

INTERNAL ASSESSMENT

Ongoing Monitoring

- engagement by engagement basis
- emphasis on PERFORMANCE Std.

Periodic Self Assessment

- Gives a holistic view
- Comprehensive review of all stds. & IA activity

EXTERNAL ASSESSMENT

FULL EXTERNAL ASSESSMENT

- Conformance with stds. & Code of ethics
- Efficiency & effectiveness of IA
- Extent to which expectations of BOD & SM are met

Self Assessment with Independent Validation

- Fully documented
- Onsite validation
- Limited attention to Benchmarking

*PEER REVIEW among 3 unrelated org. may satisfy INDEPENDENCE



REPORTING on QAIP

1. Scope & frequency of internal & external assessment
 2. Qualification & independence of assessors.
 3. Conclusions
 4. Corrective Action plans
- Ongoing Monitoring results communicated At least ANNALLY

UNIT-1: INTERNAL AUDIT OPERATIONS

1. INTRODUCTION TO INTERNAL AUDITING

NATURE of WORK: IA credibility & value are enhanced

- When (i) auditors are PROACTIVE &
(ii) evaluations offer INSIGHTS &
(iii) considers FUTURE IMPACT

Governance: Combination of processes & structures implemented by BOD to INFORM, DIRECT, MANAGE & MONITOR activities towards achievement of objectives

RISK MANAGEMENT: Process to IDENTIFY, ASSESS, MANAGE & CONTROL potential events to provide REASONABLE ASSURANCE regarding achievement of org.'s objectives.

CONTROL: Any action taken by mgmt., BOD & other parties to manage risk & increase likelihood that established goals & objectives are achieved.

CONTROL PROCESSES: P&P, & activities that are part of a control framework, designed & operated to ensure that risks are contained within RISK APETITE of org.

⇒ CAE interviews BOD & SM about responsibilities of Stakeholders

BOD: Responsible for Governance

SM: Responsible for

- (i) Risk mgmt &
- (ii) Control

⇒ When determining strategy to assess GRC, CAE considers:-

- (i) Maturity of processes
- (ii) Seniority of responsible persons
- (iii) Org. Culture

⇒ GRC are ADEQUATE if mgmt. has planned & designed to provide REASONABLE ASSURANCE of achieving org.'s goals & objectives EFFICIENTLY & ECONOMICALLY.

⇒ REASONABLE ASSURANCE is provided if most cost-effective measures are taken in the D&I of controls

ASSURANCE SERVICES

- An objective examination of evidence for providing INDEPENDENT ASSESSMENT on GRC of an org.

- e.g. Financial, Performance, Compliance, Security & DUE DILIGENCE

CONSULTING SERVICES

- Advisory & related client service activities, the NATURE & SCOPE of which is agreed with client, are intended to ADD VALUE & improve GRC.

- e.g. TRAINING, ADVICE, COUNSEL & FACILITATION

2. I.A. ADMINISTRATIVE ACTIVITIES

⇒ IA is EFFECTIVELY MANAGED when: 

1. PAR are included in IA charter
2. It conforms with standards
3. Individual members conform with Ethics & Standards
4. Considers TRENDS & EMERGING ISSUES

⇒ CAE must establish P&P for IA activity.

FORM, CONTENT & REVIEW of P&P

Form & Content depends on:

1. Size of IA
2. Structure of IA
3. Complexity of work

Form: MATURE IA ⇒ FORMAL OPERATIONS MANUAL

CONTENT:

(a) POLICIES include

- (i) Purpose & responsibility
- (ii) Compliance with mandatory guidance
- (iii) Independence & Objectivity
- (iv) Ethics Requirements
- (v) CONFIDENTIALITY
- (vi) Retention of IA RECORDS

(b) PROCEDURES for

- (i) Drafting audit plan based on Risk assessment
- (ii) Drafting plan for specific engagements
- (iii) Performance and documentation
- (iv) Communication of results
- (v) Monitoring & follow-up

- (c) Guidance on QAI P
- (d) Mgmt of IA related to
 - (i) Professional training & certification
 - (ii) CPE
 - (iii) Evaluation of AUDITORS

REVIEW: P&P should be reviewed periodically by CAE or IA mgt.

⇒ CAE is responsible for creating BUDGET.

⇒ CAE is responsible for HIRING

⇒ Developing effective interviewing skills / techniques is reqd.

STRUCTURED INTERVIEWS

- Designed to eliminate individual bias
- Set of questions & standard answers

BEHAVIORAL INTERVIEW

- Determine how candidate handled PAST SITUATIONS
- Past performance is indicative of future performance

SITUATIONAL

JOB KNOWLEDGE

JOB SAMPLE SIMULATION

WORKER Requirement

3. STAKEHOLDER RELATIONSHIPS

AUDIT COMMITTEE MEMBER:

1. No member may be an employee of org., except as a BOD
2. At least 1 member is FINANCIAL EXPERT

ROLE OF AUDIT COMMITTEE

→ To promote independence of internal & external auditor by protecting from mgmt.'s influence

Regarding IA

1. Selecting CAE & compensation
2. Review IA's work
3. Resolve disputes b/w mgmt. & IA
4. Approve charter
5. Review & approve work plan
6. Communicating with CAE
7. Oversee corrective action for deficiencies
8. Enquiry with CAE & mgmt. to determine whether AUDIT SCOPE & BUDGETARY LIMITATIONS impede IA's ability

Regarding EA

1. Selecting EA & fee
2. Oversee & review work
3. Resolve disputes b/w EA & mgmt.
4. Review report.

PARTICIPATIVE AUDITING

- Objective is to minimize conflict b/w IA & mgmt.

4. INTERNAL AUDIT RESOURCE REQUIREMENT

CAE must ensure that the IA resources are APPROPRIATE, SUFFICIENT & EFFECTIVELY DEPLOYED to achieve Plan.

⇒ To determine SUFFICIENCY of RESOURCE ALLOCATION, CAE considers:-

1. Communication received from BOD & mgmt.
2. Information about ongoing & new engagements
3. Consequences of not completing engagement
4. KSC of staff.



⇒ COMPETENCIES of IA should be APPROPRIATE.

∴ CAE conducts documented SKILL ASSESSMENT

⇒ Resources need to be SUFFICIENT . . . , RESOURCE PLANNING includes :-
(i) Audit universe (iv) Coverage expectations
(ii) Relevant ~~risk~~^{risk} levels (v) Estimate of unplanned activities
(iii) IA Plan



⇒ Resources must be EFFECTIVELY DEPLOYED

Advantages of FIELD OFFICE

1. Reduced time & travel expense
2. Increased Authority ⇒ Better morale
3. Improved service
4. Possibility to employ person who don't wish to travel

⇒ While selecting appropriate audit staff CAE considers:-

1. Complexity of engagement.
2. Experience level
3. Training needs
4. Available resources

⇒ EXTERNAL SERVICE PROVIDER must make org. aware that responsibility of maintaining an effective IA lies with org. itself.

