Chartered Institute of Internal Auditors

Communication with the board, top management and the auditee.

Chief Audit Executive Forum – Oslo 12 November 2018

Presented by:

Stephen Maycock QiCA, CMIIA, CFIIA, CIA, CRMA, CIRM

Agenda

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- Escalating concerns to the board and top management.
- Design and application of rating scales.
- Issues resolved before internal audit report is published.
- Periodic reporting to the board and top management.
- Key Performance Indicators for Internal Audit

Communications

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Mission of Internal Audit

Chartered Institute of Internal Auditors

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

Mission of Internal Audit

Chartered Institute of Internal Auditors

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

Core Principles *(extract)*

- Communicates effectively.
- Provides risk-based assurance.
- Is insightful, proactive, and future-focused.
- Promotes organizational improvement.

Topic 1

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When is an observation so serious that it should be immediately discussed with the board and top management?

What criteria could be used?

Escalation criteria

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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 organisation, the chief audit executive must discuss the matter with senior management. …

IIA Standards – January 2017

Implementing Standard 2600

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CAE must understand:

- The level of risk that the board considers acceptable
- The organisations formal risk acceptance process
- The requirements for reporting on risk.

Applying Standard 2600

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Stephen's top tips

- Criteria = Risk appetite.
- Seek agreement of manager responsible.
- Escalate to audit sponsor.
- Escalate one step at a time.
- Align with corporate reporting requirements.
- Encourage managers to escalate.
- Consider joint escalation.
- Do not concede – unless convinced.
- Do be open to alternative solutions.

Escalation criteria

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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 organisation, 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.

IIA Standards – January 2017

Standard 2600 - Interpretation

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The identification of risk accepted by management may be observed through:

- an assurance or consulting engagement,
- monitoring progress on actions taken by management as a result of prior engagements,
- or other means

It is not the responsibility of the chief audit executive to resolve the risk.

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How should rating scales be designed and applied?

Rating scales

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Application to:

- Individual findings
- Assurance assignments
- Periodic opinions

Rating scales

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Individual findings

Ratings – individual findings

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Criteria for ratings frameworks:

- Objectives – level of threat to achievement
- Risk – exposure v appetite
- Control – design / operation / effectiveness
- Level of management attention
- Timeframe – urgency

Ratings – individual findings

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High

A significant control deficiency that requires the immediate attention of senior management as the organisation is exposed to a high level of risk that is likely to impact the achievement of one or more of the organisation's key objectives.

Ratings – individual findings

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Criteria for ratings frameworks:

- Objectives – level of threat to achievement
- Risk – exposure v appetite
- Control – design / operation / effectiveness
- Level of management attention
- Timeframe – urgency

Which criteria (or combination) do you prefer?

Ratings – individual findings

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High

A significant control deficiency that requires the immediate attention of senior management as the organisation is exposed to a high level of risk that is likely to impact the achievement of one or more of the organisation's key objectives.

Rating scales

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Assurance assignments

Ratings – assurance assignments

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Key design decisions

- What to rate (subject matter)
- Time dimension – past, present or future
- Single or multiple ratings
- Design of criteria
- Effect of organisational context

Ratings – assurance assignments

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Conclusion on:	Criteria		
Risk identification	Multiple techniques used - likely to identify risks.	Techniques used, but some deficiencies.	Insufficient use of risk identification techniques.
Risk response	Risks mitigated to an acceptable level.	Some improvements required.	Risks not mitigated to an acceptable level.
Action plans	Prompt action taken.	Action defined.	No action defined.
Monitoring	Sufficient monitoring.	Monitoring incomplete.	No/minimal monitoring.
Grading	Acceptable	Issues	Unacceptable

Rating scales

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Periodic opinions

Ratings – periodic opinion

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Overall Opinion

The rating, conclusion, and/or other description of results provided by the chief audit executive addressing, at a broad level, governance, risk management, and/or control processes of the organization.

Ratings – periodic opinion

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Overall Opinion

The rating, conclusion, and/or other description of results provided by the chief audit executive addressing, at a broad level, governance, risk management, and/or control processes of the organization.

An overall opinion is the professional judgment of the chief audit executive based on the results of a number of individual engagements and other activities for a specific time interval.

IIA Standards – January 2017

Ratings – periodic opinion

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What sources of information could be used to support a periodic opinion?

Ratings – periodic opinion

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Information sources:

- Assurance engagements
- Consulting engagements
- Follow-up activities
- Other assurance providers results
- Attendance at executive meetings
- Discussions with executives
- Organisation data
- Employee survey results
- Any other sources

Ratings – periodic opinion

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Standard 2450 Overall Opinion

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.

Ratings – periodic opinion

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Standard 2450 Overall Opinion

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.

IIA Standards – January 2017

Standard 2450 – interpretation

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The communication will include:

- The scope, including the time period to which the opinion pertains. [plus scope limitations].
- Consideration of all related projects, including the reliance on other assurance providers.
- A summary of the information that supports the opinion.
- The risk or control framework or other criteria used as a basis for the overall opinion.
- The overall opinion, judgment, or conclusion reached.

