



Red Book & Internal Auditing

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CRMA

Course Objectives

1

Identify key requirements of the International Professional Practices Framework and related guidance from the Institute of Internal Auditors.

2

Understand the relationship between the internal audit function and the audited organization.

3

Recognize how the internal audit function helps an organization accomplish its objectives.

Topics

- **International Professional Practices Framework (IPPF)**
- **Generally Accepted Government Auditing Standards (GAGAS)**
- **Internal v. External Auditing**
- **Historical Perspective**
- **The Next Generation**
- **Elements of the Profession**
- **Three Lines Model**
- **IIA Value Proposition**
- **The Effective Internal Auditor**
- **How to Add Value**
- **7 Deadly Sins of Internal Auditing**

Passing the Exam...

Pay close attention and take extra notes wherever this symbol appears!





*Association of Inspectors General
Historic Carpenters' Hall
320 Chestnut Street
Philadelphia, PA 19106*

PRINCIPLES AND STANDARDS FOR OFFICES OF INSPECTOR GENERAL

- Statement of Principles
- Quality Standards for Offices
- Quality Standards for Investigations
- Quality Standards for Inspections, Evaluations, and Reviews
- Quality Standards for Audits

**MAY 2014
REVISION**



The AIG recommends that OIGs perform audits pursuant to one of the following:

1. Government Auditing Standards,
or
2. Standards for the Professional Practice of Internal Auditing

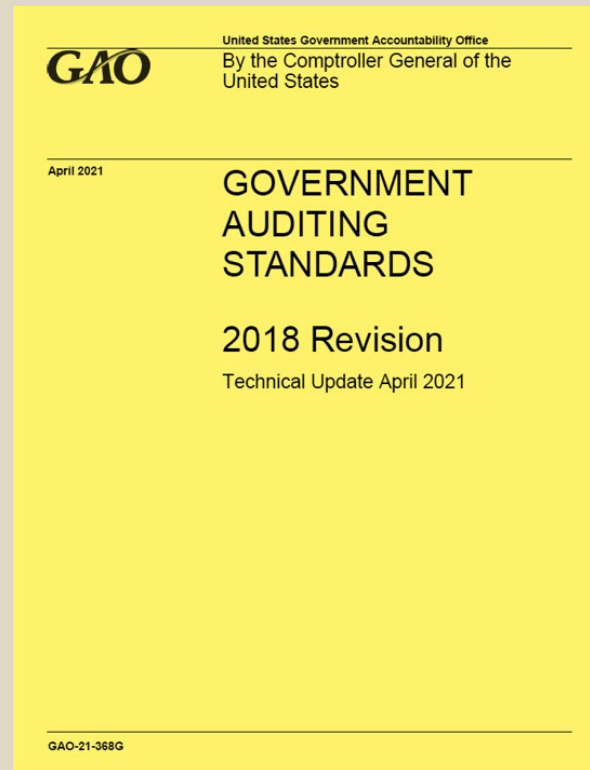


Issues the International Professional Practices Framework (Red Book)

International Professional Practices Framework (Red Book)

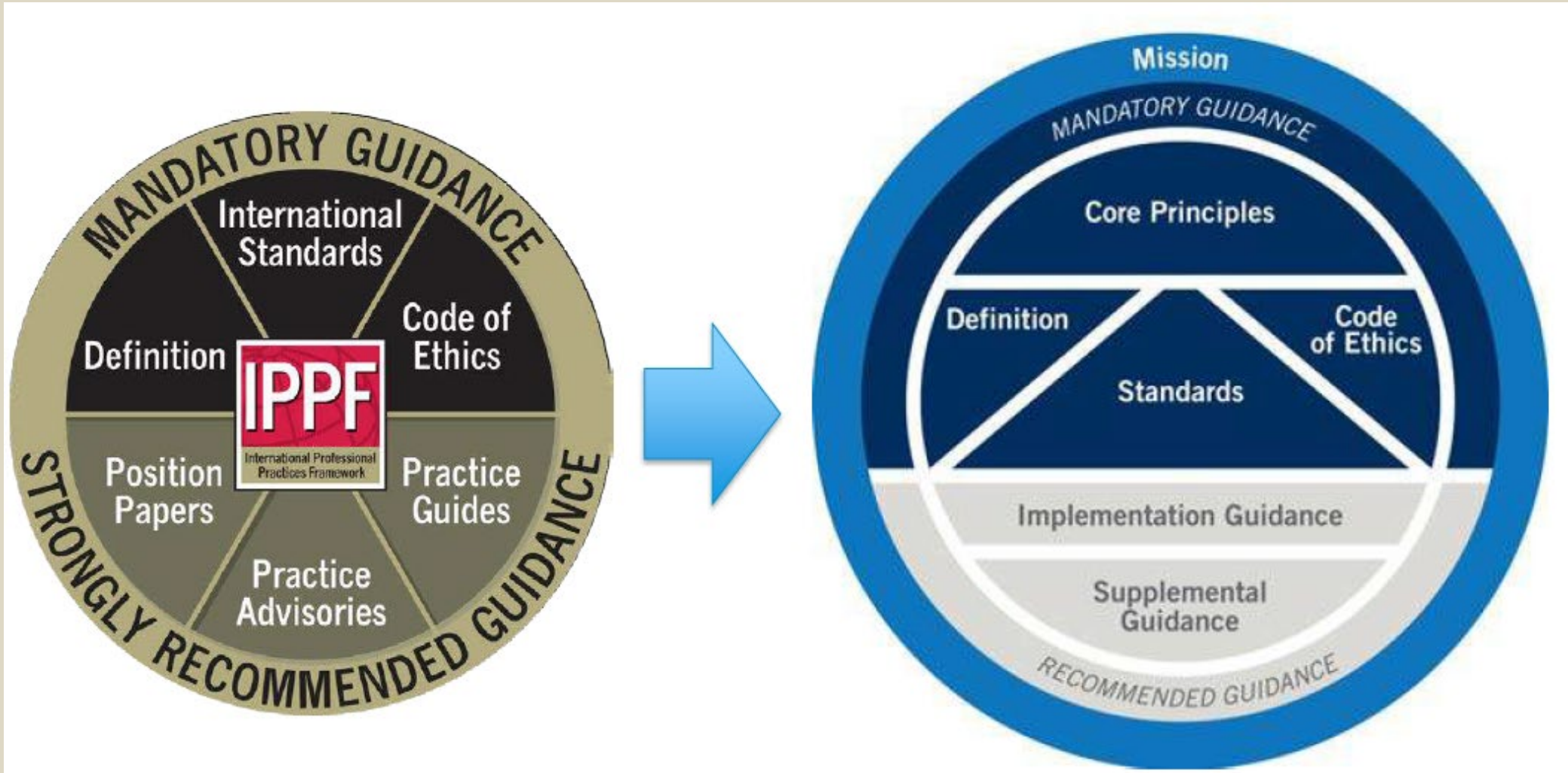


Generally Accepted Government Auditing Standards (Yellow Book)

