





## **MINISTRY OF FINANCE**

Central Harmonization Unit  
For Internal Audit

### **INTERNAL AUDIT MANUAL**

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**With the assistance of PIFC2**

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Financed by EU







**Dear readers!**

It's my pleasure to introduce to you one of the most important documents for the activity of Internal Audit, the Manual of Internal Audit.

Reforms undertaken from the Government during the process of European Integration of Albania require the set up and development of a static and modern system of Public Internal Financial Control, where internal audit is part of.

Set up and functioning of audit structures in spending units of public funds is not only a requirement of standards but necessity that derives from role of internal audit in public organizations to estimate control and governance systems as well as to support heads of entities in achievement of their objectives.

Ministry of Finance through Central Harmonization Unit for Internal Audit together with internal audit structures in line ministries and with the support of PIFC project offered support and cooperation for drafting full legal frame of Internal Audit activity in compliance with best practices and standards in this field.

This Manual determines main directions of Internal Audit activity, serving as guidance for internal auditors, in local and central government, to prepare the charter of audit and special manual (instruction) of their activity.

Internal Audit Manual shows continuous attempts aiming at raise of accountability for the use of taxpayers' money, through offering an audit service as per best practices and standards of time.

**RIDVAN BODE**

  
**MINISTËR I FINANCAVE**

# FOREWORD AND MISSION STATEMENT

## MISSION STATEMENT

We aim to help public sector organisations which accomplish their objectives through independent, objective and risk-based, as mentioned below:

1. Evaluation, assurance and opinions;
2. Consultancy services; and
3. Balanced and constructive advices to all management, particularly. Authorising Officers.

Vision – To improve and add value to public sector culture and operations in Albania and to ensure the correct use of public funds

Values - We value:

- Integrity:** Honesty, objectivity, proficiency, avoiding conflicts of Interests.
- Continuous Learning:** Continuously striving for improvement in themselves and in the organisations they serve, auditors should be looking ahead to the future and keep their knowledge up to date, and learn from each other.
- Professionalism:** Application of professional standards with due care and rigour, supportive methodology and sensitivity to those organisations we Audit.
- Exchanging the Best Practices:** Openness, transparency, and information exchange

This Manual has been prepared by the Ministry of Finance, the new Central Harmonisation Unit for Internal Audit in close cooperation with the experts of a project funded by EU.

Internal Audit is an essential component of governance in the public sector in the Republic of Albania. There have been significant advances since 2004 when the previous Internal Audit Manual was issued. Governance, risk management and finance professionalism have all been transformed. This Audit Manual supports these developments.

As public sector internal Auditors, we believe that internal Audit is an activity

most effectively conducted jointly with the Audited organisations and their employees. We are convinced that through such an approach the best joint outcomes are achieved, because no one is more familiar with the activity of the organisation. At each stage of our Audit activity joint involvement and cooperation of management and Auditor is essential.

The Manual comprises nine sections.

- Section I outlines the management of the internal Audit function, introduces the role of internal Audit, its responsibilities and the principles and policies that guide it.
- Section II covers the processes for developing strategic and annual planning.
- Section III describes the activities of the Audit unit completing an individual Audit and will be useful as a guide to Auditors as they work on their Audit assignments.
- Section IV covers reporting and the process for monitoring the quality of the Audit work.
- Section V covers the way in which the Internal Audit should be recorded and the evidence that should be obtained to support the Audit conclusion.
- Section VI covers the specific rules and requirements relating to the Internal Audit of European pre-accession funds.
- Section VII includes the International Internal Audits Standards that should be complied with during the all Internal Audit assignments.
- Section VIII contains a checklist and supporting guidance for use by staff working for the Central Harmonisation Unit (Internal Audit) when monitoring the quality of the Internal Audit work that has been undertaken.
- Section IX contains a number of frequently asked questions which should be a quick reference point

The principles of Internal Audit are universal. International Standards “for the Professional Practices of Internal Auditing” have been issued by the Internal Audit Standards Board of the Institute of Internal Auditors, the global professional body. These standards act as best practice throughout the European Union and have been incorporated in relevant sections of this manual, amended as necessary for the specific requirements of Albania.

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# Chapter I

## **Purpose and Content of this Internal Audit Manual**

### **1.1. Purpose of this Internal Audit manual**

This manual has been written to set out: policies, Standards and the procedures that should be followed for all public sector Internal Audit activities within the Republic of Albania.

This Internal Audit manual offsets out the rules and procedures that must be followed from the initial planning phase through to the audit execution and reporting of findings to the management of the entity being audited. This manual is based on the law for internal audit and on recognised Internal Auditing standards and reflects the knowledge and experiences gained from the previously used practices in relation to this activity.

### **1.2 Keeping the manual up-to-date**

To ensure that the methodology and procedures remain consistent with best practice and reflect changes in the legal and Audit environments, the Director of the CHU (Internal Audit) is responsible to propose to the Minister of Finance improvements and adds in the Internal Audit Manual for keeping the Audit approach, methodology and obligatory templates up-to-date. A review of the manual should be made at least annually in order to ensure that it is up to date and meets the needs of the Internal Audit Units that will be using it.

The manual should be revised where necessary to meet new legislative or governance requirements and to maintain compliance with International Standards of Internal Audit.

Amendments or additions to the manual should be made on the written or delegated authority of the CHU (Internal Audit); dated as to their implementation and included in the manual or an annex.

Directors of Internal Audit Units should use their professional judgment to customise the Internal Audit Manual to suit their local circumstances. The manual of internal auditing and any other changes made to this manual shall be approved by the Minister of Finances.

### **1.3 Preparing the specific methodologies - In implementation of the Internal Audit Manual.**

This Internal Audit manual provides general guidance on the development and conduct of internal audits in the public sector, but it could not cover from technical and methodical part every scenario within the entire public sector.

This is due to the fact that internal auditing must consider the characteristics and the specifics of each subject and an audit program must be prepared that meets the needs of each organisation.

The heads of Internal Audit Units are responsible for the preparation of specific methodologies, which must be prepared by tailoring the internal audit manual with the specific conditions of the subjects where they operate and at the same time using their professional judgement. The preparation of the specific methodologies must cover the whole audit field of the subject and they must be in accordance with this manual. The head of Internal Audit Unit prepares the specifics of the internal audit manual or the methodologies – taking into consideration the opinion of specialists in other fields. The head of the relevant entity approves them only after the CHU/IA in the Ministry of Finance gives its opinion in accordance with the Internal Audit manual.

All internal auditing units of the public sector must prepare “specific methodologies of the internal auditing” no later than 6 months after this manual enter into force. Such a process is part of the development of methodologies of internal auditing system in the public sector and as such it must be done in collaboration with the CHU/IA. A copy of the approved specific methods must be submitted to this unit.

### **1.4 Purpose of Internal Audit**

Public sector organisations are large, complex entities spending large amounts of public money and providing main services to the people of Albania.

The size of the entities means that it is not always possible for the senior managers to personally check that the organisations are operating effectively.

In order to ensure that the organisation operates effectively it is important that within it (the organisation) the internal audit work is done in accordance with the legislation. It is the role of Internal Audit to provide independent, objective assurance to the management of an entity that will add value and improve the organisation’s operations.

Internal Audit activity in the public sector should:

- Help in keeping ministries accountable to the public by assessing and measuring adherence to established law, regulations, and controls, as well ensuring effectiveness, economy, and efficiency of operations;
- Provide objective assurance to oversight bodies about the reliability and credibility of financial and performance reports produced by management structure;
- Help public sector management achieve their goals and objectives by improving organisational systems and services;
- Deter fraud, waste, and abuse; and
- Help employees improve their overall job performance and adherence to established controls.

Internal Audit work includes:

- Identifying and evaluating significant risk and contributing to the improvement of risk management systems;
- Evaluating the controls which address risk;
- Encouraging effective and efficient controls and promoting continuous improvement;
- Evaluating and highlighting processes that ensure reliability and integrity of financial and operational information;
- Recommending control enhancements which assist the governance process to:
  1. Promote appropriate ethics and values within the organisation;
  2. Ensure effective organisational performance management and accountability of the unit; and
  3. Effectively communicate risk and controls to appropriate areas of the organisation.

### **1.5 Types of internal audit**

#### **1.5.1 Audit Engagement For Assurance Services**

a. An audit engagement in relation to assurance services is done through a system based audit, regularity audits, performance audits, financial audits, Information Technology audits, or through the combination of different audits.

b. Audit engagement for consultancy services – includes consultancy activities and other as these such as: consults, advice, help and training, whose nature and objective gets approved by the head of organisation.

The Internal Audit legislation and standards refers to different types of Internal Audit activities as follows:

#### **1.5.2 Systems Based Audits**

System based audits refers to a detailed evaluation of the financial management systems and internal controls that management have put in place, aiming at seeing if they are operating effectively and efficiently.

This is the most effective type of Internal Audit work because, if the controls are operating as they were intended, then both the Internal Auditors and the management of the organisation can take assurance from those controls.

#### **1.5.3 Regularity Audits**

Regularity Audits refers to the examination of the organisations' activities during the process of achieving their objectives in accordance with, rules and

regulations.

Regularity Audits are designed to test whether the organisation complies with the relevant legislation in a particular area. The report to the management does not cover the general internal controls in a particular area, but simply confirms whether the legislation has been complied with.

### 1.5.4. Performance Audits

Performance audits, or value for money auditing, is the process of assessing achievements in relation to effectiveness, efficiency and economy.

- Economy is the effective and careful use of resources during an activity, maintaining the necessary quality.
- Effectiveness means the link of the result of goods, services, or other products (results) and the resources used for their production.
- Efficiency means the level of the realization of the objectives and the relationships between the expected result to the real result.

A performance Audit looks at how well a service is actually delivered and whether that service gives value for money.

For example, Internal Auditors could assess how good the rubbish collection is in a particular City and evaluate it in relation the costs.

Performance Audits usually involve comparing information about costs and service delivery with other similar organisations and may involve surveys of service users.

### 1.5.5. Financial Audits

The purpose of financial audits is to evaluate the accuracy and the completeness of registers and statement of accounts. Financial audits use essential tests, analytical reviews, and other evaluation procedures which might or might not include functional tests or the review of transactions.

Financial audits determine if the financial information of the organisation honestly presents the financial state, operational results and the avoidances to financial state of the audited subject in accordance with the approved Accounting International Standards. The Financial Audits Procedures are more detailed in the Financial Audit Methodical.

### 1.5.6. IT Audits

An IT Audit is an Audit that only focuses on the IT controls that are in place within an organisation. This can be an overview of all of the IT arrangements in an organisation or be restricted to the IT controls in an individual account area. IT Audits are often undertaken when a new computer system is introduced in

a particular account area.

Although this manual covers some basic IT works (see Standard Template No.12), considering that IT auditing is a very specialised area and remains outside the scope of this Internal Audit manual. The IT system Audits are developed according to the composed method by CHU/IA and approved from Minister of Finance.

### **1.5.7 Advisory Assignments**

An advisory assignment is a review of a particular account area in order to improve the internal controls that are in place. It is more restrictive than a system based Audit as it does not look to test the internal controls that are in place, but simply looks at the design of the particular account area. An advisory assignment is similar to stage 6 of the Internal Audit work that is covered in section 3 of this manual.

### **1.5.8 Audit Assignments for Consultancy Service**

Consultancy work is where Internal Auditors act in an advisory capacity to the management of the organisation. This involves Internal Auditors taking an active role in a particular area rather than independently reviewing what management have proposed.

Care needs to be taken when agreeing to undertake this type of work so as not only to compromise the independence of the Internal Auditors. It would be impossible for Internal Auditors to review an account area in an objective way if they had been heavily involved in the design of that area/activity.

The contract of this Service and way of payment are approved with the Order given by the Minister of Finance.

## **1.6 Internal Audit Charter**

Each Internal Audit Unit should have its own Charter of the IA. It establishes the organisational status of the Unit by defining its purpose, authority and responsibility of the Internal Audit Unit.

An example Internal Audit Charter has been included at Standard Template 1 at the end of this section and Internal Audit Units may find this to be a helpful starting point. The suggested areas for inclusion in the Internal Audit Charter are as follows:

<b>Chapter</b>	<b>Overview</b>
<b>Mission and Scope of Work</b>	Sets out the broad aims of the Internal Audit Unit and the area that could be subject to Internal Audit work.
<b>Accountability</b>	Determines the reporting line of the Chief Audit Executive and the head of Audit Unit and how this will be done
<b>Independence</b>	Determines the legal regulations to ensure that independence is maintained.
<b>Responsibility</b>	Determines the role and the responsibility of internal audit and how these will be discharged.
<b>Authority</b>	Sets out the Internal Audit Unit's rights of access to the records and staff of the organisation and also the limits on the work that it is appropriate for the Internal Audit Unit to undertake.
<b>Integrity</b>	The Internal Audits Integrity is faithful and consequently and ensures trust basis in their judgements.
<b>Standards of the Audit Practices</b>	Confirms that relevant International Standards for Internal Audit work will be followed.

### 1.7 Role and Responsibilities of the Internal Audit

The roles and responsibilities for the provision of Internal Audit work are set out below.

#### 1.7.1 Role and responsibilities of the Central Harmonisation Unit for Internal Auditing (CHU)

The CHU is responsible for:

1. Developing, the administration and implementation of a harmonised strategy for internal audit in the public sector and monitoring such an activity on a national scale;
2. Providing recommendations for the improvement of primary and secondary legislation regarding public internal auditing, in collaboration with other structures of this ministry;
3. Preparing the auditing methods for the determination and the evaluation of risk and performance;
4. Proposing to the Internal Audit Committee and to the Minister of Finance the review of internal audit manual, guidance and procedures of internal auditing, in order for it to comply with the legislation of EU members and with internationally accepted internal audit standards;
5. Determining and designing a system for the reporting of findings for all internal audit activities in the public sector, including periodical and annual reports;
6. Providing opinions and recommendations in relation to the internal audit standards in case of important disagreements between internal auditors and auditees.
7. Collaborating with CHU for Financial Management and Control, among other things, in preparing the annual report for the Public Internal Financial Control (PIFC), which is submitted to the Minister of Finance and to the first Authorised Employees.
8. Supervising and evaluating the activity of audited structures in all audited subjects (auditees). It does so in compliance with standards and Manual requirements, methods and guidance approved by the Ministry of Finance;
9. Preparing and designing strategies and national policies for the updated educational system, continuous and obligatory trainings and the procedures of the auditors' employment;
10. Approving methods prepared by Internal Audit Units of the Audited Subjects, to supplement the internal audit Manual concerning specific aspects of internal auditing;

11. Collaborating with the structures of personnel of the institution in order to determine the auditors' recruiting criteria;
12. Collaborating with the head of internal Audit Units of audited subjects and in accordance with existing legislation, providing an opinion about appointments, discharging and the relocation of auditors in the central institution, as well as opinion on apportionments, discharging and relocation of the head of internal audit units of subsidiaries;
13. Determining the form of the registration of given recommendations by internal audit's structures of auditees.

### **1.7.2 Role and responsibilities of Internal Audit Units**

The roles and responsibilities of the Internal Auditing Units are:

1. Preparing of methods or guidance on specific aspects of internal auditing, implementing the internal audit manual or other acts issued by the Ministry of Finance, and their submission for approval to the CHU/IA.
2. Preparing Annual and Strategic plans of the Internal Audit work to be undertaken.
3. Conducting internal audit engagements in accordance with guidance and methods approved by the CHU/IA, aiming at evaluating the transparency, efficiency, effectiveness and the economy of the system of Financial Management and Control as well as the performance of the audited organization.
4. Undertaking follow up procedures and periodically reporting findings, conclusions, and recommendations that result from their audit activity, as well as providing the information CHU/IA concerning the non-implementation of recommendations by the head of audited subjects and about the consequences of failing to implement them.
5. Each internal audit unit prepare annual or periodical reports that are submitted to the CHU/ IA. These Reports contain data related to;
  - Engagement and the scope of audit work undertaken during the reported period, duration of each audit, and if there have been deviations from the plan, they need to give the reasons and the relevant arguments;
  - Conclusions and findings related to the functioning of controlling systems within an organisation, together with the recommendation for improvements: and
  - The actions undertaken by the management for implementing the recommendations, as well as any recommendation that has not been implemented.

In cases where there is a difference of thought between the head of the organisation being audited and internal auditors, then the Directorate of Methodology and Information near CHU/IA must be informed in order to provide a solution.

### 1.7.2.1 Heads of Internal Audit Sections

The Head of an Internal Audit Section, except the role and responsibilities of the above mentioned Internal Audit Unit, has responsibility for:

- Ensuring Audits undertaken comply with international standards of internal Auditing as contained in this Internal Audit Manual; and
- Attending, or when not possible, appointing a deputy to attend, the initial and wash-up meetings with the entity Audited.
- Review of the quality work audit

### 1.7.2.2 Audit Unit Leaders

The Unit Leader should oversee the Audit work to ensure that the Auditors are receiving necessary assistance; that Audit resources are used with efficiency and effectiveness and that the Audit is conducted:

- According to the approved plan;
- In compliance with the appropriate methodology and defined standards;
- At a suitable level of entity management or process; and
- In discussion with Auditors on the more efficient approaches for Audit work and preparation of recommendations. On important matters, the Unit Leader can provide written tasks for Auditors.

If in the Unit Leader's judgement a deviation is required to be done from the Audit Plan, Manual and / or International Standards, this should be discussed with the Head of the Audit Section and fully documented and approved.

### 1.7.2.3 Audit Staff

The independence of internal Auditors must be guaranteed in compliance with professional Standards. To confirm compliance with these Standards, Internal Auditors declare in advance their independence by completing a declaration of independence. The Head of Audit assesses the declaration, takes the final decision of appointing the staff for the execution of Audits and retains the declaration on the Audit file.

Audit staff should informally discuss Audit matters with the Unit Leader to update them on the Audit Programme fulfilment, obstacles, and matters arising as well as needs of Auditors till engaged in the Audit work. For large Audits, this update may be through interim reports. The reporting procedures should

be set out in the Audit Programme.

### **1.8 Inter-institutional Relationships**

The devolved Audit organisations in Albania - Central Harmonisation Unit, Internal Audit, Investigations Unit and External Auditors and other structures have separate responsibilities, which are clearly set out in the relevant legal and regulatory framework. However, all should cooperate professionally to efficiently enhance public sector management on behalf of the Albanian people.

The legal and regulatory framework sets out the obligation of the CHU/ IA (Internal Audit) to set out and to maintain effective relationships with the other sectors of Audit under the new legislative framework with a view to co-operating in the enhancement of governance generally.

This collaboration involves the exchange of information on professional bases for the auditees, annual and strategic plans as well as the submission of the consolidated annual Plan to Supreme State Audit (SSA), Exchanging information, plans and reports aiming at improving the planning process, avoiding overlapping, the enhancement of security level of the information and above all, the increase of performance level of the auditing activity in the whole public sector.

### **1.9 Independence and Objectivity**

Independence is defined as being the freedom from conditions that threaten objectivity or the appearance of objectivity. Such threats to objectivity must be managed at the individual Auditor, engagement, functional, and organizational levels

Objectivity is defined as being an unbiased mental attitude that allows internal Auditors to perform engagements in such a manner that they have an honest belief in their work product and that no significant quality compromises are made. Objectivity requires internal Auditors not to subordinate their judgment on Audit matters to others. Independence is essential for Internal Auditors to carry out their work in an effective manner. It is important for Internal Audit staff to be both independent and also to be seen to be independent.

In order not to compromise their independence, internal auditors must not engage in management activities (e.g. installing accounting procedures or preparing records), that they may subsequently review and appraise. Objectivity need not be adversely affected, by internal auditors recommending standards or by consulting on controls to be applied in the development of the systems and processes that will be reviewed. Internal Auditors are only prohibited from public sector activities where there either is a conflict of interest with their internal audit activities or where there may appear to be such a conflict.

Internal Auditors are independent when they can carry out their work freely and objectively. Independence permits internal Auditors to render the impartial and unbiased judgments that are essential to the proper conduct of internal

Audit engagements. This is achieved through the organisational status and objectivity of professional internal Auditors.

The Central Harmonisation Unit and the Internal Audit Units in the public sector are functionally and organisationally independent within the public entity.

Functional independence means that the Audit structures are independent in planning, performing and reporting the Audit results and recommendation from the Audited entity. The Audit performance should be according to regulations and Standards proposed by the Central Harmonisation Unit and authorised by the Ministry of Finance and should not be subject to other influence from people with authority inside or outside the entity. The Auditors respect Audited entity structures and regulations of ethics and behaviour in civil services.

Organisational independence within the entity means that the Audit structures report directly to the principal director of the public subject, who is the highest level of decision making in the organisation being Audited. The Audit Structures cannot be engaged in other duties inside the organization, which have nothing to do with the functioning of internal Audit. They are part of management structures and not of the operational entity structures.

There can be a number of other potential threats to independence, whether perceived or actual, of Internal Auditors as follows:

Self Interest Threat	This occur where the Internal Auditors may have, or could reasonably be perceived to have, an economic or other incentive which may cause them to change or distort their behaviours in a way which compromises their independence or impairs the objectivity of their judgment (for example, agreeing not to include a particular piece of work in the work programme; or, being overly positive in a report to secure good feedback from the management of the organisation being Audited).
Self Review Threat	This could occur if Internal Auditors find themselves, or could reasonably be perceived as being, in the position of reviewing their own or colleagues' work that was undertaken at the organisation. This could happen where one of the Internal Audit Unit previously worked at the organisation being Audited or where Internal Auditors engage in management activities (e.g. installing accounting procedures or preparing records), that they may subsequently review and appraise.
Management Threat	This happen where an Internal Auditor undertakes work that involves judgments and decisions, which are the responsibility of management (such as setting policies and strategic direction, authorising transactions or taking responsibility for designing, implementing and maintaining internal control).
Familiarity Threat	This can occur when the relationship between the Internal Auditor and the organisation being Audited becomes, or could reasonably be perceived as being, so close that they are not sufficiently sceptical. This can occur when the Internal Auditors have been in their role for a long time.

Advocacy Threat	This occur when the Internal Auditor may become, or could reasonably be perceived as acting as, an advocate for or against the position taken by the Government or the organisation being Audited.
Intimidation Threat	This occur where the Internal Auditors may be, or could reasonably be perceived as being, intimidated by threat, by a dominating personality or by other pressures either actual or feared, which may cause a change in behaviours in a way that compromises independence or impairs objectivity of judgment. Such a threat may arise from an organisation being Audited or from another stakeholder.

Independence and objectivity need not be adversely affected by Internal Auditors through their recommending standards of the organization that is audited.

Internal Auditors should demonstrate compliance with objectivity and independence, by completing an Auditor’s Independence Declaration, Standard Template which is given in the end of this chapter.

There may be a number of instances where there is either an actual or perceived threat to the independence of the Internal Auditors.

The Head of the Internal Audit Unit is the person with the overall responsibility to determine what action is necessary to retain the Internal Auditor’s independence. In some cases this may involve making decisions which are either unpopular or cause operational difficulties. However, these are essential if the independence of the Internal Audit Unit is to be maintained.

Risk	Possible Mitigating Action
An Internal Auditor pays local taxes to the City Council.	None is required as the relationship between the Internal Auditor and the Council is no different to that of any other citizen.
An Internal Auditor is a close personal friend of a senior manager of an organisation.	The Internal Auditor should not undertake Audit work at this entity.
An Internal Auditor is a close personal friend of a junior employee of an organisation.	The Internal Auditor should not undertake work in the account area where the junior employee is employed.
An Internal Auditor is pursuing a claim for negligence against an organisation.	The Internal Auditor should not undertake Audit work at this entity.

**Templates**  
**for**  
**Chapter I**

### Standard Template 1: Model Internal Audit Unit Charter

Each Internal Audit Unit should have its own Charter. Model displayed as below may be a helpful starting point for the designed charter.

#### Mission and Scope of Work

The mission of the internal Auditing unit is to provide independent, objective assurance and consulting services designed to add value and improve the organisation's operations. It helps the organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

The scope of work is to determine whether the organisation's network of risk management, control, and governance processes, as designed and represented by management, is adequate and functioning in a manner to ensure:

- Risks are appropriately identified and managed.
- Effective interaction with the various governance groups occurs where necessary.
- Significant financial, managerial, and operating information is accurate, reliable, and timely.
- Employee's actions are in compliance with policies, standards, procedures, and applicable laws and regulations.
- Resources are acquired economically, used efficiently, and adequately protected.
- Programs, plans, and objectives are achieved.
- Quality and continuous improvement are embedded into the internal control process.
- Significant legislative or regulatory issues impacting the organisation are recognized and addressed properly.

Opportunities for improving management control, profitability, and the organisation's image may be identified during Audits. They will be communicated to the appropriate level of management.

#### Accountability

The chief Audit executive (CAE), in the discharge of his/her duties, shall be accountable to management and Audit Committee (if existing) to:

- To provide annually an assessment of the adequacy and effectiveness of the organisation's internal controls and risk management in the documented scope of Audit work.
- To report significant control weaknesses identified by the Audit in a timely

fashion with recommendations aimed at improvements of internal control environments.

- To inform periodically senior management on the status and results of the annual Audit plan and the sufficiency of departmental resources.
- To coordinate with and provide oversight of other control and monitoring functions (risk management, compliance, security, legal, ethics, environmental, external Audit).

### Independence

To provide for the independence of the Internal Audit Unit, its personnel report to the CAE, who reports administratively to the chief executive officer and functionally to the board and, if existing, as well Audit Committee.

### Responsibility

The CAE and staff of the internal Auditing department have responsibility to:

- To develop an annual flexible Audit plan using appropriate risk-based methodology, including any risks or control concerns identified by management, and submits that plan to the management and any existing Audit committee for agreement.
- To implement the annual Audit plan, as approved, including, and as appropriate, any special tasks or projects requested by management.
- To maintain a professional Audit staff with sufficient knowledge, skills, experience, and professional certifications to meet the requirements of this Charter.
- To establish a quality assurance program by which the CAE assures the operation of internal Auditing activities.
- To perform consulting services, beyond internal Audit assurance services, to assist management in meeting its objectives. Examples may include facilitation, process design, training, and advisory services.
- To evaluate and assess significant merging/consolidating functions and new or changing services, processes, operations, and control processes under development, implementation, and/or expansion.
- To issue periodic reports to the management summarizing results of Audit activities and emerging trends and successful practices in internal Auditing.
- Provide a list of significant measurement goals and results to any Audit committee.
- To assist in the investigation of significant suspected fraudulent activities within the organisation and notify management and any Audit committee of

the results.

- To consider the scope of work of the external Auditors and regulators, as appropriate, for the purpose of providing optimal Audit coverage to the organisation at a reasonable overall cost.

**Authority**

The CAE and staff of the internal Auditing department are authorized to:

- To have unrestricted access to all functions, records, property, and personnel.
- To have full and free access to any Audit committee.
- To allocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish Audit objectives.
- To obtain the necessary assistance of personnel in the organisation who perform Audits, as well as other specialized services from within or outside the organisation.

The CAE and staff of the internal Auditing department are not authorized to:

- To perform any operational duties for the organisation or its affiliates.
- To initiate or approve accounting transactions external to the internal Auditing department.
- To direct the activities of any organisation employee not employed by the internal Auditing department, except to the extent such employees have been appropriately assigned to Auditing units or to otherwise assist the internal Auditors.

**Standards of Audit Practice**

The internal Auditing department will meet or exceed the International Standards for the Professional Practice of Internal Auditing of The Institute of Internal Auditors.

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Chief Audit Executive

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Chief Executive Officer

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Audit Committee Chair

Dated

**Standard Template 2 Independence Declaration of the Auditee**

The signatory \_\_\_\_\_ Auditor appointed to the Audit assignment on the entity \_\_\_\_\_ by order of service no. \_\_\_\_\_ date \_\_\_\_\_ completed this declaration.

No	Relationships With The Auditee Impacting on Independence	Yes	No
1	Do you have any financial relations with people that can limit the range or weaken the Audit?		
2	Do you have any prejudice towards the organisational audited staff that could influence your opinions by exerting his authority or otherwise influence you?		
3	Did you have a management position or were involved in some way with the activity of the Auditee in the last three years?		
4	Were you involved in the internal Audit control system processing or implementation, or in certain specific elements of it?		
5	Are you husband/wife or relative up to three generations with the Auditees' managers, members of board or directors of departments?		
6	Do you have any political social or friendly connection with the members of board of the directorate or directors of departments?		
7	Were you employed during this last three years in the entity part-time or full-time or conducted services on its behalf?		
8	Do you have directly or indirectly any financial interest in the entity?		