⇒ OVERSIGHT & RESPONSIBILITY of IA must NOT be outsourced.

5. COORDINATION

OPERATIONAL MANAGEMENT (First Line of Defense)

- Functions that own & manage risk

- D & I control & risk mgmt. process

BUSINESS ENABLING FUNCTIONS (2nd Line of Defense)

- Functions that OVERSEE risks (RISK OFFICER OR, CENTRALIZED COORDINATOR)

INTERNAL AUDIT (3rd Line of Defense)

- Provide independent assurance

→ CAE Should (1) Share info
(2) Coordinate activities
(3) Rely upon work of internal & external
assurance & consulting service providers
To (1) ensure proper coverage &
(2) Minimize duplication of efforts

⇒ INTERNAL PROVIDERS report to SM or be part of SM
↳ 2nd line of defense

⇒ EXTERNAL PROVIDERS report to SM, external parties
or, CAE

ASSURANCE MAPPING:

- Connects risk categories & sources of assurance
- Assess each category

COMBINED ASSURANCE MODEL: IA coordinates activities with
2nd line of defense

CRITERIA CAE uses to consider reliance on a Service provider:

- Objectivity, Independence, Competency & due prof care of provider
- Scope, objectives & results of the service provider
- Assess service provider's findings to see if they meet STANDARDS
- Incremental effort reqd.

UNIT-2: ASSURANCE & COMPLIANCE ENGAGEMENTS

1. ASSURANCE ENGAGEMENTS

ASSURANCE SERVICES: An objective examination of evidence to provide an independent assessment on GRC for the org.

- NATURE & SCOPE is determined by: IA.

FINANCIAL ASSURANCE

- Provides analysis of economic activity of an entity as measured & reported by ACCOUNTING METHODS.
- FINANCIAL AUDITING
 - ↳ Looks at PAST to determine whether financial info was properly recorded & adequately supported.
 - ↳ Assess whether FINANCIAL STATEMENT ASSERTIONS are Fair & Accurate

COMPLIANCE ASSURANCE

- Review of FINANCIAL & OPERATING controls to ASSESS CONFORMANCE with LAWS, STDS, P&P, contracts, etc.
- COMPLIANCE AUDITING
 - ↳ Looks at PAST & EXAMINES PRESENT to ask :-
 - (i) Adhered to law & reg.?
 - (ii) Currently comply with L&R?
 - (iii) What are our org.'s corporate stds of business conduct?
 - (iv) All staff & mgmt. comply with P&P?

OPERATIONAL ASSURANCE.

- Review of function/process to appraise EFFICIENCY & Economy of operations & EFFECTIVENESS with which those functions achieve its objectives.

- OPERATIONAL AUDITING

↳ Focussed on PRESENT & FUTURE.

↳ EVALUATES EFFECTIVENESS, EFFICIENCY & Economy of operations

↳ Includes areas like (a) Product Quality (b) Customer Service

(c) REVENUE MAXIMIZATION (d) EXPENSE MINIMIZATION

(e) FRAUD PREVENTION (f) ASSET SAFEGUARDING

(g) CSR (h) STREAMLINE WORKFLOW (i) SAFETY (j) Planning

ASSURANCE SERVICES

IT AUDITING

FINANCIAL
AUDITING

REPORTING

OBJECTIVES
of IC

COMPLIANCE
AUDITING

COMPLIANCE

OBJECTIVES
of IC

OPERATIONAL
AUDITING

OPERATIONAL

OBJECTIVES
of IC

ASSURANCE MAPPING

ASSURANCE MAP is a VISUAL REPRESENTATION of Risk & ASSURANCE activities. It includes following:

1. IDENTITY of Assurance providers
2. RISK
3. ASSURANCE LEVEL
4. URGENCY on Imp. of ISSUE
5. ACTION to be taken

1 ASSURANCE PROVIDERS are INTERNAL or EXTERNAL STAKEHOLDERS

- MANAGEMENT: Provides assurance through COMPLIANCE with laws & regulations, QA & SA.
- BOD: Provides assurance through IA
- EXTERNAL STAKEHOLDERS: Provide assurance through
 - i) Independent EA (ii) Govt. Regulators (iii) ISO

2. RISK determined by judging :-

- (i) INHERENT Risk of activity
- (ii) Risk that IC may not prevent or detect non-compliance
- (iii) POTENTIAL CONSEQUENCES of Non-Compliance

3. ASSURANCE LEVEL determined by considering:-

(i) QUALITY (ii) EXTENT & (iii) COST of IC

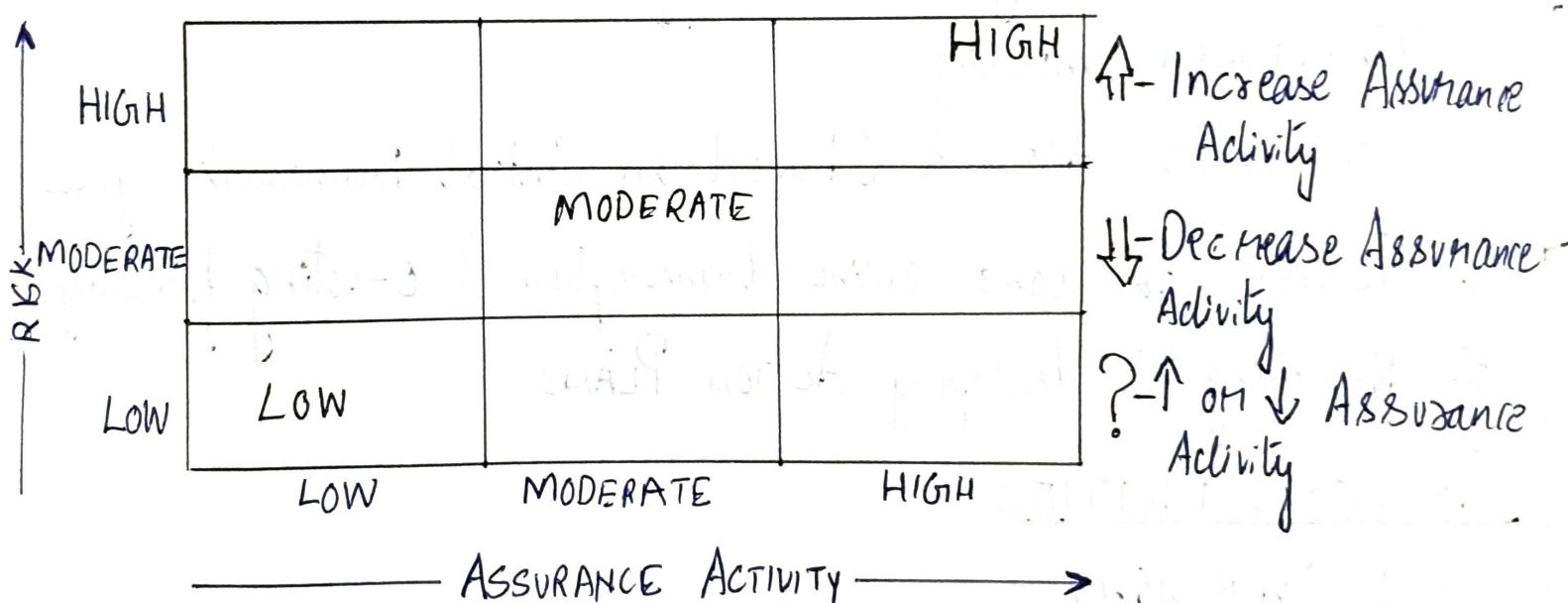
4. \uparrow RISK \Rightarrow \uparrow URGENCY

