The Institute of Internal Auditors
2004 Annual Report

Dave Richards Accepts Top Position at IIA Headquarters, Perpetuating Legacy of Excellence

Due to the untimely passing of IIA President Bill Bishop, Dave Richards, CIA stepped into his new position as IIA president a few months earlier than anticipated. Bishop, who had planned to retire in September, died unexpectedly on March 7, 2004. Richards was selected to lead The IIA as a result of a global search. As a former IIA chairman of the board and a seasoned and well-respected internal audit executive, he brought to his post a stellar background and a well-demonstrated commitment to the profession. Having championed many initiatives as an IIA volunteer leader, Richards transitioned naturally into his new role as the head of The Institute and readily began to lead the organization toward accomplishing its goals and objectives.

In honor of his predecessor, Richards, along with the staffs and volunteer leaders of The IIA and The IIA Research Foundation established a memorial fund in Bill Bishop's name and dedicated The IIA headquarters facility to his memory.

The Institute of Internal Auditors 2004 Year-end Global Highlights

This global message puts into perspective a successful year for the internal audit profession worldwide. While the financial-related information in this report specifically reflects the monetary status of IIA global headquarters, the year-end highlights depict the state of the profession around the globe.

The IIA and The IIA Research Foundation's financial statements are presented in a consolidated format in accordance with The AICPA's Accounting Statement of Position 94-3.

Strategic Objectives

Through its strategic objectives, The IIA embarked on new paths that will impact the internal audit profession in years to come. The IIA Executive Committee, led by 2003-04 Chairman Robert N. McDonald, CIA, CGAP and 2004-05 Chairman Betty McPhilimy, CIA, oversaw the final implementation phase of the four 2002-2004 strategic objectives that comprise professionalism, technology, global promotion, and organizational infrastructure.

2002-2004 STRATEGIC OBJECTIVES

1. Encourage internal audit practitioners to demonstrate greater professionalism and competence.
2. Demonstrate and provide leadership in regard to internal auditing's role in technology.
3. Be the global voice for the profession.
4. Assess our infrastructure to make it more efficient and effective, thereby allowing the organization to focus its energies on internal auditors and their organizations.

Membership Growth

In 2004, IIA membership increased from 89,166 to 99,433 – an increase of 11.5 percent. This increase was due in large to heightened public awareness of the profession and The Institute. The growing awareness was a result of The IIA's response to the governance crises and its ongoing commitment to provide members with relevant products, services, and guidance.

New IIA affiliates were formed in Papua New Guinea, Paraguay, Romania, Florida East Coast, and Bangladesh. At the close of 2004, the breakdown of membership was 49 percent within North America and the Caribbean and 51 percent elsewhere.

The IIA special membership sections were originally designed to advance and strengthen the overall profession of internal auditing and help meet audit specialty or industry-specific needs on a global basis. In 2004, membership in the CAE Services Program (CAE), Control Self-Assessment Center (CSA), Gaming Audit Group, and Financial Services Auditor Group (FSA) grew to a total of 5,670 members. Twenty-five issues of the popular *CAE Bulletin* were distributed to CAE Services Program members during the year.

In 2004, The IIA's Customer Service Center supported the membership by processing 163,033 transactions and responding to approximately 36,481 telephone calls. Additionally, 19,762 members updated their member profiles via the Web, attesting to the success of the Customer Service Center's and The IIA's Information Systems' continued efforts to provide members convenient methods of communicating with The IIA.

IIA Web Site Drives E-commerce and Communication

The IIA's Web site maintained its status as a highly successful, comprehensive source of internal audit-related information. Visits to the site during 2004 totaled 3,530,800 (a 29 percent increase over 2003) with 23,326,158 page views (a 24 percent increase over 2003), with *ITAudit*, IIA affiliates, The Research Foundation Bookstore, and certification being the most popular.

Affiliates that utilize the Web template and site hosting offered by The IIA enjoyed 347,836 visits and 1,840,380 page views, making them the fourth-most visited section of www.theiia.org. In 2004, the number of affiliate sites using The IIA's template increased from 103 to 131 -- 18 in North America and 10 representing members from Colombia, Estonia, Haiti, Greece, Lebanon, Lithuania, Nairobi (Kenya), Oman, Qatar, and Uganda. The affiliate templates were altered for UNICODE viewing (as opposed to Western European), which allows affiliates to set up sites in all languages. The templates were also enhanced to allow affiliates to modify global settings such as format for dates and currency amounts.

