<u>Back to Basics</u>

<u>Managing the Audit Department: Process Management</u>

In this final article in the series on Managing the Audit Department, Bev Cole will outline the elements involved in Audit Process Management.  The previous two articles can be viewed on the ACCA Virtual Learning Centre (VLC) and cover an overview of managing the audit department and roadmap (see Diagram A below); audit governance and strategy; key performance indicators; and audit resource management.  In addition there is an article on the VLC on assurance planning.

The final article on Managing the Audit Department takes you through Audit Process Management.  Let's start with a quick reminder of the roadmap.

*covered in separate articles

<u>Diagram A: Roadmap for Managing the Audit Department</u>
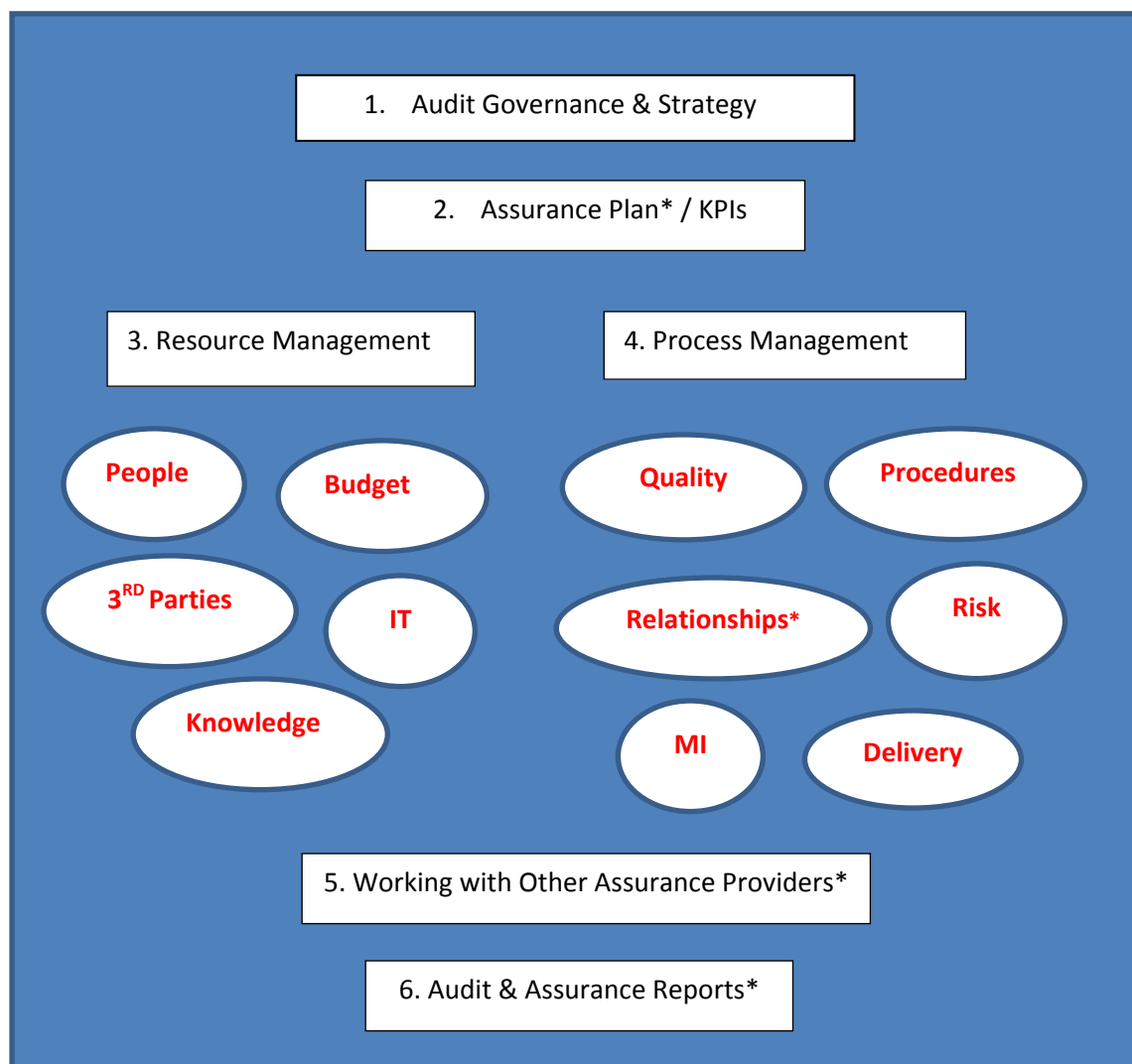
<u>Step 4 – Audit Process Management</u>