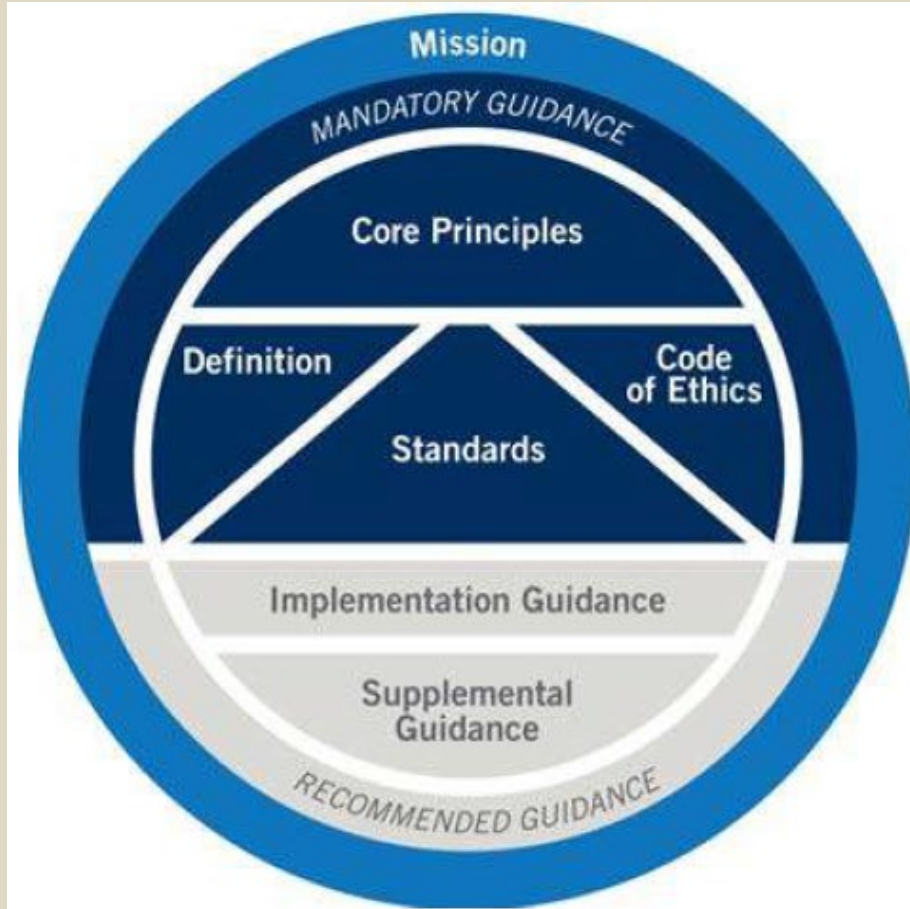


2011 Yellow Book updated in 2018, effective July 1, 2019 for performance audits and June 30, 2020 for financial audits

Red Book NEW AND IMPROVED!

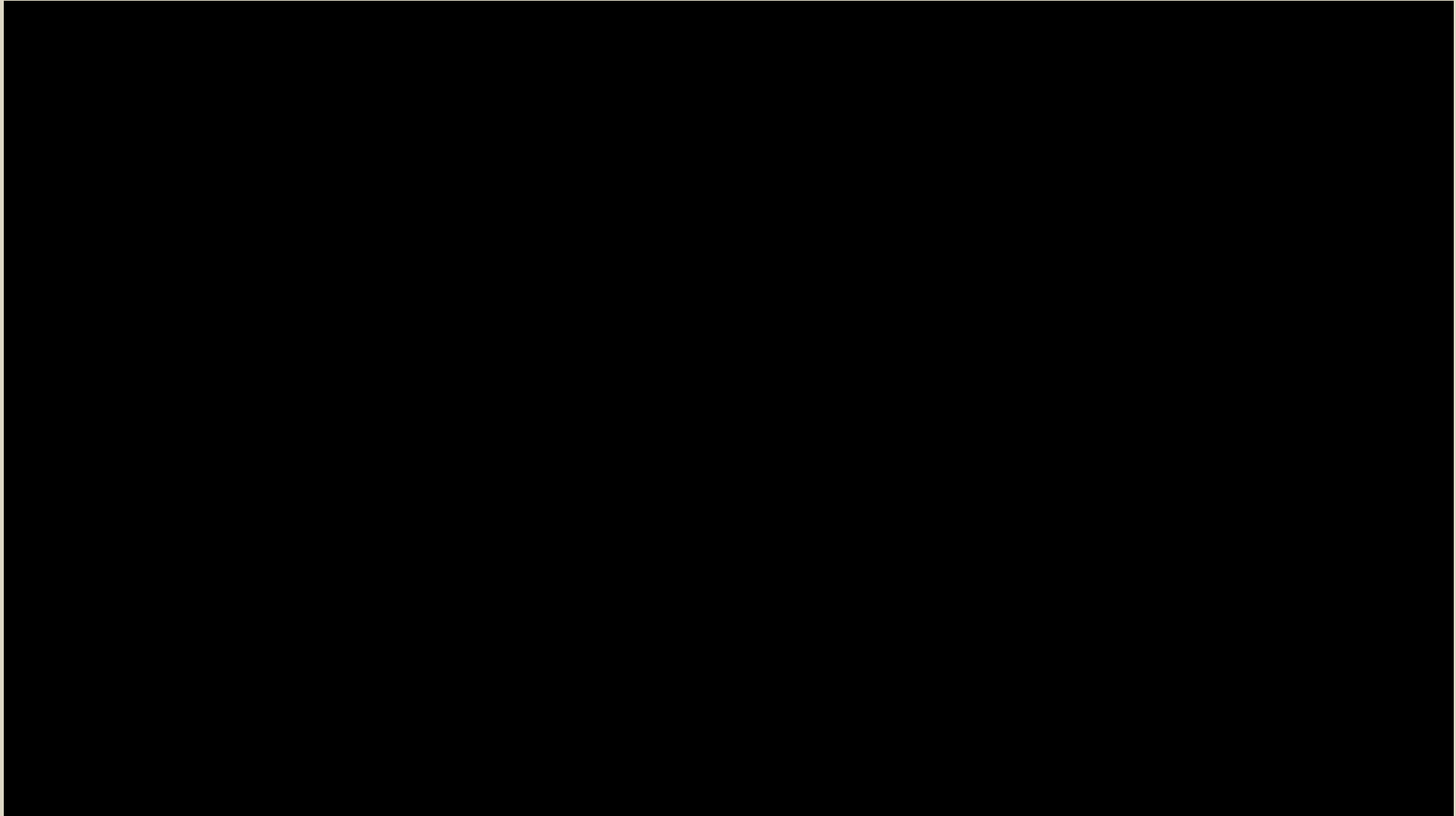


Red Book



- Launched July 2015
 - Introduced Mission.
 - Introduced 10 Core Principles.
 - Implementation Guides.

Effective Date – Jan 1, 2017



Red Book (Cont'd.)

Why Revise the Standards?

- The Standards must remain current, relevant, and timely for the profession
- The IPPF process requires that the Standards be reviewed at least once every three years
- Ongoing changes are a key component of the continued development of the IPPF

New IPPF introduced in 2015

- Included new mandatory guidance, the Core Principles for the Professional Practice of Internal Auditing.

IIASB reviewed relationship between the Standards and the Core Principles.

- Proposed changes better highlight the relationship.

Top Five Areas of Concern

Ranked by percentage of respondents expressing concerns.

Standard	Percentage
1112 Interpretation – Chief Audit Executive Roles Beyond Internal Auditing	14.3
2010 – Planning	11.5
1112 – Chief Audit Executive Roles Beyond Internal Auditing	10.2
1130.A3 – <i>implementation standard related to 1130 – Impairment to Independence or Objectivity</i>	10.2
2060 Interpretation – Reporting to Senior Management and the Board	9.7

Key Changes to the Standards



New standards address:

- Stakeholder expectations for Chief Audit Executive roles that have expanded over time.
- Potential objectivity-impairing situation of performing assurance role after previous consulting role.

Updates to existing standards clarify requirements:

- Relationship between new Core Principles, such as “Is insightful, proactive and future-focused,” and the Standards.
- Quality assessment and improvement program.
- Communications between chief audit executive, the board, and senior management.
- Scope of external quality assessment: must opine on conformance with the Standards and Code of Ethics.

Key Changes to the Standards

Updates to the Introduction:

- Clarify that the Standards, together with the Code of Ethics, encompass all Mandatory Guidance elements including Definition and Core Principles.
- Modifications to enhance the flow and clarify the Introduction.