Ratings – periodic opinion

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	CE	RM	IC	CA	Mon
Entity A					
Entity B					
Entity C					
Entity D					
Division X					

Ratings – assurance assignments

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Conclusion on:	Criteria		
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Ratings – periodic opinion

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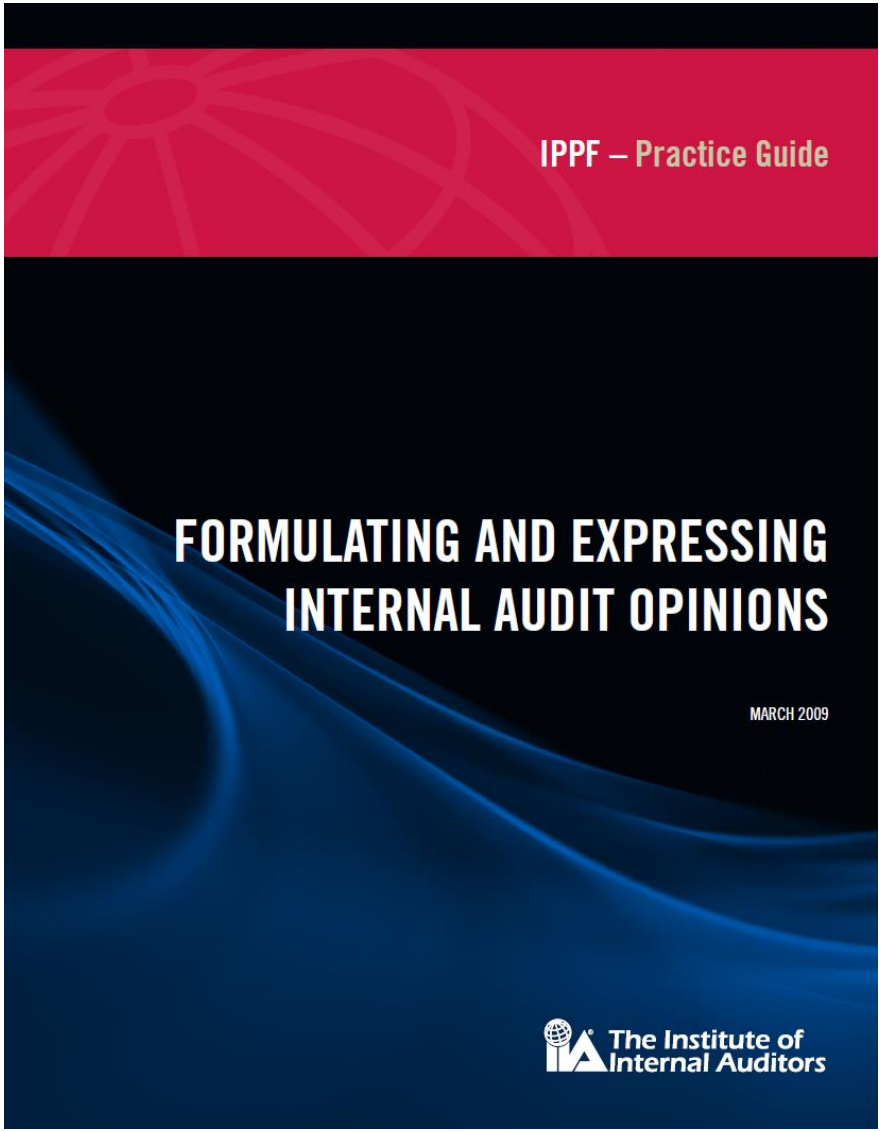
	Risk id	Mitigation	Action	Monitor
Entity A				
Entity B				
Entity C				
Entity D				
Div' X				



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Rating scales - design

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Stephen's top tips:

- Clear definitions – include time dimension
- Avoid personal criticism
- Avoid formulaic criteria for deciding rating
- Consider multiple ratings for assignments
- Make use of risk / control frameworks
- Consider using 4 point scales
- Align with risk management taxonomy

Rating scales - application

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Stephen's top tips:

- Use the guidance
- Compare with instinct
- Compare rating with wording
- Peer review and challenge