If there is any disagreement during the Audit that is not declared above, or other disagreements I will immediately notify the Audit unit manager.

Name and surname of Auditor ( \_\_\_\_\_ )

Date: ( \_\_\_\_\_ )

Approval of Auditor for assignment, and any guidance or action in relation to declaration above:

Manager of the Audit unit ( \_\_\_\_\_ )

Date: ( \_\_\_\_\_ )



# Chapter II

## **Strategic and Annual Planning**

### Introduction

Planning is an essential part of the Audit process. It determines how the limited Internal Audit resources can be used to the greatest effect.

Audit planning is done in three separate ways:

Strategic planning – sets out the work that will be undertaken over a long period (usually five years, according to the scheme ¼) Because of the long timeframe, this planning will be very broad in its nature. The strategic plan should be updated each year in order to ensure that it remains relevant.

Annual planning – sets out in more detail the Internal Audit activities that will be undertaken in the next twelve months.

Mission planning – covers the work that will be undertaken as part of each Internal Audit assignment and it is very detailed.

If the mission planning is done well, it will ensure the right systems/fields are covered in the right amount of detail – meaning that Internal Audit can add value to the entity being reviewed.

Internal Audit is based on an extensive understanding of the business and the information systems which contribute in the internal controls and financial reporting.

To understand the business the Audit unit must consider the general business risks which the entity faces, the external environment in which the entity operates, the legal and regulatory framework, the entity's previous financial performance and its internal control systems. This should assist in planning an Audit approach which:

- Efficient**      Audit Resources are targeted on the areas of greatest risk and Audit methods are chosen which meet objectives of Internal Audit Unit Directorates at minimum cost;
- Effective**      Obtains sufficient relevant evidence to support the conclusions and recommendations in the Audit report; and
- Adds value**      Senior management of the Audited entity are offered constructive advice on risk management and internal control relevant to their circumstances.

All Audit planning should be risk based – in other words Internal Audit focuses their efforts on systems/fields where there is the greatest potential for things to go wrong.

Risk assessment is performed throughout the entire Audit, but particularly at the planning stages in an annual and strategic level, even during the audit assignment.

Differences between strategic / annual planning and Audit planning include:

Strategic / Annual planning risk assessment	Audit planning risk assessment for each mission
Covers the whole organisation	Covers the processes selected for Auditing.
Uses general information available about risks	Uses more detailed information about risks.
Information about risks may not be the latest	Auditors use updated information in relation to risks.
Risks may be assessed by the auditor only or jointly with management	Risks are assessed by the Auditor alone.
Concerned with strategic risks to high level processes.	Risks usually more operational activity level processes.
Inherent risks assessed separately from internal controls.	The risk assessment is one part of assessing the internal control system of the selected process.

Audit planning for individual systems (that is each Internal Audit mission) is covered in Section 3 of this Internal Audit Manual.

In order to ensure that the Audit planning is effective, the Auditors must have a good understanding of the organisation being audited, the environment in which it operates and the major risks it faces.

Auditors produce a strategic Audit plan which outlines the major planned activities over an extended period of five years and the Internal Audit Unit will need to ensure that all major systems/fields that have been evaluated as high risk areas are covered in that time.

The areas that Internal Audit could possibly cover include:

- Financial management systems such as payroll, accounting system, revenues, and the payments for goods and services;
- Organisational processes such as budgetary control, risk management and medium term financial planning;
- Other high risk systems such as major IT and capital projects (public investments)
- The recruitment process systems.

Information Sources which help in the planning process are internal or external according to the organization

Internal sources of information can be obtained from the management of the entity. Although the Auditors will probably have regular meetings with the senior managers of the entity throughout the year, a specific meeting to help inform the annual and strategic Audit plans will be useful for two purposes:

Auditors should collaborate with the management of the entity and to help

them take some ownership of the Internal Audit plans; and

Auditors identify concerns of the management and other risks that the Auditor may not have been aware of previously.

As part of the Audit planning process, Auditors should also look at the key documents that the organisation has produced. This may include strategic plans, annual reports etc and will help the Internal Audit Unit build up a picture of what the organisation is trying to achieve and what risks it faces.

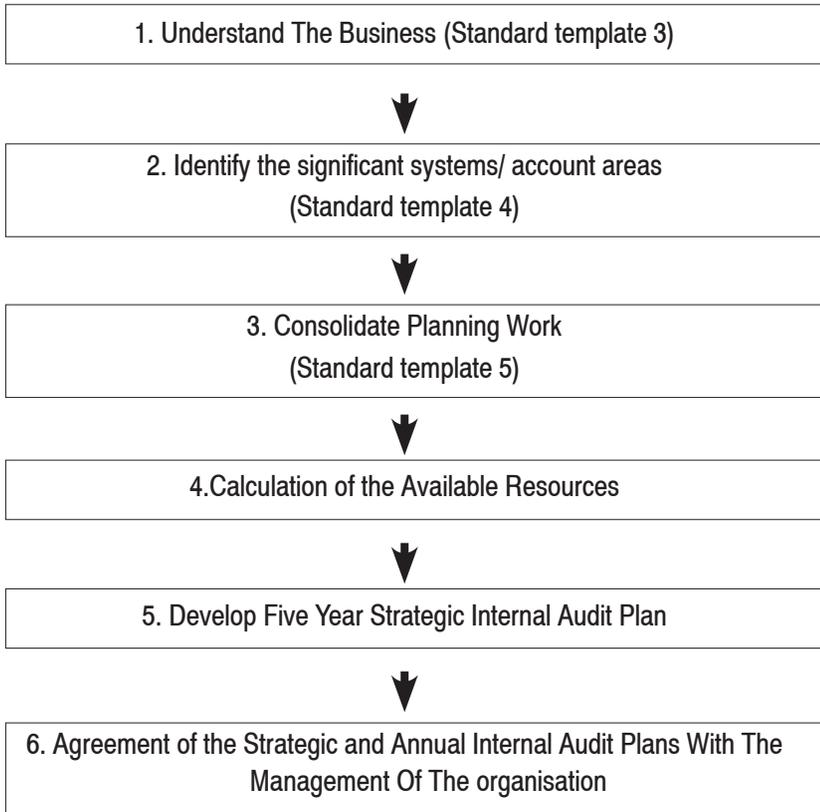
### **2.1 Strategic Audit Planning**

As stated earlier, it is not possible to cover every area each year as there are unlikely to be sufficient Internal Audit resources available.

Internal Auditors therefore produce a strategic Internal Audit plan that ensures that the key risks are covered over an extended period (usually five years).

The key stages in developing a strategic Audit plan are set out in the flowchart on the following page. Further information on each stage is included within this section of the manual.

### 2.1.1 Strategic Internal Audit Planning Flowchart



#### 2.1.1.1 First Stage – Understanding The Business

Auditors must have a good understanding of the organisation being audited, the environment in which it operates and the major risks it faces in order to ensure that the strategic plan is focussed on the correct areas.

Understanding the business will also help the Internal Auditors obtain an understanding of the key business processes in place at the organisation. This will include budget setting, financial planning, risk management etc.

Standard template 3 at the end of this section has been designed to help Internal Audit Units record their understanding of the organisation they will be Auditing.

Some of the information necessary to complete Standard template 3 will already be known by the Internal Audit Unit because of their previous work at the organisation being Audited. However, to ensure that Standard template 3 is based on the most up to date information, it will be necessary to interview the senior managers of the organisation and to review the most up to date reports and business plans.

### **2.1.1.2 Second Stage – Identify the Significant systems/ Account Areas**

#### a).Systems

In order to determine the systems being audited, internal auditors must understand the activities of organisation being audited. This could be done by identifying and reviewing all systems used by the organisation aiming at ensuring that all its objectives and activities have been included in this process.

The head of Internal Audit Units must bear in mind that some systems might address one or more management objectives, whereas some others might address them partially. In order to do this, the head of Internal Audit Unit has to evaluate the systems carefully and try to classify them into comparative groups, for example, recruiting system, training system, payroll system, and so on.

While trying to identify the system being audited, the head of Internal Audit Unit must take into consideration the information of previous periods, previous audit reports if there is any, as well consulting the heads of the organisation.

Classification of systems into groups can be done as follow:

- **Functional Manner** – according to this manner systems are separated based on their function they support to and the role they play to the whole of the organisation’s internal controls (e.g., Operational systems, monitoring systems etc)
- **Recruiting Manner** – according to this manner the systems are separated into relatively small numbers based on the organisation’s organizational structures (e.g. Director, general Director, Sectors, etcetera))
- **Combining Manner** – this method combines the above mentioned Manner (e.g. A functional system that is implemented in some Directorates)

#### b). Accounting Areas

In order to assess which financial areas to look at, the Auditors will need to have a good understanding of the major sources of income and main items of expenditures for the entity. This can be obtained by looking at the budgets and financial statements for the entity.

Standard Template 4 at the end of this section can be used to help Auditors assess which account areas are in place for the organisation being reviewed.

### 2.1.1.3 Third Stage – Consolidate Planning Work

Completing Standard Template 3 and 4 will give the Internal Audit Unit a good understanding of the organisation, the systems used by it and the challenges it faces. However, having identified these systems, Internal Auditors need to demonstrate how they will plan their work to treat these risks. Standard Template 5 has been designed to pull together the risks that have been identified.

Using their professional judgement, internal auditors determine the critical areas that require the internal audit attention. Risk evaluation starts with the reviewing of factors that have the greatest possibility to cause an unexpected event, and prioritising those areas which have a higher chance to have a negative impact from the unexpected event. The three main elements of risk are as follow:

1. An unexpected event that might have an impact in the realisation of an organisation's objectives
2. The chance of this event occurring
3. The negative impact that this event might have on the realisation of the objectives if this event happens.

Determining the frequency of internal audit work and the extension of audit work for the identified systems must be done in a way to ensure sufficient inclusion in order to enable an overall environment of existing control of financial management and control systems:

Factors to take into account include:

- **Significance** – is the system/ area important to the entity? Would a failure in this system/ area cause major problems for the organisation?
- **Materiality** – this means: does the account area cover a large proportion of the income or expenditure of the entity?
- **Change** –To determine the effect of this factor we should take into account if there have been any changes within the area since the last Internal Audit review was undertaken and if there are any future changes planned?
- **Risk** – for this factor internal auditors must evaluate the level of risk of the specific object being audited and they need to take into consideration problems identified from previous audits if there are any.
- **Management point of view** – here the internal auditors take into consideration the opinions of the heads/management of the organisation about the performance of organisation in relation to this specific audit system/account area.
- **External scrutiny** – this factor has to do with the inclusion of other interested groups concerning this issue, object or the organisation being audited. So, the level of interest of other organisations for this issue is

evaluated. For example, the collection rates for local taxes may be of interest to Central Government.

- **Frequency**

Strategic planning must include all indentified systems, but the inclusion of all aspects of internal control within a one year period would not be realistic.

Concerning systems that are evaluated as high risk ones; the strategy of internal auditors is to audit these with a frequent frequency, usually annually. Conversely, systems with a low risk level could be planned to be audited rarely.

When we initially audit a high risk system, the internal controls need to be reviewed in detail, aiming at determining which the key controls are and how effective are they.

Meanwhile, in the following audit at a high risk, the audit work could be focused on verifying if the objectives of systems, objectives of control, risks and controls are the same ones as they have previously been, and in this case the compliance tests of key controls must be conducted.

The Internal Auditors will need to consider to the above factors when in their assessing when to undertake an Internal Audit review and how much time to allocate to it. The guide below are important and must be used in the audit works.

Factor	Internal Audit Response
Significance	Internal Auditors will generally spend more time on areas that are of great significance to the organisation.
Materiality	Internal Auditors will generally spend more time for big areas of income and expenditure and less time (or even no Audit time) for more trivial areas.
Change	Where an account area or business process has changed, then the risk increases and so the Internal Auditors should look for this area in the year that the change was made.
Risk	A risk based approach means that Internal Audit resources will be dedicated to areas where the risk is higher.
Management views	As Internal Audit is providing a service to the management of an organisation, it is important that the strategic plan meets the managers concerns. Areas that are of concern to the organisation's management should be given prominence in the strategic plan. However, caution should be given to the managers views as they try to deflect the Internal Auditors attention away from important areas.
External scrutiny	The existence of external scrutiny raises the importance of a particular area and greater Internal Audit input may be appropriate.
Frequency	The systems that have been assessed as high risk should be audited more frequently auditing. On the other hand, the systems evaluated as low risk should be audited less often

However, in practice, the strategic Internal Audit plan will need to balance out the above factors. There is no scoring methodology that can be used to produce the strategic plan and this will depend on professional judgement. Ultimately, the Internal Auditors need to ensure that the five year strategic plan is a reasonable reflection of the work that should be undertaken.

Standard Template 5 will be helpful in setting out how a five year strategic Audit plan could be developed. Below is an example of such a completed Standard Template 5.

Systems/Area	Source	Significance	Materiality
Collecting Local Taxes	Standard Template 3 and 4	Effective collection is essential to the financial well being of the organisation	20% of the organisation's income comes from this source
Payroll	Standard Template 3 and 4	If staff are not paid correctly the organisation will not be able to operate	More than 60% of the organisation's expenditure relates to staff costs
Collecting planning fees	Standard Template 3 and 4	This is not of significance to the organisation	Less than 2% of the total income are provided from planning fees gathering
Budget setting	Standard Template 3 and 4	This is essential if the organisation is to function properly	Covers all of the organisation's income and expenditure
Petty cash expenditure for planned expenditures	Standard Template 3 and 4	This is of no significance to the organisation	This is kept to a minimum and is insignificant.

Change	Risk	Management Views	External Scrutiny	Internal Audit Response
The system has not changed and there are no plans to make any amendments	System is well established and there have been no significant problems with this account area	Management do not have any concerns related to this account area	Central Government monitor the collection rates	Some rate coverage each year, more detailed review in years 2 and 4
The system is expected to change in the next two years	There have been previous problems and management have agreed to make major changes in this account area	Management are concerned that internal control weaknesses still exist	There is no external scrutiny	Review this area each year. Extra time to be spent in the year when the system changes
No changes expected	Minor weaknesses found last year	Management do not have any concerns related to this account area	There is no external scrutiny	Follow up previous recommendations in year 1. Review again in year 4
The system has not changed and there are no plans to make any amendments	This is a well controlled process and no major weaknesses have been found in the past	Management have no concerns	Central Government acts if the budget is overspent or under spent	Review in years 1, 3 and 5
The system has not changed and there is no change	There is a high risk that small amounts of money could be stolen	Management have no concerns	There is no external scrutiny	None – not to be included in the Internal Auditors' plans

### 2.1.1.4 Forth Stage – Calculate Available Resources

Initially, the time allocated to the Internal Audit work each year will be limited to the Internal Audit resources that are currently available.

#### Duration

The head of IAU must determine the number of working days needed to audit the identified systems during the next 4 years.

To determine the expected Standard time needed for an audit activity, the level of risk for each system is taken into consideration:

- Systems evaluated as high risk- need more time.
- Systems evaluated as medium risk- need less time than those evaluated as high risk ones and more time than those evaluated as low risk ones.
- Systems evaluated as low risk- need less time than those evaluated as medium ones.

Also needs to be considered the complexity of an account area or system. The simple systems need less time than complex areas. For example, it would take longer to audit payroll than to audit photocopier income.

The head of internal audit unit calculates the days necessary for each year of the strategic planning and later he completes a request for the human resources needed to conduct auditing activities.

Determining human resources needed for an internal audit activity.

The available resources should be calculated for the Internal Audit Unit each year, taking into account time for training, holidays etc and possible absence due to sicknesses. This will ensure that the plan is achievable.

For a team of 4 people, the available resources each year could be 812 days in total, in the example as follows:

Description	Days	Calculation
Maximum time available	1040	52weeks x 5 days x 4 people
Annual Holidays	(80)	4 weeks per person
Bank Holidays	(32)	8 days person
Sickness	(20)	1 week per person
Training	(40)	2 weeks per person
Team Meetings	(16)	Quarterly meetings
Contingency Allowance	(40)	2 weeks per person
Total Resources Available	812 Days	(203 days per person)

When calculating the exact resources available, issues such as part-time working as well as the actual annual leave and bank holidays in the year should be considered. The available resources should be reviewed each year to reflect any changes that will have an impact on the delivery of the planned work such as long-term sickness, staff vacancies and maternity leave.

However, over the longer term, the strategic planning should be used to establish the extent of the Internal Audit input that is required in each area.

For example, a high risk organisation may only have a relatively small Internal Audit Unit and, over time, it may be appropriate to increase the level of resources that are available. Conversely, some large well managed organisations may have excess Internal Audit resources.

In due course, it may be necessary to bring in additional Internal Audit resources to cover areas where a specific level of expertise is required, for example of a major IT project where they may not be sufficient skills available.

Based on the above calculations, the head of an internal audit unit can determine the number of auditors that are needed to undertake the planned work.

By dividing the total number of days planned with the number of available days for an Internal Auditor, the calculation will be an approximation of the number of internal auditors that are needed.

So, if the total number of Internal Audit days needed in one year is 1080 and the average Internal Auditor can input 203 working days, the necessary resources are:

$$1080 / 203 = 5.32 \text{ persons}$$

Such a calculation would enable the comparison of the numbers of Internal Auditors that are needed with the number of existing auditors. This will help to ensure that the right resources are available.

A needs assessment would ensure that the IAU would have the necessary staff to realise this plan. If more auditors are needed then the head of IAU will be responsible for filling the vacancy.

Such an assessment would also forecast the use and contracting of external resources or outsourcing. In the cases where no extra resources can be found then the head of IAU needs to make an efficient use of the available resources, perhaps by fine-tuning the five year strategic plan or re-visiting the risk assessment.

It is important to emphasise that even though sufficient care has been taken during planning phase, total accuracy regarding the resources can never be achieved.

The strategic planning needs to be reviewed and updated annually. This means that the second year of current strategic planning will be the first year

of the coming year and it will be the bases of the annual plan of the coming year (working plan for the coming year + strategic planning for next four years).

Internal audit strategic planning must be prepared together with the annual planning for the coming year. A review of strategic planning should be done when there are big changes being made to the activity and the way organisation is organised.

During the planning phase of the strategic plan, the head of Internal Audit Unit could allocate specific to Internal auditors that have to do with the gathering and analysis of necessary data relating to the activities and strategic objectives of the organisation.

The auditors should also be asked to help in determining the objectives and priorities of Internal Audit, by identifying systems that need to be audited as well as the risk and their evaluation. While segregating the duties, the head of Internal Audit Unit must take into consideration the abilities, experience, and the professional level of the auditors.

### 2.1.1.5 Fifth Stage – Develop of the Internal Audit Strategic Plan

The next stage is to take the information about the organisation and its account areas and turn these into a strategic plan.

When planning the work at a strategic level, Auditors may choose to look at entire areas each year, as follows:

Area	Year 1	Year 2	Year 3	Year 4	Year 5
Payroll	√				
Risk Management System		√			
Major building projects			√		
Budgetary Control System				√	
Property Maintenance					√

Alternatively, Auditors may choose to look at different aspects of an account area over a number of years.

An example of the payroll system which includes these account areas is as follows:

Area	2010	2011	2012	2013	2014
Payroll – overview	√				
Overtime payments		√			
New starters			√		
Leavers				√	
Additional allowances					√

The latter approach may be appropriate if the available days are limited meaning that it is not possible to cover an entire account area in any one year.

### 2.1.1.6 Sixth Stage – Agreeing the Five Year Strategic Internal Audit Plan

Internal Auditors exist to provide independent assurance to the management of an organisation. As such, it is important for the strategic Internal Audit plan to be discussed with the management of the entity and for it to be agreed with them.

This work practise has the benefits of ensuring that the strategic plan covers all of the risk areas in the organisation as well as getting the management to buy into the Internal Audit process.

If there are any disagreements between the management and the Internal Audit Unit, these should look to be resolved by negotiation. However, where this is not possible, the independence of the Internal Auditors and the rights of access to both information and personnel that are included in the Internal Audit Charter mean that the final decision over the contents of the Internal Audit strategic plan rests with the Internal Audit Unit. In practice, such disagreements are likely to be very rare.

## 2.2 Annual Audit Planning

The annual Audit planning can only be done once the strategic Internal Audit plan has been produced.

As treated above, the strategic Internal Audit plan gives an outline of what will be covered over the next five year whereas the annual Audit plan provides more information about the exact nature of the Internal Audit work that will be

undertaken in the next year.

Whilst the strategic Internal Audit plan will be a very high level plan, the Annual Audit Plan will be more detailed and based on a more informed risk assessment.

As part of the production of the Annual Audit Plan will be the completion of the overall control environment checklist (see Standard template 7).

This template needs to be completed once each year as part of the annual Audit planning exercise. In future years, it will not be necessary to complete the overall control environment checklist from scratch; the Internal Auditors can simply improve it to reflect any changes.

Standard template of the overall control environment checklist is used to help with the risk assessment for each account area being reviewed and is therefore best done when the annual plan is being produced.

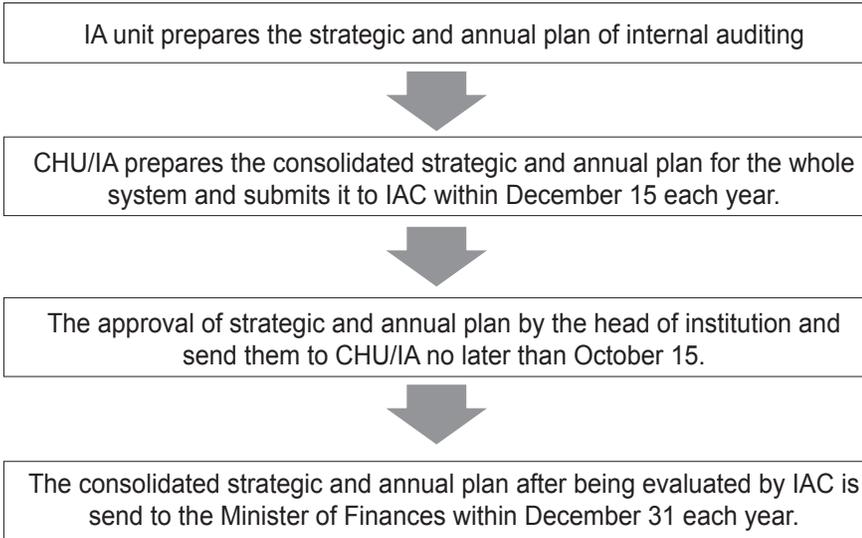
### **2.3 The deadline for preparing the strategic and annual planning**

The strategic and the annual plan, prepared by IA units after the approval by the head of institution need to be submitted no later than October 15 to the IA unit of the relevant ministry of central insitution. the latter ones prepare the summurising strategic and annual plan in Ministry of central insitution level, which include the strategic and annual plan of IA unit as well as the startegic and annual plans of subsidairies. . This plan of all managing line of ministry or central insitutions, together with the annual plan approved by the head of insitution is send in an official way and via on line to the CHU/IA within October 30 each year.

In particular, the strategic and annual plans of the IA unit of local government (municipalities, communes, coulcil of districs etc), after the heads apporval are send to to the CHU/IA no later than October 30

CHU/IA prepares every 15 December of each year the Consolidated Strategic and Annual Plan about the overall Internal Audit activity in the public unit.The Plan is submitted to the Minister of Finance after its evaluation from the Internal Audit Committee.

The reporting way of the Strategic and Annual Plan are defined with specific guidelines



### 2.4 Links Between Strategic Internal Audit Planning and the Annual Audit Plan

An example strategic Internal Audit is included within the Standard templates at the end of this section.

An extract from a strategic Internal Audit plan could look like:

Systems	2010	2011	2012	2013	2014
Payroll	20 days	10 days	10 days	10 days	10 days
Risk Management System		30 days			20 days
Major building projects	50 days				
Budgetary control System	15 days		15 days		15 days
Property Maintenance				20 days	

The Annual Audit Plan then converts the first column of the five year plan (i.e. the next financial year) into greater detail. An example, based on the above extract, could be as follows:

Main Area	Details of work to be carried out	Budget
Payroll	Follow on the recommendations in the last Internal Audit report	2 days
	Document and assess the new procedures for payroll and carry out a detailed assessment of the internal controls in place	18 days
Major building projects	Assess how well expenditure on major projects is planned and controlled	15 days
	Review the arrangements for prioritising potential projects	10 days
	Assess how the revenue implications of capital schemes are considered when setting the budget	5 days
	Assess how the organisation ensures that major building projects offer value for money	20 days
Budgetary control	Assess the arrangements for monitoring the organisation's income and expenditure each month and for reporting variances to the senior management	15 days

As with the strategic Internal Audit plan, and for Annual Audit Plan should be agreed also with the senior management of the organisation. These plans are approved from the head of the organisation

### 2.5 Review of the Strategic and Annual Internal Audit Plans

Time to time there will be issues within an organisation that may require the Internal Audit plans to be reviewed and changed.

Internal Audit is intended to be a helpful service to the management of an organisation and it is therefore important form Internal Audit plans to respond to any changes.

Whilst the Internal Audit planning will involve discussions with officers, there may still be developments which were not known at the time the plans were set. Changes could include:

- A new IT system in a particular account area;
- A major building project;
- A large fraud; or
- A merger with another organisation.

Any changes to the Internal Audit plans need to be approved by the Director of the Internal Audit Unit and also agreed with the management of the entity.

Because of this, some Internal Auditors will include a small contingency allowance within their plans which can be used to deal with emerging issues as and when they arise. The use of this 'contingency allowance' should be included within the Annual Report.

All revised annual and strategic five year Internal Audit plans should be sent to the CHU/IA together with an explanation of the changes.



**Templates  
for**  
**Chapter II**

Standard Template 3 – Strategic Planning Questionnaire – Understanding The Internal Audit procedures

Question	Possible Sources Of Evidence	Response
Are there any significant issues at the organisation that were identified during previous Internal Audit missions?	Previous Internal Audit Reports Knowledge of the Internal Audit Unit	
What are the key objectives of the organisation? Is it likely that the organisation will not achieve any of these objectives?	Enquiries of the management of the organisation Business Plans Knowledge of the Internal Audit Unit	
What are the important account areas for the organisations?	Standard Template 4 Enquiries of the management of the organisation	

The key Internal Audit risks relating to the organisation and the proposed Internal Audit response should be summarised below

Summary Of Risks Identified	
Risk	Proposed Internal Audit Work

### Instructions for Completing Standard Template 3

Understanding the business is the first stage of producing a strategic plan. The Internal Auditors should complete this standard template each year, although it may be possible to use the previous year's standard template as a starting point and update this for any known changes.

Possible sources of information are included on the standard template as an example only. The actual sources of information will vary from organisation to organisation.

When looking to answer the questions, Internal Auditors should think about more what may happen over the next five years rather than what will happen in the near future. Thus, for example, if an organisation is planning a major building project in three years time, this may need to be included within the strategic Internal Audit plan in the relevant year.

Auditors should look to obtain information at such a level that will impact on their general approach over the next five years. They must not try to identify every single planned change or every piece of legislation, but simply those things that would affect the amount of Internal Audit work they plan to do.

The identified risks and the planned Internal Audit work should be summarised at the end of the Standard Template.

### Standard Template 4 – Identification of the Organisation System

The purpose of this Standard Template is to help Auditors identify the account areas that are in place at the organisation being audited.

An account area is a process or set of financial transactions that are subject to the same procedures and internal controls.

For example, an organisation (University) may charge tuition fees to its students. To each student it is applied the same procedure in order to ensure that:

- All students pay tuition fees
- All students pay the correct tuition fees
- All incomes are banked promptly
- All income is correctly analysed within the University's main accounting system.

The University may also obtain income from the sale of the products (e.g. books, canteens etc). However, even if these are all income sources for the University, they will all be subject to different processes and so form different account areas.

When planning the Internal Audit coverage, Internal Auditors need to consider both the risks of the account area and also the significance of it to the organisation.