Significant changes in content and functionality on www.theiia.org included a font switch from Times to Arial to give the site a cleaner, more polished look; a new rollover effect for the navigation buttons across the top and down the left side of every page; a "Recent News" area that archives home page news items for up to six months; a "printer-friendly" status that is automatically enabled on every page; and a new site map that more clearly defines the navigation of the site.

Other 2004 accomplishments:

- The Global Auditing Information Network (GAIN) was transitioned to The IIA's Web site with updates to content and navigation, a new utility for uploading "Flash Survey" questions, and new online forms.
- The IIA Web Style Guide was developed to give guidance on writing and layout for the Web and instructions on how to use The Institute's Web content management system.
- *Internal Auditor* magazine gained a new online presence with programming support from the Web site staff.

Educational Products and Research Reports

In January 2004, The IIA Research Foundation (The Foundation) merged with The IIA's educational products area. The merger capitalized on the powerful synergies of the two entities, as they both play pivotal strategic and operational roles in research and education for the profession of internal auditing. Some of the key reports and products released during 2004 include:

- *Enterprise Risk Management: Identifying Risks in B2B E-commerce Relationships*
- *Changing Internal Audit Practices in the New Paradigm: Sarbanes-Oxley Environment*
- *Proactively Detecting Occupational Fraud Using Computer Audit Reports*
- *Key Controls: The Solution for Sarbanes-Oxley Internal Control Compliance*
- *The Internal Auditor Job Market 2004*
- *Enterprise Risk Management – Integrated Framework* (COSO Report)

In addition to producing a wealth of new resources, The Foundation also established The William G. Bishop III, CIA, Memorial Fund. This initiative supports ongoing research for the profession's *common body of knowledge* (CBOK).

Training

The IIA presented seminars to 11,191 attendees at 474 courses. This includes publicly held seminars, corporate and chapter on-site seminars, Vision University, government on-site programs, co-sponsored seminars, and Organizational Effectiveness Training (OET). The IIA teamed up with Deloitte & Touche LLP to develop a comprehensive 13-course information technology audit curriculum introduced in August 2004 and taught by D&T IT auditors who work with the latest technology every day.

Several other new-in-2004 seminars include Countdown to Internal Quality Assessment: Are You Ready?, Vision University: The Experienced CAE, SOX 404 Readiness Workshop, Effective Writing for Auditors, Fighting Fraudulent Financial Reporting, and Enhanced Communications for Auditors.

The IIA hosted nine headquarters-sponsored conferences in 2004 with 2,081 attendees. Two of the nine were brand new: Information Technology for Today's Auditor and Converging Roles; an IIA/AICPA joint event.

In 2004, IIA webcasts experienced dramatic growth, with registrations increasing by more than 47 percent from the prior year. AuditLearning™, an a-la-carte training website developed by The IIA, experienced unprecedented success, increasing new student registrations and e-commerce orders by more than 500 percent. The primary drivers for this exceptional growth were the exponential expansion of the core course offerings, the addition of *Internal Auditor* magazine and webcast quizzes, and an influx of group sales. Additionally, web-based training's annual subscription product, www.IIAOnlineCPE.org experienced healthy growth in 2004, with subscriptions increasing by more than six percent.

Certification Growth

The CIA exam celebrated its 30th anniversary in 2004. To put the growth of the CIA exam in perspective, in 1974, 654 candidates took a total of 2,299 parts. In 2004, 30,634 candidates took a total of 63,144 parts. The May 2004 Certified Internal Auditor (CIA) exam was conducted at 228 sites in 78 countries. Approximately 9,439 candidates took a total of 17,325 exam parts. The May 2004 CIA exam included changes to the exam syllabus based on the global role delineation study conducted in 2002. The following are the most significant changes:

- The new Parts I, II, and III – considered to be the core global syllabus of the CIA exam – offer a stronger focus on corporate governance and risk issues and exhibit

increased alignment with The IIA's Professional Practices Framework. Additionally, various accounting and finance concepts were moved from Part IV to the core global syllabus.

- The number of questions on each exam part increased from 80 to 125, providing a broader range of questions within each exam part and enhancing the rigor of the exam.

The November 2004 CIA exam was conducted at 257 sites in 81 countries. Approximately 21,195 candidates took a total of 45,819 parts. Eighty-four percent of the parts were taken outside North America. The CAE Testing-on-Demand Program was introduced to accommodate those CAEs who desire timeliness and anonymity in taking the CIA exam. Twenty individuals took advantage of this premium service in 2004.

In 2004, the Certification in Control Self-Assessment (CCSA) exam was taken by 598 candidates, which was a six percent increase over 2003. Additionally, this specialty exam was translated into Japanese and Italian. The Certified Government Auditing Professional (CGAP) and Certified Financial Services Auditor (CFSA) exams were offered globally for the first time in November 2004. The number of CGAP exams taken increased by 10 percent over 2003 and the number of CFSA exams increased by more than 70 percent from the prior year.