Topic 3

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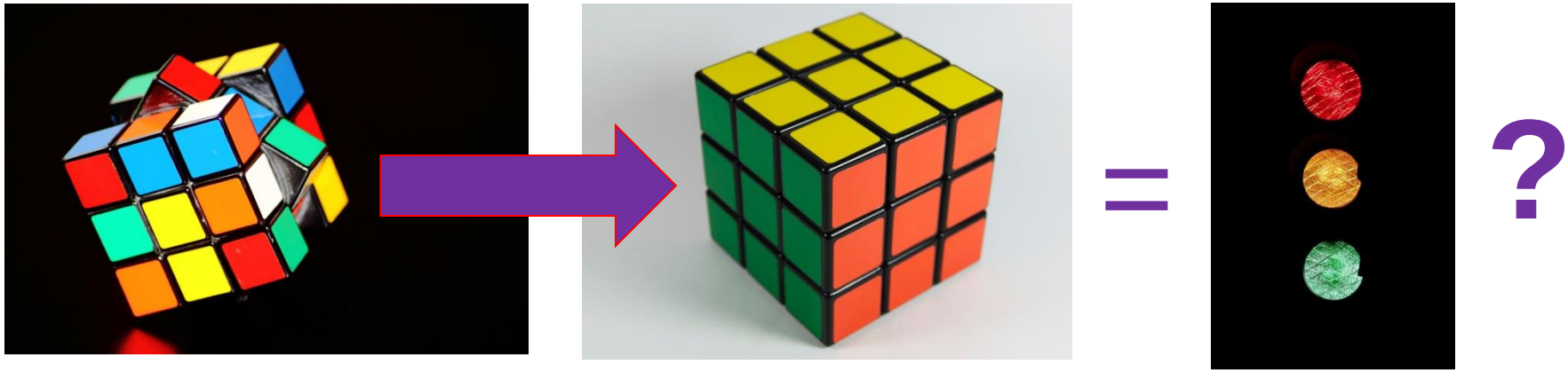
When management resolve issues before an internal audit report is published – how should this affect the rating?



Resolved issues – impact on rating

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Stephen's top tips:

- Ensure design of rating scales clear
- Ensure approach clear in IA methodology
- Focus on the purpose of ratings
- Consider motivational effect of ratings
- Never lose sight of your mission
- Remember you are on the same team
- Always give credit for management action
- Make effective use of executive summary

Topic 4

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Periodic reporting to the board and the top management.

Periodic reporting

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1111 – Direct Interaction with the Board

The chief audit executive must communicate and interact directly with the board.

IIA Standards – January 2017

Periodic reporting

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1110 – Organizational Independence

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

IIA Standards – January 2017

Standard 1110 - interpretation

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Organizational independence is effectively achieved when the chief audit executive reports functionally to the board. Examples of functional reporting to the board involve the board [inter alia]:

- Approving the risk-based internal audit plan.
- Approving the internal audit budget and resource plan.
- Receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters.

IIA Standards – January 2017

Periodic reporting – Standard 2060

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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
- performance relative to its plan
- conformance with the Code of Ethics and the *Standards.*

Periodic reporting – Standard 2060

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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.*

Periodic reporting – Standard 2060

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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.

IIA Standards – January 2017

Standard 2060 - Interpretation

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*The **frequency and content** of reporting are determined collaboratively by the chief audit executive, senior management, and the board.*

*The **frequency and content** of reporting depends on the importance of the information to be communicated and the urgency of the related actions to be taken by senior management and/or the board.*

(cont)

Standard 2060 - Interpretation

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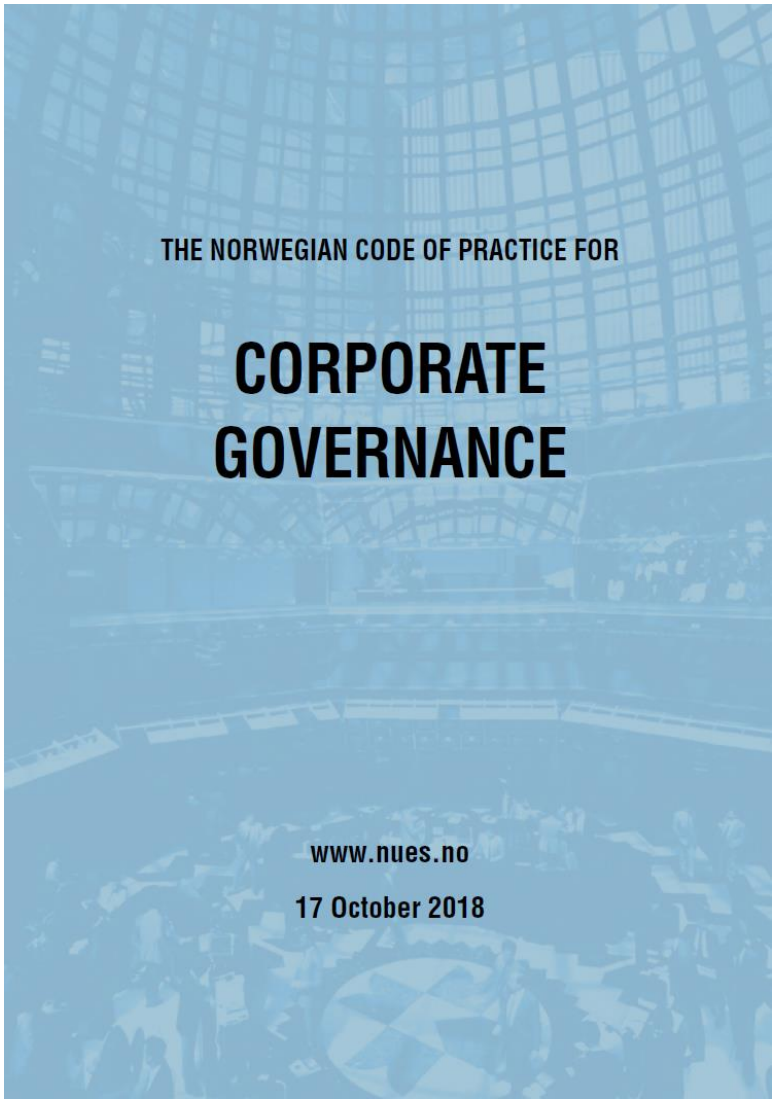
CAE reporting to SM and board must include:

- *The audit charter.*
- *Independence of the internal audit activity.*
- *The audit plan and progress against the plan.*
- *Resource requirements.*
- *Results of audit activities.*
- *Conformance with the Code of Ethics and the Standards, and action plans to address any significant conformance issues.*
- *Management's response to risk that, in the chief audit executive's judgment, may be unacceptable to the organization.*



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Norwegian Corporate Governance

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10. Risikostyring og intern kontroll

Styret skal påse at selskapet har god intern kontroll og hensiktsmessige systemer for risikostyring i forhold til omfanget og arten av selskapets virksomhet.

Norwegian Corporate Governance

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Internkontrollen og systemene bør også omfatte selskapets retningslinjer mv. for hvordan det integrerer hensyn til omverdenen i verdiskapingen.

Norwegian Corporate Governance

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Styret bør årlig foreta en gjennomgang av selskapets viktigste risikoområder og den interne kontroll.

Periodic reporting

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Annual Report – structure

- Internal Audit role and functioning
- Internal Audit activities – planned and completed
- Results of internal audit activities
- Internal Audit performance

Periodic reporting

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Annual Report – contents

Internal Audit role and functioning:

- Charter: mandate and responsibilities
- Independence: organisational + free from interference
- Conformance with the Code of Ethics and Standards

Periodic reporting

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Annual Report – contents

Internal Audit activities – planned and completed

- Internal Audit plan: assurance / consulting / other
- Items removed from plan
- Items added to plan
- Status of assignments
- Actual resources v planned resources for each element

Periodic reporting

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Annual Report – contents

Results of internal audit activities

- Summary of results
- Detail of significant issues
- Results of follow-up
- Overall Opinion

Periodic reporting

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Annual Report – contents

Internal Audit performance

- KPI's: targets and results
- Quality assurance and improvement program
  - Activities (reviews)
  - Results
  - Actions to improve

Periodic reporting

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Interim reporting – primary focus:

- Plan completion (progress)
- Changes to plan
- Summary of results
- Detail of significant issues
- Results of follow-up
- QAIP results

Content and timing – consult with audience

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Graphics – examples

Summary assurance results

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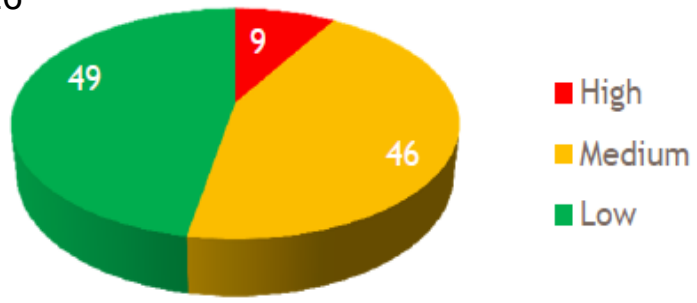
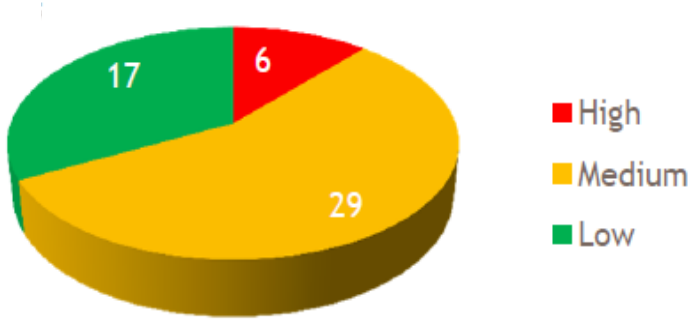
Recommendations raised and their significance:

2016



2017



Summary assurance results

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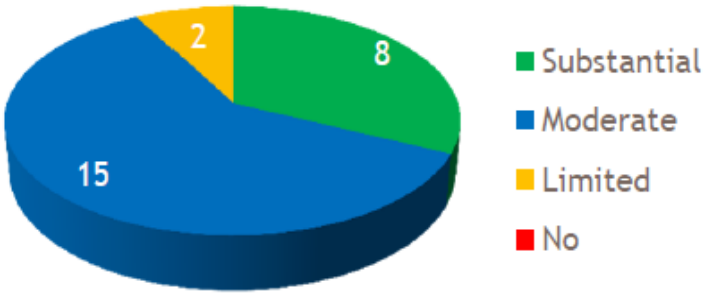
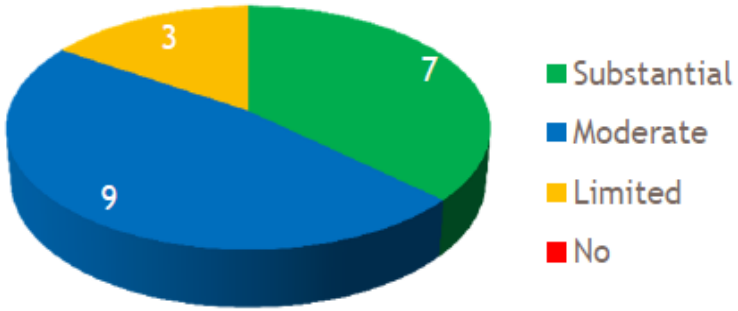
Assurance levels for assignments:

2016



2017



Follow-up statistics

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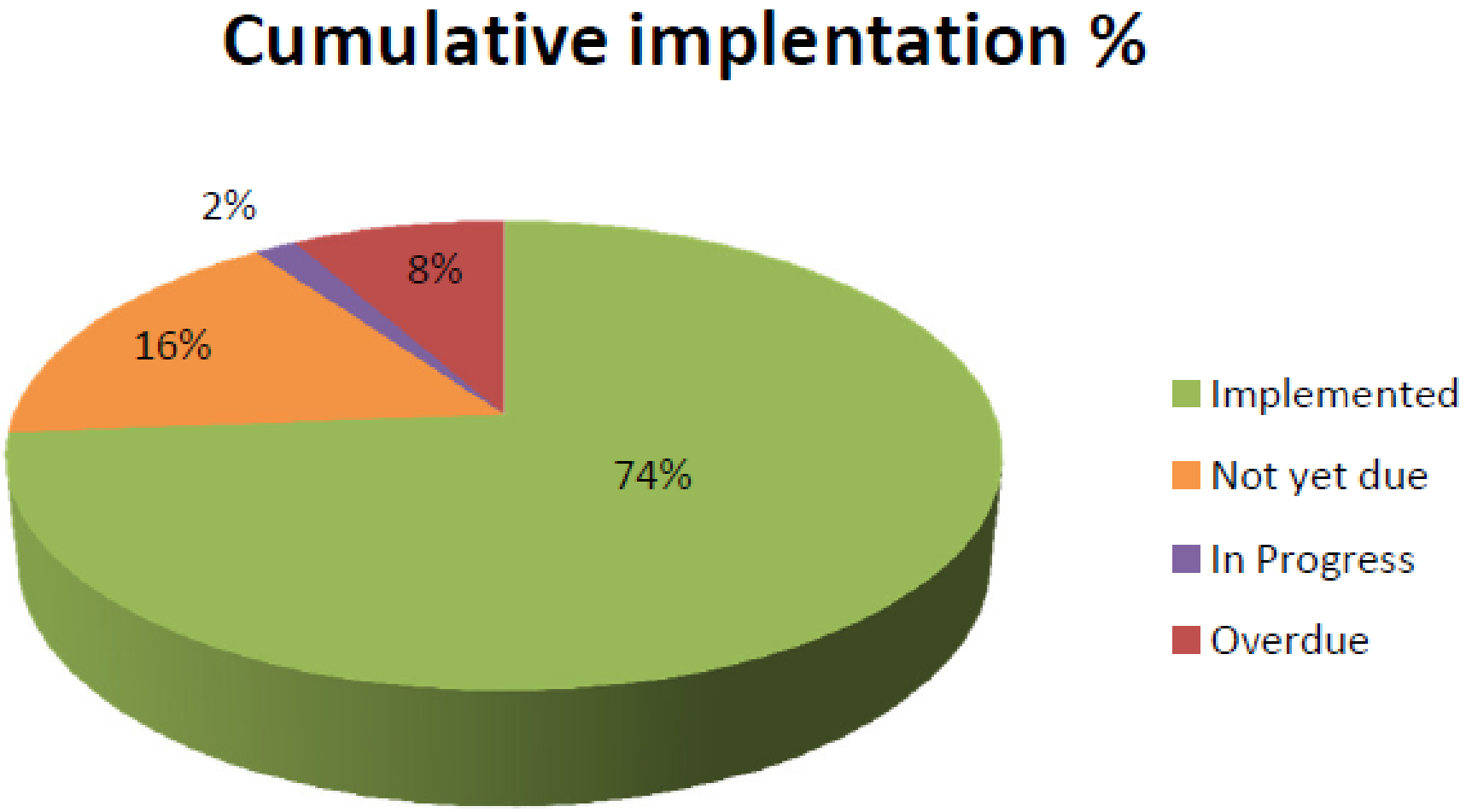

