

# INTERNAL AUDITING: ASSURANCE, INSIGHT, AND OBJECTIVITY



# WHAT IS INTERNAL AUDITING?

“**INTERNAL AUDITING**” – business people all around the world are familiar with the term. But do they understand the value it brings to their organizations? Exactly what is this somewhat illusive profession all about and why is it so essential to efficient and effective business operations? And why is it so critical to optimal governance and organizational sustainability?

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**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.

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Internal auditors have an in-depth understanding of the organization’s systems, processes, and culture. They provide assurance to executive management and governing bodies that governance processes are sound and that existing internal controls are adequate to mitigate risks. They also serve as consultants who evaluate emerging technologies, analyze opportunities, and offer recommendations for improvement.

All of this means that internal auditors assess whether things are going as they should in order for an organization to meet its strategic, financial, and operational goals, and to maintain an ethical environment and culture of accountability. Simply put, internal auditors bring enormous value to the organizations and stakeholders they serve.



## **INTERNAL AUDITING = ASSURANCE, INSIGHT, AND OBJECTIVITY**

Governing bodies and senior management rely on internal auditing for objective assurance and insight on the effectiveness and efficiency of governance, risk management, and internal control processes.

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### **INTERNAL AUDITING'S VALUE**

**ASSURANCE, INSIGHT, AND OBJECTIVITY** – the value of internal auditing can be described by these three very important words.

Management and governing bodies can look to their internal auditors to provide assurance on whether policies are being followed, controls are effective, and the organization is operating as management intends. Internal auditors have unique insight on which risks might lead to disaster; how to improve controls, processes, procedures, performance, and risk management; and ways to reduce costs, enhance revenues, and increase profits. And internal auditors view the organization with the strictest sense of objectivity that separates them from — but makes them integral to — the business.

Today's internal audit professionals bring to their organizations a broad range of backgrounds that

might include experience and education from outside of the finance and accounting fields. Many internal auditors come from operations, engineering, and information technology (IT), and they can serve in a variety of capacities. They are catalysts for solutions, best-practice advocates, risk and control experts, and quality-oriented efficiency specialists. They are the best resource available to management for assurance on the effectiveness and efficiency of governance, risk management, and internal control processes. And as a result of their insight, objectivity, and assurance, they are a safety net for management, the board, and the organization at large.

Although value can be viewed as a subjective quality, when it comes to internal auditors, subjectivity has no role to play. Executive management and boards of directors agree: Internal auditors are invaluable!



## ASSURANCE = GOVERNANCE, RISK, AND CONTROL

Internal auditing provides assurance on the organization's governance, risk management, and control processes to help the organization achieve its strategic, operational, financial, and compliance objectives.

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## MITIGATING RISKS

**MANY ORGANIZATIONS** achieve greatness through growth — and one of the keys to successful growth is effective risk management. As defined by The IIA's *International Standards for the Professional Practice of Internal Auditing*, risk management is “a systematic process for assessing and integrating professional judgments about probable adverse conditions or events.” Risk impacts an organization's ability to compete and to maintain its financial strength and quality of its products and services.

The skills internal auditors possess assist them in accurately identifying the risks an organization faces. As internal auditors analyze risks, they must investigate the sources, rank their severity, provide assurance that adequate controls are in place, and communicate their

findings to the organization. Changing trends impact the way an internal auditor assesses risk. Internal auditing has changed from a reactive, control-based activity to one that is risk-based and proactive which places greater emphasis on the internal auditor's role in mitigating and providing assurance over risk.

Internal auditors must be flexible to the changing business environment. Evaluating risk in a rapidly changing world means that internal auditors have to stay abreast of global and workplace issues such as mergers and acquisitions, emerging technology, and international commerce. By focusing on effective enterprise risk management, the internal auditor not only offers remedies for current trouble areas, but also anticipates problems or opportunities.