Key Issues around the World

The list of issues of concern to the internal audit profession globally continues to include corporate governance, risk and control, and ethics. Sustainable development or corporate social responsibility has also evolved into an important global issue. How internal auditors should address technology is, and will continue to be, an ongoing concern. As such, The Institute introduced the Global Technology Audit Guide series.

During the past few years, advocacy for the profession has taken center stage — so much so that IIA headquarters has designated an entire business unit to advocacy efforts. In addition to reacting and responding to proposed positions and regulations, in 2004 The Institute put into place an extensive proactive plan to reach out to like-minded organizations throughout the world to form alliances that will further the internal audit profession. Implementation of the plan will be reported on in the years ahead.

Many representations by The IIA were completed including to the: SEC, PCAOB, OSC, AICPA, GAO, INTOSAI, COSO, IFAC, ISACA, and others.

To learn how key global issues were addressed in specific countries in 2004, visit The IIA's list of affiliates by location.

Throughout the year, IIA global headquarters continued to provide members with updates on frauds and failures and resulting legislation and regulation, and served as a media resource for real answers and guidance on compliance and best practices.

Promoting the Profession

By increasing media exposure and visibility on internal audit issues, identifying the profession as an ideal career choice, and publicizing the value internal audit processes bring to shareholders, IIA affiliates can significantly participate in promoting the profession, an important IIA initiative.

The International Marketing Affiliates Program (IMAP), designed to encourage IIA affiliates to be advocates for the profession by elevating the profile of internal auditing, is a global award presented each year at the International Conference. The 2004 IMAP Award was presented to IIA-New Orleans for its success in promoting the profession.

Various IIA affiliates celebrated May as International Internal Audit Awareness Month. The purpose of the commemoration is to provide a unified structure for intensive promotional activity throughout the world. Although advocacy for the profession is an ongoing initiative that must be nurtured and maintained throughout the year, having one month focused on bringing attention to internal auditing provides a framework for enhanced exposure. Throughout the year, The Institute provided additional resources and counsel for promoting the profession to individuals and affiliates alike. View 2004 Awareness Month activities.

Examples of 2004 media interviews with top IIA officials and media coverage include: *Accounting Today, Bloomberg News, Board Alert, Board News – Finland, Business Finance, Business Insurance Magazine, CBS MarketWatch, CFO.com, CFO-IT, Chicago Tribune, Chief Learning Officer, Compliance Week, Corporate Accountability Report, Corporate Gov Alliance, Corporate Secretary, CPA Journal, Dallas Morning News, Director's Monthly-Extra, Directorship, Dow Jones, Financial Executive, Insight Magazine/Illinois CPA Soc., Journal of Accountancy, Kansas City Star, Knowledge Leader, Miami Herald, MSI Magazine, NACD's BRC update, New AccountantUSA.COM, newsobserver.com, NPR Marketplace, NY German Press, Orlando Business Journal, Operational Risk, Republican, Reuters, Tennessean, Treasury & Risk Magazine, USA Today, Women's Wear Daily (*NOTE: Multiple placements occurred in many of these publications.)

The IIA also published four issues of its corporate governance newsletter, *Tone at the Top*, which is designed to promote the profession and the value of internal auditing to top management, boards of directors, and audit committees. The newsletter is available in print free of charge and archived online.

- February 2004- New Governance Rules Require Internal Auditing
- July 2004- Ensuring There Are No Holes in Your SOX
- October 2004- This Game Is Not Child's Play
- November 2004- An Ounce of Prevention

Progress through Sharing

The financial position of The Institute at the end of 2004 was very healthy (all in US dollars). Total assets increased $3.5 million to $20.2 million from the previous year in 2003, while total liabilities increased by $1.2 million to $7.8 million. Unrestricted net assets increased $2.2 million to $12.4 million, reflecting a contribution of $2.1 million plus a net gain on investments of $100,000.

The IIA sincerely thanks its affiliates, leaders, members, customers, and other constituents and expresses appreciation to all who have supported the work of the association in the spirit of The IIA's motto, "Progress through Sharing."

The IIA Board of Directors 2004–2005

2004–2005 North American Committee Members

2004–2005 Regional and District Representatives

REGIONAL DIRECTORS

The IIA Board of Directors 2003–2004

THE INSTITUTE OF INTERNAL AUDITORS, INC.

