Republic of Kenya

PSASB
PUBLIC SECTOR ACCOUNTING STANDARDS BOARD (KENYA)

GOVERNMENT OF KENYA

PUBLIC SECTOR ENTITIES
INTERNAL AUDIT MANUAL MODEL

April 2022

Distribution of this Manual

This Manual is strictly for use by all Internal Auditors working in the public sector entities in the Republic of Kenya. No parts of this Manual may be copied without the express written permission of its authors.

How to use this Manual

This Manual has been prepared to conform to the International Professional Practices Framework issued by the Global Institute of Internal Auditors. The International Standards for the Professional Practice of Internal Auditing are highlighted in grey in the Manual and annexed to the manual in Appendix C. Internal Auditors are encouraged to refer to the latest version of the standards available at www.global.theiia.org.

Audit templates will be provided separately at the Public Sector Accounting Standards Board website www.psasb.go.ke. The templates are designed to assist Internal Auditors in implementing best practices in Internal Auditing and Auditors may customize the templates to suit their individual circumstances.

Auditors should refer to the acronyms and definitions of words provided to understand the meaning attributed to names, words and phrases used in this Manual.

Contact Information

The Public Sector Internal Audit Manual was developed by the Public Sector Accounting Standards Board in collaboration with representatives of Heads of Internal Audit from public sector entities. Section 194 of the Public Finance Management Act, 2012, mandates PSASB to prescribe Internal Audit procedures. The Board, through a Gazette notice No. 5440 dated 8th August 2014, prescribed the International Professional Practices Framework for use by all public sector entities.

For further information regarding this manual contact.

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FOREWORD

Internal audit is a mandatory service in all public-sector entities, as stipulated in Public Finance Management Act, 2012 (PFMA) section 73(1) which requires all National government entities to establish Internal Audit functions. National Government Public Finance Management Regulations (PFMR) r161 require these Internal Audit functions to conduct Internal Audit in accordance with the International Professional Practices Framework (IPPF) and with policies and guidelines issued by the Public Sector Accounting Standards Board (PSASB) to ensure uniformity and consistency as stipulated in PFMA s194 (1) (c). Internal Audit functions are required to comply with Constitution of Kenya (2010) and other relevant laws, legislations, regulations and guidelines prescribed for the public sector.

The Head Internal Audit is charged with the responsibility of coordinating Internal Audit services.

The legal and policy mandate of Head Internal Audit is to support the Accounting Officer in ensuring they have effective Internal Audit functions that can enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight.

Internal Audit in the public sector plays a critical role in evaluating and providing reasonable assurance that the entities have implemented effective and efficient governance, risk management and control systems that will ensure the entities achieve their mandate and strategic objectives.

The development of this Manual is therefore a milestone in setting accepted government standards in Internal Auditing and intends to streamline the operations of Internal Audit in all the public sector entities in line with IPPF.

Public sector entities are required to customize this section for purposes of approval by the respective Governing bodies.

FCPA PIUS MUNGAI NDUATIH

CHAIRMAN, PUBLIC SECTOR ACCOUNTING STANDARDS

ACKNOWLEDGEMENT

The Public Sector Entities Internal Audit Manual has been developed to guide Internal Audit functions and Internal Auditors in public sector. This Manual reflects international best practices and standards, and is benchmarked against the policies and procedures of a number of countries and organisations and aligned to Mwongozo Code of Governance for State Corporations and the Public Sector Risk Management guidelines among other regulations.

The implementation of this Manual will demonstrate compliance with the Global Institute of Internal Auditors' International Professional Practices Framework (IPPF) to enhance the quality of Internal Audit work towards improvement of governance, transparency, accountability and integrity in public finance management.

We wish to acknowledge the invaluable support and encouragement received from the Heads of Internal Audit in the public sector and their support and input towards the development of the Public Sector Entities Internal Audit Manual.

FCPA FREDRICK RIAGA

CHIEF EXECUTIVE OFFICER, PUBLIC SECTOR ACCOUNTING STANDARDS

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LIST OF ABBREVIATIONS

ACFE	Association of Certified Fraud Examiners
CAATS	Computer Assisted Audit Tools and Techniques
CAE	Chief Audit Executive
CAF	Current Audit File
CIA	Certified Internal Auditor
COSO	Committee of Sponsoring Organizations of the Treadway Commission
CoK	Constitution of Kenya
EACC	Ethics and Anti-Corruption Commission
HIA	Head(s) of Internal Audit
IAF	Internal Audit Function
ICF	Internal Control Framework
ICT	Information Communication Technology
IIA	Institute of Internal Auditors
IPPF	International Professional Practices Framework
ISO	International Organization for Standardization
OAG	Office of the Auditor General
PAF	Permanent Audit File
PFM	Public Finance Management
PFMA	Public Finance Management Act
PFMR	Public Finance Management Regulations
PPRA	Public Procurement Regulatory Authority
PSASB	Public Sector Accounting Standards Board
QAIP	Quality Assurance and Improvement Program

PREAMBLE

A. BACKGROUND INFORMATION

The Public Finance Management Act (PFMA), 2012, and Public Financial Management Regulations (PFMR), 2015 requires National Government entities to establish Internal Audit functions and Audit Committees. Further Internal Audit functions and the Audit Committees are subject to the provisions of the Constitution of Kenya (2010), Mwongozo Code of Governance for State Corporation, Gazette notices, Government circulars, Audit Committee Guidelines (Audit Committee Charter and attendant templates provided in Appendix B) and any other applicable laws and regulations.

B. INTRODUCTION

Entities have made numerous strides following the establishment of Internal Audit function and Audit Committees in each public sector entity. The Public Sector Entities Internal Audit Manual was developed to guide Internal Auditors in the adoption of International Internal Auditing Standards to better deliver Internal Auditing services. The Manual includes procedures on audit engagements and management of the Internal Audit function, outlines the roles and responsibilities of Internal Auditors, and provides templates to help auditors document procedures carried out. The Internal Audit function has undergone reforms to enable it cope with the challenges of a dynamic practising environment.

The Manual reflects best practices in Internal Auditing as stipulated in the IPPF promulgated by the Global Institute of Internal Auditors (IIA). This Manual together with the Mwongozo Code of Governance for State Corporations and the Internal Audit guidelines provide a clear roadmap on practical implementation of Internal Audit Standards and position Internal Audit to contribute to the improvement of governance, transparency, accountability and integrity in public finance management. Additional guidelines will be issued from time to time on specific areas on Internal Audit work.

Through Gazette Notice 5440 of 8 July 2014, Public Sector Accounting Standards Board approved the adoption and application of International Professional Practices Framework by all Internal Auditors in public-sector entities.

In order to continue adding value in the delivery of Internal Auditing services, the Manual will be subject to amendments and periodic reviews to cater for new developments in the profession and include experience and lessons learnt in its implementation.

In implementing this Manual public sector entities will be required to customize the introduction section to include background information about the entity and respective primary legislation that govern the entity's mandate.

C. OBJECTIVES OF THE MANUAL

2040 – Policies and Procedures
The chief audit executive must establish policies and procedures to guide the internal audit activity.

This Public Sector Entities Internal Audit Manual (Manual) is developed and issued by the Public Sector Accounting Standards Board in accordance with its mandate in PFM Act s194 to provide frameworks and set generally accepted standards for the development and management of accounting and financial systems by all National Government entities. The Manual is aligned with the requirements of the Public Finance Management Act, 2012 (PFMA), Public Finance Management Regulations 2015 (PFMR r161), the IPPF, Internal Audit Charter, Internal Audit Guidelines 2016 published by the Public Sector Accounting Standards Board (PSASB) and the Audit Committee Guidelines, 2016.

The Internal Audit Manual is intended to:

1. Provide Internal Auditors in public sector with practical professional guidance, tools, and information for managing the Internal Audit function, and steps for planning, executing and reporting on Internal Audit work. The use of the Manual should help bring a systematic and disciplined approach to the audit of governance, risk management, and control processes, and additionally assist the Internal Auditor to meet the goal of adding value to their respective organisations.
2. Enhance the quality and effectiveness of the Internal Audit Function by paving the way to put into practice procedures and processes that would help it conform to International Professional Practices Framework (IPPF).
3. Be a source of reference on Internal Audit profession for the public sector entities in Kenya.

The Manual provides perspectives on Governance, Risk Management, Internal Control, and Fraud that underpin almost all Internal Audit work. The Manual also provides procedures and processes for maintaining a quality Internal Audit service.

Users of the Manual are expected to have at least basic knowledge and understanding of management frameworks including governance, risk management and control processes. In addition to the Manual, Internal Auditors and users of the Manual are expected to: familiarize themselves with the IPPF; have a comprehensive understanding of the Constitution of Kenya, laws, regulations, policies, procedures, strategies, rules, and directives established by the Parliament and National Government that govern the areas they are auditing including international and local development agencies and financial institutions requirements in order to design appropriate audit procedures. The users of this Manual shall make further reference to the IPPF Standards, Implementation and Supplemental guidelines.

The Manual is designed to be flexible and unrestrictive. It is not intended to restrict any initiative that Internal Auditors can bring to their work based on prior work experience, knowledge, and skills. In many instances, Internal Auditors are encouraged to exercise professional judgement, particularly in determining levels of risk, adequacy of internal control processes, and types of tests to carry out.

Where an Internal Auditor faces difficulties in understanding or complying with the Manual, then appropriate clarifications and/or assistance should be obtained from the Head Internal Audit. The HIA may seek further guidance from the Public Sector Accounting Standards Board (PSASB)

D. SCOPE AND APPLICATION OF THE MANUAL

This Manual applies to the Internal Audit functions in the public sector.

E. EFFECTIVE DATE AND REVIEW

This Manual shall be effective on the date approved by the PSASB. The Manual will take account of the latest international developments in Internal Audit and shall be reviewed every three years or when circumstances dictate.

F. CUSTOMIZATION

This being a model Internal Audit Manual and due to the diverse and wide range of assurance and consultancy services provided by Internal Audit functions, the various sizes and organisational structures of public sector entities, it is appreciated that the Manual may be customized by public sector entities to suit their situations and circumstances. In doing this, they shall ensure that such Internal Audit Manuals are consistent with the Public Finance Management Act, 2012, the Public Finance Management Regulations, 2015, the IPPF and this Model Internal Audit Manual. Requirements of the standards and law shall not be customised. The PSASB shall be at hand to assist the Internal Audit functions which may require assistance in the development of such Internal Audit Manuals.

G. STRUCTURE OF THE MANUAL

Internal Audit functions exist to help an entity accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes. This Manual demonstrates the systematic approach as outlined in the chapters herein as follows;

Chapter 1 Mandate of Internal Audit Function

Chapter 2 Managing the Internal Audit Activity

Chapter 3 Nature of Internal Audit Services

Chapter 4 Internal Auditing Process

Chapter 5 Quality Assurance and Improvement Programme

CHAPTER 1 – MANDATE OF INTERNAL AUDIT FUNCTION

Chapter 1 covers:

(i.) Definition of Internal Auditing
(ii.) Mission of Internal Audit
(iii.) Internal Audit Charter
(iv.) Core Principles for the Professional Practice of Internal Auditing
(v.) Standard 1000: Purpose, Authority, Roles and Responsibilities of the Internal Auditing
(vi.) Recognition of the Mandatory Guidance
(vii.) Standards 1100: Independence and Objectivity of the Internal Audit function
(viii.) The Code of Ethics

1.1 INTERNAL AUDIT DEFINITION

Internal Audit functions in the public sector must be consistent with the mandatory elements of the IPPF which include the Core Principles for the Professional Practices of Internal Auditing, the Code of Ethics, the Standards and the Definition of Internal Auditing.

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

1.2 MISSION OF IAF IN THE ENTITY

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

The IAFs in pursuit of their mission are to help the entity to satisfy their statutory and fiduciary responsibilities and employ public resources effectively and efficiently. The Internal Auditors shall ensure an independent and systematic evaluation of risk management, control and governance processes in the entity. IAFs should leverage the entire IPPF to facilitate their ability to achieve the mission.

1.3 INTERNAL AUDIT CHARTER

1000 – Purpose, Authority and Responsibility
The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework (the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the Standards, and the Definition of Internal Auditing). The chief audit executive must periodically review the internal audit charter and present it to Senior Management and the board for approval.

1010 - Recognizing Mandatory Guidance in the Internal Audit Charter
The mandatory nature of the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the Standards, and the Definition of Internal Auditing must be recognized in the internal audit charter. The chief audit executive should discuss the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework with Senior Management and the board.

1100 - Independence and Objectivity
The internal audit activity must be independent, and internal auditors must be objective in performing their work.

1110 – Organizational Independence
The chief audit executive must report to a level within the organization that allows the internal audit activity to fulfil its responsibilities. The chief audit executive must confirm to the board, at least annually, the organizational independence of the internal audit activity.

1111 – Direct Interaction with the Audit Committee
The chief audit executive must communicate and interact directly with the board.

1.3.1 MANDATORY RECOGNITIONS IN THE INTERNAL AUDIT CHARTER

The Internal Audit Function shall develop an Internal Audit Charter that prescribes the purpose, authority and responsibility of the function. The Charter must recognize the mandatory nature of the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, International Standards for the Professional Practice of Internal Auditing (Standards), and the Definition of Internal Auditing. The Charter shall be approved by the Governing body. The HIA shall be responsible for ensuring the purpose of IAF is achieved.

The Internal Audit Charter provides for:

(1.) **Purpose of the Internal Audit** is to provide reasonable assurance on the effectiveness and efficiency of the entity's risk management, control and governance. (Assurance and consulting services)

(2.) **Internal Audit Authority:**

The Charter should be consistent with the Mission of Internal Audit and the mandatory elements of the IPPF. The IAF shall:

(a) Have full, free, and unrestricted access to all functions, records, property, and staff pertinent to carrying out any engagement, subject to accountability for confidentiality and safeguarding of records and information.

(b) Allocate resources, set frequencies, select subjects, determine scopes of work, apply techniques required to accomplish engagement objectives, and issue reports.

(c) Obtain assistance from the necessary personnel of the entity as well as other specialized services from within or outside the entity in order to complete the engagement.

(3.) **Internal Audit Independence and Objectivity:**

Independence is the freedom from conditions that threaten the ability of the Internal Audit activity to carry out Internal Audit responsibilities in an unbiased manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the Internal Audit activity, the Head Internal Audit has direct and unrestricted access to Senior Management and the Governing body. This can be achieved through a dual-reporting relationship. Threats to independence must be managed at the individual auditor, engagement, functional, and organizational levels.

Objectivity is an unbiased mental attitude that allows Internal Auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that Internal Auditors do not subordinate their judgment on audit matters to others. Threats to objectivity must be managed at the individual auditor, engagement, functional, and organizational levels.

The PFMR r.162 has various provisions to ensure the organizational, functional, operational and reporting independence of the HIA and the Internal Auditors. The provisions include:

(a) The HIA reports administratively to the Accounting Officer, and functionally to the Governing body;

(b) The HIA shall have unrestricted, direct and prompt access to all records, officials or personnel holding any contractual status and to all the premises and properties of the entity for the purpose of performing the Internal Audit function;

(c) Internal Auditors shall have no direct operational responsibility or authority over any of the activities they review and shall not develop nor install systems or procedures, prepare records, or engage in any other activity which would normally be audited;

(d) Internal Audit activities shall remain free of influence by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of an independent and objective mental attitude necessary in rendering reports;

(e) The Governing body shall approve the annual work plan of the IAF and monitor its execution through communications received from the HIA;

(f) The IAF should be provided with an independent budget allocation to fund the Internal Audit activities which shall be approved by the Governing body; and

(g) The Internal Auditors have a responsibility not to accept any gift, fees or hospitality from an employee, supplier, business associate or client, the acceptance of which will impair the auditor's objectivity.

(4.) **Internal Audit Reporting Structure:**

(a) Functional Reporting to the Governing Body

As provided in PFMR the HIA reports functionally to the Governing body through the Audit Committee which shall:

(i.) Approve the Internal Audit Charter;

(ii.) Approve the risk-based Internal Audit plan;

(iii.) Approve the Internal Audit budget and resource plan;

(iv.) Receive communications from the HIA on the Internal Audit function's performance relative to its plan and other matters;

(v.) Approving decisions regarding the appointment and removal of the HIA;

(vi.) Make appropriate inquiries of management and the HIA to determine whether there are inappropriate scope or resource limitations; and

(vii.) Drive the assessment of the performance of the Head Internal Audit.

(b) Administrative reporting to the Accounting Officer:

As stipulated by PFMR r.162 (2), Accounting Officer shall ensure that the Internal Audit function is appropriately structured to safeguard its independence and objectivity and to ensure the function achieves its roles and responsibilities.

The HIA shall administratively report to the Accounting Officer who shall ensure that the organizational structure of the IAF facilitates:

(i.) The function to accomplish its purpose and responsibilities;

(ii.) Internal Auditors with sufficient authority to promote independence and to ensure broad Internal Audit coverage and adequate consideration of audit reports;

(iii.) Appropriate action to be taken on Internal Audit recommendations; and

(iv.) The Internal Auditors to be independent of the programs, operations, and activities he or she audits to ensure the impartiality and credibility of the audit work undertaken.

The ***Internal Audit Charter Template 1*** is provided in the Appendix.

1.4 CORE PRINCIPLES FOR THE PROFESSIONAL PRACTICE OF INTERNAL AUDITING

The IIA's Core Principles for the Professional Practice of Internal Auditing are part of the Mandatory Guidance of the IPPF. The Core Principles taken as a whole demonstrate Internal Audit effectiveness.

For an Internal Auditor as well as an Internal Audit function to be considered effective, all principles should be present and operating effectively. Failure of an Internal Auditor or the Internal Audit function to achieve any of the principles means that the Internal Audit function may not be effective as it should be in achieving the Internal Audit's mission.

In demonstrating the Core Principles for the professional practice of Internal Auditing, HIAs are encouraged to refer to relevant recommended guidance materials. The Institute of Internal Auditors has provided a practice guide on demonstrating the Core Principles for the Professional Practice of Internal Auditing

The Internal Audit function should demonstrate the following Core Principles;

(1.) Demonstrates Integrity

(2.) Demonstrates competence and due professional care

(3.) Is objective and free from undue influence (independent)

(4.) Aligns with the strategies, objectives and risks of the organization

(5.) Is appropriately positioned and adequately resourced

(6.) Demonstrates quality and continuous improvement

(7.) Communicates effectively

(8.) Provides risk-based assurance

(9.) Is insightful, proactive and future-focused

(10.) Promotes organizational improvement

1.5 IMPAIRMENT TO INDEPENDENCE OR OBJECTIVITY

1120 – Individual Objectivity
Internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest.

1130 – Impairments to Independence and Objectivity
If independence or objectivity is impaired in fact or appearance, the details of the impairment must be disclosed to appropriate parties. The nature of the disclosure will depend upon the impairment.

1112 – Chief Audit Executive Roles Beyond Internal Auditing
Where the chief audit executive has or is expected to have roles and/or responsibilities that fall outside of internal auditing, safeguards must be in place to limit impairments to independence or objectivity.

1.5.1 ACTIVITIES THAT MAY IMPAIR INDEPENDENCE OR OBJECTIVITY

PFMR r. 162(5) requires that all Internal Audit activities remain free of influence by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of an independent and objective mental attitude necessary in rendering reports.

There are situations in which certain responsibilities may create (actual or perceived) impairment of the Internal Audit independence or objectivity. Such responsibilities include:

(1.) Supporting management in the development and implementation of policies and procedures.

(2.) Conducting investigations.

(3.) Compliance or risk management implementation activities.

Internal Auditors may at times be in situations that may result to impairment of their independence or objectivity. These include:

(1.) Auditing an area where recently the Internal Auditor was undertaking a management role.

(2.) Auditing an area which may result to conflict of interest e.g. an area where family member of close friend is working in or an area where the Internal Auditor has self-interest.

(3.) Preconceived ideas towards individuals, or towards the audited bodies or their projects or programmes.

(4.) Auditing an area where the Internal Auditor recently provided consulting services in which the nature of the consulting impaired objectivity and the individual objectivity was not managed when assigning resources to the assignment.

(5.) Financial interest by the Internal Auditor or close association in the audited body, or its activities.

(6.) Assuming without evidence that an area under audit is acceptable based solely on prior positive experience.

(7.) Long-term deployment of Internal Audit staff to one Department or Function can affect their independence and impartiality.

Impairment to the independence or objectivity of Internal Audit function may also arise due to:

(1.) HIA reporting functionally to an office which the IAF is expected to audit.

(2.) HIA does not have functional reporting to the Audit Committee.

(3.) Limitation of scope.

(4.) Limitation of authority.

(5.) Lack of control over the budget of the IAF.

(6.) Resource limitation including funding, human capital.

(7.) Undue influence on the plan, audit procedures and audit reports.

(8.) Restricted access to those charged with governance, records, other personnel, physical resources and assets necessary for the performance of the audit;

(9.) HIA is unable to conduct audits and report findings, opinions, and conclusions objectively without fear of reprisal.

1.5.2 SAFEGUARDS TO LIMIT IMPAIRMENTS TO INDEPENDENCE OR OBJECTIVITY

To manage the risk of impairment of IAF or Internal Auditor independence or objectivity the Governing body and Accounting Officer shall work with the HIA to:

(1.) Ensure Internal Auditors do not;

- (a) Perform management or operational duties;
- (b) Initiate or approve accounting transactions external to the IAF; or
- (c) Direct the activities of any employee in the entity not employed by the IAF, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the Internal Auditors.

(2.) Where management activities have been assigned to IAF by the Governing body and Accounting Officer, a transition plan to be developed by the Accounting Officer to move these activities out of IAF.

(3.) Ensure Internal Auditors exhibit professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined or audited.

(4.) Ensure Internal Auditors make balanced assessments of all available and relevant facts and circumstances and disclose all material facts known which if not disclosed could distort the reports or conceal unlawful practice.

(5.) Ensure Internal Auditors take necessary precautions to avoid being unduly influenced by their own interests or by others in forming judgments.

(6.) Ensure Internal Auditors do not accept any gifts, inducements, or other benefits from employees of the function being audited, or their suppliers and other third parties.

(7.) Obtain external assurance on management activities being undertaken by IAF.

(8.) Regularly review the responsibilities assigned to the HIA and the impact they have on independence and objectivity of IAF and Internal Auditors.

(9.) Regularly review the reporting lines of the HIA and assess if there are any factors that would impair Internal Audit objectivity and independence.

(10.) Ensure the HIA has developed an effective system for identifying, reporting and resolving impairment factors which shall include:

- (a) Ensuring an Internal Auditor shall not perform audit assignments for providing assurance relating to activities and structures on which he or she has provided consulting services or in which he had been employed over in the last twenty-four months as stipulated by PFMR r. 168; and
- (b) IAF performance management system balances between audit client feedback, results of the audit process and undertaking audit engagements.
- (c) Undertaking adequate supervision by reviewing of each audit assignment

(11.) Ensure the HIA discloses any interference and related implications in determining the scope of Internal Auditing, performing work, and/or communicating results to the Governing body and Accounting Officer.

(12.) Establish a system for Internal Auditors to report conflict of interest.

(13.) Ensure that planning and assigning Internal Auditors to audit engagements reduces the risk of conflict of interest.

(14.) Ensure the Internal Auditors sign a declaration of independence and objectivity on a regular basis or at least annually.

The ***Declaration of Independence and Objectivity, Template 2*** is provided in the Appendix.

(15.) Ensure the Accounting Officer and the Governing body receive confirmation from the HIA at least annually on the independence of the Internal Audit Function.

(16.) Ensure there are safeguards in place to limit impairments to independence or objectivity in instances where the HIA has been assigned roles and responsibilities that fall outside of Internal Auditing role.

Where the HIA determines that a certain threat will impair the organizational independence and objectivity of the Internal Audit function, he or she shall communicate in writing to the Audit Committee. The HIA shall include the following in the report;

(1.) The identified threat(s)

(2.) Analysis of the threat(s), including root cause analysis

(3.) Projected impact of the threat(s)

(4.) Suggested safeguard interventions

The Audit Committee shall discuss the threats to Organizational Independence and objectivity in their meetings. The Audit Committee shall pursue the matter with the Management to provide for safeguards against such threats and action plan towards eliminating the threats.

1.6 CODE OF ETHICS

Internal Auditors shall maintain high standards of professional ethics and shall observe the ethical and professional requirements of their professional bodies. Internal Auditors shall be expected to conform to the IIA Code of Ethics that outline the principles and rules of conduct for the internal audit profession. (Provided in Appendix B).

CHAPTER 2 – MANAGING THE INTERNAL AUDIT ACTIVITY

Chapter 2 covers factors that the Head Internal Audit needs to put in place to effectively manage the Internal Audit Function.

2000 – Managing the Internal Audit Activity
The chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organization.

The Internal Audit Function is considered to be adding value to the organization and its stakeholders when it considers strategies, objectives and risks impacting the organization; and strives to offer ways to enhance governance, risk management and controls processes and systems of the organization.

2.1 STRATEGIC & ANNUAL PLANNING

2010 - Planning
The chief audit executive must establish a risk-based plan to determine the priorities of the internal audit activity, consistent with the organization's goals.

To ensure the planning process is risk-based, the HIA shall consult with the Governing Body and Senior Management and consider the Entity's strategies, key business objectives, associated risks, and risk management processes. In developing the IAF Strategic Plan and Annual Risk Based Plans, HIA are encouraged to refer to relevant guidance materials. The Institute of Internal Auditors has provided practice guide on;

(1.) Developing the Internal Audit Strategic Plan

(2.) Developing a Risk-based Internal Audit Plan

2.1.1 STRATEGIC PLANNING

PFMR r. 170 requires the HIA to prepare a three-year strategic plan from which an annual Internal Audit function plan shall be developed. In preparing this plan the HIA shall consider: the strategies, objectives, and risks of the Entity; and the Internal Audit Charter. The HIA shall ensure the Internal Audit Strategic Plan is in-line with the Entity's Strategic Plan. The Internal Audit strategic plan shall contain:

(1.) Vision

This is a possible and desirable future state of the Internal Audit Function in the entity. It describes aspirations for the future – a destination for the IAF.

(2.) Mission

The Mission of Internal Audit articulates what Internal Audit aspires to accomplish within an entity. It explains why the Internal Audit function exists, what its overall goal is, identifying the goal of its operations. The mission of Internal Audit forms part of the mandatory elements of the IPPF. The framework articulates that the mission of Internal Audit is;

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

(3.) Stakeholder Analysis

In the broadest sense, the beneficiaries of the services of Internal Audit are the taxpayers who are considered indirect customers. The stakeholders of Internal Audit services include organs that have oversight, management, and operating responsibilities of Entity. The organs include:

S/No.	Stakeholder	Expectations
1	Governing body	Timely and objective reporting. Value addition to improve organization processes
2	Senior Management	Timely and objective reporting. Value addition to improve organization processes
4	Office of the Auditor-General	Collaboration and co-operation for efficiency and effectiveness
5	Any other stakeholders as appropriate to the respective entities	Assurance on effectiveness of risk management, control, and governance processes

(4.) Goals

These are the key focus areas for the strategy that should be aligned to the strategic plan of the Entity.

(5.) Objectives and Strategies

These are performance targets to be achieved under each focus area. Each objective should have strategies of how it will be achieved and activities to support the strategies. Timelines for implementing each activity, associated costs, resources required and person to implement the activity should also be defined in the Internal Audit Strategic Plan.

(6.) Monitoring and Evaluation

The strategic plan should include a framework to monitor the implementation of the plan. The strategic plan should include a risk matrix indicating events that impede achievement of the plan and strategies instituted to manage these risk events. The Internal Audit Strategic Plan shall be reviewed during its mid-term in order to be responsive to the changes in the Entity's business, risks, operations, programs, systems, and controls.

(7.) Assumptions

The strategic plan should include information on the assumptions on which the plan is based on.

In addition to the above, the strategic plan shall also contain Critical success factors; SWOT Analysis; Budget; and Implementation plan.

The ***Internal Audit Strategic Plan, Template 3*** is provided in the Appendix.

2.1.2 ANNUAL PLANNING

PFMR r. 170 requires the HIA to prepare an annual risk-based audit plan based on the three-year strategic plan. The Internal Audit plan should be flexible enough to allow the HIA to review and adjust it as necessary in response to changes in the organization's business, risks, operations, programs, systems, and controls. Significant changes must be communicated to the Governing body and Senior Management for review and approval.

A risk-based plan enables the HIA to determine the priorities of the IAF that are consistent with the entity's objectives.

The annual planning process commences with;

(1.) Establishing the audit universe i.e. all auditable area that may include functions, processes, systems and locations.

(2.) Grouping the audit universe into manageable audit areas.

(3.) Risk assessment and risk mapping of the auditable areas.

(4.) Prioritization of the audit assignment in the annual risk-based audit plan.

(5.) Approval of the audit plan.

The ***Internal Audit Universe, Template 4*** is provided in the Appendix.

Risk-based auditing is adopted as per PFMR r. 170 (1) to ensure that limited resources are directed to areas of greater risk to the achievement of Entity objectives. This helps to prioritise limited audit activities. The IAF shall assess and rank each auditable unit based on its significance to the achievement of the Entity's objectives, its complexity in terms of ensuring that intended outcomes are achieved, and its sensitivity in terms of the public or the intended beneficiaries.

The HIA shall consider approaches such as the risk factor approach and the risk assessment approach when determining the areas in the audit universe that are to be audited in a particular financial year.

2.1.2.1 RISK FACTOR APPROACH

Under the risk factor approach the following factors (each factor is weighted based on its importance) can be considered:

(1.) **Risk assessment**: Based on the results of the Entity's Risk Assessment process, the HIA shall establish the high-risk areas that need to be audited from the audit universe (the all processes or functions that can be audited). Where the entity has not undertaken a risk assessment, the HIA shall facilitate a risk assessment (i.e. work with management to undertake risk assessment or undertake risk assessment and have management validate the results). This enables the HIA to focus the audit on high-risk areas instead of all the areas in the audit universe.

(2.) **Budgetary Allocation**: the HIA shall review the entity's strategic plan, annual budget, annual work plan, performance contract and other relevant literature to establish areas that will be allocated significant funding. Such areas are considered to be of higher risk compared to those that receive less funding.

(3.) **Areas of Management Concern**: the HIA shall engage the Senior Management to establish areas that management would like the Internal Audit to focus in the upcoming year. This may include areas that are: experiencing significant changes like process re-engineering, policy changes, automation, new policies and procedures etc; areas of high staff turnover; areas of weak performance; and areas of weak control.

(4.) **Significant Operational Changes**: the HIA shall engage the audit client to determine significant changes in systems, processes and personnel and the impact they have on the achievement of objectives and management of risks.