There are many aspects involved in audit process management which need to be in alignment.  Details are as outlined below:

a) Procedures

Performance Standard 2040** states that "The chief audit executive must establish policies and procedures to guide the internal audit activity".  Audit procedures should ideally cover all elements of audit activity, but the absolutely critical procedures are those covering the audit assignment and quality assurance as these are your core activities and are of most interest to the Audit Committee, external audit and Regulators.  Management Information (MI) and IT procedures are also vital as this is where you are probably dependent of one or two key people.

Within procedures covering the audit assignment, be sure to include:

- Assignment planning
- Assignment fieldwork
    - Assessing risk and control
    - Audit testing
- Assignment reporting
- Follow up of management actions

More detail is on the VLC on all these elements.  Some common difficult areas include:

- Aligning audits / management of hand over points
- Agreement of audit terms of reference and audit reports within Audit
- The extent of business involvement in terms of reference and audit reports
- Documentation of business processes / Reliance on business processes already documented e.g. for Sarbanes Oxley
- Using information within risk registers
- How to incorporate assurance work undertaken by other assurance providers
- Audit testing policy on sample sizes, sample selection and substantive testing
- Obtaining extracts of test data from business systems
- Structuring audit findings into meaningful issues
- Audit report ratings (definition and usage) and minor issues for verbal reporting only
- Agreement of management actions
- Process and authority for acceptance of audit issues / risks within the business (and on-going review of this)
- Review and approval of working papers, by whom and when
- Following up an agreed action / resolving risks identified by the audit
- Escalation of audit issues not agreed or not resolved

- Time recording and elapsed time recording
- Disclosure of audit issues and reports to other assurance functions / external audit / Regulators
b) Quality Assurance

Quality assurance is a vital element to ensure you provide reasonable assurance which can be relied on. It is undertaken at a departmental level; over MI, assurance plans and reports; and at an assignment level. You should expect mention of quality within your strategy; your key performance indicators; individual performance measures; assignment feedback and your training and routine communication. It should be a completely embedded process running throughout your operation and not an 'add on'. It is very important that quality assurance does not just include compliance with standards, policies and procedures, but that it looks at whether the evidence on file supports the conclusions drawn and the judgements made.

This is not just 'good practice', Attribute Standard** 1300 states that "The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity."

At a departmental level, you should have quality checks to ensure you comply with the "Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics."**

Your periodic assessments of overall quality should be both internal and external. Internal assessments of quality can be undertaken by a central technical team if you have one, or could be self-assessment through peer review. It could also be undertaken by a team outside the department if they have knowledge of internal auditing and your procedures.

External assessments are needed periodically to get a completely independent and objective view of quality and performance and are also useful to get a view of how your department is performing relative to others in the same industry. Attribute Standard** 1312 requires that "External assessments must be conducted at least once every five years by a qualified independent reviewer or review team from outside the organization. The chief audit executive must discuss with the board:

- The need for more frequent external assessments; and
- The qualifications and independence of the external reviewer or review team, including any potential conflict of interest."

Like any work undertaken by a third party, it is critical to get bids from a selection of suitable suppliers; have a clear written specification of work required (which could include benchmarking for example as well as just quality assessment); review the bids and interview potential suppliers; negotiate the price; ensure a robust contract is in place including clear deliverables and deadlines; personnel and qualifications; clarity over contacts; clarity of customer (is it the Audit Committee or the Audit Department?);

confidentiality agreement; information security requirements; declaration of conflicts of interest; quality expected – exit clauses; and ensure that an appropriate level of indemnity insurance is in place. Do include the experts within your Procurement and Legal Departments in this process.

Quality assurance work is also advisable over your assurance planning, assurance reporting and MI. This is just part of routine supervision of work undertaken, often within a central technical team. However, it is sometimes overlooked and this would be very unwise, as errors appearing in reports and presentations to the Risk or Audit Committee could undermine all the good assurance work undertaken by the department as a whole.

The vast majority of quality assurance work is undertaken at an individual assignment level. The person managing the assignment needs to ensure that the terms of reference has been followed; that risks and controls have been appropriately assessed; that testing undertaken is sufficient; that valid conclusions have been drawn and comprehensively and appropriately drafted into issues for reporting. Also compliance with standards, policies and procedures should be assessed. Formally this assessment is evidenced through quality review of working papers and evidence from this is critical for any independent assessment of controls over quality. However, don't forget that discussion with your assignment team about coverage, approach and findings is a key input to early assessment of the robustness of quality.