CONSOLIDATING FINANCIAL STATEMENTS

(With The Accompanying Independent Auditors' Report)

For The Years Ended December 31, 2004 and 2003

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The Audit Committee
The Institute of Internal Auditors, Inc.
Altamonte Springs, Florida

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying consolidating statements of financial position of The Institute of Internal Auditors, Inc. ("the Institute") as of December 31, 2004 and 2003, and the related consolidating statements of activities and cash flows for the years then ended. These consolidating financial statements are the responsibility of the Institute's management. Our responsibility is to express an opinion on these consolidating financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidating financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidating financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidating financial statements referred to above present fairly, in all material respects, the consolidating financial position of The Institute of Internal Auditors, Inc. as of December 31, 2004 and 2003, the consolidating changes in its net assets and its consolidating cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Graham, Cottrill, Jackson, Batts & Hostetter, LLP

GRAHAM, COTTRILL, JACKSON, BATTS & HOSTETTER, LLP

February 18, 2005

THE INSTITUTE OF INTERNAL AUDITORS, INC.

CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

	December 31,				
	2004				2003
	The Institute of Internal Auditors, Inc.	Institute of Internal Auditors - Research Foundation	Eliminations	Consolidated Total	Consolidated Total
ASSETS					
Cash and cash equivalents	$ 2,739,438	$ 434,484	$ —	$ 3,173,922	$ 1,101,399
Restricted investments	—	135,000	—	135,000	135,000
Investments	9,815,649	1,039,171	—	10,854,820	9,863,544
Due from affiliate, net	117,023	—	(117,023)	—	—
Accounts receivable, net	1,242,081	143,451	—	1,385,532	959,978
Inventories	—	151,904	—	151,904	150,634
Prepaid expenses and advances	821,067	—	—	821,067	308,448
Property and equipment, net	4,196,878	—	—	4,196,878	4,322,075
Deferred project costs, net	101,071	80,228	—	181,299	270,718
Employee savings plan	1,183,093	—	—	1,183,093	1,176,227
Total assets	**$20,216,300**	**$1,984,238**	**$ (117,023)**	**$22,083,515**	**$18,288,023**
LIABILITIES					
Accounts payable and accrued expenses	$ 2,817,567	$ 66,974	$ —	$ 2,884,541	$ 2,108,848
Due to affiliate, net	—	117,023	(117,023)	—	—
Deferred revenue	3,774,628	2,803	—	3,777,431	3,282,680
Deferred employee compensation	1,183,093	—	—	1,183,093	1,176,227
Total liabilities	**7,775,288**	**186,800**	**(117,023)**	**7,845,065**	**6,567,755**
NET ASSETS					
Unrestricted	12,441,012	1,541,629	—	13,982,641	11,518,762
Temporarily restricted	—	120,809	—	120,809	66,506
Permanently restricted	—	135,000	—	135,000	135,000
Total net assets	**12,441,012**	**1,797,438**	**—**	**14,238,450**	**11,720,268**
Total liabilities and net assets	**$20,216,300**	**$1,984,238**	**$ (117,023)**	**$22,083,515**	**$18,288,023**

The Accompanying Notes Are An Integral Part
Of These Consolidating Financial Statements

THE INSTITUTE OF INTERNAL AUDITORS, INC.