## TESTING CONTROLS

**INTERNAL CONTROLS** are actions taken by management, a governing body, and other parties to manage risk and increase the likelihood that objectives and goals will be achieved. As a part of control, organizations establish policies and procedures, as well as processes to ensure they are followed. Controls also help ensure the consistent adherence to the organization's ethical values and performance measures. Everyone within the organization plays an important role in internal control.

Internal control is at the very center of the internal auditor's world. It is also integral to effective organizational governance, and thereby is critical to management and the governing body. Internal auditors evaluate control efficiency and effectiveness and determine whether the controls in place are adequate to mitigate risks that threaten, or have the potential to threaten, the organization. Internal auditing's role in assuring internal controls are functioning as designed is essential to organizational governance and success.

## EVALUATING GOVERNANCE: SIMPLY GOOD BUSINESS

**ORGANIZATIONAL GOVERNANCE** comprises the procedures established by governing bodies to provide oversight of the risk and control processes administered by management.



According to The IIA and other thought-leading organizations, the four cornerstones of effective corporate governance are the governing body, executive management, internal auditing, and external auditing. When these entities work together well with healthy interdependence, internal controls are strong, reporting is accurate, ethics are maintained, oversight is effective, risks are mitigated, and investments are protected. Good organizational governance is simply good business.

## ASSURING COMPLIANCE

**COMPLIANCE** — conformity to fulfill obligations — ensures that organizations adhere to rules such as laws and regulations. Management's role is to implement policies and maintain extensive knowledge of the compliance requirements of all applicable laws, regulations, and contracts. When management fails to fulfill these obligations, the organization is subject to significant risk.

Part of an internal auditor's role is to review how well management meets the organization's compliance responsibilities. Specifically, internal auditors are responsible for reviewing objectives, providing insight into the impact that noncompliance would have to an organization, and informing senior management of significant noncompliance. They not only need to identify areas that do not comply with policies and guidelines, but also ensure that objectives set by management adhere to the organization's overall mission, vision, and goals.

Regulations in some parts of the world require those who manage and govern public companies to be legally responsible for financial statement accuracy. Internal auditors may assist them by evaluating the adequacy and effectiveness of controls throughout the organization. Their work includes an examination of the reliability and integrity of financial and operational information, the effectiveness and efficiency of operations, and the ways in which the organization safeguards assets and complies with laws, regulations, and contracts. Based on their findings, the internal auditors can provide assurance to management that financial statements are accurate.



## INSIGHT = CATALYST, ANALYSES, AND ASSESSMENTS

Internal auditing is a catalyst for improving an organization's effectiveness and efficiency by providing insight and recommendations based on analyses and assessments of data and business processes.

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### ANALYZING OPERATIONS

**WHEN AN ORGANIZATION** creates objectives and goals, it must follow the appropriate procedures to ensure those goals are achieved. Internal auditors review operations closely, assessing whether correct protocols are being followed and goals are met. This insight is vital to the organization's well-being.

Internal auditors assess whether assets in their organization are adequately protected and, if they are not, auditors make recommendations to ensure the risk of loss is appropriately mitigated. Assets are not just tangible items such as computers, printers, and copiers, but are also intangible items such as employees, IT, and knowledge management. Internal auditors must also be

able to evaluate the procedures used within operations to mitigate risks such as theft, fire, and illegal fraud or improper activities and make the necessary recommendations to reduce the likelihood and impact of these risks.

Today, internal auditors work more closely than ever with their customers. By doing so, they are more insightful in their recommendations and help the organization better achieve its objectives. As a valuable resource who provides insight into internal processes and operations, the internal auditor continues to provide value in analyzing organizational operations.

## ASSESSING EFFICIENCY AND EFFECTIVENESS

**INTERNAL AUDITORS** strive to provide value in addressing the challenges organizations face and constantly enhance their skills and knowledge. They must thoroughly understand the business, industry and objectives of their organization and have the ability to assess its efficiency and effectiveness.