The embedding of quality assurance means that I would expect quality measures within your Key Performance Indicators (KPIs) are reviewed by the audit management team at least quarterly. Attribute Standard** 1320 requires that "The chief audit executive must communicate the results of the quality assurance and improvement program to senior management and the board". So any external reviews should be reported upon completion and internal assessments should be reported at least annually.

A couple of extra points to note on quality assurance, Attribute Standard** 1321 states that "The chief audit executive may state that the internal audit activity conforms with *the International Standards for the Professional Practice of Internal Auditing* only if the results of the quality assurance and improvement program support this statement." Then 1322 states that "When non-conformance with the Definition of Internal Auditing, the Code of Ethics, or the *Standards* impact the overall scope or operation of the internal audit activity, the chief audit executive must disclose the non-conformance and the impact to senior management and the board."

   c)  Risk Management

It is clearly good practice within Internal Audit to identify your risks; be clear on your risk appetite; put appropriate controls in place; ensure they are complied with and are effective; and record this risk assessment and review. After all, this is what we expect of everyone else, but do you formally do it? Is it as easy as it sounds – especially defining

risk appetite?  You are probably working within an organisation large enough to have a formal operational risk management process with risk registers etc.  and you must ensure you comply with it.

Do you look at major incidents within the organisation and look back at why the risks, missing controls or non-compliance with controls weren't picked up by your audit coverage?  Personally I believe this should be a key control that every department has in place.  Not to 'go on a witch hunt', but to learn lessons and improve quality.  Additionally it could be that your work was completely valid within the remit of providing 'reasonable assurance' and undertaking some back-checking will help you to justify your work.

Similarly if things do go wrong and you hadn't identified issues you should, do you just blame lack of resource, lack of budget or management pressure to drop issues?  These are risks which *you* must manage.  Internal Audit is just as accountable for their work as everyone else in the organisation.

Effective risk management is what we believe in and what we get paid to assess in others, yet talking to internal audit colleagues in many different organisations over the years I don't believe we take it as seriously as we should in our own department.

d) Delivery Management

You need mechanisms in place to ensure you delivery against your promises, including delivery of the audit plan.  This means not just monitoring the number of audits delivered, it also means ensuring that changes to the plan and delivery issues haven't affected your ability to deliver reasonable assurance overall.  Also you need to manage the audit pipeline effectively as well.  To do this you can monitor whether audit stage deadlines are being met and whether mandays used reflect the audit stage achieved.

e) Management Information (MI)

All departments need MI to manage their performance and to communicate effectively with others.  The KPIs outlined in the first article of this series should be reported to and discussed monthly by the audit management team.  Audit automation has ensured we have lots of information at our disposal from the audits themselves which can be divided in different ways very easily.  We can report on outstanding issues for example at a company level, divisional level, by audit assignment and often by risk category.  We can report missed issue deadlines and time since the issue was raised. We can report audit ratings at a company and divisional level as well.  We can report on trends over time.  Are you using this information well within your business and providing useful information for stakeholders on a routine basis?

f) Relationship Management

There is an article within the VLC on Business Relationship Management which covers this topic.  However, I'll cover here a brief overview of stakeholder relationship management. We all know that managing relationships well means that we are more likely to achieve our goals and to do so in as painless a way as possible.  However, have you formally assessed your stakeholders?

A useful tool is a Stakeholder Map, outlining who your key stakeholders are, with one axis being how influential they are and the other being their degree of advocacy towards Audit. If they are highly influential and a strong advocate, then your action is to maintain that level of advocacy.  If they are neither influential nor an advocate, then is it worth spending a lot of time and effort to improve their advocacy level?  Your time and effort are best spent where someone is highly influential, but is not an advocate.  You should develop a plan of action to try to improve their level of advocacy.  Try to get to know what their goals are and what irritates them and then tell them what Audit has achieved and will review going forward and how that will help them to achieve those goals and address those annoying things.

I hope you found this series of articles on Managing the Audit Department helpful.  They can all be found on the VLC, together with Audit Practitioners Guides and Q&As.  Look out for articles in the future on Working with Other Assurance Providers and Assurance Reporting.

** For more information on all the standards, please refer to http://www.iia.org/