CONSOLIDATING STATEMENTS OF ACTIVITIES

	For The Years Ended December 31,				
	2004				2003
	The Institute of Internal Auditors, Inc.	Institute of Internal Auditors - Research Foundation	Eliminations	Consolidated Total	Consolidated Total
CHANGE IN UNRESTRICTED NET ASSETS FROM OPERATIONS					
REVENUES					
Learning Center	$12,715,303	$ —	$ —	$12,715,303	$12,370,465
Global Practices Center	4,969,031	—	—	4,969,031	4,332,012
Communications Center	2,009,109	—	—	2,009,109	1,823,667
Quality Auditing Services	1,211,953	—	—	1,211,953	741,230
President	191,503	—	—	191,503	68,381
2003 International Conference	—	—	—	—	1,946,283
Contributions	53,705	187,230	—	240,935	136,511
Publication sales	—	2,096,154	—	2,096,154	102,163
Dividend and interest income	232,995	32,847	—	265,842	197,927
Total revenues	21,383,599	2,316,231	—	23,699,830	21,718,639
Net assets released from use restrictions	3,458	61,123	—	64,581	144,561
Total revenues and net assets released from use restrictions	21,387,057	2,377,354	—	23,764,411	21,863,200
EXPENSES					
Learning Center	8,998,451	—	—	8,998,451	8,200,917
Global Practices Center	3,457,350	—	—	3,457,350	2,927,556
Communications Center	2,723,363	—	—	2,723,363	2,669,922
Quality Auditing Services	905,461	—	—	905,461	630,033
President	1,565,100	—	—	1,565,100	1,166,314
Business Center	1,592,585	—	—	1,592,585	1,382,457
2003 International Conference	—	—	—	—	1,590,824
Educational products	—	1,772,118	—	1,772,118	12,810
Research projects	—	159,992	—	159,992	424,711
Academic programs	—	17,680	—	17,680	22,006
Academic relations	—	23,169	—	23,169	—
General and administrative	—	231,623	—	231,623	72,448
Total expenses	19,242,310	2,204,582	—	21,446,892	19,099,998
Change in unrestricted net assets from operations	**2,144,747**	**172,772**	**—**	**2,317,519**	**2,763,202**
CHANGE IN TEMPORARILY RESTRICTED NET ASSETS FROM OPERATIONS					
Contributions	3,458	111,390	—	114,848	163,182
Dividend and interest income	—	3,780	—	3,780	3,616
Net assets released from use restrictions	(3,458)	(61,123)	—	(64,581)	(144,561)
Change in temporarily restricted net assets from operations	**—**	**54,047**	**—**	**54,047**	**22,237**
NET GAIN ON INVESTMENTS	**136,465**	**10,151**	**—**	**146,616**	**481,485**
CHANGE IN NET ASSETS	**2,281,212**	**236,970**	**—**	**2,518,182**	**3,266,924**
NET ASSETS – Beginning of year	**10,159,800**	**1,560,468**	**—**	**11,720,268**	**8,453,344**
NET ASSETS – End of year	**$12,441,012**	**$1,797,438**	**$ —**	**$14,238,450**	**$11,720,268**

The Accompanying Notes Are An Integral Part
Of These Consolidating Financial Statements

THE INSTITUTE OF INTERNAL AUDITORS, INC.

CONSOLIDATING STATEMENTS OF CASH FLOWS

	For The Years Ended December 31,				
	2004				2003
	The Institute of Internal Auditors, Inc.	Institute of Internal Auditors - Research Foundation	Eliminations	Consolidated Total	Consolidated Total
CASH FLOWS FROM OPERATING ACTIVITIES					
Change in net assets	$ 2,281,212	$ 236,970	$ —	$ 2,518,182	$ 3,266,924
Adjustments to reconcile change in net assets to net cash flows from operating activities:					
Depreciation	246,683	—	—	246,683	232,177
Amortization of deferred project costs	106,524	91,315	—	197,839	231,699
Net gain on investments	(136,465)	(10,151)	—	(146,616)	(481,485)
Net gain on sales of property and equipment	(479)	—	—	(479)	(464)
Change in due to/from affiliate, net	(127,148)	127,148	—	—	—
Change in accounts receivable, net	(286,587)	(138,967)	—	(425,554)	216,833
Change in inventories	—	(1,270)	—	(1,270)	(58,302)
Change in prepaid expenses and advances	(512,619)	—	—	(512,619)	(69,581)
Change in accounts payable and accrued expenses	724,958	50,735	—	775,693	287,492
Change in deferred revenue	501,844	(7,093)	—	494,751	476,386
Total adjustments	516,711	111,717	—	628,428	834,755
Net cash flows from operating activities	**2,797,923**	**348,687**	—	**3,146,610**	**4,101,679**
CASH FLOWS FROM INVESTING ACTIVITIES					
Proceeds from sales of investments	1,794,987	227,901	—	2,022,888	1,586,897
Purchases of investments	(2,647,793)	(219,755)	—	(2,867,548)	(6,550,461)
Proceeds from sales of property and equipment	479	—	—	479	464
Purchases of and improvements to property and equipment	(121,486)	—	—	(121,486)	(70,896)
Expenditures for deferred projects, net	(74,864)	(33,556)	—	(108,420)	(39,032)
Net cash flows from investing activities	**(1,048,677)**	**(25,410)**	—	**(1,074,087)**	**(5,073,028)**
CHANGE IN CASH AND CASH EQUIVALENTS	**1,749,246**	**323,277**	—	**2,072,523**	**(971,349)**
CASH AND CASH EQUIVALENTS – Beginning of year	**990,192**	**111,207**	—	**1,101,399**	**2,072,748**
CASH AND CASH EQUIVALENTS – End of year	**$ 2,739,438**	**$ 434,484**	**$ —**	**$ 3,173,922**	**$ 1,101,399**

The Accompanying Notes Are An Integral Part
Of These Consolidating Financial Statements

NOTE A – NATURE OF ACTIVITIES

The Institute of Internal Auditors, Inc. ("the Institute") was formed in 1941 and is a not-for-profit corporation organized to cultivate, promote and disseminate knowledge and information concerning internal auditing and related subjects. The Institute's primary program activities include conducting seminars and conferences to educate and train internal auditors; publishing and selling periodicals and materials which inform internal auditors and members of the Institute of current professional issues, standards and practices; offering examinations and certifications to internal auditors; and evaluating the performance of internal audit departments.