\downarrow RISK \Rightarrow \downarrow URGENCY

URGENCY \propto RISK

5. ACTION of URGENCY

ASSURANCE MAP



2. RISK AND CONTROL SELF-ASSESSMENT

⇒ Managers & Auditors are interested in :

(i) Improving assessment of RM & C

(ii) Identifying ways to improve effectiveness of RM & C

⇒ BASIC PHILOSOPHY : Control is RESPONSIBILITY of everyone.

ELEMENTS OF CSA

1. Front-end planning & Preliminary Audit work.

2. In-person meeting

3. STRUCTURED AGENDA (based on Control Framework e.g. Coso)

4. SCRIBE to take online transcription & e-voting for anonymity

5. Reporting & developing ACTION PLANS

RESPONSIBILITIES

SM: OVERSIGHT

OPERATING MANAGER: Assessment of R & C in their units.

IA & EA: ASSURANCE about EFFECTIVENESS of RM & C.

HOW IA USES CSA ?

1. SPONSOR, D&I, & OWN PROCESS

2. Conduct TRAINING

3. Supply FACILITATORS, SCRIBE & REPORTERS

4. Coordination b/w mgmt. & work teams

⇒ CAE (a) Monitors OBJECTIVITY of IA Staff
· (b) Takes steps to MANAGE OBJECTIVITY
· (c) AUGMENTS IA testing to ensure BIAS
OR PARTIALITY don't affect final judgement.

⇒ A CSA Program (a) Increases Coverage of Assessment of C
(b) Improves QUALITY of CORRECTIVE ACTIONS
(c) Focus IA's work on HIGH RISK processes

⇒ CSA also FOCUSES on
(a) VALIDATING the EVALUATION CONCLUSIONS by CSA
(b) SYNTHESIZE Info gathered
(c) EXPRESS OVERALL JUDGEMENT about
EFFECTIVENESS of C to SM & BOD.

KEY FEATURES

1. Identify key risks
2. Assessing control processes that MITIGATE or MANAGE Risks
3. Develop ACTION PLANS to reduce risk to acceptable levels
4. Determine LIKELIHOOD to achieve objectives

⇒ CSA ASSUMES Mgmt. & WORK-TEAMS UNDERSTAND
RISK & CONTROL CONCEPTS.

OUTCOMES

1. People in BUS. get TRAINED in ASSESSING R & C
2. Informal, SOFT Controls are MORE EASILY Identified
3. People are MOTIVATED to take OWNERSHIP of Controls
4. Entire Objectives-Risk-Control Structure is Subject to GREATER MONITORING & continuous improvement.
5. IA Staff learns about CSA by serving as FACILITATORS
6. IA can LEVERAGE Additional information to ALLOCATE SCARCE RESOURCES
 - ↳ Greater effort devoted to SIGNIFICANT CONTROL WEAKNESS & HIGH-RESIDUAL RISK
7. Mgmt's responsibility of RM & C. is reinforced.
8. PRIMARY Role of IA continues to be VALIDATION of Adequacy & effectiveness of RM & C system

APPROACHES

- Reflects differences in (a) INDUSTRY (b) GEOGRAPHY (c) STRUCTURE
(d) CULTURE (e) Degree of emp. empowerment
(f) Mgmt. Style (g) Manner of planning

FACILITATION APPROACH

OBJECTIVE BASED FORMAT

Focus: BEST WAY to accomplish
a business objective

Aim: ARE Control procedures
working effectively to keep
RESIDUAL RISK under ACCEPTABLE
LEVELS?

CONTROL BASED FORMAT

Focus: How well controls are
working?

Aim: GAP b/w how controls
are working & how mgmt.
expects them to work.

⇒ FACILITATOR identifies R&C
before starting workshop.

RISK BASED FORMAT

- List All Risks to achieve an objective
- Determine Significant RESIDUAL RISKS

PROCESS BASED FORMAT

- Selected activities that are elements of a chain of processes
- Evaluate, validate, update, improve & STREAMLINE the PROCESS
- Provides GREATER BREADTH of analysis than CONTROL BASED APPROACH

SURVEY APPROACH

- Tend to ask YES/NO or, have/havenot questions
- Used when there are MANY RESPONDENTS
- Used when org. culture LIMITS OPEN, CANDID discussions
- Used when mgmt. desires to MINIMIZE COST of gathering information

SELF-CERTIFICATION APPROACH

- USE MANAGEMENT produced analysis about Selected BP, RM & C activities
- IA uses this analysis + OTHER info to enhance understanding about control & share knowledge with mgmt.

LIMITATIONS

1. IA may not use CSA Approaches EFFECTIVELY
2. Persons performing SA may not be SKILLED in RM&C
3. Relevant Risks & Controls may not be identified or assessed.

3. AUDITS OF THIRD PARTIES AND CONTRACT AUDITING

EXTERNAL BUSINESS RELATIONSHIPS

EBRs may involve following :-

1. Service Providers
2. Supply-Side Partners
3. Demand-Side Partners
4. Strategic Alliances & JVs
5. Intellectual Property (IP) Partners

⇒ EBR partners may offer :-

1. Lower costs
2. Better Operational Efficiency
3. ~~Special~~ ^{NEW} Technology
4. Special Expertise
5. Economies of Scale

⇒ IA helps mgmt. identify, assess, manage & control
REPUTATION RISKS & ECONOMIC RISKS

SIGNIFICANT RISKS OF EBR

1. EBRs not identified at all & so, not managed in accordance with P&P, assessed OR monitored.
2. Reputation Risk
3. INADEQUATE INSURANCE COVERAGE
4. Service/Product is Unsatisfactory
5. Conflicts of Interest
6. Licensing of IP
7. EBR Partner may become INSOLVENT
8. OVERCHARGED for
9. CONFIDENTIAL Info may be lost

AUDITING EBRs

⇒ IA MUST first determine whether EBR has agreed to Audit
↳ AUDIT CLAUSE should be created in CONTRACT.

