

# Internal Auditing Update

# War for Talent

1. Job Market
  - FCPA
  - SOX
2. Demand
  - ↑ Internal Audit Departments
  - ↑ Size of Departments
  - ↑ Big 4 Demand
  - ↑ Middle Market
  - ↑ Control Groups
  - ↑ Technology
  - ↑ Globalization
3. Issues
  - ↑ Turnover
  - ↑ Recruiting Costs
  - ↑ Open Positions
  - ↑ Time to fill slots
  - ↑ Generation Conflict

# War for Talent (cont.)

4. Supply
  - Secondary Market
  - IAEP Programs
    - Funding Support
5. Skill Sets
  - Behavioral
  - Academic
    - Systems (Primary Challenge)
    - Business
6. Attributes
  - Integrity
  - Communication
  - Teamwork
  - Work Ethic
  - Analysis
7. Who hires the best?

# Audit Planning

1. Resource Allocation
  - Rebalancing
    - ↓ SOX
    - ↑ IT
    - ↑ Operational
    - ↑ Fraud
    - ↑ Traditional
    - ↑ Process Audits
  - Allocation
    - ↓ Assurance
    - ↑ Consulting
2. Audit Committee Review
3. Focus
  - ↑ Processes
  - ↓ Transaction

# Entity Level Audits (Governance)

1. Employee Surveys
2. ERM
3. Conflict of Interest
4. Complaint Process
5. Executive Expense Reports
6. Reserves Audit
7. Ethics Audit

# Risk Focus

1. COSO-Risk
2. Resource Allocation
3. Engagement Planning
4. Quality Assessment
5. Exam Coverage
6. Fraud Risk
7. New Language
8. Managing the Business Risk of Fraud: A Practical Guide

# Fraud Focus

Employee —————> Management

Lower Level —————> Top

Small —————> Large

Detrimental —————> Beneficial

Reactive —————> Proactive

Discovery —————> Planning

Detection —————> Prevention

# Evidence Gathering

↓ Traditional Details

↑ Analytics

↑ Technology

## Internal Control Focus

↑ Soft

↓ Hard

# Certification

- Computer Based Testing
  - May 2008
  - Register in April
  - Six months to take after registration
  - Offered year-round
  - Increased Flexibility
  - Retest a minimum of 90 days after failing an exam part
  - Pearson VUE Testing
  - Immediate Feedback
- New Model Exam in 2009
- Format change in 2009 based on CBOK

# New Standards

- IPPF
  - International Standards for the Professional Practice of Internal Auditing
  - Exposure Draft on IIA Website

## IIA International Conference - 2008

- San Francisco
- Full Track on IAEP Topics

# Managing the Business Risk of Fraud: A Practical Guide

1. Exposure Draft
  - ACFE
  - AICPA
  - IIA
2. Contents
  - Introduction
  - Fraud Risk Governance
  - Fraud Risk Assessment
  - Fraud Prevention
  - Fraud Detection
  - Investigation and Response
  - Conclusion
  - Appendices
    - Fraud Governance Policy
    - Sample Fraud Policy
    - Fraud Risk Assessment Framework Example
    - Fraud Risk Exposures
    - Fraud Prevention Scorecard
    - OCEG Alignment
    - COSO Fraud Risk Management Activities

## APPENDIX C1: FRAUD RISK ASSESSMENT FRAMEWORK EXAMPLE

This example is for illustrative purposes and focuses solely on potential revenue recognition risks within financial reporting. A full fraud risk assessment would consider fraudulent financial reporting in other areas relevant to the organization, such as accounts subject to estimation, related-party transactions, and inventory accounting. In addition, the risk of misappropriation of assets, corruption, and other misconduct would be assessed in the same manner.

Fraud Risks Identified (1)	Likelihood (2)	Significance (3)	People and/or Department (4)	Antifraud Controls (5)	Assess Effectiveness of Controls (6)	Residual Risks (7)	Fraud Risk Response (8)
Financial Reporting Revenue recognition	Reasonably possible	Material	Sales personnel	Controlled contract administration system.	Tested by IA		Periodic testing by IA
<ul style="list-style-type: none"> <li>Backdating agreements</li> <li>Channel stuffing</li> </ul>				Insignificant	N/A		N/A
<ul style="list-style-type: none"> <li>Holding books open</li> </ul>	Reasonably possible	Material	Accounting	Standard monthly close process.  Reconciliation of invoice register to general ledger.  Established procedures for shipping, invoicing, and revenue recognition. Established process for consolidation	Tested by IA  Tested by management  Tested by IA  Tested by IA	Risk of management override	Testing of late journal entries  Cut off testing by IA
<ul style="list-style-type: none"> <li>Late shipments</li> </ul>	Reasonably possible	Significant	Shipping dept.	Integrated shipping system, linked to invoicing and sales register.  Daily reconciliation of shipping log to invoice register.  Required management approval of manual invoices.	Tested by IA  Tested by management  Tested by IA	Risk of management override	Cut off testing by IA
<ul style="list-style-type: none"> <li>Side letters/agreements</li> </ul>	Probable	Material	Sales personnel	Annual training of sales and finance personnel on revenue recognition practices.  Quarterly signed attestation of sales personnel concerning extra contractual agreements.	Tested by management  Tested by management	Risk of override	Disaggregated analysis of sales, sales returns, and adjustments by salesperson
<ul style="list-style-type: none"> <li>Inappropriate journal entries</li> </ul>	Reasonably possible	Material	Accounting & Finance	Established process for consolidation.  Established, systematic access controls to the general ledger.  Standard monthly and quarterly journal entry log maintained. Review process in place for standard entries, and nonstandard entries subject to two levels of	Tested by IA  Tested by IA  Tested by management	Risk of override  N/A  N/A	Data mining of journal entry population by IA for: <ul style="list-style-type: none"> <li>Unusual Dr/CR combinations</li> <li>Late entries to accounts subject to estimation</li> </ul>