(5.) **Results of Prior Audits**: the HIA shall review the outcome of previous Internal, external, ISO auditors and other audits to identify areas that had significant weak governance, risk management and controls systems and processes and consider them for inclusion in the current annual audit plan. The HIA shall also consider: feedback from management on the implementation of audit recommendations; and the time lapse since an area was last audited.

Illustration 1 provide a guide that the HIA can adopt in determining the areas to audit in a financial year. The HIA can adjust the planning factors and weights appropriately during the annual planning process.

Illustration 1: Annual Auditing Plan Factors

Planning Factor	Weight (%)	Sub-Factors
Risk Assessment	30%	a. Risks that impact on the function b. Risk maturity level c. Fraud or corruption has been reported
Budgetary Allocation	25%	a. Rating based on budgetary allocation
Management Concern	20%	a. Weak performance of the area b. Consistent weak controls c. Opportunities to increase revenue or reduce costs
Significant Operational Changes	15%	a. New regulatory requirements b. High staff turnover c. New policies, procedures or systems d. Change in organizational structure
Prior Audit Results	10%	a. Internal Audit conclusion on governance, risk management and controls b. OAG audit opinion and areas of concern c. Rating by other assurance providers d. The last time the area was audited
Total	**100%**	

Illustration 2 provides sample planning factors and criteria for rating each planning factor. The HIA can adopt a score of; 3 for high rating; 2 for medium rating and 1 for low rating. The HIA can adjust the rating criteria and rating factors appropriately during the annual planning process.

Illustration 2: Annual Auditing Plan Factors Rating

Planning Factor	Sub-Factors	Rating
Risk Assessment	**Risks that impact on the function**	a. **High**: function impacted by strategic risks b. **Medium**: function only impacted by operational risks that are rated high and medium c. **Low**: function impacted by operational risks that are rated low risk
	Risk maturity level	a. **High**: No risk management established. Management have not identified risks and risk management strategies b. **Medium**: Risk management established and management has not identified all the risks and the risk strategies c. **Low**: risk management process is effective. Governing body and Accounting Officer are aware of the strategic risks, are providing oversight over their management and receive regular reports
	Fraud or corruption has been reported	a. **High**: in the last 12 months b. **Medium**: in the last 24 months c. **Low**: in the last 36 months or not reported at all
Budgetary Allocation	**Rating based on budgetary allocation**	a. **High**: i. More than Kes 10m; or ii. More than 10% of total budget b. **Medium**: i. Between Kes 1m and Kes 10m; or ii. Between 5% to 10% of total budget c. **Low**: iii. Less than Kes 1m; or i. Less than 5% of total budget
Management Concern	**Weak performance of the area**	a. **High**: variance of actual performance has been more than 10% in the last financial year b. **Medium**: variance of actual performance has been between 5% and 10% in the last financial year c. **Low**: variance of actual performance has been less than 5% in the last financial year
	Consistent weak controls	a. **High**: controls managing high risk areas have not performed as expected in the last 12 months b. **Medium**:

Planning Factor	Sub-Factors	Rating
		i. Controls managing medium risk areas have not performed as expected in the last 12 months; or ii. Controls managing high risk areas were reported not to have performed as expected more than 12 months ago but less than last 24 months ago c. **Low**: i. Controls managing low risk areas have not performed as expected in the last 12 months; or ii. Controls managing medium risk areas were reported not to have performed as expected more than 12 months ago but less than last 24 months ago iii. Controls managing high risk areas were reported not to have performance as expected more than 24 months ago but less than last 36 months ago
	Opportunities to increase revenue or reduce costs	a. **High**: i. Revenue may be increased by more than 5 % of last financial year audited accounts; or ii. Expenditure will reduce by more than 10% of last financial year audited accounts b. **Medium**: i. Revenue may increase by between 2.5% to 5% of last financial year audited accounts; or ii. Expenditure will reduce by between 5% and 10% of last financial year audited accounts c. **Low**: i. Revenue may be increased by less than 2.5 % of last financial year audited accounts; or ii. Expenditure will reduce by less than 5% of last financial year audited accounts
Significant Operational Changes	**New regulatory requirements**	a. **High**: the new law or regulation has a strategic impact on the entity and impacts on an area b. **Medium**: the new law or regulation has an operational impact on the entity and impacts on an area c. **Low**: the new law or regulation has little or low impact on the entity and impacts on an area
	High staff turnover	a. **High**: i. Turnover at the governance level ii. 10% and above turnover of Senior Management

Planning Factor	Sub-Factors	Rating
		b. **Medium**: i. Less than 10% but more than 5% turnover of Senior Management ii. 10% and above turnover of middle management/supervisors c. **Low**: i. Less than 5% turnover of Senior Management ii. Less than 10% but more than 5% turnover of middle management iii. 10% and above turnover of employees below middle management
	New policies, procedures or systems	a. **High**: i. Changes impact one or more directorates or divisions (this is the highest level of operation). ii. Changes impact departments in more than one directorate (this is the middle level of operation). b. **Medium**: the changes impact one or more departments within a directorate/division c. **Low**: the changes impact one or more processes (this is the middle level of operation) within a department
	Change in organizational structure	a. **High**: the changes impact on the governance level and Senior Management positions b. **Medium**: the changes impact on the middle management positions c. **Low**: the changes impact on the employees below middle management positions
Prior Audit Results	**Internal Audit conclusion on governance, risk management and controls**	a. **High**: rated as weak b. **Medium**: rate as strong with key areas of improvement c. **Low**: rated as strong
	OAG audit opinion and areas of concern	a. **High**: adverse opinion and areas that led to the opinion b. **Medium**: disclaimer opinion and area that led to the opinion c. **Low**: unqualified opinion

Planning Factor	Sub-Factors	Rating
	Rating by other assurance providers	a. **High**: i. Adverse opinion by external assurance providers e.g. Public Procurement Regulatory Authority (PPRA), Ethics and Anti-Corruption Commission (EACC) etc ii. Governance, risk management and controls rated as weak by Internal assurance providers b. **Medium**: Governance, risk management and controls rated as strong with key areas of improvement by other assurance providers (i.e. that are not IAF or OAG) c. **Low**: Governance, risk management and controls rated as strong by other assurance providers (i.e. that are not IAF or OAG)
	The last time the area was audited	a. **High**: more than 3 years ago b. **Medium**: more than 2 years ago c. **Low**: last financial year

2.1.2.2 RISK ASSESSMENT APPROACH

Using the risk assessment approach, the following steps are followed to assess the risks in each auditable unit;

(1.) Understanding the processes and objectives - Assessment of each auditable unit risk assessment begins with an understanding of the entity and unit, activities, or processes.

(2.) Identifying risks - The entity's strategic, financial, operational, regulatory and reputational risks at both a strategic and operational level are identified. Risks whether from external or internal sources are categorised using a suitable risk model. A ***Risk Model, Template 5*** is provided in the Appendix. Information on risks can be gathered:

- (a) From interviews of Senior Management;
- (b) By consulting external audit;
- (c) By reviewing recent audit reports;
- (d) From planning documents such as budgets, strategic plan etc;
- (e) From the external environment; and,
- (f) From other stakeholders.

(3.) Risk analysis

- (a) **Inherent risk assessment** - Risks are identified and assessed before considering the controls management has put in place.

(b) **Residual risk assessment** - The controls to mitigate the risks are mapped and their effectiveness considered in determining the residual risk rating based on management's perception and the auditor's professional judgement.

Where management has implemented a risk management framework, Internal Auditors should make use risk assessment conducted by management in developing Internal Audit plans. The ***Risk Control matrix, Template 6***, will be used to analyse the risks and arrive at a consensus of the risk rating.

Individual risks are profiled by combining the estimated risk likelihood and impact to give the significance of each risk. Risks shall be assessed as high, medium or low where:

(1.) **High**- A fundamental objective is not met or there is a critical weakness in controls. Resolution would help avoid a potentially critical negative impact involving loss of material assets, reputation, critical financial information, or ability to comply with the most important laws, policies, or procedures.

(2.) **Medium** - An important objective is not met or there is a significant weakness in controls. Resolution would help avoid a potentially significant negative impact on the unit's assets, financial information, or ability to comply with important laws, policies, or procedures.

(3.) **Low** - Objectives are mostly met but further enhancement of the control environment is possible. Resolution would help improve controls and avoid problems in the unit's operations.

Individual risk scores are grouped for each auditable area (process) to give the relative significance of each auditable area in the audit universe. Overall risk ratings can be classified as lower, moderate and higher risks and plotted on a ***Heat Map, Template 7***, provided in the Appendix. IA should consider the risk assessments conducted by management when preparing the Annual Audit Plan.

2.1.3 ANNUAL RISK-BASED INTERNAL AUDIT PLAN

Upon considering either of the above approaches and factors therein, the HIA shall develop the Annual Risk-Based Internal Audit Plan that includes:

(1.) A list of audit engagements and specification regarding whether the engagements are: assurance or consulting in nature; governance, risk management or controls engagements; and follow-up audits (as separate engagements or undertaken as part of engagements).

(2.) Objectives, scope and timing of each proposed engagement.

(3.) Rationale for selecting each proposed engagement based on assessment of the factors (i.e. risk assessment, budgetary allocation, management concern etc.)

(4.) Priority level of each engagement based on the risk rating. Area/s of high risk should have a higher frequency of review compared to those of lower risk rating.

Illustration 3 provides a guide on determining the frequency of auditing an area based on its risk. The allocation of audit frequency is a matter of professional judgement.

(5.) A list of initiatives or projects that result from the Internal Audit strategy but may not be directly related to an audit engagement.

(6.) Time allocated to undertake ad-hoc engagements requested by the Audit Committee or Accounting Officer. Ad-hoc requests by management must be approved by the Accounting Officer. There are times where the ad-hoc requests require more time than what has been allocated in the annual plan. The HIA shall assess the risk profile of the requests and compare with the scheduled engagements to determine if the ad-hoc requests have a higher priority (have a higher risk) than some of the scheduled engagements and adjust the annual plan appropriately.

(7.) The staff resources and other resources available, expected and budgeted.

(8.) The resource gap if any, including proposals on how this gap could be dealt with, and the risks consequences arising if the proposals are not able to be implemented.

(9.) A summary of capacity building that is planned to take place during the period.

Annual Risk-Based Internal Audit Work Plan Template 8 is provided in the Appendix.

Illustration 3: Auditing Frequency

Risk Rating	Frequency of Auditing
High	More Than Once every year
Medium	Every year
Low	Every three years.

2.2 INTERNAL AUDIT FUNCTION STAFFING AND PROFICIENCY

2.2.1 STAFFING INTERNAL AUDIT FUNCTION

The IAF should be appropriately staffed in terms of numbers, grades, qualification levels, and experience, having regard to the Internal Audit Charter, Internal Audit Strategic Plan and Annual Internal Audit Risk-Based Plan. The HIA shall ensure that those with appropriate background, personal qualities, and potential should be recruited as Internal Auditors. Thereafter, steps should be taken to give them the necessary training and experience.

The HIA shall work with the Accounting Officer to ensure the human capital management programme and terms of employment (Career Progression Guidelines) enable the IAF to attract and retain staff with the appropriate academic and professional qualifications, experience, and personal attributes. The HIA shall specify the required competencies, including minimum qualification, experience, and other criteria for appointment/promotion of Internal Auditors to the more senior grades.

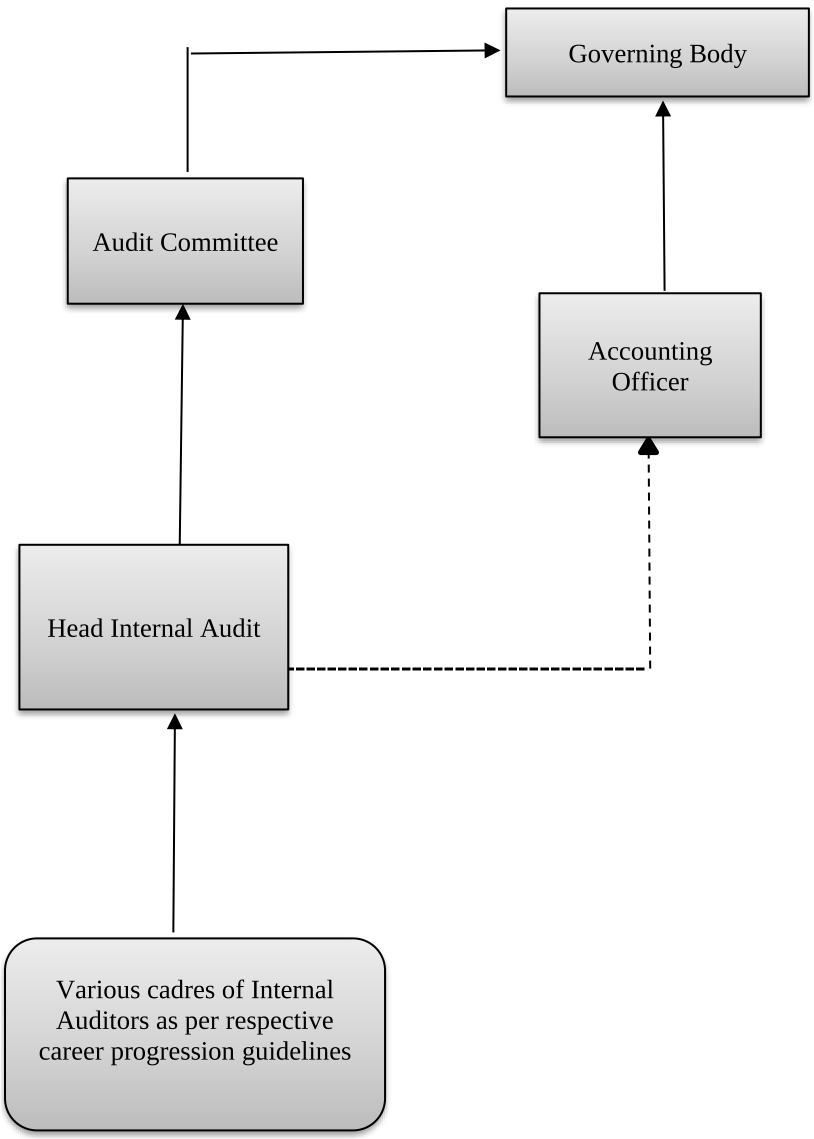
As stipulated in PFMR r. 162(2) the Accounting Officer shall ensure the Internal Audit Function is appropriately placed and the HIA is appropriately positioned to enable: the IAF accomplish its Internal Audit responsibilities; the Internal Auditors have sufficient authority to promote independence, ensure broad Internal Audit coverage and adequate consideration of Internal Audit reports; appropriate action is taken on Internal Audit recommendations.

The Audit Committee guidelines through the gazette notice no.2691 provide that the HIA reports functionally to the Audit Committee that in turn reports to the Governing Body.

To ensure the entity's Internal Audit Function has the appropriate human capital to meet the required proficiency levels, the IAF shall have a hierarchy that best fits the entities' structure as approved by the relevant Government bodies.

The IAF Structure is provided in Illustration 4.

Illustration 4: Internal Audit Function Structure



Key

------------------------- Administrative reporting

__________________ Functional reporting

NB: ***Standard 1110 Organizational Independence*** - The HIA must report to a level within the organization that allows the Internal Audit activity to fulfil its responsibilities. Mwongozo Code of Governance for state corporations requires Audit Committee to ensure that the HIA holds a senior position in the management team, is professionally qualified and is a member in good standing of the professional body responsible for regulating Internal Auditors.

Job descriptions and job specifications shall be as provided in Career progression guidelines adopted for the entity.

2.2.2 RESOURCE MANAGEMENT

> **2030 – Resource Management**
> The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

2.2.2.1 STRATEGIC PLAN RESOURCING

The HIA shall establish the resources required in implementing the Internal Audit Strategic Plan and timelines of acquiring the same. This shall be integrated with the entity's strategic and business plans to ensure that as the entity is seeking funding to implement its strategic plan the funding requirements of IAF are also considered. The Internal Audit Strategic Plan shall be implemented through the Annual Risk-Based Internal Audit Plan and thus resource mobilization to support the Strategic Plan shall be undertaken through the annual audit plan.

The HIA shall ensure the resources are appropriate in terms of the mix of knowledge, skills, and other competencies needed to perform the plan. The resources should also be sufficient in terms of the quantity of resources needed to accomplish the plan. Resources shall be deemed to be effectively deployed when they are used in a way that optimizes the achievement of the approved plan.

2.2.2.2 ANNUAL PLAN RESOURCING

The Annual Risk-Based Internal Audit Plan contains Internal Audit engagements and a list of initiatives or projects that result from the Internal Audit strategy but may not be directly related to audit engagements. The HIA, in developing the budget to support the annual audit plan, shall consider the two elements. The HIA shall consider the following steps in establishing the budget to support the Annual Risk-Based Internal Audit Plan.

(1.) Establishing Human Capital Resources

Based on the auditable areas identified in the Annual Risk-Based Audit Plan, the HIA shall:

(a) **Assess the Workload**: consider the effort required to audit each area selected for audit. This can be based on factors like: resources required in the past to undertake the audits; changes in the area that may require less/more resources; or challenges faced in the past in undertaking audits in the areas. When developing the schedule for Internal Audit engagements the HIA shall consider key activities of the entity to ensure availability of the audit client.

(b) **Determine the Resources available:** This is estimated by taking the number of man-days to be provided by each staff in the IAF after making allowance of time for training, annual leave, holidays, estimated sickness time and any other non-productive time. In determining the resources available, the HIA shall ensure there is appropriate mix of knowledge, skills and other competencies needed to achieve the annual plan.

Time management: To enhance time management on audits, a time budget should be prepared for each audit assignment and used as a "benchmark" for the actual hours spent on the assignment. Furthermore, the Internal Auditors should prepare daily time sheets which show the tasks accomplished on each working day and the number of "person-hours" spent on each task. Those time sheets should be reviewed and approved by the HIA and filed in the administration section of the audit file.

Daily time sheet, Template 9 and ***Work allocation and time budget, Template 10*** are provided in the Appendix.

(c) **Balancing the resources available with the Workload:** this involves getting more resources (either through hiring, out-sourcing or co-sourcing) or reducing the workload to fit with the resources available. In reducing the workload, the HIA should evaluate the risk exposure of not covering an area. Reducing the workload can be achieved through:

(i.) Omitting certain tasks from the annual plan with the intention of completing them in the following year;

(ii.) Reducing the staff budgets for the individual tasks by reducing the depth of each assignment; and

(iii.) Reducing the frequency of auditing an area.

In balancing the workload, the HIA shall also provide reserves to cater for changes in the annual audit plan that may result due to: ad-hoc requests by the Audit Committee or management; or new high-risk areas detected (by Audit Committee, management or Internal Audit) during the financial year.

A ***Resource calendar or Chronogram, Template 11*** provided in the Appendix, shall be completed for all activities in the annual plan.

(2.) Establishing Non-Human Capital Resources

The HIA shall establish the resources required to support the Internal Auditors in implementing the Annual Risk-Based Internal Audit Plan. This shall include:

(a) **Travel, accommodation and other ancillary costs:** the HIA shall establish the level of travel and related expenses that are required in undertaking the Internal Audit engagements based on the expected work load.

(b) **Tools and equipment:** the HIA shall review the existing tools, equipment and technology requirements vis-à-vis what is required to meet the expected workload to determine sufficiency of the same. Where there is a gap the HIA shall consider developing a resourcing strategy to obtain the required tools, equipment and techniques. The HIA shall consider the acquisition and management of data analysis tools – CAATs to extract and analyse large volumes of data, which would be inefficient to do manually. This will be in conformance with the IPPF standards that require Internal Auditors to possess sufficient knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work.

(c) **Non-audit strategic initiatives:** the HIA shall review the Internal Audit Strategic Plan to establish the strategic initiatives that are to be implemented in the financial year under consideration and determine the resources required to support their implementation.

(d) **Administrative resources:** the HIA shall establish in-direct costs related to supporting the achievement of the annual audit plan. This includes costs related to capacity building/training and other administrative tasks.

(3.) Compiling IAF Budget

The HIA shall compile the human capital and non-human capital requirements to establish the IAF annual budget.

Annual Risk-Based Internal Audit Work Plan, Template 8 provided in the Appendix contains items to be considered in formulating the IAF Budget.

2.2.3 INTERNAL AUDIT STAFF COMPETENCY

> **1200 – Proficiency and Due Professional Care**
> Engagements must be performed with proficiency and due professional care.

Performing engagements with proficiency and due professional care is the responsibility of every Internal Auditor. The HIA shall be responsible for ensuring that all Internal Auditors perform engagements with proficiency and due professional care by ensuring they possess the required knowledge, skills and other competencies. The HIA shall achieve this through attracting and retaining competent staff; ensuring continuous capacity building; and adequate planning, staffing and supervision.

2.2.3.1 PROFICIENCY

Proficiency is a collective term that refers to the knowledge, skills, and other competencies required of Internal Auditors to effectively carry out their professional responsibilities. It encompasses consideration of current activities, trends, and emerging issues, to enable relevant advice and recommendations.

> **1210 – Proficiency**
> Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

Internal Auditors shall seek to maintain and develop their professional knowledge, skills, and competencies as provided for in the entity's Career Progression Guidelines. Internal Auditors shall seek the highest levels of proficiency and take personal responsibility for self-improvement and professional development.

The HIA shall ensure the individual Internal Auditors and the IAF collectively have the required mix of knowledge, skills and other competencies to implement: the Internal Audit Charter; Internal Audit Strategic Plan and Annual Risk-Based Internal Audit Plan; and to add value to the entity.

Internal Audit should be performed by or be under the control of auditors who have the technical skills, experience, and perspective in other areas of audit that will enable them to comply with the IPPF and this Manual. Internal Auditors should be properly trained to fulfil their responsibilities and should maintain and enhance their professional competence through an appropriate ongoing development programme.

2.2.3.2 DUE PROFESSIONAL CARE

1220 – Due Professional Care

Internal auditors must apply the care and skill expected of a reasonably prudent and competent internal auditor. Due professional care does not imply infallibility.

Due professional care requires the Internal Auditors to understand the IPPF, have the competencies and work with diligence to implement this Manual (that has been aligned to IPPF and Government of Kenya Internal Audit Guidelines for National Governments) and other guidelines issued by the Government. The Internal Auditor shall be expected to apply professional judgement, apply the required expertise, and take appropriate steps when planning, executing (gathering and evaluating audit evidence) and reporting on an audit engagement. This will enable the Internal Auditor to gain the respect and co-operation from the audit clients.

In undertaking Internal Audit activities, the Internal Auditors shall be expected to exercise skills of a reasonably prudent and competent Internal Auditor in the same or similar circumstances. However, the Internal Auditor shall be expected to provide reasonable assurance and not absolute assurance. Reasonable assurance includes the understanding that there is a remote likelihood that material misstatements will not be prevented or detected on a timely basis. Absolute assurance on the other hand means that there is no assurance risk. In exercising due professional care, the Internal Auditors shall be alert to:

(1.) The possibility of intentional wrong doing.
(2.) Errors and omission.
(3.) Unusual transactions.
(4.) Unauthorized operations.
(5.) Inefficiency, waste, and ineffectiveness.
(6.) Conflicts of interest.
(7.) Fraud and corruption.
(8.) Conditions and activities likely to give rise to non-compliance.
(9.) Inadequate controls including inadequate record keeping.

Due professional care should be appropriate to the objectives, complexity, nature, and materiality of the audit being performed. In exercising due professional care, the Internal Auditor shall: assess the adequacy of the risk management, governance and controls of the area/s being audited; consider and document the work needed to achieve engagement objectives; and use all reasonable care and attention to obtain sufficient, relevant, and reliable evidence on which to base audit conclusions and opinions.

2.2.3.3 CONTINUING PROFESSIONAL DEVELOPMENT

1230 – Continuing Professional Development

Internal auditors must enhance their knowledge, skills and other competencies through continuing professional development.

The Internal Auditors shall be required to consider current activities, trends, and emerging issues, to enable them to provide relevant advice and recommendations to Senior Management and the Governing Body. This requires the Internal Auditors to continuously enhance their proficiency. The Internal Auditors shall be responsible for ensuring they continuously obtain the required knowledge, skills and other competencies in order to enhance their proficiency.

Although each individual Internal Auditor is responsible to maintain his/her proficiency, the HIA shall be responsible for ensuring the IAF has the minimum required mix of competencies. The HIA shall report on the adequacy of resources including competencies to the Audit Committee and shall develop a Training and Development Plan to achieve this which shall contain strategies to:

(1.) Enhance Internal Audit techniques.

(2.) Provide on-the job training, coaching and mentoring to enable the Internal Auditors to enhance their experience.

(3.) Sensitize and provide training on the operations of the entity to enable the Internal Auditors to have an in-depth understanding of the operations of the entity.

(4.) Acquire specialist training for those Internal Auditors responsible for a particular activity such as ICT audit, forensic auditing, data analytics, system design, procurement audit, compliance audit, technical audits, project management etc.

(5.) Enhance the professional development of the Internal Auditors by developing a competency framework aligned to the IIA competency framework, entity's career progression guidelines and ensuring the Internal Auditors attain relevant certifications and qualifications including the Certified Internal Auditor, Certified Government Audit Professional, Certified Information Systems Auditor, Certified Fraud Examiner among others.

(6.) Manage training for Internal Auditors with responsibility for managing and directing Audit Teams, together with those staff members who show potential for management positions.

(7.) Continuously develop Internal Auditors professionally as per the requirement of their respective professional bodies.

(8.) Ensure regular assessment of available competencies in the IAF vis-à-vis current and future demand for Internal Audit services.

(9.) Link the policy and plan to the entity's performance management system.

(10.) Ensure appropriate information is maintained for all capacity building initiatives and their effectiveness (closing skill gaps identified during performance evaluation) are continuously assessed.

(11.) Ensure the capacity building programme are adequately resources.

2.3 PLAN COMMUNICATION AND APPROVAL

2020 – Communication and Approval
The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to Senior Management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.

As stipulated in the PFMR r. 170(1) the Annual Risk-based Internal Audit Plan and budget preparation and communication to Governing body and Senior Management shall be in-line with the entity's budgeting process and timelines so as to ensure the final approved plan and budget forms part of the entity's budget. This session enables HIA to obtain the support of the Senior Management in implementing the annual plan and obtain the required resources to support the annual plan. The Accounting Officer as stipulated in PFMR r. 162 shall ensure the IAF has vote and adequate budget allocation to fund Internal Audit function activities. The HIA shall then submit the updated Risk-Based Internal Audit Plan and budget to the Governing Body for review and final approval.

On a quarterly basis the HIA shall provide progress reports to the Governing Body and Senior Management on the implementation of the plan and budget (reviews, adjustments and re-allocations). Such reports shall provide information on any resource constraints that the IAF is facing and the impact of this on the implementation of the Internal Audit plan and the risk exposure that the entity may face.

2.4 COORDINATION AND RELIANCE

2050 – Coordination and Reliance

The chief audit executive should share information, coordinate activities, and consider relying upon the work of other internal and external assurance and consulting service providers to ensure proper coverage and minimize duplication of efforts.

In implementing Standard 2050, HIA are encouraged to refer to relevant guidance materials. The Institute of Internal Auditors have provided the following implementation and practice guides;

(1.) Co-ordination and Reliance
(2.) Reliance by Internal Audit on other Assurance Providers
(3.) Co-ordination and Reliance: Developing an Assurance Map

In coordinating activities, the Head Internal Audit may rely on the work of other assurance and consulting service providers. The Head Internal Audit should have a clear understanding of the scope, objectives, and results of the work performed by other providers of assurance and consulting services. Where reliance is placed on the work of others, the Head Internal Audit is still accountable and responsible for ensuring adequate support for conclusions and opinions reached by the Internal Audit activity. Examples of coordinating activities may include:

(1.) Synchronizing the nature, extent, and timing of planned work.

(2.) Ensuring a common understanding of assurance techniques, methods, and terminology.

(3.) Providing access to one another's work programs, workpapers, and reports.

(4.) Relying on one another's work to minimize duplication of effort.

(5.) Meeting intermittently to determine whether it is necessary to adjust the timing of planned work, based on the results of work that has been completed.

Roles of assurance and consulting service providers vary by entity and can generally be categorized as either internal providers or external providers.

(1.) Internal providers include oversight functions that either report to Senior Management or are part of Senior Management. Their involvement may include areas such as environmental, financial control, health and safety, IT security, legal, risk management, compliance, or quality assurance. These are often considered "second line of defence" activities, according to The IIA's Three Lines Model.

(2.) External assurance providers may report to Senior Management or external stakeholders, or they could be hired by and report to the HIA.

A consistent process for the basis of reliance should be established, and the Head Internal Audit should consider the following factors:

(1.) **Objectivity**: does the service provider have any real or perceived conflict of interest? Has existing conflict of interest been reported?

(2.) **Independence**: what is the service provider reporting relationships and the impact of this arrangement?

(3.) **Competency**: verify whether the provider's professional experience, qualifications, certifications, and affiliations are appropriate and current.

(4.) **Due professional care**: by understanding the service provider's methodology and whether the work undertaken is appropriately planned, supervised, documented, and reviewed. This may also involve understanding the standards by which the other service provider operate on.

(5.) **Reasonableness of work done**: gain an understanding of the scope, objectives, and results of the actual work performed to determine the extent of reliance that may be placed on the provider's work. This involves assessing whether the output of the work done is based on sufficient, reliable and relevant evidence.

(6.) **Confidentiality requirement**: the HIA shall consider the entity's confidentiality requirements especially when dealing with sharing information with external service providers.

The process of coordinating assurance activities varies by entity. One way to coordinate assurance coverage is to create an assurance map by linking identified significant risk categories with relevant sources of assurance and rating the level of assurance provided for each risk category. Because the map is comprehensive, it exposes gaps and duplications in assurance coverage, enabling the HIA to evaluate the sufficiency of assurance services in each risk area. The results can be discussed with the other assurance providers so that the parties may reach an agreement about how to coordinate activities to minimize duplication of efforts and maximize the efficiency and effectiveness of assurance coverage. Another approach to coordinating assurance coverage is a combined assurance model, where Internal Audit may coordinate assurance efforts with second line of defense functions, such as a compliance function, to reduce the nature, frequency and redundancy of Internal Audit engagements.

2.4.1 COORDINATION AND COLLABORATION WITH THE OFFICE OF THE AUDITOR GENERAL

The Office of the Auditor General who is the external auditor of the entire public sector is established under Article 229 of the Constitution. The Public Audit Act Section 33 stipulates that: the final Internal Audit report which has been deliberated on and adopted by an Audit Committee of an entity, may be copied to the Auditor-General; and the Auditor-General shall have unhindered access to all Internal Audit reports of an entity. The Public Audit Act stipulates that the Accounting Officer shall support the OAG in fulfilling its mandate. Internal Audit is part an entity's internal controls and the OAG has the mandate to review effectiveness of all internal controls.