⇒ IA needs to understand all elements of EBR

1. Initiating an EBR
2. Contracting for EBR
5. Discontinuing EBR
3. Procurement
4. Managing & Monitoring EBR
(including control environment considerations of I&O of mgn.)

⇒ AUDIT PROCEDURES may:-

1. Discover MISSED REVENUE
2. IMPROVE REPORTING
3. ADD VALUE by:
 - (i) LIMITING FRAUD
 - (ii) INCREASING TRUST
 - (iii) Fostering feedback
 - (iv) Improving relationships
 - (v) Improve IC&EC

⇒ CAE DECIDES WHETHER to AUDIT

- (1) Each EBR Separately
- (2) Certain EBRs
- (3) Total EBRs

CYCLE OF EBR AUDIT

1. Understanding the org., its environment, its processes, & nature of EBR
2. ASSESSING EBR
3. Performing AUDIT
4. REPORTING
5. MONITOR Progress

THIRD PARTY AUDITS

- ⇒ Routine for org.s that ISSUE GENERAL-USE financial statements & for many EBRs.
- For e.g. if. org. is a Service provider, IA & EA must obtain assurance about Security of operations & CONTRACTUAL Obligations
 - Performed by a QUALIFIED REGISTRAR like ISO 9000
- ⇒ IA & 3rd Party AUDITORS COORDINATE with each other

CONTRACT AUDITING

LUMP-SUM CONTRACTS

- IA may have LITTLE to EVALUATE when work is performed in accordance with contract.
- Agreement should consider :-
 1. Progress payments
 2. INCENTIVES (e.g. for early completion)
 3. ESCALATOR CLAUSE
(e.g. Entire price to be due in case of BREACH of CONTRACT)
 4. Adjustment to LABOUR costs
 5. CHANGE ORDERS

COST-PLUS CONTRACTS

- Ways to cope with uncertainties about COST by setting PRICE =
 1. COST + FIXED Amount
 2. COST + FIXED %
- PROBLEM: LITTLE INCENTIVE for ECONOMY + EFFICIENCY
- PROVISION FOR :-
 1. MAXIMUM COSTS, with SAVINGS Shared by parties
 2. INCENTIVES for EARLY COMPLETION

UNIT PRICE CONTRACTS

- Used when convenient measure of work is available
 - ↳ KEY ISSUE: ACCURATE MEASUREMENT OF WORK
- IA should be involved throughout CONTRACTING PROCESS

SOURCE CODE Escrow CLAUSE

- ↳ When reviewing Contract for purchase of BUSINESS APPLICATION SYSTEM, IA should RECOMMEND this CLAUSE
 - ↳ Requires APPLICATION SOURCE CODE to be held in ESCROW by a trusted 3rd party
 - ↳ 3rd party RELEASES Source code to PURCHASER, or LICENSEE, on OCCURENCE of event Specified in clause

4. QUALITY AUDITING

TRADITIONAL VIEW: Rejection or Reworking of DEFECTIVE Goods.

MODERN VIEW: QUALITY is a VALUE ADDED Activity throughout all processes, from product design → Raw material acquisition

↓
Final Inspection

TOTAL QUALITY MANAGEMENT

- ⇒ Increases Revenue & Decreases Cost Significantly.
- ⇒ Continuous Pursuit Of Quality through:
 1. Philosophy of doing it right the first time
 2. Employee training & empowerment
 3. Promotion of teamwork
 4. Improvement of Processes
 5. Attention to Satisfaction of internal & external customers

★ ⇒ Role of IA (not just CAE) is to EVALUATE entire QUALITY FUNCTION

1. IA is well qualified to perform RISK ASSESSMENT & PROMOTE CONTINUOUS IMPROVEMENT.
 - ↳ Personnel involved with technical improvements may not qualified w.r.t. RM & C
2. IA performs procedures to provide assurance that basic objectives of TQM are reached:
 - (i) Customer Satisfaction
 - (ii) Continuous Improvement
 - (iii) Promotion of teamwork
3. TQM applies to IA as well. For e.g. PERIODIC INTERNAL ASSESSMENT

5. SECURITY AND PRIVACY AUDITS

NOTE: PHYSICAL SECURITY, such as SAFEGUARDS against Environmental risks & WRONGFUL USE/ACCESS to COMPUTERS, must be AUDITED, Even if S/W provides most of PROTECTION ~~from Security~~ for information.

INFORMATION SECURITY AUDITING

1. IA may ACT in CONSULTING CAPACITY to IDENTIFY SECURITY issues & by working with Users to D&I controls.
2. IA works with SM & BOD to ASSIST in performance of governance function w.r.t. Information Security.

IMPLEMENTATION STANDARD 2130.A1

⇒ IA MUST EVALUATE the adequacy & effectiveness of Controls in responding to the risks within org.'s governance, operations & IS regarding the:

1. Achievement of org.'s Strategic Objectives
2. Reliability & Integrity of financial & operational information
3. Effectiveness & Efficiency of operations & programs
4. SAFEGUARDING of ASSETS
5. Compliance with LAWS, REGULATION, P&P, Contracts

INFORMATION RELIABILITY AND INTEGRITY

1. Information reliability includes ACCURACY, COMPLETENESS & SECURITY.
IA determines whether SM & BOD clearly understand that it is MANAGEMENT RESPONSIBILITY for ALL CRITICAL INFORMATION regardless of its FORM.
2. CAE determines whether SM & BOD & IA will be promptly notified about THREAT
3. IA periodically assess effectiveness of preventive, detective & mitigative measures against past & future attacks.

PRIVACY AUDITING

DEFINITIONS of PRIVACY:

1. Personal Privacy (PHYSICAL + PSYCHOLOGICAL)
2. Privacy of Space (Freedom from Surveillance)
3. Privacy of Communications (Freedom from Monitoring)
4. Privacy of Information (Collection, Use, & Disclosure of PI by others)

⇒ BOD is ULTIMATELY RESPONSIBLE for identifying principal risks, implementing controls & managing Privacy Risks
e.g. By establishing & monitoring privacy framework.

