

Internal Audit & its Activities

FINANCE LEARNING FORUM

ICF Diakonia Centre

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What does IA do?

1. Continues review of the effectiveness of :

- Risk management
- Control, and
- Governance processes

2. Provides recommendations for improvements

Risk Management (IIA)

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

Control (IIA)

Any *action* taken by management, the board and other parties to manage risk, provide reasonable assurance and increase the likelihood that established goals and objectives will be achieved.

Management plans, organizes and directs the performance of sufficient actions

Governance – (IIA)

- The combination of processes and structures implemented by the board to**
- **Inform, direct, manage and monitor the activities of the organization toward the achievement of its objectives.**

GOVERNANCE

Strategy
Structures &
Processes
Goals & objectives
Policies & Procedures

RISK MANAGEMENT

Identify Risks
Risk Analysis
Risk Profiles
Risk Monitoring

CONTROL

Control Activities
Compliance with Policies
and Procedures
Laws and Regulation

*Achieve
Organization's Goals
Manage Risks
Objectives;*

Scope of Work

1. Assurance services
2. Consulting services
3. Value-adding services

Assurance services

- Objective examination of evidence, for the purpose of providing an independent assessment of RMCG processes.

Types of Assurance service:

- Assurance auditing – where IA provides information related to financial, operational and compliance activities as well as other efforts such as control and risk management activities
- Financial audit – focuses on the accuracy of financial statements in according with GAAP. Internal controls are studied to determine the extent of account balance testing to perform.

Value-adding services

Focusing on efficiency and effectiveness to improve

- Processes
- Economical use of finances and resources.

Types of Value-adding service:

- **Operational audit** – reviews of the functions of an organization, focusing on the efficiency and economy of operations and the effectiveness with which those functions achieve their objectives.
- **Control Self-assessment** – directly involves employees in a business activity in evaluating the risks, controls, efficiencies, strength/ weaknesses or other aspects of the activity.

Consulting services

Advisory related client activities,

- the nature and scope of which are *agreed-upon* with the client, and which
- Are intended to add value & improve operations.

Types of Consulting

service:

- **Consultative auditing** – uses problem-solving methodologies to make direct improvements in the circumstances or conditions of the client
- **Compliance audit** – Review of procedures, processes or transactions to determine if established laws, regulations, policies or guidelines are followed. It sometimes includes a review of the internal controls.

Types of Consulting

service:

- **Program audit** – review of plans and procedures established to achieve the specific end result of a program. It differs from review of continuing activities within the organization.
- **IT audit** – review of general and application controls to ensure automated transactions are processed with CAATS (complete, accurate, authorized, timely & safeguarded).

Types of Consulting

service:

- **Fraud audit** – special audit performed by trained auditors in addressing the majority risk, whose mindset should be **investigative and anomaly-oriented**

IA and Fraud: IA Standards

IIA Standard 1200: Proficiency and Due Professional Care

1210.A2 – “Internal auditors must have sufficient knowledge to evaluate the *risk of fraud* and the manner in which it is managed by the organization, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud”.

IA and Fraud: IA Standards

IIA Standard 1220: Proficiency and Due Professional Care

1220.A1 – “Internal auditors must exercise due professional care by considering the:

.... Probability of significant errors, fraud or non-compliance.

IA and Fraud: IA Standards

IIA Standard 2060: Reporting to Senior Management and the Board

The Chief Audit Executive (CAE) must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility and performance, relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues and other matters needed or requested by SM and the board.

IA and Fraud: IA Standards

IIA Standard 2120: Risk Management

2120.A2 – “ The internal audit activity must evaluate the potential for the occurrence of fraud and how the organization manages fraud risk.”

IA and Fraud: IA Standards

IIA Standard 2210: Engagement Objectives

2210.A2 – “Internal auditors must consider the probability of significant errors, *fraud*, non-compliance and other exposures when developing the engagement objectives.”