Updates to the Glossary:

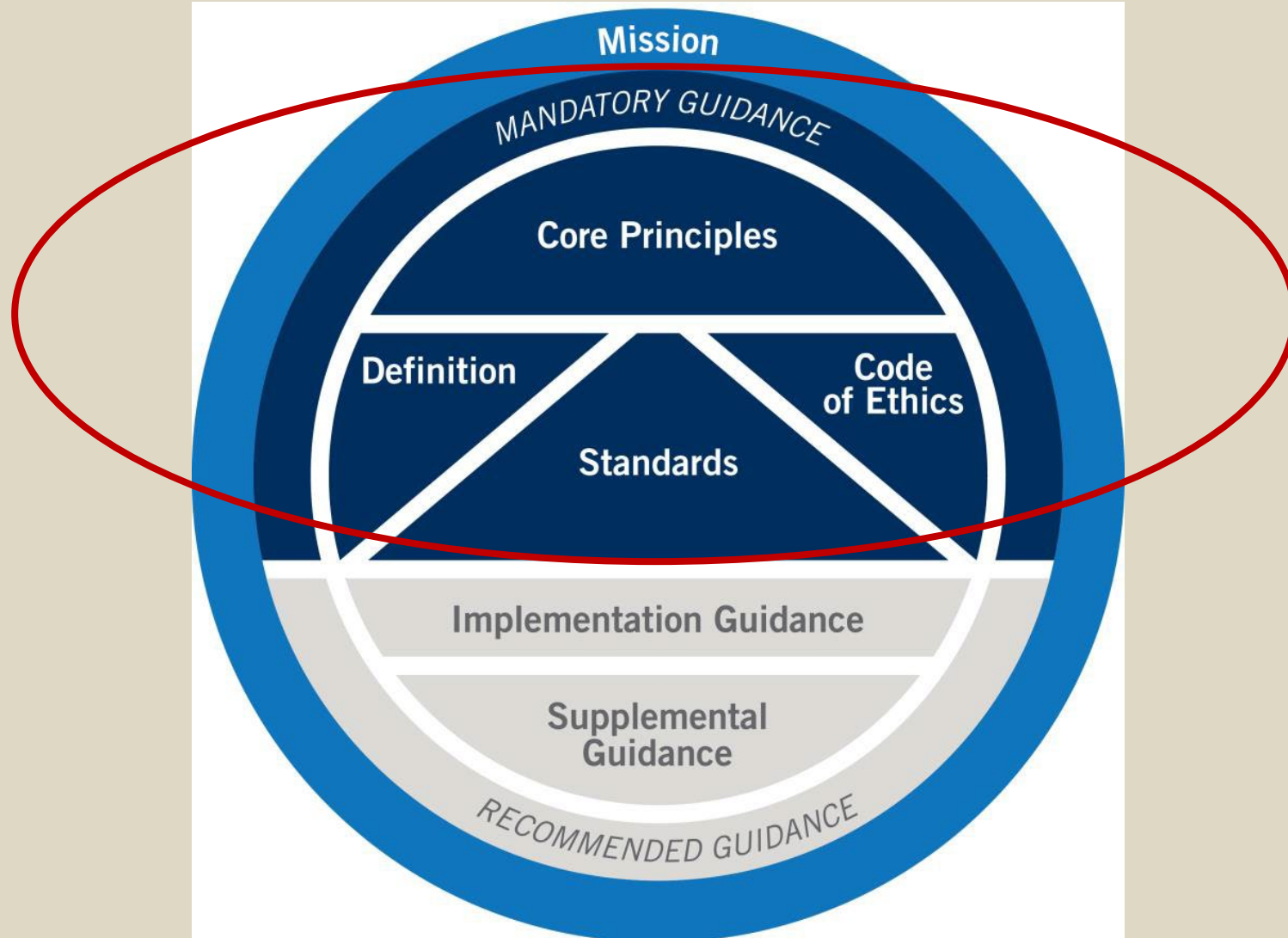
- Added definition of Core Principles.
- Modified definition of Board.
- Modified definition of IPPF.
- Modified definition of chief audit executive.

Mission



“To enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight.”

Mandatory Guidance



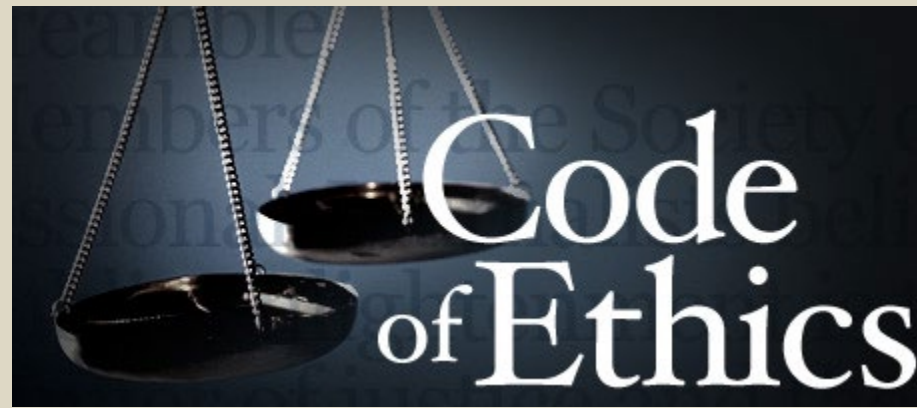
Core Principles

1. Integrity
2. Competence/Due Professional Care
3. Objective/Independent
4. Aligned with Organization
8. Position and Resources
6. Quality
7. Communicates Effectively
8. Risk-based Assurance
9. Insight and Foresight
10. Promotes Organizational Improvement



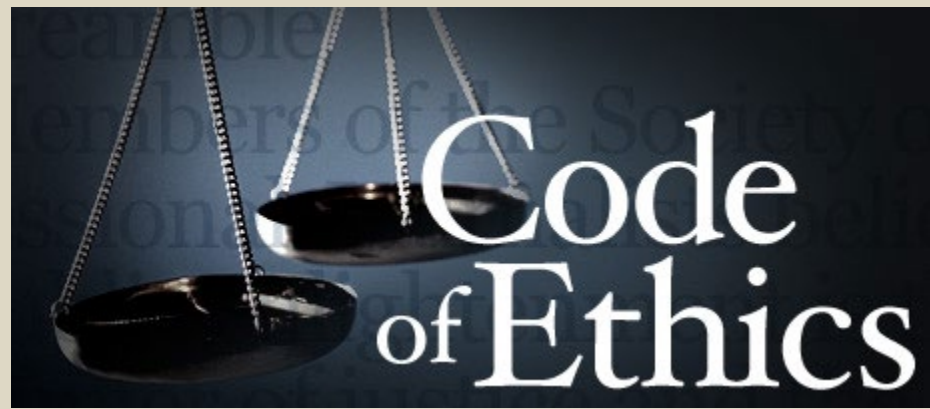
Definition of Internal Auditing

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.