Follow-up statistics

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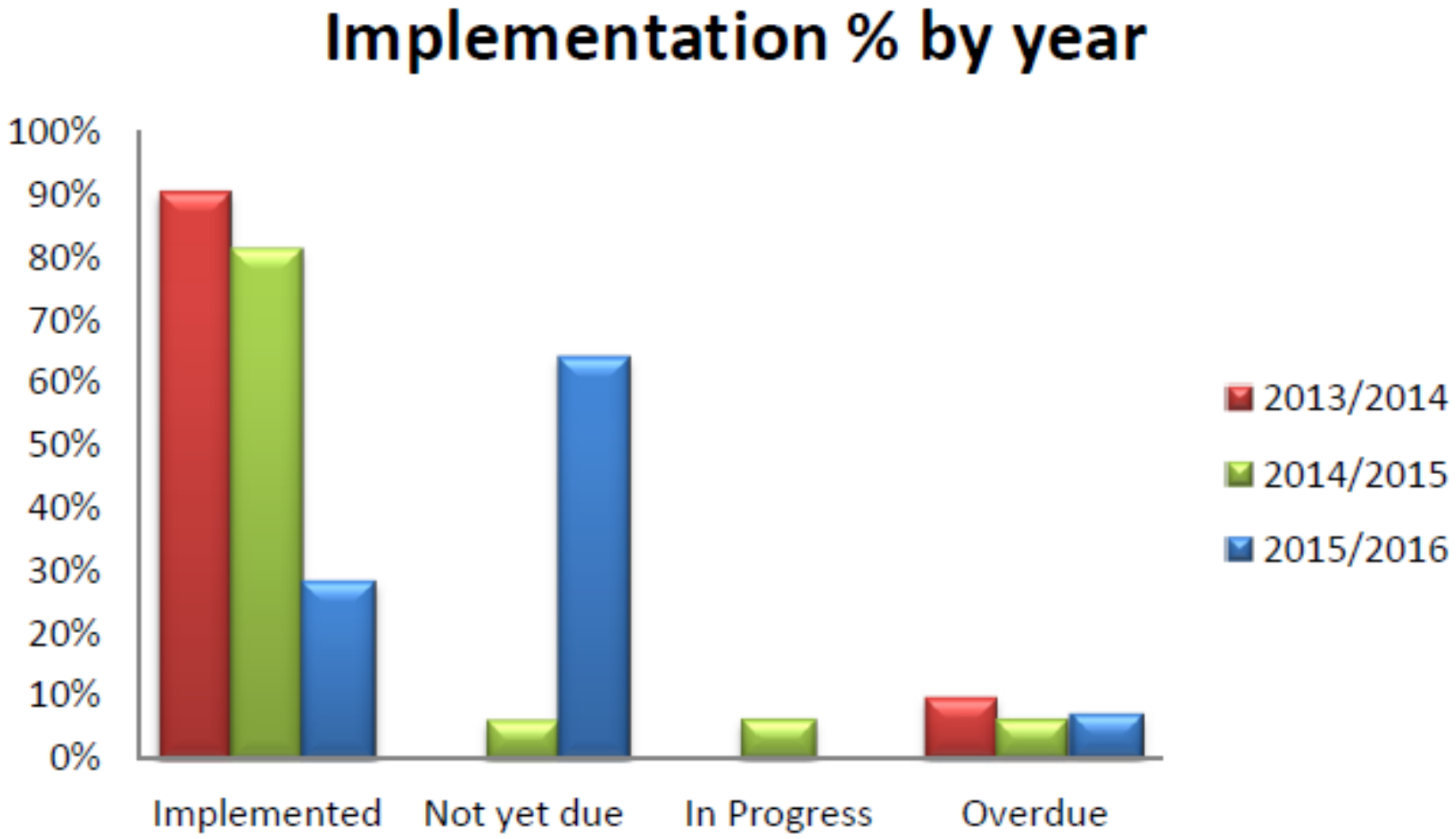