IIA's CODE OF ETHICS

1. IA shall be PRUDENT in USE & PROTECTION of information
2. IA shall NOT USE information for PERSONAL GAIN

6. PERFORMANCE AUDITING

⇒ PROVIDES ASSURANCE about org.'s KEY PERFORMANCE INDICATORS.

- Consulting engagement may be performed to DESIGN a PMS.

1. Effective mgmt. control requires PERFORMANCE MEASUREMENT & FEEDBACK

2. Performance Evaluation Model may be INCONSISTENT with Org.'s model of Managerial Decision Making.

↳ To achieve consistency, models should be in SYNC

BALANCED SCORECARD

⇒ CONNECTS CRITICAL SUCCESS FACTORS with financial/non-financial MEASURES of ELEMENTS of PERFORMANCE.

- CSFs are identified by SWOT Analysis

- Specific, Reliable measures must be determined for each factor

- Balanced Scorecard DE-EMPHASIZES short term financial results & FOCUSES on FUTURE SUCCESS

⇒ DEVELOPMENT & IMPLEMENTATION of COMPREHENSIVE BALANCED SCORECARD requires ACTIVE PARTICIPATION by SM.

1. BSC should contain DETAILED MEASURES to permit everyone to understand how higher efforts affect results
2. BSC & Strategy must be communicated to all managers & used as a basis for COMPENSATION Decisions
3. Determine whether objectives are achieved at expense of others. e.g. Reduce Customer Service Spend $\Rightarrow \downarrow$ CSAT

⇒ BSC includes MEASURES in 4 categories

1. FINANCIAL - ULTIMATE Results provided to owners
2. CUSTOMER - Measures Customer needs & CSAT
3. INTERNAL measures of key processes drive business.
e.g. QUALITY, PRODUCTIVITY, FLEXIBILITY of RESPONSE to change
4. LEARNING, GROWTH & INNOVATION measures are basis for FUTURE SUCCESS

7. OPERATIONAL AUDITING

PROCESS (FUNCTIONAL) ENGAGEMENT

→ Follow process-crossing organisational lines, service units

Focus: How EFFECTIVELY & EFFICIENTLY Org. units CO-OPERATE

↳ CHALLENGES due to SCOPE & Conflicting objectives

Typical Processes :-

1. Purchasing & Receiving
2. Distribution of Services
3. Modification of products
4. SCRAP Handling
5. BUDGET Development
6. Marketing

PROGRAM RESULTS ENGAGEMENT

- Because benefits can't be quantified in financial terms, special concern is ability to measure EFFECTIVENESS
- Program is a FUNDED ACTIVITY NOT part of NORMAL Continuing operations of the org. e.g. Expansion of IS

$$\text{PRODUCTIVITY RATIO} = \text{O/P} \div \text{I/P}$$

PRODUCTIVITY INDEX measures PRODUCTION POTENTIAL

RESOURCE USAGE RATE measures Resource Use relative to Available resources

OPERATING RATIO measures OPERATIONAL EFFICIENCY

8. COMPLIANCE AUDITING

COMPLIANCE: Adherence to Plan, Policies, Procedures, Laws, Regulation, Contracts, OR other requirements.

⇒ IA is encouraged to consult LEGAL COUNSEL in all matters involving legal issues. Requirements may vary significantly in different jurisdictions.

COMPLIANCE PROGRAMS help in:-

1. Provide insurance claims
2. Determining DIRECTOR/OFFICER LIABILITY
3. CREATE/Enhance Corporate Identity
4. Decide appropriateness of punitive damages.

RESPONSIBILITY

1. SM should be involved
2. High-level personnel should have SUBSTANTIAL CONTROL of the org. & SUBSTANTIAL ROLE in making Policy.
3. CHIEF COMPLIANCE OFFICER should report directly to the CEO

MONITORING & REPORTING

Monitoring & AUDITING Systems for DETECTING ILLEGAL/UNETHICAL behavior & EMPLOYEE HOTLINES should be used.

COMPLIANCE REVIEW considers:-

1. Effectiveness of written material
2. Employee Receipt of Communication
3. Handling of VIOLATIONS
4. FAIRNESS of DISCIPLINE
5. Observance of any protection given to informants
6. Fulfilment of COMPLIANCE UNIT responsibilities

⇒ ATTORNEY-CLIENT & ATTORNEY-WORK-PRODUCT PRIVILEGES
protect certain info disclosed to (or produced by) an ATTORNEY
from being used by an adverse party in a legal proceeding.

⇒ An ATTORNEY MONITORING the HOTLINE is BEST

⇒ Employees may have little confidence in :-

1. HOTLINES
2. WRITE-IN REPORTS
3. OFFSITE PERSON assigned to hear Compliants

⇒ Employees may have confidence in :-

HOTLINE answered by INHOUSE Representative & backed by NON-
RETALIATION POLICY

* HOTLINE DOES NOT ASSURE ANONYMITY

⇒ OMBUDPERSON : On-site official to receive & investigate
Complaints

OMBUDPERSON is more effective if he/she :-

1. Reports directly to CHIEF COMPLIANCE OFFICER
2. Keeps name of informants secret
3. Provides guidance to informants
4. Follow-up to ensure retaliation has not occurred

⇒ FAILURE to DETECT/PREVENT a serious violation indicates that
COMPLIANCE PROGRAM needs to be RESTRUCTURED

↳ COMPLIANCE PERSONNEL MAY be TRANSFERRED OR REPLACED

UNIT-3: FINANCIAL, ENVIRONMENTAL & CONSULTING ENGAGEMENTS

1. FINANCIAL ENGAGEMENTS

PERFORMANCE STANDARD: IA Activity must evaluate the effectiveness & contribute to the RM process.

INTERPRETATION OF STD.: Determining whether RM process are effective is a judgement resulting from assessment that:-

1. Org. objectives align with org. mission
 2. Significant risks are identified
 3. Risk Response Align with RISK APPETITE
- & Relevant risk info is captured & communicated timely

IMPLEMENTATION OF STD.

IA must evaluate RISK EXPOSURES related to org.'s governance, Operations, & IS regarding the :-

1. Achievement of org.'s objectives
2. Reliability & Integrity of financial & operational info
3. Effectiveness & Efficiency of operations & programs
4. Compliance with laws, regulations, P&P and CONTRACTS.

MANAGEMENT'S ASSERTIONS

Mgmt. implicitly or explicitly makes assertions about measurement, presentation & disclosure of financial stmts.

- Part of any engagement may involve testing these assertions whether they are supported with evidence
- Determining if assertions are supported with evidence helps IA to determine if controls are working as designed.