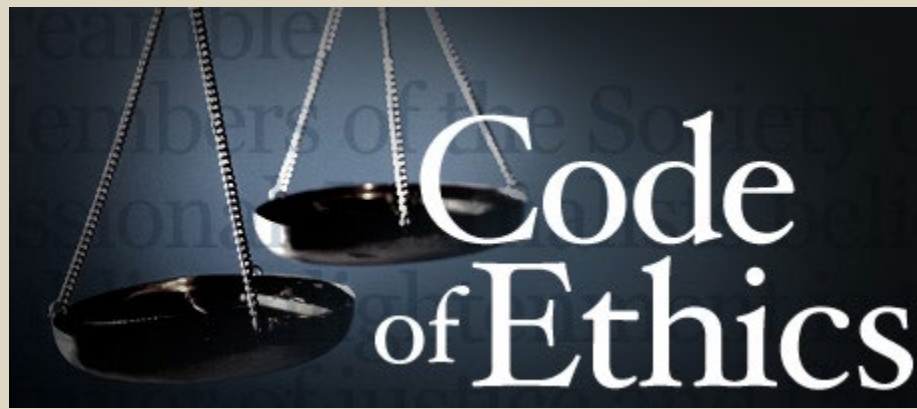
- **Two Essential Components**
- **Applies to both entities and individuals**
- **Promotes an ethical culture**
- **Compliance is mandatory**





Principles

1. Integrity – Establishes trust
2. Objectivity - Not unduly influenced
3. Confidentiality - Nondisclosure
4. Competency - KSAs



Rules of Conduct

Break down the four (4) Principles into applicable rules for internal auditors (“Shalls” and “shall nots”)

Internal auditors:

- **1.1 Shall perform their work with honesty, diligence, and responsibility**
- **2.1 Shall not accept anything that may impair, or be presumed to impair their professional judgment.**

The *Standards*



- Compliance is mandatory
- Applies to the individual internal auditor and the internal audit activity

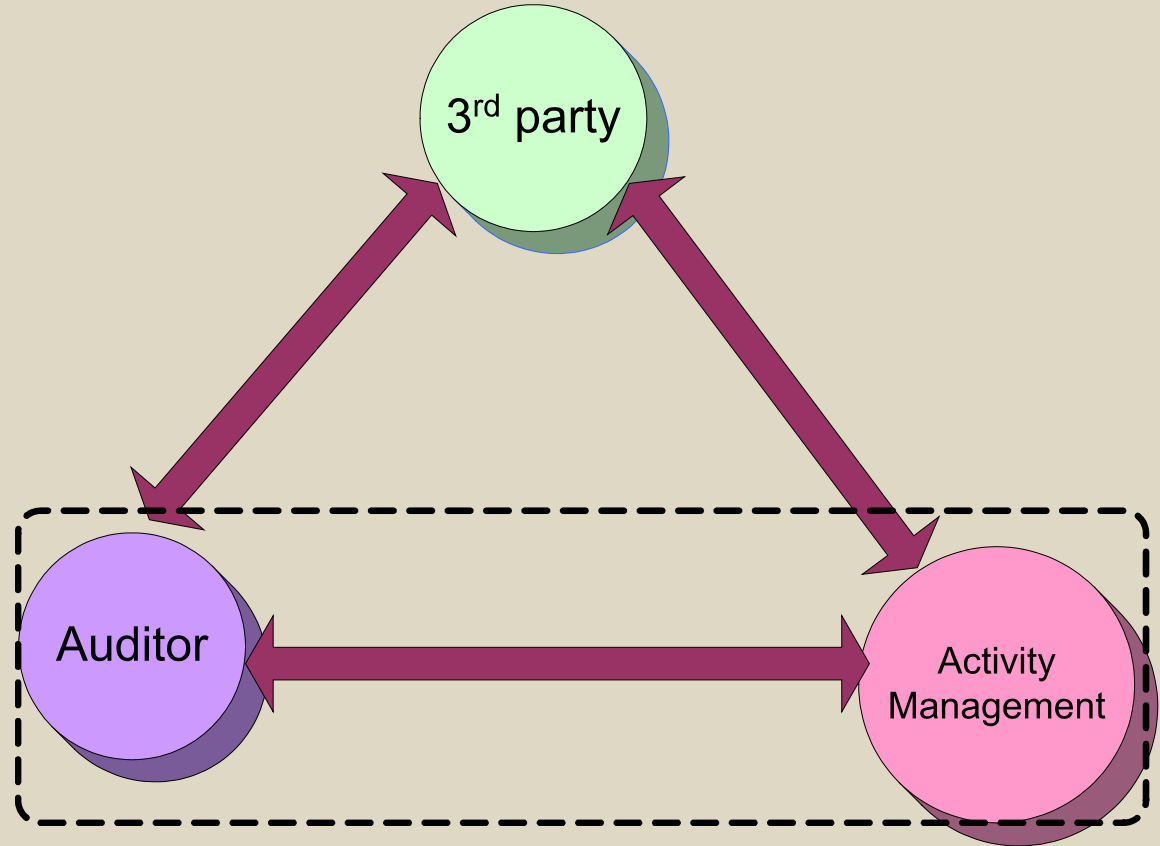


Assurance Services



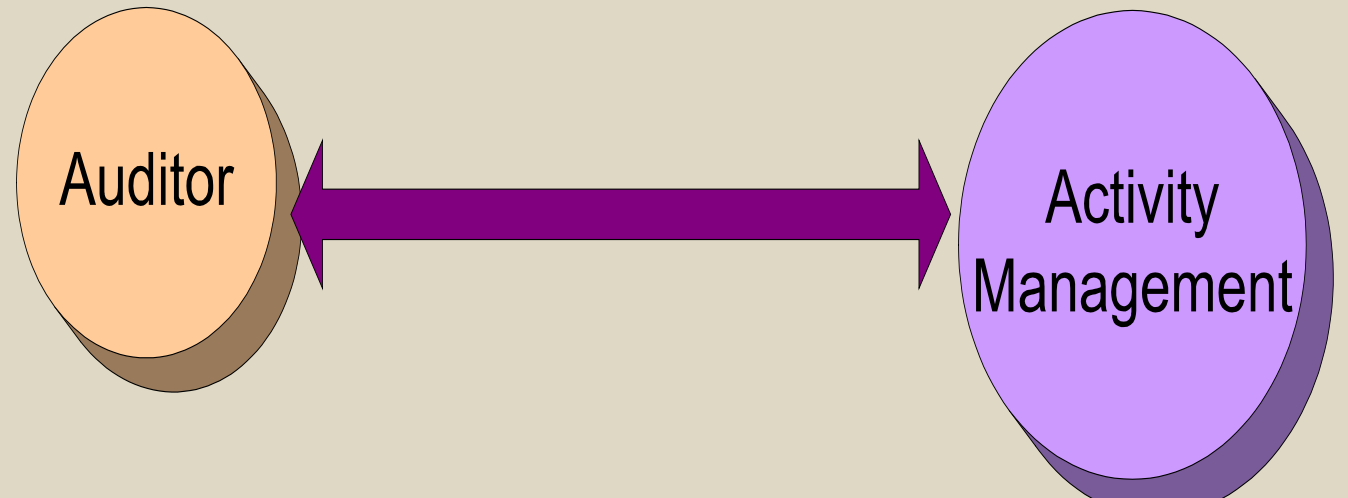
Include:

- **Financial**
- **Compliance**
- **Performance**



Consulting Services

- Internal auditors should NOT assume management responsibility
- Should maintain objectivity



The *Standards* Consist of

Attribute Standards

- Organization and Auditor

Performance Standards

- Audit work

Interpretations

- *Provide further clarity to terms and phrases*

Implementation Guidance

- *Provide more guidance based on the specific type of audit engagement (Assurance or Consulting)*

Standards Overview

Attribute Standards :



Performance Standards :



Key Terminology

- **Board** (*Organization's governing body*)
- **Chief Audit Executive (IG)** (*for Audit director*)
- **Engagement** (*specific assignment*)
- **Engagement Work Program** (*list of procedures for an engagement*)
- **Internal Audit (OIG) Activity** (*for department*)

Attribute Standards

1000 – Purpose, Authority, and Responsibility

- The purpose, authority, and responsibility of the internal audit (OIG) activity must be formally defined in an internal audit (OIG) charter.
- The chief audit executive (IG) must periodically review the internal audit (IG) charter and present it to senior management and the board for approval.



Attribute Standards (Cont'd.)

1100 – Independence and Objectivity

The internal audit activity (OIG) must be independent, and internal auditors must be objective in performing their work.

- *Organizational Independence*
- *Direct Interaction with the Board*
- *Chief Audit Executive (IG) Roles Beyond Internal Auditing*
- *Individual Objectivity*
- *Impairment to Independence or Objectivity*



Attribute Standards (Cont'd.)

1200 – Proficiency and Due Professional Care

Engagements must be performed with proficiency and due professional care.