In addition to the Constitution and the Public Audit Act, the International Standards of Supreme Audit Institutions (ISSAI) that guide how the Office of the Auditor General undertakes external audits provides on how the office can cooperate with the Internal Auditors:

(1.) ISSAI 1/3/par.3 provides for guidance on how the OAG can assign tasks and cooperate with Internal Auditors where the OAG in their own judgement have assessed the IAF to be effective.

(2.) ISA 315, 23 provides guidance on how the OAG can determine whether the IAF is likely to be relevant to the audit being undertaken.

(3.) ISA 610 and ISSAI 1610 provides guidance on how OAG can use the work of the Internal Auditor.

PFMR r. 172 (1) stipulates that the Accounting Officer shall be responsible for the implementation of audit recommendations of the audit reports, both external and Internal Audit reports and further develop response and action plan which they shall submit to the Chairperson of the Audit Committee within fourteen days. PFMR r. 172 (2) and Gazette Notice 2691 stipulate that the Audit Committee shall provide oversight over the implementation of audit recommendations by OAG.

2.5 REPORTING TO THE SENIOR MANAGEMENT AND THE GOVERNING BODY

2060 – Reporting to Senior Management and the Board
The chief audit executive must report periodically to Senior Management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan and on its conformance with the Code of Ethics and the Standards. Reporting must also include significant risk and control issues, including fraud risks, governance issues, and other matters that require the attention of Senior Management and/or the board.

Accounting Officer of the concerned entity and the Audit Committee within 14 days after the end of the quarter. At the end of each financial year the HIA shall prepare a comprehensive annual report that consolidates the quarterly reports. The HIA should allocate time in the annual audit plan for preparing the quarterly and annual reports in accordance with formats prescribed by the Public Sector Accounting Standards Board.

2.5.1 QUARTERLY INTERNAL AUDIT REPORTS

The quarterly reports will include information on:

(1.) Work performed in comparison with the approved Annual Work Plan;

(2.) A report on consulting engagements undertaken and other special assignments.

(3.) Key issues emerging from Internal Audit work.

(4.) Management response to key audit findings and recommendations.

(5.) Major disagreements with management.

(6.) Major limitations affecting the achievement of Internal Audit objectives.

(7.) A report on cooperation between internal and external audit

(8.) Internal and External Quality Assurance reports on the Internal Audit function if any

(9.) Funding: utilization vs approved budget and impact of lack of adequate resources on the achievement of the annual audit plan and the resultant risk exposure

(10.) Staffing and performance

Internal Audit Quarterly Report, Template 12 is provided in the Appendix.

2.5.2 INTERNAL AUDIT ANNUAL REPORTS

The annual reports must include information on:

(1.) **Overall status of governance, risk management and controls**: this summarizes the quarterly reports.

(2.) **Other assurance providers' findings** and status of implementation of corrective actions

(3.) **Adherence to Internal Audit Charter:** assurance that the IAF adhered to the Internal Audit Charter, IPPF, Internal Audit Procedures Manual and relevant laws and regulations. The HIA can report on factors that may have or cause the independence or objectivity of IAF to be impaired and required corrective action.

(4.) **Value addition:** audit client satisfaction rating; number of improvements in processes and systems arising from Internal Audit work; number of committees and task forces audit is involved in (advisory services); amount of identified cost savings or revenue increase due to Internal Audit work; and number of innovations arising from Internal Audit work.

(5.) **Human Capital**: staff competency index; staff engagement index; staff turnover; staff satisfaction rating; and training hours.

(6.) **Quality Assurance and Improvement Program**: results of on-going, annual, or external quality assessments.

(7.) Independence of the Internal Audit function

(8.) Conformance with the Code of Ethics and the Standards, and action plans to address any significant conformance issues.

(9.) Management's response to risk that, in the HIA's judgment, may be unacceptable to the organization.

(10.) Annual review of Internal Audit Charter

Internal Audit Annual Report Template 13 is provided in the Appendix.

2.5.3 RESPONSIBILITIES OF AUDIT COMMITTEE SECRETARY

Audit Committee guidelines through gazette notice no.2691, requires that the HIA shall be the secretary to the committee. The HIA should support the Chairperson of the committee in identifying matters to be discussed. The Chairperson of the committee and the secretary should agree procedures for commissioning briefing to accompany business items on the committee's agenda and timetables for the issue of meeting notices, agendas, and minutes. The Chairperson of the committee should always review and approve minutes of meetings before they are circulated. The specific responsibilities of the Audit Committee Secretary should include;

(1.) Ensuring that new members receive appropriate induction training, and that all members are supported in identifying and participating in ongoing training.

(2.) Meeting with the Chairperson of the Committee to prepare agendas for meetings.

(3.) Draft the work plan for the Audit Committee for the Chairperson and members' review.

(4.) Circulating meeting documents in good time before each meeting.

(5.) Arranging for executives to be available as necessary to discuss specific agenda items with the committee during meetings.

(6.) Keeping a record of meetings and providing draft minutes for the Chairperson's approval.

(7.) Ensuring action points are being taken forward between meetings.

(8.) Support the Chairperson in the preparation of Audit Committee reports to the Governing Body.

(9.) Keeping the Chairperson and members in touch with developments and relevant background information of the entity.

(10.) Any other role as guided by the Audit Committee.

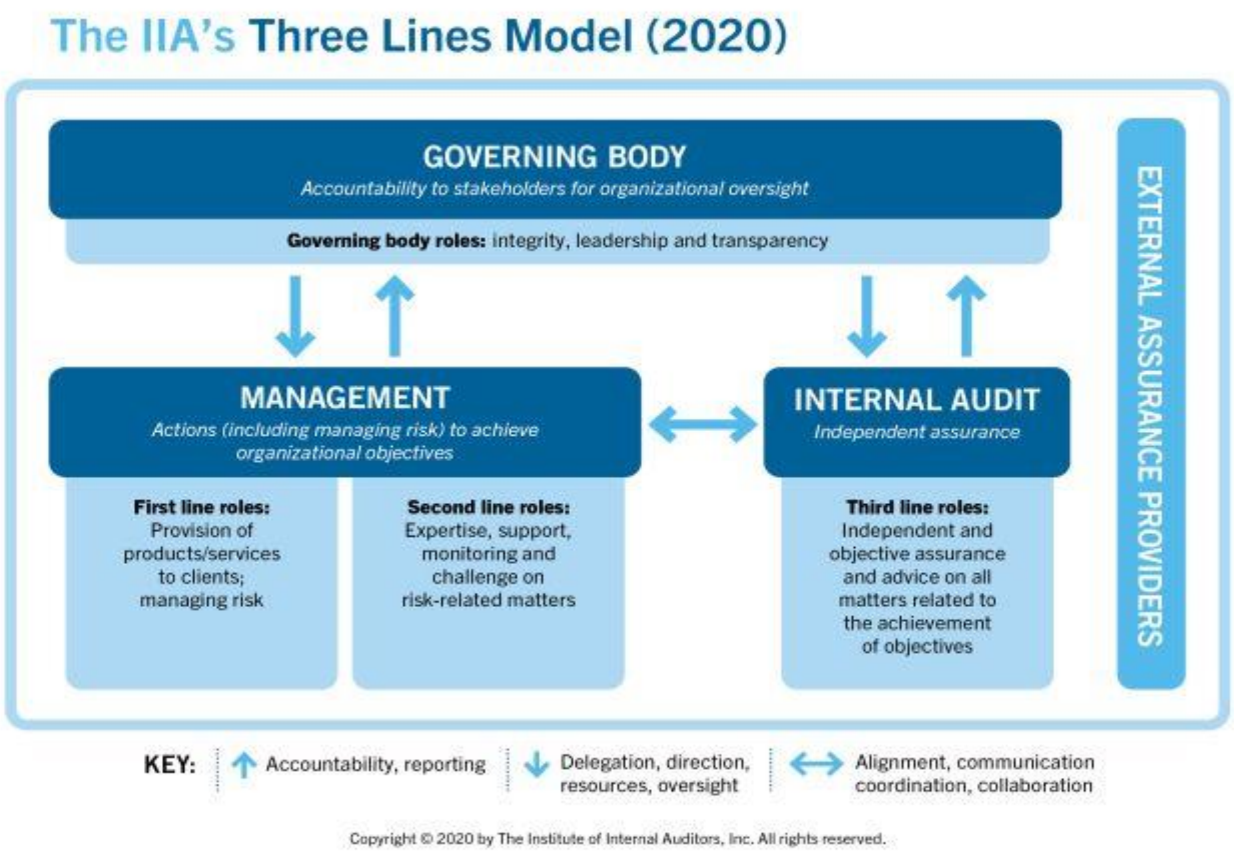
HIA Assessment Template 14 is provided in the Appendix.

CHAPTER 3 – NATURE OF INTERNAL AUDIT SERVICES

Chapter 3 covers the nature of Internal Audit services and the various types of audits that the Internal Audit Function shall undertake. The chapter is aligned to IIA Standard 2100 on Nature of Work.

2100 – Nature of Work
The internal audit activity must evaluate and contribute to the improvement of the organization's governance, risk management, and control processes using a systematic, disciplined, and risk-based approach. Internal audit credibility and value are enhanced when auditors are proactive and their evaluations offer new insights and consider future impact.

Internal Auditors need to understand the entity to perform meaningful evaluations and may use established governance, risk management and control frameworks as a guide in their evaluation. In addition, Internal Auditors may use their knowledge, experience and leading practices to proactively highlight observed weaknesses and make recommendations for improvement. The Institute of Internal Auditors uses the three lines model to describe key roles in the entity.



Typically, the Governing Body is responsible for guiding the governance process while the Senior Management are accountable for leading risk management and control processes. Governance, risk management and controls are closely interrelated and linked to each other. Effective governance activities consider risks when establishing entity's goals, objectives and implementation strategies, and the related operational plans. Controls are as a result of risks in the sense that controls represent the actions that are taken to manage risks and increase the likelihood of achieving the established goals and objectives. Effective governance mechanisms rely on the effectiveness of the internal controls. External assurance providers comply with legislative and regulatory expectations as well as requests by Senior Management and governing body to complement internal sources of assurance. These linkages and their impact on the entity should be clearly understood and appreciated as they are core elements in the practice of Internal Auditing and encompass all phases of an audit.

The IAF can provide assurance or consulting services in relation to governance, risk management and controls with a view of: providing reasonable assurance that they are operating as intended to ensure entity's objectives are achieved and risks managed; and provide recommendations for improving the entity efficient, effective and economic use of public resources.

3.1 ASSURANCE SERVICES

Assurance services involve the Internal Auditor's objective examination of evidence for the purpose of providing an independent assessment on governance, risk management, and control processes for the entity. The need for assurance arises from an entity's governance processes. Its origin is in the stewardship relationship between the Governing body and its stakeholders. This stewardship relationship demands that Governing body establish processes to both delegate and limit power to pursue the entity's strategy and direction in a way that enhances the prospects for the entity's long-term success. Assurance processes are needed to allow the Governing body to monitor the exercise of that power. Risk management is a management process that promotes the efficient and effective achievement of entity's objectives. Assurance and risk management are complementary processes. In support of the risk management process, the major role of Internal Audit and other independent assurance providers is to provide assurance that:

(1.) The risk management process has been applied appropriately and that elements of the process are suitable and sufficient.
(2.) The risk management process is keeping with the strategic needs and intent of the entity.
(3.) Processes and systems are in place to ensure that all material risks have been identified and are being treated.
(4.) All prioritized intolerable risks have cost-effective treatment plans in place.
(5.) Controls are being correctly designed in keeping with the outputs of the risk management process.
(6.) Key controls are adequate and effective.
(7.) Risks are not over-controlled or inefficiently controlled.
(8.) Line management review and other non-audit assurance activities are effective at maintaining and improving controls.
(9.) Risk treatment plans are being executed.
(10.) There is appropriate and as-reported progress in the risk management plan.

The assurance strategy is closely aligned with the entity strategic plan. The legal, legislative, cultural, and economic environment in which the entity is operating, as well as the nature of the entity's activities and its long-term plans drives assurance needs. It is an important to identify who will be the users of the entity's assurance. Clearly, the Governing body and Senior Management are the primary users. Other users may include the regulators, government, or stakeholders for whom the entity is a critical service provider or supply component.

3.2 CONSULTING SERVICES

The IAF shall perform consulting services in a manner consistent with the Internal Audit Charter. Policies for the types of consulting service assignments which are performed by the IAF, and issues concerning objectivity and independence are discussed in this section.

1000 - Purpose, Authority and Responsibility
1000.C1 – The nature of consulting services must be defined in the internal audit charter.

1130 – Impairment to Independency or Objectivity
1130.C1 – Internal auditors may provide consulting services relating to operations for which they had previous responsibilities.
1130.C2 – If internal auditors have potential impairments to independence or objectivity relating to proposed consulting services, disclosure must be made to the engagement client prior to accepting the engagement.

1210 – Proficiency
1210.C1 – The chief audit executive must decline the consulting engagement or obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

1220 – Due Professional care
1220.C1 – Internal auditors must exercise due professional care during a consulting engagement by considering the:

- Needs and expectations of clients, including the nature, timing, and communication of engagement results.
- Relative complexity and extent of work needed to achieve the engagement's objectives.
- Cost of the consulting engagement in relation to potential benefits.

2010 – Planning
2010.C1 – The chief audit executive should consider accepting proposed consulting engagements based on the engagement's potential to improve management of risks, add value, and improve the organization's operations. Accepted engagements must be included in the plan.

2120 – Risk Management
2120.C1 – During consulting engagements, internal auditors must address risk consistent with the engagement's objectives and be alert to the existence of other significant risks.
2120.C2 – Internal auditors must incorporate knowledge of risks gained from consulting engagements into their evaluation of the organization's risk management processes.
2120.C3 – When assisting management in establishing or improving risk management processes, internal auditors must refrain from assuming any management responsibility by actually managing risks.

2130 – Control
2130.C1 – Internal auditors must incorporate knowledge of controls gained from consulting engagements into evaluation of the organization's control processes.

2201 – Planning Considerations
2201.C1 – Internal auditors must establish an understanding with consulting engagement clients about objectives, scope, respective responsibilities, and other client expectations. For significant engagements, this understanding must be documented.
2210 – Engagement Objectives
2210.C1 – Consulting engagement objectives must address governance, risk management, and control processes to the extent agreed upon with the client.
2210.C2 – Consulting engagement objectives must be consistent with the organization's values, strategies, and objectives.
2220 – Engagement Scope
2220.C1 – In performing consulting engagements, internal auditors must ensure that the scope of the engagement is sufficient to address the agreed-upon objectives. If internal auditors develop reservations about the scope during the engagement, these reservations must be discussed with the client to determine whether to continue with the engagement.
2220.C2 – During consulting engagements, internal auditors must address controls consistent with the engagement's objectives and be alert to significant control issues.
2240 – Engagement Work Program
2240.C1 – Work programs for consulting engagements may vary in form and content depending upon the nature of the engagement.

2330 – Documenting Information
2330.C1 – The chief audit executive must develop policies governing the custody and retention of consulting engagement records, as well as their release to internal and external parties. These policies must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

2410 – Criteria for communicating
2410.C1 – Communication of the progress and results of consulting engagements will vary in form and content depending upon the nature of the engagement and the needs of the client.
2440 – Disseminating Results
2440.C1 – The chief audit executive is responsible for communicating the final results of consulting engagements to clients.
2440.C2 – During consulting engagements, governance, risk management, and control issues may be identified. Whenever these issues are significant to the organization, they must be communicated to senior management and the board.

3.2.1 NATURE OF INTERNAL AUDIT CONSULTING SERVICES

Consulting services refer to advisory and related client service activities, the nature and scope of which are agreed with the client, are intended to add value and improve an entity's governance, risk management, and control processes without the Internal Auditor assuming management responsibility. Consulting services work may be driven by risk-based planning but may also be at management request where the entity's risk and control systems and processes are embryonic or not yet mature.

The IAF 's Strategic and Annual Audit plan should include anticipated consulting engagements. The audit planning process may include consideration of consulting service assignments to address areas considered high risk. Specific assignments that have been accepted should be included in the Annual Audit Plan along with unallocated hours for non-specified but anticipated consulting engagements.
Internal Auditors should incorporate knowledge of risks gained in audit assignments into the process of identifying and evaluating significant risk exposures of the entity.

Consulting services engagements are of various types that may include the following;

(1.) **Formal consulting engagements** – These are planned engagements and are subject to written agreement.

(2.) **Informal consulting engagements** – These are routine advisory activities. The HIA may provide for slack time in the Internal Audit work plan to allocate time for consulting engagements.

(3.) **Special engagements** - These may be done to assist Heads of Department in dealing with issues before they become audit or investigation problems; and

(4.) **Emergency consulting engagements** – participation on a team established for recovery or maintenance of operations after a disaster or other extraordinary event or a team assembled to supply temporary help to meet a special request or unusual deadline.

The consulting roles undertaken by Internal Audit may be one of the following:

(1.) **Facilitator -** Leading a control self-assessment workshop – brainstorming risks and controls and acting as a catalyst for change.

(2.) **Trainer -** Induction presentation to new staff regarding the role of Internal Audit or corporate governance best practice guidance.

(3.) **Educator -** Supporting management in imparting appropriate risk and control skills and techniques so that managers are better equipped to undertake their own role effectively.

(4.) **Advisor -** On risk and control issues at all levels within the entity from strategic through to operational, offering advice but not undertaking any tasks on behalf or instead of management. Advice offered by Internal Audit and accepted by management does not transfer or reduce management's accountability for their areas of responsibility.

The above roles may be at the request of Senior Management or the governing body or because of a change programme or project and should add value and improve entity's operations. Whilst consulting in nature, this type of activity may also provide some level of assurance and may significantly contribute to Internal Audit's unique position in terms of being able to provide Senior Management with a more holistic view of the entity, its operations and culture.

3.2.2 STEPS TO GUIDE IN HANDLING AUDIT CONSULTING ENGAGEMENTS

When handling consulting engagements, the following steps needs to be undertaken;

(1.) The Internal Audit charter must specify the consulting services that Internal Auditors may provide, and the circumstances under which they may be provided.

(2.) All requests for engagement consulting shall be to the Head Internal Audit.

(3.) The HIA shall subject the request to the criteria referred to in the previous section above and shall make a decision to accept or reject the consulting activity.

(4.) Where consulting activity is accepted, consideration shall be made based on the nature, complexity, auditor's availability and experience to allocate an auditor or team to handle the consulting engagement.

(5.) Full understanding of assignment shall be established with the client covering assignment objectives, scope, respective responsibilities and expectations

(6.) Audit work engagement planning, and execution shall then follow.

(7.) During planning and execution, the HIA and client shall be timely updated on all material issues including any need to review and adjust scope and audit objectives as may be necessary.

(8.) All relevant issues shall be documented.

(9.) The HIA shall periodically meet with the client management for clarifications and any additional wrap-up discussion prior to preparing a report. This gives a chance to highlight progress noted during the engagement, and to discuss and seek client buy-in on opportunities noted. The client should be allowed sufficient time to consider the engagement results, and to document an action plan that can be included in the consulting report.

(10.) The HIA shall ensure that a consulting engagement report is prepared at the completion of the project. The report should follow the basic format suggested below;
(a.) Background,
(b.) Objective(s),
(c.) Scope,
(d.) Methodology,
(e.) Findings,
(f.) Conclusions/opportunities for improvement,
(g.) Action plan developed together with the Client

(11.) The HIA shall provide direction on disseminating results on the engagement, concerning what level of management will be included in the distribution of a report.

(12.) To the extent agreed upon with the client, the HIA shall monitor the disposition of results of the engagement by performing a follow-up process.

3.2.3 ROLES BEYOND INTERNAL AUDITING

1112 – Chief Audit Executive Roles Beyond Internal Auditing
Where the chief audit executive has or is expected to have roles and/or responsibilities that fall outside of internal auditing, safeguards must be in place to limit impairments to independence or objectivity.

To address the risk of impairment, the HIA should gain an understanding of any proposed role that falls outside of Internal Auditing and speak to Senior Management and the Governing body about the reporting relationships, responsibilities and expectations related to the role. During such discussion, the HIA should emphasize the International standards for the Professional Practice of Internal Auditing (*standards*) related to independence and objectivity, the potential impairment presented by the proposed role, the risks associated with the proposed role and safeguards that could mitigate those risks.

Internal Auditors shall document any safeguards that were established to address potential impairments to their independence or objectivity. When undertaking consulting role, safeguards should be discussed and put in place by HIA, Governing body and Senior Management to limit impairments to the independence and objectivity.

Steps that can be taken to minimize the effects of impairment include;

(1.) Assigning different Internal Auditors to perform the consulting engagement instead of auditors who were involved in conducting earlier audit or investigative assignments.
(2.) Establishing independent management and supervision through assigning Internal Auditors who were not involved in supervising earlier audit or investigative \assignments; and
(3.) Disclosing the presumed impairment to the department staff who have requested the services.

3.2.4 CONSULTING SERVICE LIMITATIONS

Consulting engagements should be accepted when the assignment's objectives are consistent with the current or prospective values and goals of the entity. Internal Auditors should refrain from providing consulting services for assignments where they feel that they cannot be objective. Further, if the IAF lacks the knowledge, skills, or other competencies needed to perform all or part of the assignment or the consulting assignments are prohibited by the terms of the Internal Audit charter or conflict with its policies and procedures, or do not add value and promote the best interests of the entity, the HIA should decline to perform the assignment. Where the IAF lacks the knowledge, skills, or other competencies, the necessary competence should be obtained either through internal or external sources.

Disclosure of potential impairments to independence and objectivity of Internal Auditors should be communicated to the relevant Head of Department in a timely manner prior to commencement of the consulting services by the IAF. However, in the event that impairment(s) subsequently develop during the assignment, disclosure should be made immediately. Independence may be compromised for assignments relating to operations for which the IAF had previous responsibilities or had conducted audit assignments.

Considerations for accepting or rejecting a consulting activity may include:

(1.) Time availability for carrying out the consulting engagement which may not materially affect the annual planned activities.
(2.) Independence considerations that may include being free from personal, external and entity's impairment factors.
(3.) Knowledge and skill requirements to deliver the assignment
(4.) Consider consulting the governing body in certain engagement requests
(5.) Any other factors considered necessary.

3.2.5 CONSULTING SERVICES PLANNING

In most cases, consulting engagements will be treated in accordance with this Manual. However, the requirements for production of a consulting services plan, notification to entity staff who have requested the assignment, work papers, and a formal report may be waived by the HIA for fairly informal consultations such as brief telephone conversations or individual committee meetings involving limited scope contact with the entity's Management or staff who have requested for the services.

The IAF should develop and record a plan for consulting services which will assist in:

(1.) Identifying the needs of the consulting service, including the nature, timing, and communication of assignment results;
(2.) Understand possible motivations and reasons of the subject in requesting the service;
(3.) Determine the extent of work needed to achieve the assignment's objectives and the skills and resources needed to provide the consultancy services;
(4.) Assessing the effect on the scope of the Annual Audit Plan and potential impact on future audit assignments. The consideration will be on whether to include the services provided as a regular item in the Audit Plan; and
(5.) Identify potential benefits to be derived by the entity from the assignment.

Adequate engagement planning requires that the Internal Auditor in charge of the consulting assignment establish an appropriate scope that addresses concerns of department / staff that has requested the consulting services, and considers relevant risks of the activity being reviewed. The Internal Auditor should then develop a consulting service plan, obtain the approval and communicate this plan to Management or employee who has requested these services. Documentation of these planning activities is also required.

3.2.5.1 CONSULTING ENGAGEMENT PLAN

Work plans for consulting services assignments should vary in form and content depending upon the nature of the assignments. In general, a consulting services work plan should be prepared in advance of field work and should outline:

(1.) Department (of the auditee) objectives and goals;
(2.) Policies, plans, procedures, laws, regulations and contracts having significant impact on operations;
(3.) Entity's information
(4.) Budget information, operating results and financial data;
(5.) Results of prior reviews including reports of external auditors and other assurance providers, correspondence files and relevant authoritative and technical literature;
(6.) Engagement objectives;
(7.) Scope and degree of testing required to achieve the objectives in each phase of the review;
(8.) Procedures for collecting, analysing, interpreting and documenting information during the review; and
(9.) Technical aspects, risks, processes and transactions which should be examined.

The review timing and preliminary objectives of the consulting services should be mutually agreed with the relevant Senior Management of the assignment in advance before commencing the engagement. The Internal Auditor in charge of the consulting engagement should obtain and review relevant information about the consulting engagement being reviewed.

3.2.5.2 NOTIFICATION

A formal notification should be sent by the Internal Auditor in charge of the assignment to the appropriate head of department summarizing the agreement for the scope of work. For larger

engagements, an entrance meeting should normally be conducted with the audit client in order to reach mutual agreement on the scope, objectives, timing, and reporting of the review.
The following individuals should be invited and encouraged to attend the meeting:

(1.) Heads of department responsible for the operation/activity/process being audited.
(2.) Staff who work in the specific area being reviewed; and
(3.) The HIA for all high-risk assignments.

The IAF should confirm that those receiving the service understand and agree with the guidance contained in the Internal Audit Charter, the IAF's policies and procedures, and other related guidance governing the conduct of consulting assignments.

3.2.5.3 RISK ASSESSMENT

As part of planning for the engagement, the Internal Auditor should address risk consistent with the engagement's objectives and should be alert to additional significant risks. Various tools and techniques useful for audit engagements may also be useful for consulting services, to identify key controls and gain an understanding of the related risk. The possibility of fraud should be considered in the preliminary assessment of risk related to the engagement.

3.2.5.4 DOCUMENTATION

Documentation to evidence the planning procedures should include:

(1.) A record of mutual agreement with the department staff requesting the consulting services and the procedures to be performed. This may take the form of service terms of reference or other communication.
(2.) For larger assignments requiring over 40 hours, an assignment sheet or work plan with scope, objectives, purpose, timing, budget, and contacts of department staff requesting the services should be developed and signed by the HIA.

3.2.6 SCOPE OF WORK IN CONSULTING ENGAGEMENTS

The IAF should reach an understanding about the objectives and scope of consulting service assignments with those receiving the service. Any reservations about the value, benefit, or possible negative implications of the consulting services should be communicated to those receiving the service. The scope of work should be designed to ensure that professionalism, integrity, credibility, and reputation of the IAF will be maintained.

During planning, Internal Auditors should design objectives to meet the appropriate needs of department receiving these services. In the case of special requests by Management, Internal Auditors may consider the following actions if they believe that the objectives that should be pursued go beyond those requested by Management:

(1.) Persuade Management to include the additional objectives in the scope of work;
Or
(2.) Document the fact that the objectives were not pursued and disclose that observation in the final communication of the results of the consulting services; and include the objectives in a separate and subsequent audit assignment.

Work programs for formal consulting engagement should document the objectives and scope of the assignment as well as the methodology to be used in satisfying the objectives. The form and content of the work plan may vary depending on the nature of the assignment.
The objectives, scope, and terms of the assignment should be periodically reassessed and adjusted during the course of the work. Internal Auditors should be observant of the effectiveness of risk management and control processes during consulting engagements. Substantial risk exposures or material control weaknesses should be brought to the attention of the Internal Auditor in charge and HIA as well as the entity's Management if deemed necessary.

3.2.7 CONDUCTING A CONSULTING ENGAGEMENT

Conducting consultancy services involves examining, evaluating and documenting the information pertinent to the area under review in order to support review results. Consulting services objectives and other relevant information should be documented. The HIA and Internal Auditor in charge should communicate the goals and objectives, risks and other relevant information to the Internal Auditors in order to provide the guidance and understanding necessary to conduct a high-quality assignment. The Internal Audit team and the audit client should maintain regular communication throughout the consulting engagement to ensure risks, observations, and conclusions are adequately addressed and resolved.
Supervision and work paper documentation and review throughout the consulting service process ensures goals, objectives, risks and observations are addressed and resolved and conclusions reached supported. In conducting the assignment, due professional care is exercised by considering the:

(1.) Expressed expectations of the department staff requesting the services, including the nature, timing, and communication of assignment results;
(2.) Relative complexity and extent of work needed to achieve the assignment's objectives;
(3.) Cost of the consulting services assignment in relation to the potential benefits;
(4.) Possible motivations and reasons of those requesting the service;
(5.) Skills and resources needed to conduct the assignment;
(6.) Effect on the scope of the audit plan previously approved by the Governing body;
(7.) Potential impact on future audit assignments; and
(8.) Potential benefits to the entity as a whole and the department to be derived from the assignment.

The level and frequency of review and communication during a consulting depends upon the experience of the assigned staff and the risk associated with the review.

3.2.8 WORKING PAPER DOCUMENTATION

Working paper file documents the work the Internal Auditor has done. The working papers serve as the connecting link between the work performed by the auditor and the final report. Working papers contain the work plan, fieldwork and other documentation supporting interviews, analyses and conclusions reached. All changes to the scope or consulting engagement plan should be documented and approved by the HIA. Consulting engagement working papers may be in any form prescribed by audit management. If working papers are in a form other than paper, appropriate backup procedures should be developed and followed.
All working papers should be independently reviewed to ensure there is sufficient evidence to support conclusions and that consultancy services objectives have been met. Work papers should be signed off and dated by the preparer and the reviewer.

3.2.9 REPORTING RESULTS OF A CONSULTING ENGAGEMENT

The IAF should maintains a process for communicating the results and recommendations for all consulting engagements to the department requesting the services and the Senior Management. Communication of the progress and results of consulting engagement should be tailored to meet the needs of the department requesting the consulting services. The process for reporting results generally includes draft report preparation and reviews, quality assurance reviews and final report issuance and distribution. The form and content of such reports may vary depending on the nature of the assignment and the services requested.

Reports can be in written or oral format. In drafting a written consulting services report, the auditor should consider whether the inclusion of the elements in an assurance audit report would be useful to Management. All results should be reviewed with Management prior to being placed in final format to ensure that Management's needs and expectations have been met.

In other circumstances, with the agreement of the HIA, consulting services results may be communicated orally. In such cases, presentations should be reviewed in advance with the HIA. The working papers should contain a record of communications with the audit client.
For larger consulting services, a pre-issuance quality assurance review of draft and final written reports should normally be performed by the Internal Auditor in charge of the assignment or an independent party and be reviewed by the HIA. The HIA should review and approve the final report prior to issuance.

Written and oral reports should be issued as soon as practical following the completion of consulting services. Written consulting services reports should be addressed to the head of department requesting the services and the Senior Management. In addition:

(1.) Information copies should be provided to the Internal Auditor, in charge of the consulting engagement as well as the HIA.
(2.) Other staff may receive a report copy, at the discretion of the HIA in consultation with the Senior Management.

A management response to a consulting service may be required.