The University probably gets a much larger proportion of its income from Student's tuition fees than from the sale of books and so this will be a more important area to look at.

### **Template 4 Identification of systems/Account Areas**

Instructions for completion

The Internal Auditors should obtain a copy of the most recent budget for the organisation being Audited. They should then list the areas of income and expenditure on this template and allocate these two separate account areas. This will ensure that all account areas have been considered as part of the Audit planning work.

A fictional example for a University is set out below. Please note that this has been simplified for ease of reading.

Area	Amount (million lekë)	Individual Account Areas				
		Student Tuition Fees	Accommodation Charges	Cash Income	Payroll	Payments for Goods and Services
Income						
Student Fees	xxx	√				
Student Flats	xxx		√			
Restaurant	xxx			√		
Book Sales	xxx			√		
Photocopying	xxx			√		

Area	Amount (million lekë)	Individual Account Areas				
		Student Tuition Fees	Accommodation Charges	Cash Income	Payroll	Payments for Goods and Services
Expenditure						
Teaching Staff	xxx				√	
Administrative Staff	xxx				√	
Property maintenance	xxx					√
Food	xxx					√
Books	xxx					√
Electricity and Gas	xxx					√
Travel	xxx					√
Security Costs	xxx				√	
Stationery	xxx					√

In this particular example, the organisation has five separate account areas: student tuition fees, accommodation charges, cash income, payroll and payments for goods and services.

**Standard Template 5- Linking between Risk and the Planned Internal Audit Work**

Area	Source	Significance	Materiality	Change	Risk	Management Views	External Scrutiny	Internal Audit Response

Standard Template 6 : Example of Five Year Strategic Internal Audit Plan

Area	Year 1	Year 2	Year 3	Year 4	Year 5
1. Finance Directorate	123	103	103	103	103
Cash & Bank	10	10	10	10	10
Local Taxes	15	30	15	15	15
Debtors	8	8	8	8	8
Payments for Goods and Services	15	15	15	15	15
Main Accounting System	5	5	5	5	5
Incoming and expenditures Control	20		20		20
Payroll	20	20	20	20	20
Insurance & Risk Management	5	5	5	5	5
Capital Expenditure	20	5		20	
Inventory (Stock)	5	5	5	5	5
2. Human Resources and supportive Services Department	40	30	45	25	40
Human Resources	5		5		
Services Allowances		5			5
Car Loans & Allowances	10		10		10
Property Management	5	5	5	5	5
Corporate Property Maintenance		5		5	
Legal Services	5		5		5
Community Safety			5		
Economic Development	5	5	5	5	5
Electoral Registration & Expenses		5		5	
Committee Services	5		5		5
Security	5		5		5
Market Income		5		5	

2. Other Areas	102	145	130	150	135
Organisation Environment management	5		5		5
IT Audit	30	30	30	30	30
Internal Audit Plan	5	5	5	5	5
Following Recommendation Procedures	10	10	10	10	10
Others	100	80	105	85	85
Total days (1+2+3)	278	278	278	278	278

**Standard Template 7: Overall Control Environment Checklist**

Entity name: ..... Ref..... Year: 20.. Internal Audit  
 Unit:.....

Control Issue	Yes	No	Comment
1. Integrity and ethical values			
1.1 Is there a Code of Ethics (or equivalent) in place?			
1.2 Have staff been trained on the Code of Ethics, and the implications of non-compliance and has it been implemented effectively? Are sanctions taken where the Code of Ethics is not complied with?			
1.3 Are you aware of any major concerns (for example in the press, parliament etc) regarding ethical behaviour at the entity?			
2. Staff Competence			
2.1 Have realistic objectives for staff been set by the management?			
2.2 Is staff performance regularly assessed against these objectives?			
2.3 Does the recruitment process ensure that staff have the necessary skills, qualification and experience?			
2.4 Is there an effective programme of staff training, including internal control?			
3. Audit Committee			
3.1. Does the Audited entity have an Audit Committee?			
If the entity does have an Audit Committee:			
3.2. Is the Audit Committee operational?			
3.3. Does the Audit Committee have sufficient authority?			
3.4. Does the Audit Committee meet frequently enough?			
3.5. Does the Audit Committee get enough information in order to take decisions?			
3.6. Are the members of Audit Committee independent of management?			
3.7. Do the Auditors have the right to interact directly with Audit Committee members?			
4. Risk Management			
4.1 Is risk management undertaken at the entity?			
4.2 If yes, is this risk management effective?			
4.3 Do management stress the importance of strong internal control?			
4.4 Do management stress the importance of complying with laws and regulations?			

Control Issue	Yes	No	Comment
<b>5. Organisational structure</b>			
5.1 Is there an approved, up to date and clearly defined organisational structure in place?			
5.2 Is the organisational structure adhered to?			
5.3 Have the accountability and reporting lines been defined and communicated throughout the organisation?			
5.4 Does the organisational structure support the achievement of the organisation's objectives?			
5.5 Is there a system in place to assess the overall performance of the organisation?			
5.6 Does the organisational structure support effective decision-making?			
<b>6. Segregation of Duties</b>			
6.1 Are staff responsibilities described in their job descriptions and employment contracts?			
6.2 Are there rules for delegation and authorising transactions?			
6.3 Are the rules regarding segregation of duties and authorising transactions adhered to?			
6.4 If decision-making has been delegated to lower management levels, is this accompanied with sufficient management supervision?			

Control Issue	Yes	No	Comment
<b>7. Human Resources</b>			
7.1 Is there a comprehensive HR policy, covering workforce planning, recruitment, retention, promotion, termination, ethical values, training, appraisal and remuneration?			
7.2 Is there appropriate induction training for new staff? (for example, showing how the organisation works and what their own job will involve)			
7.3 Are the remuneration and promotion systems motivating?			
7.4 Is the staff turnover done at those levels that enable the achievement of organisational objectives?			
7.5 Is there a system in place to assess staff performance?			
7.6 Do the staff feel that the employee appraisal system is objective?			
7.7 Does the employee appraisal system take into consideration professional and ethical Standards?			
Overall Assessment: High / Medium / Low			

### Instructions for the completion of the Standard Template 7 – The overall control environment checklist

The overall control environment checklist is intended to help the Internal Audit Unit understand how well the entity is managed.

The aim of the audit group is to produce an overall assessment for the entity as to whether it is high, medium or low risk.

These can be summarised as follows:

**High Risk** – there are major concerns about how the entity is managed and more Internal Audit work is asked to be spent.

**Medium Risk** – the entity is reasonably well run, although there is scope to improve how well it is managed in some areas.

**Low Risk** – the entity is well run and the Internal Auditors do not have any major concerns. As a consequence less Internal Audit work is considered appropriate.

### Completion of the Standard Template

Standard Template of the overall control environment checklist should be completed once each year and this should be done as part of the initial planning process.

As the overall control environment assesses the management of the entity, the conclusion will apply to each of the areas being reviewed by Internal Audit.

Initially, the form will take a lot of effort to complete. However, in subsequent years it will simply be a case of updating the form for any known changes.

The Internal Audit Unit should answer all of the questions on the overall control environment and should include comments to justify their explanations for each question.

In some cases, may have positive evidence to support an answer – for example ‘does the entity have an Audit Committee?’

In other cases, audits staff may be looking for negative evidence. For example, they may assume that all staff are appropriately skilled and competent unless they have evidence to the contrary.

The overall conclusion should be based on the Auditor’s professional judgement, taking into account the significance of each question. It is not a mathematical exercise that can be done using a set of rules.

The Auditors should answer with ‘Yes’ or ‘No’ for each questions and should not answer ‘possibly’, ‘maybe’ or “sometimes”.

To help in the overall risk assessment, the answers which are at a low risk have

been shaded grey and the answers which are high risk are blank.

The Auditors should ensure that they include a supporting comment alongside each answer and that they obtain sufficient evidence to support their answer.

Where the arrangements have been assessed as being unsatisfactory, the Auditors should make recommendations to the entity to ensure that the problems are treated.

# Chapter III:

**Internal Audit Execution,  
including follow up Recommendation**

### Purpose

The definition of the Institute of Internal Auditors states that “ Internal Auditing is an independent activity that provides objective assurance and consultancy, designed to add value and to improve operations of the organisation. It helps the organisation by using a systematic and disciplined method for the effective evaluation of risk management process, control and governance.”

A systematic and disciplined method can be achieved when the internal auditors implement a common methodology and comply with the professional Standards. This chapter describe a standard method for undertaking internal audit activity. Internal auditors should become familiar with the details of this manual in order to harmonise the internal audit practices and at the same time the quality assurance of audit work in all public sector organisations.

This chapter introduces activities that internal auditors conduct within the framework of a specific internal audit mission, participation in the process, their function and responsibilities at each phase of the audit process (planning, execution, reporting and follow up procedures ( on previous recommendations).

This chapter may be used for the auditing of financial systems/areas (such as the payroll system, budgetary management and control) and can be easily adopted to cover the work of internal audit in other fields, such as risk management and the systems of financial management.

This chapter also provides a set of internal audit working papers which guide internal auditors during audit engagement and record the necessary audit evidence. This will ensure the fulfilment of internal audit standard requirements in relation to audit documentation.

Internal audits can be different, depending on the organisation, processes, and the method used and therefore it may not be necessary to use all working templates. Equally, in some cases extra documents may be required. For this reason the internal auditors shall use their professional judgement in order to determine which documents are useful and suitable for each internal audit assignment.

### 3.1 Audit process diagram

Audit working papers mentioned on the above paragraph shall be used on four phases of each audit mission, which are as follows:

First phase – Audit Engagement Planning

Second phase –Execution phase

Third phase – Reporting

Fourth Phase – Follow up procedures

Identified systems to be audited are determined in the strategic and annual plans of the Internal Audit Unit. The task of internal auditors is to help management of the audited organisation to detect and evaluate the major risks and give recommendations for the improvement of financial management and controls that operate in this organisation.

In general, a system means a group of transactions that are subject to a common process – for example payroll or system payments for goods and services.

Through internal audits, internal auditors assess the controls and mechanism that exist, the way that they function and the scale of their impact on the objectives of the organisation. This can be realised by examine and evaluating whole processes in the organisation.

The following diagram summarises the process of internal audit that is going to be done for each identified system being audited according to what has been determined in strategic and annual plans for the organisation.

Auditors should prepare a separate plan for each system that is going to be audited that matches the time of each area. This ensures that the work of internal audit ends at the right time and within deadlines. Budget and personal planning will completely finish only after step 7 in the internal audit process diagram.

### 3.1.1 Engagement Planning

Before the detailed Audit work as outlined in the audit process flowchart on the previous page can begin, the practical arrangements for undertaking and reviewing the work need to be determined.

In general, in order to conduct an audit effectively, the planning phase includes the following two major steps:

1. Preparation for auditing
2. Planning of audit activities and the allocation of resources.

Standard Template 10 provides a framework for this mission planning exercise.

The factors that need to be considered include:

- Membership of the Audit unit
- Individual responsibilities of each audit staff
- Timescales
- Quality Assurance arrangements

### 3.1.1.1 Membership of the Audit Unit

When planning the engagement, you will need to decide what unit members will undertake the work.

Factors to consider include:

Whether there are any potential independence issues with Internal Audit staff that would prevent them undertaking Audit work at this organisation or in this system;

- The size and complexity of the organisation;
- The complexity and risk of the system/ account area being Audited;
- The experience of the staff and the number of auditors; and
- Whether there are any additional training for the staff involved.

You should always aim to use the staff appropriately. Therefore more experienced members of the Internal Audit Unit should undertake the planning of the work, with more junior members being used to complete the detailed testing.

Where an organisation is being Audited is very complex, or the system being reviewed is assessed as being high risk, you should aim to involve more experienced Internal Audit staff where this is possible.

Equally, if the planned Internal Audit work is of a very specialist area (for example reviewing a major construction project) then you should look to use staff members with experience in this area.

Recruitment of this expertise will be a matter of the Head subject after the submitted approval from CHU/IA. Payments for the experts is a special order given by the Minister of Finance.

### 3.1.1.2 Individual responsibilities of each auditee

Put simply, the mission planning needs to consider 'who does what'.

It is essential for every single one of the tasks, from the initial planning through to the issuing of the final Internal Audit report, to be allocated to individual members of the unit. This will ensure that the Internal Audit mission can be undertaken in an efficient way. Standard Template 10 and template 11 will help with this.

When allocating the individual tasks to be completed, you should consider the relative experience and skills of the staff that will be used on the mission. This will ensure that the more experienced staff are used on the most complex areas of the work.

### 3.1.1.3 Duration (Timescales)

Unless a proper project plan is produced, it is possible for there to be delays in the completion of the Internal Audit work and for the work to take longer than was originally planned. Standard Templates 10 and 11 will help with this planning.

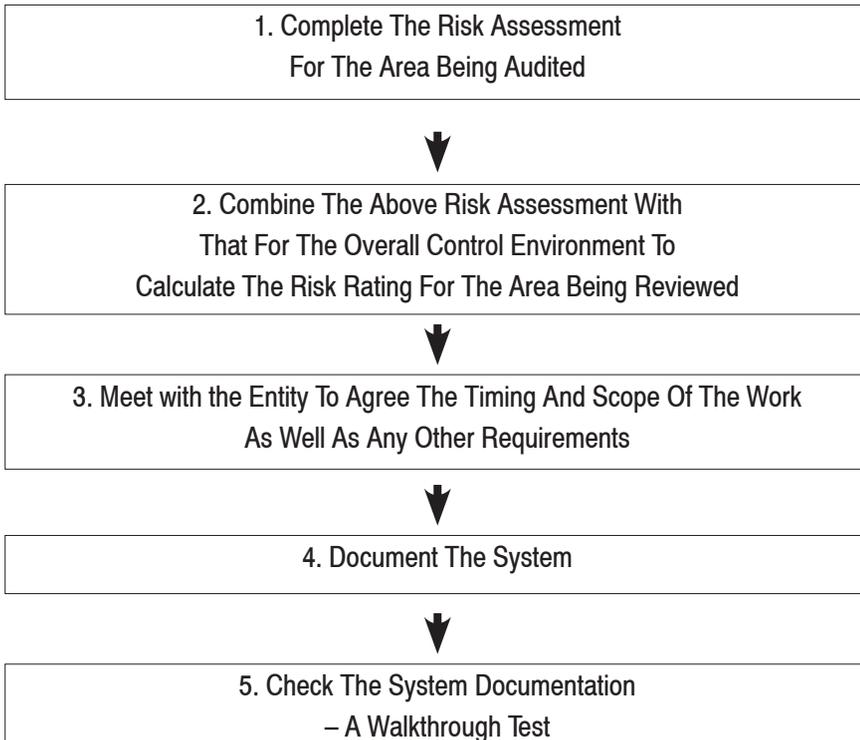
As part of the initial meeting with the organisation being Audited, you should discuss the planned timescales with the senior managers of the entity and agree the timescales with them. This is particularly important for aspects of the Internal Audit work where input from the organisation itself – such as supplying information regarding the system/area being Audited or responding to the draft Internal Audit report.

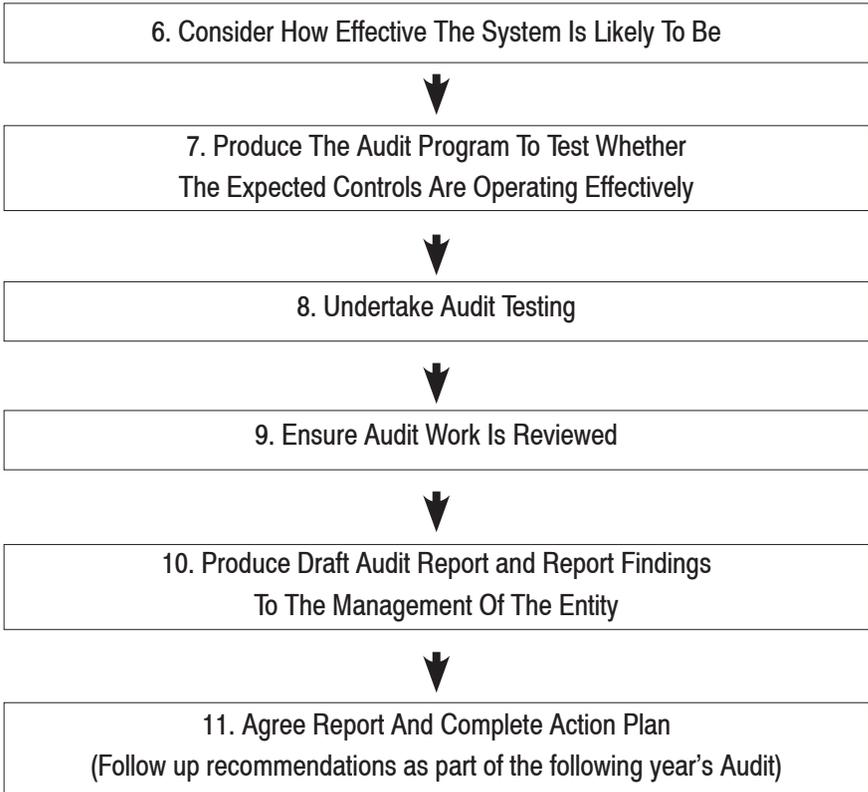
### 3.1.1.4 Quality Assurance Arrangements

Chapter IV of this Internal Audit manual covers quality assurance in more detail.

However, as quality assurance needs to take place throughout the mission, it is important for this to be built into the overall mission plan. This will ensure that there are not delays caused by the Internal Audit Unit group should review waiting the work during one stage before they move onto the next stage.

The individual steps of the Internal Audit flowchart are now covered in more detail.





**3.1.2 Step 1: Complete the Risk Assessment for System/ the Area Being Audited**

As has been stated elsewhere in this manual all Internal Audit work is risk-based. This ensures that limited Internal Audit time is spent on the most important areas.

The first stage of the execution work is the completion of the risk assessment for the area being reviewed and this is included with the Standard Templates section of this part of the manual –( see Standard Template 8). Detailed instructions regarding the completion of the risk assessment are set out below.

a). As part of the initial entity-wide planning process, the overall control environment was assessed.

The valuation of Risk for special systems is done Furthermore

b).The differences between the account area risk assessment and the overall control environment assessment are as follows:

	Overall Control Environment Assessment	Account Area Risk Assessment
Timing	Completed during the overall Audit planning for the year.	Completed as part of the execution stage for the area being reviewed.
Completion	Completed once a year.	Completed once for each account area.
Coverage	Covers the whole entity.	Coverage restricted to the account area being Audited.
Assessment	The assessment covers the whole entity and a high risk assessment means that the entity is badly run.	The assessment is restricted in coverage and a high risk assessment does not necessarily mean that the area is badly managed, it may simply be that there is a high inherent risk in that area.

### **3.1.3 Step 2: Calculation Coefficient Overall Risk Assessment that is audited**

The Audits members combine the risk assessment of a special system with a general control assessment in order to calculate the risk coefficient for the system that is audited. As part of the strategic and annual audit planning, the Internal Auditors will complete the standard template of the overall control environment checklist-( see Standard Template 7 in the Chapter II end).

Step one, above, requires the Internal Auditors to assess the risk for the system / account area being reviewed.

These two risk assessments can be combined to give an overall risk assessment for the area being reviewed, using the table overleaf.

Assessment of overall control environment	Assessment of system/ area being reviewed	Overall Risk Assessment
High	High	High
High	Medium	High
High	Low	Medium
Medium	High	High
Medium	Medium	Medium
Medium	Low	Medium
Low	High	Medium
Low	Medium	Medium
Low	Low	Low

So, for example, if the overall control environment is assigned as a high risk, but the assessment of the system / account area is assigned as a low risk, the overall assessment results to a medium risk.

**3.1.4 Step 3. Meet with the Entity to Agree the Timing, Scope Of The Work and Any Other Requirements**

The Internal Audit Unit should meet with relevant staff of the entity at the start of the Audit process. This will enable the Internal Audit Unit to outline what work they plan to do, when they will do and which will be the key contacts.

As a rule, The Director of the IAU notifies the organisation 10 days in advance of the initial meeting to assist full co-operation and communication between the entity and the Audit unit.

In special cases, however, the Internal Audit Unit leader need not notify the Auditee in advance. These special cases are based upon the judgment of the Audit manager, mainly related to special Audits, where, for example, there is evidence of misuse or abuse, as well as possible penal actions. In these circumstances, advance notification to the organisation could result in critical information being hidden by management from the Auditors. For any case of intervention without prior notification, the Director of the IAU is obliged to retain in the Audit file the justification and cause of the Audit.

The initial meeting with the Audited entity should openly discuss the Audit objectives, Audit approach, timetable and the reporting arrangements. Internal Auditors should consider any areas of management concern or identified risk on which the entity management could benefit from an independent internal Audit assessment. Wherever possible, the Audit plan should provide jointly

assurance over such risks. The meeting should be documented and minutes agreed.

The head of Internal Audit Unit approves the service Order that is prepared by the working group in accordance with annual planning of the internal audit unit. Such a document represents the mandate for the completion of the audit engagement in the relevant organisation.

A suggested agenda for the initial meeting is included within the Standard Templates 9.

Before the meeting with the entity can take place, the Audit unit should agree the scope of their work and the objectives they are trying to achieve. This should link to the earlier planning work for the entity and the scope should cover:

- Name of Audited entity;
- Audited period;
- Internal Audit Objectives for the area being reviewed;
- Internal Audit Objectives for the systems/areas being reviewed, documents to be checked; and
- Location for specific other testing

Example: Audit objectives: Ministry x manages the pay roll for its staff

**Audit Risk:** The Ministry may not fully comply with contractual or legislative requirements; may not have adequate systems and controls to accurately identify staff salary entitlements; or may not effectively manage the staff payroll.

**General Audit Objectives** may include to:

- Assess whether the payroll process conforms to relevant legislation, management policy and procedures.
- Ensure that the payroll system pays staff according to their contracts and on time;
- Payroll procedures that the payrolls are effective and efficient.

**Specific Audit Objectives** may include ensuring

- Staff working hours and leavers, promotions, salaries and salary deduction are properly authorised;
- Time sheets are properly reviewed, approved, processed, documented and accurately recorded to the appropriate accounting or budget code;
- Gross pay, deductions and net pay are accurate and based on authorised contractual arrangements;
- Taxation and social security information is accurately and promptly reported as required by the established authorities;and
- Payroll information is handled and maintained confidentially.

### 3.1.5 Step 4: Documentation of the System (through a diagram)

Before the detailed Audit testing can take place, the Auditors will need to have a full understanding of the area that they will be Auditing.

This will require discussions with the relevant staff at the entity and these staff will have been identified in the initial planning meeting covered above.

As set out above, Auditors begin by completing the risk assessment for the system/ area being audited. Standard Template 8 helps them obtain an understanding of the risks relating to that system/ account area and the controls that the entity's management have put in place.

Once the Standard Template has been completed, the Auditors should assess whether the system is high, medium or low risk.

The next stage is for the Auditors to document the system that they are looking to Audit.

This should be very comprehensive and should cover every single stage of the process at the organisation. Also, when auditing a payment for example, Auditors should separately record the process when people join the organisation (starters) and when they stop being employed by the organisation (leavers) as well as the processes for paying overtime etc.

The documentation of these systems should be in a diagrammatic form through a block diagram or a flow chart which records the whole of the Audit trail and management and transactional controls built into the process.

The Auditor should ensure that the system documentation is entirely updated and should be specified if their previous diagrams are used or if the Audited organisation has provided the diagrams. The Auditors are responsible for the accuracy of the system diagrams which are used during Audit planning.

As a starting point, the Internal Audit Unit should establish a permanent file for each organisation. The Internal Audit Unit should limit requests for additional information about the organisation or process to systems/areas not on the permanent file.

The Internal Audit Unit should later update the permanent file with additional relevant Audit information and delete out-of-date or superfluous material. Permanent file contents are described in Section 5.

As well as recording the actual process, the Auditors should also record the internal controls that are in place.

### A practical example of Internal Controls

Imagine you are the owner of a bar. You would probably want the following things:

- All customers to pay the right amount for their drinks;
- Customers to pay for all of the drinks they had been served;
- Cash was not stolen; and
- Staff salary should be at the right amount and paid only for the hours they actually worked.

How would you ensure that the above mentioned things are going to be executed rigorously?

You would probably introduce a range of processes which you would expect your staff to comply with. Perhaps you would get all staff to complete timesheets which are authorised by the manager of the bar before the staffs were paid. These processes are known as internal controls and help safeguard the business.

The same applies to the organisations which are Audited. The management should have put in place effective internal controls to safeguard that entity.

Control procedures are the policies and procedures that management establish to protect against fraud, loss, irregularity and errors. They could have preventive or detective in nature.

### 3.1.5.1 Preventive Internal Control

A preventive internal control stops things going wrong in the first place. For example, the authorisation of a timesheet before a member of staff is paid helps to prevent an incorrect payment being made.

### 3.1.5.2 Detective Internal Control

A detective Internal Control finds out if things have gone wrong. For example, by comparing the total on the till roll to the amount of cash in the till can detect any problems with the cash collection procedures in place.

The procedures of internal control shall be followed for all transactions for a system/or specified area. For example:

- Every time a new employee joins an organisation, a new starters form is completed;
- Whenever an invoice is paid by an organisation, it matches it to the original order and the goods received note in order to ensure that the invoice relates

to something that has (a) been required and (b) has been delivered to the organisation.

- Each time a payment for rental income is received, a duplicate receipt is produced. One is given to the person renting the property and the other is filed by the organisation.

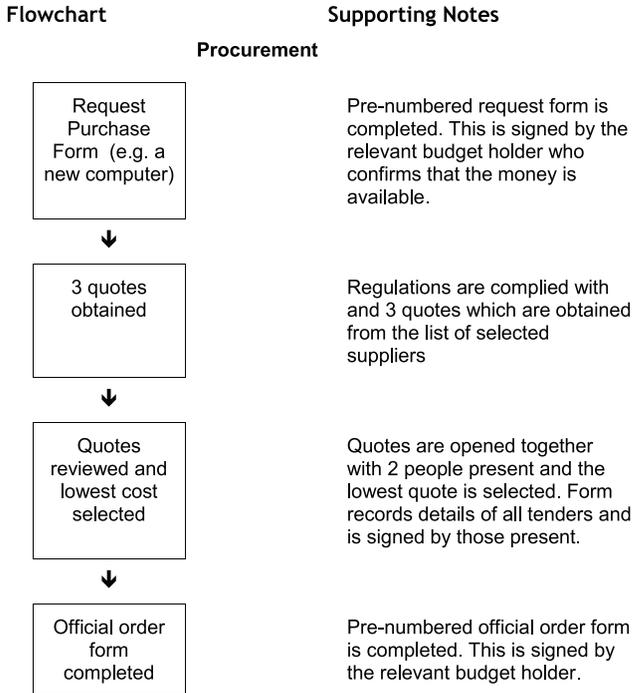
The organisation should have a written set of procedures so that all staff working in that particular account area understands how the process is intended to work.

Internal Auditors are not responsible for designing a system of internal control. The role of Internal Audit is to check how the system established by management is working and to provide assurance to the entity's management that the internal control procedures are effective or else to make recommendations as to how the processes and procedures can be improved.

There are a number of different ways of classifying control procedures but for Audit purposes they can be described broadly as below:

- **Management controls:** They encompass the supervision from high level and review by management. They are generally detective and include for example management review of exception reports, the performance against budgets and the use of professional experts.
- **Organisational controls:** Determined from the way in which the organisation is structured and can be both detective and preventive. Normally they include well-defined responsibilities and the segregation of incompatible functions such as procurement initiation, processing, recording and payment.
- **Authorisation controls:** These normally operate at the individual transaction levels and have a preventive nature. Their purpose is to stop a transaction from being processed if it has not been approved at an appropriate level. Effective authorisation controls are specific about who can approve what, the extent of checking required and how these checks should be evidenced.
- **Operational controls:** Focused on the completeness and accuracy of processing and may be preventive, detective or corrective. They may include: sequence checking to provide assurance on the completeness of numbered documents; comparison of one set of documents to another (example: purchase orders to invoices); and the use of control totals and reconciliations.
- **Physical controls:** Designed to be preventive and include controls over access to access and accounting records through simple physical measures such as passes and safes but also logical controls such as password access to computer files.

