

INTERNAL AUDITING STANDARDS: WHY THEY MATTER

In today's business environment, having an efficient and effective internal audit function is a true necessity. Internal auditing is among the cornerstones of effective organizational governance.

Internal audit's mission is to enhance and protect organizational value by providing stakeholders with risk-based and objective assurance, advice, and insight. Generally under the oversight of an audit committee, internal auditors review the organization's processes, operations, and goals, and they provide senior management and the board with information needed to make informed decisions on critical issues.

Because internal auditing is *vital* to good corporate health, an essential board responsibility is to ensure that the internal auditors do it well. But how can a board make sure the internal auditors serve the organization effectively?

The answer lies in the *International Standards for the Professional Practice of Internal Auditing (Standards)*. The *Standards*, promulgated by The IIA, are the primary mechanism for ensuring an organization's internal auditors consistently and accurately provide essential services in a timely, cost-effective manner.

"The *Standards* give internal auditors a compass for planning and performing their work, including, for instance, in preparing for an audit and conducting it," said Patty Miller, CIA, QIAL, CRMA, CPA, CISA, president of PKMiller Risk Consulting, LLP, retired Deloitte partner, and current chair of the International Internal

Audit Standards Board (IIASB). According to Miller, the *Standards* help ensure that internal auditors add value and improve their organizations' operations by establishing minimum acceptable levels of performance. The *Standards* also:

- Provide a framework for performing a broad range of value-added internal auditing.
- Delineate basic principles that represent the practice of internal auditing.
- Establish the basis for the evaluation of internal audit performance.
- Foster improved organizational processes and operations.



Globally Recognized Standards for Professionalism

The *Standards* are recognized as the benchmark for internal auditors throughout the world and are available in more than three dozen officially authorized translations. They also have been incorporated into legislation and regulation in some countries.

Developed and updated by the IASB, the *Standards* represent the views of a much wider group of internal auditors, stakeholders, academics, and other subject matter experts throughout the world. The IASB engages in extensive consultation and discussion prior to issuing proposed changes, and those proposed changes can take effect only after the draft has been made publicly available for comment during a minimum 90-day “exposure draft” period. Afterward, the proposed changes must be approved by the IASB.

Further, the International Professional Practices Framework Oversight Council (IPPFOC), an oversight body appointed by The IIA’s Board of Directors, evaluates and advises on the rigor of the standard-setting process to ensure that the *Standards* are appropriate for use by any organization — small or large, private or public. The result is a set of guidelines sufficiently flexible for any work environment, yet rigorous enough to give board members necessary assurance regarding the quality of the internal auditing services they receive.

Reliable Information for Informed Decision-making

The *Standards* are key for those who rely upon and use the services of internal audit. “Boards need to establish an expectation that the internal audit function operates in conformance with the *Standards*,” Miller said. In turn, boards of directors can then use the *Standards* to evaluate the internal audit function. The *Standards* require organizations to have an independent external quality assessment

Internal Audit Oversight

OVERSIGHT OF the internal audit function goes beyond assuring conformance with professional standards. As part of its oversight responsibilities, an audit committee should:

- Review and concur with the chief audit executive’s appointment, replacement, reassignment, and dismissal.
- Review/approve the internal audit charter and ensure its compatibility with the audit committee’s charter.
- Review the audit plan and any significant changes to the plan.
- Ensure internal auditor neutrality and objectivity.
- Review the internal audit department’s budget and staffing.
- Encourage internal auditor certification and other professional development.
- Meet privately with the CAE.
- Receive reports from the CAE on audit findings and information on technological advances and trends.
- Review internal auditing’s conformance with the *International Standards for the Professional Practice of Internal Auditing*.

at least once every five years, which includes a review of conformance with the *Standards*. Successful completion of an assessment enables the internal auditors to state that their activities are conducted in accordance with the *Standards*, thereby providing assurance to the board and audit committee about the professional competence of the internal audit function.

External auditors must also obtain an understanding of the internal audit function. During this

process, the external auditors normally will review conformance with the *Standards* either by using them to evaluate the internal audit department directly, or by reviewing the results of the internal audit department's most recent independent quality assurance assessment.

Failure to Conform: What Could Go Wrong?

Internal auditing is a complex task that involves identifying the risks that could keep an organization from achieving its goals, helping to ensure the organization's leaders know about these risks, and proactively recommending improvements to help reduce the risks to an acceptable level. The *Standards* help to ensure that internal auditors consistently perform their essential duties effectively.

"The biggest issue is false assurance," Miller said, "when auditors miss something in an audit and conclude processes are well-controlled, when in fact they are not. When internal auditing is not performed according to the *Standards*, important risks may be overlooked." In consequence, business opportunities may be missed, and the odds may increase that the organization won't meet its stated objectives.


Less common, boards may face increased liability if internal auditors do not conform with the *Standards*. For example, the *Standards* require that the chief audit executive (CAE) establish a process to monitor and ensure that internal audit recommendations are effectively implemented by management or that the organization understands and accepts the risk of not taking action. This can be essential for limiting board liability. Imagine the potential consequences when a board has been notified of an ongoing fraud, but nobody monitors the situation to ensure the problem is addressed satisfactorily. Informing the board of the problem but not ensuring adequate corrective actions are taken might leave the door open for charges of board negligence.

On the other hand, when an internal audit function performs its work in accordance with the *Standards*, the internal auditors help their organization accomplish objectives by bringing a systematic,

disciplined approach to evaluate and improve risk management, control, and governance processes.

At first glance, internal audit standards might seem complex and mysterious. But directors who understand them will be better positioned to fulfill their fiduciary duties, and take advantage of the services offered by the internal auditors. If you haven't talked with your internal auditors recently about their conformance with the *Standards*, you might want to put this topic on the agenda for your next audit committee or board meeting.

For more information, visit The IIA's website at www.theiia.org/guidance.



Top 5 questions the audit committee should ask to determine if the organization is conforming with the *Standards*:

1. Is the CAE proactively disclosing any areas of known *Standards* nonconformance and their impact?
2. Does the internal audit activity have an ongoing Quality Assurance and Improvement Program (QAIP) that includes reporting on internal assessment and external assessment results?
3. Does the internal audit function have a charter that specifically recognizes the mandatory nature of the *Standards*?
4. Does the CAE proactively elevate any areas where independence or objectivity could be impaired?
5. Does the CAE elevate areas where management's acceptance of risk may be unacceptable to the organization?

Quick Poll Question

How well does your organization's internal audit function achieve its mission to enhance and protect organizational value?

Visit www.theiia.org/goto/quickpoll to answer the question and see how others are responding.

About The IIA

The Institute of Internal Auditors Inc. (IIA) is a global professional association with more than 180,000 members in more than 170 countries and territories. The IIA serves as the internal audit profession's chief advocate, international standard-setter, and principal researcher and educator.
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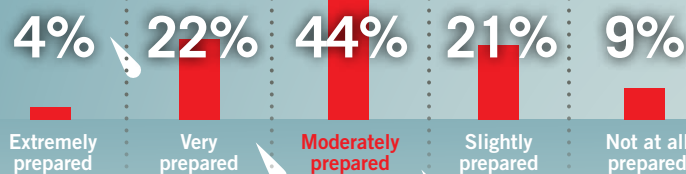
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Quick Poll Results:

How prepared is your organization to respond to a reputation crisis?



Based on 406 respondents. Source: The Institute of Internal Auditors' Tone at the Top March/April 2015 survey. Total may not equal 100% due to rounding.