Phases of an Internal Audit

Plan (2200)

Execute (2300)

Report (2400)

“Preliminary Survey”

“Fieldwork”

“Reporting”

Determine
Scope and
Objectives
Of Audit

Preliminary Review
(Identify Internal
Controls)

Entry Conference

Perform Audit Tests

Prepare
Audit
Report

Design of
Control

Operation
of Control

- - - Develop Audit Findings - - -

Audit Alert
Notice

Audit Programs

Exit
Meeting

Draft
Audit
Report

Final Audit
Report

Engagement Plan

----- Audit Workpapers -----

Audit Process - Continuation



Post-audit survey

Audit Follow-up

Annual Audit Report

What does IA review and examine?

1. Pre-determined criteria
Articles of Incorporation & by-Laws,
Policies & procedures; Manuals,
Agreements & contracts, Standards,
Laws & regulations
2. Organizational Charts, Minutes of
meetings, reports & evaluations, etc.
3. Processes, controls, systems & activities
4. Financial records, transactions & reports
5. Asset listings
6. Stakeholders of organizations

How does IA perform its work?

1. Review and identify applicable criteria
2. Assess gaps or deficiencies between criteria & current condition
3. Analytical procedures
4. Walk through / Re-performance
5. Transactional analysis

How does IA perform its work?

6. Confirmation / verification
7. Questioning
8. Investigation/ Inquiring
9. Match and/or compare records
10. Audit sampling
11. Observation
12. Monitoring techniques

Developing an Audit Finding

1. Identify

- Criteria
- Current condition
- Issue (gap)
- Risk or consequence

2. Provide recommendation for improvement/ action to be taken

Audit Report

- 1. Risk is assessed and quantified, i.e. determine its materiality level.**
- 2. Material items are summarized and reported.**
- 3. Client's response is incorporated in the final report**

Sample - Audit Opinion

- **Limited Risks** $\Rightarrow 80\%$
- **Acceptable Risks** $71\% - 79\%$
- **Significant Risks** $66\% - 70\%$
- **Unacceptable Risks** $\leq 65\%$

Fraud – Top 5 Office Crimes

- **Taking office supplies & eqpt.**
- **Lying to supervisor or co-workers**
- **Stealing funds**
- **Having an affair with co-worker**
- **Taking credit for work not done**

Fraud schemes

- Tampering of documents (fingerprints, signatures)
- Producing fraudulent documents
- Obtaining blank receipts from Vendors
- Adding items in receipts obtained from Vendors
- Lack of distribution lists for items purchased

How do we address fraud?

- **Develop Fraud Policy**
- **Increase the capacity of staff through orientation**
- **Conduct Fraud awareness training**
- **Strengthen internal controls**
- **Hire competent & honest employees**

Samples of Fraudulent Document



ING
SENG

Tel : _____

Address: _____

No. **000064**

VENDOR'S RECEIPT –

စဉ် No	ပစ္စည်း Name of Goods	ပမာဏ Quantity	ယူနစ် Unit Price	စုစုပေါင်း Amount
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
NET TOTAL				

_____ / The Buyer

_____ to _____

_____ / The Seller

Shop: 63

Shop: 63

Tel: 63

INVOICE

INVOICE

No. 100

Date: 10/6/2013

10/6/2013

Sl. No.	Name of Goods	Quantity	Unit Price	Amount
1				
2	SAFF	10000		
3				
4				
5				
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
17				
18				
			TOTAL	10000

Buyer

The Buyer

The Seller

10000

MARKET
RECEIPT –

Group Activity: Case Study

Determine or identify:

- Weaknesses
- Possible causes
- Consequences or risk
- Opportunity for fraud
- Recommendation to strengthen controls

CASE 1

Weaknesses:

Causes:

Consequences:

**Opportunity for
Fraud:**

Recommendation:

Shop: _____ Tel: _____

INVOICE

Date: 10/2/13

No	Name of Goods	Quantity	Unit Price	Amount
1	...			42000
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
17				
18				
19				
TOTAL				42000

Buyer / The Buyer: _____

Seller / The Seller: _____

CASE 2

A Project Manager submitted advance settlement transactions for its Travel & Mission Expenses in the province, including per diem claims and other travel expenses. The Finance staff processed and received all the documents.