KEY RISKS

Key risks affecting RELIABILITY & INTEGRITY of financial info include:

1. OVERSTATING REVENUES (e.g. IMPROPER TIMING of REVENUE Recognition)
2. UNDERSTATING EXPENSES (e.g. IMPROPER CAPITALIZATION of expense)
3. Applying Unreasonable Accounting Estimate (e.g. accounting estimates are neither consistent with PAST Results nor FUTURE)
4. Applying Accounting Principles that are no longer in effect.

FRAUD RISK

⇒ AUDITOR'S INITIAL RESPONSIBILITY regarding ERRORS DISCOVERED is to ASSESS RISK OF MISREPRESENTATION.

1. FRAUDULENT FINANCIAL REPORTING

↳ INTENTIONAL Misstatement of data

2. MISAPPROPRIATION OF ASSETS

↳ RESULT from THEFT, EMBEZZLEMENT OR, an action that causes payment for items not received

PERFORMANCE STANDARD

TA must participate in maintaining EFFECTIVE Controls by evaluating their effectiveness & efficiency & by promoting CONTINUOUS IMPROVEMENT

IMPLEMENTATION STD.

The TA activity must evaluate the adequacy & effectiveness of controls in responding to risks with org's governance, operations & responding the re

1. Achievement of org.'s strategic objective
2. Reliability & Integrity of financial & operational info
3. Effectiveness & Efficiency of operations & programs
4. Safeguarding of assets
5. Compliance with L, R, P&P & Contracts

⇒ NON-DISCOVERY is most likely to suggest a VIOLATION of the IPPF

⇒ Evaluating EFFECTIVENESS of CONTROLS :- RCM is USED

⇒ Evaluating EFFICIENCY of CONTROLS :- Internal Auditors consider whether mgmt. MONITORS the COSTS + BENEFITS of CONTROL.

(i) Resources >> Benefits (ii) Controls create significant issues

⇒ Promoting CONTINUOUS IMPROVEMENT

- CAE may recommend a CONTROL FRAMEWORK IF none exists
- IA may recommend improvements in CONTROL ENVIRONMENT

REPORTING ON EFFECTIVENESS OF INTERNAL CONTROL

⇒ CAE's report is USUALLY presented ANNUALLY to SM & BOD.

Report describes :-
(i) Role of Control processes
(ii) Work performed
(iii) Reliance on other assurance providers

⇒ BOD MUST RELY on mgmt. to MAINTAIN Adequate & Effective IC.

- It RE-INFORCES this reliance by INDEPENDENT OVERSIGHT

1. Controls are EFFECTIVE if mgmt. directs processes to provide REASONABLE ASSURANCE that OBJECTIVES are ACHIEVED
2. Controls are ADEQUATE if mgmt. has designed them to provide REASONABLE ASSURANCE that
 - (a) RISKS are MANAGED EFFECTIVELY
 - (b) OBJECTIVES are ACHIEVED EFFECTIVELY

ROLES FOR THE INTERNAL AUDITOR

- ⇒ CAE's ALLOCATION of RESOURCES & Org.'s RISK ASSESSMENT to FIN. REP., GOVERNANCE & CONTROL PROCESSES
- ⇒ CONTROLS need to be ADEQUATE to ENSURE:
 1. Prevention & Detection of FRAUD
 2. Prevention & Detection of SIGNIFICANT ERRORS
 3. Prevention & Detection of INCORRECT ASSUMPTIONS + ESTIMATES
 4. Prevention & Detection of OTHER Events that cause INACCURATE

FINANCIAL REPORTING

1. Providing info relevant to appointment of Independent Accountants
2. CO-ORDINATING Audit Plans, Coverage & Scheduling with external Auditors
3. Sharing Audit RESULTS with EA
4. Communicating PERTINENT Observations to EA
5. Participating in Financial Reports & Disclosure review process with BOD, SM & EA
6. EVALUATE Quality of Financial Reports
7. Assess ADEQUACY + EFFECTIVENESS of IC related to FCRP
8. Monitoring mgmt.'s COMPLIANCE with Code of Conduct

GOVERNANCE

- ⇒ Reviewing Org.'s Policies relating to:-
 - (i) COMPLIANCE with L & R
 - (ii) ETHICS
 - (iii) COI
 - (iv) FRAUD
- ⇒ Reviewing pending litigation or regulatory proceedings
- ⇒ Providing info on employee COI, misconduct, FRAUD, etc

CORPORATE CONTROL

1. Reviewing the Reliability & Integrity of Operating & Financial info
2. Analysis of Controls over CRITICAL A/c policies & comparing with preferred practices. e.g. off-b/s A/c treatment compared to IFRS
3. EVALUATING reasonableness of ESTIMATES + ASSUMPTIONS
4. EVALUATING process of preparing, reviewing, approving & posting JEs
5. EVALUATING ADEQUACY of controls in A/C function
6. Ensure ESTIMATES + ASSUMPTIONS are CONSISTENT with org. info & similar items reported by other org.

2. ENVIRONMENTAL ENGAGEMENTS

⇒ CAE includes EHS risks in any org-wide Risk Assessments

RISK EXPOSURES :-

1. Org. Reporting Structure
2. Likelihood of causing environmental harm, FINES & PENALTIES
3. Expenditures mandated by govt.
4. HISTORY of INJURY + DEATH
5. HISTORY of LOSING Customers
6. Episodes of -ve PUBLICITY

ENVIRONMENTAL AUDIT FUNCTION

1. CAE & EA Executive are in separate functional units + LITTLE CONTACT
2. CAE & EA Executive are in separate functional units + CO-ORDINATE Activities
3. CAE has responsibility of EA

RESEARCH FINDINGS

1. EHS Audit function is ISOLATED from other Audit activities
2. EHS mgn. report to PHYSICAL FACILITIES being AUDITED
3. Audit Reports not distributed above Senior Environmental Executive
4. ACCESS to EHS Audit info is RESTRICTED

ROLE of CAE

1. If environmental audit function does not report to CAE Then,
 - (i) CAE offers to review audit plan
 - (ii) Performance of engagements
 2. Periodically, CAE schedules QAR of EAF, If EAF is organizationally independent of IA activity.
 3. An EHS Audit Program may be:
 - (a) COMPLIANCE-focused
 - (b) Mgmt. System-focused
 - (c) COMBINATION of both
 4. CAE evaluates whether environmental auditors, who are NOT part of CAE's org., are CONFORMING with(i) AUDIT Stds
& Independence(ii) Code of Ethics
 5. CAE evaluates org. placement of EAF, to ensure issues are reported to BOD.
- ⇒ It is an advantage to conduct audits under the direction of IA activity, because of its position within the org.