3.3 GOVERNANCE

2110 - Governance
The internal audit activity must assess and make appropriate recommendations to improve the organization's governance processes for:

- Making strategic and operational decisions.
- Overseeing risk management and control.
- Promoting appropriate ethics and values within the organization.
- Ensuring effective organizational performance management and accountability.
- Communicating risk and control information to appropriate areas of the organization.
- Coordinating the activities of, and communicating information among, the board, external and internal auditors, other assurance providers, and management.

3.3.1 GOVERNANCE DEFINITION

The IIA has, as part of the Standards, defined **governance** as the combination of processes and structures implemented by the Governing Body to inform, direct, manage, and monitor the activities of the entity towards the achievement of its mandate and objectives and those operations are carried out in an ethical and accountable manner.

Governance also includes activities that ensure a public entity's credibility, establish equitable provision of services, and assure appropriate behaviour of public officials so as to reduce the risk of fraud. An entity in enhancing governance should comply with the national values and principles of governance under Article 10 of the Constitution of Kenya (2010).

The Mwongozo Code of Governance defines corporate governance as the structure and system of rules, practices and processes by which an organisation is directed, controlled and held accountable. It encompasses authority, accountability, stewardship, leadership, direction and control exercised in organisations. It also provides the framework for achieving the objectives of the entity and creates benchmarks for the measurement of corporate performance and disclosure.

The Governing Body and Senior Management are responsible for establishing appropriate governance processes and systems. The Governing Body, Senior Management, OAG and the IAF are considered key components on an effective governance system. Management is responsible for supporting the Accounting Officer implement the governance systems and processes established by the Governing Body.

The OAG and IAF provide reasonable assurance that the governance, risk management and controls processes and systems are appropriately designed and are working as expected. PFMR r. 160(1) (b) requires the HIA to provide reasonable assurance through the Governing body on the state of governance systems and process of the entity.

The HIA should assess the maturity of the governance process and system during the annual audit planning process. A more mature and effective governance process may indicate strong oversight by the Governing Body and Senior Management which may result to strong risk management and control systems.

During the annual planning process, the HIA shall assess whether to provide assurance or consultancy services on the entity's governance system and processes. Where the governance processes and systems are immature the HIA may prefer to provide consulting services, given that governance issues may already be known. In providing assurance services, the HIA may decide to assess governance in each area of review when undertaking audit engagements instead of undertaking a single governance audit.

In assessing the governance system and processes the Internal Auditor may assess:

(1.) **Decision making process**: how Governing Body and management make strategic and operational decisions to establish if: consistent decision-making process has been established; and Governing Body and management directives are effectively communicated, implemented and feedback on the same provided.

(2.) **Risk management and control oversight**: the effectiveness of the annual risk assessment process; if risk management is a key agenda in Governing Body and management meetings; how risk management and controls information is communicated from and to Governing Body and management and the relevance of the information communicated; employees understanding of their responsibilities and ownership of risk management and controls; linkage of risk management to policies, procedures, annual work plan, budgets and performance management; effectiveness of management self-assessment on the effectiveness of implemented risk management strategies.

(3.) **Promotion of appropriate ethics and value within the entity**: how the Governing Body and Senior Management are promoting a culture of ethics and compliance to laws, regulations, policies and standards both internally and among the entity's external stakeholders. This may involve assessing the effectiveness of adherence to the entity's code of conduct and resolving non-compliance incidences. The Internal Auditor can assess how the entity's mission and value statements have been internalized by all employees and how these are supported by human capital management programmes (recruiting, retaining and training). The Internal Auditors can assess the effectiveness of the whistle blowing/hot line system in protecting the whistle-blower and expediting investigations resulting from the system.

(4.) **Strategy**: how well the strategies have been developed, communicated and adopted throughout the entity. This involves assessing whether strategies; are developed through a disciplined process and supported by the best available information; are commonly understood by the staff; serve as a platform for all major decisions; enhance stakeholder value; align with other strategies, both top-down and across the entity; clearly reflected in objectives, structures, and operations at all levels; enable alignment of measurement and rewards; eliminate redundancies; are documented; manage/maintain risks within risk tolerance limits; allow risk expectations to be well understood by stakeholders such as regulators, interest groups, citizens, among others.

(5.) **Compliance**: this relates to compliance with laws and regulations. Audit functions may consider the need for technical assistance from the legal department or an outside third party when evaluating legal and regulatory compliance. It involves assessing whether the methods by which the entity fosters compliance knowledge and commitment in its employees.

(6.) **Entity's Accountability / Effectiveness of the performance management system**: the entity's target setting, performance evaluation, accountability for results and staff compensation and how these supports the desired behaviour (i.e. prevent or detect unaccepted behaviour or risk-taking) and ensures alignment to the achievement of the strategic plan. When assessing accountability the auditor should consider the entity's legal or legislative appointment, legal structures, and applicable laws and regulations; formal and comprehensive "delegated authorities" and "powers reserved"; documented acknowledgement of their accountabilities by key staff; processes to monitor accountabilities and corrective actions taken when accountabilities are not met.

(7.) **Coordination of Governing Body and management activities**: the effectiveness of establishing the Governing Body calendar of activities and management annual programme and how efficiently this is implemented. The Internal Auditors can assess adherence to the Governing Body terms of reference. The Internal Auditors can assess the effectiveness of Governing Body and management meetings e.g., frequency of meetings, receipt of agenda and necessary materials on time, quorum, contribution by members, establishing resolutions, management of minutes etc.

(8.) **Monitoring**: The purpose of monitoring is to provide Governing Body and management with early indications of progress being made, or not made, in achieving the entity's objectives. It assists in making timely decisions, hold people accountable and continually improve performance. Assessing monitoring considers relevance; reliability; adaptability to address new or changing risks; accuracy; objectivity; completeness; cost-effectiveness; timeliness; usefulness; communication and reporting content.

(9.) **IT Governance**: This consists of leadership, entity's structures, and processes that ensure that the entity's IT supports the entity's strategies and objectives. Effective IT governance should a cohesive and integrated process aligned with the operations, compatible with management decision-making style and culture, and perceived by management to be providing value. Auditors may use widely recognized IT governance frameworks in establishing criteria to assess IT governance such as ISO 38500, Corporate Governance of Information Technology; COBIT 5; GTAGs; IT Infrastructure Library (ITIL).

(10.) **Audit Committee**: The Audit Committees should ensure that it is fulfilling its governance responsibilities, the right governance processes are in place within the entity and operating effectively, and transparent communication exists between the entity and its stakeholders. In assessing Audit Committee performance, auditors should focus on a three-pillar framework;

  (a.) **Assessing compliance with charter obligations**. Does the Audit Committee discharge its responsibilities as stated in the charter?

  (b.) **Assessing the participation of the Audit Committee members**. Is there a formal and effective assessment of each member's performance and contribution to the Audit Committee?

  (c.) **Assessing value-added activities pursued and outcomes achieved**. Does the Audit Committee add value to the entity by facilitating well-informed and effective decision-making, promoting and monitoring an ethical culture, implementing an effective system of risk oversight and management, implementing an effective and efficient internal control system, promoting effective communication with internal and external auditors and responding appropriately to matters they raise, promoting high-quality internal and external reporting financial and nonfinancial information?

In providing consultancy services, the IAF may provide advisory services to various oversight and investigatory committees instituted by the entity. The IAF may also consider outsourcing governance audit and undertaking peer reviews under the provision of coordination in Internal Auditing.

3.4 RISK MANAGEMENT

2120 – Risk Management
The internal audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes.

3.4.1 RISK MANAGEMENT DEFINITION

The IIA defines risk as the possibility of an event occurring that will have an impact on the achievement of objectives. Risk management is the process whereby management identifies and assesses business and operational risks (internal and external) and puts in place controls and other measures to mitigate the risk so as to have reasonable assurance of achieving the entity's objectives.

According to ISO 31000:2018, **risk** is the "effect of uncertainty on objectives" and an effect is a positive or negative deviation from what is expected. Risk is measured in terms of the likelihood of an adverse event occurring and the impact of that event on the achievement of objectives in case it does occur. COSO Enterprise Risk Management – Integrating with Strategy and Performance, 2017, defines **risk** as "the possibility that events will occur and affect the achievement of strategy and business objectives."

It's the role of the Senior management of the entity to ensure a risk management framework is established that builds robust business operations and includes fraud prevention mechanisms as stipulated by the PFMR r. 165. The Internal Auditor is expected to provide reasonable assurance through the Governing body on the state of the risk management framework established by the Senior Management as stipulated by the PFMR r. 160(1) (b) and the public sector risk management guidelines issued by PSASB.

It is primarily the responsibility of the IAF to provide objective assurance on the effectiveness and efficiency of the risk management process. The Internal Auditor can achieve this by assessing the following:

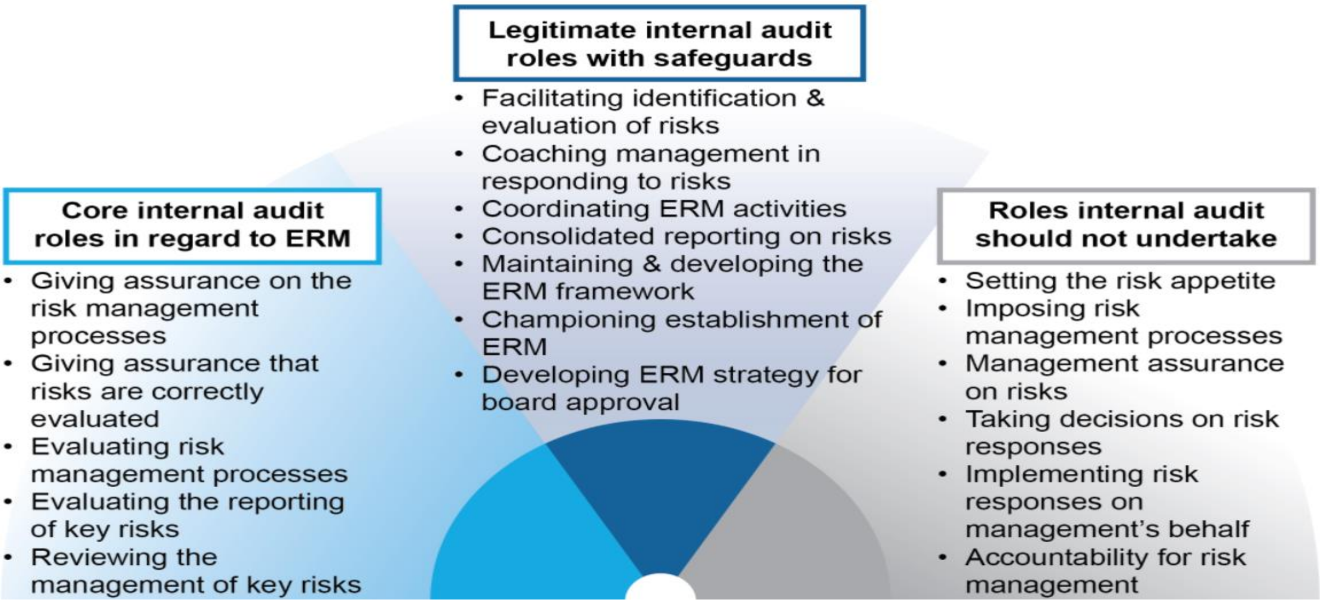
(1.) **Risk governance:** the oversight role played by the governing body and Senior Management in ensuring the entity has a culture of risk management. This shall involve assessing: if risk management is a key agenda of governing body and management meetings; how expected risk attitudes and behaviour are communicated to all employees and how the governing body and Senior Management obtain feedback on the risk culture; how the governance body and Senior Management obtain a view of the key risks impacting the entity; how risk management is integrated with decision making; risk management ownership and accountability; risk management function is appropriately positioned; cross-functional risk management; linkage of risk management with performance management; risk management capacity building.

(2.) **Integrating risk management with the business:** This may involve assessing how strategic objectives are aligned to mandate, vision and mission; linkage of strategic and operational objectives; effectiveness of setting risk appetite and risk tolerance and how management ensures the same is adhered with; significant risks are identified and are linked to objectives; risks are correctly prioritized; effective risk management strategies and actions are established; integrating risk management strategies with annual plans, budgets, policies and procedures; if management have selected appropriate risk strategies that are aligned with the approved risk appetite; policies on accepting risks and if management are accepting risks beyond approved risk appetite; the effectiveness of the risk management strategies implemented by management; if management are able to identify new and emerging risks and take appropriate action; and effectiveness of risk monitoring and reporting at a functional level and entity level.

(3.) **Risk management process:** This may involve assessing effectiveness of the process for identifying, assessing, prioritizing, treating, monitoring and reporting risks; whether the risk management process identifies both threats and opportunities; how the governing body and Senior Management obtain assurance on the effectiveness of the risk management process; and whether the risk management process is adequately funded. Risk management assurance services may be undertaken as part of the normal audit engagement or may be undertaken as a separate engagement.

The Governing Body and the Senior Management are expected to undertake risk assessment at least annually. The HIA may use the output of the annual assessment in developing the Annual Risk-Based Internal Audit Plan. The assessment of the effectiveness of the risk management process may enable the HIA to determine on whether to rely on the results of the annual risk assessment. Where the HIA concludes that management has accepted a level of risk that may be unacceptable to the entity, this matter must be discussed with the Governing body and Senior Management.

Where the IAF is to provide consulting services on risk management, this should be clearly stated in the Internal Audit Charter and adequate safeguards put in place as outlined in the Public Sector Risk Management Guidelines. The Institute of Internal Auditors Position Paper: The Role of Internal Auditing in Enterprise-wide Risk Management provides guidance on Internal Audit's role in risk management. The core functions and legitimate functions with safeguards are provided in diagram below:



(Source: IIA Position Paper: The Role of Internal Auditing in Enterprise-Wide Risk Management January 2009)

3.5 CONTROLS

2130 – Controls
The internal audit activity must assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

3.5.1 INTERNAL CONTROL DEFINITION

PFMR r. 165 requires the Senior Management to ensure the entity has established a system of internal control that builds robust business operations. Internal control system comprises the whole system of controls, financial and otherwise, established by management in order to carry on operations in an orderly and efficient manner, ensure adherence to management policies and directives, safeguards assets, and secure as far as possible the completeness and accuracy of records.

An internal control is a process, effected by the entity Governing Body, management, and other staff, that is designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance. The controls established enables the Entity to achieve its objectives in an efficient and economical manner and at the same time manage its risks. Controls are established through policies, procedures, directions, processes and systems and implemented through directing, supervising, monitoring, and reporting on all operations, functions and activities.

The Senior Management are responsible for establishing, administering and assessing effectiveness of controls whereas the Internal Auditor is expected to provide reasonable assurance to the Governing Body and Senior Management that the controls are operating as intended.

Controls are classified into:

(1.) **Preventive controls** – Designed to prevent the occurrence of inefficiencies, errors, or irregularities. While preventive controls cannot guarantee that the controlled factor will not occur, they do reduce the chance of it occurring.

(2.) **Detective controls –** Designed to detect inefficiencies, errors, or irregularities. Detective controls help to ensure that errors are identified and corrected as quickly as possible.

(3.) **Corrective controls –** Designed to help mitigate damage once a risk has materialised.

(4.) **Directive controls –** Designed to ensure that a particular outcome is achieved.

3.5.2 COSO INTEGRATED CONTROL FRAMEWORK

In conformance with PFMR r. 165, the Senior Management and the Internal Auditors in the entity may adopt the guidance provided by the COSO Integrated Control Framework (ICF), 2013, as a benchmark to understand and assess whether all aspects of an internal control are considered, all the controls are adequate to manage all the key risks of the entity and the entity's objectives are effectively and efficiently achieved. Governance, risk management and internal controls requirements are embedded in PFMA, PFMR, guidelines, policies, manuals and procedures.

COSO ICF is a model developed by the Committee of Sponsoring Organizations of the Treadway Commission for the purpose of establishing and evaluating effective internal controls. The COSO ICF identifies the following five components and seventeen principles as necessary for effective internal control:

(1.) **Control Environment** – This is the set of standards, processes and structures that provide the basis for carrying out internal control across the entity. It sets the tone of an entity, influencing the control consciousness of its people. Principles relating to the control environment include:

i. The entity demonstrates a commitment to integrity and ethical values

ii. The Governing body demonstrates independence from management and exercises oversight of the development and performance of internal control.

iii. Management establishes, with Governing body oversight, structures, reporting lines and appropriate authorities and responsibilities in pursuit of objectives.

iv. The entity demonstrates a commitment to attract, develop and retain competent individuals in alignment with objectives.

v. The entity holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

(2.) **Risk Assessment –** involves a dynamic and iterative process for identification and analysis of relevant risks that threaten the achievement of objectives; it forms the basis for determining how the risks should be managed. Principles relating to the risk assessment include:

vi. The entity specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives

vii. The entity identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.

viii. The entity considers the potential for fraud in assessing risks to the achievement of objectives.

ix. The entity identifies and assesses changes that could significantly impact the system of internal control.

(3.) **Control Activities –** These are actions established by policies and procedures to help ensure that management directives to mitigate risks to the achievement of objectives are carried out. Principles relating to the control activities include:

x. The entity selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.

xi. The entity selects and adopts general control activities over technology to support the achievement of objectives.

xii. The entity deploys control activities through policies that establish what is expected and procedures that put policies into action.

(4.) **Information and Communication –** Information is necessary for the entity to carry out internal control responsibilities in support of achievement of its objectives. Communication occurs both internally and externally and provides the entity with the information needed to carry out day-to-day controls. Principles relating to the information and communication include:

xiii. The entity obtains or generates and uses relevant, quality information to support the functioning of the internal control.

xiv. The entity internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.

xv. The entity communicates with external parties regarding matters affecting the functioning of the internal control.

(5.) **Monitoring –** On-going evaluations, separate evaluations, or some combination of the two are used to ascertain whether each of the five components of internal control, including controls to effect the principles within each component, is present and functioning. Findings are evaluated and deficiencies communicated in a timely manner, with serious matters reported to Senior Management and to the Governing body. Principles relating to monitoring activities include:

xvi. The entity selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.

xvii. The entity evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective actions, including Senior Management and the Governing body, as appropriate.

3.5.3 INTERNAL CONTROL SERVICES

PFMR r. 160(1)(b) requires the HIA to provide reasonable assurance through the Governing body on the state of the entity controls. The Internal Auditor can provide reasonable assurance in relation to controls by assessing the following;

(1.) Controls are clearly linked to objectives that they are supporting their achievement; and risks they are managing. This will enable the Internal Auditor to establish areas of under-control (i.e. weak or no controls to support achievement of objectives or management of risks) or over-control (i.e. areas where the costs of implementing control/s is more than the benefit derived in relation to achieving objectives and managing risks).

(2.) Management have adopted an appropriate risk management strategy i.e. avoid, accept, transfer/share, mitigate or pursue (for opportunities).

(3.) Management is implementing an appropriate risk treatment activity. This will involve assessing the: design of the treatment activity and if the activity has been implemented as designed.

Where the IAF is to provide consulting services in improving internal controls, this should be clearly provided in the Internal Audit Charter.

A ***pre-engagement / control questionnaire, Template 15*** is provided in the Appendix.

3.6 FRAUD

1210.A2 - Proficiency
Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

2120.A2 – Risk Management
The internal audit activity must evaluate the potential for the occurrence of fraud and how the organization manages fraud risk.

2210.A2 – Engagement Objectives
Internal auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.

3.6.1 FRAUD DEFINITION

IIA defines **fraud** as any illegal act characterized by deceit, concealment, or violation of trust. These acts are not dependent upon the threat of violence or physical force. Frauds are perpetrated by parties and entity to obtain money, property, or services; to avoid payment or loss of services; or to secure personal or business advantage.

Fraud have adverse impacts on entity and their true cost is even higher than just the loss of money, given their impact: on time spent to detect, investigate, prosecute, and recover lost funds; loss of reputation and trust by ordinary citizens.

Internal Auditors should be alert to situations/circumstances that can cause fraud including:

(1.) **Opportunity**: ability to execute fraud scheme without being detected. This can be caused by weak governance, risk management and controls.

(2.) **Pressure**: financial or social pressure pushing an individual towards committing fraud. Pressures can include money problems, gambling debts, alcohol or drug addiction or overwhelming medical bills. There may be pressure from other to prove that an individual is better than others in breaking into systems.

(3.) **Rationalization**: personal justification of dishonest action. The individual manages to justify what he or she is committing the fraud e.g. they are just going to borrow the stolen goods, or that they need the money more than the "big" place they are stealing from.

(4.) **Capability**: refers to the personal traits and ability of persons that enable them to perpetrate fraud, beyond the environmental or situational factors of opportunity, rationalization and pressure. This includes a person's knowledge of the policies, procedures and controls of the entity and in particular the weaknesses there in; and involvement in and influence over key relationships either internal relationships within the business, or external relationships with third parties.

Good governance, risk management, and internal controls can help establish a combination of prevention, detection, and deterrence measures to minimise opportunities for fraud. It's the role of the Senior Management to ensure risk management and controls are established that prevent fraud as provided by PFMR r. 165.

It's the role of the Senior Management to establish: fraud prevention system which includes a fraud-prevention policy; integrate fraud risk assessment with entity risk management framework; whistleblowing system that protects the whistle-blower and ensures effective expedition of reported fraud causes; preserving evidence, handling the results of investigations, reporting and communicate the results of investigations to appropriate authorities. Internal Auditors may assist in the evaluation of the policy.

PFMR r. 167 requires the HIA to report indicators of fraud, material breaches and wasteful expenditure to the Cabinet Secretary. Internal Auditors when undertaking their engagements are expected to take due professional care to detect possibility of fraud. Although Internal Auditors are expected to detect fraud they are not expected to have the expertise of someone whose role is solely to detect fraud (i.e. due professional care does not imply infallibility).

Audit procedures alone even when performed with due professional care, cannot guarantee that fraud will be detected. Consequently, the Senior Management should establish effective systems for preventing, detecting and resolving fraud.

Internal Auditors need to be aware that fraud can be a one-off transaction or can be perpetuated for a long time. Being that fraud is concealed it may be hard to detect. Internal Auditors should look for the following red flags that may be indication that fraud **may** be occurring:

(1.) Management override of controls or established controls not applied consistently.
(2.) Weak supervision of activities or unclear lines of responsibility and accountability.
(3.) Unexplained over-performance especially where there is general poor performance in other areas of the entity or sector.
(4.) Non-routine or unusual transactions or journal entries.
(5.) Delays or refusal to provide requested information during audits.
(6.) Unsupported or unapproved transactions.
(7.) Staff who don't go for leave or when they are on leave no other staff is able to perform their work.
(8.) Lack of employee rotation in sensitive positions.
(9.) Staff living beyond their means.
(10.) Staff always complaining of dissatisfaction with their job.
(11.) Unusual close association with suppliers and customers.
(12.) Significant changes in suppliers and customers.
(13.) Staff with personal financial stress.
(14.) Staff addicted to drugs, alcohol or gambling.
(15.) Staff who consistently rationalise poor performance.
(16.) Staff who perceive beating the system to be an intellectual challenge.
(17.) High turnover among staff in supervisory positions.

(18.) Staff refusing transfers.

(19.) Staff being protected by their seniors.

Where the IAF is to undertake investigations, this should be clearly provided in the Internal Audit Charter. The Internal Auditor may have the primary responsibility for conducting investigation or may act as a resource to support the investigation team (e.g. evidence collection and analysis, review investigation output and recommend controls improvement).

Safeguards should be established where IAF is to undertake investigations to protect the independence and objectivity of Internal Auditors; and perception of the IAF by the audit clients as a trusted business advisor and not an investigator. The HIA should ensure the team (either the Internal Audit team or external consultant) undertaking the investigation has sufficient proficiency to achieve the objectives of the investigation. Code of ethics should be complied with when undertaking fraud investigations.

The HIA should consult with the legal counsel on the investigation process and output to ensure all legal requirements are adhered to being some investigation may result to prosecution or the action taken based on the investigation may be challenged legally. Under investigations resulting to prosecution, only certified fraud examiners registered with ACFE, may present evidence to the court.

All investigations must be approved by the Governing body and/or Senior Management with clear terms of reference. The terms of reference may include protocols covered when undertaking fraud investigations:

(1.) Gathering, documenting and preserving evidence.

(2.) Considering legal rules of evidence, and the business uses of the evidence.

(3.) Determining the extent of the fraud.

(4.) Determining the techniques used to perpetrate the fraud and how come the fraud was not detected by management, Internal Auditors, external auditor or other assurance providers.

(5.) Evaluating the cause of the fraud.

(6.) Identifying the suspects.

(7.) Form and periodicity of reporting on the findings of the investigations.

(8.) Recommend on how to strengthen controls to prevent occurrence of fraud in future or ensure they are detected on time.

(9.) How the results of the investigation will be used for instance to strengthen controls, recover the lost resources or prosecute.

The IIA has developed a practice guide on Internal Auditing and fraud that should be used as a reference to increase the Internal Auditor’s awareness of fraud and provide guidance on how to address fraud risks on Internal Audit engagements. The practice guide outlines the roles and responsibilities for fraud prevention and detection for Internal Auditors as detailed below.

3.6.2 Roles/Responsibilities for Fraud Prevention/Detection for Internal Auditors

Internal Auditors evaluate risks faced by their entities based on audit plans with appropriate testing. Internal Auditors need to be alert to the signs and possibilities of fraud within an entity. While external auditors focus on misstatements in the financial statements that are material, Internal Auditors are often in a better position to detect the symptoms that accompany fraud. Internal Auditors usually have a continual presence in the entity that provides them with a better understanding of the entity and its control systems.

Specifically, Internal Auditors can assist in the deterrence of fraud by examining and evaluating the adequacy and the effectiveness of internal controls. In addition, they may assist management in establishing effective fraud prevention measures by knowing the entity's strengths and weaknesses and providing consulting expertise. The importance an entity attaches to its Internal Audit activity is an indication of the entity's commitment to effective internal control and fraud risk management.

The Internal Auditor's roles in relation to fraud risk management could include initial or full investigation of suspected fraud, root cause analysis and control improvement recommendations, monitoring of a reporting/whistle-blower hotline, and providing ethics training sessions. If assigned such duties, Internal Auditing has a responsibility to obtain sufficient skills and competencies, including knowledge of fraud schemes, investigation techniques, and laws.

Internal Auditors may conduct proactive auditing to search for misappropriation of assets and information misrepresentation. This may include the use of computer-assisted audit techniques, including data mining, to detect particular types of fraud. Internal Auditors also can employ analytical and other procedures to find unusual items and perform detailed analyses of high-risk accounts and transactions to identify potential fraud. At the appropriate time when enough information has been obtained, the HIA should keep Senior Management and the Governing body informed of special investigations in-progress and completed.

3.6.3 Internal Audit Responsibilities During Audit Engagement

To the degree that fraud may be present in activities covered in the normal course of audit work, the *Standards* state that Internal Auditors have the following responsibilities with respect to fraud detection:

(1.) Due Professional Care (Standard 1220).
(2.) Risk Management (Standard 2120).
(3.) Engagement Objectives (Standard 2210).

A well-designed internal control system should help prevent or detect material fraud. Tests conducted by Internal Auditors improve the likelihood that important fraud indicators will be detected and considered for further testing.

3.6.4 Internal Auditor Scepticism

Professional scepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence. An objective, sceptical Internal Auditor neither assumes that management or employees are dishonest nor assume unquestioned honesty.

In all audit work, the exercise of professional scepticism is paramount. Inadequate professional scepticism is frequently cited as a significant reason why material fraud has not been detected. Internal Auditors play a critical role in the success or failure of fraud risk management.

With their intimate knowledge of the workings of an entity, Internal Auditors are in a unique position to identify many of the indicators of fraud. When Internal Auditors act with scepticism and they focus on the effectiveness of internal controls, the likelihood that they will notice the common characteristics of fraud is increased, and they might uncover possible fraudulent activity if and where it exists.

To allow Internal Auditors to exercise scepticism, IIA Standard 1111: Direct Interaction with the Board states that the HIA must communicate and interact directly with the Board. In addition, Standard 1120: Individual Objectivity states that Internal Auditors must have an impartial and unbiased attitude, which is consistent with exercising scepticism. The Governing body's oversight and support of the Internal Audit activity helps the Internal Auditors to maintain independence and objectivity as well as keep an attitude of scepticism.

EACC Reporting Format on the Implementation Of Fraud Risk Mitigation Plan, Template 16 is provided in the Appendix

3.7 TYPES OF AUDITS

The mandate of the Internal Auditors as provided for in PFMR r.160 (1), can be achieved through carrying out a number of types of audits. Audits may be categorised under the following types;

(1.) Financial audits

The assertions for which the Internal Auditor seeks evidence relate to the reliability and integrity of the financial and operating information. It involves the correctness, entirety, legitimacy, provability and regularity of financial transactions, revenue and expenditure, account balances of assets and liabilities, including physical verification of tangible fixed assets, and integrity of accounting books and records.

(2.) Compliance audits

These audits are intended to determine whether an entity has complied with specific policies, procedures, laws, regulations, or contracts that affect the business of the Entity such as the Constitution of Kenya, 2010, Public Finance Management Act 2012 and its regulations, Public Procurement and Disposal Act, 2015 and its regulations, among others.

(3.) Operational audits

These audits cover the review and evaluation of the processes the management has established to ensure the achievement of the objectives and goals, economical, effective and efficient use of resources and safeguarding of assets. This is also referred to systems audits where the evaluation involves the design and operation of an organisation's systems and process rather than locations or departments. e.g. Order –to- pay cycle.

(4.) Information Systems audits

This is a process that collects and evaluates evidence to determine whether the information systems and the related resources adequately safeguard assets, maintain data and systems integrity, provide relevant and reliable information, achieve the entity's goals effectively and use of resources efficiently. The process also determines whether internal control exist that provide reasonable assurance that organisational, operational, and control objectives will be met and the undesired events will be prevented or detected and corrected in a timely manner.

(5.) Value For Money Audit (Performance Audit)

Review for processes to determine whether resources have been used efficiently, effectively and economically.

(6.) Procurement Audit

Reviews different contracts and contracting processes to determine the completeness, efficacy as well as the accuracy of the procurement process.

(7.) Project and Technical Audits

Examining, researching, and verifying a project for consistency and relevance to the basic parameters (quality, performance, cost-effectiveness) that are pre-set at the very beginning of the project.

(8.) Governance Audit

Reviews to ensure the entity conforms to the highest standards of good governance. This includes audit of culture, environmental and sustainability audits.