- *Proficiency*
- *Due Professional Care*
- *Continuing Professional Development*

Attribute Standards (Cont'd.)

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 (OIG) activity.



Attribute Standards (Cont'd.)



1300 – Quality Assurance and Improvement Program (continued)

Internal Assessments

- *Ongoing internal monitoring*
- *Periodic*

External Assessments

- *Periodic*
- *Reporting of the Quality Assurance and Improvement Program*
- *Use of “Conforms with the International Standards for the Professional Practice of Internal Auditing” (OIG)*
- *Disclosure of Nonconformance*



Why Uphold Standards???

CREDIBILITY

CREDIBILITY

CREDIBILITY

CREDIBILITY

CREDIBILITY

CREDIBILITY

SOMETIMES IT'S THE LAW



Performance Standards

2000 – Managing the Internal Audit (OIG) Activity

The chief audit executive must effectively manage the internal audit (OIG) activity to ensure it adds value to the organization.

- *Planning*
- *Communication & Approval*
- *Resource Management*
- *Policies and Procedures*
- *Coordination and Reliance*
- *Reporting to Senior Management and the Board*
- *External Service Provider and Organizational Responsibility for Internal Auditing (OIG)*



Performance Standards (Cont'd.)

2100 – Nature of Work

- The internal audit (OIG) activity must evaluate and contribute to the improvement of the organization's governance, risk management, control processes using a systematic, disciplined, and risk-based approach.
- Internal audit (OIG) credibility and value are enhanced when auditors are proactive and their evaluations offer new insights and consider future impact.
 - *Governance*
 - *Risk Management*
 - *Control*

Performance Standards (Cont'd.)

2200 – Engagement Planning

Internal auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing and resource allocations. The plan must consider the organization's strategies, objectives, and risks relevant to the engagement.

- *Planning Considerations*
- *Engagement Objectives*
- *Engagement Scope*
- *Engagement Resource Allocation*
- *Engagement Work Program*

Performance Standards (Cont'd.)

2300 – Performing the Engagement

Internal auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement's objectives.

- *Identifying Information*
- *Analysis and Evaluation*
- *Documenting Information*
- *Engagement Supervision*

Performance Standards (Cont'd.)

2500 – Monitoring Progress

The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.



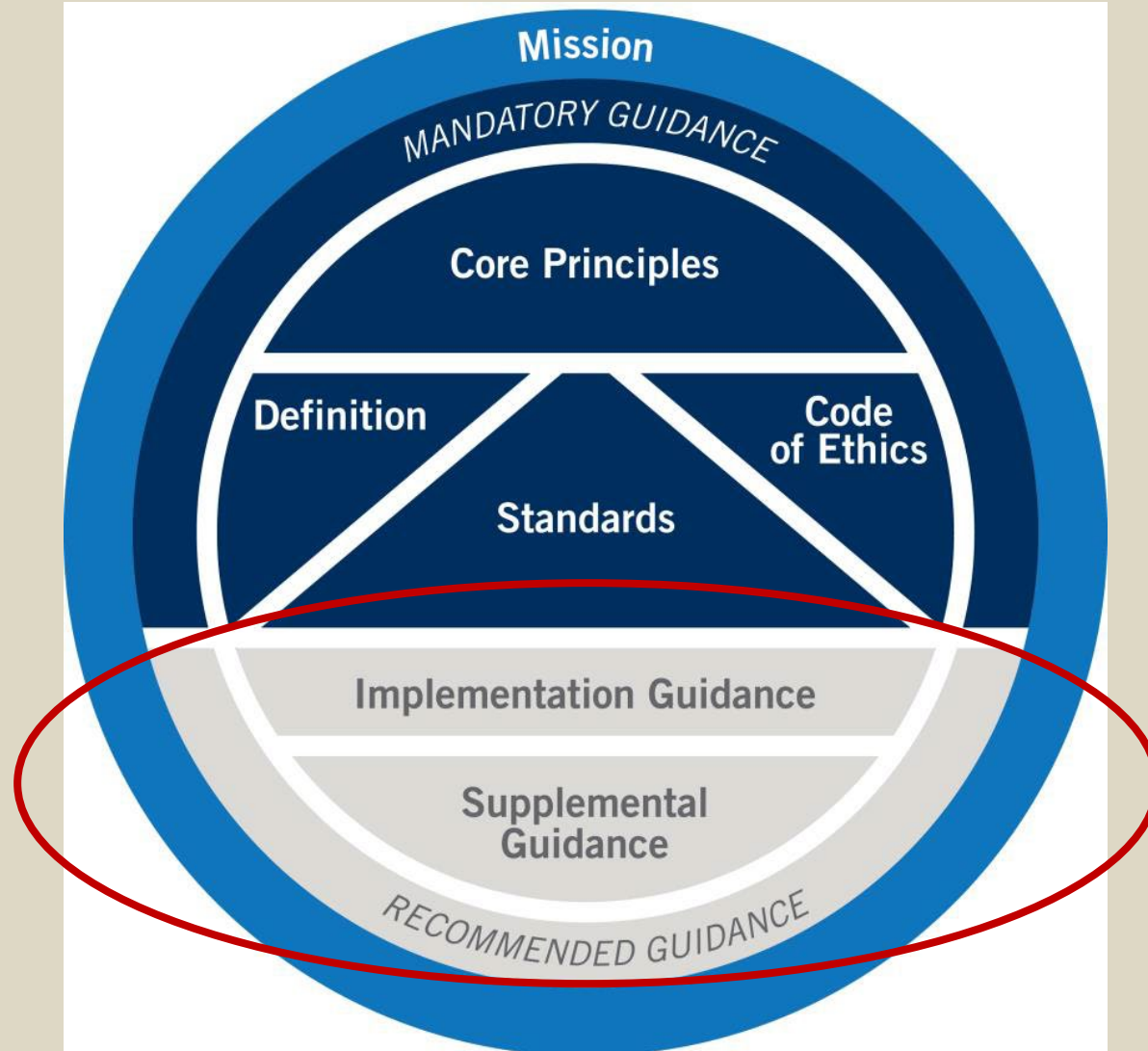
Performance Standards (Cont'd.)

2600 – Communicating the Acceptance of Risks

- When the chief audit executive concludes that management has accepted a level of risk that may be unacceptable to the organization, the chief audit executive must discuss the matter with senior management.
- If the chief audit executive determines that the matter has not been resolved, the chief audit executive must communicate the matter to the board.



Implementation Guidance



Implementation Guidance

- Provide more guidance based on the specific type of audit engagement (Assurance or Consulting)
- Begin with the letters “IG”



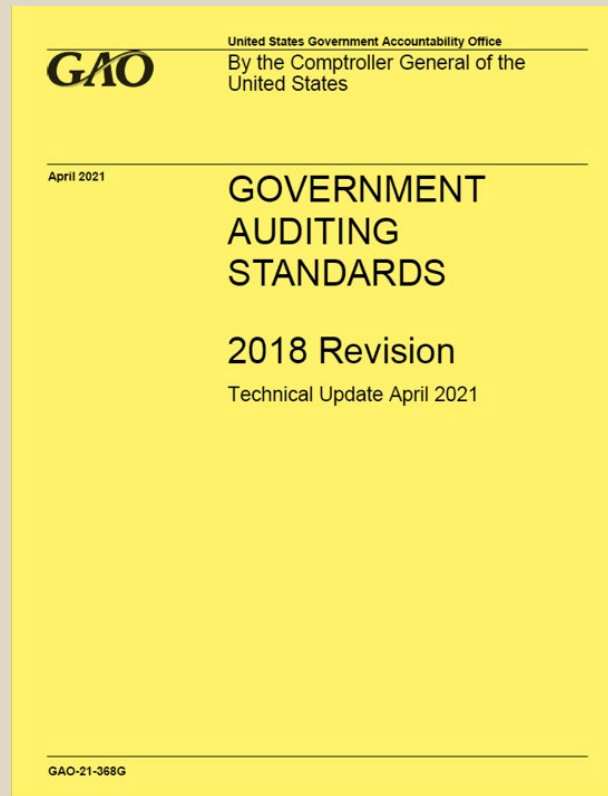
Supplemental Guidance/Practice Guides

- 11 Global Technology Audit Guides (GTAG)