Institute of Internal Auditors - Research Foundation ("the Foundation") is a not-for-profit corporation formed to promote research and education in internal auditing. The Institute's Board of Directors appoints the Foundation's Board of Trustees. Additionally, the Foundation is a supporting organization of the Institute. Accordingly, in conformity with Statement of Position 94-3, issued by the American Institute of Certified Public Accountants, the Institute's consolidating financial statements include the accounts of the Foundation. All significant interorganization transactions and balances have been eliminated.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Restricted and unrestricted revenue and support

Contributions received are recorded as unrestricted, temporarily restricted or permanently restricted support, depending on the existence and/or nature of any donor restrictions. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidating statements of activities as "net assets released from restrictions."

Revenue recognition and center activities

The Institute recognizes revenue and incurs expenses in its operation of the following functions:

Learning Center

Conference and seminar fees are recognized as income in the period in which the event is held. Educational product sales are recognized as income when the related inventory is shipped. Certification fees are recognized as income in the period in which the exams are given. Global Auditing Information Network ("GAIN") subscription fees are recognized as income when the product is shipped. Expenses include all costs associated with administration and the direct costs of conducting seminars, conferences and exams, and fulfillment of GAIN subscriptions. During 2003, expenses also included costs associated with producing and distributing educational products, a function conducted by the Foundation after December 31, 2003.

Global Practices Center

Membership dues are recognized as income ratably throughout the year. Membership application fees are nonrefundable and are recognized as income when received. Expenses include all costs associated with administration and the direct costs of delivering member benefits, as well as costs associated with the global integration program.

Communications Center

Subscriptions and print advertising revenue are recognized as income in the period in which the related publications are issued. Website advertising revenue is recognized as income ratably over the length of the advertising contract. Expenses include all costs associated with administration and the direct costs of producing and delivering publications, website maintenance, information technology, and human resources. Advertising costs are expensed as incurred.

Quality Auditing Services

Quality Assessment Service fees are recognized as income as the related service is provided based on the percentage of the engagement completed. Expenses include all costs associated with administration and the direct costs of conducting Quality Assessments.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

President
The excess of revenues over expenditures from the 2004 International Conference was recognized as income during 2004. Expenses include costs associated with the governance activities of the Institute, including committee meetings, executive travel and strategic initiative development and implementation.

Business Center
Expenses include costs of supporting the infrastructure of the Institute, including accounting, customer service, mailroom, copy center, facility maintenance, and other shared expenses.

During 2003, expenses related to the administrative tasks conducted by the Institute on behalf of the Foundation were included with "research projects" in the accompanying 2003 consolidated financial statements. Expenses related to supporting the auditing profession through college and university programs were included with "academic programs" in the accompanying 2003 consolidated financial statements. During 2004, the Foundation reimbursed the Institute for certain personnel-related costs and certain shared costs. Such reimbursements are reflected as expenses of the Foundation based on the nature of the specific expenses. Additionally, the Institute absorbs certain overhead costs of the Foundation for which reimbursement is not required.

Revenue received in advance of the recognition period is included in "deferred revenue" in the accompanying consolidating statements of financial position.

Cash and cash equivalents
The Institute considers all investment instruments purchased with original maturities of three months or less to be cash equivalents.

Restricted investments
Restricted investments consist of endowment funds given to the Foundation, the investment income from which is to be used for scholarships for internal auditing students.

Investments
Investments are carried at fair market value.

Allowance for doubtful accounts
Accounts receivable are stated net of an allowance for doubtful accounts. The Institute estimates the allowance for doubtful accounts based on an analysis of specific accounts, taking into consideration the age of the past due account and an assessment of the client's ability to pay. Accounts are considered past due when payments are not made in accordance with specified terms. Accounts are written off upon such time that management determines such amounts are uncollectible.

Inventories
Inventories consist of publications and are carried at the lower of cost or market value using the first-in, first-out (FIFO) cost flow method.

Property and equipment
Property and equipment are stated at cost. The Institute uses the straight-line method of depreciating property and equipment over estimated useful lives.