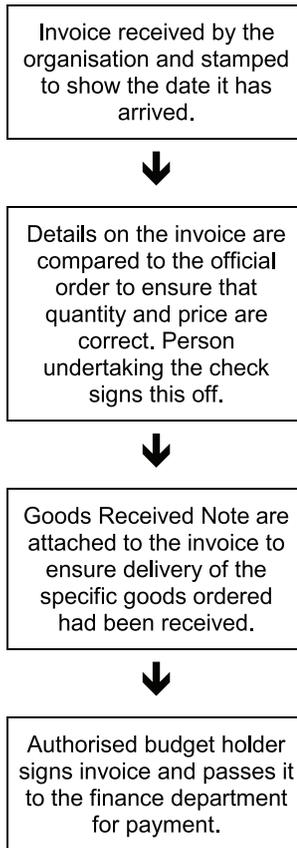
The Auditor should record these controls in the notes that support the flowchart.  
An extract from such a flowchart for making purchases is shown overleaf



It is essential for the systems documentation to record every stage separately that occurs in the process. It is often common for Internal Auditors – or for the organisation staff being Audited – to take shortcuts (avoiding some stages of documentation) or miss out stages in the documentation of an account area.

For example, rather than stating that an invoice is submitted to the finance department for payment, we must think about all of the stages that are involved.

Documentation:



The systems flowchart should therefore include every stage of the process. When a document is completed in duplicate – or even in triplicate – the systems documentation should record what happens to each copy of the form.

### **3.1.6 Step 5: Control of the System Documentation – A Walkthrough Test**

The purpose of a walkthrough test is to ensure that the system documentation is correct.

Financial systems and other processes (such as risk management or setting a budget) are often complex in large entities.

The Audit group therefore needs to ensure that it has correctly understood how the system actually works.

Auditors should perform such step-by-step walkthrough to confirm their understanding and provide some indication of how the controls may operate in practice. Such checks can be particularly useful where controls operate over individual transactions.

This is done by selecting one transaction and tracing it through the system to ensure that the expected processes have been followed. This is known as a walkthrough test.

To realize this, the Auditor needs to identify the starting point for a particular transaction. A certain process may be displayed as follows:

Transaction	Starting Point For Transaction	Calculation
Visiting a restaurant	Customer ordering the meal	52weeks x 5 days x 4 people
Employing a new member of staff	Completing a vacancy request form which is signed by the budget holder to confirm the funds are available. This is approved by the Human Resources department who issue a position number.	
Paying an invoice	A pre-numbered request form is completed. This is signed by the relevant budget holder who confirms that the money is available.	
Paying overtime	Overtime work is approved firstly by the employee's line manager and an authorisation form is completed and signed by both the line manager and the employee concerned.	

Once the starting point has been found, the Auditor should select one transaction and follow it through the whole process. This will ensure that:

- The documentation is correct and that all of the controls that are in place have been recorded in the flowchart; and
- The controls that should be operated are actually applied in practice.

To undertake a walkthrough test, the first thing for the Auditor that needs to do is to pick one transaction for the year in the system/ account area being Audited. This can be selected at random. If for example, you are Auditing payments for goods and services, you should select one invoice that was paid by the organisation during the year.

Once you have selected the transaction you are Auditing, you need to then identify the starting point for that particular transaction. So, in the above example, if you have selected an invoice for the purchase of some office furniture then you will need to locate the official order for that transaction.

You should then follow this transaction right through the process to see what actually happened in the organisation. Effectively you are re-tracing the processing of that transaction.

As an example, when the payments of goods and services are audited, the stages are as follows:

1. Selection of a transaction at random in the year – for example an invoice that the organisation has paid.
2. Identification of the starting point for that transaction. This will be what the organisation did to originally start the process. A lot will have happened before an invoice is sent to the entity and the Auditor needs to go right back to the very start of the process. In the case of a payment for goods and services, this is likely to be the completion of an official order for that transaction. Once the starting point for the transaction has been identified, the Auditor will then need to follow the transaction through the expected process.
3. Look at the official order form and assess what actually happened to it. So, who completed it, which authorised it and what happened next? By undertaking this process right through to the end of the process, the Auditors will be able to get an understanding of the processes that are in place for that particular system/ account area.

### 3.1.7 Step 6: System Effective Evaluation

Once the accuracy of the system recording has been confirmed, the Audit unit should assess how effective the system design is likely to be.

An experienced member of the Audit unit should do this work.

Areas to consider include:

**Supervision** – is there enough involvement of senior managers in the entity? For example, there should be regular management reports and key reconciliations should be independently reviewed. There should also be regular checks by a supervisor to ensure the work has been undertaken properly. For example, a supervisor may review a certain percentage of all payments made each week.

**Segregation of duties** – are key tasks allocated between a number of people, or is one person involved in the whole process? Is there a clear distinction between the roles of the supervisors and those staff undertaking transaction processing?

**Frequency** – do the controls operate often enough? For example, Banking should be done daily and key reconciliations done often and in a timely manner.

**Completeness** – Auditors should evaluate whether the arrangements ensure that all transactions are recorded. Key documents such as official orders and

receipts should be pre-numbered.

**Security** – are passwords used? Is cash held in a safety place? Are important papers such as official orders and receipts kept securely? Are computer systems backed up regularly?

**Regularity** – Are there checks to ensure that the transactions comply with the underlying legislation and the rules and regulations of the organisation?

When reviewing the adequacy of a system/account area, the Auditors should consider what features they would expect to see in place in relation to internal controls. It is the responsibility of the organisation’s management to introduce internal controls in each system/ account area to ensure that these safeguards are actually present.

Examples of the desirable features for a number of systems/ account areas could be as follows:

Payroll	Payments for Goods and Services	Income from Property Rentals
Only genuine employees of the entity are paid.	Goods are bought at the lowest possible price.	The rent is collected on all properties owned by the entity.
All staff is paid at the correct rate.	Only goods ordered by the organisation are actually paid for.	Unpaid rent is chased promptly.
To look if all overtime has actually been worked and was necessarily completed.	Only goods received by the organisation are actually paid for.	Rental income is securely held.

Please note that the above table is for illustrative purposes only. In practice there are likely to be more internal controls and safeguards in place.

When assessing the adequacy of the internal controls within a particular account area, the Auditors should consider the following Audit assertions:

**Occurrence** – how does the organisation ensure that all the transactions and events that have been recorded in its financial systems have actually occurred and relate to the organisation?

**Completeness** – how does the organisation ensure that all transactions and events that should have been recorded have actually been recorded in its financial systems?

**Accuracy** – how does the organisation ensure that amounts and other data relating to recorded transactions and events have been recorded appropriately?

**Cut-off** – how does the organisation ensure that all transactions and events have been recorded in the correct accounting period?

**Classification** – how does the organisation ensure that transactions and events have been recorded in the correct accounts?

**Regularity** – is the expenditure in line with legislative requirements?

Examples of how the assertions can relate to individual account areas are shown in the table below:

Assertion	What does this mean for payroll?	What does this mean for the payments of goods and services?
Occurrence	How does the organisation ensure that only genuine employees are paid?	How does the organisation ensure that payments are only made for goods and services that have been ordered and received?
Completeness	How does the entity ensure that all staff payments are recorded?	How does the entity ensure that all payments for goods and services are recorded?
Accuracy	How does the entity ensure that staff payments are recorded at the correct amount?	How does the entity ensure that all payments for goods and services are recorded at the correct amount?
Cut off	How does the entity ensure that all staff payments made in a particular year 20XX is actually recorded in the correct financial year?	How does the entity ensure that all payments for goods and services made in a particular year are actually recorded in the correct financial year?
Classification	How does the entity ensure that payments to staff are allocated to the right department and are correctly shown as staff costs?	How does the entity ensure that all payments for goods and services are allocated to the right department and are correctly split between IT costs, furniture, and buildings maintenance etc?
Regularity	How does the entity ensure that the payments and allowances made are in accordance with the relevant legislation?	Is procurement legislation complied with? Does the organisation have the legal powers to incur expenditure of this type?

Except the above assertions, Internal Auditors should also assess whether the processes in place for the systems/ account area offer value for money. For example, when reviewed payments for goods and services, is there a requirement to get more than one quote from potential suppliers?

Internal Auditors should also consider the possibilities of fraud or theft within a system/ (account area. Areas to consider are:

- Is cash securely held and banked each day?
- Is there an appropriate segregation of duties – or can one person be involved in an entire transaction from beginning to end?

Examples of the types of internal controls that could be in place in the payroll account area are shown below. However, it should be noted these are only illustrations of the internal controls that could be in place. It is up to the management of the entity to ensure that there are appropriate internal controls in place in each account area.

Expectation of management	Possible internal controls
Only the factual employees of the organisation are paid	<ul style="list-style-type: none"> <li>• Departmental managers sign a list of their employees each month to confirm that they work for the entity.</li> <li>• Salaries are transferred to the employees bank accounts and no cash payments are made</li> <li>• Salaries are transferred to the employees bank accounts and no cash payments are made</li> <li>• A form is completed for each new employee and this is signed by both the Human Resources manager and the departmental manager.</li> <li>• Each employee has their own staff number. This is allocated by the Human Resources department once the individual's personnel file has been created.</li> </ul>

Expectation of management	Possible internal controls
Staff are paid at the correct amount	<ul style="list-style-type: none"> <li>• Departmental managers sign a list of their employees each month to confirm their salaries.</li> <li>• There is an independent check that the salary on the payroll system has been correctly transferred from the new employee form.</li> <li>• The salary reflects the amount included within the legislation.</li> <li>• There is an independent check that all deductions are correct.</li> <li>• All overtime is approved in advance by the departmental manager.</li> <li>• There is an independent check that any additional allowances on the payroll system have been correctly transferred onto the payroll system from the new employee form.</li> </ul>

When the adequacy of the existing internal controls is assessed in place within the account area that is being reviewed, the Internal Auditors should also consider the effective of the IT controls that are in place.

Although IT Auditing is a separate activity that is outside the scope of this manual, there are several assessments that Internal Auditors will be able to undertake as part of the assessment of the adequacy of the account area being reviewed. There is a simple checklist within the Standard Templates section of this manual that may be helpful in assessing the adequacy of the IT controls.

Where deficiencies in the system design have been found, these should be reported to the entity's management and the Auditors should make recommendations on how to improve the system. Where major deficiencies are found, an urgent communication to the management of the organisation may be appropriate. Further information on this is included within section 4 of this manual.

Auditors should also be alert to the fact that there may be duplication (repeated things) or other inefficiencies in the entity's system of internal control and should also report these to the management.

### **3.1.8 Step 7: Preparation of the Audit Programme to Test Whether the Expected Controls Are Operating Effectively**

Having established how the system/ accounting area to be audited should operate, the Internal Audit Unit now needs to undertake detailed work to assess how well the system or accounting area actually operates. As an example, just because something should be authorised doesn't mean that it will actually be authorised.

The size of the samples that need to be audited will depend on both the risk of that system/ area and also the frequency of the controls.

Controls instances might be –agreeing that the total cash collected to the till should send to the bank on a daily basis; checking every month that the correct number of people is being paid etc.

The risk assessment can be determined by looking at the way that risk assessment of the overall control environment and the risk assessment for the systems/ account area that is being reviewed (Standard Template number 7 and8).

The table below shows all the possible combinations of the overall control environment risk assessment and the risk assessment for the account area / system that will be audited.

Assessment of overall control environment (Standard Template 7)	Assessment of system/ area being reviewed (Standard Template 8)	Overall Risk Assessment
High	High	High
High	Medium	High
High	Low	Medium
Medium	High	High
Medium	Medium	Medium
Medium	Low	Medium
Low	High	Medium
Low	Medium	Medium
Low	Low	Low

Auditors have to do their combination of overall control environment risk assessment and risk of the account area within the table and use this to find the overall risk assessment.

The Auditors should apply to the sample sizes suggested in the table below, the risk coefficient according as:

- High risk – Coefficient 1.6
- Medium risk – Coefficient 0-7
- Low risk – Coefficient 0-0

These Coefficients are generally used during the audit. The Internal Auditors during their work will concentrate mostly in higher risk systems/areas and less time work in lower risk systems/areas.

Control Frequency	Recommended Sample No.
More than weekly	15
Weekly	10
Monthly	5
Quarterly	2

Example

The Auditors feel that the overall control environment is operating satisfactorily and have assessed this as being low risk. The account area that is going to be audited is also assessed as being low risk.

The control being tested is the weekly agreement of cash banked to the income per the rent system.

The Auditor first calculates the overall risk assessment using the table in this manual.

Assessment of overall control environment	Assessment of systems area being reviewed	Overall Risk Assessment
Low	Low	Medium

For this example the risk is low and so a coefficient of 0.6 will be used.

The control is undertaken weekly and so the sample size will be 6. Equation is:

$$\text{Recommended samples number (10)} \times \text{Risk Coefficient (0.6)} = 6$$

The testing that will be undertaken should ensure that systems of control are functioning effectively. The Audit method will be based more on auditing systems rather than in checking individual transactions.

The Auditors do this by looking at the existing system controls that they have documented.

In the earlier example regarding purchases, there were a number of controls in place. These Controls are reflected as follows:

System/Area	Control
Authorisation	The request is signed by a person in the organisation, who has the required authority to make such an order. It is likely that there will be different authorisation levels. So that although a person may be able to order stationery, they cannot buy a new building.
Affordability	The authorized person confirms that there is enough budget available.
Compliance with legislation and value for money	The organisation should take into consideration three written quotes from potential suppliers. The lowest one should be chosen.
Authorisation	An official order is completed and sent to the supplier. This must be signed by a person in the entity with the required authority to make such an order.

The Auditor then needs to design tests in order to ensure that these controls are operating effectively.

Examples of these tests that could be undertaken are:

Expected Controls	Audit Test
The request is signed by a person in the organisation with the required authority to make such an order. It is likely that there will be different authorisation levels within an entity, so that although a person may be able to order stationery, they cannot buy a new building.	Using the earlier guidance regarding the frequency of controls and the overall risk assessment, calculate the sample size to be used. Select that number of paid invoices at random. In each case check that the correct documentation has been completed and that it has been signed by an authorised person.
The authorized person confirms that there is enough budgets available.	Using the earlier guidance regarding the frequency of controls and the overall risk assessment, calculate the sample size to be used. Select that number of paid invoices at random from organisation. Check that the authorising employee confirmed that there was sufficient budget available in each case.
The organisation should take into consideration three written quotes from potential suppliers. The lowest one should be chosen.	Using the earlier guidance regarding the frequency of controls and the overall risk assessment, calculate the sample size to be used. Select a number of paid invoices at random and ensure that the procedures regarding quotes were complied with in each case. Confirm that the lowest quote was chosen in each case.
An official order is completed and sent to the supplier. This must be signed by a person in the entity with the required authority to make such an order.	Using the earlier guidance regarding the frequency of controls and the overall risk assessment, calculate the sample size to be used. Select a number of paid invoices at random from the organization and ensure that an official order form was completed for each one. Check that each official order has been signed by an authorised person.

**3.1.9 Audit recording work**

The Audit group should record all of the work that they undertake and should retain sufficient Audit evidence to enable the work to be reviewed and to enable the findings to be discussed with the entity’s management.

An example of how the findings may be recorded is set out overleaf. This format is an example and will need to be modified to reflect the actual single step substantive tests being performed.

Organisation name...

Ref No: .....

Year 20xx

Internal Audit Unit [name]

Test Objective – Ensure compliance with authorization rules. Procedure - Take a sample of 10 contracts and verify that they are signed by the person specified in the organisations’ contracting procedure						W/P Ref
Number	Contract Name	Date	Signed by	Position	Exception	
1	abc	22/7/09	K Cat	Manager		
2	def	24/05/09	D Bray	Manager		
3	xyz	13/04/09	G Bhambra	Manager		
4						
5						
6						
7						
8						
9						
10						

Alternatively, the Internal Audit Unit may consider it to be more efficient to select a sample of transactions and perform a number of Audit tests on these transactions took as a sample.

An example of how the results may be recorded is set out overleaf. This format, which is an example, will need to be modified to reflect the actual tests being performed.

Sample Number	Date	Amount	Details	3 quotes received?	Lowest quote chosen?	Official Order made?	Order correctly signed?
1							
2							
3							
4							
5							
6							
7							
8							

**3.1.10 Errors**

When testing controls Auditors normally plan that they do not expect to find any test failures.

If no failures are found the objective of the test has been met and no further work is required.

If one test failure is found, the original sample should be doubled.

Therefore, if the original sample was e.g. 20 invoices, the Auditor will need to do another 20 invoices.

If no more failures are found the objective of the test has been met and no further work is required. This sample tests procedures can be summarised in the following table.

Number of errors	Action
0	Conclusion is that the controls are operating effectively.
1	Double the original sample size and undertake further testing. If no further errors are found, conclude that the controls are operating effectively but report the one failure to management. If other errors are found, conclude that the controls are not operating effectively and report to management.
More than one failures	Conclude that the controls are not operating effectively and report to management.

When reporting the errors to management, Auditors should:

- Think what the failure means – What could happen because the control did not work? Could it be that fictitious employees are paid by the organization or that money could be stolen?
- Consider what caused the error to happen and how could the organization avoid a repetition?
- Think about the money involved. If staff bonuses were incorrectly calculated, how much did this mistake cost to the organization?

There is more information on reporting in the chapter 4 of the manual.

### Possible Tests for Payroll

These tests are included as an example. The actual work undertaken should depend on the design of the account area in the entity being Audited.

Test Number	Suggested Test
1	Select a number of employees and ensure the basic salary is correct.
2	Select a number of transactions and repeat the calculations to ensure that tax and other deductions are correctly calculated.
3	Select a number of new employees and ensure that the format have been properly authorised.
4	Select a number of employees leaving the entity and ensure that the formats have been properly authorised.
5	Check that the payments to the employee's bank accounts have been properly authorised.
6	Check if payments to the Government for tax and other deductions are correctly made and submitted in time.
7	Check if any other deductions (such as fines and telephone costs) are correctly deducted
8	Check that the payments made agree to those in the main accounting system (general ledger) and that these are regularly reconciled.
9	Check that the payroll system is regularly backed up.
10	Review the check that all people being paid are genuine employees of the entity.

### Possible Tests for Payments Made for Goods and Services

These tests are included as an example. The actual work undertaken should depend on the design of the account area in the entity being audited.

Test Number	Suggested Test
1	Select a number of payments made by the entity and ensure that there is an official order form that has been properly completed.
2	Select a number of payments made by the entity and ensure that there is a supporting invoice that is addressed to the entity.
3	Select a number of payments made by the entity and ensure that there has been a check that the goods or services have been received by the entity
4	Select a number of payments made by the entity and ensure that the invoice has been approved by a suitably authorised person.
5	Select a number of payments made by the entity and ensure that the invoices have been stamped 'paid' so as to avoid the possibility of a duplicate payment being made.
6	Select a number of payments made by the entity and ensure that the appropriate number of quotes were obtained by the entity.
7	Review the reconciliation between the payments for goods and services system and the entity's main accounting system.
8	Ensure that the account area covering payments for goods and services is regularly backed up.
9	Select a number of payments made by the entity and ensure that the expenditure has been allocated to the correct ledger code.
10	Review the budgetary control processes in place at the entity and assess how effective these are in managing the expenditure at the entity.

### Possible Tests for Income

These tests are included as an example. The actual work undertaken should depend on the design of the account area in the entity being Audited.

Test Number	
1	Review a number of receipts (i.e. income received) and ensure that this has been correctly classified on the organisation's main accounting system.
2	Check that there is adequate segregation of duties between the people responsible for sending out invoices and those responsible for collecting the money.
3	Ensure that a receipt is issued for all income received by the organisation.
4	Check that there is reconciliation between the number of properties owned by the organisation and the number of invoices that have been issued.
5	Ensure that cash is securely held at the organisation.
6	Ensure that cash is banked on a daily basis.
7	Ensure that all invoices and receipts are individually numbered.
8	Select a number of invoices and check that the correct rental has been charged for each property.
9	Check that there is a daily reconciliation between the income system and the amount of cash that has been collected.
10	Check that there is the production of an aged debtors listing and that money due to the organisation is chased promptly.

### 3.1.11 Step 8 Undertake Audit Testing

After having planned the Internal Audit testing, the next stage is for the work to be completed.

Guidance for doing this is included in step 7, above, on sample selection and recording the testing that was done.

All working papers should be individually numbered and cross referenced where appropriate.

### 3.1.12 Step 9: Ensure Audit Work Is Reviewed

Quality Assurance is essential, as through review should be assured if the Internal Audit work has been done according to the higher Standard.

Chapter IV of this manual covers the Quality Assurance processes. This process should be followed for each Internal Audit assignment. Quality Assurance can involve both the direct review of Internal Audit work by a more experienced member of staff as well as the attendance at important meetings with the management of the entity by a more experienced member of staff.

There is no 'one size fits all' approach to Quality Assurance. Although the following factors should always be considered:

- The risk of the organisation being reviewed, based on the assessment of the overall control environment;
- The risk of the area being reviewed, based on the account area risk assessment;
- The experience of the Internal Audit Unit;
- Any others issues, e.g. difficult client relationships, political sensitivity etc.

Whilst this section will not duplicate the contents of chapter 4 of this Manual, it is important to note that the Audit work for each assignment should be reviewed at the following stages by the senior member of the Internal Audit team:

- After the completion of the risk assessment for the system, subsystem or account area being reviewed and the overall risk assessment (high / medium / low) for that system, subsystem or account area.
- Once the scope of the Internal Audit review has been determined, a senior member of the Internal Audit Unit should attend the set up meeting with the management of the organisation being reviewed.
- After the production of the Internal Audit programme.
- Once the detailed Internal Audit testing has been completed.
- Once the draft report has been produced. A senior member of the Internal Audit Unit should attend the meeting with the management of the organisation being reviewed to discuss the draft report.

- Once the action plan has been completed and the Internal Audit report is about to be finalised, the action plan is the organisation's response to the recommendations made by the Internal Auditors – what will be done, who is responsible and when will they do it?

### **3.1.13 Step 10: Produce Draft Audit Report and Report findings to the management of the organisation**

Reporting the findings of your work to the management of the organisation is an important part of the Internal Audit process. Through reporting, management is informed over audit findings and about recommendations to improve things in the future.

As soon as the fieldwork has been completed, the Internal Auditors who undertook the fieldwork should produce a draft Audit report.

The Internal Auditors should agree the factual accuracy of their findings with staff from the organisation as and when the actual fieldwork is completed.

Further details on reporting are included within section 4 of this Internal Audit manual.

The draft report should be subject to review by a more senior member of the Internal Audit Unit (usually the team leader) as well as the head of sector or any other person acting in the same capacity before it is sent to the organisation.

### **3.1.14. Step 11: Agree Report and Complete Action Plan**

The final stage of the execution stage is to agree the report with the organisation and to get the action plan completed. This action plan will establish the basis of every work in order to follow the procedures in the future.

Within the Internal Audit report there are likely to be a number of recommendations. The action plan sets out:

- What will be done related to recommendations;
- Who will be responsible for implementing the recommendation; and
- When the work of recommendations will be done.

There is an example of action plan in section IV of this manual – ( Standard Template 13).

The person or group of people with whom the report will be agreed should be discussed at the original set up meeting – (see stage 3 of the Audit flowchart).

The completed action plan will form the basis of any future follow up work in this area.

As the Internal Auditors should agree the factual accuracy of their findings with staff from the organisation as and when the actual fieldwork is completed, it

is not expected that there would be many differences between the draft report and the final report.

Further information on reporting and agreeing action plans is included within chapter IV of this manual.

As part of the initial set up meeting, the timescales for reporting should be agreed. Normally the draft report should be sent to the organisation within 2 weeks of completing the Internal Audit fieldwork.

The auditors should then aim to agree the draft report with the management of the organisation – including the action plan – as well to finalise the report within 2 weeks after sending the draft report to the organisation.

### 3.2 Follow up Work

Introduction

***IIA Standards 2500 details follow up procedures. To ensure that International Standards have been complied with, the Audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.***

An important role of an Internal Audit Unit is in ensuring that previous recommendations have actually been implemented by the entity.

Internal Auditors assess the adequacy, effectiveness and timeliness of the actions undertaken by management to address each Audit's recommendations.

This is known as 'follow-up work' and can either be done as part of the Audit work for the following year where this is included in the strategic Internal Audit plan or as a separate exercise if no work in that account area has been planned.

Follow up work is very important because unless the management of the entity implement the agreed recommendations in an effective way, the operation of the entity will not improve.

#### 3.2.1 Undertaking Audit Recommendation Work

The starting point for undertaking the follow up work is the completed action plan from the previous Internal Audit report. An example of a completed action plan has been included at Standard Template 13 within chapter IV of this Internal Audit manual.

The agreement of an action plan is the management's commitment to implement all of the recommendations that were made by the Internal Audit Unit.

Follow up work is simply ensuring that the organisation's management have completed the work that they agreed to do when the original action plan was agreed.

Although all of the recommendations within the original Internal Audit report are important, some may be more significant than others. We therefore allocate a rating to each recommendation importance level and the three criteria that should be used are as follows:

- **Major** – This applies to a significant control weakness and is a matter that should be for urgent attention of senior management
- **Intermediate** – This applies to an important control weakness. Whilst it should be dealt with as a matter of urgency, but in fact it is not necessarily something that should be dealt with by the top management of the organisation.
- **Minor** – This applies where insignificant (not important) control weaknesses have been identified. The changes should be implemented in due course, but will not necessarily be a priority for the organisation to deal with.

Internal Auditors will devote more time to major recommendations than minor recommendations

The extent of the Audit follow up work depends on the:

- Risk of an adverse event occurring if remedial measures aren't taken;
- Importance of the weaknesses discovered;
- Extent of risk to achievement of the organisational objectives;
- Cost and effort associated with improving the Audited process;
- Scope of remedial action for all organisational units; and
- Timeframe for implementing changes.

Effective Audit follow-up procedures include:

- Evaluating and verifying management responses; and
- Ensuring the appropriate management authority is aware of unsatisfactory responses or the organisation's acceptance of risks.

It is important to note the fact that it is the responsibility of the organisation's management to ensure that all agreed recommendations are actually implemented. However, the Audit Unit Leader may write a reminder letter to the organisation management perhaps a week before expiry of the deadline for implementing each recommendation.

Some recommendations may be easy for an organisation to implement (for

example stamping invoices as paid) whereas others may take much longer time(for example the redesign of a particular system).

Where there is a long implementation time, the Internal Audit Unit should assess the progress being made by the organisation rather than simply waiting until the previously agreed deadline has been reached.

The completed action plan at Standard Template 13 within chapter IV of this Internal Audit manual contains two recommendations as follows:

Number	Recommendation	Ranking
1	The organisation should ensure that all line managers confirm the attendance of their staff on a monthly basis.	Intermediate
2	The organisation should introduce a check to ensure that all staff salaries are in accordance with the legislation.	Major

The follow up work that will be undertaken for these two recommendations could be as follows:

### **Recommendation 1 (Intermediate)**

Enquire of the management what they have done regarding this recommendation.

The Internal Auditors should select a number of departments and check whether the line managers are actually confirming the attendance of their staff each month. The tests should be for a number of departments across a number of months.

The Internal Auditors should also review the procedures notes for this account area and check whether the guidance to staff operating the internal controls has been updated to reflect the changes that have been made.

### **Recommendation 2 (Major)**

The significance of this recommendation means that the Internal Auditors will want to do more work to have confidence that the organisation's management have introduced the agreed changes.

Internal Auditors will need to ensure that any changes are a permanent feature of the way the internal controls are implemented rather than being a short-term change that may not continue.

The starting point will again be to ask the management of the organisation what they have done regarding this recommendation.

The Internal Auditors will want to check that the approach has been followed throughout the organisation and will therefore want to do more testing to be satisfied that this is the case.

The Internal Auditors will again want to review the procedures notes for this system/ account area and check whether the guidance to staff operating the internal controls has been updated to reflect the changes that have been made. As this is a major recommendation you should assess whether there has been training to the relevant staff and how the new requirement has been communicated within the organisation.