ENVIRONMENTAL AUDITING

IF environmental L&R have significant impact on org.
THEN org. Should ESTABLISH an EMS

FEATURES of EMS:-

- (i) Reviewing adequacy & effectiveness of controls for HAZARDOUS WASTE
- (ii) Review of REASONABILITY of CONTINGENT LIABILITIES ACCRUED from environmental remediation

SEVEN TYPES OF AUDITS

1. COMPLIANCE AUDIT : Most Common for INDUSTRIAL org.
EXTENT & Degree of NON-COMPLIANCE

- ⇒ Usually involve review of All environmental MEDIA, the site contamination e.g. AIR, WATER, LAND
- ⇒ Usually range from PRELIMINARY ASSESSMENTS to:-

(i) Detailed Tests (ii) INSTALL Ground Water Wells (iii) Laboratory

2. EMS AUDIT : MAY Arise from practices that were LEGAL when undertaken.

TRANSACTIONAL AUDIT

↳ ASSESS environmental RISK + LIABILITIES of LAND/FACILITIES
PRIOR to SALE/PURCHASE of PROPERTY.

↳ Requires DUE-DILIGENCE from auditor at each phase

PHASE - 1 : QUALITATIVE SITE Assessment involving review of records + SITE RECONNAISSANCE

PHASE - 2 : SAMPLING for POTENTIAL CONTAMINATION

PHASE - 3 : CONFIRM RATE of Contamination + Cost of Remediation

4. TREATMENT, STORAGE & DISPOSAL FACILITY

- ⇒ HAZARDOUS MATERIALS tracked from ACQUISITION → CREATION → DISPOSAL, by means of a document (MANIFEST)
- ⇒ ALL OWNERS in chain of title may be LIABLE
- ⇒ If OUTSIDE VENDOR is used for TSDF Then :-
 - (i) REVIEW Vendor's documentation on HAZARDOUS MATERIAL
 - (ii) Review FINANCIAL SOLVENCY of Vendor
 - (iii) Review EMERGENCY RESPONSE PLANNING of Vendor
 - (iv) Vendor APPROVED by Govt.
 - (v) Obtain Vendor's PERMIT number
 - (vi) INSPECT Vendor's facilities

5. POLLUTION PREVENTION AUDIT

1. Recovery as useful product
2. Elimination at Source
3. RECYCLE + REUSE
4. ENERGY CONSERVATION
5. TREATMENT
6. DISPOSAL
- (7) RELEASE w/o TREATMENT

6. ENVIRONMENTAL LIABILITY ACCRUAL AUDIT

IA. may be responsible for ASSESSING REASONABILITY of COST ESTIMATE for environmental remediation

7. PRODUCT AUDITS

Determine whether products are environment friendly or not.

Process may result in development of :-

1. Fully Recyclable Products
2. Change in Use + Recovery of packaging
3. Phaseout of Some chemicals

3. CONSULTING ENGAGEMENTS - OVERVIEW

"ADVISORY + Related client service activities, the NATURE & SCOPE of which are agreed with the client, are intended to ADD VALUE & IMPROVE GRC, without assuming mgmt. responsibility."

⇒ NATURE of CONSULTING Services MUST BE DEFINED in CHARTER

⇒ ASSURANCE can result from CONSULTING Engagements as well

⇒ CONSULTING does not IMPAIR IA's objectivity

↳ Objectivity is not impaired by decisions made by mgmt.

⇒ CAE should DISCLOSE/PRESENT info to SM & BOD, even if found during a CONSULTING ACTIVITY

⇒ IA is first & foremost an IA.

↳ All services to be performed in accordance with IIA Code of Ethics, Attribute, Performance Std. & IPPF

↳ RESOLUTION OF CONFLICTS need to be consistent with CODE of ETHICS + Stds.

FORMAL CONSULTING

↳ Planned & Subject to written agreement.

2. INFORMAL CONSULTING

1. Participation on STANDING COMMITTEE (3) AD-HOC Meetings
2. Limited Life Project (4) ROUTINE info exchange

3. SPECIAL CONSULTING

Engagements include participation on a M & A team OR, SYSTEM CONVERSION TEAM

4. EMERGENCY CONSULTING

Engagements include participation on a team

(a) Established for recovery or maintenance of ops after DISASTER + EXTRAORDINARY BUSINESS EVENT

(b) Assembled to supply TEMPORARY HELP to meet UNUSUAL DEADLINE

⇒ AUDITORS generally should not agree to conduct CONSULTING eng.
IF, an ASSURANCE engagement is MORE APPLICABLE.

4. CONSULTING ENGAGEMENTS - INTERNAL AUDITOR

⇒ IAs may provide consulting services relating to ops for which they had previous responsibilities

⇒ IF IMPAIRMENT to INDEPENDENCE & OBJECTIVITY are made

- (i) PRIOR to commencement of engagement OR,
- (ii) DURING the engagement

IMMEDIATE DISCLOSURE to mgmt.

⇒ INDEPENDENCE & OBJECTIVITY are IMPAIRED IF

Assurance Services provided within 1 year of
FORMAL CONSULTING engagement

⇒ MINIMIZE effects of IMPAIRMENT by :-

1. Assigning different audits

2. Establish independent mgmt. & Supervision

3. Defining SEPARATE ACCOUNTABILITY

4. DISCLOSE PRESUMED IMPAIRMENT. Mgmt. RESPONSIBLE for accepting & implementing recommendations

DUE PROFESSIONAL CARE

IA's exercise DPC by understanding:-

1. NEEDS of mgmt.

5. Effect on Scope of AUDIT PLAN

2. Possible MOTIVATION

6. POTENTIAL IMPACT on FUTURE engagements

3. EXTENT of WORK

7. POTENTIAL Org. Benefits

4. SKILLS + Resources needed

⇒ IA's DECLINE to perform Consulting engagements that :-

1. Are prohibited by CHARTER

2. CONFLICT with P&P of IA activity

3. Do NOT ADD VALUE to org.

⇒ RISK BASED PLAN may INCORPORATE & RELY on CONSULTING eng

SCOPE OF WORK

IF mgmt makes special request AND IA believes objectives Go BEYOND those requested by mgmt.

THEN,

1. PERSUADE mgmt. to include additional objectives
2. DOCUMENT FAILURE to pursue objectives
 - + DISCLOSE observation in FINAL Engagement Communication
 - + INCLUDE those objectives in a Separate ASSURANCE engagement

COMMUNICATING RESULTS

⇒ Communication of progress & results VARY in FORM & CONTENT depending on (i) NATURE of engagement
(ii) Needs of client

⇒ CAE is RESPONSIBLE for COMMUNICATING FINAL RESULTS

⇒ During CONSULTING engagement, IF GRC issues are IDENTIFIED,

THEN → COMMUNICATE to SM & BOD

⇒ IA may communicate results beyond those who requested or received service. ∴ IA takes following steps until satisfied with resolution of matter:-

1. DETERMINE GUIDANCE provided in AGREEMENT of Consulting engagement
2. PERSUADE to EXPAND communication to appropriate parties
3. DETERMINE GUIDANCE per IA CHARTER
4. DETERMINE GUIDANCE per org.'s code of conduct, ethics, other policies
5. DETERMINE GUIDANCE PER IIA stds & CODE OF ETHICS

⇒ IAS DISCLOSE to SM & BOD, NATURE EXTENT & OVERALL RESULTS of FORMAL CONSULTING engagements.