Deferred project costs
Costs related to seminars, website development and design, and educational product development or revision are deferred until the related projects are completed. Seminar costs are amortized over three or four years using the straight-line method, website costs over three years using the straight-line method, and educational product development or revision costs over three years at 60% the first year, 30% the second year, and 10% the third year. During 2003, the Institute transferred certain components of its Educational Products department to the Foundation.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Restrictions on net assets
Temporarily restricted net assets consist of amounts restricted for various research projects. Permanently restricted net assets consist of endowment funds, the investment income from which is to be used for scholarships for internal auditing students.

Income taxes
The Institute is exempt from federal income tax under Internal Revenue Code Section 501(a) as an organization described in Section 501(c)(6) and from state income tax pursuant to Florida law. The Institute engages in certain activities which are "unrelated business activities" as defined by the Internal Revenue Code, and which are subject to taxation. Income taxes on unrelated business income are recognized as expenses as incurred. The Foundation is exempt from federal income tax under Internal Revenue Code Section 501(a) as an organization described in Section 501(c)(3) and from state income tax pursuant to Florida law. The Foundation has not incurred unrelated business income taxes.

Use of estimates
Management uses estimates and assumptions in preparing consolidating financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and reported revenues and expenses. Significant estimates used in preparing these consolidating financial statements include those used in determining the useful lives of property and equipment and assessing the collectibility of accounts receivable. Actual results could differ from the estimates.

Reclassifications
Certain amounts included in the 2003 consolidated financial statements were reclassified to conform with adoptions made during 2004. Those reclassifications had no material effect on the accompanying consolidating financial statements.

NOTE C – CONCENTRATION OF CREDIT RISK

The Institute maintains its cash and cash equivalents in deposit accounts and money market funds which may not be federally insured, may exceed federally insured limits, or may be insured by an entity other than an agency of the federal government. The Institute has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk related to cash and cash equivalents.

NOTE D – INVESTMENTS

Investments consisted of the following:

			December 31,	
			2004	2003
	The Institute	The Foundation	Consolidated Total	Consolidated Total
U.S. government obligations	$1,946,325	$ 300,977	$ 2,247,302	$1,555,540
Corporate bonds	1,950,302	263,627	2,213,929	1,642,035
Equity securities	5,919,022	609,567	6,528,589	4,778,127
Certificates of deposit	—	—	—	2,022,842
Subtotal	9,815,649	1,174,171	10,989,820	9,998,544
Less: Restricted investments	—	(135,000)	(135,000)	(135,000)
Net investments	$9,815,649	$1,039,171	$10,854,820	$9,863,544

NOTE D – INVESTMENTS (Continued)

The Institute considers all dividends and interest from investments as operating revenues for purposes of the consolidating statements of activities. Gains and losses related to investments are considered to be nonoperating activities for purposes of the consolidating statements of activities.

Net gain on investments consisted of the following:

			December 31,	
			2004	2003
	The Institute	The Foundation	Consolidated Total	Consolidated Total
Unrestricted	$ 136,465	$ 9,895	$ 146,360	$ 481,485
Temporarily restricted	—	256	256	—
Total	$ 136,465	$ 10,151	$ 146,616	$ 481,485

NOTE E – PROPERTY AND EQUIPMENT

Property and equipment consisted of the following:

	December 31,	
Category	2004	2003
Land	$ 114,103	$ 114,103
Buildings and building improvements	3,726,517	3,726,517
Furniture and equipment	1,335,806	1,226,795
Total property and equipment	5,176,426	5,067,415
Less: Accumulated depreciation	(979,548)	(745,340)
Net property and equipment	$4,196,878	$4,322,075

Depreciation expense amounted to approximately $247,000 and $232,000 for 2004 and 2003, respectively.

NOTE F – INTERNATIONAL CONFERENCE

The Institute's 2003 consolidated financial statements include the revenues and expenses associated with the 2003 International Conference. Expenses related to the International Conference include approximately $60,000 paid to the Las Vegas chapter in recognition of its services as the host chapter for the International Conference.

NOTE G – OPERATING LEASES

The Institute leases office equipment under operating leases expiring through October 2007. Approximate future lease payments are as follows:

Year Ending December 31,	
2005	$171,000
2006	142,000
2007	26,000
Total	$339,000

NOTE G – OPERATING LEASES (Continued)

Total rent expense related to the above leases and additional amounts for short-term rentals and related charges amounted to approximately $473,000 and $320,000 for 2004 and 2003, respectively.

NOTE H – RETIREMENT PLANS

The Institute maintains a Section 401(k) retirement plan. All full-time employees over the age of twenty-one who have completed 90 days of service are eligible to participate in the plan. The Institute contributes three percent of the total salary of eligible employees to the plan.