### **3.2.2. Reporting Follow Up Work To The Organisation**

The strategic Internal Audit Plan sets out the areas that will be looked at over the next five years. Some account area may account for a significant part of the income or expenditure for an organisation and may therefore be looked at each year.

If this is the case, the Internal Auditors should include the progress on the implementation of the previously agreed recommendations in the Internal Audit report for that account area.

Where there is not to be a full Internal Audit review in the following year, the Internal Auditors should provide a brief report to the management of the organisation setting out what progress has been made on implementing the previously agreed recommendations.

### **3.2.3. Encouraging Organisations to execute the Internal Audit Recommendations**

A well-run organisation will want to have arrangements in place to ensure that every recommendation made by the Internal Audit Unit has been properly implemented.

The Internal Audit Unit should encourage organisations to appoint a senior employee to keep a record of all Internal Audit recommendations and to monitor the progress that has been made regarding their implementation. This will help to ensure that improving internal controls is the responsibility of the organisation's management rather than being a role of the Internal Audit Unit.

**Templates  
for**  
**Chapter III**

Standard Template 8: Account Area Risk Assessment

Control Issue	Yes	No	Comments
1. General Questions			
1.1 Have there been previous significant problems with the area being Audited at this organisation?			
1.2 Have the procedures for the account area changed since it was last Audited?			
1.3 Have there been any significant personnel changes in this account area at the entity being Audited?			
1.4 Does the area being reviewed require the use of any judgement, for example interpreting legislation?			
1.5 Does the area being reviewed deal with lots of small transactions?			
1.6 Does the area being reviewed deal with a small number of large transactions?			
1.7 Does the system involve cash income or payments in cash or other assets such as stock? These will be particularly vulnerable to theft.			
1.8 Is the area being reviewed complex?			
1.9 Does the area being reviewed involve any information from third parties?			

Standard Template 8 continued: Account Area Risk Assessment

Control Issue	Yes	No	Comments
<b>2. Management controls in Audited area</b>			
2.1 Does management periodically (at least quarterly) review reports to identify potential problems or errors? These are not just Internal Audit reports, but also budgetary control reports, exception reports, and general management information report.			
2.2 Is management able to use the above reports to spot problems or errors?			
2.3. Does management get timely information on the causes of problems it detects?			
2.4. Does management initiate corrective actions related to problems?			
2.5 Does management check the successful implementation of corrective actions?			
2.6 Does management act quickly to address Audit findings (except those above mentioned)?			
<b>3. Risk assessment in area being Audited</b>			
3.1. Based on the overall internal control environment for this organisation, is risk management at this organisation considered to be effective?			
3.2 If yes, is risk management considered effective in the account area being reviewed?			

Template 8 continued: Account Area Risk Assessment

	Yes	No	Comments
<b>4. Information and communication for Audited area</b>			
4.1 Does the organisation have the information it needs at the right time in this account area?			
4.2 Are information requirements and deadlines clearly set out? This should cover what is required, when it is needed and in what format the information should be provided?			
4.3 Are the information systems adequate, both internally and externally?			
Overall risk assessment:    High / Medium / Low			

Prepared by: .....

Date: .....

Reviewed by: .....

Date: .....

Instructions for the Completion of Standard Template 8:

This Standard template helps the Audit units to understand the risks in the area being audited and needs to be completed once for each account area being reviewed.

The risk assessment for the account area is combined with that for the overall control environment to arrive at an overall risk assessment for the area being reviewed.

Auditors need to answer all of the questions and to consider all of the answers before concluding whether the area is high risk, medium risk or low risk. This is not a case of counting the answers but forming an overall judgement. One or two major problems could make an area high risk overall.

The risk assessment (high, medium or low) determines how much work is needed in each account area. The higher is the risk, the more work needs to be done.

The guidance below may help with the overall risk assessment.

Suggests High Risk	Suggests Low Risk
Previous problems	No previous problems
Procedure changes in the account area	No procedure changes in the account area
Personnel changes in the account area	No personnel changes in the account area
Significant use of judgement or estimates	No use of judgement or estimates
Small number of large transactions	Large number of small transactions
Vulnerable assets	No vulnerable assets
Complex area	Simple area
Third parties involved	No third parties involved
Little management supervision	Regular management reviews
Ineffective management	Prompt and effective management action
Objectives not set or not monitored	Objectives set and monitored
Poor risk management	Good risk management
Untrained staff with poor communication	Knowledgeable staff with good communication

The Auditors should answer ‘Yes’ or ‘No’ for each question and should not answer ‘possibly’, ‘maybe’ or “sometimes”.

To help with the overall risk assessment work, the answers which are low risk have been shaded grey and the answers which are high risk are blank.

The Auditors should write comments to support their answer and should also obtain sufficient evidence to support their answer. This will enable the account area risk assessment to be reviewed by a more senior person as part of the Quality Assurance process outlined in chapter 4.

## Standard Template 9: The Initial Meeting with the Organisation

Draft - Agenda

Audit name:

Year 20..

Internal Audit Unit [name]

Draft Agenda for Initial Meeting

- Introduction of the Audit Unit Group and identification of the contacts: name, telephone number and e-mail address.
- Outline Audit objectives and scope.
- Provide an overview of the Audit process and the accounting period that will be covered by the review.
- Discuss how the Audit unit will communicate with the Auditee staff and management.
- Indicate what information will be required by the Audit unit.
- Agree what else will be needed by the Internal Audit Unit – for example IT access, other accommodation etc
- Confirm the Audit start and end dates of the Internal Audit work.
- Schedule next meeting.
- Any other items

The draft agenda for the meeting is intended to serve as a reminder of the areas that will need to be covered during the meeting and should therefore not be too detailed.

It is helpful to send a copy of the draft agenda to the organisation's staff that will be attending the meeting.

Standard Template 10- Budget and Timescales for Audit Assignments

Task	Auditor	Start Date	Finish Date	Budget (Hours)	Actual Time (Hours)
Complete the risk assessment format for the area being Audited					
Calculate the risk coefficient for the system/area that is going to be reviewed					
Determine the scope of the work					
Meet with the organisation staff to agree the timing and scope of the work					
Document the system					
Check the system documentation using a walkthrough test					
Consider the effectiveness of the system					
Determine the Audit tests to be undertaken					
Complete Audit testing					
Prepare draft Audit report					
Discuss findings with the management of the organisation					
Complete the action plan and finalise the Audit report					

Standard Template 11: Allocation of Individual Internal Audit Tests

Internal Audit Test	Auditor	Start Date	Finish Date	Budget (Hours)	Actual Time (Hours)
Select a number of employees and ensure the basic salary is correct.					
Select a number of transactions and repeat the calculations to ensure that tax and other deductions are correctly calculated.					
Select a number of new employees and ensure that the forms have been properly authorised.					
Select a number of employees that have left the organisation and ensure that the forms have been properly authorised.					
Check that the payments to the employee's bank accounts have been properly authorised.					
Check if payments to the Government for tax and other deductions are correctly made and submitted in time.					
Check that any other deductions (such as fines and telephone costs) are correctly deducted					
Check if the payments made agree to those in the main accounting system (general ledger) and that these are regularly reconciled.					
Check that the payroll system is regularly backed up.					
Review the check that all people being paid are genuine employees of the organisation.					

### 3.3 Instructions for Completing Standard Template 11

Once the controls in place in the system/account area have been identified, the detailed Internal Audit work can then be planned.

All of the controls that need to be completed should be set out in Standard Template 11.

An example has been included for payroll and this will enable the detailed Internal Audit testing to be allocated between the various members of the unit.

#### Standard Template 12- IT Assessments

Control Issue	Yes	No	Comments
Is access to the system and individual PCs controlled by the use of passwords?			
Are passwords required to be changed on a regular basis?			
Is access to the IT system restricted to that staff that needs to use the system?			
Is access to the IT system appropriate to the needs of the user? For example, a supervisor would need greater access than someone inputting data onto the system.			
Does the system record all users?			
Are there arrangements to remove users who no longer need access to the system, perhaps because they change jobs or leave the organisation?			
Is the server in a safe location?			
Is the system backed up on a daily basis?			
Are the back-ups stored securely and away from the main computer so that a fire or flood would not destroy everything?			
Does the organisation have an up to date disaster recovery plan that sets out how it would deal with a major IT problem?			
Has the organisation checked that its disaster recovery plan works?			

# Chapter IV

## Reporting and Quality Assurance

# Reporting and Communication of Audit Reporting

## Introduction

This chapter aims to help auditors to make reports and other forms of Audit communication more effectively, both in terms of content and presentation. This chapter sets out the recommended format for Audit reports and provides guidance on good practice for effective Audit reporting, which will help auditors to prepare the report right since first time. This will enable the auditors to save time and effort, as well as that of report editors and reviewers.

The key outputs of an Audit are the different types of report that are produced. Effective communication is very important if your Audit work aims to have a positive impact and add value to the organisation.

All readers of your reports need to understand what you have written and be clear what they, or others, may need to do as a result.

Reports are your 'shop window', enabling you to demonstrate the quality of your work, make an impact, secure beneficial change and foster a good relationship with the organisation being Audited.

The best planned and performed Audit procedures or comprehensive working papers do not count for much if, at the end of the process, you produce a poor report. So, it is worth investing time in getting your reports right.

At the end of any Audit assignment, the Auditors should report the findings of their work to the management of the entity within the agreed timescales.

***The principle of reporting all Audit findings applies irrespective of what the Auditors actually found.***

If no problems were identified, the Auditor is providing assurance to the management that the controls are operating effectively.

If problems are identified, the Auditor should make helpful recommendations to improve the structure, processes and procedures at the organisation as appropriate.

## 4.1 Communication of Auditors

International Internal Audit Standards require that Auditor communications to be accurate, objective, clear, concise, constructive, complete, and timely (IIA 2420). Good communications are an essential feature of a well organised Audit. They assist Audit efficiency and effectiveness and aid the Audited organisations understanding of the Audit process which can contribute to achieving beneficial enhancement to risk and control management.

Internal Auditor communication should be:

### 1) Accurate:

- Supported by sufficient Audit evidence;

### 2) Objective:

- Relevant Communication and in perspective;
- Reports should be unbiased, and free of distortion.

Highlighting very minor matters can be a form of inaccuracy as it could give the impression that there are a lot of problems with the entity whereas this may not necessarily be the case.

### 3) Clear:

- Follow a logical trail from evidence to the conclusions;
- Include cross references to other relevant documents;
- Avoid technical terms and jargon without clear explanation;
- Provide adequate background for complex problems;
- Clarify complex matters by charts, graphs, or other visual aids;
- Avoid long sentences which impede clarity.

The Auditors must fully understand the Audit evidence supporting their conclusions so that they can report their findings in a clear manner and be able to defend these findings in the event of a rejection from the organisation's management.

### 4) Concise:

- Conciseness does not necessarily mean brevity;

When considerable information must be reported, the internal Auditor should provide an executive summary of key points.

### 5) Timely:

- Sufficiently timely to obtain prompt corrective action;
- For significant findings or risks, Auditors may use informal discussion or interim communications to expedite management consideration and action;
- The final communication should meet professional standards which may take time to prepare and review, but should include all significant findings and any management action taken prior to the report.
- Final reports should be provided while they remain relevant to assessment of the management control environment.

### 6) Constructive:

- Have an appropriate, professional tone.
- Avoid naming individuals or highlighting their mistakes;
- Consider the significance of the matters addressed and avoid minor matters.

The communication should assist enhanced management controls of relevance to the recipient. Senior management generally consider and address corporate issues - general concepts of significance to the organisation as a whole, and divisional managers address specific operational controls.

In addition to the above comments, the following guidelines can assist simple, clear writing styles:

- Avoid sentences that are too long to readily understand;
- Use short paragraphs and numerous headings and brief descriptive titles;
- Use bullet points, numbered lists and clearly defined references where appropriate;
- Maintain a logical presentation, avoiding irrelevant matters;
- Use consistent sentence structure, and vocabulary;
- Avoid ambiguity from the use of pronouns with unclear antecedents or careless word ordering;
- Avoid jargon and technical language (or scholarly knowledge) which may not be familiar to the reader - where absolutely necessary for understanding they should be simply and briefly explained;
- Use active tense rather than passive for sentences (e.g. the manager approved the payment rather than the payment was approved by the manager).

### 4.2 Structure of Internal Audit Reports

The purpose of all Internal Audit reports is the same, they are used:

- To inform the management of the entity what work has been undertaken and the reason for this;
- To report the findings and the conclusions from the work to the organisation; and
- To make constructive recommendations to help the organisation improve its operations.

When writing any report, the key thing is to think about your Audience in advance – who is report aimed at and what level of information and detail will they require?

Internal Audit reports should all follow the same format, as follows:

***Executive summary***

Not all users/readers of Internal Audit reports will have either the time or the need to read the whole Internal Audit report. An executive summary contains a very brief introduction to the report (one or two paragraphs) explaining what was done and why it was done. The executive summary should also include the overall conclusion of the report and its main recommendations.

***Introduction***

The introduction should set out the background of the Audit, what was done and why it was done. The auditors should try not to include too much information here and avoid including information the reader would already know.

***Audit Approach***

How did you go about your work? What period did the Audit work cover? Did the auditors interviewed people? Did they read key documents? What sampling methodology is used? It is important to be very clear what work you have done so that the reader knows what assurance they can place on it.

***Findings and Conclusions***

What did the auditors find as a result of their work? Try to put this into sections so that the reader can easily follow your report. For example, you might have one section on budget setting, another on budgetary control and another on medium term financial planning. Always include the key findings first. Try to think about what caused the problem to occur – was it a lack of training, poor segregation, lack of internal controls etc.

***Action Plan***

All recommendations should be summarised in an action plan. The management should respond to all recommendations made. See later in this chapter for further information on the completion of action plans.

### 4.3. Reporting Findings and Conclusions

Auditors should be very clear when reporting their findings. Don't say 'we found a number of problems within payroll', but instead say, what you did and what we found. For example, the auditors may express 'we audited 20 overtime payments and found that none of these had been authorised by the appropriate line manager.'

Where possible, include the amounts involved, as readers of Internal Audit reports will often ask 'so what' when looking at what the Auditors have found. Sometimes it may be possible to extrapolate errors across the whole population to give readers a better idea of the extent of the problem.

The example below is very clear about the problems found and the potential impact within the organisation being audited:

'We Audited 20 monthly timesheets and found that four contained arithmetical errors resulting in an overpayment of 14,000 leke. If this level of error occurred throughout the year, there could be a total overpayment of approximately 1.68 000 million leke (12x 14 000)\*'

### 4.4. Reporting Recommendations

Internal Auditors should always summarise their findings and conclusions in a clear and concise manner and should cross reference these to the relevant section of the report.

When in special cases the findings of the group are important and show a high level of abuse for the organisation being audited, an advanced report is prepared which is delivered to the Internal audit Unit Director in order to put into action the Financial Inspection Structures.

Recommendations should be specific, relevant, and time-related and which are directed clearly at an individual, unit or department for remedial action. It is important that you are clear on what you would expect any organisation to do in order to address the weakness you have found.

Imagine you were looking at the system/ account area for payroll and you found that overtime payments were incorrectly made. Don't write that: "The organisation should not make incorrect overtime payments in the future" as this is stating the obvious and is not helping the management of the organisation, but to think what the problem was, what caused it and how this can be avoided in the future".

The following recommendations are much better:

### Recommendations

- The organisation should update its procedures manual regarding the payment of overtime.
- All staff should receive a briefing on the process of working and claiming overtime. All overtime should be requested in advance using the 'overtime approval form" which should be signed by the employee's line manager.
- Overtime payments should not be made unless a properly completed 'overtime approvals form' is submitted to the payroll department.

In order to make the Internal Audit reporting more effective, a system of ranking for the recommendations should be used. The three criteria that should be used are as follows:

- **Major** – This applies to a significant control weakness and is a matter that should be for urgent attention of senior management
- **Intermediate** – This applies to an important control weakness. Whilst it should be dealt with as a matter of urgency, it is not necessarily something that should be dealt with by the top management of the organisation.
- **Minor** – This applies where insignificant system control weaknesses have been identified. The changes should be implemented in due course, but will not necessarily be a priority for the organisation to deal with.

All Internal Audit recommendations should be included within an action plan. This is a summary of all of the recommendations made in the report with the response from the entity's management.

An example action plan is given below is given below, although for ease of reading, a landscape Format may be more appropriate. A completed example is included within the templates section – (see Standard Template 13).

Recommendation number	Recommendation	Level Ranking	Paragraph Reference in report	Management response	Target Date

The Internal Auditors should pay close attention to the both the management response and the target date for implementing the agreed recommendation as follows:

- **Management response** – has the organisation acknowledged the seriousness of the Internal Auditor’s findings? Will the planned action address the problem that was identified? Does the organisation have the resources or capacity to implement the agreed recommendation in the way the management have suggested? How confident are you that the management will become permanent and that the organisation will not revert to its old way of working over time payment (refer to the previous example)?
- **Target date** – does the timescale appear reasonable for the recommendation to be implemented? If the time period is too far into the future, it may be that the management have no intention of implementing it. If the timescale is too short, it may suggest that it will not possible for the management to take the necessary remedial action.

All recommendations should be:

- Specific about what action the organisation needs to take;
- Useful, practicable and based on an assessment of the benefits to the entity for implementing them; and
- Take into account even the costs of implementation. If the cost of implementation is considerable, then report this.

### 4.5 Draft Reports and Final Reports

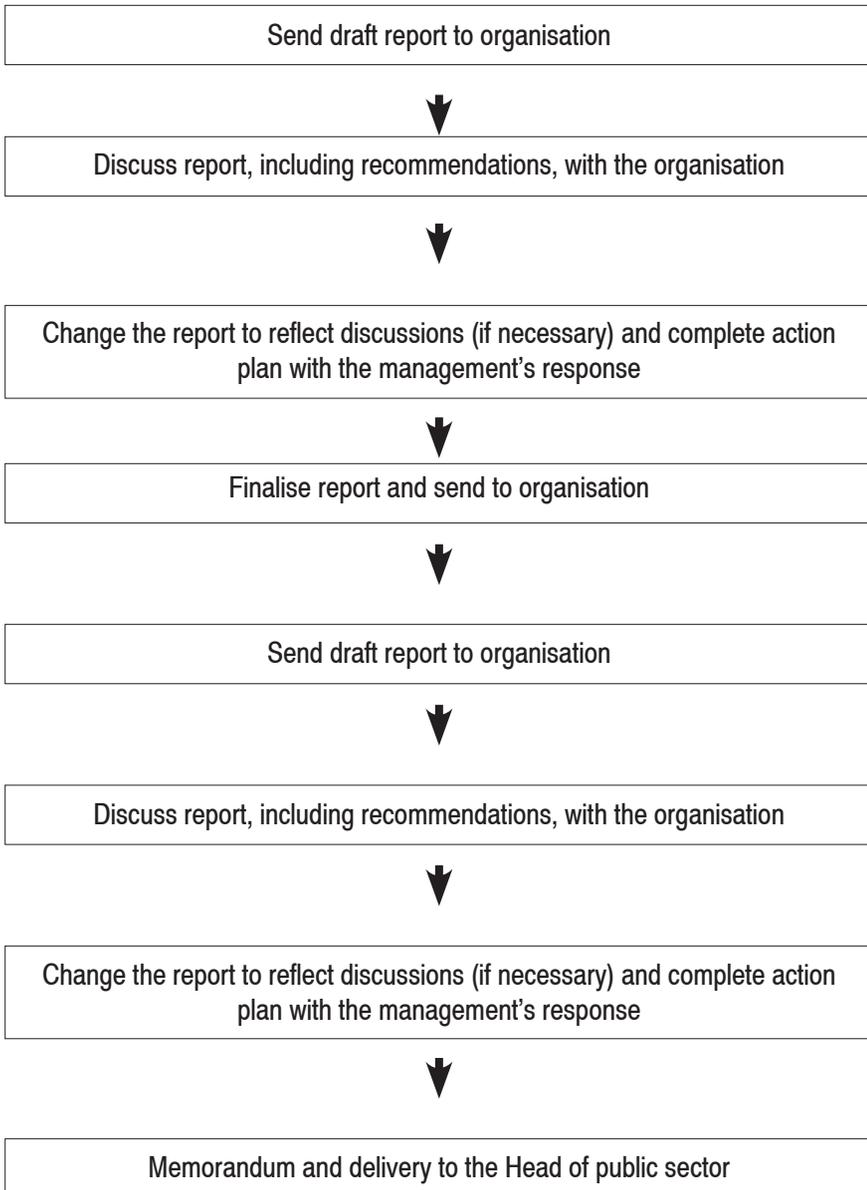
The first report that is sent to the organisation is known as the draft report. This report will be accompanied by a formal request for the management in which it is required to the organisation to react related to the draft recommendations within the report. By the time the draft report has been issued, the Internal Audit work and the report itself will have been subject to the required internal reviews and quality assurance. This is important because it is not possible for the Internal Auditors to ‘ask for the draft report back’ if subsequent quality assurance procedures reveal that the original report was incorrect.

After the draft report has been sent to the organisation (if requested by parties concerned) , the Internal Auditors will then meet with the management of the organisation to agree the contents of the report and to complete the action plan setting out the organisation’s response to the Internal Audit recommendations.

The factual accuracy of the Internal Audit work should be agreed with the organisation as the Internal Audit work is undertaken. This will ensure that any misunderstandings are avoided and will ensure that the draft report does not

come as a surprise to the management of the entity.

Once the action plan has been agreed, this should be added to the back of the report before being formally submitted to the senior management of the organisation as a final report, with copies to the head of the account area that has been reviewed.



As part of the initial set up meeting, the timescales for reporting should be agreed. Normally with draft report should be sent to the organisation within 2 weeks of completing the Internal Audit fieldwork.

The auditors should then aim to agree the draft report with the management of the organisation – including the action – and finalise the report within 2 weeks of sending the draft report to the organisation.

### 4.6 Memorandum

The Audit group, after the delivery of the Final Report to the audited organisation, prepares a short summary report which is concise and keeps the report structure. This summary is called memorandum.

Memorandum is a summary of the finalized report, which is compiled on purpose in order to inform the Head of Public sector. Memorandum is compiled from the audit work group and should be: clear, concise, not so detailed (synthetic), able for conclusions.

A copy of the document it is sent attached with the final report to the CHU/IA (ref. 8.14)

### 4.7 Periodic Report and Annual Report of IA

At the completion of each assignment, the Internal Auditors will issue a report to the management of that audited organisation. The report is based on the work that they have undertaken.

In addition to the individual assignment reports, the Internal Audit Unit should also submit to the institution an Annual and Periodic Report which summarises the Internal Audit activities in the year.

The Annual Report should indicate the number and type of Internal Audit assignments carried out in the year, the recommendations made as a result of that work and the action taken by the management of the organisation on those recommendations.

After the consent of the Head Institution the Periodic and Annual Reports, prepared by the IA units, are sent to the IA unit in Ministry ore proper central institution.

They both prepare a summary report at a high Level (ministry or central institution), which include the periodic and annual report of IA unit as well of other dependent institution.

This summary report for all Ministry and Central Institution Management is submitted officially and in electronic format to the CHU/IA not longer then 15 days of the final report period.

Especially, after the head approval, the periodic and annual report of the Audit Unit of local government ( municipality, commune, council of districts. etc),is submitted to the CHU/IA not longer than 15 days of final report period. CHU/

IA prepares a Consolidated periodic and annual report for all the IA activity in the public sector and submit it to Internal Audit Committee within 45 days from final report period.

The Consolidated Report is submitted to the Finance Minister, after it is assessed from IAC (Internal Audit Committee), who then submit it to the Council of Ministers according to the legal definitions.

Reporting forms are defined by special guidance from CHU/IA.

### 4.8 Quality Work Assurance

#### Introduction

Quality Assurance is the expression that is used to describe the processes that are undertaken in order to ensure that all Internal Audit assignments meet the expected Standards and are helpful to the entity being Audited.

This Internal Audit manual contains an Audit methodology that is based on internal audit law, International Auditing Standards. Quality Assurance is part of the process that ensures that this manual is complied with.

Quality Assurance can be obtained in three main ways:

- On ongoing process of supervision and review throughout the course of each Internal Audit assignment. This process is performed by work group which realise the assignment
- A detailed Quality Control review which can be undertaken within the Internal Audit Unit internally for each assignment, (usually this process is done by an experienced member of the unit, which usually is the head of unit, the head of sector or any other person acting in their capacity; or
- A detailed Quality Control review which can be undertaken by a third party that is external to the Internal Audit Unit. Such a process is undertaken by the Central Harmonisation Unit for Internal Auditing.

Issues identified as part of the overall Quality Assurance processes should be reviewed to see whether there is a need to:

- Update or clarify the contents of this Internal Audit manual;
- Develop training programmes for the Internal Auditors as a whole; or
- Coach individual members of the Audit unit on certain aspects of their work.

### 4.8.1 Support and Review

There should be an ongoing process of support and review throughout the course of all Internal Audit assignments. The extent to which this should be applied will depend on a number of factors, including:

- The experience of the member(s) of staff undertaking the work;
- The complexity of the organisation; and
- The complexity and sensitivity of the system/area being reviewed.

As a minimum, the following should be applied:

- The initial planning work should be reviewed and the Audit approach should be agreed before any detailed work is undertaken;
- The Internal Audit working papers and draft report should be reviewed before these are sent to the top directors of the organisation. The person reviewing the Audit work should be a senior and experienced member of the Internal Audit Unit. As such, this person has the right to amend the draft -report or the final report as they see fit.
- Reasons for such amendments to the draft report could include:
  1. Improving the grammar in the report; or
  2. Changing the order of the findings or the emphasis of the findings; or
  3. Improving the recommendations to make them more relevant to the organisation.

The arrangements in place for maintaining the independence of the Internal Audit Unit apply to those staff undertaking Quality Assurance as well as staff undertaking the initial planning and detailed fieldwork.

The Director of the IAU is responsible for assuring that internal Audit assignments are properly supervised:

- Ensuring that the Auditors assigned possess the requisite knowledge, skills, and other competencies to perform the assignment during planning; when mobilizing the unit and through coaching and review during Audit execution;
- Providing appropriate support during the planning of the assignment; approving the Audit Plan; and ensuring that the approved Audit Plan is carried out unless changes are justified and authorized;
- Determining that Audit working papers adequately support the assignment observations, conclusions, and recommendations;
- Ensuring that Audit communications are accurate, objective, clear, concise, and timely and that Audit objectives are met; and

- Providing opportunities for developing internal Auditors' knowledge, skills, and other competencies.

Appropriate evidence of review and supervision should be documented and retained. The extent of supervision depends on the proficiency and experience of internal Auditors and the complexity of the Audit. The Director of IAU has overall responsibility for review but may delegate the review to a person within the unit.

The Audit completion checklist template (Standard Template 14) given at the end of this section provides a key quality review document used by the Audit Unit Leader and Director of the IAU to verify that all steps in the Audit have been completed.

### 4.8.2 Outsourced Audit Work

If there are not enough resources in the Internal Audit to undertake some parts of the work – or if specialist skills are required – then may be outsourced Internal Audit to a third party. The third party will be responsible for all aspects of any work that is undertaken.

However, in order to ensure that there are high Standards of public Internal Audit within Albania, the Director of the Internal Audit Unit outsourcing the work should ensure that the third party is suitably qualified and experienced in work of this type. The Director should also review a sample of the Internal Audit files of the third party in order to ensure that the required quality has been achieved in the work that has been outsourced.

### 4.8.3. Quality Control

Appropriate supervision and review from more senior members of the Internal Audit team on a day to day basis are fundamental components of an effective quality assurance process.

However, the Internal Audit Unit should also ensure that independent reviews of their work are undertaken. These reviews are a stand-alone process and are not part of the day-to-day Quality Assurance processes that the Internal Audit Units will have in place.

Such reviews can be undertaken either in an internally or externally way as follows:

**Internal Reviews** should be conducted periodically by members of the Internal Audit staff to assess the quality of the audit work undertaken within that Unit. Such reviews are usually completed by either an individual person or a small team of Internal Auditors who have been selected by the Director of the Internal Audit Unit. All Internal Audit Units should appoint an individual with overall responsibility for quality assurance. Such a thing is required mainly in cases when internal audit units consist of more than seven people, in other cases the

head or the head of sector does it.