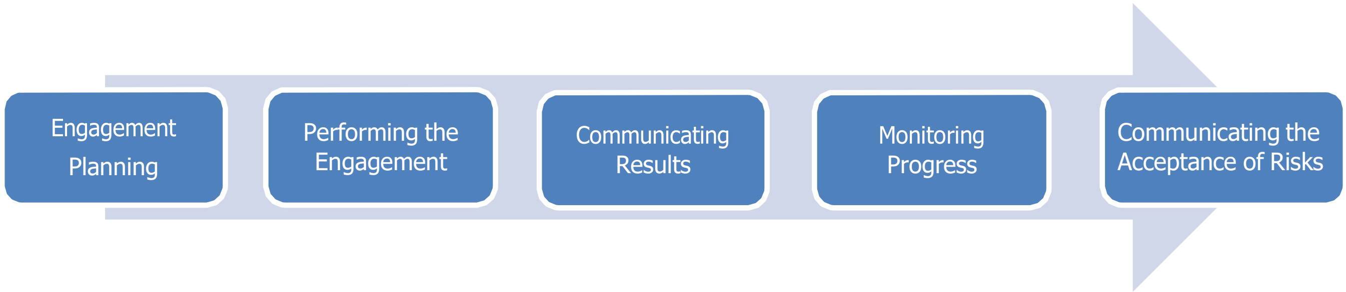
(9.) Emerging areas of Audit

There are emerging areas where auditors should consider focussing on as may be appropriate. These include specialized audits such as: Culture audits, Investigative audits, Forensic audits, Environment audits and Sustainability audits among others

CHAPTER 4 –INTERNAL AUDITING PROCESS

Chapter 4 provides information on the framework for undertaking all Internal Audit engagements from planning to reporting and monitoring progress on the implementation of audit results. The chapter is aligned to the following IIA Standards:

1. Standard 2200: Engagement Planning.
2. Standard 2300: Performing the Engagement.
3. Standard 2400: Communicating Results.
4. Standard 2500: Monitoring Progress.
5. Standard 2600: Communicating the Acceptance of Risks.



4.1 4.2 4.3 4.4 4.5

In undertaking the different assurance assignments, the Internal Auditor shall adhere to the key tasks outlined in this chapter.

4.1 ENGAGEMENT PLANNING

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.

The HIA shall ensure an engagement plan is established for all engagements that will enable the goals and the objectives of the Annual Risk-Based Internal Audit Plan to be achieved. An engagement plan describes the overall audit strategy for an audit engagement, approved by the HIA. Although the Internal Auditor who is in charge of a specific engagement is responsible for the planning, execution and reporting of an audit engagement, the HIA retains overall responsibility to ensure all engagements are effectively and efficiently planned, executed and reported.

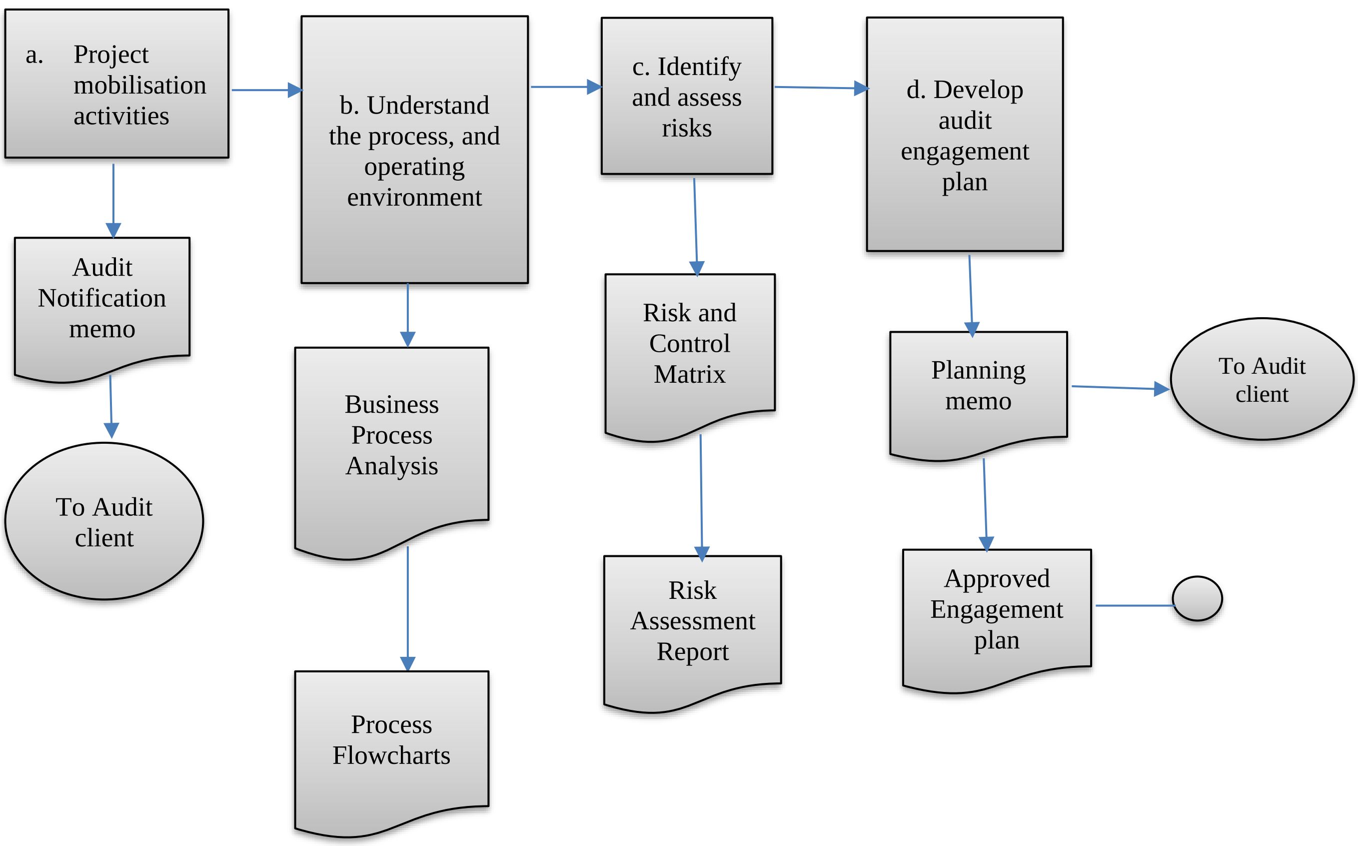
An engagement plan should:

(1.) Define the objective of the engagement and management expectations.
(2.) Establish the scope of the engagement.
(3.) Define the resources required to undertake the engagement.
(4.) Define audit steps to achieve the engagement objectives and adequately cover the scope i.e. engagement work program or audit program.
(5.) Contain a communication plan detailing how the results of the engagement execution shall be communicated.
(6.) Be approved together with the supporting audit program/s before commencement of the engagement by the HIA.

Engagement Plan, Template 17 is provided in the Appendix.

The illustration 5 below gives an overview of the engagement planning activities. The activities may be performed concurrently.

Illustration 5: Overview of Engagement Planning Activities



(1.) Project mobilization activities entail:

(a.) Confirm that the audit is in the approved work plan with approved resources.

(b.) Assembling the audit team.

(c.) Determination of scope and objectives.

(d.) Identifying of business risks.

(e.) Audit delivery timelines

(f.) Generating the list of preliminary requirements

(2.) Understanding the process and operating environment will involve:

(a.) Documenting process flow.

(b.) Major changes in the process since the last time it was audited.

(c.) Emerging issues in the operating environment.

(d.) Alignment to strategic objectives.

(3.) Risk and controls identification and assessment

Based on risk maturity of the entity, identification of risks and controls can be drawn from existing risk registers [for risk mature environments] and fresh risk identification in collaboration with management [for risk naive environments]. Where there are risk registers, Internal Audit evaluates the risks to establish completeness and adequacy before the auditor places reliance on the risk register.

The Internal Audit function is not immune to risks. In addition to assessing how the entity manages risks, the HIA shall be expected to effectively manage risks that impact on the IAF.

Audit risk is the risk of reaching invalid conclusions and/or providing faulty advice based on the audit work conducted.

Business risk is the risk of the entity failing to meet its objectives.

Risks that impact on the IAF which include: false assurance, audit failure and reputational risk. The HIA needs to take necessary steps to ensure that such risks are managed:

(a.) Audit Failure: This is failure to meet audit objectives.

(b.) False Assurance: Giving false confidence or assurance based on perceptions or assumptions rather than fact.

(c.) Reputation risks: Damage to the efficacy of Internal Audit.

(4.) Develop audit engagement plan

To adequately plan an audit engagement, the HIA should ensure that the Internal Auditors have an understanding of the legal framework and other documents maintained in the permanent audit file. A thorough understanding of the process to be audited is undertaken during the planning process (preliminary survey). The HIA should also have an understanding of the business environment and the complexity of the area to be audited such as the audit of projects to determine the skills required. The extent of the preliminary survey will depend on whether: an area has been audited before; the Internal Audit team assigned to the assignment has audited the area before or not; type of audit. A number of techniques can be used to analyse and present the information required at the planning stage. The techniques include:

(a.) Interviews/meetings with the process owners.
(b.) Process walkthroughs or observation.
(c.) Review of relevant literature review including:
  (i.) Functional operational plans aligned to the strategic plan, annual work plan, department budget, function performance contract.
  (ii.) Policies, procedures, flowcharts, system documentation, technical literature.
  (iii.) Management reports and management accounts.
  (iv.) Risks register and risk-control matrix.
  (v.) Minutes of function and management meetings and key correspondence.
  (vi.) Function organogram/structures, key staff job description and key staff turnover.
(d.) Undertaking analytical procedures.
(e.) Internal control survey.
(f.) Narrative notes.
(g.) Flow Charting.
(h.) Data analysis.
(i.) Questionnaires.

The HIA should ensure that documents reviewed by the Internal Auditors during the engagement planning process are appropriately retained as part of work papers including the review notes.

The engagement planning process can also establish if it's feasible to undertake an engagement or not. Where conducting an engagement is not feasible, the HIA should revise the annual audit plan and appropriately communicate the same to the Senior Management and the Governing body. Some of the factors that may result in an engagement not being undertaken include:

(1) Management having strategic commitments resulting in key personnel not being available.
(2) Delays in completing prior audit engagements resulting in the Internal Auditors not being available to commence an engagement.
(3) Required resources (non-human capital) not being made available by the Accounting Officer.

4.1.1. PLANNING CONSIDERATIONS

2201 – Planning Considerations
In planning the engagement, Internal Auditors must consider:

- The strategies and objectives of the activity being reviewed and the means by which the activity controls its performance.
- The significant risks to the activity's objectives, resources, and operations and the means by which the potential impact of risk is kept to an acceptable level.
- The adequacy and effectiveness of the activity's governance, risk management, and control processes compared to a relevant framework or model.
- The opportunities for making significant improvements to the activity's governance, risk management, and control processes.

In developing the audit engagement plan the HIA should ensure the following factors about the area to be audited have been taken into consideration:

(1.) Objectives of the function and how this is linked to the achievement of the entity's strategic plan.

(2.) Risk assessment of the function by management and management's opinion on the effectiveness of the entity's risk management framework. The Internal Auditor should consider management's opinion on how well risks are being managed.

(3.) Management expectations.

(4.) Reviewing the risk management strategies established by management to manage risk identified.

(5.) Governance process and management's opinion on its effectiveness.

(6.) Reviewing the effectiveness of the design of the: risk management strategies and activities/control; and governance system/s and documenting the same in work papers.

(7.) Key changes in processes, systems, people, risk management and governance since the annual audit planning was done.

(8.) Outcome of prior Internal Audits engagements.

(9.) Outcome of work done by other assurance providers both internal assurance providers and external assurance providers.

(10.) Outcome of management controls self-assurance.

(11.) If the current engagement will involve follow-up on the implementation of management action plan on recommendations of previous audits of IAF, OAG or other assurance providers.

(12.) Internal Audit skills and other resources needed to undertake the engagement.

(13.) How will IAF add value in strengthening governance, risk management and internal controls.

The HIA may use the ***pre-engagement / control questionnaire, Template 15*** to obtain necessary engagement planning information from the audit client.

4.1.1.1 EFFECTIVELY MANAGING AUDIT RISKS

At audit planning stage, the Internal Auditor should assess and document the potential audit risks in relation with the specific audit assignment including the planned actions to mitigate those risks. Examples of audit risks to any Internal Audit assignment include:

(1.) The Internal Auditor may misunderstand the scope of the audit. A too wide scope may not be covered within the available timeframe and resources, whereas a too narrow scope may not fully address the audit objectives. This risk should be addressed by proper audit "scoping" during the planning process.

(2.) Conflict of interest may exist between the Internal Auditor and his/her work, which may impair objectivity and undermine the audit results. In mitigation, any threat to independence and objectivity must be disclosed at the planning stage or any other time and the affected Internal Auditor removed from the specific assignment.

(3.) The audit may not meet the expectations of the users. This should be addressed by thorough audit planning, continuous reference to the plan and audit objectives and discussions with management throughout audit testing.

(4.) Less than adequate audit testing or inadequate audit evidence obtained, hence incorrect audit conclusions, due to lack of expertise, experience and proper supervision of the audit team. Close supervision during audit execution can provide timely and invaluable feedback and direction to the audit team.

The HIA should continuously make arrangements for the training of Internal Auditors to uplift their skills and to keep them current with the trends in the Internal Audit profession and standards.

(5.) Audit recommendations are not implemented due to the lack of support from the Senior Management of the audited entity. This requires proper handling of "client" relationships throughout the audit process. The auditor should bear in mind that dealing with Senior Management of the audited entity is relatively sensitive compared to other staff, and that it is crucial to make them aware of the audit findings before they are reported to other parties.

(6.) The audit timetable may be missed due to lack of cooperation from the audited entity's staff. This issue must be addressed during the audit planning meeting to obtain commitment from the personnel.

(7.) The audit timetable may be missed due to poor time management by the audit team. The issue should be mitigated by close supervision of the assignment, improved time plans and management on the part of the auditors – use of weekly time charts and daily action checklists are useful tools.

(8.) Quality of audit reports could be inadequate, contain errors or even be inaccurate. Appropriate review and completing the quality control questionnaire at each stage of the audit will mitigate reporting errors.

In addition, the following templates provided in the Appendix may be used in the planning stages of an engagement.

#	***Template Title***
Template 18	*Audit Notification*
Template 19	*Request for Audit Information*
Template 20	*Information Request Monitoring Checklist*
Template 21	*Business Process Analysis form*
Template 22	*Understanding the IT environment*

Template 23	*Assessing IT general controls and application controls*
Template 24	*Standard Flow Charts Symbols & Narratives*
Template 25	*Fraud Risk Assessment*

4.1.2. ENGAGEMENT OBJECTIVES

2210 – Engagement Objectives

Objectives must be established for each engagement.

The engagement objective should be linked to the goals and objectives of the Annual Risk-Based Internal Audit Plan. The engagement objective should answer the following questions:

(1.) Why are we undertaking the audit?

(2.) What value will IAF add to the area being audited?

(3.) Are we focusing on the risky areas? This will ensure resources are focused on area/s of high risk?

The engagement objective should be linked to the risk/s of the area being audited and should ensure the results of the audit meet management expectations of the Internal Audit services are put into consideration. In developing the engagement's objective/s, the HIA should consider the objective of prior audit engagements of the area and assess if they were achieved and any lessons learnt (i.e. did we set the correct objective, was the objective clear to the Internal Auditors and audit client, did we achieve the engagement objectives).

4.1.3. ENGAGEMENT SCOPE

2220 – Engagement Scope

The established scope must be sufficient to achieve the objectives of the engagement.

Audit scope defines the boundaries of the audit engagement i.e. what is in-scope and what is out-of-scope. This identifies the extent of the processes, systems, staff and physical properties, policies, procedures and timeframe to be reviewed to ensure the engagement objectives is achieved. In defining the audit scope, the HIA should ensure that the Internal Auditors are aware that the IAF does not have limitless resources to audit everything, but they should focus on high-risk areas.

The HIA should ensure factors that may lead to scope limitation are identified during the engagement planning process and strategies to manage the same are established. The HIA should ensure any limitation of scope encountered during engagement implementation is included in the engagement report and appropriately reported to the Senior Management and the Governing body in the quarterly reporting. The HIA should establish if the Internal Auditors will rely on the work done by other assurance providers (refer to Section 2.4 of the Manual) and provide this in the scope statement.

4.1.4. ENGAGEMENT WORK PROGRAM/AUDIT PROGRAM

2240 – Engagement Work Program
Internal Auditors must develop and document work programs that achieve the engagement objectives.

2240.A1
Work programs must include the procedures for identifying, analyzing, evaluating, and documenting information during the engagement. The work program must be approved prior to its implementation, and any adjustments approved promptly.

The HIA shall ensure for each audit engagement an engagement work program/audit program is established defining the audit steps/procedures to be carried out to achieve the engagement objective/audit objective and ensure adequate coverage of the audit scope. In establishing the audit program, the HIA should ensure:

(1.) The engagement objectives and scope are defined.

(2.) The nature, extent and timing of the audit steps are clearly defined. This provides a means: of clearly communicating the necessary instructions to the Internal Audit team; for planning, managing and controlling the engagement; and a basis for reviewing the working papers.

(3.) The audit steps are focusing on the key risk management strategies/controls to be evaluated.

(4.) Procedures for identifying, collecting, analysing, evaluating/interpreting and recording audit evidence are provided.

(5.) Population, sampling criteria and technique and sample size are defined.

(6.) Special audit procedures (e.g. computer-assisted audit techniques) are identified and documented.

(7.) Preliminary assessment of governance, risk management and controls undertaken during the engagement planning phase is considered.

(8.) The audit steps are specific to avoid scope creep (going beyond the defined scope).

(9.) The engagement work program has provision for work paper references.

(10.) Identifies the persons responsible for undertaking the audit steps and reviewing the work done.

(11.) The engagement work program is approved before commencement of field work (engagement execution). The engagement program should be flexible enough to enable the Internal Auditors make appropriate adjustments during field work. Any adjustments should be approved promptly by the HIA or other responsible officer.

4.1.5. ENGAGEMENT RESOURCING

2230 – Engagement Resource Allocation

Internal Auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

The HIA shall ensure all engagements are appropriately and sufficiently resourced to achieve the engagement objective and adequately cover the engagement scope. To achieve this the HIA should ensure engagements are:

(1.) **Appropriately resourced**: human capital (mix of knowledge, skills and other competencies) and non-human resource to ensure the engagement is performed competently and thoroughly.

(2.) **Sufficiently resourced**: the quantity of resources (human and non-human) is adequate to undertake the engagement objective with due professional care.

In determining that each engagement is appropriately and sufficiently resourced the HIA should consider:

(1.) Resourcing planning strategies established during the annual auditing process.

(2.) The audit effort based on the engagement work program or audit programme.

(3.) Consider if there are adequate resources within IAF, staff from other functions within the entity who can be seconded to IAF (safeguards should be put in place to safeguard the objectivity and independence of the employees seconded) or external sources (IAF from other Government entities or consultants).

(4.) Logistics.

(5.) Key management activities being undertaken by management in the area to be audited and the impact it has on the availability of key personnel of the area to be audited.

(6.) Timelines of undertaking the audit and if the outcome of the audit will form a key input in management decision making process.

(7.) Language barriers that may arise e.g. where the audit engagement entails review of community projects.

(8.) Level of supervision required based on the nature and complexity of the audit engagement compared to resources assigned to the engagement.

(9.) Impact of relying on the work of other assurance providers.

(10.) Opportunities of using the engagement as a training ground for Internal Auditors.

(11.) How the application of the resources will be assessed and reported.

Further information on ensuring engagements are adequately resourced is covered under Section 2.2.2 Resource Management and 2.2.3.1 Proficiency.

4.1.6. COMMUNICATING THE ENGAGEMENT PLAN

The outcome of the engagement planning process is the Internal Audit Planning Memo, which should contain the following subject headings:

(1.) Engagement objectives.

(2.) Engagement scope.

(3.) Justification of objectives and scope based on risk analysis.

(4.) Management concerns or expectations.

(5.) Key information required for the engagement.

(6.) Engagement Resources:

 (a) Staffing.

 (b) Time budget/engagement activity-timelines i.e. kick-off meeting, field work, exit meeting, draft report and final report.

 (c) Non-human capital resources e.g. logistic costs, hire of special equipment etc.

(7.) Responsibilities and roles of the Internal Audit team and audit client.

(8.) Summary results of the pre-field work analysis (where appropriate).

(9.) Key audit client contacts.

(10.) Approval by the HIA or a designated officer.

The approved Internal Audit Planning Memo and audit notification should be issued to the audit client 14 days before the commencement of field work/audit engagement and confirmation of the kick-off meeting date. This however does not prevent an Internal Auditor to undertake surprise audit in cases of suspected fraud. The Internal Auditor leading the engagement should ensure the Audit Planning Memo is filed under the current audit working papers.

Engagement Work Program, Sample and Internal Audit Planning Memo, Template 26 are provided in the Appendix.

Note: Internal Audit functions operating with Internal Audit management systems may use templates adopted in the system or customize as provided above.

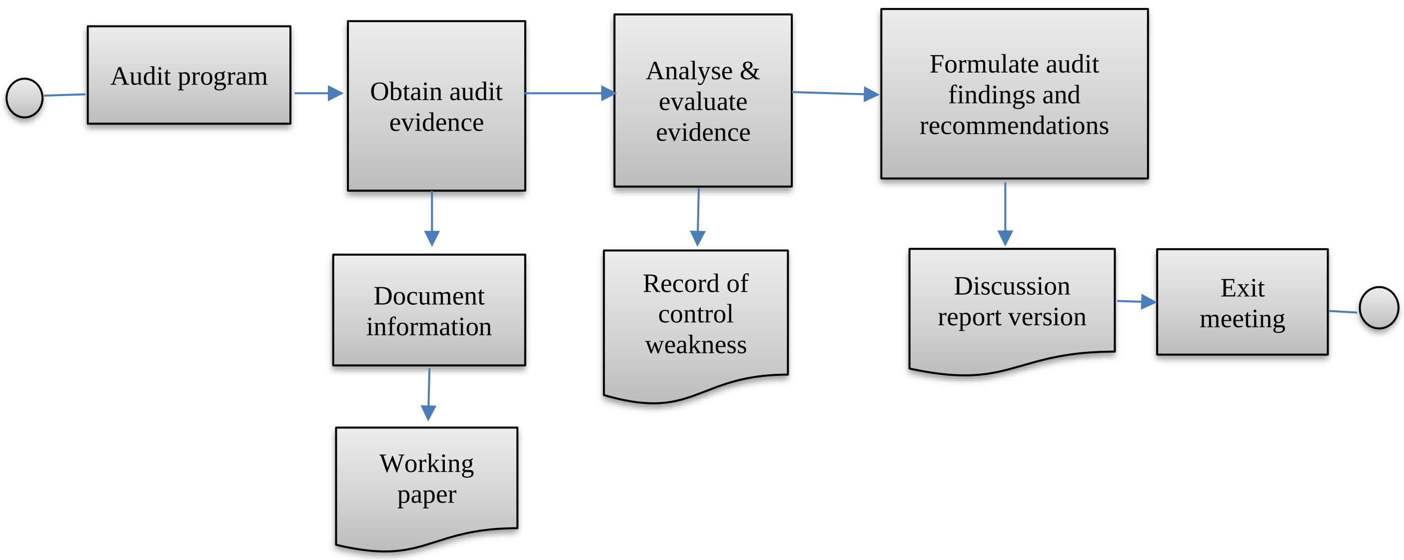
4.2 PERFORMING THE ENGAGEMENT

2300 – Performing the Engagement

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

The illustration 6 below gives an overview of the performing phase of an audit engagement.

Illustration 6 : Overview of Engagement Performing Phase



The HIA shall ensure the audit steps defined in the engagement work program/audit programme are fully implemented so as to ensure sufficient, reliable, relevant and useful information is obtained to: support the observations/findings, recommendations, conclusion and opinion; and ensure the engagement (assurance or consulting) objectives are achieved and management expectations are met.

To ensure the Internal Audit process is systematic and disciplined, the HIA shall ensure each audit engagement has appropriate audit procedures for identifying, analysing, evaluating and documentation information required to achieve the engagement objectives.

4.2.1 AUDIT ENTRANCE MEETING

Performing the engagement commences with the audit entrance meeting where the Internal Audit Planning Memo is discussed. The HIA or the lead Internal Auditor should liaise with the process owner to ensure key staff and the process owners are available to attend the Audit Entrance

Meeting.

The agenda of the Audit Entrance Meeting will include:

(1.) Introduction of audit client's key staff and the Internal Audit team. This shall include clarifying on the roles of the audit client and the Internal Audit team.

(2.) Engagement objectives.

(3.) Engagement scope.

(4.) Concerns or management requests.

(5.) Business conditions and operations of the activity being audited, including recent changes in systems, processes and staff.

(6.) Timelines of key milestones e.g. end of field work, exit meeting, issue of draft report, obtaining management feedback on draft report, and issue of final report.

(7.) Overview of the Internal Audit process.

(8.) The process of communicating throughout the audit, including the methods, time frames, and individuals who will be responsible.

(9.) Availability of key information that had been requested in the Internal Audit Planning Memo.

(10.) Matters of particular interest or concern to the Internal Auditor.

(11.) Description of the IAF's reporting procedures and follow up processes.

Minutes of the Audit Entry Meetings should be maintained and circulated appropriately. The minutes should be maintained as working papers.

Entry Meeting Agenda and Minutes, Template 27 is provided in the Appendix.

4.2.2 IDENTIFYING INFORMATION

2310 – Identifying Information
Internal Auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

HIA shall ensure that the engagement work program/audit programme has audit steps that will enable the Internal Auditors to identify and obtain audit evidence that is:

(1.) **Sufficient**: factual, adequate, convincing, current and collaborated to support the achievement of the engagement objectives. The information identified should enable a prudent person (with the required proficiency) undertaking the audit steps carried out by the Internal Auditors to arrive at the same conclusion. In determining sufficiency of audit evidence, the Internal Auditors must establish if they will test the entire population or test a sample (refer to Section 4.2.2.1 on sampling criteria).

(2.) **Reliable**: obtained through the best attainable information through the use of appropriate audit techniques.

(3.) **Relevant**: supports engagement's observations/findings, recommendations, conclusions and opinion. The information identified should be in-line with the engagement objectives.

(4.) **Useful**: enables the Internal Auditor make recommendations that add value i.e. enable the entity to enhance its governance, risk management and controls processes and systems and thus achieve its mandate, goals and objectives.

(5.) **Other factors**:

(a) **Legally obtained**: adhere to legal and regulatory requirements on assessing information.

(b) **Efficient and economically obtained**: the IAF does not have unlimited resources, the audit steps should enable the Internal Auditor/s to prioritize the most relevant and useful information. This would require the Internal Auditors to review all the information sources as a whole to enable them to determine the best sources and techniques of acquiring the information.

Some of the audit procedures that Internal Auditors can use to obtain sufficient, reliable, relevant, useful, legal and prioritized audit evidence include:

(1.) **Document review**: reviewing relevant literature which may include plans, budgets, policies, procedures, standards, performance reports and minutes of meetings.

(2.) **Enquiry**: holding interviews or meetings with the process owner and other key officers inside and outside the entity to obtain the required audit evidence. They should be well planned for to ensure key participants are available and follow an agreed outline (interview form/checklist or meeting agenda) which should be flexible to accommodate changes. The degree of reliability that the Internal Auditor attaches to evidence obtained in this manner is dependent on the Internal Auditor's opinion of the competence, experience, independence, and integrity of the respondent.

(3.) **Observation**: looking at an operation or procedure being performed by the process owner with a view to determining the manner of its performance. Observation provides reliable evidence as to the manner of the performance at the time of observation, but not at any other time. Enable the Internal Auditor to have a better understanding of the process and collaborate audit evidence that was gathered through other procedures like documents review.

(4.) **Walkthrough**: understanding a system and its related controls by following one transaction through the entire system, from start to finish. This determines the reliability of a system, and whether there are any issues that should be brought to the attention of management.

The HIA shall ensure the audit teams adopts an open and collaborative communication style with the audit client to enable them to obtain the required information.

Audit evidence can also be classified into:

(1.) **Primary vs secondary evidence**: primary evidence gathered directly by the Internal Audit Team whereas secondary evidence is information gathered by the audit client or third party provided to the Internal Auditor. Primary evidence is considered more reliable than secondary evidence.

(2.) **Conclusive vs circumstantial evidence**: conclusive evidence cannot be contradicted by any other evidence. Conclusive evidence is so powerful that it needs no additional corroboration. Circumstantial evidence is indirect evidence because it proves intermediate facts for which a primary fact that is material to the matter being reviewed may be deduced. Circumstantial evidence relies on an inference to connect it to a conclusion of fact and may require additional evidence to prove the fact.

(3.) **Direct vs hearsay evidence**: direct evidence is proof without presumption or inference e.g. source documents or testimony by the performer of an act or key witness. Hearsay/indirect evidence is a statement made by an individual other than the person declaring the statement.

(4.) **Corroborative evidence**: this is evidence that supports other evidence.

(5.) **Testimonial evidence** is obtained from others through oral or written statements in response to an auditor's inquiries. Techniques that could be used to gather testimonial evidence include interviews, focus groups, surveys, expert opinions, and external confirmation.

(6.) **Documentary evidence** is obtained from information and data found in documents or databases. Techniques that could be used to gather documentary evidence include entity's documents, file reviews, databases and spreadsheets, internal audits and evaluations, reports from consultants, studies from other jurisdictions, recalculation, and re-performance.

The Internal Auditor shall consider the following when assessing the quality of audit evidence:

(1.) Evidence generated by the auditor is more reliable than evidence provided by the management or staff of audit client;

(2.) Evidence obtained from external sources is more reliable than that provided internally; and,

(3.) Documentary evidence is more reliable than oral evidence.

4.2.2.1 SAMPLING CRITERIA

Audit sampling is the application of audit tests/procedures to less than 100% of items within a class of transactions (population). Audit sampling is used to provide factual evidence and a reasonable basis to draw conclusions about a population from which a sample is selected.

Determining the number of transactions to test is key in determining if the Internal Auditor has obtained sufficient audit evidence to support achievement of the engagement objective. In determining the amount of data/information needed the Internal Auditors has also to consider the efficiency and economy of obtaining the required evidence. This may lead to the Internal Auditor preferring to review a sample instead of the entire population.

The Internal Auditors will consider the following factors when deciding on the sample size:

(1.) **Engagement/audit objectives**: which may include assessing control's design adequacy, if the control has been operating effectively, quantify the impact of control weakness and compliance level.

(2.) **Population quality**: the variability, volatility and completeness of the population to be tested. The Internal Auditor must establish that population from which the sample is being obtained is appropriate to attain the engagement objectives e.g. when testing payments, the Internal Auditor may prefer to sample transactions from bank transactions compared to a list of payment vouchers.

(3.) **Population size**: this depends on the frequency of implementing the control/task/activity with those implemented more than once daily having more transactions compared to those implemented at a less frequency e.g. weekly, monthly or yearly. This will enable the Internal Auditor to establish if the transaction/s to be tested have occurred during the period under review.

(4.) **Risk and materiality:** rating of risks impacting the area being audited and the significant of achieving/not achieving the objective/s of the area under review.