The Finance Manager upon review of the “transaction details in the General Ledger” noted that travel dates to the province coincide with the Organization’s activity in Phnom Penh.

Identify the issues, cause, risk and recommendations.

Case 3

A project staff submitted the ff. documents to the Finance Department:

- Distribution Lists (DL) of children's school supplies amounting to \$2,000 – aged 6 to 10 years old.
- Issues noted:
 1. Big fingerprints were noted in the acknowledgment column of the DL.
 2. Same names of children for previous month's DL of shoes to children were found. However, fingerprints of the children in 2 DLs were not found similar.

**** Identify the weaknesses, cause and consequence.
Provide documents to improve internal controls.**

**Additional Slides for
Reference Only**

Models In Delivery of IA Services

1. In-house – services provided by employees; managed in-house
2. Co-sourced – combined services of employees & service providers
3. Outsourced with in-house management – service providers, managed by in-house employee
4. 100% outsourced – IA services and management of IA function are provided by contracted service provider. Project management of the service provider contract is done by in-house employee.

Features of Good Practice IA services

1. Risk-based: IA work is risk-based and client focused
2. Independence & appropriately positioned
3. IA Planning & work: with well-developed business strategy; clear roles & responsibilities; adheres to Standards
4. Resourcing: w/ sufficient resources; auditors have necessary skills, experience & personal attributes; experts in technical/ subject matters

Features of Good Practice IA services

5. Communication and reporting

- IA has the confidence of key stakeholders including the board of directors, the audit committee, the chief executive officer, and senior management.
- IA provides reports and other services, based on efficient and effective work practices that are valued by stakeholders.
- IA provides an annual report of its work, including an assessment of the effectiveness of the organization control system.
- IA advises the audit committee and management of patterns, trends and systemic issues identified from its work.

Features of Good Practice IA services

5. Communication and reporting

- IA facilitates communication between external audit and management of the organization.
- IA regularly informs the audit committee of progress in the
- implementation of agreed internal audit and external audit recommendations.

5. Review and improvement

- IA disseminates lessons learned arising out of its work
- IA is subject to periodic assessment and review as part of a continuous improvement process.

Assurance of the quality of IA work

Internal audit is required to maintain a quality assurance and improvement program that includes:

☐ Ongoing internal assessments, for example:

- Working paper reviews.
- Actual versus budgeted analysis for time spent on internal audit engagements.
- Audit customer feedback surveys from management after each internal audit engagement.
- Performance evaluations.
- Results of internal audit performance measures.

☐ Periodic internal assessments usually performed annually:

☐ Review of the internal audit charter for conformance with the internal audit

Assurance of the quality of IA work

☐ Periodic internal assessments usually performed annually:

- Review of the internal audit charter for conformance with the internal audit standards.
- Self– assessment of conformance with the internal audit standards

☐ External Assessments conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization.

It is a requirement of the IA standards for the results of the quality assurance and improvement program to be reported to the audit committee and senior management.

IA's Purpose:

1. To support the
 - Board of Directors
 - Audit Committee and the
 - Chief Executive Officer
2. To protect the interest of other Stakeholders.

Purpose - Support Mgmt by:

- Reviewing achievement of orgn's objectives
- Assessing if decisions are properly authorized
- Assessing reliability and integrity of information
- Reviewing assets are safeguarded

Purpose – Support Mgmt by:

- Assessing compliance with laws, regulations, policies & contracts
- Assessing efficiency, effectiveness and economy of business activities
- Reviewing opportunity for fraud and corruption

Purpose: Support the Mgmt by:

- Following-up previous audits to assess if remedial action has been effectively implemented
- Looking for better ways of doing things.

IA & the management - summary

IA supports the management by:

1. Providing independent, objective (unbiased) assessment of the organization's operations
2. Providing management with information on the effectiveness of RCG processes.
3. Being an adviser, that tells mgmt what and when it needs to know.

Audit Process Chart

Annual Audit
Plan

Audit Alert
Notice

Preliminary
Review

Entry Conference

Fieldwork

Audit Finding
Summary

Exit Conference

Audit Draft
Report

Final Report

Post-audit
survey

Audit
Follow-up

Annual Audit
Report