Fraud Risks Identified (1)	Likelihood (2)	Significance (3)	People and/or Department (4)	Antifraud Controls (5)	Assess Effectiveness of Controls (6)	Residual Risks (7)	Fraud Risk Response (8)
• Roundtrip transactions	Remote	Insignificant	N/A	N/A	N/A	N/A	N/A
• Manipulation of bill and hold arrangements	Remote	Insignificant	N/A	N/A	N/A	N/A	N/A
• Early delivery of product	Reasonably possible	Significant	Sales and shipping	Systematic matching of sales order to shipping documentation; exception reports generated.	Tested by management	Adequately mitigated by controls	N/A
• Partial shipments	Reasonably possible	Significant	Sales and shipping	Systematic shipping documents manually checked against every shipment. Systematic matching of sales order to shipping documentation; exception reports generated. Customer approval of partial shipment required prior to revenue recognition.	Tested by management	Adequately mitigated by controls	N/A
• Additional revenue risks				Systematic shipping documents manually checked against every shipment.			

- Fraud Risks Identified:** This column should include a full list of the potential fraud and misconduct risks that may face the organization. This list of risks will be different for different organizations and should be informed by (a) industry research, (b) interviews of employees and other stakeholders, (c) brainstorming sessions, and (d) activity on the whistleblower hotline.
- Likelihood of Occurrence of the Fraud Risk:** To design an efficient fraud risk management program, it is important to assess the likelihood of the identified fraud risks such that the organization establishes proper antifraud controls for the risks that are deemed most likely. For purposes of the assessment, it should be adequate to evaluate the likelihood of risks as remote, reasonably possible, and probable.
- Significance to the Organization:** Quantitative and qualitative factors should be considered when assessing the significance of fraud risks to an organization. For example, certain fraud risks may only pose an immaterial direct financial risk to the organization, but could greatly impact its reputation, and therefore, would be deemed to be a more significant risk to the organization. For purposes of the assessment, it should be adequate to evaluate the significance of risks as immaterial, significant, and material.
- People and/or Department Subject to the Risk:** As fraud risks are identified and assessed, it is important to evaluate which people inside or outside the organization are subject to the risk. This knowledge will assist the organization in tailoring its fraud risk response, including establishing appropriate segregation of duties, proper review and approval chains of authority, and proactive fraud auditing procedures.
- Antifraud Internal Controls:** Map pre-existing controls to the relevant fraud risks identified. Note, this occurs subsequent to fraud risks being identified and being assessed for likelihood and significance. By progressing in this order, this framework intends for the organization to assess identified fraud risks on an inherent basis, without consideration of internal controls.
- Assessment of Internal Controls:** The organization should have a process in place to evaluate whether the identified controls are operating effectively and mitigating fraud risks as intended. Companies subject to the provisions of Sarbanes-Oxley Section 404 will have a process such as this in place. Organizations not subject to Sarbanes-Oxley should consider what review and monitoring procedures would be appropriate to implement to gain assurance that their internal control structure is operating as intended.
- Residual Risks:** After consideration of the internal control structure, certain fraud risks may not be adequately mitigated due to several factors, including (a) properly designed controls are not in place to address certain fraud risks or (b) controls identified are not operating effectively. These residual risks should be evaluated by the organization in the development of the fraud risk response.
- Fraud Risk Response:** Residual risks should be evaluated by the organization and fraud risk responses should be designed to address the risk. The fraud risk response could be one or a combination of the following: (a) implementing additional controls, (b) designing proactive fraud auditing techniques, and/or (c) reducing the risk by exiting the activity.

# Common Body of Knowledge Study 2006

1. Most comprehensive global study ever conducted about the Internal Audit profession
  - Global compliance with the standards
  - The global state of the profession
  - Staffing, skills, and competencies
  - Emerging roles
  - 472 pages

# Reporting

Board

CEO

Audit Committee

Functional

Proactive  
Review

Administrative

- Primary Report
- Audit Plan
- Overview of Administrative
- Executive Summary
- Charter
- Performance Evaluation
- Promotions
- Hiring – Rotation - Termination
- Resources
- Office Space
- Budget
- Training
- Travel
- Staffing

Internal Audit

- CAE
- Charter

# Internal Audit Challenges

1. Globalization
2. Business Complexity
3. Rate of Change
4. Technology
  - Dash Board
  - XBRL
5. Knowledge Diversity