Internal Quality Reviews provide assurance to the Director of the Internal Audit Unit by indicating compliance or non-compliance with international Standards for Internal Auditing professional practices. The Director of the Internal Audit Unit should ensure that the internal quality reviewers are experienced and not part of the group that undertook the audit mission. The review should provide recommendations for improvements where necessary. The Director is responsible for ensuring proper action is taken.

**External Reviews** may be conducted to confirm independently the quality of the Internal Audit work. These reviews should be by Central harmonisation Unit for Internal Auditing or outsourced to a third party. Such reviews should:

- Be conducted at least every five years or when considered appropriate;
- Provide a written report analysing the extent of compliance with the International Internal Auditing Standards and the Internal Audit Unit Charter, with recommendations for improvements where appropriate;
- Give independent qualified assurance to senior management, the Audit Committee as well as to the external auditors;
- Result in the Internal Audit Unit director preparing a written action plan in response to the comments and recommendations included in the external reviewer's report and forwarding the plan to the CHU (Internal Audit) and the Audit Committee where there is one. Following the recommendations is also the responsibility of the Director of the Internal Audit Unit.

The external reviewer should have the technical skills and educational background appropriate for the Audit activities to be reviewed, but could be an Internal Auditor from another Internal Audit Unit, with independence from the organisation's management and the Internal Audit Unit being reviewed.

International Standards determine the following guidelines for external review:

- The review should cover all the Auditing period.
- The external reviewer staff should be professionally qualified and independent of the Audit staff;
- The review ends with a written report to the authority who requested the review copied to Audit unit management;
- The director of the Audit unit should draft procedures for resolving conflicts that could arise from the quality review.

The report should be objective, fair and cover all Audit areas with:

Its format should include:

- Proper titles and subtitles;
- Comments referring to working papers and the report;
- Examples to support comments;

- A summary that gives an opinion on the quality on the work done;
- Constructive recommendations and suggested improvements (giving explanations why the Audit work and enhancements are required)

### **4.8.4 Managing Feedback From Auditees**

It is important for our Internal Audit work to add value to the entities being audited and for them to appreciate the work that has been done.

As with any service being provided, 'customer' feedback is a helpful way of improving the overall quality of what is being offered.

With the final Internal Audit report, the Director of the IAU distributes an Audit feedback survey to Audited recipients holding a supervisor, manager or higher position, including persons with whom the Audit unit interacted most frequently, and at least one person from each department Audited.

The completed survey forms are sent back to the IAU, where they are summarised and the results provided to the Director of the IAU. A summary of the feedback should be included in or appended to any annual internal Audit activity report.

An example of an Audit feedback survey and the covering letter are included at the end of this section at (see Standard Templates 15 and 16).



**Templates**  
**for**  
**Chapter IV**

4 . Standard Template 13: Example Action Plan

Recommendation Number	Recommendation	Level Ranking	Paragraph Reference in Report	Management response	Target Date
1	The organisation should ensure that all line managers confirm the presence of their staff on a monthly basis.	Intermediate	45	All line managers will be reminded of the need to confirm the presence of the employees within their department. The payroll manager will take overall responsibility for chasing up any confirmations that have not been provided.	31 March 201xx
2	The entity should introduce a check to ensure that all staff salaries are in accordance with the legislation.	Major	67	The payroll manager has already begun this check and is reporting the results to the Director of Finance on a weekly basis.	31 July 20XX

Standart Template 14: Audit Completion Checklist

Audit name: ..... Ref No: ..... Year: 20..

Internal Audit Unit.....

	Audit Review	Yes	No	N/A
1.	Were the detailed objectives and scope of the Audit discussed with Auditee management at an Initial meeting?			
2.	Have all scope items and areas of focus highlighted in the scope and objectives been completed? If not, have the reason(s) been fully documented			
3.	Have any and all indications of fraud been reported? In particular, consider control weaknesses such as: <ul style="list-style-type: none"> <li>• In segregation of duties</li> <li>• In missing or inadequate transaction information</li> <li>• in unclear reconciling items and suspense accounts?</li> </ul>			
4.	Does each Audit matter arising (finding) follow a structured standard format?			
5.	Were all matters timely documented and discussed with Auditee management during the Audit?			
6.	Were all facts contained in the matters arising agreed with Auditee management prior to the closing meeting?			
7.	Was a closing meeting held within one week of completion of fieldwork?			
8.	Was a working copy of the draft report discussed with Auditee management at the closing meeting?			
9.	Was the overall control rating discussed with the head of Internal Audit Unit prior to presentation of the rating to Auditee management?			
10.	Were Audit requirements for management comments communicated to management at the closure meeting: <ul style="list-style-type: none"> <li>• Agreement with observations</li> <li>• Action plan to address identified weaknesses with completion dates and persons responsible.</li> </ul>			
11.	Were all outstanding prior Audit findings followed-up and re-reported?			

## Chapter IV

	Audit Review	Yes	No	N/A
1.	Was the draft Audit report issued electronically to the Auditee's management in the standard Format within 10 working days of the closing meeting?			
2.	Has the draft report been referenced to the detailed working papers prior to issuance (quality)?			
3.	Are the reasons for not completing planned steps documented and if appropriate noted in the scope section of Audit report?			
4.	Are the reasons for not reporting issues clearly documented?			
5.	Was the final Audit report issued to the Auditee's management and Audit Committee in Standard Format?			
6.	Has the Current Audit File been updated and finalized?			
7.	Were any necessary changes to the Standard Audit work program routed through the appropriate channels for approval?			

Signed by Unit Leader

Date.....

	Audit Review	Yes	No	N/A
1.	Were all working papers containing matters arising reviewed by the Audit Unit Leader in the field prior to the closing conference?			
2.	Were all issues recorded into the follow-up database for subsequent follow-up with management?			
3.	Did the Director of Internal Audit Unit review the final report prior to release and was this documented in the working papers?			

Signed by Director IAU.....

Date.....

**Standard Template 15 - Audit Feedback With Covering Letter**

Audit name: .....  
Year: 20..

Ref No: .....

Internal Audit Unit.....



Republic of Albania

Ministry of \_\_\_\_\_

To: Name of Audited public entity

Subject: Feedback on Audit mission from (starting date) to (completion date)

Honourable Mr. / Ms.(Head of the public entity Audited).

The Internal Audit Unit recently performed a review of [Audit Name]. To help us evaluate our Audit approach and assess the Audit unit's performance, I would be grateful if you could complete the attached Audit feedback survey.

Your reply should be sent to my office where it will be included in our Audit quality assessment.

Your participation in this survey will help us to continuously improve the quality of the service your Internal Audit Unit provides.

I appreciate your assistance in our quality assurance process.

Sincerely,

Director of Internal Audit Unit

Audit name: .....

Audit unit leader:.....

Please return to: Internal Audit Unit [name and address]

**Standard Template 16 Audit Feedback Survey**

Audit name: ..... Ref No: ..... Year: 20..

Internal Audit Unit.....

With your participation in this survey, we can continuously improve the quality of service Audit provides. Please evaluate the Audit approach and unit based on the criteria set out below.

Please can you use the scale of 1 to 5 where 1 = agree strongly and 5 = disagree strongly. Please can you also add any supporting comments to further help us improve the service we offer.

**1. Professionalism.**

The unit effectively used employee time and resources. The approach and unit were objective and independent and the audit method has been effective

Agree ↔ Disagree

1	2	3	4	5
---	---	---	---	---

Comments:

**2. Communication of the process and status.**

The unit communicated findings and issues throughout the review, explaining the Audit approach clearly and issues and risks that the Audit identified.

Agree ↔ Disagree

1	2	3	4	5
---	---	---	---	---

Comments:

**3. Execution of the assignment.**

The unit understood Audit-related processes, were organised, thorough, and sensitive to organisational needs.

Agree ↔ Disagree

1	2	3	4	5
---	---	---	---	---

Comments:

**4. Accuracy and Relevance of the Audit report.**

The reported evidence was factually accurate; risks valid and reasonably assessed and recommendations well considered.

Agree  $\longleftrightarrow$  Disagree

1	2	3	4	5
---	---	---	---	---

Comments:

**5. Overall value of the Audit.**

The Audit provided constructive advice and recommendations, supporting ongoing enhancement of the internal management control environment.

Agree  $\longleftrightarrow$  Disagree

1	2	3	4	5
---	---	---	---	---

Comments:



# Chapter V

## **Audit Documentation and Evidencing**

### Introduction

A separate Audit file needs to be produced for each Audit assignment. There is an index in the standard Templates part of this chapter and this should be used for each piece of work that is undertaken. See Standard template 17.

A standardised approach to the structure of Internal Audit files helps ensure the quality assurance processes are followed and helps reviewers and other Auditors who will use the files.

The index allocates a different reference number for each stage of the work and all working papers should be allocated a unique reference number within that.

For example, section J covers the detailed Audit testing. The first test should be referenced J/1, with the second test being referenced J/2 and so on. Any supporting evidence or other supporting working papers should be referenced J/2a and J/2b etc.

Wherever possible, working papers should be cross referenced in order to enable the file to be easily reviewed.

### 5.1 Level of documentation

International Standards set out the minimum Standards of documentation that are required and these principles should be applied across all of your work.

Your working papers should record:

- The name of the entity being Audited
- The area being audited reviewed
- The period covered by this review
- The person who did the work and the date it was undertaken
- The person who reviewed the work and that date on which the review took place
- A special working papers reference number
- Details of the work that was undertaken i.e. your objective and approach
- The results of the work;and
- The conclusions drawn from the evidence obtained

### 5.2 What is Audit evidence?

Audit evidence is information that is obtained during the course of your work. It could be obtained from the reviews of key documents, interviews with staff from the organisation or from the testing of individual transactions.

Audit evidence is not merely documentation. It is a critical component of the Audit process as it allows you to draw reasonable conclusions on which to

base a judgement. Without sufficient Audit evidence, your conclusions will be little more a guess or a 'gut feeling' and will not stand up to challenge from the organisation being reviewed.

Audit evidence is obtained either through inspection, observation, enquiry and confirmation, computation or analytical procedures. The choice of which method to use is dependent, in part, upon the availability of the evidence and the form in which records are maintained.

Your assessment as to what is sufficient appropriate Audit evidence is influenced by such factors as:

- the significance of the issue being examined
- your experience gained during previous Audits and knowledge of the organisation, unit or sector;
- findings from other work performed during the Audit;
- the source and reliability of information available; and
- the nature of the system/accounting and internal control systems, including the overall control environment

The reliability of evidence is influenced by its source. Audit evidence is more persuasive when items of evidence from different sources or of a different nature are consistent with each other.

When Audit evidence from one source is inconsistent with that from another, you should determine what additional work is needed to resolve the inconsistency. For example, an interview with a person from the payroll department may conflict with your own documentation of the system that the auditors created.

While the reliability of Audit evidence is dependent on individual circumstances, the following guidelines should help in assessing that reliability:

- evidence in the form of documents and written representations is more reliable than oral representations;
- original documents are more reliable than photocopies, faxes or e-mails
- Audit evidence obtained from the Audited body's records is more reliable when the related accounting and internal control systems operate effectively.
- evidence obtained directly by Auditors is more reliable than that obtained by or from the Audited body
- Audit evidence obtained from external sources(third parties) is more reliable than that obtained from the Audited body's records

The Audit documentation should enable a fellow professional Auditor, with

More Reliable	↔	Less Reliable
An external independent source	Source of information	The entity's records
You obtain directly	Who obtains it	The entity
Documents	What form	Verbal presentations
Original documents		Copies

no previous experience with the entity or the work on that account area, to understand the work performed and the basis of the principal decisions taken and judgements made. You should document Audit processes in sufficient detail to allow the process to be repeated. For example, when testing invoices, you must record the exact details of examined records:

- Number and invoice number; and
- file in which invoice is held; and

Where your evidence has been obtained via interviews of the entity's staff, you must record:

- The person interviewed;
- The date of the interview;
- their position interviewer ion of int or role in the Audited body;
- what was asked of them; and
- An accurate reflection of their response.

Evidence to support findings should be recorded as soon as possible and, preferably, upon receipt of the information.

Your working papers should not:

- simply record everything that you have done unless it is relevant to your findings; or
- include multiple copies of documents. Where different versions of a document exist, they should only be retained if the differing versions are relevant to your work and conclusions reached

It is often necessary to support your own Audit working papers with further evidence from the entity, either in hard copy or electronic form. The decision as to whether Audited body documents (for example business plans) should be retained is a matter for individual professional judgement, but this should be exercised within the following parameters:

1. Documents should not be retained simply because they have been examined in the course of our work. For example, after reviewing 10 invoices there is no benefit from adding copies of these to the file unless they demonstrate that exceptions (e.g. failure of control) have been identified. If you can re-perform the procedure without maintaining a copy do not retain unless:
  - it is evidence of a matter arising;
  - it is evidence of a weakness;
  - it is evidence of something warranting reporting to those charged with management; or
2. it is something of a 'permanent' nature.
3. Documents should not normally be retained if they are available from other sources, for example general legislation. However, there may be certain circumstances where it is necessary or sensible to retain documents, even if they are available from other sources. Examples may include work undertaken by junior/ inexperienced staff, or potentially high profile issues where further review/ re-performance is likely. In these circumstances, it is likely that the original documentation will need to be seen and it would be uneconomical not to retain the information for ready access.
4. A careful assessment needs to be made of the risk of the Audited body destroying these documents before you discard them, taking account of the formality and sensitivity of the document and the entity's policy on document retention and destruction.
5. You should only retain documentation that is relevant to your work and conclusions; for example, you should not retain or attach a full strategy document if your finding relates to a single paragraph or page. Note that this may not be applicable for some types of work where the whole document is being evaluated to inform judgements made.

Original documents such as invoices, personnel files etc should not be retained by the Internal Audit Unit and should remain the property of the organisation being Audited, but if the audit unit judges it necessary to obtain copies of document they can do so.

### 5.3 Permanent Files

Auditors need to have a good knowledge of the entity, its operational activities and financial systems in order to ensure that their work is relevant to the organisation being Audited.

It is helpful for this information to be held in one place and for such information to be made available to all members of the Internal Audit Unit. We refer to this as the permanent file and a separate permanent file should be maintained for each organisation that is Audited.

The permanent file should be updated after the completion of each Audit assignment in order to ensure the contents remain up to date.

The use of an up-to-date permanent file can make Audits more efficient as it prevents Auditors having to request information on numerous occasions and can also help Audit work from one year be rolled forward to the next year.

The information retained on a permanent file will depend upon the Auditor's judgment as to what would be helpful, but may include:

- The name of the organisation and its key activities and functions;
- Key plans and main documents relating to the organisation's activities, such as business plans and Annual Reports;
- Relevant laws, regulations and administrative instructions that will impact on the Audit of the entity – there is no need to collect all of legislation that relates to the entity, just the key areas that may interest the Auditors;
- An organisational chart which sets out the departmental structures and the internal reporting arrangements;
- The names and job titles of relevant staff within the entity;
- Administrative arrangements i.e. phone numbers, e-mail addresses etc.
- Internal procedures notes of the entity covering key account areas such as the payments for goods and services, payroll etc.
- Flowcharts of account areas produced by the Internal Auditors in previous years;
- The current Internal Audit strategic plan for the entity;
- The current Internal Audit annual plan for the entity;
- Previous Audit reports;
- Any other relevant documents that may helpful as part of the Audit.

A suggested permanent file index is included within the Standard Templates– Template 18 of this chapter. All documents within the permanent file should be individually numbered in order to make the contents easier to locate. Documents should be removed and / or updated as necessary.

**Templates  
for**  
**Chapter V**

### Standard Template 17: Suggested Index For Audit Files

Internal Audit Working Papers File	
Entity:	
System/ Area Being Reviewed:	
Audit Period:	
Contents	Section Reference
Final report to the entity for this review	A
Draft reports to the entity for this review	B
Notes from meetings with the entity to discuss the scope of the work and the reports	C
Extract from annual Internal Audit plan	D
Audit budget and time records	E
Copy of overall control environment Standard template	F
Previous Internal Audit report on this area (if available)	G
System/ Account area risk assessment	H
System documentation	I
Audit programme and detailed Audit testing	J

### Standard Template 18: Suggested Index for Permanent Files

Permanent File Index	
Entity:	
Contents	Section Reference
Details of the organisation's key activities and functions	A
Key plans and documents of the organisation	B
Relevant laws, regulations and administrative instructions	C
Organisational chart	D
The names and job titles of relevant staff within the organisation	E
Administrative arrangements i.e. phone numbers, e-mail addresses etc	F
Internal procedures notes of the organisation covering key account areas such as the payments for goods and services, payroll etc.	G
Flowcharts of account areas produced by the Internal Auditors in previous years	H
The current Internal Audit strategic plan for the entity	I
The current Internal Audit annual plan for the entity	J
Previous Audit reports;	K
Any other relevant documents that may helpful as part of the Audit*	L

\*you can use sections M onwards as well if helpful

# Chapter VI

## **European Union Internal Audit Requirements**

### Introduction

All Audits should be undertaken to the internationally accepted Internal Audit Standards upon which this manual has been based. However, the Audit of EU funds does on occasions require adherence to specific additional provisions. This chapter of the Internal Audit manual therefore sets out these requirements and the approach that should be followed in these instances. However, the basic principles contained within this manual will still need to be followed.

### 6.1 The Instrument for Pre-Accession (IPA)

As can be seen above, there are 5 components within the IPA:

1. **Transitional assistance and institution building:** This component may be used to finance capacity and institution building as well as investment. Assistance may also be used to support Albania's participation in Community programmes and agencies. In addition, assistance may be provided for regional and horizontal programmes.
2. **Cross border cooperation:** This component may support cross border and, where appropriate, transnational and interregional co-operation between beneficiary countries and between beneficiary countries and Member States. Co-operation shall have the objective of promoting good neighbourly relations, fostering stability, security and prosperity in the mutual interest of all countries concerned, and of encouraging their harmonious, balanced and sustainable development. This component may, amongst other things, be used to finance capacity and institution building as well as investment.
3. **Regional development:** This component provides support in policy development as well as preparation for the implementation and management of the European Community's cohesion policy, in particular, in the preparation for the European Regional Development Fund and the Cohesion Fund, notably in the areas of transport, environment, regional competitiveness and infrastructure.
4. **Human Resources–** This component provides support for the strengthening of economic and social cohesion through actions including, increasing adaptability of workers, enhancing access to employment, and enhancing human capital. This component is also implemented in preparation for the post-accession structural and cohesion funds.
5. **Rural Development:** This Component provides support for rural development activities in order to contribute to the following objectives: improving the competitiveness of agriculture and forestry, improving the environment, improving the quality of life in rural areas. This component is also implemented in preparation for the post-accession rural development fund.

Further details on these five areas are given in articles 8-12 of EC Regulation 1085/2006.

### 6.2 Key Legislation

The key legislation / documents that relate to the implementation of EU Pre-Accession Funds are:

1. European Council Regulation No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities
2. European Commission Regulation No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of Council Regulation No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities
3. European Council Regulation No.1085/2006 of 17 July 2006 establishing an Instrument for Pre-accession Assistance (IPA)
4. European Commission regulation No. 718/2007 of 12 June 2007 implementing European Council Regulation No.1085/2006 establishing an Instrument for Pre-accession Assistance (IPA)

These are supported by further detailed legal documents, notably:

1. Framework Agreement. This is concluded between the Commission and the beneficiary country in order to set out and agree on the rules for co-operation concerning EC financial assistance.
2. Sectorial Agreement. This contains component 5 specific provisions. Currently no Sectorial agreements apply to components 1-4
3. Multi-Annual Indicative Financial Framework (MIFF). This lays out the allocation of funds between countries.

In addition specific documentation at Country level apply to the implementation of Pre-accession funds through IPA:

1. European Partnership or Accession Partnership – Changes required for country to make progress towards accession
2. Multi-Annual Indicative Planning Documents – These set out the assistance that is to be provided
3. Annual Action Programmes – These are component specific and details the projects that will be implemented for each year of funding

Further details are set out in Articles 4-7 of EC Regulation 1085/2006 and Articles 5-8 of EC Regulation 718/1007.

### 6.3 Responsible authorities

Beneficiary countries are also required to designate certain bodies and authorities to ensure the correct management of Instrument for Pre-Accession (IPA) funds:

- National IPA Co-ordinator;
- Strategic Co-ordinator for the Regional Development and the Human Resource Development Components;
- Competent Accrediting Officer;
- National Authorising Officer;
- National Fund;
- An operating structure by IPA component or programme – to include internal Audit of its different constituting bodies; and
- An Audit Authority

Further details of the roles of each of these authorities are given in Article 21 of European Commission Regulation No 718/2007.

### 6.4 Common rules for implementation of Pre-Accession funds

The relevant EC regulations outline certain common rules concerning the implementation of Pre-Accession funds under IPA. These regulations are:

- Assistance under the IPA Regulation shall be consistent and coordinated within and between the IPA components, both at planning and programming levels.
- Any overlap between actions covered by different components shall be avoided and no expenditure shall be financed under more than one operation.
- For each IPA component or programme, an operating structure shall be established to deal with the management and implementation of assistance under the IPA Regulation (Article 28 of EC Regulation No.718/2007). The operating structure shall be a body or a collection of bodies within the administration of the beneficiary country. The operating structure shall be responsible for managing and implementing the programme or programmes concerned in accordance with the principle of sound financial management. For those purposes, it shall carry out a number of functions that include: “ensuring internal Audit of its different constituting bodies;”

### 6.5 Specific requirements concerning the role of internal Audit

The European Commission retains overall responsibility for the execution of funds from IPA and it may manage them under either a centralised or decentralised arrangement. Where decentralised management arrangements apply, certain conditions must be respected by the beneficiary country prior to the European Commission's decision to allow decentralised management. These include provisions that cover internal Audit and which include:

- Internal Audit including handling of Audit reports and recommendations (this is distinct from control activities and management supervision)
- Ensuring that top managers are provided with some independent reviews of the functioning of their systems at subordinate levels. This may involve some retrospective transaction checking but should be more focussed on effectiveness and efficiency of system and organisation design.

For certain components (notably Component 5), prior to the accreditation of the operating structure to which funds are to be decentralised, an external Audit to internationally accepted Audit Standards must be undertaken confirming the fulfilment of the management and control systems are functioning as laid out in EC regulations and / or separate agreements (i.e. sectorial/financing agreements).

These requirements include ensuring the existence of internal Audit of the different constituting bodies of the operating structure. Additional specific instructions apply to the operating structure under Component 5 (rural Development) which are detailed below. Only after the satisfactory completion of these requirements can the European Commission approve the conferral of management powers to a country.

### 6.6 Responsibilities for EU Pre-Accession Funds

As the senior government official responsible for the overall financial management of EU funds in the beneficiary country, the National Authorising Officer (NAO), is responsible for the effective functioning of management and control systems under the IPA regulation. This will necessitate the review of Audit reports prepared by the external Audit body (the Audit Authority), which may base its work on the work on individual internal Audit units.

### 6.7 Role of Internal Audit Units

The role of Internal Audit Units will be to provide senior management within the operating structure with assurance that the management and control systems are operating effectively and to provide recommendations as to where they can be improved.

European Council Regulation No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities (Articles 85- 87) states:

- Each institution shall establish an internal Auditing function which must be performed in compliance with the relevant international Standards. The internal Auditor appointed by the institution shall be answerable to the latter for verifying the proper operation of budgetary implementation systems and procedures. The internal Auditor may not be either authorising officer or accounting officer.
- The internal Auditor shall advise his/her institution on dealing with risks, by issuing independent opinions on the quality of management and control systems and by issuing recommendations for improving the conditions of implementation of operations and promoting sound financial management.

Internal Audit shall be responsible in particular:

- for assessing the suitability and effectiveness of internal management systems and the performance of departments in implementing policies, programmes and actions by reference to the risks associated with them; and
- for assessing the suitability and quality of the internal control and Audit systems applicable to every budgetary implementation operation.

Internal Auditor shall perform their duties on all the institution's activities and departments. They should have full and unlimited access to all information required to perform their duties, if necessary on the spot, including in the Member States and in third countries.

Internal Auditors should report to the institution on their findings and recommendations. The institution shall ensure that action is taken on recommendations resulting from Audits. The internal Auditor shall also submit to the institution an annual internal Audit report indicating the number and type of internal Audits carried out, the recommendations made and the action taken on those recommendations.

Each year the institution shall forward a report to the discharge authority summarising the number and type of internal Audits carried out, the recommendations made and the action taken on those recommendations. An example is included at Standard Template 19 at the end of this section.

Special rules applicable to the internal Auditor shall be laid down by the institution and shall be such as to guarantee that he/she is totally independent in the performance of his/her duties and to establish his responsibility.

If the internal Auditor is an official or other member of staff, he/she shall assume responsibility as laid down in the Personnel Regulations and spelt out in the implementing rules.

These requirements shall be interpreted as follows:

- Each institution responsible for the management/handling of EU funds shall have an Internal Audit Unit established within it.
- Internal Audit Units must perform their work in compliance with the relevant international Standards. This Internal Audit Manual should therefore be adopted by all Internal Audit Units responsible for Auditing EU funds.
- The structure of the institution responsible for managing / handling EU funds must ensure that the Head of the Internal Audit Unit answers directly to the head of the institution in question and reports on the verification of the proper operation of budgetary implementation systems and procedures.
- Special rules applicable to the internal Audit unit shall be laid down by the institution and shall be such as to guarantee that an internal Auditor is totally independent in the performance of his/her duties and to establish his/her responsibilities. This would normally be undertaken in the law establishing the institution or within any internal operating procedures. Likewise, if the internal Auditor is an official or other member of staff within an institution, he/she shall assume responsibility as laid down in the internal Staff Regulations and spelt out in the relevant implementing rules.
- The Head of the Internal Audit Unit may not be either the Institution's authorising officer or accounting officer.
- The Internal Audit Unit shall advise their institution on dealing with risks, by issuing independent opinions on the quality of management and control systems and by issuing recommendations for improving the conditions of implementation of operations and promoting sound financial management. Following this Internal Audit Manual will ensure that this requirement is met.

Specifically, the Internal Audit Unit shall be responsible for:

- Assessing the suitability and effectiveness of internal management systems and the performance of departments in implementing policies, programmes and actions by reference to the risks associated with them. Within this Internal Audit Manual this would be classed as an assurance Audit.
- Assessing the suitability and quality of the internal control and Audit systems applicable to every budgetary implementation operation. Within this Internal Audit Manual this would be classed as systems based Audit.

The Internal Audit Unit shall ensure that their Audit work covers all the institution's activities and departments over a defined period of time. A maximum of 5 years is recommended, although where problems are identified, these areas should be subject of repeat Audits. Further information on strategic Internal Audit planning is included within section 2 of this manual.

The Internal Audit Unit shall enjoy full and unlimited access to all information required to perform their duties, if necessary on the spot, including in the Member States and in third countries..

The Internal Audit Unit shall report to the institution on their findings and recommendations. Further information on reporting is included within section 4 of this manual.

The institution shall ensure that action is taken on recommendations resulting from internal Audits. Provision for the Internal Audit Units to ensure that appropriate action has been taken is covered within section 3 of this Internal Audit manual and this is known as follow up work.

The Internal Audit Unit shall also submit to the institution an annual internal Audit report indicating the number and type of internal Audits carried out, the recommendations made and the action taken on those recommendations. This provision is covered within section 4 of this manual.

Each year the institution shall forward a report to the authority overseeing the management of the funds by that institution concerned which summarises the number and type of internal Audits carried out, the recommendations made and the action taken on those recommendations. An example return is shown at StandardTemplate 19 at the end of this section.

### 6.8 Specific Component requirements

Under Component 5 there are additional specific requirements concerning the establishment, role, functions and responsibilities of Internal Audit Units.

The decision on the Accreditation of the operating body (the IPARD Agency) by the National Authorising Officer on the basis of an external Audit conducted to internationally accepted Audit Standards, must take account of the provisions for internal Audits within the IPARD Agency. This requires the following:

The organisational structure of the IPARD Agency must include the technical services and the internal Audit service.