↳ NEITHER Detail reports NOR Specific results are required to be communicated

↳ BUT An APPROPRIATE Description of type of engagement & SIGNIFICANT Recommendations are communicated

↳ INFORM mgmt. & BOD about HOW AUDIT RESOURCES ARE DEPLOYED

DOCUMENTATION

⇒ CAE must develop P&P governing CUSTODY + RETENTION + RELEASE of records.

⇒ DOCUMENTATION requirements for ASSURANCE engagements are DIFFERENT than that of CONSULTING engagements

5. BENCHMARKING

⇒ PRIMARY Tools USED in T&M. ⇒ SOURCE for CONSULTING ENGAGEMENTS

⇒ CONTINUOUS EVALUATION of practices in BEST Orgs in their class + ADAPTATION of processes to reflect Best of these practices

1. COMPETITIVE BENCHMARKING

- Studies org. in SAME INDUSTRY

2. GENERIC BENCHMARKING

- Observes process in one operation & companies with process having similar characteristics

- BUT IN DIFFERENT INDUSTRY

PROCESS (FUNCTION) BENCHMARKING

- ⇒ Studies OPERATIONS of Org. with SIMILAR PROCESSES REGARDLESS of INDUSTRY
- ⇒ BENCHMARK NEED NOT BE A COMPETITOR OR, even SIMILAR Org.
- ⇒ MAY INTRODUCE IDEAS with Significant Competitive advantage

STRATEGIC BENCHMARKING

- ⇒ Search for Successful competitive strategies

INTERNAL BENCHMARKING

- ⇒ Application of BEST PRACTICES in one part of the org. To other parts

BENCHMARKING PROCESS

PHASE - I

PHASE - II

- ⇒ SELECT & PRIORITIZE Benchmarking projects
 1. Understand CSF of org. & then develop parameters defining what process to benchmark
 2. CRITERIA for Selecting what to Benchmark & CSAT
- ⇒ ORGANIZE BENCHMARKING TEAMS
 - TEAM organization permits FAIR DIVISION of LABOUR
 - Benchmarking Team must thoroughly document & investigate internal processes

PHASE - III { MOST DIFFICULT PHASE }

- ⇒ RESEARCHING & IDENTIFYING Best-in-class performance
- 1. Setting up DBs
- 2. Choosing info gathering methods
- 3. FORMATTING QUESTIONNAIRES
- 4. SELECTING BENCHMARKING PARTNERS

PHASE - IV

DATA ANALYSIS

1. IDENTIFY GAPS
2. UNDERSTAND REASONS for GAPS
3. PRIORITIZE ACTION ITEMS

PHASE - V

- ⇒ LEADERSHIP is MOST IMPORTANT in IMPLEMENTATION PHASE

6. CONSULTING ENGAGEMENTS - OTHER TYPES

1. INTERNAL CONTROL TRAINING

1. IAs may perform consulting engagements to provide IC training
2. Co-ordination b/w IA & EA \Rightarrow JOINT TRAININGS
3. CSA provides training to other employees
4. ETHICAL CULTURE & GOVERNANCE PROCESSES of an org.

ETHICAL CULTURE is MOST IMP. SOFT CONTROL

\Rightarrow IAs may take up roles like ETHICS EXPERT or ETHICS COUNSELOR

2. DUE DILIGENCE AUDITING

- \Rightarrow DETERMINE the BUSINESS JUSTIFICATION of a MAJOR TRANSACTION & whether JUSTIFICATION is VALID or not.
- \Rightarrow ESTABLISHES WHETHER EXPECTED BENEFITS of TRANSACTION are LIKELY to be REALIZED
- \Rightarrow EFFECTIVENESS + EFFICIENCY of engagement & CO-ORDINATION b/w Groups involved
 - For e.g. USE SAME SW for preparation of electronic wks
 - For SHARING INFO
- \Rightarrow MAY BE USED for ENVIRONMENTAL Audits

3. BUSINESS PROCESS MAPPING

→ BUSINESS PROCESS RE-ENGINEERING

- Involves PROCESS INNOVATION + PROCESS REDESIGN
- DOES NOT IMPROVE existing procedures
- Finds NEW WAYS to do things

↳ EMPHASIS: ELIMINATE NON-VALUE ADDING ACTIVITIES

↳ NOT a CONTINUOUS PROCESS

↳ Should be Reserved for MOST IMPORTANT PROCESSES

⇒ WORK MEASUREMENT

- Involves ANALYSIS of Activities

1. APPROPRIATE When mgmt. uses ENGINEERED COST APPROACH.

↳ WORKLOAD is DIVISIBLE in CONTROL FACTOR UNITS.

↳ VARIABLE Cost = Cost of CONTROL FACTOR UNIT

2. MICROMOTION STUDY = Videotaping assembly line activities

3. WORK SAMPLING = Random Observation of an activity
To DETERMINE STEPS reqd.

⇒ BPR + TQM ELIMINATE TRADITIONAL CONTROLS

1. Assume that humans will be MOTIVATED to work actively

2. EMPHASIS on developing AUTOMATED + SELF-CORRECTING Controls
that require MINIMAL HUMAN INTERVENTION

4. SYSTEM DEVELOPMENT REVIEWS

- ⇒ IA involvement in SDLC can ensure
- (i) Appropriate IC } are included in application
(ii) AUDIT TRAIL }
- ⇒ BASIC CONTROL ISSUES should be addressed in All System development & acquisition work :-
1. User Requirements should be documented
 2. SYSTEM DESIGN Should follow FORMAL PROCESS
 3. SYSTEM DEVELOPMENT Should be STRUCTURED
 4. TESTING Should ensure elements work as per requirement
 5. APPLICATION MAINTENANCE & CHANGE MANAGEMENT

5. DESIGN OF PERFORMANCE MEASUREMENT SYSTEMS

- ⇒ ASSURANCE Engagement : Conduct performance audits
To measure how well org. is achieving targets for its KPIs.
- ⇒ CONSULTING Engagement : IA works with CLIENTS
To IMPROVE PERFORMANCE measured by KPIs