- Additional Practice Guides will be issued regularly

Generally Accepted Government Auditing Standards (Yellow Book)

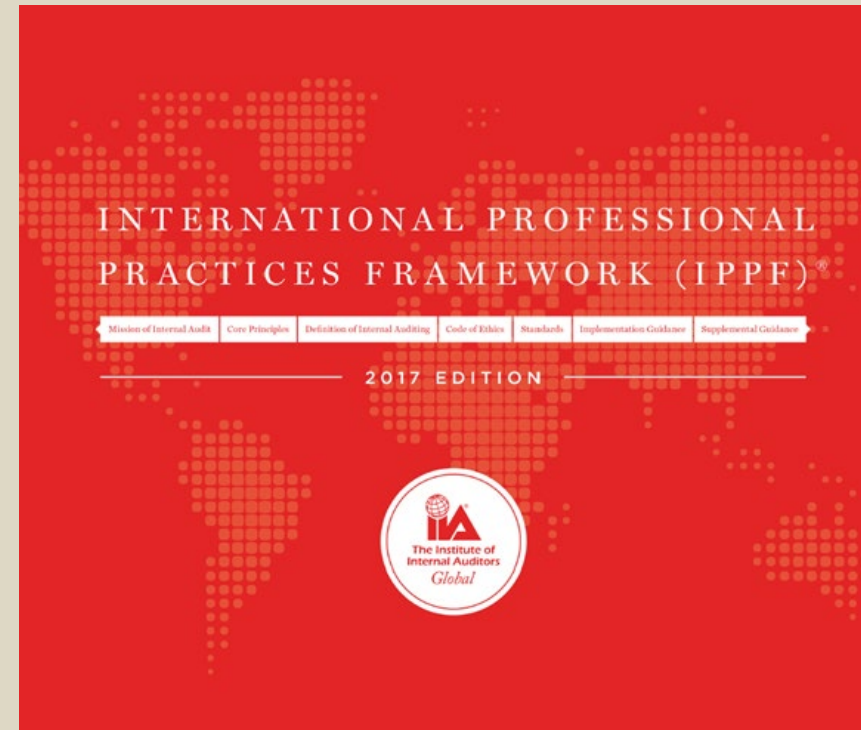
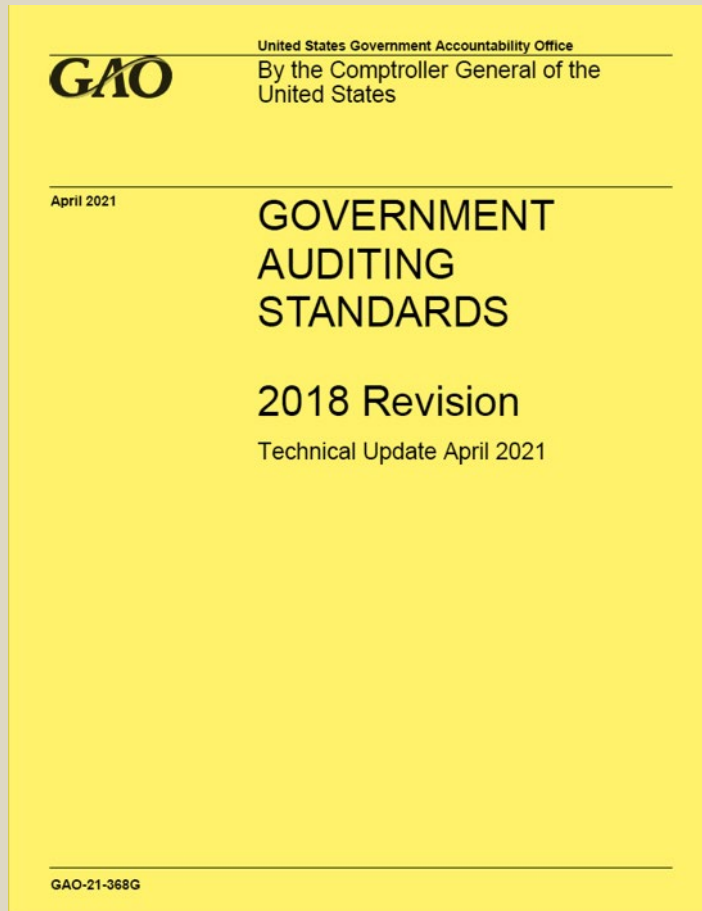


2011 Yellow Book updated in 2018, effective July 1, 2019 for performance audits and June 30, 2020 for financial audits

Yellow Book

-  Required for appointed federal inspectors general for audits of federal establishments, organizations, programs, activities, and functions (IG Act)
-  Required for audits of major executive branch departments' and agencies' financial statements (CFO Act)
-  Required for audits of executive agencies not subject to the CFO Act (The Accountability of Tax Dollars Act)
-  Required for audits of state and local governments and nonprofit entities that receive federal awards (Single Audit Act)
-  May be required by state and local laws
-  May be required by contract
-  May be required by federal audit guidelines for program requirements

Yellow Book and Red Book Comparison



Yellow Book Vs. Red Book

YELLOW BOOK	RED BOOK
AIG Recommended Standard	AIG Recommended Standard
Used both in the United States and in other countries voluntarily	Used both in the United States and in other countries voluntarily
Three types of engagements/audits: financial, attestation, and performance	Two types of engagements/services: assurance and consulting
Requires completion of 80 hrs. of CPE in every 2-year period.	Requires enhancement of knowledge, skills and other competencies through continuing professional development.
Non-financial program audits include processes, projects, studies, policies, operations, activities, entities, and functions.	Assurance services audits apply to the entity, operation, function, process, system, or other subject matter.

Internal Vs. External Audit

	Internal Audit	External Audit
Placement	Internal - Administratively part of organization (employees)	External - Independent body outside of the organization
Appointment	CAE Hired by board, audit committee, or senior executive (Administratively reporting to the organization's management structure to facilitate day-to-day operations)	Appointed by Organization stakeholders (Typically through the Audit Committee)
Responsibility	Operations, information technology, strategic initiatives, fraud investigations, process and control optimization, compliance, etc.	Financial statements, financial accounts, financial risks, etc.
Objectives	Engagements directed by annual, risk-based audit plan	Required – Statute, regulation, etc.

Internal Auditing—A Historical Perspective

- **Generations**
 - Pre-1980's
 - 1980's
 - 1990's
 - 2000's



A Historical Perspective (Cont'd.)

1st Generation
(Pre 1980's)
Controls
Start with existing processes, procedures and control activities
Audit for Compliance

A Historical Perspective (Cont'd.)

1st Generation	2nd Generation
(Pre 1980's)	(1980's)
Controls	Control Framework
Start with existing processes, procedures and control activities	Start with financial compliance risks
Audit for Compliance	Determine controls that should be in place. Audit for design, operational effectiveness and compliance

A Historical Perspective (Cont'd.)

1 st Generation	2 nd Generation	3 rd Generation
(Pre 1980's)	(1980's)	(1990's)
Controls	Control Framework	Risks
Start with existing processes, procedures and control activities	Start with financial compliance risks	Start with a thorough understanding of the organization and associated risks
Audit for Compliance	Determine controls that should be in place. Audit for design, operational effectiveness and compliance	Determine controls that should be in place. Audit for design, operational effectiveness, and compliance

A Historical Perspective (Cont'd.)