(5.) **Available resource**: available tools and techniques where adoption of CAATs will enable the Internal Auditors review a bigger sample of digital data compared to using a manual process. The proficiency of the Internal Auditors in applying the tools and techniques where more skilled Internal Auditors will be able to review bigger and complex sample data. The Internal Auditors should consider the time allocated to undertake the engagement to ensure best use of available time. However, the Internal Auditors should refer to the HIA or their supervisors if there is good reason to devote more time to an audit than was originally planned. The Internal Auditors should also assess the cost benefit analysis of analysing a large sample compared to a smaller one.

(6.) **Previous assessments outcome**: based on initial assessment of risks and controls during the planning process; outcomes of previous audits by IAF and other assurance providers; and key changes in processes, systems and staff of the area being audited.

(7.) **Sampling risk**: the risk that the Internal Auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedures. In selecting a sample, the Internal Auditor needs to establish tolerable errors i.e. the maximum numbers of errors that the Internal Auditor is willing to accept and still reach a conclusion that the underlying assertion is correct. In establishing the tolerable errors, the Internal Auditor needs to consult with the HIA and the process owner. This may also be influenced by prior audit results, changes in processes and evidence/conclusions from other sources.

Where Internal Auditors are in doubt about the size of samples to use they should discuss this with the HIA or the Auditor leading the engagement.

In order to select an appropriate sample, it is important to define the population of data. This will be influenced by the period that is covered by the audit. There are a number of methods that can be used to select a sample to try and ensure Internal Auditors cover an appropriate cross section of the population. These include, amongst others, the following:

(1.) **Random sampling**: selection of a transaction to test is not governed by predetermined consideration and thus every unit in the population has an equal probability/chance of being selected for testing.

(2.) **Systematic (interval) sampling**: is a type of probability sampling method in which sample members from a larger population are selected according to a random starting point and a fixed periodic interval. This interval, called the sampling interval, is calculated by dividing the population size by the desired sample size.

(3.) **Stratified sampling**: the population is divided into separate groups, called strata. Then, a probability sample (often a simple random sample) is drawn from each group.

(4.) **Attribute sampling:** used to determine the characteristics of a population being evaluated.

(5.) **Variable sampling**: used to determine the monetary impact of characteristics of a population.

(6.) **Discovery sampling**: used where evidence of a single error or instance would call for intensive investigation.

(7.) **Judgmental sampling**: is a type of non-random sample that is selected based on the opinion of the Internal Auditor. Results obtained from a judgment sample are subject to some degree of bias, due to the frame and population not being identical.

Although there are no established rules about the sample size, Illustration 7 provides a guide that can be adopted by the Internal Auditors in deciding a suitable sample size. In applying the sampling guide, the Internal Auditors should apply their professional judgement based on the risk of the area under review and the engagement objectives to determine if they need to increase the sample size.

Illustration 7: Sample Size Criteria

Frequency of control	No. of transactions/ activities where the control is invoked in a year	Low Risk of failure	Higher Risk of Failure
Annual	1	1	1
Quarterly	2 – 6	1+1	1+1
Monthly	7 – 30	2	3
Weekly	31 – 100	5	8
Daily	100 – 365	15	25
Recurring	More than 365	25	40

The auditor shall exercise professional judgement to determine risk of failure. If stuck, the auditor shall contact HIA for guidance. To determine risk of failure (higher or lower), the following factors shall be considered in part or as a whole:

(1.) Whether there have been changes in the volume or nature of transactions.
(2.) History of errors/ audit queries or fraud.
(3.) Changes to the control design.
(4.) Effectiveness of directive controls [policy and procedures];
(5.) Competence and turnover of the personnel who perform the control or monitor the control;
(6.) Whether the control relies on the performance of an individual; and
(7.) Complexity of the control [more complex controls may have higher risk of failure].

The Internal Auditor will consider the following further guidelines when sampling;

(1.) Where a control is automated, the audit team will carry out data analytics and sample the exceptional items from the results of analytics to confirm if the gaps identified are true.
(2.) Where control is manual, a representative random sample will be taken from the population.
(3.) Where control is semi-automated, the automated part can be subjected to analytics and sample taken to confirm the gaps. The manual process will be sampled from the population.
(4.) Maximum sample size for each control test of operating effectiveness shall not exceed 40 items.

Audit workpapers should include sufficient detail to describe clearly the sampling objective and the sampling process used. The workpapers should include the source of the population, size of the population, sample size, the sampling method used, sampling period and items sampled.

4.2.3 ANALYSING AND EVALUATION

2310 – Identifying Information
Internal Auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

Collected data should be analysed and evaluated against audit criteria to make conclusions. Analysis refers to the breaking down data/activities/processes into smaller, more manageable parts to determine attributes, relationships, cause, effect and make inferences or determine whether further examination is required. Evaluation on the other hand is the systematic determination of the merit, worth, significance of the best subject matter to arrive at a judgement in terms of adequacy, efficiency or effectiveness.

The HIA should ensure that the audit procedures enable the Internal Auditors based on the audit evidence obtained to assess that the controls have been:

(1.) **Adequately designed and implemented**: to enable the entity achieve its mandate, goals and objectives and at the same time manage its risks. Assessing if controls are adequately designed may commence during the engagement planning stage as the Internal Auditors establish which controls needs to be tested. Where a control is poorly designed, the Internal Auditor may not need to undertake further audit tests to assess if it's been operating effectively. In testing if the control is adequately designed, the Internal Auditor needs to test one (1) transaction, activity or task to confirm implementation.

(2.) **Operating effectively**: operating as designed during the review period (defined in the audit scope). This is also called substantive testing.

In testing if the control is adequately designed, the Internal Auditor will use the sampling criteria (refer to Section 4.2.2.1 of the Manual) to establish an adequate sample size to test. The Auditor tests that the control is consistently applied for all sampled items.

Once the required information is obtained the Internal Auditors will establish if the control is adequately designed and/or operating effectively by undertaking appropriate analysis and evaluation techniques.

(1.) **Analysis Techniques**: some of the analyses techniques that the Internal Auditors can undertake include (performing these techniques also enables the Internal Auditor to gather audit evidence):

(a) **Inspection**: reviewing or examining records, processes or properties and comparing with what is expected (this can be defined in the policies, procedures, laws, regulations or standards).

(b) **Re-performance**: re-performing the steps/tasks undertaken by the process owner and assessing if the output obtain by the Internal Auditor is similar to that obtained by the process owner.

(c) **Vouching**: testing the validity of a transaction or recorded information by following it backwards to a tangible source.

(d) **Tracing**: testing the completeness of information by tracking information forward from a tangible source to a subsequent prepared document/report. The difference between vouching and tracing is the direction of the audit procedure i.e. vouching moves backwards from the final document to the source where tracing moves forward from the source to the final document.

(e) **Computation**: checking the arithmetic accuracy of accounting records or performing independent calculations.

(f) **Confirmation**: soliciting and obtaining written verification of the information from an independent third party e.g., circularization to debtors and suppliers to confirm accounts receivable and accounts payable balances respectively.

(g) **Analytical procedures:** to compare actual performance against expectations. Analytical procedures include ratio, trend, and regression analysis; reasonableness tests; period-to-period comparisons; forecasts; benchmarking information against similar sectors or entity units. Internal Auditors may further analyse significant deviations from the expectations (expected variations which failed to occur or unexpected variations) to determine the cause and/or reasonableness of the variance.

The analytical procedures to undertake will depend on the nature, accessibility, and relevance of the data available.

(h) **Data analytics** examining data sets to draw conclusions about the information they contain. With the increase in the volume of data being generated by entities (Big Data), data analytics is being adopted by Internal Auditors to enable them to develop recommendations that provide insight and foresight.

(2.) **Evaluation**: based on the results of the analysis undertaken, the Internal Auditors apply their professional judgement (experience, logic and professional scepticism) to make a conclusion on the engagement objectives and make recommendations. Evaluation also involves assessing the root cause of the audit observation/finding to enable the Internal Auditor provide recommendations to close or correct the audit finding and resolve the root cause.

The analysis and evaluation should be recorded in the ***Record of Control Weakness, Template 28*** provided in the Appendix

4.2.4 DOCUMENTING INFORMATION

2330 – Documenting Information
Internal Auditors must document sufficient, reliable, relevant, and useful information to support the engagement results and conclusions

The HIA shall ensure work papers contain sufficient, reliable, relevant and useful information to: support the observations/findings, recommendations, conclusion and opinion; and ensure the engagement objectives are achieved.

The HIA shall ensure all audit evidence obtained during engagement planning and execution are documented in the work papers. While audit testing and audit findings must be adequately documented and supported in the working papers, auditors should ensure that clarity and functionality is not lost in the volume of data and supporting documents kept.

The HIA shall ensure work papers are appropriately referenced to ensure there is a clear linkage between the audit procedures in the engagement work program and the results of the audit tests (which includes supporting documents).

Internal Audit follows a systematic and disciplined approach. Maintaining appropriate work papers is key in ensuring the Internal Audit process follows a systematic and disciplined approach. Appropriate working papers are those that can stand on their own without requiring any supplemental oral explanation from the Internal Auditor(s) who did the work. Consequently, an independent reviewer should be able to understand all the audit work performed, the findings, how exceptions and other issues were resolved, and the conclusions drawn from the work done.

The working papers are used to:

(1.) Demonstrate whether the engagement was done in compliance with the relevant standards.

(2.) Aid in the organisation, control, administration, and review of the audit work.

(3.) Evidence the engagement work program was fully executed and provides evidence of the conclusions drawn from the audit work done.

(4.) Support the Internal Audit report.

The HIA shall ensure appropriate work papers are maintained which may include the following elements:

(1.) Indexed/referenced and consistently organized.

(2.) Title or heading that identifies the area or process under review.

(3.) Date or period of the engagement.

(4.) Scope of work performed.

(5.) Statement of purpose for obtaining and analysing the data.

(6.) Source(s) of data covered in the workpaper.

(7.) Description of population evaluated, including sample size and method of selection.

(8.) Methodology used to analyse data.

(9.) Details of tests conducted, and analyses performed.

(10.) Conclusions including cross-referencing to the workpaper on audit observations.

(11.) Proposed follow-up engagement work to be performed.

(12.) Name of the Internal Auditor(s) who performed the engagement work.

(13.) Review notation and name of the Internal Auditor(s) who reviewed the work.

(14.) Consistently organisation and documentation, irrespective of the type of audit.

Working Paper, Template 29 is provided in the Appendix.

The HIA shall ensure that as the Internal Auditors come across significant findings, they complete a ***Draft Finding Sheet provided as Template 30*** in the Appendix. The information contained in the finding sheet enables the lead Internal Auditor to compile information necessary to inform a discussion report version for the exit meeting and to efficiently document the draft report. The HIA shall ensure the information recorded in the draft finding sheet includes:

(1.) **Criteria**: standard/criteria i.e. expected condition/should be

(2.) **Condition**: observation i.e. what the actual condition is and how it’s different from the criteria.

(3.) **Cause**: Identify with the audit client what is the reason for the existence/occurrence of the finding.

(4.) **Consequence**: identify if risk will crystallize and the impact if the condition and root cause are not resolved.

(5.) **Corrective Action**: suggested approaches to address the weakness, strengthen the control environment and assist management in achieving desired results. [Note that the recommendation should address the root cause and close the finding/observation. The recommendation should be feasible].

4.2.4.1 ORGANIZATION/STRUCTURE OF WORKING PAPERS

The HIA shall ensure working papers are organized in a manner that enhances efficiency and facilitates accessibility. The HIA shall organize working papers into Permanent Audit File (PAF) and Current Audit File (CAF). Having an index on what should be contained in the PAF and CAF enables: the HIA to assess if all the working papers have been prepared; and enables an Internal Auditor or other user of the audit file to easily navigate through the file. Each major section of PAF or CAF is identified by a unique alpha-numeric reference e.g. PAF and Roman Number for PAF and CAF and Roman Number for CAF. The documents within a section are referenced starting with the section reference and then a number, alphabet or alpha-numeric. This information can be maintained in either hard copy or soft copy for manual or electronic environment.

(1.) Permanent Audit Files

The **Permanent Audit File** (PAF) contains information that should be relevant to the current and future audits. A PAF is useful for the following reasons:

(a) Information/documents that are long term in nature (i.e. important for more than one audit) are consolidates in one location.

(b) To avoid the necessity to re-read the full documents during successive audits, key information may be summarised and included in the PAF for easy future reference.

(c) Information carried forward from previous audits can be filed in the PAF.

There is no standard organisational rule for the PAF. However, the following types of documents may be included in the PAF:

(a) Strategic information.

(b) Organisation charts.

(c) Relevant legal and regulatory requirements.

(d) Correspondence of continuing interest to future audits.

(e) Risk assessment/risk registers.

(f) Key ratios and expected operational deviation.

(g) Updated engagement work program/audit programme.

Illustration 8 provides an index that can be adopted for the PAF.

Illustration 8: PAF Index

Index Ref	Type of Information
PAFI	**Entity/Function Information** which may include: overview of the area being audited and linkage to mandate; objective; organizational structure; key staff and their job description; contracts and key procurements; committees and their terms of reference; and staff authorization limits.
PAFII	**Policies and Procedures**: which may include system documentation (system notes, flow charts); internal control questionnaires; internal control evaluations/self-assessment by management; and risk register.
PAF III	**Rules and Regulations**: relevant laws, regulations, government circulars, standards and directives (internal and external).
PAF IV	**Previous Year Audit History**: copies of previous Internal Audits reports and OAG reports; copies of follow-up reports; recommendation implementation status report by audit client; review notes that were not closed in the previous audit and are relevant in the current review; and matters deserving attention and follow-up in subsequent reviews.
PAV V	**Correspondence**: strategic or important communication received or sent by the function.
PAV VI	**Internal Audit Information**: audit universe; and engagement work program/audit program.

(2.) Current Audit Files

The **Current Audit File** (CAF) contains schedules and documents relevant to the current audit. There is also no standard organizational rule for the CAF. However, the CAF should contain, as a minimum, following working papers:

(a) Internal Audit Planning Memorandum.

(b) Results of the audit steps including significant observations/findings/issues, their causes, impact of the observation and recommendation.

(c) Other documents supporting the audit test results e.g. copies of audit client documents, testimonials, data extracts etc.

(d) Feedback from the audit client on the results of the engagement.

(e) Copies of the draft and final audit reports.

(f) Latest Corrective Action Plan.

(g) Follow up of prior audit reports and matters that have not been resolved.

(h) Administration/correspondence memos and documents.

Illustration 9 provides an index that can be adopted for the CAF.

Illustration 9: CAF Index

Index Ref	Type of Information
CAFI	**Audit Report**: final audit report, draft audit report, interim audit report, ad-hoc audit reports and latest feedback from management on draft, interim and ad-hoc reports, follow-up of prior audits, summary of findings,
CAFII	**General Information**: discussion with management (minutes and notes); and extract of minutes (management, Audit Committee)
CAFIII	**Audit Procedures**: engagement plan, Internal Audit planning memorandum, engagement work program; other planning issues.
CAFIV	**Audit Evidence:** work papers containing audit evidence arranged as per the audit procedures; other documents supporting audit results.
CAFV	**Audit Management**: review and check list (review notes and check lists); audit time summary and budget; and administration/correspondence memos and documents.

4.2.5 ENGAGEMENT SUPERVISION

2340 – Engagement Supervision
Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.

The HIA has the overall responsibility of providing the conclusion and opinion of each audit engagement. This requires the HIA to ensure all audit engagement are properly supervised from planning to communicating results to ensure: the engagement work program is fully implemented so as to achieve the engagement objectives; management expectations are met; quality is maintained which involves adherence to the procedures in this Manual and conformance to Standards; establish if there are any scope limitations; and engagement results are fully supported. The HIA may delegate the supervision responsibility to the Lead Internal Auditor who should be an experienced Internal Auditor.

The HIA shall determine the extent of supervision required for each engagement based on the nature and complexity of the engagement compared to the proficiency of the Internal Audit team. Engagement supervision commences during engagement planning and ends when the results of the audit have been communicated to the audit client. During engagement planning, supervision involves review and approval of the engagement plan. During engagement execution, supervision involves ensuring the engagement work program is fully implemented; any amendments of the engagement work program are approved; results of the audit steps are recorded in the work papers; and work papers are reviewed.

During communication of audit results, supervision involves reviewing the accuracy, objectivity, clarity, constructiveness, completeness and concise of information contained in the report and timely issuance of the audit report.

The lead Internal Auditor shall review the work papers on an on-going basis as they are prepared by the Internal Audit team and any discrepancies or information gaps identified rectified. On completion of field work and before the issuing of the draft report, the lead Internal Auditor shall issue the reviewed audit file to the HIA for further view. On receipt of feedback from the audit client, the lead Internal Auditor shall ensure necessary additional audit steps are undertaken; additional information is acquired; appropriate work papers are maintained; and final audit report is prepared. The lead Internal Auditor shall issue the final report and updated audit file to the HIA for final review and issuance of the final report to the audit client.

Responsibility for first stage work paper review (during field work) and second stage work paper review (before issuance of draft report) will depend on the seniority of the Internal Auditor who performed the detailed audit work. Illustration 10 provides guidance on who can undertake the first and second stage reviews.

Illustration 10: Work Paper Review

Audit Performed By:	First Stage Preview	Second Stage Review
Internal Auditor or below	Senior Internal Auditor	Deputy Head Internal Audit
Senior Internal Auditor	Deputy Head Internal Audit	Head Internal Audit

Irrespective of the person performing the first and second stage review, the HIA must review and sign all documents issued to the audit client including Internal Audit Planning Memo, draft Internal Audit report and final Internal Audit report.

The HIA shall ensure there is documentary evidence of engagement supervision. This may include: review notes/sheet and responses to the same (which includes updating the appropriate work papers); and reviewer initials and dating each work paper after it is reviewed. Issues arising from the review, which are not resolved immediately, should be noted on a review sheet by the reviewer. The review should be conducted at a level of responsibility higher than that of the preparer of the working papers. ***Review Notes, Template 31*** is provided in the Appendix that can be adopted by the HIA.

Supervision provides the HIA or the lead Internal Auditor an opportunity to conduct on the job training to the Internal Audit team. Reviewing of the work papers enables the HIA or the lead Internal Auditor to assess the performance of the Internal Audit team and identify skill gaps. The reviewers should use the review sheets to provide feedback to the Internal Auditors and to ensure that lessons are learnt for future audits. To be effective, this feedback should be provided as promptly as possible. In addition to reviewing work papers at the end of field work, the HIA should plan to visit the Internal Audit team while they are undertaking their field work to observe their performance and discuss significant audit observations and challenges that the team may be facing.

Other ways of undertaking engagement supervision to ensure quality assurance include;

(1.) Audit Client Satisfaction Survey

The HIA shall ensure that an audit client satisfaction survey is conducted for each engagement. The Audit Client Satisfaction Survey form shall be submitted to the audit client with the draft Internal Audit report. The completed survey shall be returned by the audit client with the comments on the draft Internal Audit report.

A meeting should be scheduled with the audit client to discuss any negative feedback contained in the completed audit client satisfaction survey. The issues raised should also be discussed at the team debriefing, even if the audit client declines to meet in this regard.

Note that the ***Audit client Satisfaction Survey, Template 32*** provided in the Appendix contains the minimum content and the relevant Team Leader can add additional content on which feedback is required if deemed necessary meet the IAF requirements.

(2.) Engagement Completion Checklist

The HIA shall ensure an Engagement Completion Checklist is completed for each engagement. The checklist is important in assisting the Internal Audit team in: ensuring that all required activities have been undertaken and this Manual has been adhered to in planning, executing, reporting and following-up engagements; and the required documentation is in place.

The completion checklist must be signed-off by the relevant lead Internal Auditor throughout the engagement to ensure that the checklist is accurately completed, and the working paper file is complete. The HIA must also sign-off the checklist as an indication that he / she is satisfied that the audit working paper file is accurate and complete to substantiate the final audit report.

An Engagement Completion Checklist, Template 33 is provided in the Appendix which the HIA can amend appropriately to meet the IAF requirements.

(3.) Post-Engagement Review

The IAF may select a sample of engagements from a particular timeframe and conduct a review to assess compliance with IPPF and this Manual. These reviews are typically conducted by Internal Auditor who was not involved in the respective engagement.

4.3 COMMUNICATING RESULTS

2400 – Communicating Results
Internal Auditors must communicate the results of engagements.

PFMR r. 171 (1) stipulates that the HIA shall ensure that results of all engagements are communicated promptly to the audit client. In disseminating engagement results, the HIA shall ensure they meet the expectation of the audit client, Senior Management and the Governing body.

PFMR r. 171 (3) (c) stipulates that the HIA shall ensure the written report issued to the audit client is objective, clear, concise, timely, acknowledges satisfactory performance and constructive (recommendations for potential improvement). The report shall clearly present the purpose, scope and results of the engagement.

The HIA shall ensure that each engagement has a communication plan that provides guidelines on what shall be communicated, who shall receive the engagement results, strategies of communicating (verbal and non-verbal); and timing of disseminating the results. The HIA shall also ensure the entity's policy on communication (internal and external) and legal and regulatory provisions are adhered to when communicating engagement results.

4.3.1 CRITERIA FOR COMMUNICATING

2410 – Criteria for Communicating
Communications must include the engagement's objectives, scope, and results.

2410. A1
Final communication of engagement results must include applicable conclusions, recommendations and/or action plans. Where appropriate, the Internal Auditors' opinion should be provided, taking into account the expectations of Senior Management, the Board, and other stakeholders which must be supported by sufficient, reliable, relevant, and useful information.

2410.A2
Internal Auditors are encouraged to acknowledge satisfactory performance in engagement communications.

2410.A3
When releasing engagement results to parties outside the organization, the communication must include limitations on distribution and use of the results.

The HIA shall ensure that each engagement contains a communication plan that has been agreed with the audit client. The communication plan can be part of the Internal Audit Planning Memo. The communication plan shall define:

(1.) **Why** we need to communicate to the audit client. The audit client should be informed whether the engagement objective was met and management concerns addressed.

(2.) **What** to be communicated to the audit client. The audit client should be informed of the objective, scope, observations, recommendation, conclusion and opinion. What to communicate is also influenced by whom the information is being sent to e.g. the process owner may be issued with the entire audit report whereas the Senior Management may be issued with only the executive summary section of the report. The contents of the report to the Audit Committee is subject to agreement between the HIA and the Audit Committee.

(3.) To **whom** communication will be sent. This can be guided by: who needs to provide an action plan for the recommendations made; who needs to act on the action plan or ensure the plan is implemented; or who needs to be aware of the results of the audit (although they may not be expected to provide any feedback or act). On a minimum the Internal Audit report should be issued to the process owner and copied to the Accounting Officer. The communication plan shall consider if there are audit reports that need to be issued to parties outside the entity. In relation to communication to external parties, the HIA should consider the legal requirements, entity's communication policy and impact of such communication to the reputation of the entity. This may require the HIA to consult with Legal Function and Communication Function to ensure required approval are received before the Internal Audit Report is sent to external parties and appropriate communication channels are utilized.

(4.) **How** to communicate to the audit client the audit results. Communication may be verbal (e.g. exit meeting, presentation through Ms Power Point) or in writing (e.g. issuing a draft and final report). The plan should identify the best communication strategy at the different stages of the audit cycle.

(5.) **When** to communicate to the audit client. Communication of results with the audit clients commences during engagement planning (i.e. preliminary study undertaken during engagement planning can identify issues that can be communicated e.g. lack of controls to manage specific risks), is carried on during engagement execution (observations are communicated to the audit client as they are identified) and end when the final audit report is issued. Communication of results also happens when the Internal Auditors are undertaking follow-up audits.

The HIA shall ensure the audit report provides information on the following:

(1.) Engagement objective.

(2.) Engagement scope. Statement of limitation of scope where it was encountered and the impact of achieving the engagement objective or management concerns.

(3.) Management concerns if any.

(4.) Summary of the audit approach/methodology.

(5.) Outcome of engagement tests:

(a) Satisfactory performance – The internal controls are working efficiently and effectively as expected.

(b) Significant audit findings/observations. This shall provide information on what is expected/criteria (based on laws, regulations, policy, procedures, standards or good business practise) and what is the actual condition. Colour coding of findings can be adopted where the high-risk issues are coded red, medium risk issues coded yellow and low risk issues coded green (may not be included in the report being they are not significant).

(c) Causes of the observations.

(6.) Risk exposure and impact/effect of the observations.

(7.) Recommendations that calls for action to rectify the weakness (or improve efficiency) and resolve the cause.

(8.) Management action plan to implement the recommendations. This should provide information: on the activity that shall be implemented by management to resolve the audit finding and close remedy the cause; when the activity shall be undertaken; the person to implement the activity; and resources required to implement the activity (where appropriate).

(9.) Proposed time when a follow-up audit will be undertaken.

(10.) Conclusion.

(11.) Limitation on the use of report by parties outside the entity.

4.3.2 QUALITY OF COMMUNICATING

2420 – Quality of Communicating
Communications must be accurate, objective, clear, concise, constructive, complete, and timely.

2421 – Errors and Omissions
If a final communication contains a significant error or omission, the chief audit executive must communicate corrected information to all parties who received the original communication.

The HIA shall ensure the information contained in audit reports (draft or final) issued to the audit clients has the following attributes:

(1.) **Accurate**: The Internal Audit Report should be free from errors and distortions. The information in the audit report should be based on facts and appropriately supported by audit evidence contained in the work papers.

(2.) **Complete**: The Internal Audit Report should contain all material facts (lacks nothing that is essential) known to the Internal Auditors that if not disclosed will distort the meaning of what is being reported. The report should contain all the significant and relevant information to support the engagement observations, recommendations and conclusion.

Where the HIA identifies errors and omissions after issuing a final report, s/he must assess if the errors or omissions are significant enough (i.e. magnitude (quantitative or qualitative), relevance and impact) to change the audit observation/finding, recommendation, conclusion or opinion. Where the errors or omissions are significant (i.e. relative importance within the context of what is being considered) the HIA shall:

(a) Establish the cause of the errors or omissions and how to prevent such occurring in future engagements.

(b) Establish the most appropriate way to communicate the corrected information to the recipients of the original final engagement communication and communicate.

(c) Ensure the corrected final audit report provides information on: what has been corrected; cause of the error or omission; and strategies for HIA to prevent such causes from recurring again in future audits.

(3.) **Objective**: The Internal Audit report should be fair, impartial and unbiased. The report should demonstrate that the audit process was a balanced assessment of all relevant facts and circumstances. The Internal Auditors should adopt balanced reporting where satisfactory performance is also contained in the report. Satisfactory reporting may include: effectives of controls assessed; improvement in governance, risk management and controls since the previous audit; or implementation of audit recommendations raised by the Internal Auditors, OAG and other assurance providers. Balanced reporting is important to ensure the results of the engagement does not alienate the reader being the key objective of the engagement report is to "call for action" i.e. to make the audit client take effective remedial action.

(4.) **Clear and concise:** The Internal Audit report should be easily understood by its recipients. This requires the report to be logical with high risk issues being reported first; only contain significant and relevant information; be precise and to the point (avoid unnecessary elaboration, redundancy, wordiness); and only include terminologies used by the entity, sector or government entities (avoid jargons).

(5.) **Constructive**: Recommendations provided in the Internal Audit reports should add value i.e. result to the improvement of governance, risk management or controls.

(6.) **Timely**: Internal Audit reports should be issued on a timely basis (as per the communication plan) to ensure management can take timely corrective action and the reports can contribute to management decision making process. A report issued late may be irrelevant to management decision making process resulting to the Internal Audit process not adding value.

4.3.3 OVERALL OPINIONS

2450 – Overall Opinions
When an overall opinion is issued, it must take into account the strategies, objectives, and risks of the organization; and the expectations of the Senior Management, the board and other stakeholders. The overall opinion must be supported by sufficient, reliable, relevant, and useful information.

An audit opinion provides the HIA professional judgement on the status of the entity's governance, risk management and controls. The audit opinion is based on the conclusion of a number of engagements. The HIA shall decide on an appropriate frequency to provide an audit opinion to the Audit Committee and Senior Management with the minimum frequency being annual. When issuing overall opinions, HIA are encouraged to refer to relevant guidance materials. The Institute of Internal Auditors have provided an implementation guide overall opinions and practise guide on formulating and expressing internal audit opinions.

In determining the audit conclusion and/or opinion the HIA shall consider:

(1.) The scope of the engagement/s including the period to which the opinion pertains.

(2.) Scope limitations.

(3.) Impact on the reliance of other assurance providers.

(4.) Summary of the information that supports the opinion.

(5.) Sufficiency, reliability, relevance and usefulness of the audit evidence on which the audit conclusion or opinion is based on.

(6.) The overall opinion, judgement, or conclusion reached.

(7.) Effectiveness of the risk management process.

The reasons for an unfavourable overall opinion must be stated. An overall opinion is the rating, conclusion, and/or other description of results provided by the Head Internal Audit (HIA) when addressing — at a broad level — governance, risk management, and/or control processes of the organization. An overall opinion is the professional judgment of the HIA based on the results of a number of individual engagements and other similar activities — such as reviews by other assurance providers — for a specific time interval. The opinion will be contained in the conclusion part of the Audit Report. Overall opinions differ from conclusions in that a conclusion is drawn from one engagement, and an overall opinion is drawn from multiple engagements. Also, a conclusion is part of an engagement communication, while an overall opinion is communicated separately from engagement communications. It is important to note that the HIA is not required to issue an overall opinion; issuance of such an opinion is at the discretion of the organization and would be discussed with Senior Management and the Governing body.

The HIA shall be responsible for issuing audit conclusion. The HIA shall ensure that the engagement final report provides a conclusion of the audit work undertaken. A conclusion answers the question being raised by the engagement objective e.g. if the audit objective was to assess if the controls of a particular process are working, the conclusion provides feedback if the controls are working as expected or not. The HIA may provide the following conclusions:

(1.) **Satisfactory:** where all key risks have been identified and controls have been properly designed and implemented;

(2.) **Partially satisfactory:** where some important risks have either not been identified and/or the required controls have either not been established or are not functioning effectively; or

(3.) **Not satisfactory:** where key risks have not been identified and/or related controls have not been implemented or are not functioning in accordance with the plan.

4.3.4 DISSEMINATING RESULTS

2440 – Disseminating Results
The chief audit executive must communicate results to the appropriate parties.

2440.A1
The chief audit executive is responsible for communicating the final results to parties who can ensure that the results are given due consideration.

2440.A2
If not otherwise mandated by legal, statutory, or regulatory requirements, prior to releasing results to parties outside the organization the chief audit executive must:

- Assess the potential risk to the organization.
- Consult with Senior Management and/or legal counsel as appropriate.
- Control dissemination by restricting the use of the results.