Organizational resources are valuable. It's in the organization's best interest to defend and guard them against potential waste. By reviewing the controls (policies and procedures) in place, internal auditors can evaluate whether efficiencies are being recognized, and by making suggestions, internal auditors constantly add value to the organization. This means today's internal audit professional can vastly impact the efficiency and effectiveness of operations throughout the organization.

## BEING A CATALYST FOR IMPROVEMENT

**COMPETENT**, professional internal auditors accurately interpret facts and figures of organizational processes and serve as catalysts for continuous improvement and for bringing various areas together to address challenges facing the organization. A key attribute of effective internal auditors is the desire and commitment to improve or change anything found to be deficient within the organization. Further, they must influence and persuade others to improve.

After evaluating processes, internal auditors report their findings and recommend appropriate courses of action. By developing a strong relationship and partnership with management and the governing body, internal auditors can submit recommendations that are the starting point for the enhancement of risk management, internal control, and governance. Through a strong commitment to the organization's values and goals, internal auditors' understanding of the entire enterprise plays a crucial role in the overall success of the organization.





## OBJECTIVITY = INTEGRITY, ACCOUNTABILITY, AND INDEPENDENCE

With commitment to integrity and accountability, internal auditing provides value to governing bodies and senior management as an independent source of objective advice.

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### ESTABLISHING OBJECTIVITY AND INDEPENDENCE

**INTERNAL AUDITORS** pave a path toward continuous improvement by providing objective and independent advice to all levels of management. As such, independence and objectivity are two of the most critical components of an effective internal audit activity. Internal auditors occupy a unique position as they are employed by the organization, but are expected to review the conduct of its management.

This could be viewed as a conflict of interest. Therefore, to ensure their independence, The IIA suggests the chief audit executive (CAE) has a dual reporting relationship. For day-to-day administrative purposes, the CAE should report to the most senior executive, ideally to the chief executive officer (CEO) of the or-

ganization. Administrative reporting typically includes responsibilities such as budgeting and management accounting, and administration of the organization's internal policies and procedures. For functional purposes, the CAE should have a direct reporting line and unrestricted access to a governing body - such as an audit committee of a board of directors - which provides direction, enables full support and access to organizational resources, and ensures there is no impairment to independence. This reporting relationship allows for open communication without fear of reprisal or interference, and sets the stage for honest, straightforward feedback. It also allows the internal auditors to raise red flags, draw attention to concerns, and engage in further investigation as warranted.

Internal auditors must also maintain the attribute of objectivity while performing engagements. The internal auditor should have an impartial, unbiased attitude and avoid conflict of interest situations that may impair judgment. To help achieve objectivity, internal auditors should not assume any of management's operational responsibilities.

## EMBRACING THE PRINCIPLES OF INTEGRITY AND ACCOUNTABILITY

**THE ORGANIZATION'S** internal controls should not be viewed as something to be considered only by those in management. Each employee throughout the organization should understand the importance of a collective consciousness about, and accountability for, a strong system of internal control, an unwavering code of ethics, and high standards of excellence. More than just a philosophy, the desired state of an organization's culture requires the active agreement and participation of all its employees (or associates).

Few attributes are more critical to internal auditors than integrity, accountability, and unwavering ethical conduct. Effective internal auditors are grounded in professionalism, well-disciplined in their work, and subscribe to a professional code of ethics. Uncompromising ethics, the ability to listen with an open mind, and the strength and integrity to be firm under pressure are attributes that enable internal auditors to stand up and advise an organization what it sometimes does not want to hear.

With a holistic view of the entire organization and its wide range of risks, internal auditors are in a unique position to help executive management and the governing body ensure that the corporate culture is ethical. They assist management by making recommendations for improving and maintaining an ethical corporate culture, and play an important role in helping management achieve organization-wide agreement and participation in creating the desired ethical culture.