Where documents relating to the claims authorised, expenditure committed and controls effected as well as those relating to projects not selected are retained by other bodies, both these bodies and the IPARD Agency shall set up procedures to ensure that the location of all such documents that are relevant to specific payments made by the National Fund or IPARD Agency is recorded, and that these documents shall be made available for inspection at their offices at the request of the persons and bodies who would normally have the right to inspect such documents, and including:

- the IPARD Agency 's staff who deal with the claim,
- the National Fund or IPARD Agency 's internal Audit services,
- the Audit Authority that attests the NAO's annual declaration,
- duly authorised officials or representatives of the NAO or the CAO, and

- Authorised agents or representatives of the Community.

Furthermore, for each of its different constituting bodies, structures, authorities and bodies of the management and control system (as defined in Articles 6 – 8 of the Framework Agreement) shall adopt in this respect the following procedures:

- The internal Audit service shall be independent of the other departments and shall report directly to the top management. This provision is already covered by the generally applicable rules referred to above.
- The internal Audit service shall verify that procedures adopted by the concerned structures, authorities and bodies of the management and control systems, and modifications thereto, are adequate to ensure that compliance with the Agreements is verified, that the functioning of their systems at subordinate levels operates efficiently and that the accounts are accurate, complete and timely. Verifications may be limited to selected measures and sub-measures and to samples of transactions provided that an Audit plan ensures that all significant areas, including the departments and bodies responsible for authorisation and those departments and bodies to which functions have been delegated, are covered over a period not exceeding five years. May involve some ex-post transaction checking but should be more focussed on effectiveness and efficiency of system and organisation design.

These requirements are covered by this Internal Audit Manual as follows:

No	Requirement	Section of Internal Audit Manual
I	Verify that procedures adopted by the concerned structures, authorities and bodies of the management and control systems, and modifications thereto, are adequate to ensure that compliance with the (EU) Agreements is verified,	Section 3 – Audit execution
ii.	that the functioning of their systems at subordinate levels operates efficiently	Section 3 – Audit execution
iii.	that the accounts are accurate, complete and timely.	This requirement is not currently met within the Internal Audit Manual, as it is work objective of IEAK.
iv.	Verifications may be limited to selected measures and sub-measures and to samples of transactions provided that an Audit plan ensures that all significant areas, including the departments and bodies responsible for authorisation and those departments and bodies to which functions have been delegated, are covered over a period not exceeding five years.	Section 2 – Activity Internal Audit Programme
v.	May involve some ex-post transaction checking but should be more focussed on effectiveness and efficiency of system and organisation design	Section 3 – Internal Audit execution

The Internal Audit Unit's work shall be performed in accordance with international Auditing principles, shall be recorded in working papers and shall result in reports and recommendations addressed to the top management. Such a request is fulfilled through the approval and use of Internal Audit manual.

The Audit plans and reports shall be made available to the Audit Authority, to the duly authorised officials or representatives of the CAO and the NAO, and to the duly authorised agents or representatives of the Community to undertake financial Audits and for the sole purpose of appraising the effectiveness of the internal Audit function.

No provisions to fulfil this requirement currently exist within the Internal Audit Manual. However, in due course, copies of all Internal Audit Unit Audit plans and reports will need to be made available as a matter of course, to the external Auditor – the Audit Authority, to the formal representatives of the Competent Authorising Officer and to the National Authorising Officer; and to the formal representatives of the European Commission.

**Standard Templates  
for**  
**Chapter VI**

Standard Template 19: Example Annual Report From Institution To Its Discharge Authority Covering The Work Of Their Internal Audit Unit

1. Dates covered by this report (e.g. 1 January – 31 December 2011)

2. Line Ministry/Public body covered by the Internal Audit Unit:

3. Report produced by: (Name), Head of Institution

Address

Tel:

Fax:

E-Mail:

4. Number and type of internal Audits undertaken during the year in question:

a. Systems based Audits which includes:

Information technology controls

Management controls

accuracy and timeliness of financial and management information as well as their use to support decision making processes

safeguarding and effective administration of public property assets

b. Compliance Audits

c. Performance d. Financial Audits

e. agreed advisory assignments on behalf of the Audited body

5. Recommendations made and the action taken on those recommendations.

Type of Audit	Subject of Audit	Recommendations made	Action taken

Signed:

Name

Date:

# Chapter VII

## **Internal Audit Standards**

### INTRODUCTION

Internal Auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Internal Audit activities are performed in diverse legal and cultural environments: within organizations that vary in purpose, size, complexity, and structure; and by persons within or outside the organization. While differences may affect the practice of internal Auditing in each environment, compliance with the International Standards for the Professional Practice of Internal Auditing is essential if the responsibilities of internal Auditors are to be met. If internal Auditors are prohibited by laws or regulations from complying with certain parts of the Standards, they should comply with all other parts of the Standards and make appropriate disclosures.

Assurance services involve the internal Auditor's objective assessment of evidence to provide an independent opinion or conclusions regarding a process, system or other subject matter. The nature and scope of the assurance engagement are determined by the internal Auditor. There are generally three parties involved in assurance services: (1) the person or group directly involved with the process, system or other subject matter – the process owner; (2) the person or group making the assessment – the internal Auditor; and (3) the person or group using the assessment - the user.

Consulting services are advisory in nature, and are generally performed at the specific request of an engagement client. The nature and scope of the consulting engagement are subject to agreement with the engagement client. Consulting services generally involve two parties: (1) the person or group offering the advice – the internal Auditor; and (2) the person or group seeking and receiving the advice – the engagement client. When performing consulting services the internal Auditor should maintain objectivity and not assume management responsibility.

The purpose of the Standards is to:

1. Delineate basic principles that represent the practice of internal Auditing as it should be.
2. Provide a framework for performing and promoting a broad range of value-added internal Audit activities.
3. Establish the basis for the evaluation of internal Audit performance.
4. Foster improved organizational processes and operations.

The Standards consist of Attribute Standards, Performance Standards, and Implementation Standards. The Attribute Standards address the characteristics of organizations and parties performing internal Audit activities.

The Performance Standards describe the nature of internal Audit activities and provide quality criteria against which the performance of these services can be evaluated. While the Attribute and Performance Standards apply to all internal Audit services, the Implementation Standards apply to specific types of engagements.

There is one set of Attribute and Performance Standards; however, there are multiple sets of Implementation Standards: a set for each of the major types of internal Audit activity. The Implementation Standards have been established for assurance (A) and consulting (C) activities.

The Standards are part of the Professional Practices Framework. The Professional Practices Framework includes the Definition of Internal Auditing, the Code of Ethics, the Standards, and other guidance. Guidance regarding how the Standards might be applied is included in Practice Advisories that are issued by the Professional Issues Committee.

The Standards employ terms that have been given specific meanings that are included in the Glossary.

The development and issuance of the Standards is an ongoing process. The Internal Auditing Standards Board engages in extensive consultation and discussion prior to the issuance of the Standards. This includes worldwide solicitation for public comment through the exposure draft process.

All exposure drafts are posted on The IIA's Web site as well as being distributed to all IIA Affiliates. Suggestions and comments regarding the Standards can be sent to:

The Institute of Internal Auditors

Global Practices Centre, Professional Practices Group

247 Maitland Avenue

Altamonte Springs, FL 32701-4201, USA

E-mail: [standards@theiia.org](mailto:standards@theiia.org)

Web: <http://www.theiia.org>

## 7.1 ATTRIBUTE STANDARDS

### 1000 – Purpose, Authority, and Responsibility

The purpose, authority, and responsibility of the internal Audit activity must be formally defined in an internal Audit charter, consistent with the Definition of Internal Auditing, the Code of Ethics, and the Standards. The chief Audit executive must periodically review the internal Audit charter and present it to

senior management and the board for approval.

1000.A1 – The nature of assurance services provided to the organization must be defined in the internal Audit charter. If assurances are to be provided to parties outside the organization, the nature of these assurances must also be defined in the internal Audit charter.

1000.C1 – The nature of consulting services must be defined in the internal Audit charter.

1010 – Recognition of the Definition of Internal Auditing, the Code of Ethics, and the Standards in the Internal Audit Charter

The mandatory nature of the Definition of Internal Auditing, the Code of Ethics, and the Standards must be recognized in the internal Audit charter. The chief Audit executive should discuss the Definition of Internal Auditing, the Code of Ethics, and the Standards with senior management and the board.

### **1100 – Independence and Objectivity**

The internal Audit activity must be independent, and internal Auditors must be objective in performing their work.

1110 – Organizational Independence

The chief Audit executive must report to a level within the organization that allows the internal Audit activity to fulfil its responsibilities. The chief Audit executive must confirm to the board, at least annually, the organizational independence of the internal Audit activity.

1110.A1 – The internal Audit activity must be free from interference in determining the scope of internal Auditing, performing work, and communicating results.

### **1111 – Direct Interaction with the Board**

The chief Audit executive must communicate and interact directly with the board.

### **1120 – Individual Objectivity**

Internal Auditors must have an impartial, unbiased attitude and avoid any conflict of interest.

### **1130 – Impairment to Independence or Objectivity**

If independence or objectivity is impaired in fact or appearance, the details of the impairment must be disclosed to appropriate parties. The nature of the disclosure will depend upon the impairment.

1130.A1 – Internal Auditors must refrain from assessing specific operations for which they were previously responsible. Objectivity is presumed to be impaired if an internal Auditor provides assurance services for an activity for which the internal Auditor had responsibility within the previous year.

1130.A2 – Assurance engagements for functions over which the chief Audit executive has responsibility must be overseen by a party outside the internal Audit activity.

1130.C1 – Internal Auditors may provide consulting services relating to operations for which they had previous responsibilities.

1130.C2 – If internal Auditors have potential impairments to independence or objectivity relating to proposed consulting services, disclosure must be made to the engagement client prior to accepting the engagement.

### **1200 – Proficiency and Due Professional Care**

Engagements must be performed with proficiency and due professional care.

#### **1210 – Proficiency**

Internal Auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal Audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

1210.A1 – The chief Audit executive must obtain competent advice and assistance if the internal Auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

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.

1210.A3 – Internal Auditors must have sufficient knowledge of key information technology risks and controls and available technology-based Audit techniques to perform their assigned work. However, not all internal Auditors are expected to have the expertise of an internal Auditor whose primary responsibility is information technology Auditing.

1210.C1 – The chief Audit executive must decline the consulting engagement or obtain competent advice and assistance if the internal Auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

#### **1220 – Due Professional Care.**

Internal Auditors must apply the care and skill expected of a reasonably prudent and competent internal Auditor. Due professional care does not imply infallibility.

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

- Extent of work needed to achieve the engagement's objectives;
- Relative complexity, materiality, or significance of matters to which assurance

procedures are applied;

- Adequacy and effectiveness of governance, risk management, and control processes;
- Probability of significant errors, fraud, or noncompliance; and
- Cost of assurance in relation to potential benefits.

1220.A2 – In exercising due professional care internal Auditors must consider the use of technology-based Audit and other data analysis techniques.

1220.A3 – Internal Auditors must be alert to the significant risks that might affect objectives, operations, or resources. However, assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.

1220.C1 – Internal Auditors must exercise due professional care during a consulting engagement by considering the:

- Needs and expectations of clients, including the nature, timing, and communication of engagement results;
- Relative complexity and extent of work needed to achieve the engagement's objectives; and
- Cost of the consulting engagement in relation to potential benefits.

### **1230 – Continuing Professional Development**

Internal Auditors must enhance their knowledge, skills, and other competencies through continuing professional development.

### **1300 – Quality Assurance and Improvement Program**

The chief Audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal Audit activity.

1310 – Requirements of the Quality Assurance and Improvement Program

The quality assurance and improvement program must include both internal and external assessments.

### **1311 – Internal Assessments**

Internal assessments must include:

- Ongoing monitoring of the performance of the internal Audit activity; and
- Periodic reviews performed through self-assessment or by other persons within the organization with sufficient knowledge of internal Audit practices.

Periodic reviews are assessments conducted to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards.

Sufficient knowledge of internal Audit practices requires at least an understanding of all elements of the International Professional Practices

Framework.

### **1312 – External Assessments**

External assessments must be conducted at least once every five years by a qualified, independent reviewer or review unit 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 reviewers or review units, including any potential conflict of interest.

An independent reviewer or review unit means not having either a real or an apparent conflict of interest and not being a part of, or under the control of, the organization to which the internal Audit activity belongs.

### **1320 – Reporting on the Quality Assurance and Improvement Program**

The chief Audit executive must communicate the results of the quality assurance and improvement program to senior management and the board.

### **1321– Use of “Conforms with the International Standards for the Professional Practice of Internal Auditing”**

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.

### **1322– Disclosure of Non-conformance**

When non-conformance with the Definition of Internal Auditing, the Code of Ethics, or the Standards impacts 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.

## **7.2 PERFORMANCE STANDARDS**

### **2000 – Managing the Internal Audit Activity**

The chief Audit executive must effectively manage the internal Audit activity to ensure it adds value to the organization.

### **2010 – Planning**

The chief Audit executive must establish risk-based plans to determine the priorities of the internal Audit activity, consistent with the organization’s goals.

2010.A1 – The internal Audit activity’s plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process.

2010.C1 – The chief Audit executive should consider accepting proposed consulting engagements based on the engagement’s potential to improve management of risks, add value, and improve the organization’s operations. Accepted engagements must be included in the plan.

### **2020 – Communication and Approval**

The chief Audit executive must communicate the internal Audit activity’s plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief Audit executive must also communicate the impact of resource limitations.

### **2030 – Resource Management**

The chief Audit executive must ensure that internal Audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

### **2040 – Policies and Procedures**

The chief Audit executive must establish policies and procedures to guide the internal Audit activity.

### **2050 – Coordination**

The chief Audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimize duplication of efforts.

### **2060 – Reporting to Senior Management and the Board**

The chief Audit executive 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 senior management and the board.

### **2100 – Nature of Work**

The internal Audit activity must evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic and disciplined approach.

### **2120 – Risk Management**

The internal Audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes. Risk management processes are monitored through ongoing management activities, separate evaluations, or both.

2120. A1 – The internal Audit activity must evaluate risk exposures relating to the organization’s governance, operations, and information systems regarding the:

- Reliability and integrity of financial and operational information.

- Effectiveness and efficiency of operations.
- Safeguarding of assets; and
- Compliance with laws, regulations, and contracts.

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

2120.C1 – During consulting engagements, internal Auditors must address risk consistent with the engagement's objectives and be alert to the existence of other significant risks.

2120.C2 – Internal Auditors must incorporate knowledge of risks gained from consulting engagements into their evaluation of the organization's risk management processes.

2120.C3 – When assisting management in establishing or improving risk management processes, internal Auditors must refrain from assuming any management responsibility by actually managing risks.

### **2130 – Control**

The internal Audit activity must assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

2130.A1 –The internal Audit activity must evaluate the adequacy and effectiveness of controls in responding to risks within the organization's governance, operations, and information systems regarding the:

- Reliability and integrity of financial and operational information;
- Effectiveness and efficiency of operations;
- Safeguarding of assets; and
- Compliance with laws, regulations, and contracts.

2130.A2 – Internal Auditors should ascertain the extent to which operating and program goals and objectives have been established and conform to those of the organization.

2130.A3 – Internal Auditors should review operations and programs to ascertain the extent to which results are consistent with established goals and objectives to determine whether operations and programs are being implemented or performed as intended.

2210.A3– Adequate criteria are needed to evaluate controls. Internal Auditors must ascertain the extent to which management has established adequate criteria to determine whether objectives and goals have been accomplished. If adequate, internal Auditors must use such criteria in their evaluation. If inadequate, internal Auditors must work with management to develop appropriate evaluation criteria.

2130.C1 – During consulting engagements, internal Auditors must address

controls consistent with the engagement's objectives and be alert significant control issues.

2130.C2 – Internal Auditors must incorporate knowledge of controls gained from consulting engagements into evaluation of the organization's control processes.

### **2110 – Governance**

The internal Audit activity must assess and make appropriate recommendations for improving the governance process in its accomplishment of the following objectives:

- Promoting appropriate ethics and values within the organization;
- Ensuring effective organizational performance management and accountability;
- Communicating risk and control information to appropriate areas of the organization; and
- Coordinating the activities of and communicating information among the board, external and internal Auditors, and management.

2110.A1 – The internal Audit activity must evaluate the design, implementation, and effectiveness of the organization's ethics-related objectives, programs, and activities.

2110.A2 – The internal Audit activity must assess whether the information technology governance of the organization sustains and supports the organization's strategies and objectives.

2110.C1 – Consulting engagement objectives must be consistent with the overall values and goals of the organization.

### **2200 – Engagement Planning**

Internal Auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations.

### **2201 – Planning Considerations**

In planning the engagement, internal Auditors must consider:

- The objectives of the activity being reviewed and the means by which the activity controls its performance;
- The significant risks to the activity, its objectives, resources, and operations and the means by which the potential impact of risk is kept to an acceptable level;
- The adequacy and effectiveness of the activity's risk management and control processes compared to a relevant control framework or model; and
- The opportunities for making significant improvements to the activity's risk management and control processes.

2201.A1 – When planning an engagement for parties outside the organization, internal Auditors must establish a written understanding with them about objectives, scope, respective responsibilities, and other expectations, including restrictions on distribution of the results of the engagement and access to engagement records.

2201.C1 – Internal Auditors must establish an understanding with consulting engagement clients about objectives, scope, respective responsibilities, and other client expectations. For significant engagements, this understanding must be documented.

### **2210 – Engagement Objectives**

Objectives must be established for each engagement.

2210.A1 – Internal Auditors must conduct a preliminary assessment of the risks relevant to the activity under review. Engagement objectives must reflect the results of this assessment.

2210.A2 – Internal Auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.

2210.A3 – Adequate criteria are needed to evaluate controls. Internal Auditors must ascertain the extent to which management has established adequate criteria to determine whether objectives and goals have been accomplished. If adequate, internal Auditors must use such criteria in their evaluation. If inadequate, internal Auditors must work with management to develop appropriate evaluation criteria.

2210.C1 – Consulting engagement objectives must address governance, risk management, and control processes to the extent agreed upon with the client.

### **2220 – Engagement Scope**

The established scope must be sufficient to satisfy the objectives of the engagement.

2220.A1 – The scope of the engagement must include consideration of relevant systems, records, personnel, and physical properties, including those under the control of third parties.

2220.A2 – If significant consulting opportunities arise during an assurance engagement, a specific written understanding as to the objectives, scope, respective responsibilities, and other expectations should be reached and the results of the consulting engagement communicated in accordance with consulting standards.

2220.C1 – In performing consulting engagements, internal Auditors must ensure that the scope of the engagement is sufficient to address the agreed-upon objectives. If internal Auditors develop reservations about the scope during the engagement, these reservations must be discussed with the client.

to determine whether to continue with the engagement.

### **2230 – Engagement Resource Allocation**

Internal Auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

### **2240 – Engagement Work Program**

Internal Auditors must develop and document work programs that achieve the engagement objectives.

2240.A1 – Work programs must include the procedures for identifying, analyzing, evaluating, and documenting information during the engagement. The work program must be approved prior to its implementation, and any adjustments approved promptly.

2240.C1 – Work programs for consulting engagements may vary in form and content depending upon the nature of the engagement.

### **2300 – Performing the Engagement**

Internal Auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement's objectives.

### **2310 – Identifying Information**

Internal Auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

### **2320 – Analysis and Evaluation**

Internal Auditors must base conclusions and engagement results on appropriate analyses and evaluations.

### **2330 – Documenting Information**

Internal Auditors must document relevant information to support the conclusions and engagement results.

2330.A1 – The chief Audit executive must control access to engagement records. The chief Audit executive must obtain the approval of senior management and/or legal counsel prior to releasing such records to external parties, as appropriate.

2330.A2 – The chief Audit executive must develop retention requirements for engagement records, regardless of the medium in which each record is stored. These retention requirements must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

2330.C1 – The chief Audit executive must develop policies governing the custody and retention of consulting engagement records, as well as their release to internal and external parties. These policies must be consistent

with the organization's guidelines and any pertinent regulatory or other requirements.

### **2340 – Engagement Supervision**

Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.

### **2400 – Communicating Results**

Internal Auditors must communicate the engagement results.

#### **2410 – Criteria for Communicating**

Communications must include the engagement's objectives and scope as well as applicable conclusions, recommendations, and action plans.

2410.A1 – Final communication of engagement results must, where appropriate, contain internal Auditors' overall opinion and/or conclusions.

2410.A2 – Internal Auditors are encouraged to acknowledge satisfactory performance in engagement communications.

2410.A3 – When releasing engagement results to parties outside the organization, the communication must include limitations on distribution and use of the results.

2410.C1 – Communication of the progress and results of consulting engagements will vary in form and content depending upon the nature of the engagement and the needs of the client.

#### **2420 – Quality of Communications**

Communications must be accurate, objective, clear, concise, constructive, complete, and timely.

#### **2421 – Errors and Omissions**

If a final communication contains a significant error or omission, the chief Audit executive must communicate corrected information to all parties who received the original communication.

2430 – Use of “Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing”

Internal Auditors may report that their engagements are “conducted in conformance with the International Standards for the Professional Practice of Internal Auditing”, only . However, internal Auditors may use the statement only if the results of the quality assurance and improvement program support the statement.

#### **2431 – Engagement Disclosure of Non-conformance**

When non-conformance with the Definition of Internal Auditing the Code of Ethics or the Standards impacts a specific engagement, communication of the results must disclose the:

- Principle or rule of conduct of the Code of Ethics or Standard(s) with which full conformance was not achieved;
- Reason(s) for non-conformance; and
- Impact of non-conformance on the engagement and the communicated engagement results.

#### **2440 – Disseminating Results**

The chief Audit executive must communicate results to the appropriate parties.

2440.A1 – The chief Audit executive is responsible for communicating the final results to parties who can ensure that the results are given due consideration.

2440.A2 – If not otherwise mandated by legal, statutory, or regulatory requirements, prior to releasing results to parties outside the organization the chief Audit executive must:

- Assess the potential risk to the organization;
- Consult with senior management and/or legal counsel as appropriate; and
- Control dissemination by restricting the use of the results.

2440.C1 – The chief Audit executive is responsible for communicating the final results of consulting engagements to clients.

2440.C2 – During consulting engagements, governance, risk management, and control issues may be identified. Whenever these issues are significant to the organization, they must be communicated to senior management and the board.

#### **2500 – Monitoring Progress**

The chief Audit executive must establish and maintain a system to monitor the disposition of results communicated to management.

2500.A1 – The chief Audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.

2500.C1 – The internal Audit activity must monitor the disposition of results of consulting engagements to the extent agreed upon with the client.

#### **2600 – Resolution of Senior Management’s Acceptance of Risks**

When the chief Audit executive believes that senior management has accepted a level of residual risk that may be unacceptable to the organization, the chief Audit executive must discuss the matter with senior management. If the decision regarding residual risk is not resolved, the chief Audit executive must report the matter to the board for resolution

Audit Name ...

Head of Audit Group....

Please send to the address: Internal Audit Unit [name and address]

# Chapter VIII

## **Quality Assurance Checklist for the staff of the Central Harmonisation Unit (Internal Audit)**

### Introduction

This section of the Internal Audit manual contains the Quality Assurance checklist and supporting guidance that will be used by the staff of the Central Harmonisation Unit (Internal Audit) to assess the quality of the work that has been undertaken.

As well as assessing the quality of the work, the Central Harmonisation Unit staff will also look to assess:

- Examples of good practice identified that can be shared with other Internal Auditors;
- Areas where the Internal Audit manual needs to be amended, clarified or enhanced;
- Details of common misunderstandings so that any training needs can be identified.

This section will only be used by Central Harmonisation Unit staff, but it is included here in the spirit of openness and transparency. Staff may find both the checklist and supporting guidance helpful in understanding the overall approach to Quality Assurance.

### Introduction

- In accordance with International Standard on Internal Auditing No. 1300 “Quality Assurance and Improvement Program”, the chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the Internal Audit activity. The International Standards on Internal Auditing require these arrangements to include both internal and external assessments. This guide can be used for both these quality assurance reviews.
- Quality Assurance refers to three separate activities:
- First activity is the on-going, day to day supervision and review of Internal Audit work. This is a routine part of undertaking an Internal Audit assignment and is conducted by more senior members of the Internal Audit team.
- Second activity is known as an essential review which is performed by another Internal Audit Director who reviews an assignment which has been assessed as high risk or where the findings are particularly significant. Such reviews are not common and will occur for only a minority of Internal Audit assignments.
- Third activity is a Quality Control Review. This is undertaken as an additional exercise to the ‘normal’ Internal Audit review work. A Quality Control Review is undertaken by staff that has had no previous involvement with the Internal Audit assignment. The Quality Control Review team can be either part of the Internal Audit Unit (an internal review) or from another organisation (an

external review). Regarding the external review there is a possibility that this review is audited from another audit organisation.

### **8.1 The objective of reviewing Internal Audit work**

The overall objective of the review process is to check that an appropriate amount of Internal Audit work has been undertaken and that this work meets the Standards set out in both the Ministry of Finance's Internal Audit Manual and also in the International Standards on Internal Auditing.

This is achieved by confirming that:

- Strategic and Annual Internal Audit plans have been prepared that are based on an understanding of the organisation being audited and the risks it faces. The plans should set out how and when the audits will be conducted and how sufficient appropriate audit evidence is obtained to enable appropriate conclusions to be drawn;
- The fieldwork has been performed in accordance with the approved Internal Audit plans and have resulted in sufficient appropriate audit evidence being obtained to support the audit conclusions and the findings and recommendations in the reports to the management of the organisation;
- The planning assumptions remain appropriate, taking account of any significant events occurring after the approval of these plans;
- All significant issues arising during the audit have been satisfactorily addressed; and
- The audit has been performed and reported in accordance with International Internal Auditing Standards and the Albanian Ministry of Finance's Internal Audit Manual.

### **8.2 The principle of review**

All working papers, audit reports and other communications with the organisation being audited must be reviewed by someone other than the person who prepared them (the preparer). This review work should be undertaken by a more experienced member of the Internal Audit Unit.

Reviews should aim to be constructive and aimed at improving the overall Standard of Internal Audit work rather than being overly critical.

### **8.3 Review and the Internal Audit quality assurance process**

Review is only one aspect of the financial audit quality assurance process. Direction and supervision are equally important elements in securing audit quality and all three are closely linked.

Direction involves ensuring that all members of the audit team have the appropriate skills to undertake the assignment, are aware of their responsibilities, the nature of the client's business and accounting and auditing issues that may arise. Audit planning is an important means of providing direction to audit staff. Directors play a key role in the development of the strategic and annual Internal Audit plans and are responsible for the approval of the assignment planning prior to the commencement of the detailed audit fieldwork.

Supervision includes considering the progress of the audit, ensuring that the audit work is being carried out in accordance with the audit plan and that significant issues arising during the audit are being addressed.

Effective direction and supervision will help to ensure that quality is built into audit processes from the outset and will in turn facilitate efficient and effective review.

### 8.4 The responsibilities for review

For all Internal Audit assignments, the responsibilities for review are as follows:

- The Team Leader is responsible for supervising the work of any assistants during the audit and for ensuring that the audit work is adequately documented. This includes the responsibility for ensuring the work is performed in accordance with the approved plans. An experienced Team Leader may also undertake detailed review under delegated arrangements.
- The Assistant Director is responsible for ensuring that a detailed review is performed.
- The Director is responsible for carrying out an overall review of the Internal Audit work.

### 8.5 Essential reviews

For all audits where the approved strategic and annual Internal Audit plans identify particularly sensitive areas or significant audit risks – or where major problems are identified during the course of the work – an independent Director should perform a review of the work that has been undertaken. This is known as a peer review should occur only in exceptional circumstances.

A peer review entails a review of the audit plans, the proposed audit report and selected working papers at the reviewer's discretion to provide additional assurance that the audit objectives have been achieved.

A Standards Assurance Review is performed by an independent Internal Audit Director who should be familiar with the auditing and reporting practices used and sufficiently objective not to be unduly influenced by the views of the Director responsible for the Internal Audit assignment.

The benefits of a peer review can best be realised when the independent

reviewer is designated as early as possible in the audit. This means that they are available for consultation at the audit planning stage, reviewing any interim work and consultation on matters as they arise during the conduct of the audit.