The HIA shall be responsible for reviewing and approving the draft and final audit reports before they are issued to the audit client, Senior Management, Audit Committee or any other appropriate recipient. Engagement results are disseminated based on the communication plan i.e. why we are communicating, to whom to communicate, what to communicate, how to communication and when to communicate.

The HIA shall ensure a distribution list is maintained for the recipients of the Internal Audit reports. The HIA shall establish a system that enables recipients of Internal Audit reports to confirm receipt of the same. Such information is key where: the HIA is to issue a corrected or revised report (refer to Section 4.3.2 on issuance of a revised report in case of significant errors or omissions); or where the audit client or any other officer who was supposed to receive the report claims that the same was not received by them.

In conformance to the Code of Ethics, and PFMR r. 162(4), confidentiality of the Internal Audit reports is critical and HIA shall ensure that all reports are handled and distributed under confidential cover. Where the Internal Audit report is disseminated in soft copy, a signed hard copy of the final report shall be maintained by the HIA.

The HIA disseminates engagement through:

(1.) **Regular updates**: The Internal Auditors communicate significant audit observations to the audit client as they arise during the audit. The Internal Audit team can agree with the audit client to be holding regular meetings where the team can update the client on the progress of the engagement and significant findings. These sessions can also be used to communicate challenges that the team is facing.

(2.) **Interim audit reports**: Inform the audit client on the progress of the engagement and changes in the audit objective or scope that have occurred during engagement execution. It can also be used to communicate information that requires immediate attention during the course of field work.

(3.) **Exit Meeting**: In conformance to PFMR r. 171(3) (a) that requires an oral preliminary report to be given, the HIA shall ensure an exit meeting is held at the end of field work for every engagement to discuss significant observations and proposed recommendations with the audit client. The meeting provides an opportunity for:

(a) **The Internal Auditor**: To obtain feedback from the audit client on the accuracy of the audit results; determine if further work needs to be done based on the feedback provided by the audit client; and sensitize the audit client that recommendations are more of advisory rather than mandatory; the performance of the Internal Audit team;

(b) **Audit client**: To clarify and agree on the audit findings and recommendations before they are put in the audit report; propose alternative recommendations that are more practical; provide more information where the same had not been provided before; provide information on the management action plan to address the audit recommendations; and communicate areas where they accept the existing risks and justification for the same.

(4.) The HIA shall ensure exit meetings are planned for well to ensure the process owner is available to attend and personnel in the function that are key in implementing recommendations. This also ensures that HIA gets buy-in for the Internal Audit report as this is key in ensuring the process owner provides feedback on the audit report. Besides the key audit issues, the exit meeting should cover the tentative timetable for the issuance of the draft audit report and what the entity would be expected to do after the receipt of the draft report which is to provide written comments on the report and submit them to the auditor within the prescribed timeframe. The HIA shall ensure minutes of the exit meeting are prepared and distributed appropriately and maintained as part of the work papers. ***Exit Meeting Agenda and Minutes, Template 34*** is provided in the Appendix.

(5.) **Draft report**: it is issued to the audit client **within established timelines in the entity but not more than 30 days after the exit meeting**. The purpose of the draft report is to: inform the audit of the key audit observations and recommendations made by the Internal Auditor; request the audit client to provide feedback in writing on the accuracy of the report; reasonableness of the recommendations and conclusions; and request the audit client to provide an action plan on implementing the audit recommendations. ***Internal Audit Draft Report, Template 35*** is provided in the Appendix.

(6.) **Final report**: this contains feedback received from the audit client on the draft report and management action plan on implementing the audit recommendations. **The audit client should provide feedback on the draft report within 14 days after receiving the draft report**. If the Internal Auditor and audit client disagree about the audit results, the final audit report may state both positions and the reasons for the disagreement. The audit client written comments may be included as an appendix to the audit report, in the body of the report or in a cover letter. The report should also communicate where management accepts risks (refer to Section 4.5 of the Manual). ***Internal Audit Final Report, Template 36*** is provided in the Appendix.

The HIA should ensure the final signed audit report is issued to the audit client and copied to the Accounting Officer (at a minimum) **within 30 working days of date of issuing the draft report**.

The HIA shall ensure the draft and final audit reports contain:

(a) **Cover page**: should include name of the entity, author of the report (i.e. IAF), type of report (e.g. draft, final etc), unit/process being reviewed, report date (month and year), type of audit (e.g. ICT Audit) and report reference number. The HIA should innovate ways to secure the confidentiality of the report such including watermarks, headers or footer.

(b) **Report recipients**: designation and use of the report i.e. action required (provide management comment or/and act on recommendation) and for information purpose. The section includes report distribution restrictions to ensure that the report is not used for a purpose that it was not intended for.

(c) **Executive summary**: summarizes the most significant information in the report. Should be organized according to the sequence of the main report. Where necessary the executive summary should stand on its own (communicate independently of the main report). All the information in the executive summary should be supported by the main report. Executive summary should contain summaries on:

i. PFMR requirements on preparing the report
ii. Area being reviewed.
iii. Objective and scope. Limitation of scope if it occurred.
iv. Positive attributes.
v. High risk/key findings.
vi. Overall conclusion.

(d) **Table of content**: generated from the report should have three levels i.e. Heading 1, Heading 2 and Heading 3.

(e) **Introduction**:

i. Background: PFMR requirements on preparing the report, information about the area being reviewed, type of audit, who commissioned the audit and why the audit is being undertaken.
ii. Engagement objective.
iii. Engagement scope including limitation of scope.

iv. Methodology.

(f) **Positive attributes**: status of implementing recommendations of prior audits and area where governance, risk management and controls are effective.

(g) **Detailed findings**: the findings should be prioritized based on their risk level based on a finding rating matrix. The finding matrix should be defined in the report and can be contained in this section or as an appendix. For each finding the following should be provided

i. Criteria: what should be.

ii. Condition: what is i.e. actual status.

iii. Cause: likely cause of condition.

iv. Potential Risk and Consequence: this should be linked to the risks register.

v. Corrective Action: address the cause and the condition.

vi. Management response: action that the audit client will undertake to address the cause and the condition. Should include timeliness, responsibility and resources requirements.

(h) **Conclusion**: overall opinion of the HIA on the effectiveness of governance, risk management or controls of the area being reviewed. A criterion on how the HIA arrived at the conclusion should be provided in this section or as an appendix.

(i) **Acknowledgement**: appreciate the audit client and officers from other functions that assisted during the engagement.

(j) **Approval**: signing of the report by the HIA or appropriate officer in the IAF. For special assignments like investigation the team members involved should also sign the report to ensure ownership.

(k) **Appendix**: includes necessary additional information to support audit findings, recommendations and conclusion that would otherwise interrupt the flow of the report if included in the main body of the report.

(7.) **Quarterly and annual reports**: In compliance with PFMR r. 173(2) and in addition to issuing engagement reports, the HIA is expected to issue quarterly and annual audit reports to the Accounting Officer and Audit Committee. The quarterly report highlighting the significant observations of assurance engagements shall be submitted within 14 days after the end of a quarter. The HIA may maintain a database of significant observations/findings and respective recommendations and management action plan to enable the HIA to: prepare the quarterly and annual reports; and to follow-up implementation of recommendations.

Audit Findings Database, Template 37 is provided in the Appendix.

(8.) **Annual report by the Internal Audit Function**: The HIA shall prepare an annual report that consolidates the quarterly audit assurance reports (considering only assurance engagements) prepared by the Internal Audit function in accordance with formats prescribed by the Public Sector Accounting Standards Board.

4.4 MONITORING PROGRESS

2500 – Monitoring Progress
The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.

2500.A1
The chief audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that Senior Management has accepted the risk of not taking action.

PFMR r. 171(2) and 172 stipulates that the Accounting Officer shall be responsible for the implementation of audit recommendations made in the audit reports and shall develop response and action plan and submit the same to the Chairperson of the Audit Committee within 14 days of receiving the audit report. ***Template 38*** (***Quarterly Summary of Status of Implementing Audit Recommendations***) is provided in the Appendix for use by the Accounting Officer to communicate to the Audit Committee the status of implementing audit recommendations. The Accounting Officer in communicating to the Audit Committee on implementation of audit recommendation shall provide the following information:

(1.) Status of the most recently issued Internal Audit reports which should include status of previously issued reports.

(2.) Status of implementing audit recommendations from OAG and Public Investments and Accounts Committee (PIAC).

(3.) Status of implementing Audit Committee directives and directives from the Governing Body in relation to audit issues.

(4.) Reason for non-implementation of audit recommendations (e.g. lack of resources, no longer applicable etc) and indicate strategy to overcome implementation challenges and provide a new anticipated implementation date.

The Audit Committee shall follow-up the implementation of the response and action plan. Audit Committee Guidelines for National Government Entities (Gazette Notice 2691 of 15 April 2016) Section 2.2(a)(vi) and Section 3.1(b) provides for the mandate and objective of the Audit Committee that includes providing oversight over the implementation of accepted audit recommendations of the Internal Auditor and external auditor.

The HIA shall discuss with the Audit Committee and the Accounting Officer in establishing an effective and efficient system for monitoring the implementation of management action plan in relation to audit recommendations. Such a system shall include:

(1.) Mechanisms of process owners to report to Senior Management and Accounting Officer on the status of implementing the management action plan.

(2.) Follow-up activities undertaken by other assurance providers.

(3.) Role of IAF in following-up implementation of management action plan in relation to:

(a) Internal audit engagements (assurance and consultancy).

(b) OAG recommendations.

(c) Other assurance providers: what they are monitoring, frequency of monitoring, methodology and tools used for monitoring and reporting on the outcome of the monitoring process.

(d) Frequency of monitoring progress. High risk observations should be followed-up within 12 months of their reporting.

(4.) Role of IAF in coordinating receipt of feedback from process owners on the implementation of audit recommendations and submitting a report to the Accounting Officer and the Audit Committee.

(5.) IAF follow-up strategies which may include:

(a) Obtaining feedback from management on the implementation of management action plan.

(b) Undertaking follow-up as part of an engagement.

(c) Undertaking specific follow-up assignment which covers a specific period or a number of engagements.

In undertaking follow-up engagements, the HIA may consider the following:

(1.) Verify the activity reported as implemented by management (***Implementation Status, Template 38*** provided in the Appendix, may be used by management to report on status of implementing agreed management action).

(a) Adequacy of the control's design.

(b) If the control has been operating effectively.

(c) Timeliness of implementation.

(2.) Verify that the action implemented has resolved the weakness identified during the audit

(3.) Verify if implementing the action plan has led to benefit perceived at the time of the undertaking the engagement. This enables the HIA to assess if the recommendations provided by Internal Audit are adding value.

(4.) Assess the rate of implementing the action plan. Where key activities have not been fully implemented (i.e. partially implemented, not implemented or suspended), the Internal Auditor should discuss with the process owner to establish the cause which may include: lack of resources; complexity of the activity vis-à-vis current capacity; unrealistic timelines initially assigned; the cost of implementing the activity being more than the benefit; or risk exposure declining since the time of the engagement.

The nature, extent and timing of follow up should be guided by the following factors:

(1.) Significance of the reported finding. The following approach could be adopted:

(a) Major finding: – follow up promptly after the agreed date for implementation;

(b) Significant finding – follow up review during the next scheduled audit visit; and,

(c) Minor finding – rely on the feedback provided by management on implementation of recommendation.

(2.) Degree of effort and cost needed to correct the reported condition.

(3.) Complexity of the corrective action.

(4.) Time period involved.

The HIA shall ensure the results of the monitoring progress are reported to the process owner, Senior Management, Accounting Officer and Audit Committee. Reporting to the process owner may be done as part of the engagement report and reporting to the Audit Committee and Accounting Officer may be done as part of the quarterly reporting. Where the Internal Auditors have undertaken a specific follow-up engagement, a specific report will be issued for the engagement and distributed accordingly. The summary results of the follow-up shall be used to update the database of findings (refer to ***Audit Findings Database, Template 37***).

Reports on monitoring progress can be included in the engagement report of the audit where the follow-up was undertaken or can be in a separate follow-up report. The separate follow-up report may include the following information:

(1.) **Objective of the follow-up**: Confirming implementation of management action plan; assessing the effectiveness of activities implemented; or verifying the impact of audit recommendations.

(2.) **Scope of the follow-up**: Covering certain period; covering a number of previous Internal Audit engagements; or covering a number of assurance providers.

(3.) **Status of implementation**: The Internal Auditors should focus their effort on monitoring the implementation of action plan that relate to high risk findings/observations. The report may contain information on:

(a) Action plan completed on time.

(b) Activities that are over-due.

(c) Percentage of activities completed.

(d) Impact of implementing action plan e.g. improvement in efficiency, cost saving, increase in revenue etc.

(e) Poorly implemented activities.

(f) Areas where management has accepted the risk and thus planned action plan has not been implemented. The Internal Auditor shall obtain audit evidence to justify this.

(4.)**Conclusion**: On the degree of satisfaction with the implementation of management action plan.

The format used to report on engagements shall be used to report monitoring progress ***(refer to Template 35 and 36 in the Appendix).***

4.5 COMMUNICATING THE ACCEPTANCE OF RISKS

> **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.

In undertaking assurance or consultancy engagements, the Internal Auditor may establish an area where management is taking risk/s that is above the approved risk appetite. The Internal Auditor can also discover such areas when: undertaking audit follow-ups; reviewing management reports, minutes of meetings or documents; or reviewing the reports of the OAG or other assurance providers. The unacceptable risk levels may be as a result of: weak risk management strategies; failure to identify key risks and act on them; or accepting risks based on inaccurate assumptions.

For the Internal Auditor to establish that management has accepted a level of risk that may be unacceptable, the Internal Auditor should understand the entity's risk management policy framework, approved risk appetite statements and approved risk tolerance levels.

Once the Internal Auditors identify instances where management has accepted a level of risk that may be unacceptable, they shall communicate the same to the HIA. The HIA shall assess the same to determine if the assertion by the Internal Auditors is accurate based on the nature, urgency and potential impact of the risk. The HIA shall ensure there is adequate audit evidence to support the assertion that management has accepted a level of risk that is unacceptable.

Where the HIA establishes that management has accepted a level of risk that may be unacceptable, the HIA shall communicate the same to the process owner recommending corrective action. Where the process owner does not adequately address the issue, the HIA shall escalate the matter to the appropriate member of Senior Management for appropriate action. Where the matter is not resolved by Senior Management, the HIA shall escalate the matter to the Accounting Officer and eventually to the Audit Committee where the same is not resolved by the Accounting Officer.

In reporting the matter of management taking unacceptable risk, HIA shall be aware that it's not the role of Internal Audit to manage risk but this is a management role. Thus, the HIA shall use professional judgement when escalating the matter. The HIA shall use the established risk management communication channels (based on the entity's risk management policy framework) when communicating and escalating instances where management has accepted a level of risk that may be unacceptable. The HIA shall also establish the best strategy to communicate to management which may include a combination of both verbal and written communication.

CHAPTER 5 – QUALITY ASSURANCE AND IMPROVEMENT PROGRAM

Chapter 5 covers Standard 1300: Quality Assurance and Improvement Program

1300 - Quality Assurance and Improvement Program

The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.

1310 - Requirements of the Quality Assurance and Improvement Program

The quality assurance and improvement program must include both internal and external assessments.

PFMR r. 166(1) requires that in each year the Head Internal Audit function shall assess its own effectiveness through an internal performance appraisal and shall carry out annual review of the performance of the Internal Audit function commenting on its effectiveness in the annual report to the Governing body. Further, each year the Governing body shall carry out annual review of the independence, performance and competency of the Internal Audit function and comment on their effectiveness in the annual report.

PFMR 166 (3) requires that at least once every three years, but not more than five years, Internal Audit function shall undergo a professional assessment of its effectiveness undertaken by a professionally recognized body or institution.

The work of Internal Audit should be controlled at each level of operation to ensure that a continuously effective level of performance is being maintained. Consequently, the HIA shall establish a Quality Assurance and Improvement Program (QAIP) that enables continuous: evaluation of IAF conformance with the Standards and Internal Auditors application of the Code of Ethics; assessment of the IAF conforms to good practices of the Internal Auditing profession; assessment of IAF efficiency and effectiveness; assessment of the value added by the IAF; and identifies opportunities for improvement.

The HIA shall ensure the QAIP covers all aspects of operation and management of the IAF. The HIA should have mechanism for: assessing the implementation of the action plan resulting from internal and external quality assessment; and continuously enhancing QAIP.

In establishing and maintaining a quality assurance improvement program, HIA are encouraged to refer to relevant guidance materials. The Institute of Internal Auditors have provided QAIP Manual and implementation guide on Standard 1300 for further reference.

5.1 OBJECTIVES AND REQUIREMENTS OF QAIP

The objectives for establishing and maintaining a quality assurance improvement program include;

(1.) Conformance with the definition of Internal Auditing, the Institute of Internal Auditors Code of Ethics, and the Standards for the Professional Practice of Internal Auditing, including timely corrective actions to remedy any significant instances of nonconformance.

(2.) Adequacy of the Internal Audit Charter, goals, objectives, policies, and procedures.

(3.) Contribution to the entity's governance, risk management, and control processes.

(4.) Compliance with applicable laws, regulations, and government or industry standards.

(5.) Effectiveness of continuous improvement activities and adoption of best practices.

(6.) The extent to which the Internal Audit function adds value and improves the entity's operations.

The HIA shall ensure the QAIP established consists of:

(1.) Internal assessment.

(2.) External assessment.

(3.) Communication on QAIP results.

(4.) Use of "Conforms with the *International Standards for the Professional Practice of Internal Auditing*."

(5.) Disclosure of Non-conformance.

The HIA can only use the statement (in writing or verbally) that internal audits are conducted in conformance to IPPF if the results of the internal and external assessments conclude that the IAF generally conforms to IPPF.

5.2 INTERNAL ASSESSMENTS

1311 – Internal Assessments
Internal assessments must include:

- Ongoing monitoring of the performance of the internal audit activity.
- Periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices.

Internal assessment ensures there is consistent conformance to IPPF and quality delivery. The internal assessment consists of on-going monitoring and periodic self-assessment.

5.2.1 ON-GOING MONITORING

The HIA shall ensure ongoing monitoring is an integral part of the day-to-day supervision, review, and measurement of the Internal Audit activity. Monitoring ensures that there is adherence to IPPF and quality is improved on an engagement-by-engagement basis.

The HIA shall ensure there is on-going monitoring from engagement planning to dissemination of engagement results which shall be achieved through: effective engagement supervision; consistent application of this Manual and templates (provided as appendices) which will ensure standard work practice; sign-offs of work papers by the preparer; review of the work papers and engagement results which shall be evidenced by sign-offs by the reviewer.

The HIA shall ensure the on-going monitoring provide feedback on the adequacy of this Manual (and associated appendices). Periodic assessment of achievement of IAF's Key Performance Indicators (KPIs) shall form part of the on-going monitoring.

On-going monitoring shall include:

(1.) Engagement supervision.

(2.) Audit client feedback/survey.

(3.) Engagement completion checklist.

(4.) Post-engagement review.

These have been discussed in chapter 4 section 4.2.5 above.

5.2.2 PERIODIC SELF-ASSESSMENT

Periodic self-assessments are conducted to validate that ongoing monitoring is operating effectively and to assess whether the Internal Audit activity is in conformance with the Standards and whether Internal Auditors apply the Code of Ethics. Through conformance with the Standards and the Code of Ethics, the Internal Audit activity also achieves alignment with the Definition of Internal Auditing and the Core Principles for the Professional Practice of Internal Auditing.

The main objectives of periodic self-assessments are:

(1.) To identify the quality of ongoing performance and opportunities for improvement in Internal Audit processes and procedures.

(2.) To check and validate the objectives and criteria used in the QAIP to determine whether they are still up to date, adequate, and valid.

PFMR r. 166(1) requires the HIA to undertake an annual self-assessment to assess the effectiveness of the IAF and provide recommendations on improving the same. Periodic self-assessments focus on evaluating:

(1.) Conformance with the Internal Audit charter, The IIA's Definition of Internal Auditing, the Code of Ethics, and the *Standards*.

(2.) The quality of the audit work, including adherence to the Internal Audit methodology for selected engagements.

(3.) The quality of supervision.

(4.) The infrastructure, including the policies and procedures, supporting the Internal Audit activity.

(5.) The ways the Internal Audit function adds value to the entity.

(6.) The achievement of performance standards/indicators.

Periodic self-assessments should be conducted through:

(1.) Working paper reviews for conformance with the Definition of Internal Auditing, the Code of Ethics, the *Standards*, and Internal Audit policies and procedures by staff not involved in the respective audits.

(2.) Self-assessment of the Internal Audit activity with objectives/criteria established as part of the QAIP

(3.) Review of Internal Audit performance metrics and benchmarking of best practices.

(4.) Periodic activity and performance reporting to the Governing body and other stakeholders as deemed necessary.

Following a self-assessment, an action plan should be developed to address any identified areas for improvement. This plan should include proposed timelines for actions. The result of the periodic self-assessments and the level of conformance to the *Standards* must be reported to the Governing body at the completion of the self-assessment.

A ***Self-Assessment, Template 39*** is provided in the Appendix that the HIA can customize to support in undertaking Periodic Self-Assessments.

5.3 EXTERNAL ASSESSMENTS

1312 – External Assessment

External assessments must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization. The chief audit executive must discuss with the board:

- The form and frequency of external assessment.
- The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.

PFMR r. 166(3) stipulates that the HIA shall ensure an external assessment is undertaken at least every three years and not more than five years. The external assessment may be undertaken more frequently where there is: change in the leadership of the IAF; high turnover of Internal Auditors; change in the entity structure of the IAF; and significant changes in the Internal Audit Charter and this Manual.

There are two approaches to the conduct of external assessments:

(1.) A full external assessment involves the use of a qualified, independent assessor or assessment team to conduct the full assessment.

(2.) A self-assessment with independent (external) validation (SAIV) involves the use of a qualified, independent assessor or assessment team to conduct an independent validation of the self-assessment completed by the Internal Audit activity.

Regardless of which approach is selected for the external assessment, a qualified, independent external assessor or assessment team must be retained to complete the assessment. The HIA usually consults with Senior Management and the Governing body to select the assessor or assessment team. Assessors or assessment teams must be competent in two main areas: the professional practice of Internal Auditing (including current in-depth knowledge of the IPPF), and the external quality assessment process. Entities may seek additional qualifications and competencies for assessment team leaders and independent validators, including:

(1.) An additional level of competence and experience gained from previous external assessment work.

(2.) Completion of the IIA's quality assessment training course or similar training.

(3.) HIA (or comparable Senior Internal Audit management) experience.

(4.) Relevant technical expertise and industry experience.

Individuals with expertise in other areas may provide assistance, as appropriate. The HIA should determine the skills sets desired for the external assessment and use professional judgment to select the assessor or assessment team. Each individual on the team does not need to possess all of the preferred competencies; rather, the team as a whole should possess the necessary qualifications to provide the best results.

The HIA, Senior Management, and the Governing body should consider and discuss several factors related to independence and objectivity when selecting an external assessor or assessment team. External assessors, assessment teams, and their organizations should be free from actual, potential, or perceived conflicts of interest that could impair objectivity. The HIA are encouraged to refer to the Implementation guidance on Standard 1312 – External Assessments.

5.3.1 FULL EXTERNAL ASSESSMENT

The scope of a full external assessment typically includes three core components:

(1.) The level of conformance with the Standards and the Code of Ethics. This may be evaluated via a review of the Internal Audit activity's charter, plans, policies, procedures, and practices. In some cases, the review may also include applicable legislative and regulatory requirements.

(2.) The efficiency and effectiveness of the Internal Audit activity. This may be measured through an assessment of the Internal Audit activity's processes and infrastructure, including the QAIP, and an evaluation of the Internal Audit staff's knowledge, experience, and expertise.

(3.) The extent to which the Internal Audit activity meets expectations of the Governing body, Senior Management, and operations management, and adds value to the entity.

5.3.2 SELF-ASSESSMENT WITH INDEPENDENT EXTERNAL VALIDATION

The second approach to meeting the requirement for an external assessment is an SAIV. This type of external assessment typically is conducted by the Internal Audit activity and then validated by a qualified, independent external assessor. The scope of an SAIV typically consists of:

(1.) A comprehensive and fully documented self-assessment process that emulates the full external assessment process, at least with respect to evaluating the Internal Audit activity's conformance with the Standards and the Code of Ethics.

(2.) Onsite validation by a qualified, independent external assessor.

(3.) Limited attention to other areas such as benchmarking; review, consultation, and employment of leading practices; and interviews with senior and operations management.

5.3.3 PEER REVIEW

Peer review arrangements can provide a cost-effective approach to meeting the requirements of Standard 1312, particularly for small Internal audit activities. However, peer reviewers are required to meet the *independence* and *qualifications* criteria specified in the Standard.
The following briefly outlines some of the key considerations:

(1.) All members of the assessment team who perform the external assessment are to be independent of that organization and its Internal Audit activity personnel. Real, potential, and perceived conflicts of interest should be considered.

(2.) Within the public sector, individuals working in separate Internal Audit activities in a different entity within the same tier of government may be considered independent for purposes of conducting external assessments, as long as they do not report to the same HIA.

(3.) Two entities may not review each other mutually. Reciprocal external assessment teaming arrangements between three or more organizations (e.g., within an industry or other affinity group, regional association, or government departments) may be structured in a manner that achieves the independence and objectivity. Still, care must be exercised to ensure that independence and objectivity are not impaired, and all team members are able to exercise their responsibilities fully.

5.4 REPORTING ON THE QUALITY ASSURANCE AND IMPROVEMENT PROGRAM

1320 – Reporting on the Quality Assurance and Improvement Program
The chief audit executive must communicate the results of the quality assurance and improvement program to Senior Management and the board. Disclosure should include:

- The scope and frequency of both the internal and external assessments.
- The qualifications and independence of the assessor(s) or assessment team, including potential conflicts of interest.
- Conclusions of assessors.
- Corrective action plans.

The results of any internal and external assessments, and the level of Internal Audit conformance with the *Standards*, must be communicated to Senior Management and the Governing body at least annually. The results of ongoing monitoring must be communicated annually to the Governing body and other appropriate stakeholders. Further, the results of any periodic self-assessments or external assessments, and the level of conformance with the *Standards*, must be reported to the Governing body after their completion. The QAIP and the resulting action plan (sometimes referred to as a management action plan) should be made available to external assessors and be robust enough for external reliance.

During an external assessment, the assessor may provide recommendations to address areas that were not in conformance with the Standards, as well as opportunities for improvement. The HIA should communicate to Senior Management and the Governing body any action plans to address recommendations from the external assessment. The HIA may also consider adding the external assessment recommendations and action plans to the Internal Audit activity's existing monitoring processes related to Internal Audit engagement findings (see Standard 2500 – Monitoring Progress). After recommendations identified during the external assessment have been implemented, the HIA generally communicates this to the Governing body, either as part of the Internal Audit activity's monitoring progress or by following up separately through the next internal assessment (Standard 1311), as part of the QAIP.

5.4.1 CONCLUSION OF ASSESSORS

Quality assurance and improvement program, external assessment reports include the expression of an opinion or conclusion on the results of the external assessment. In addition to concluding on the Internal Audit function's overall degree of conformance with the Standards, the report may include an assessment for each standard and/or standard series. An example of a rating scale that may be used to show the degree of conformance is:

(1.) Generally conforms – This is the top rating, which means that an Internal Audit activity has a charter, policies, and processes, and the execution and results of these are judged to be in conformance with the Standards.
(2.) Partially conforms – Deficiencies in practice are judged to deviate from the Standards, but these deficiencies did not preclude the Internal Audit activity from performing its responsibilities.
(3.) Does not conform – Deficiencies in practice are judged to be so significant that they seriously impair or preclude the Internal Audit activity from performing adequately in all or in significant areas of its responsibilities.

5.5 USE OF "CONFORMANCE WITH IPPF"

1321 – Use of "Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing"
Indicating that the internal audit unit conforms to the International Standards for the Professional Practice of Internal Auditing is appropriate only if supported by the results of the quality assurance and improvement program.

2430 – Use of "Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing"
Indicating that engagements are "conducted in conformance with the International Standards for the Professional Practice of Internal Auditing" is appropriate only if supported by the results of the quality assurance and improvement program.

Internal Auditors may only communicate in writing or verbally that the Internal Audit activity conforms with the *Standards* if results of the QAIP, including both the internal and external assessment results, support such a statement. Once an external assessment validates conformance with the *Standards*, the Internal Audit activity may continue to use the statement as long as internal assessments continue to support such a statement until the next external assessment.

The HIA **may** include a statement in the engagement report that the engagement was conducted in conformance with IPPF. Although this is not a requirement, it's good to build the credibility of the audit process and engagement report. The HIA **can only** include this statement in the Internal Audit Report or use it verbally where the results of both the internal and external quality assessment provide evidence that the IAF generally conforms to IPPF. After an external quality assessment, the HIA can only use this statement if the results of the internal assessment continue to support this until the next external quality assessment.

The HIA shall consider the following factors in determining on whether to use the statement "Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing":

(1.) If the results of either the current internal assessment or most recent external assessment do not confirm general conformance with *Standards* and the Code of Ethics, the HIA cannot use the conformance statement or where it is using it, the HIA must discontinue indicating that it is operating in conformance.

(2.) If an IAF has been in existence at least five years and has not completed an external assessment, the HIA may not indicate that it is in conformance with IPPF.

(3.) If it has been more than five years since the last external assessment was conducted in, the HIA must cease indicating that it is in conformance, until a current external assessment is completed and it supports that conclusion.

(4.) If an IAF has undergone an external quality assessment within the past five years but has not conducted an internal quality assessment annually or after every other year after the external assessment, the HIA shall consider whether it is still operating in conformance and if appropriate to indicate conformance until validated by an internal assessment.

(5.) If an IAF that has been in existence fewer than five years may indicate that it is operating in conformance with IPPF only if a documented internal quality assessment (i.e., the periodic self-assessment) supports that conclusion.

(6.) If an external quality assessment reflects an overall conclusion that the IAF was not operating in conformance with the Standards, the HIA must immediately discontinue using any statements that indicate conformance. The HIA may not resume use of a conformance statement until it has remediated the nonconformance and conducted an external assessment to validate an overall assessment of conformance with IPPF.

5.6 DISCLOSURE OF NON-CONFORMANCE

2431 – Engagement Disclosure of Non-conformance
When non-conformance with the Code of Ethics or the Standards impacts a specific engagement, communication of the results must disclose the:

1. Principle(s) or rule(s) of conduct of the Code of Ethics or Standard(s) with which full conformance was not achieved.
2. Reason(s) for non-conformance.
3. Impact of non-conformance on the engagement and the communicated engagement results.

1322 – Disclosure of Non-conformance
When non-conformance with the Code of Ethics or the Standards impacts the overall scope or operation of the internal audit unit, the Chief Audit Executive must disclose the non-conformance and the impact to the Accounting Officer and the Audit Committee.