1 st Generation	2 nd Generation	3 rd Generation	4 th Generation
(Pre 1980's)	(1980's)	(1990's)	(2000's)
Controls	Control Framework	Risks	Enterprise-Wide Risk Management
Start with existing processes, procedures and control activities	Start with financial compliance risks	Start with a thorough understanding of the organization and associated risks	Start with a thorough understanding of the organization and associated risks
Audit for Compliance	Determine controls that should be in place. Audit for design, operational effectiveness and compliance	Determine controls that should be in place. Audit for design, operational effectiveness, and compliance	Determine the risk management process that should be in place to effectively manage the key risks. Audit for design operational effectiveness and compliance within each process

A Historical Perspective (Cont'd.)

1 st Generation	2 nd Generation	3 rd Generation	4 th Generation	The Next Generation
(Pre 1980's)	(1980's)	(1990's)	(2000's)	(2010 - ?)
Controls	Control Framework	Risks	Enterprise-Wide Risk Management	?
Start with existing processes, procedures and control activities	Start with financial compliance risks	Start with a thorough understanding of the organization and associated risks	Start with a thorough understanding of the organization and associated risks	?
Audit for Compliance	Determine controls that should be in place. Audit for design, operational effectiveness and compliance	Determine controls that should be in place. Audit for design, operational effectiveness, and compliance	Determine the risk management process that should be in place to effectively manage the key risks. Audit for design operational effectiveness and compliance within each process	?

The Next Generation

- **Risk-centric**
- **Technology**
- **Continuous Auditing**
- **Timely, Concise Reporting**
- **Assessing Operations**
- **Fraud Risk Assessments**
- **Accountability and Transparency**

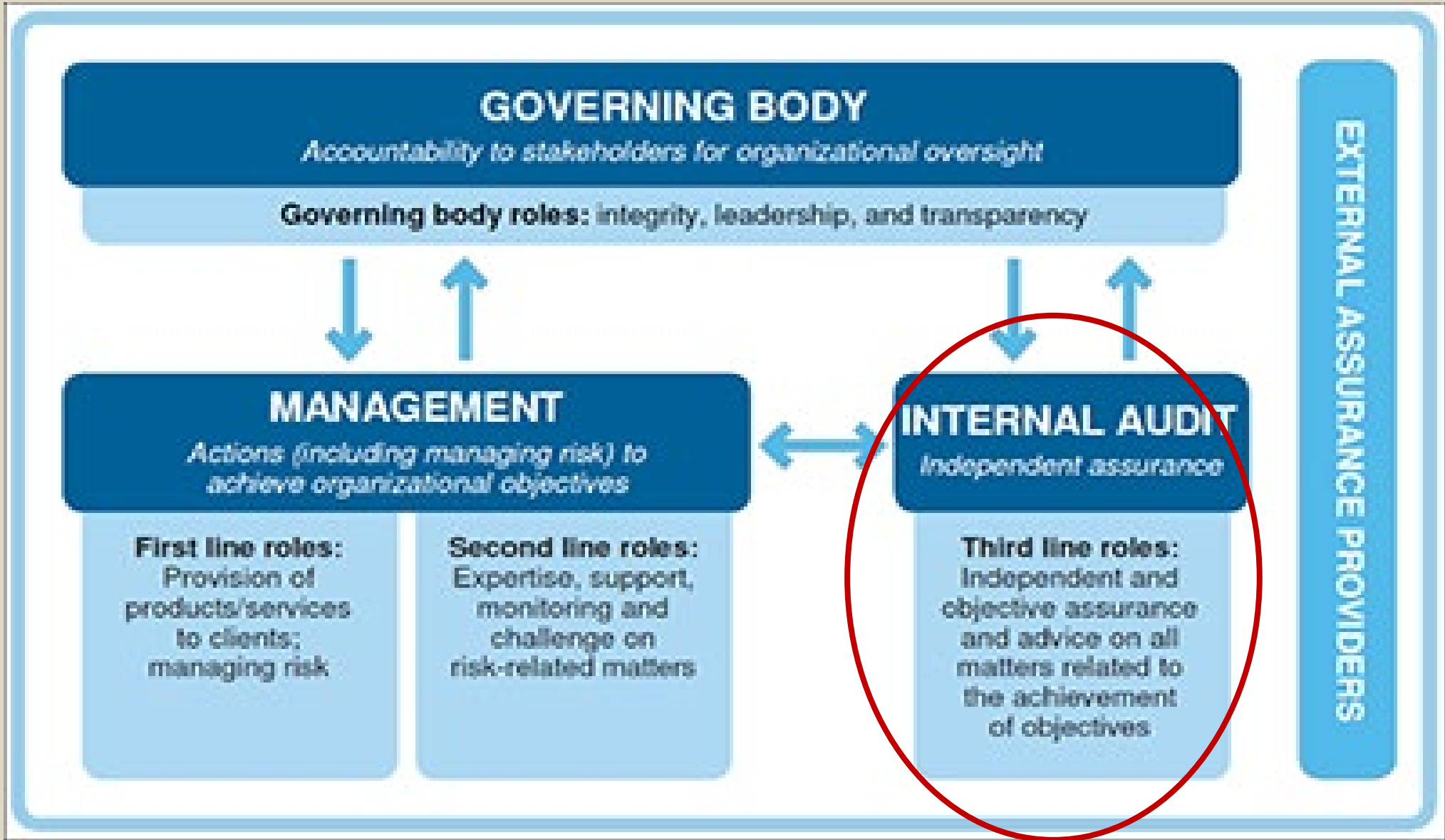
The Next Generation (Cont'd.)

- From Compliance Specialists to Strategic Advisors
- From Assurance Provider to Strategic Advisor
- Align Expectations, Build Capabilities, Deliver Quality and Increase Value

Elements of the Profession

- Initial Professional Education
- Skills/Professional Development
- Certification/Licensing
- Professional Associations
- Code of Ethics
- Organizational Certification





Source: IIA, Lake Mary, Fla. (July 20, 2020)

