to Audit committee & administrative accountability to senior management.

# Internal Audit Department Charter……contd..

5) Responsibility of Chief Audit Executive/Head Internal Audit:

a) Develop an annual Internal Audit Plan as per risks & control concerns identified by the management & submit the plan to Audit committee for review & approval & periodical updates. Circulate the audit plan to management.

b) Implement the approved annual Audit plan

c) Provide training to the Internal Audit staff to develop the skills for achieving the objectives & adding value through internal Audit process.

d) Issue periodic reports to the Audit committee and management summarizing the results of Audit activities.

e) Keep the audit committee informed of emerging trends & better practices.

f) Assist in the investigation of the suspected fraudulent activities within the organization and notify the management & Audit committee of the results.

g) Review compliance with company policies on ethical business conduct.

h) Regular follow up with Audit client for ensuring corrective actions taken on reported weaknesses.

i) Assess the current state of corporate culture with attentive listening to the audit client.

# Internal Audit Department Charter

6) Authority of Chief Audit Executive/Head Internal Audit:

a) Head Internal Audit have unrestricted access to all functions, records, property and personnel.

b) Unrestricted access to Audit committee and attend the Periodical Audit Committee meeting.

c) Obtain the necessary assistance of the personnel of the organization.

# Policy statement on management support for Internal Audit Activity

Internal Audit Department of the organisation is set up to examine & evaluate company activities to help the management in improving the performance of the organisation.
All the functional department of the organisation are committed to extend their support, to the Internal Audit department by providing information, data, records, analysis etc. related to the activities of concerned department, as required by Internal Auditor to discharge their duties.

Approved signed(Chairman Audit committee)----

Approval date- circulation date-

# Types of Audit

a) **Compliance Audit:** To identify lapses in regulatory compliance, legal compliance, Compliance of code, ethics, policies, procedures, guidelines.
b) **Operational Audit:** Sales & marketing, Production, Assets, supply chain, Human resources, Information technology, Hazards.
c) **Performance audit:** It is the process of assessing the efficiency & effectiveness of the activities of an organisation & also assessing that the resources are being utilised efficiently & effectively to achieve the objectives of the organization.
d) **Environmental audit(ISO 14000): It** is a general term that can reflect various types of evaluations intended to identify environmental compliance and management system implementation gaps, along with related corrective actions.
e) **Special investigation:** A special investigation audit is a tightly-defined audit that only looks at a specific area of an organization's activities. This type of **audit** may be initiated to identify Fraud.

# Steps for designing Internal Audit plan

a) Identify the Audit universe(It is optional to maintain it, as per International standards).
b) Discuss with the management & assess the risk in each audit areas.
c) Ask for all policies, procedures documents & organization chart.
d) Evaluate the prior audit report & key reports used by the management in the audit areas.
e) Prepare checklist of risk assessment questionnaire of each audit area.
f) Prepare risk assessment matrix.

# Risk assessment matrix

1. List all aspects of event activities.
2. Identify risk associated with each activity.
3. Use the matrix to determine the level of risk associated with each activity before applying any risk management strategies.
4. Brainstorm methods to manage risks. Find strategies to be applied to reduce the severity of the risk and the probability that something will go wrong.
5. Use the matrix to re-assess the activities.
6. Determine if you have reached an acceptable level of risk by applying risk management strategies. Consider modifying or eliminating activities that have unreasonable risk associated with them. Remember to consider how the activity relates to the mission & purpose of your organization.

## Probability That something will go wrong

| | short period of time; expected to occur frequently | to occur in time | in time | Not likely to occur but possible | occur |
|---|---|---|---|---|---|
| **CATASTROPHIC** May result in death | E | E | H | H | M |
| **CRITICAL** May cause severe injury, major property damage, significant financial loss, and/or result in negative publicity for the organization and/or institution | E | H | H | M | L |
| **MARGINAL** May cause minor injury, illness, property damage, financial loss and/or result in negative publicity for the organization and/or the institution | H | M | M | L | L |
| **NEGLIGIBLE** Hazard presents a minimal threat to safety, health and well-being of participants; trivial. | M | L | L | L | L |

| | RISK DEFINITIONS | Many events, without proper planning, can have unreasonable levels of risk. However, by applying risk management strategies, you can reduce the risk to an acceptable level. |
|---|---|---|
| E | **Extremely High Risk** | Activities in this category contain unacceptable levels of risk, including catastrophic and critical injuries that are highly likely to occur. Organizations should consider whether they should eliminate or modify activities that still have an “E” rating after applying all reasonable risk management strategies. |
| H | **High Risk** | Activities in this category contain potentially serious risks that are likely to occur. Application of proactive risk management strategies to reduce the risk is advised. Organizations should consider ways to modify or eliminate unacceptable risks. |
| M | **Moderate Risk** | Activities in this category contain some level of risk that is unlikely to occur. Organizations should consider what can be done to manage the risk to prevent any negative outcomes. |
| L | **Low Risk** | Activities in this category contain minimal risk and are unlikely to occur. Organizations can proceed with these activities as planned. |

# Contents of the Audit report

a) **Objective and background**: State the reason for selection of the area, inherent or perceived high risk, known problems, history of past issues, a management change, materiality of the area or other factors. Describe the key aspects, risks and objectives of the area reviewed.
b) **Scope**:– Describe the scope of the work, time period and business units did it cover, and which facets of operations were included. Describe the key risks it addressed.
c) **Findings** : State the overall findings & severity of findings. State whether there are significant deficiencies in internal controls or the process being reviewed.
d) **Recommendations**: State what actions must management take to adequately address the audit finding, responsibility for corrective action to be taken & timeline to be taken for taking corrective action.

# Glossary(international standards for the professional practice of Internal Auditors)

**Add value:-**Value is provided by improving opportunities to achieve organizational objectives, identifying operational improvement, and/or reducing risk exposure through both assurance & consulting services.

**Risk Management:-**A process to identify, assess, manage, and control potential events or situations, to provide reasonable assurance regarding the achievement of organization's objectives.

**Internal Control:-** Internal control is a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives of the organization.

# Glossary(international standards for the professional practice of Internal Auditors)

**Audit Universe:-** An inventory of **audit** areas that is compiled and maintained to identify areas for **audit** during the **audit** planning process. ... The **audit universe** serves as the source from which the annual **audit** schedule is prepared. The **universe** will be periodically revised to reflect changes in the overall risk profile(To maintain it is optional as per International standards).

**Audit plan:-** **Audit** planning is a process that identifies all business areas; assesses the risk of each using a standard methodology; and uses available **audit** and financial resources to determine which audits will be performed during a year.

**Governance:-** **Governance** is the combination of processes and structures implemented by the board in order to inform, direct, manage and monitor the activities of the organization toward the achievement of its objectives.

**Compliance:-** It is adherence to policies, procedures, guidelines, laws, regulations, contracts etc.

**Risks:-** The possibility of an event occurring that will have an impact on the achievement of objectives. Risk is measured in terms of impact & likelihood of occurance.

# Thank You

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