The results of any internal and external assessments may uncover impairments to independence or objectivity, scope restrictions, resource limitations, or other conditions that may affect the Internal Audit activity's ability to fulfil its responsibilities to stakeholders. The HIA shall communicate where the engagement or Internal Audit activity was not in conformance to the *Standards* and Code of Ethics of the Senior Management and the Governing Body. This can be communicated through meetings (with the audit client, Senior Management, or Governing body) or can be included as part of the Internal

Audit report. Instances of non-conformance should be adequately documented in the working papers and supported with appropriate assessment evidence. Communication shall include impact of the non-conformance to: the scope and operations of the IAF; and meeting expectation of management and the Governing body.

Some of the factors that can result to the audit process not conforming to IPPF include:

(1.) Impairment of Internal Audit objectivity and independence.

(2.) Limitation of scope.

(3.) Lack of required information/data or management issuing the Internal Auditors unreliable data/information.

(4.) IAF lacking the required proficiency.

(5.) Failure to consider risk when preparing the Internal Audit plan.

(6.) Lack of adequate resources.

HIA are encouraged to refer to the implementation guides and Quality Assessment Manual for further details on QAIP requirements. Further, HIA and other Internal Auditors are encouraged to undertake the Internal Audit Quality Assessors Program Certification, offered by IIA Kenya.

GLOSSARY OF TERMS

IIA Standards – The purpose of the International Standards for the International Professional Practices Framework (IPPF) of Internal Auditing Standards is to:

- Delineate the basic principles that represent the practice of Internal Auditing as it should be;
- Provide a framework for performing and promoting a broad range of value-added Internal Audit activities;
- Establish the basis for the evaluation of Internal Audit performance; and,
- Foster improved organisational processes and operations.

The Standards consist of Attribute Standards, Performance Standards, and Implementation Standards:

Attribute Standards address the characteristics of organisations and parties performing Internal Audit activities

Performance Standards describe the nature of Internal Audit activities and provide quality criteria against which the performance of these services can be evaluated

Implementation Standards describe how the attribute and performance standards can be applied to specific types of audit engagements. Implementation Standards have been established for **Assurance** and **Consulting** activities.

The Standards are part of the International **Professional Practices Framework** of the IIA that includes the Mission of the Internal Audit, Core Principles, Definition of Internal Auditing, the Code of Ethics, the Standards, and recommended guidance(implementation and supplemental guidance).

Accounting Officer – An officer designated in writing by the Cabinet Secretary to be responsible for the proper management of the finances of the different National Government entities as may be specified in the different designations.

Add Value – Value is provided by improving opportunities to achieve organisational objectives, identifying operational improvement, and/or reducing risk exposure through both assurance and consulting services.

Adequate Control – Present if Management has planned and organised (designed) in a manner that provides assurance that the organisation's risks have been managed effectively, and that the organisation's goals and objectives will be achieved efficiently and economically.

Analytical Review – The study and investigation of significant ratios, trends, and other statistics to form conclusions about the likelihood of weaknesses and errors in financial and operating systems.

Analytical Procedures – Tests of the reasonableness of account balances and transactions, involving comparisons of recorded amounts with expectations developed by the Auditor, and scrutinising for unusual items. Analytical procedures may be used at all stages of the audit and are required by Generally Accepted Auditing Standards to be used in the mobilisation and completion phases.

Assurance Services – An objective examination of evidence for the purpose of providing an independent assessment on risk management, control, or governance processes for the organisation. Examples may include financial, performance, compliance, system security, and due diligence engagements.
Attribute Sampling – Selection of items from a population according to attributes of the item other than its financial value.
Audit Comfort – The assurance derived by the Auditor that sufficient appropriate audit evidence has been obtained for each significant business activity and related audit area with financial reporting significance to reduce audit risk to a level that will enable the Auditor to issue his opinion on the financial statements.
Audit Documentation and Guiding Principles – Audit procedures should be documented in sufficient detail to enable a reviewer to understand what work was done (nature, timing, and extent), what evidence was seen (results) and what conclusions were drawn from the evidence obtained. There are four guiding principles: ▪ Maximise the use of the tailored audit programme, which becomes the record of work done; ▪ Write it once (in detail); ▪ Ensure effective use of additional detailed working papers for areas of higher risk and/or matters of significant judgement; and, ▪ Ensure effective application of Generally Accepted Audit Working Practices.
Audit Plan – The overall service plans to meet and preferably exceed client expectations. The Audit Plan should consider items such as developments affecting the client's business, client and stakeholder needs and expectation, risk assessment, potential critical matters, the audit strategy, engagement management, client communication, client reporting, as well as actions for other assurance services beyond the audit. The Audit Plan is communicated to the client. The format of the documentation of the Audit Plan is flexible and can range from a formal document, which can be a multi-disciplinary plan, to a very concise memo or outline containing only the minimum expected written sections on client needs/expectations and related actions.
Audit Program – A document comprising a detailed description of the work to be performed in an audit assurance or consulting engagement. When completed it forms, with supporting documentation where necessary, the record of work done.
Audit Risk –The risk of reaching invalid conclusions and/or providing faulty advice based on the audit work conducted. Audit risk consists of three components: Inherent Risk, Control Risk (Inherent and Control Risk are together referred to as the risk of material misstatement), and Detection risk.

Audit Sampling – Audit sampling is the application of auditing procedures to a representative group of less than 100% of the items within an account balance or class of transactions (or subject of either) for the purpose of evaluating some characteristic of the entire balance or class (or population tested).
Automated Controls – Controls performed by the computer systems or enforced by system security parameters.
Application Control – Manual or automated control activities that typically operate at a detailed business process or transaction level and are designed to ensure the integrity of the accounting records. Application controls, which can be preventive or detective in nature, directly support the information processing objectives of completeness, accuracy validity, and restricted access.
Business Objectives – Business can be defined at a very high level (e.g., a company mission statement) or at a lower level in the organisation (e.g., operational objectives that accomplish the strategy set by the high-level objectives) but are best clearly stated and specific. Objectives are used to measure performance, and they are essential to any planning process. For purposes of the audit, understanding the client's business objectives is the necessary first step to identifying risks because risks are defined in relation to specific objectives.
Business Process – Any sequence of transactions that takes place in order to get work done and achieve the business' objectives. These may range, in order of complexity, from a simple procedure, such as paying a bill, to a key element of the business operations, such as a wholesaler's stock management and distribution system, to functional, such as maintaining an organisation's financial records, to cross functional, like application of human resources.
Business Risk – The risk of the organisation failing to meet its objectives. Anything that can prevent the achievements of the organisation's objectives, including strategic, operational, financial, and compliance objectives. Business risks can only be identified and defined in relation to a business objective, which means understanding objectives must be a prerequisite for identifying risks. To derive real value for audit purposes risks should be defined in detail.
Chief audit executive - describes the role of a person in a senior position responsible for effectively managing the Internal Audit activity in accordance with the entities Internal Audit charter and the mandatory elements of the International Professional Practices Framework. The chief audit executive or others reporting to the chief audit executive will have appropriate professional certifications and qualifications. The specific job title and/or responsibilities of the chief audit executive may vary across organizations.
COBIT (Control Objectives for Information and Related Technologies) - Framework created by ISACA for information technology (IT) management and IT governance.
Compliance – Conformity and adherence to policies, plans, procedures, laws, regulations, contracts, and other requirements.
Computer Environment – A specific set of hardware and system software on which the client's business and accounting systems run (e.g., AS/400. UNIX).

Confidence Level – The level of assurance derived from audit testing based on samples rather than evaluation of the whole population.
Conflict of Interest – Any relationship that is, or appears to be, not in the best interest of the organisation. A conflict of interest would prejudice an individual's ability to perform his or her duties and responsibilities objectively.
Consulting Services – Advisory and related client service activities, the nature and scope of which are agreed with the client and which are intended to add value and improve an organisation's governance, risk management, and control processes without the Internal Auditor taking management responsibility. Examples include counsel, advice, facilitation, and training.
Control – Any action taken by management, the Governing body, and other parties to manage risk and increase the likelihood that established objectives and goals will be achieved. Management plans, organises, and directs the performance of sufficient actions that provide reasonable assurance that objectives and goals will be achieved.
Control Environment – The attitude and actions of the Governing body and management regarding the significance of control within the organisation. The control environment provides the discipline and structure for the achievement of the primary objectives of the system of internal control. The control environment includes the following elements: ▪ Integrity and ethical values ▪ Management's philosophy and operating style ▪ Organisational structure ▪ Assignment of authority and responsibility ▪ Human resource policies and practices ▪ Competence of personnel
Control Framework – Internal control should be evaluated against a framework of five interrelated components that should be applied at any level of the organisation (i.e. at the entity, management unit and/or business process level). These components are: Risk assessment; Control environment; Information and communication; Control activities; and Monitoring of controls. The division of internal control into the five components provides a useful framework to consider how different aspects of an entity's internal control may affect the audit. However, the primary consideration is, to evaluate and validate whether material misstatements in classes of transactions, account balances or disclosures and related assertions rather than its classification into any particular component.
Control Processes – The policies, procedures, and activities that are part of a control framework, designed to ensure that risks are contained within the risk tolerances established by the risk management process.

Control Risk – The level of business risk not being prevented or detected by the internal control environment as a whole. One of the three components of audit risk, control risk is the risk that a material misstatement that could occur in an account or cycle will not be prevented or detected and corrected on a timely basis by the client's internal controls. This risk is a function of the effectiveness of the design and operation of internal control in achieving the client's objectives relevant to the preparation of the client's financial statements. Control risk is considered through the application of the audit comfort cycle, particularly at "taking stock" meetings when relevant parties consider how much comfort has been obtained.
Corporate Governance - structure and system of rules, practices and processes by which an organisation is directed, controlled and held accountable. It encompasses authority, accountability, stewardship, leadership, direction and control exercised in organisations.
Detection Risk – Detection risk is the risk that the auditor will not detect a material misstatement that exists in an account balance or class of transaction. This risk is a function of the effectiveness of the auditing procedures and their application by the auditor. Detection risk is considered when determining the nature and extent of audit work.
Development and Implementation controls – Procedures or mechanisms in place to ensure that systems are developed, configured, and implemented to meet financial, operational, and compliance business objectives.
Direct Substantive Testing – Evaluation of an organisation's internal control environment purely through the detailed testing of individual transactions, assets, and liabilities (e.g., used when the internal control environment is too weak to justify tests of controls, or evidence of the existence and operation of controls is not available).
Engagement – A specific Internal Audit assignment, task, or review activity, such as an Internal Audit, Control Self-Assessment review, fraud examination, or consultancy. An engagement may include multiple tasks or activities designed to accomplish a specific set of related objectives.
Engagement Objectives – Broad statements developed by Internal Audit that define intended engagement accomplishments.
Engagement Work Program – A document that lists the procedures to be followed during an engagement, designed to achieve the engagement plan.
Fraud – Illegal acts characterised by deceit, concealment, or violation of trust. Fraud comprises both the use of deception to obtain an unjust or illegal financial advantage, and intentional misrepresentations affecting the financial statements by one or more individuals among management, employees, and third parties. Fraud can be broken down into two main categories: Fraudulent financial reporting, and Misappropriation of assets.
Fraud Risk –The risk of material misstatement of the financial statements due to fraud.

General computer controls – Controls used to manage the IT activities and computer environment, covering the following areas: Maintenance of existing systems, Development and implementation of new systems, information security, and computer operations.
Governance – The combination of processes and structures implemented by the Governing body in order to inform, direct, manage, and monitor the activities of the organisation toward achievement of its objectives.
Governance Arrangements – The means by which an organisation is directed and controlled.
GTAGs (Global Technology Audit Guide) - describes how members of governing bodies, executives, IT professionals, and Internal Auditors address significant IT-related risk and control issues and presents relevant frameworks for assessing IT risk and controls.
Haphazard Selection Method – A common method of selection in non-statistical sampling. This provides a method for selecting a judgmentally representative sample without relying on a truly random process. "Haphazard" does not mean without thought or effort.
Independence – The freedom from conditions that threaten objectivity or the appearance of objectivity. Such threats to objectivity must be managed at the individual auditor, engagement, functional, and organisational levels.
Information and Communication – Systems that support the identification, capture, and exchange of information in a form and time frame that enables people to carry out their responsibilities.
Information Processing Control – A type of control activity comprising two broad groupings – application and general computer controls.
Information Processing Objectives – Management's goals in relation to controls, which, if effectively met, help support management's implicit financial statement assertions: completeness of records, accuracy of records, validity of records, restricted access to assets and records.
Information Security Controls – Procedures or mechanisms in place to ensure that access (physical or logical) to systems resources and data is authenticated and authorised.
Inherent Risk – The level of business risk associated with the organisation as a whole, or the individual system being examined. Inherent risk is one of the three components of audit risk. The susceptibility of an account balance of cycle to material misstatement, assuming there were no related internal controls. These risks are specific to the client and can relate to macro-economic, industry, or company level conditions, or to characteristics of the client's accounts.
Interval Sampling – Selection of a sample by extracting every n^{th} item from the population.
ISO 38500 - provides guiding principles for members of governing bodies of organizations on the effective, efficient, and acceptable use of information technology (IT) within their organizations.

ITIL (Information Technology Infrastructure Library) - set of detailed practices for IT activities such as IT service management (ITSM) and IT asset management (ITAM) that focus on aligning IT services with the needs of business
Management Information – Any information that management uses to control the business, and on which they make business decisions. This may be the formal output from a business process or any other informal source from which management obtains information.
Management's Risk Assessment Process – The entity's process for identifying and analysing relevant risks to achievement of its objectives, forming a basis for determining how the risk should be managed.
Materiality – The degree of relevance or significance of an absent, inappropriately designed, or ineffective control or management arrangement, in relation to the business risk of the organisation. Materiality is the magnitude of an omission or misstatement of accounting information that may change or influence the judgement of a reasonable person.
Materiality by Nature – The degree of relevance towards business risk of an individual system or set of transactions arising from the characteristics of that system and its sensitivity towards public opinion.
Materiality by Value – The degree of relevance towards business risk of an individual system or set of transactions arising from its monetary value.
Monetary Unit Sampling – The selection of items from a population in such a way that the probability of an item being selected is proportional to its financial value.
Monitoring of Controls - A process that assesses the quality of internal control performance over time. This is accomplished through on-going monitoring activities, separate evaluations, or a combination of the two.
Non-sampling Risk – The risk that the auditor draws an incorrect conclusion from an item or items that (s)he has examined.
Objectivity – An unbiased mental attitude that allows Internal Auditors to perform engagements in such a manner that they have an honest belief in their work product, and that no significant quality compromises are made. Objectivity requires Internal Auditors not to subordinate their judgement on audit matters to others.
Population - The source of items to be selected by audit sampling. Can be an entire account balance or class of transactions. However, the population should be restricted to the group of transactions, for the time period and under the same system of controls that are relevant to the objectives of the test to be performed.

Precision - A term used in connection with the assurance, which substantive procedures provide. In relation to analytical procedures, the degree of precision refers to the closeness of the expectation to the "correct" amount. In relation to audit sampling, it represents the excess of tolerable misstatement over estimated misstatement and is a measure of how precise the conclusions from sampling applications need to be.
Professional Scepticism - An attitude, which means that the auditor should not accept explanations at face value but should validate or corroborate explanations with additional evidence.
Preliminary Systems Evaluation – An initial evaluation of an audited body's control environment conducted to establish whether proper accounting records are maintained to provide sufficient, relevant, and reliable audit evidence to support a systems-based audit approach.
Process – A procedure designed to pass transactions or other information through a system.
Random Sampling – A common method of selection in non-statistical sampling involving the selection of items from a sample such that all items have an equal chance of being selected, with all bias removed.
Ratio Analysis – This is the comparison, across time or to a benchmark, of relationships between financial statement accounts (e.g., return on equity), and between an account and non-financial data (e.g., cost per order or sales per square foot). Ratio analysis allows one to understand how the entity stands in relation to its industry competitors and also in relation to itself between periods.
Reasonable Assurance - is a high level of assurance regarding material misstatements, but not an absolute one. Reasonable assurance includes the understanding that there is a remote likelihood that material misstatements will not be prevented or detected on a timely basis.
Reasonableness Test – This is the analysis of account balances, or changes in account balances, between accounting periods, that involves the development of a model to form an expectation based on financial data, non-financial data, or both. In many instances, an auditor uses very simple computations. For example, an expectation for hotel revenue may be developed using a model that includes the average occupancy rate and the average room rate by category or class of room. Similarly, to develop an expectation expense, one may use a model including number of employees, pay rates, hire and termination dates, and overtime.
Reportable Condition – Matters that should be communicated because they represent significant deficiencies in the design or operation of internal control that could adversely affect the entity's ability to record, process, summarise, and report financial data consistent with management's assertions in the financial statement. Such deficiencies may involve aspects of the internal control components of: ▪ The control environment; ▪ Entity's risk assessment process;

▪ Control activities; ▪ Information system, including the related business processes, relevant to financial reporting and communication; or, ▪ Monitoring controls.
Sample Selection Method - To obtain a representative sample so that sample results can be projected to the population or stratum. Random, haphazard, or systematic methods may be applied, according to the circumstances.
Sampling Risk – The risk that sampling techniques will lead the auditor to an incorrect conclusion, compared to the conclusion reached if the whole population were tested. The risk that the conclusions drawn from an audit sample testing might be different from those that would have been reached if the auditing procedures were applied to all the items in the account or population.
Sampling Unit – The specific population characteristic that defines the items to be sampled. For example, in testing accounts receivable, the sampling unit might be the customer balance, invoice number, or individual sales transaction.
Substantive Audit Evidence -The evidence obtained from performing substantive tests, which could be either substantive analytical procedures, tests of detail, or a combination of both.
Substantive Tests – An evaluation of an individual transaction, asset, or liability in comparison to its recorded or expected value or state. Substantive tests include substantive analytical procedures and tests of details of transactions and account balances. Their purpose is to provide evidence supporting management's implicit financial statement assertions or, conversely to discover misstatements in the financial statements directed to management information capable of being related to financial statement assertions.
Substantive Error – A physical difference between the transaction or property being examined, and what the auditor expects to find.
Systems – The procedures and operations by means of which an organisation's transactions and events are affected and recorded.
Systems Based Auditing – Evaluation of the design and operation of an organisation's systems of internal control.
Systematic Selection Method – A common method of selection in non-statistical sampling. This method of selecting a sample selects every nth item. A sampling interval is established based on the number of items, without reference to size or monetary value of the item.
Targeted Testing - The preferred method of selecting items to be tested based on some characteristic, rather than selecting them "randomly" using audit sampling.
Test of Controls – The evaluation of the design and operation of an identified internal control.

Tests of Control Error – A failure to operate a control in the manner intended by management, record evidence of the operation of that control, or failure to comply with rules and policies which exercise control.
Value for Money – The economy, efficiency, and effectiveness of an organisation's operations.
Walk Through Test – The process of confirming an Auditor's understanding of a system and its related controls by following one transaction through the entire system, from start to finish.
Walk Through Error – The failure of a document or process to follow the system described to the auditor.

APPENDICES

APPENDIX A: AUDIT TEMPLATES

No.	Description	Purpose/Aim
1	Internal Audit Charter	To outline the purpose, authority and responsibility of the Internal Audit function
2	Declaration of Independence and Objectivity	To document conflict of interests and threats to the auditor's objectivity
3	Internal Audit Strategic Plan	Outlines the IAFs long term plan
4	Internal Audit Universe	List of audit areas within the entity
5	Risk Model	To categorise risks based on their source for analysis
6	Risk control matrix	To map risks and internal controls
7	Heat map	To give a graphical view of risks per auditable area
8	Annual Risk Based Internal Audit Work Plan	Lists audit assignments to be undertaken in the year
9	Daily time sheet	To show the tasks accomplished on each working day and the number of "person-hours" spent on each task
10	Work allocation and time budget	To assign work and time to assignments in the audit plan
11	Resource calendar or chronogram	For approval by the Audit Committee at the beginning of the year
12	Internal Audit Quarterly report	Summary report to the Audit Committee and Senior Management
13	Internal Audit Annual Report	Summary of all audit activities compared to the audit plan during the FY under review
14	HIA assessment	To assess performance of the Head of Internal Audit.
15	Pre-engagement / control questionnaire	Conduct survey of the entity level controls
16	Fraud Risk Mitigation Plan	To report identified fraud incidences for further action
17	Engagement Plan	Summarise audit objective, scope, key risks, controls, audit approach , audit client, team etc. for consideration and approval by the Head Internal Audit
18	Audit Notification	To Inform audit client of engagement dates, objectives, scope, documentation and other requirements/information on engagement.
19	Request for Audit Information	A list of documents to be prepared in advance by the audit client for the auditor

No.	Description	Purpose/Aim
20	Information request monitoring checklist	To track when information requested was provided
21	Business process analysis form	To document understanding of the process
22	Understanding the IT environment	To document understanding of the IT environment and assess IT complexity
23	Assessing IT general controls and application controls	To conduct a high level assessment of IT general controls and application controls
24	Standard flow chart symbols and narratives	To document flow of activities in a process
25	Fraud risk assessments	To document fraud risk assessment by the team and plan appropriate audit steps
26	Internal Audit planning memo	To inform the audit client of the scope
27	Entry meeting agenda and minutes	To be record audit client and audit team expectations
28	Record of control weakness	Form for evaluating audit finding
29	Working paper	Document work carried out
30	Draft finding sheet	A record of potential audit comments for discussion with audit client
31	Review notes	To record supervisors comments and disposal of the comments
32	Audit client Satisfaction Survey	To obtain feedback after the end of the assignment on Internal Audit service.
33	Engagement Completion Checklist	Used in wrapping up audit file to ensure completion of audit tests and working paper file
34	Exit Meeting Agenda and Minutes	To be record of audit draft findings and recommendations
35	Internal Audit draft report	Audit report format for draft client submitted for audit client comments
36	Internal Audit final report	Audit report format for final communications
37	Audit findings database	A repository of all previous audit findings
38	Quarterly summary of status of implementing audit recommendations	Database for monitoring disposal of audit findings
39	Self-Assessment	To undertake periodic internal self-assessment by the Internal Audit function
	Audit Committee Charter	
	Engagement Work Program Sample	

APPENDIX B: IIA CODE OF ETHICS

Internal auditors are expected to apply and uphold the following principles:

1. **Integrity**
   The integrity of internal auditors establishes trust and thus provides the basis for reliance on their judgment.
2. **Objectivity**
   Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgments.
3. **Confidentiality**
   Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.
4. **Competency**
   Internal auditors apply the knowledge, skills, and experience needed in the performance of internal audit services.

Rules of Conduct

1. Integrity

Internal auditors:

1.1. Shall perform their work with honesty, diligence, and responsibility.
1.2. Shall observe the law and make disclosures expected by the law and the profession.
1.3. Shall not knowingly be a party to any illegal activity, or engage in acts that are discreditable to the profession of internal auditing or to the organization.
1.4. Shall respect and contribute to the legitimate and ethical objectives of the organization.

2. Objectivity

Internal auditors:
2.1. Shall not participate in any activity or relationship that may impair or be presumed to impair their unbiased assessment. This participation includes those activities or relationships that may be in conflict with the interests of the organization.
2.2. Shall not accept anything that may impair or be presumed to impair their professional judgment.
2.3. Shall disclose all material facts known to them that, if not disclosed, may distort the reporting of activities under review.

3. Confidentiality

Internal auditors:
3.1. Shall be prudent in the use and protection of information acquired in the course of their duties.
3.2. Shall not use the information for any personal gain or in any manner that would be contrary to the law or detrimental to the legitimate and ethical objectives of the organization.

4. Competency

Internal auditors:
4.1. Shall engage only in those services for which they have the necessary knowledge, skills, and experience.

4.2. Shall perform internal audit services in accordance with the International Standards for the Professional Practice of Internal Auditing.
4.3. Shall continually improve their proficiency and the effectiveness and quality of their services.

APPENDIX C: INTERNATIONAL STANDARDS FOR THE PROFESSIONAL PRACTICE OF INTERNAL AUDITING

ATTRIBUTE STANDARDS

1000– Purpose, Authority, and Responsibility

The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework (the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the *Standards*, and the Definition of Internal Auditing). The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.

1010 – Recognizing Mandatory Guidance in the Internal Audit Charter

The mandatory nature of the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the *Standards*, and the Definition of Internal Auditing must be recognized in the internal audit charter. The chief audit executive should discuss the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework with senior management and the board.

1100–Independence and Objectivity

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

1110–Organizational Independence

The chief audit executive must report to a level within the organization that allows the internal audit activity to fulfil its responsibilities. The chief audit executive must confirm to the board, at least annually, the organizational independence of the internal audit activity.

1111 – Direct Interaction with the Board

The chief audit executive must communicate and interact directly with the board.

1112 – Chief Audit Executive Roles Beyond Internal Auditing

Where the chief audit executive has or is expected to have roles and/or responsibilities that fall outside of internal auditing, safeguards must be in place to limit impairments to independence or objectivity.

1120–Individual Objectivity

Internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest.

1130–Impairments to Independence or Objectivity

If independence or objectivity is impaired in fact or appearance, the details of the impairment should be disclosed to appropriate parties. The nature of the disclosure will depend upon the impairment.

1200–Proficiency and Due Professional Care

Engagements must be performed with proficiency and due professional care.

1210–Proficiency

Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

1220–Due Professional Care

Internal auditors must apply the care and skill expected of a reasonably prudent and competent internal auditor. Due professional care does not imply infallibility.

1230–Continuing Professional Development
Internal auditors must enhance their knowledge, skills, and other competencies through continuing professional development.
1300–Quality Assurance and Improvement Program
The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.
1310–Requirements of a Quality Assurance and Improvement Program
The quality assurance and improvement program must include both internal and external assessments.
1311–Internal Assessments
Internal assessments must include:
- Ongoing monitoring of the performance of the internal audit activity.
- Periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices.

1312–External Assessments
External assessments must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization. The chief audit executive must discuss with the board:
- The form and frequency of external assessment.
- The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.

1320-Reporting on the Quality Assurance Improvement Program
The chief audit executive must communicate the results of the Quality Assurance Improvement Program to the Senior Management and the board. Disclosure should include:
- The scope and frequency of both the internal and external assessments.
- The qualifications and independence of the assessor(s) or assessment team, including potential conflicts of interest.
- Conclusions of assessors.
- Corrective action plans.

1321 – Use of "Conforms with the *International Standards for the Professional Practice of Internal Auditing*"
Indicating that the internal audit activity conforms with the *International Standards for the Professional Practice of Internal Auditing* is appropriate only if supported by the results of the quality assurance and improvement program.
1322 – Disclosure of Nonconformance
When nonconformance with the Code of Ethics or the *Standards* impacts the overall scope or operation of the internal audit activity, the chief audit executive must disclose the nonconformance and the impact to Senior Management and the Board.
PERFORMANCE STANDARDS
2000–Managing the Internal Audit Activity
The chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organization.
2010–Planning
The chief audit executive must establish a risk-based plan to determine the priorities of the internal audit activity, consistent with the organization's goals.
2020–Communication and Approval

The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.

2030–Resource Management

The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

2040–Policies and Procedures

The chief audit executive must establish policies and procedures to guide the internal audit activity.

2050–Coordination and Reliance

The chief audit executive should share information, coordinate activities, and consider relying upon the work of other internal and external assurance and consulting service providers to ensure proper coverage and minimize duplication of efforts.

2060 – Reporting to Senior Management and the Board

The chief audit executive must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan and on its conformance with the Code of Ethics and the *Standards*. Reporting must also include significant risk and control issues, including fraud risks, governance issues, and other matters that require the attention of senior management and/or the board.

2070 – External Service Provider and Organizational Responsibility for Internal Auditing

When an external service provider serves as the internal audit activity, the provider must make the organization aware that the organization has the responsibility for maintaining an effective internal audit activity.

2100–Nature of Work

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

2110 – Governance

The internal audit activity must assess and make appropriate recommendations to improve the organization's governance processes for:

- Making strategic and operational decisions.
- Overseeing risk management and control.
- Promoting appropriate ethics and values within the organization.
- Ensuring effective organizational performance management and accountability.
- Communicating risk and control information to appropriate areas of the organization.
- Coordinating the activities of, and communicating information among, the board, external and internal auditors, other assurance providers, and management.

2120 – Risk Management

The internal audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes.

2130 – Control

The internal audit activity must assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

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.

2201 – Planning Considerations

In planning the engagement, internal auditors must consider:

- The strategies and objectives of the activity being reviewed and the means by which the activity controls its performance.
- The significant risks to the activity's objectives, resources, and operations and the means by which the potential impact of risk is kept to an acceptable level.
- The adequacy and effectiveness of the activity's governance, risk management, and control processes compared to a relevant framework or model.
- The opportunities for making significant improvements to the activity's governance, risk management, and control processes.

2210 – Engagement Objectives

Objectives must be established for each engagement.

2220 – Engagement Scope

The established scope must be sufficient to achieve the objectives of the engagement.

2230 – Engagement Resource Allocation

Internal auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

2240 – Engagement Work Program

Internal auditors must develop and document work programs that achieve the engagement objectives.

2300 – Performing the Engagement

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

2310 – Identifying Information

Internal auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

2320 – Analysis and Evaluation

Internal auditors must base conclusions and engagement results on appropriate analyses and evaluations.

2330 – Documenting Information

Internal auditors must document sufficient, reliable, relevant, and useful information to support the engagement results and conclusions.

2340 – Engagement Supervision

Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.

2400 – Communicating Results

Internal auditors must communicate the results of engagement.

2410 – Criteria for Communicating

Communications must include the engagement's objectives, scope, and results.

2420 – Quality of Communications

Communications must be accurate, objective, clear, concise, constructive, complete, and timely.

2421 – Errors and Omissions

If a final communication contains a significant error or omission, the chief audit executive must communicate corrected information to all parties who received the original communication.

2430 – Use of "Conducted in Conformance with the *International Standards for the Professional Practice of Internal Auditing*"

Indicating that engagements are "conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*" is appropriate only if supported by the results of the quality assurance and improvement program.

2431 – Engagement Disclosure of Nonconformance

When nonconformance with the Code of Ethics or the *Standards* impacts a specific engagement, communication of the results must disclose the:

- Principle(s) or rule(s) of conduct of the Code of Ethics or the Standard(s) with which full conformance was not achieved.
- Reason(s) for nonconformance.
- Impact of nonconformance on the engagement and the communicated engagement results.

2440 – Disseminating Results

The chief audit executive must communicate results to the appropriate parties.

2450 – Overall Opinions

When an overall opinion is issued, it must take into account the strategies, objectives, and risks of the organization; and the expectations of senior management, the board, and other stakeholders. The overall opinion must be supported by sufficient, reliable, relevant, and useful information.

2500 – Monitoring Progress

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

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.