The Institute also maintains a money purchase pension plan. All employees over the age of twenty-one who have completed 1,000 hours of service are eligible to participate in the plan. The Institute contributes seven percent of the total salary of eligible employees to the plan.

During 2004 and 2003, the Institute contributed approximately $579,000 and $565,000, respectively, to the above plans.

The Institute maintains a Section 457 deferred compensation plan for the benefit of certain employees. Under the provisions of the plan, employees could elect to have a portion of their salary contributed to the plan. The Institute held approximately $1,183,000 and $1,176,000 in the plan as of December 31, 2004 and 2003, respectively, which is reflected in the accompanying consolidating statements of financial position under "employee savings plan" and "deferred employee compensation". Contributions to the plan were terminated effective December 31, 2001.

NOTE I – COMMITMENTS

As of December 31, 2004, the Institute was a party to an agreement with a certain technology consultant for the implementation of, ongoing maintenance and support for, and software licensing related to the Institute's Association Management System. Total remuneration to be paid to the consultant is approximately $790,000, of which approximately $160,000 was paid during 2004 and is included in "prepaid expenses and advances" in the accompanying 2004 consolidating statement of financial position. The remaining amount of approximately $630,000 is expected to be paid during 2005 as services are rendered.

As of December 31, 2004, the Institute was also a party to an agreement with a certain webcast provider for a specified number of webcasts to be produced, hosted and distributed by the provider during 2005 for total remuneration of $134,000. Approximately $124,000 of this amount remained unpaid as of December 31, 2004 and is expected to be paid as services are rendered.

The Foundation has entered into contracts and agreements with various parties for research projects. Unpaid commitments related to these contracts and agreements totaled approximately $122,000 as of December 31, 2004.

NOTE J – EXPENSE ALLOCATIONS

Total expenses for the Institute include approximately $14,117,000 and $14,554,000 of program expenses, $5,120,000 and $4,454,000 of supporting expenses, and $5,000 and $5,000 of fund-raising expenses for 2004 and 2003, respectively.

During 2004 and 2003, the Foundation incurred approximately $20,000 and $27,000, respectively, of fund-raising expenses. Such amounts are included in "general and administrative" expense in the accompanying consolidating financial statements.

Management Report on Responsibility

The management of The Institute of Internal Auditors (The IIA) is responsible for the preparation, integrity, and fair presentation of the accompanying financial statements. The statements were prepared in accordance with generally accepted accounting principles applied on a consistent basis and are not affected by material fraud or error. The financial statements include amounts that are based on management's best estimates and judgments.

Management also prepared the supplemental information in the annual report and is responsible for its accuracy and consistency with the financial statements. The IIA's financial statements have been audited by Graham, Cottrill, Jackson, Batts, and Hostetter, P.A., independent certified public accountants, elected by the board of directors. Management has made available to Graham, Cottrill, Jackson, Batts, and Hostetter, P.A., all of The Institute's financial records and related data, as well as the minutes of the board of directors' meetings. Management believes that all representations made to Graham, Cottrill, Jackson, Batts, and Hostetter, P.A., during its audit were valid and appropriate.

The IIA maintains a system of internal control, which is designed to provide reasonable assurance to management and to the board of directors regarding: the preparation and publication of reliable and accurate financial statements; safeguarding of assets against unauthorized acquisition, use, or disposition; and compliance with applicable laws and regulations. The system includes a documented organizational structure and division of responsibility, established policies and procedures that are communicated throughout The IIA, an internal audit function reporting to the audit committee of the board of directors, and the careful selection, training, and development of our people.

This year, The IIA has voluntarily elected to evaluate its system of internal control in accordance with the requirements of the U.S. Sarbanes-Oxley Act of 2002 and the COSO framework. The Institute has documented and tested the key processes used to record the activities of The IIA and prepare its financial statements.

For the annual report as of and for the year ending, December 31, 2004, we certify that to the best of our knowledge:

- This annual report does not contain any untrue statements of a material fact or omit to state a material fact necessary to make the statements misleading with respect to the period covered by the annual statement;
- The financial information included in this annual report fairly presents in all material respects the financial condition, results of operations, and cash flows of The IIA as of and for the periods presented in the annual report;
- An adequate system for disclosing controls and procedures exists to ensure that material information relating to The IIA is made known to us by others within The IIA;
- Disclosures of any change in The IIA internal control over financial reporting that occurred during the most recent fiscal quarter and has materially affected, or is reasonably likely to materially affect, The IIA's internal control over financial reporting are included in this report.

Date: 5/11/05

Albert Holzinger
Chief Operating Officer
The Institute of Internal Auditors

Eugene J. O'Neill, CIA
Assistant Vice President, Finance
The Institute of Internal Auditors.