## THE VALUE OF PROFESSIONALISM

**THE VALUE** of internal auditing cannot be fully realized without very important requisite qualities possessed by absolute professionals. Internal audit professionalism means competence and quality. It means standing up for transparency and integrity and speaking out against unethical business practices. And it means embracing growth and change, seeking new ways of doing things, and providing fresh ideas for ensuring risks are mitigated. To be effective and provide the utmost value, internal auditors should make a commitment to professionalism by:

- Practicing in accordance with the *International Standards for the Professional Practice of Internal Auditing* and other guidance within the International Professional Practices Framework.
- Ensuring quality practices by maintaining an ongoing Quality Assurance and Improvement Program, including periodic internal and external quality assessments.
- Gaining a thorough understanding of their organization's business and culture.
- Taking advantage of ongoing professional development and membership opportunities offered by organizations such as The Institute of Internal Auditors.
- Earning professional designations such as the Certified Internal Auditor (CIA), Certified Financial Services Auditor (CFSA), Certified Government Audit Professional (CGAP), and the Certification in Control Self-Assessment (CCSA). The CIA designation is the only globally accepted certification for internal auditors and remains the standard by which individuals demonstrate their competency and professionalism in the internal auditing field.

## THE VALUE PROPOSITION TO STAKEHOLDERS

**THE INSTITUTE OF INTERNAL AUDITORS** challenges internal auditors around the world to continuously enhance their competencies as professionals, and encourages stakeholders to enthusiastically incorporate internal auditing into their organization's governance structure.

Internal auditing is a profession, and the responsibilities described here represent only a part of what is mandated for and expected of professional internal auditors. This speaks volumes as to internal auditing's value. But clearly, value is defined differently for different business functions. For some, saving money is the most important goal; for others, protecting the reputation is the focus. And for internal auditing, its value proposition to the organization's stakeholders can be best depicted as providing assurance, insight and objectivity to help management and governing bodies meet their goals. And that, without question, is of great value.

For information on "Internal Auditing's Value to Stakeholders," visit The IIA's website at [www.theiia.org/valueproposition](http://www.theiia.org/valueproposition).

**THE INSTITUTE OF INTERNAL AUDITORS (IIA)** is the internal audit profession's global voice, recognized authority, acknowledged leader, chief advocate, and principal educator worldwide. Established in 1941, The IIA is a professional association which serves members in 165 countries around the world who work in internal auditing, IT auditing, governance, internal control, compliance, risk management, security, and academia.

The world's leader in certification, education, research, and technological guidance for the profession, The Institute sets and promulgates the *International Standards for the Professional Practice of Internal Auditing* and provides various levels of accompanying guidance; certifies professionals through the globally recognized Certified Internal Auditor® (CIA®) and specialty certifications in government, control self-assessment, and financial services; presents leading-edge conferences, professional development seminars, and Web-based training; produces forward-thinking educational products; offers quality assurance reviews, benchmarking, and consulting services; and creates growth and networking opportunities for specialty groups.

The IIA also brings great value to its members through *Internal Auditor*, an award-winning professional magazine, and through other outstanding periodicals that address the profession's most pressing issues and challenges and present viable solutions and exemplary practices.

The IIA Research Foundation (IARF) works in partnership with experts from around the globe to conduct valuable research projects on the top issues affecting the business world today. It delivers leading-edge educational products through the IARF Bookstore.

To serve chief audit executives (CAEs), The IIA offers its Audit Executive Center, a comprehensive program for CAEs from industries and organizations of all sizes. The foundation of the Center is the Audit Executive Center Web portal that provides instant access to guidance, research, and thought leadership; a resource library comprising tools and templates; discussion forums allowing instant knowledge sharing; newsletters including The IIA's *CAE Bulletin*; and events focused on professional development.

The Institute's Web site, [www.theiia.org](http://www.theiia.org), is rich with professional guidance and information on IIA programs, products, and services, as well as resources for IT audit professionals.

The IIA is dedicated to providing extensive support and services to its worldwide membership through support, networking and volunteerism at local, national and international levels. For additional information, contact [PR@theiia.org](mailto:PR@theiia.org).



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