IIA Value Proposition

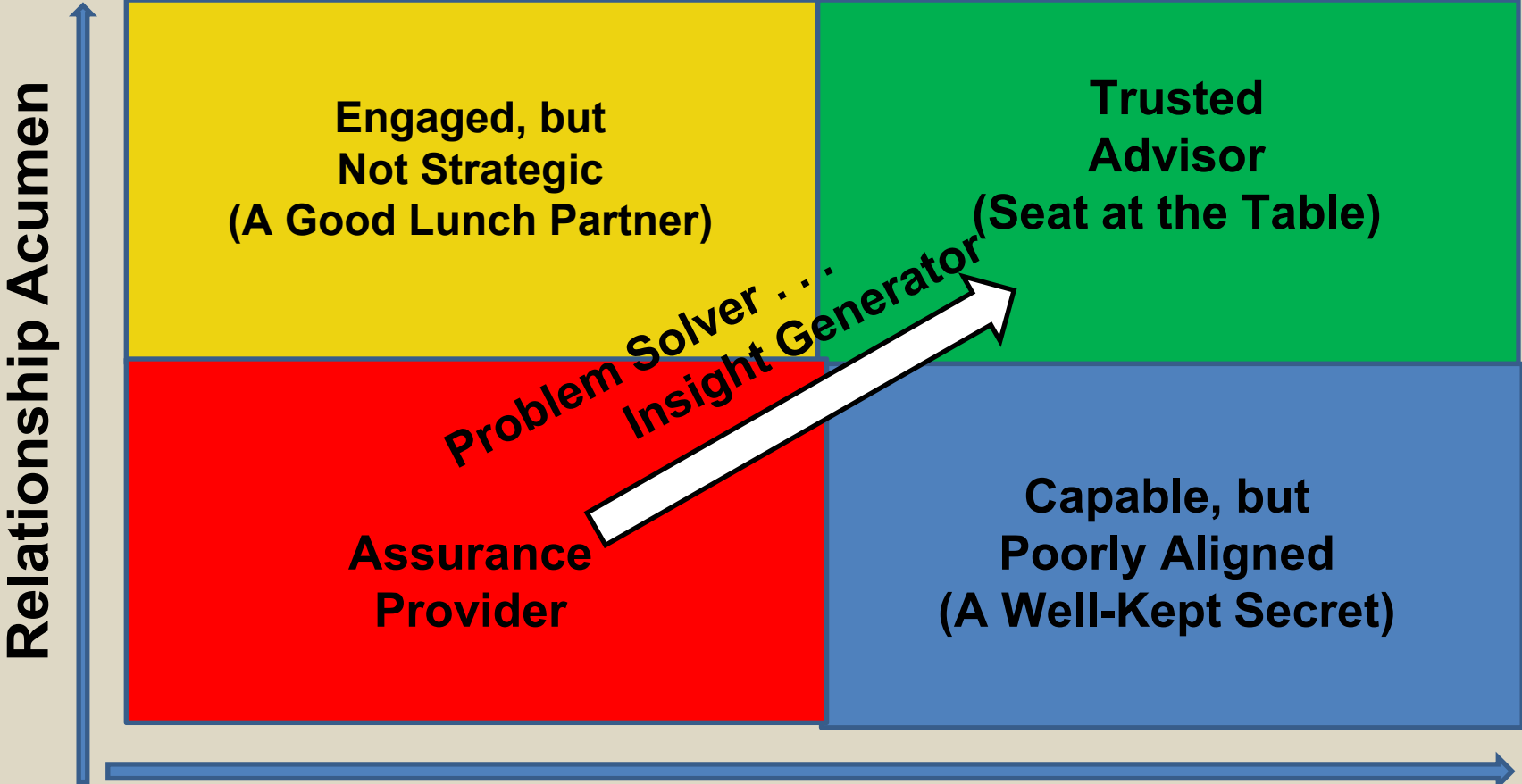




Results suggest that alignment of stakeholder expectations, and matching skills and capabilities to these expectations, helps internal audit enhance the value delivered to the organization.



Rising Shareholder Expectations



Risk, Control & Governance Expertise

"On internal audit, audit committees are still looking for greater value."

2015 Global Audit Committee Survey from KPMG's Audit Committee Institute

Trusted Advisor

$$\text{TRUSTWORTHINESS} = \frac{\text{Credibility} + \text{Reliability} + \text{Relationship Strength}}{\text{Self-interest}}$$



The Challenge



“There is no more enduring challenge for internal auditors than achieving and maintaining alignment with the expectations of our key stakeholders.”

Richard Chambers, Former President and CEO of the IIA, February 2015

Value Adding Factors

- Deep Knowledge of the Organization
- Courage to Innovate
- Creativity
- Broad Knowledge of Professional Practices



Value-Adding Characteristics

- 1. Extensive Staff Expertise**
- 2. A Challenging Work Environment**
- 3. Organizational Alignment**
- 4. Participative, Qualitative, Real-time Risk Assessment**
- 5. An Array Of Audit Services**

The Effective Internal Auditor

Technical Skills

- Auditing and Accounting Skills
- Industry Knowledge & Regulatory Awareness
- Financial and Information Technology Acumen

“Soft” or People Skills

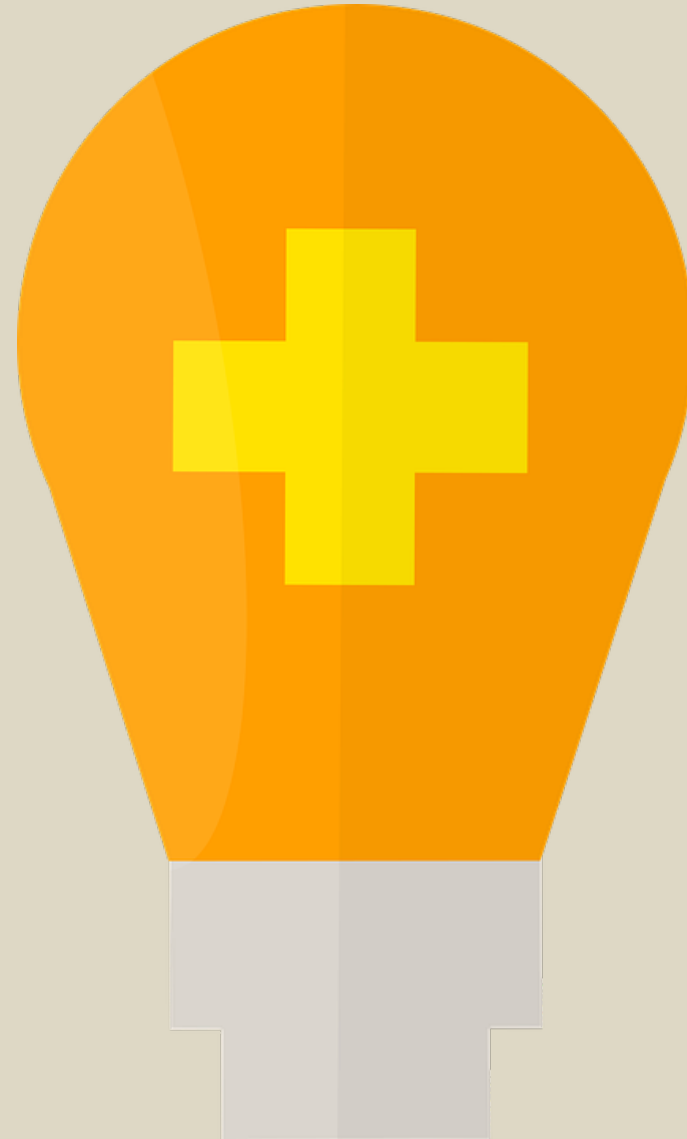
- Managing Employees
- Professional Image
- Conflict Resolution and Negotiation Skills

Value & Fit

- Understanding the value of Internal Auditing and how it fits in with the organization

Internal Auditors – Adding Value

- Relationships
- Business
- Judgment
- Competency
- Professional Development
- Attributes



Business

- **Strong Business Insight and Acumen**
- **Understanding the Business Context**
- **Knowledge of the Issues Facing the Organization**
- **Provide Management Information in terms of Dashboards not Rearview Mirrors**



Judgment

- Professionalism
- Due Professional Care
- Materiality
- Resource Utilization – Watch out for Scope Creep!

Competency

- **Diverse Skill Sets**
- **Experience**
- **Fresh Outlook – Deep Sense of Curiosity**
- **Results Oriented**
- **Certified**
- **Committed**
- **Focused**

Professional Development

- **Become Engaged in your Work and Profession**
- **Enhance your Skills through Education and Certification**
- **Become More IT Savvy**
- **Do Your Research**
- **Broaden Your Experience Base**

Attributes

- **Develop a Sense of Urgency Focused on Management Priorities**
- **Be a Team Player – Help Others Be Successful**
- **Recognize and Share Innovative Ideas and Practices**
- **Collaborate with Others**
- **Develop a Network – Before You Need It!**
- **Step Outside of Your Comfort Zone**
- **Volunteer – Identify a Need and Step Up!**

7 Deadly Sins of Internal Auditing

1. Ineffective Planning
2. Being Self-centered
3. Losing the Truth
4. Ineffective Communication
5. Failing Political Science
6. Inability to Negotiate
7. Destroying Credibility



Summary

1

Identified key requirements of the International Professional Practices Framework and related guidance from the Institute of Internal Auditors.

2

Understand the relationship between the internal audit function and the audited organization.

3

Recognize how the internal audit function helps an organization accomplish its objectives.

Resources

- The IIA – www.theiia.org
- ISACA – www.isaca.org
- AGA – www.agacgfm.org
- AIG – <http://inspectorsgeneral.org/>
- COSO – www.coso.org
- AICPA – www.aicpa.org
- AUDITNET – www.auditnet.org
- KnowledgeLeader – www.knowledgeleader.com



Questions? Comments?

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