### **8.6 The Team Leader's review**

Effective review procedures require each member of the audit team to fully understand both their responsibilities as well as the roles of other members of the audit team. All members of the audit team are responsible for presenting the results of their work to a sufficient Standard to enable the next member in the review hierarchy to complete their role efficiently and effectively.

The Team Leader will usually review the audit work performed by the audit assistants as well as completing the bulk of the fieldwork, before presenting the completed audit file to the Assistant Director.

The Director is ultimately responsible for ensuring that all significant issues raised during the audit have been satisfactorily resolved and that the Internal Audit report accurately reflects the findings of the work.

### **8.7 The Assistant Director's detailed review**

The Assistant Director's detailed review is concerned with both the quality and the efficiency of the audit, and entails a review of:

- The audit plan;
- The results of audit procedures; and
- The audit report.

The detailed review should confirm that:

#### **For the audit plan**

- the issues included within the annual and strategic Internal Audit plans have been addressed during the detailed planning for the audit assignment;
- the proposed approach is consistent with the Internal Audit manual and International Internal Auditing Standards and will meet the objectives of the audit in an effective and efficient manner; and
- the attention of the Director is drawn to any matters that require resolution before the start of audit fieldwork or that require resolution by the Director during the audit.

#### **For the results of audit procedures**

- the work has been performed in accordance with the Internal Audit manual and International Auditing Standards;
- the work has been performed in accordance with the audit plan for this particular assignment;

- the planning assumptions remain appropriate, taking account of any significant events which are presented after the approval of the audit plan that have caused approved amendments to be made;
- the work performed is adequate in the light of results obtained and has been adequately documented, particularly in areas where professional judgment has been exercised;
- that appropriate consultations with the Director have taken place and that the results of such consultations have been documented, and that all significant matters have been raised for further consideration with the Director;
- The objectives of the audit procedures have been achieved; and
- The conclusions are consistent with the work performed.

### **For the audit report**

- The audit report follows the suggested structure in the Internal Audit Manual
- The audit report is well written, easy to follow and includes all of the issues identified during the Internal Audit assignment; and
- The recommendations are constructive, will address the identified weaknesses and been agreed by the management of the organisation being audited though the completion of the action plan.

The Assistant Director is also responsible for ensuring the completeness of the working papers. The Assistant Director should ensure that the relevant templates from the Internal Audit manual have been satisfactorily completed. The reviewer is responsible for ensuring that questions raised and points made during the review have been answered satisfactorily and documented in the working papers before the draft report is issued.

The Assistant Director's detailed review involves the consideration of the results of the audit procedures as they are recorded in audit working papers and ensuring that these are satisfactory. It also involves the more difficult task of identifying those aspects of the audit procedures that should be recorded in the audit documentation but which are not.

The review of audit working papers can be undertaken at various stages through the audit where this aids efficiency. The reviewers should however bear in mind that an important aspect of review is to consider the audit documentation as a whole, to ensure the completeness of the audit documentation but also to consider the consistency of the audit documentation with other information in the file. Reviewers should always remain alert to potential inconsistencies in the audit documentation and be prepared to conduct more in-depth review procedures or make further enquires of the audit team where such inconsistencies arise.

The Assistant Director may, in consultation and with the agreement of the Director, delegate aspects of the detailed review to the Team Leader.

In deciding whether to delegate review the Assistant Director and Director will consider:

- the skills and experience of the Team Leader;
- the nature and complexity of the audit and the organisation; and
- the assessment of audit risk.

The Assistant Director will continue to be responsible for ensuring that the objectives of review have been met in accordance with the basic principle of review but will not duplicate the work of the Team Leader. As with any other team member, Assistant Directors cannot review their own work.

It is important that the results of the Assistant Director's review are available to the Director, and the Assistant Director should also consider whether further explanation of the audit or the documentation for the benefit of the further reviews.

### **8.8 The Director's overall review**

The Director should consider the quality of the audit by performing an overall review of working papers. This review should be sufficient to ensure that the working papers contain sufficient appropriate evidence to support the conclusions reached and for the audit report to be issued. The Director cannot delegate the overall review to the Assistant Director or any other member of the audit team.

Although the review need not cover all working papers, in performing the overall review the Director will consider the following:

- the adherence to the audit plan for the assignment and its compliance with the annual and strategic Internal Audit plans;
- the documentation of the processes in place within the account area being reviewed;
- all critical areas of judgment, and the quality of audit evidence relating to high risk areas;
- compliance with the Internal Audit manual;
- any working papers prepared by the Assistant Director;
- the draft audit report; and
- any other areas which the Director considers important.

The extent of the review of working papers is left to the Director's judgment. In making such a judgment, the Director will consider, among other things, the complexity of the audit, our previous experience of the organisation, and the experience of the audit staff and Assistant Director along with his own involvement in the audit (e.g. in dealing with closing issues with the organisation).

Provided that there is an effective Assistant Director review, the Director's overall review will focus on the key matters outlined above. In these circumstances, the Director needs only review the detailed audit working papers if alerted to examine matters brought to his or her attention by the completion or detailed review documentation.

### 8.9 Quality Control Reviews

The main aim of the Quality Control Review (QCR) is to provide assurance that the Internal Audit work complies with professional standards and the guidance contained within the Internal Audit manual.

This requires the Quality Control Team (QCT) to be satisfied that:

- The audit has been properly planned and carried out;
- That audit judgements have been clearly recorded;
- That appropriate and sufficient evidence has been collected;
- That it has been properly evaluated and
- That the Internal Audit report is consistent with the findings audit findings.

Such reviews will help to ensure that all members of staff can learn from examples of good practice. It will help the Ministry of Finance prepare a training and development strategy to address any issues identified in the audit work carried out. The reviews will demonstrate to external bodies that the Ministry of Finance carries out its work in line with the international auditing standards.

### 8.10 Staff who should be part of the Quality Review Team

The reviews should be undertaken by knowledgeable and experienced staff independent of the audit being reviewed. The reviews should be conducted in a constructive manner and reports arising from them should deal only with significant matters and include recommendations for improvement and not just criticism of performance.

### 8.11 Methods that the Quality Review Team should use

The Ministry of Finance will need to ensure that the sample of audits selected for quality reviews are representative of the work undertaken. Each review should aim to complete the checklist at annex A. As this is the first time that the Ministry of Finance will undertake such Quality Control Reviews, the checklist annex A goes into a lot of detail.

It is normally good practice to meet with the audit team before commencement of the Quality Review process. The main purpose of the meeting should aim to cover aspects such as how was the audit planned, what were the issues arising from execution and how were they resolved and more importantly how these were reported to the organisation.

## **8.12 Outputs from the Quality Control Reviews**

The outputs from the quality review should be:

- Examples of good practice identified;
- Areas where the Internal Audit manual needs to be amended, clarified or enhanced;
- Details of common misunderstandings so that any training needs can be identified.

## **8.13 Reporting the results of the Quality Control Reviews**

After completion of the review, the Quality Review Team should provide the audit team with the results of the review and provide them with constructive guidance to improve the audits in the future.

On a wider scale, the results of the Quality Control Reviews should be reported in a summary form so that other audit teams could benefit as well. The results should include areas where the audit manual or supplementary guidance has not been correctly applied and provide actions to ensure that the correct application is applied in the future.

In the event of a disagreement between the reviewer and audit management, both should meet with the Director of the CHU to resolve the problem to the reviewer's satisfaction.

## **Annex A**

### **Suggested Checklists for Quality Review**

Each quality assurance review will need to assess the issues included within the detailed checklists as follows:

- Checklist One – Planning
- Checklist Two – Permanent files
- Checklist Three – Execution
- Checklist Four - Reporting

It is important for the comments box to be completed by each of the review teams. This will ensure that useful response (feedback) is provided to the audit teams and will also enable an overall assessment of the Internal Audit work to be produced. The reviewers should try not to treat the checklists as a simple 'Yes' or 'No' but should aim to assess the overall quality of the work that has been undertaken.

Checklist One – Strategic and Annual Planning

	Questions	Yes / No	Comments
1.1	Is there a separate file for the current year's planning?		
1.2	Is there an index at the start of the file?		
1.3	Does the index cover all of the contents of the file?		
1.4	Has the file been divided into sections (e.g. understanding the business, overall control environment etc.)?		
1.5	Have all working papers been numbered and cross referenced where necessary?		
1.6	Do the working papers record: Name of the organisation? Year being audited? Who undertook the work? The date on which the work was done? Reviewer name and date this review was done?		
1.7	Have the team undertaken a full assessment to understand the organisation?		
1.8	Has Standard Template 3 within the Internal Audit been properly completed and is there sufficient evidence to support the responses?		
1.9	Is there evidence that the Internal Audit team have engaged with the organisation's management as part of the planning process?		
1.10	Have all of the key issues been summarised on Standard Template 3 and is the audit response appropriate?		
1.11	Have all significant account areas been identified using Standard Template 4? Is there sufficient evidence to support this?		
1.12	Has Standard template 5 been completed with all of the issues identified in the planning stage?		
1.13	Have the available Internal Audit resources been calculated?		
1.14	Has a five year strategic Internal Audit plan been developed and does this appear reasonable?		
1.15	Has the annual Internal Audit plan been developed based on the five year strategic plan?		
1.16	Is there evidence that the strategic and operational IA plans have been agreed with the organization?		

**Quality Assurance Checklist for the staff of the Central  
Harmonisation Unit (Internal Audit)**

Checklist Two – Permanent Files

No	Question	Yes / No	Comments
2.1	Is there a permanent file for the organisation?		
2.2	Has the permanent file index within the Internal Audit manual been used?		
2.3	Have all papers on the permanent file been numbered and referenced?		
2.4	Does the permanent file contain all items referred to in the audit manual and are they relevant to the audit of the organisation?		
2.5	Is there evidence that the permanent file has been used?		
2.6	Is there evidence that the contents of the permanent file have been reviewed and that any out of date material has been removed?		

Checklist Three – Audit Execution

	Question	Yes / No	Comments
3.1	Is there a separate Internal Audit file for this account area and has the index within the Internal Audit Manual been used?		
3.2	Has a risk assessment for the account area being audited been completed?		
3.3	Is there sufficient evidence to support this risk assessment?		
3.4	Has an appropriate risk assessment been made for this account area?		
3.5	Has the overall control environment risk assessment been correctly combined with the risk assessment for this account area?		
3.6	Has the account area been clearly documented?		
3.7	Does the documentation appear to cover all of the steps within the account area?		
3.8	Has the systems documentation been checked using a walkthrough test?		
3.9	Has the adequacy of the design of the system been assessed?		
3.10	Has an audit programme been prepared for this account area? Has this been based on the strategic and annual Internal Audit plans for the organisation?		

3.11	Has the audit work been undertaken in accordance with the audit programme? Have all areas within the audit programme been covered?		
3.12	Are the working papers well cross referenced?		
3.13	Have the audit team obtained sufficient evidence to support their findings?		
3.14	Have the sample sizes been calculated in accordance with the guidance in the Internal Audit Manual?		
3.15	Has the audit work been subject to an appropriate level of review?		

#### Checklist Four – Audit Reporting

	Questions	Yes / No	Comments
4.1	Was a report issued after the conclusion of the fieldwork?		
4.2	Was the draft report issued to the organisation promptly?		
4.3	Did the report follow the structure set out in the Internal Audit Manual?		
4.4	Is there evidence that the report and the Internal Audit working papers were reviewed by the Director before the draft report was issued to the organisation?		
4.5	Have all of the issues identified during the audit been reported to the organisation?		
4.6	Is the report well written and in a style that will be helpful to the management of the organisation?		
4.7	Are the recommendations sensible and do they address the issues found during the course of the audit?		
4.8	Is there evidence that the report was discussed with the management of the organisation?		
4.9	Has an action plan been completed and is this included within the report?		
4.10	Was the final audit report issued to the organisation promptly?		

# Chapter IX

## Frequently Asked Questions

### Chapter 9: Frequently Asked Questions

This section covers a number of questions that may be asked by Auditors. It supplements the guidance contained in the first six sections of this manual.

#### ***What is the purpose of Internal Audit?***

In a small business, for example a bar, the owner or manager can control all of the activities and have an overview of what is going on.

In a large, complex organisation that employs hundreds – or maybe thousands of people – across a number of sites, this is simply not possible.

The management of entities such as this need some assurance that the organisation is operating properly and this is the service that Internal Auditors provide. They provide expert, independent assurance that the processes in place are both appropriate and operating effectively.

#### ***What areas should Internal Audit cover?***

Historically, Internal Auditors have restricted their work to the key financial activities or other systems such as income, payroll and the payments for goods and services etc.

Internal Auditors now cover a wider range of areas in addition to the key financial activities and look at systems such as: risk management, budgetary control and medium term financial planning. Internal Auditors can also look at key business systems for the organisation.

#### ***What is a risk?***

Definition

A risk is the possibility of an expected event that has an impact in the achievement of the organisation's objectives. Put simply, a risk is the chance of something going wrong. It may be something that could prevent an organisation meeting one of its key objectives or, at a lower level, something that means that an inappropriate payment is made.

#### ***What does risk-based Auditing mean?***

Auditors need to focus their efforts on areas where the need for their services is greatest. If there are two similar systems/ account areas but one is badly managed and one is well managed, the Auditors will want to spend more time on the account area that is badly managed. Equally, within an organisation Auditors will want to focus their efforts on those systems/ areas where the potential problems are the greatest.

#### ***What is meant by internal control?***

An internal control is something that the management put in place to either stop something going wrong or to find out if something has gone wrong. As

an example, to prevent a payment being made for goods that have not been received, the management require all invoices to be matched to a signed delivery note.

### ***What is meant by the overall control environment?***

The overall control environment assesses how well a business is managed. Auditors assess this once a year at the planning stage and consider things such as ethical values, staff competence and the approach to risk management.

### ***What is independence and why is it important?***

Organisational independence has to do with the position of the Internal Audit Unit in the organisation, which reports directly to the head of organisation.

Independence means that the Internal Audit staff is separate from the management of the entity. Whilst Internal Audit is part of the structure of an organisation, they are not responsible for any of its day to day activities. Whilst Internal Audit should make recommendations to improve things at an entity, they should not be involved in the direct running of an area.

For example, Internal Audit should not help implement a new system covering the payments for goods and services nor write the any of the organisation's procedure notes. Note changes

It is also important for Internal Audit to be seen as being independent so staff should not undertake Internal Audit work at entities where they have recently worked or where family members or close friends are employed in a senior capacity.

### ***What planning do IA need to do?***

The first thing that needs to be done is the preparation of internal audit strategic plan, which determines the work that is going to be done during next five years.

This is known as a strategic Audit plan and recognises that Internal Audit resources are scarce and that it is not possible to look at everything in one year. The strategic plan links the work that needs to be done with the resources that are available. To produce a strategic plan, you will need to have a good understanding of the organisation in terms of what it is trying to achieve, where its income comes from, what its expenditure is on and where the major risks are.

Sources of information will be business plans, budgets, Auditor's knowledge of the organisation and discussions with the entity's management.

Once the long term, strategic plan has been produced the Auditors should then produce an annual plan. This sets out in more detail the work that will be done in the next year.

### ***What is a system/ an account area?***

An account area means the systems and procedures that apply to a similar

group of transactions. For example, it doesn't matter whether an organisation is purchasing stationery or having a room decorated, as it will go through the same process for each item of expenditure. It will seek a number of quotes, make an order, receive an invoice for authorisation and finally make a payment.

### ***where does an Audit engagement start?***

The annual Audit plan will give you an idea of the work that is required. The first thing to do is to complete a risk assessment for the account area being audited. This can be combined with the overall control environment assessment to give a risk rating for the area being reviewed. The higher the risk rating, the greater the sample sizes. This means that we do more work in higher risk areas.

You then need to set out how the system works, check this using a walk-through test and then assess how effective this is likely to be. You will then need to test whether the internal controls are actually operating as intended and report your findings to the management of the entity.

### ***How long will each Audit take?***

This is impossible to answer! It depends on a number of factors, including the size and complexity of both the organisation being Audited and the area being reviewed as well as the scope of the review.

As a very rough guide, a review of an area such as risk management or budgetary control should take one person 1 to 2 weeks.

A review of a more complex area could take one person 3 to 4 weeks.

You will find that you will be able to save time in subsequent years as things such account area risk assessments and account area documentation can be re-used if there have not been any changes.

### ***Why do I need to spend so much time on planning?***

The time spent on planning is important as it will help ensure that the limited Internal Audit resources are used to their greatest effect. Without planning, Audit time could be wasted in inappropriate areas and auditing could be costly.

### ***Why do I need to document the account area being audited?***

Before you begin testing an area, you need to understand how it actually works and what internal controls should be operating. This is best done by producing a flowchart of the process from beginning to end. It is important for this flowchart to include every single stage of the process and not look to abbreviate the documentation by missing out stages or controls.

### ***What is a walkthrough test?***

A walkthrough test involves following one transaction through the entire process from start to finish. This serves two purposes. Firstly auditors make sure that the systems documentation is correct and secondly it checks that the internal controls expected to be in place do exist.

### ***How do I record my work?***

A separate Audit file should be produced for each Internal Audit assignment using the standard index within this manual. All working papers should have a unique reference number and working papers should be cross-referenced wherever possible.

### ***How much evidence do I need?***

There is no answer to this, except to say that it should be sufficient to support your Audit conclusions. If for example you are checking 20 invoices there is no need to take a photocopy of each one. You should, however, take a photocopy of the invoice if a problem has been identified.

Some items concerning an entity (for example detailed systems notes) will be held on your permanent files and there is no need to put copies of these on the individual assignment file as well.

If only 2 pages of a document are relevant, then just take copies of the pages rather than the whole document.

Your working papers should be clear enough to enable the original documents to be located again if necessary, so include invoice numbers, dates, location etc.

### ***What do I do if there is not enough time or resources to undertake an Audit?***

It is important for sufficient time to be allocated to each assignment. We plan Internal Audit work over a five year period to be able to devote enough time to each area.

There are a number of ways in which time can be saved, for example using written procedures notes produced by the entity to help with the system documentation or by producing a summary report to the entity covering the key issues found.

You can also alter the scope of the work – with Director's approval – to focus on the key areas of a particular area if there are pressures on the time that is available. It would be important for any work that is deferred to be rescheduled for another date.

### ***What reviews are needed?***

Reviews by a senior member of the Audit unit are required at various stages of the Audit process. The extent of the review will depend on a number of factors, including the risk and complexity of the system/the account area and the organisation being Audited as well as the experience of the Internal Auditors undertaking the work. As a minimum, a number of key pieces of work should be reviewed before the Audit work progresses to the next stage. These are: the calculation of the overall risk assessment for the system/ account area (high / medium / low), setting the scope of the work, producing the program of Internal

Audit work and producing the draft Internal Audit work. The detailed Internal Audit testing should always be reviewed before the draft report is issued to the management of the entity. This will ensure that the report has been properly written and is supported by Internal Audit work of an acceptable standard.

### ***How should I review someone's work?***

When reviewing an Audit assignment, the first question to ask is 'has the Audit unit performed all the work that was planned?'

If this is the case, you should then ensure that all of the work has been properly completed and check that the evidence supports the conclusions made by the Auditors. You should ensure that the unit have calculated the sample sizes correctly and that all working papers have been numbered and cross referenced.

You should also read the draft Internal Audit report and ensure that (a) all of the Audit findings are included and (b) that the recommendations are reasonable and will help the entity to improve the weaknesses that were identified.

### ***The Internal Audit legislation refers to systems based Audits, regularity Audits, performance Audits, financial Audits, IT Audits, advisory assignments and consultancy. What are these?***

A system based Audit is the type of Internal Audit work that includes evaluation of control systems that function at the organisation. This is the most effective type of Internal Audit work because, if the controls are operating as they were intended then both the Internal Auditors and the management of the organisation can take assurance from the controls.

Regularity Audits are single purpose Audits that have been designed to test whether the organisation complies with the relevant legislation in a particular area. The report to the management does not cover the general internal controls in a particular area, but simply confirms whether the legislation has been complied with. This type of Audit is rare as Internal Auditors normally cover compliance with the legislation as part of their other work.

A performance Audit looks at how well a service is delivered and whether it delivers value for money. This is done from a service user's perspective. For example, Internal Auditors could assess how good the public transportation is.

Could it be done more cheaply or could the service be done better for the same cost. Performance Audits usually involve comparing information about costs and service delivery with other similar organisations. Performance Audits are outside the scope of this Internal Audit manual.

A financial Audit involves forming an opinion on the yearend financial statements that have been prepared by an organisation. This type of work is not usually undertaken by Internal Auditors as it is a role of External Audit.

An IT Audit is an Audit that only focuses on the IT controls that are in place within an organisation. This can be an overview of all of the IT arrangements

in an organisation or be restricted to the IT controls in an accounting system. Although this manual covers some basic IT work, IT Auditing is a very specialised area and not all aspects of this auditing are covered by this Internal Audit manual.

An advisory assignment is a review of a particular account area to improve the controls that are in place. It is more restrictive than systems based Audit as it does not look to test the internal controls that are in place, but simply looks at the design of a system/ account area. It is similar to stage 6 of the Internal Audit work that is covered in section 3 of this manual.

Consultancy work is where Internal Auditors act in an advisory capacity to the management of the organisation. Care needs to be taken when agreeing to undertake this type of work so as not to compromise the independence of the Internal Auditors. It would be impossible for Internal Auditors to review a system/an account area in an objective way if he had been heavily involved in the design of that area.

### Glossary of Internal Audit Terms

**Account Area** – A group of financial transactions that are all subject to the same processes and controls. For example, paying staff salaries or collecting rental income will all be subject to the same internal procedure. An account area is also known as a 'system'.

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

**Adequate Control** - Present if management has planned and organized (designed) in a manner that provides reasonable assurance that the organization's risks have been managed effectively and that the organization's goals and objectives will be achieved efficiently and economically.

**Assurance Services** - An objective examination of evidence for the purpose of providing an independent assessment on governance, risk management, and control processes for the organization. Examples may include financial, performance, compliance, system security, and due diligence engagements.

**Board** - A board is an organization's governing body, such as a board of directors, supervisory board, head of an agency or legislative body, board of governors or trustees of a non-profit organization, or any other designated body of the organization, including the Audit committee to whom the chief Audit executive may functionally report.

**Charter** - The internal Audit charter is a formal document that defines the internal Audit activity's purpose, authority, and responsibility. Each Internal Audit Unit must have its own Charter. The internal Audit charter establishes

the internal Audit activity's position within the organization; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal Audit activities.

**Chief Audit Executive** - Chief Audit executive is a senior position within the organization responsible for internal Audit activities. Normally, this would be the internal Audit director. In the case where internal Audit activities are obtained from external service providers, the chief Audit executive is the person responsible for overseeing the service contract and the overall quality assurance of these activities, reporting to senior management and the board regarding internal Audit activities, and follow-up of engagement results. The term also includes titles such as General Auditor, head of internal Audit, chief internal Auditor, and inspector general.

**Code of Ethics**- The Code of Ethics of The Institute of Internal Auditors (IIA) are Principles relevant to the profession and practice of internal Auditing, and Rules of Conduct that describe behaviour expected of internal Auditors. The Code of Ethics applies to both parties and entities that provide internal Audit services. The purpose of the Code of Ethics is to promote an ethical culture in the global profession of internal Auditing.

**Compliance** - Adherence to policies, plans, procedures, laws, regulations, contracts, or other requirements.

**Conflict of Interest** - Any relationship that is, or appears to be, not in the best interest of the organization. A conflict of interest would prejudice an individual's ability to perform his or her duties and responsibilities objectively.

**Consulting Services** - Advisory and related client service activities, the nature and scope of which are agreed with the client, are intended to add value and improve an organization's governance, risk management, and control processes without the internal Auditor assuming management responsibility. Examples include counsel, advice, facilitation, and training.

**Control** - Any action taken by management, the board, and other parties to manage risk and increase the likelihood that established objectives and goals will be achieved. Management plans, organizes, and directs the performance of sufficient actions to provide reasonable assurance that objectives and goals will be achieved.

**Control Environment** - The attitude and actions of the board and management regarding the significance of control within the organization. The control environment provides the discipline and structure for the achievement of the primary objectives of the system of internal control. The control environment includes the following elements:

- Integrity and ethical values.
- Management's philosophy and operating style.
- Organizational structure.
- Assignment of authority and responsibility.

- Human resource policies and practices.
- Competence of personnel.
- The existence of agreed processes and procedures.

**Control Processes** - The policies, procedures, and activities that are part of a control framework, designed to ensure that risks are contained within the risk tolerances established by the risk management process.

**Engagement** - A specific internal Audit assignment, task, or review activity, such as an internal Audit, control self-assessment review, fraud examination, or consultancy. An engagement may include multiple tasks or activities designed to accomplish a specific set of related objectives.

**Engagement Objectives** - Broad statements developed by internal Auditors that define intended engagement accomplishments.

**Engagement Work Program** - A document that lists the procedures to be followed during an engagement, designed to achieve the engagement plan.

**External Service Provider** - A person or firm outside of the organization that has special knowledge, skill, and experience in a particular discipline.

**Fraud** - Any illegal act characterized by deceit, concealment, or violation of trust. These acts are not dependent upon the threat of violence or physical force. Frauds are perpetrated by parties and organizations to obtain money, property, or services; to avoid payment or loss of services; or to secure personal or business advantage.

**Governance** - 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.

**Impairment** - Impairment to organizational independence and individual objectivity may include personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations (funding).

**Independence** - The freedom from conditions that threaten objectivity or the appearance of objectivity. Such threats to objectivity must be managed at the individual Auditor, engagement, functional, and organizational levels.

**Information Technology Controls** - Controls that support business management and governance as well as provide general and technical controls over information technology infrastructures such as applications, information, infrastructure, and people.

**Information Technology Governance** - Consists of the leadership, organizational structures, and processes that ensure that the enterprise's information technology sustains and supports the organization's strategies and objectives.

**Internal Audit Activity** - A department, division, unit of consultants, or other practitioner(s) that provides independent, objective assurance and consulting services designed to add value and improve an organization's operations. The internal Audit activity helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes.

**International Professional Practices Framework** - The conceptual framework that organizes the authoritative guidance promulgated by the IIA. Authoritative Guidance is comprised of two categories – (1) mandatory and (2) endorsed and strongly recommended.

**Irregularity** – This refers to an act or omission that may have a financial consequence for the organisation.

**Must** - The Standards use the word “must” to specify an unconditional requirement. Where the word ‘must’ is used within this Internal Audit manual, it means that this action is mandatory for the Internal Auditors working in this particular area.

**Objectivity** - An unbiased mental attitude that allows internal Auditors to perform engagements in such a manner that they have an honest belief in their work product and that no significant quality compromises are made. Objectivity requires internal Auditors not to subordinate their judgment on Audit matters to others.

**Organisation** – This refers to the body that is being subject to Internal Audit work. Many organisations may be split into a number of different departments. The expression ‘organisation’ within this Internal Audit manual refers to the body that is in overall control. The expressions ‘organisation’ and ‘entity’ have the same meaning within this Internal Audit manual.

**Residual Risk** – The risk remaining after management takes action to reduce the impact and likelihood of an adverse event, including control activities in responding to a risk.

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

**Risk Appetite** - The level of risk that an organization is willing to accept.

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

**Should** - The Standards use the word “should” where conformance is expected unless, when applying professional judgment, circumstances justify deviation.

**Significance** - The relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors, such as magnitude, nature, effect, relevance, and impact. Professional judgment assists internal Auditors when evaluating the significance of matters within the

context of the relevant objectives.

**Standard** - A professional pronouncement promulgated by the Internal Audit Standards Board that delineates the requirements for performing a broad range of internal Audit activities, and for evaluating internal Audit performance.

**System** – A group of financial transactions that are all subject to the same processes and controls. For example, paying staff salaries or collecting rental income will all be subject to the same internal procedure. A system is also known as an ‘account area’.

**Technology-based Audit Techniques** - Any automated audit tool, such as generalized Audit software, test data generators, computerized Audit programs, specialized Audit utilities, and computer-assisted audit techniques (CAATs).

### ABBREVIATIONS

Abbreviation	Full Name
IA	Internal Audit
CHU/IA	Central Harmonisation Unit (for the Internal Audit)
IAU	Internal Audit Unit
IIA	Institute of Internal Auditors (international)
PIFC	Public Internal Financial Control