Follow-up statistics

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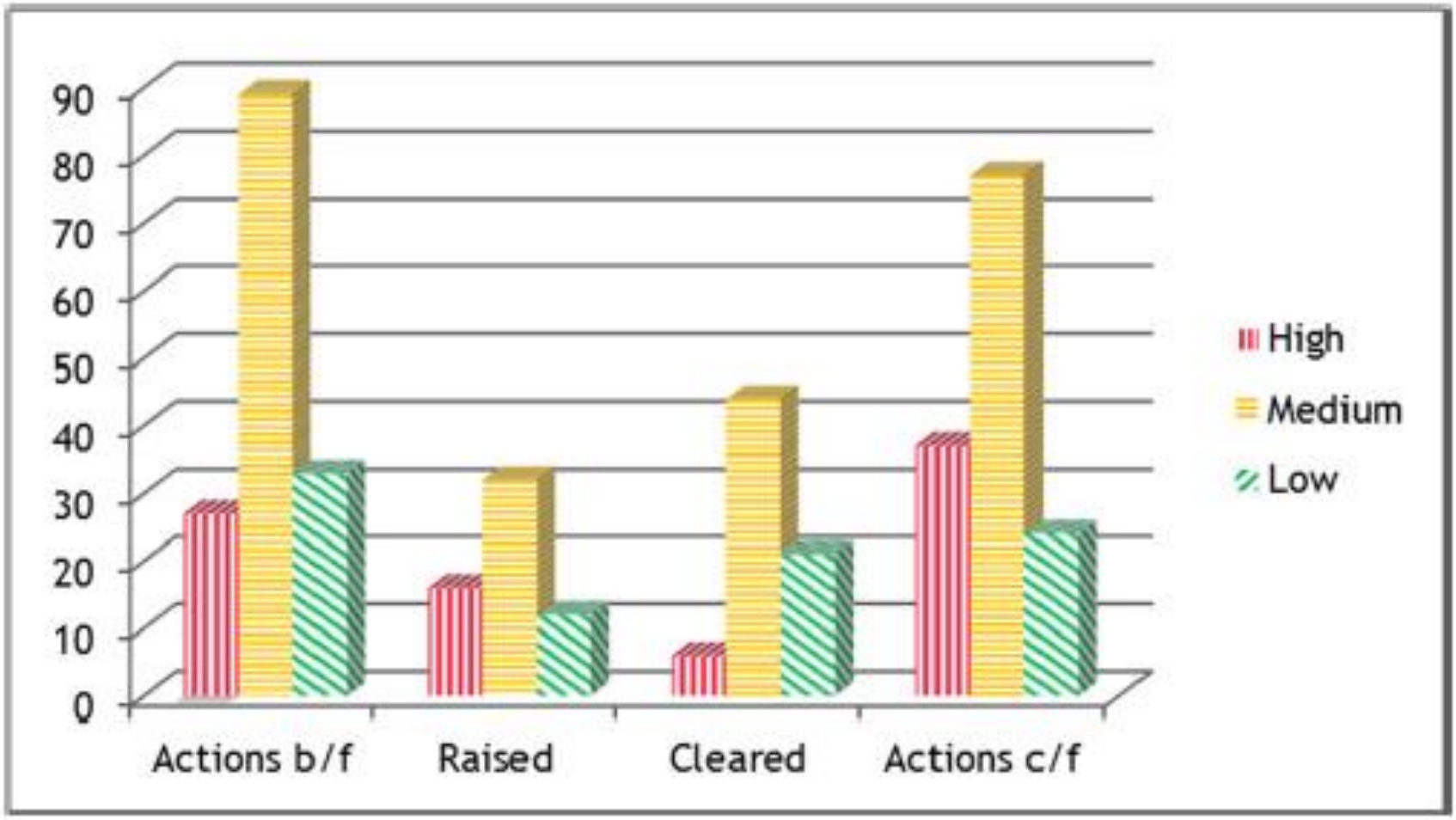

Periodic reporting

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Stephen's top tips:

- Ensure you comply with standards
- Ask the audience
- Use tables and graphics
- Research peers

Topic 5

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What are the most useful Key Performance Indicators for Internal Audit?

Assignment measures

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Assignment delivery:

- Number of recommendations made
- Person days: actual v budget
- Elapsed time: actual v planned
- Elapsed days between:
  - Fieldwork completion to draft report
  - Draft report to management response
  - Management response to final report

Assignment measures

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Auditee response

- Percentage of recommendations accepted
- Percentage of recommendations implemented on time
- Stakeholder satisfaction

Annual measures

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People

- Number of certified internal auditors on staff
- Years of experience in internal auditing
- Number of CPD hours earned

Annual measures

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Audit plan:

- Completed v planned audits
- Number of management requests

Annual measures

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Efficiency:

- Time: chargeable v non-chargeable hours
- Money: actual expenditure v budget

Annual measures

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IPPF:

- Conformance with Code of Ethics and Standards

Topic 5

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Key Performance Indicators for Internal Audit.

Exercise

Annual measures

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Skills retention:

- Staff turnover
- Staff leaving for internal v external roles

Annual measures

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Organisation benefits

- Savings (efficiency recommendations)
- Risk reduction

Annual measures

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Coverage:

- Functions / processes covered
- Risk coverage

Annual measures

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Use of technology

- % audits using data analytics
- Continuous auditing v one-off audits
- % audits using machine learning

Performance measures / indicators

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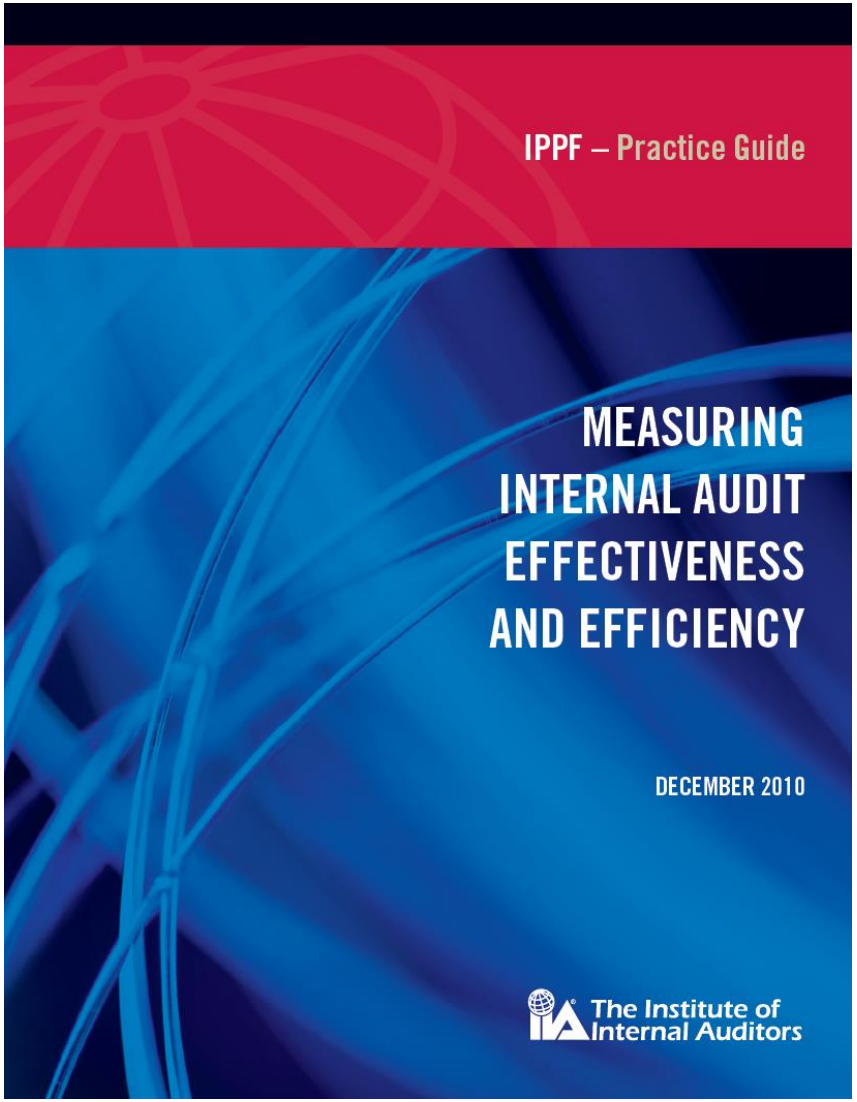
Types of performance measures / indicators:

- Measures v indicators
- Quantitative v qualitative
- Efficiency v effectiveness v ?
- Targets v management information

Differing needs amongst audience



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Performance measures / indicators

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Stephen's top tips:

Don't:

- Expect to find a holy grail
- Measure it just because you can
- Restrict yourself to quantitative data
- Have too many measures
- Let the measures be the whole story
- Be afraid of reporting bad performance

Performance measures / indicators

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Stephen's top tips:

Be clear on performance management objectives:

- Aligning internal audit with strategy
- Manage internal audit service delivery risks
- Demonstrate compliance with standards
- Improve / maintain stakeholder relationships
- Internal audit staff motivation and reward
- Support accountability of internal audit function
- Demonstrate the value of internal audit
- Drive continuous improvement in internal audit
- Maximise the positive effect on the organisation

Performance measures / indicators

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Stephen's top tips:

- Be clear on performance management objectives
- Focus on purpose and mandate
- Consider how stakeholders perceive value
- Consider how measures influence behaviours
- Select a broad set of balanced measures
- Remember what 'K' stands for
- Discuss proposals with Board / Audit Committee
- Monitor results on regular basis
- Use results to drive improvement
- Review and update (measures and targets)

Quantitative performance indicators

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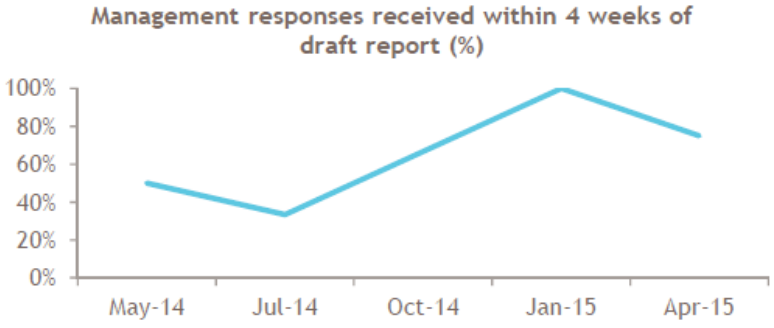
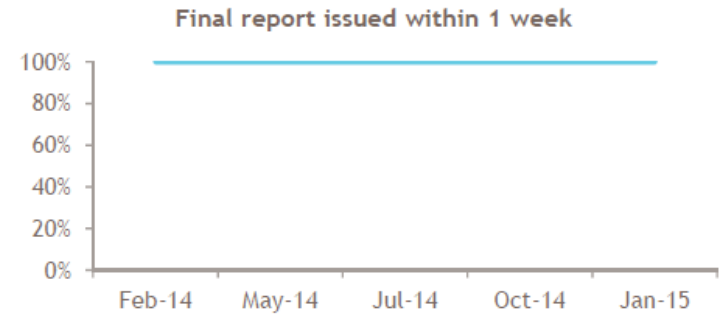
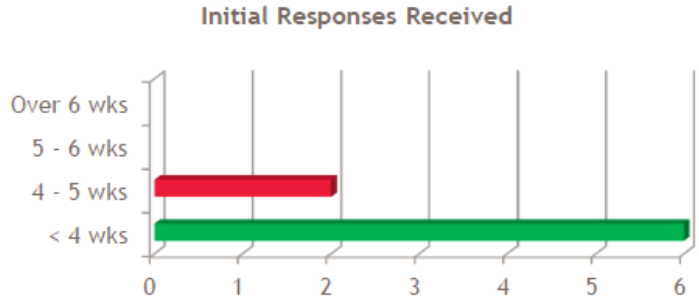


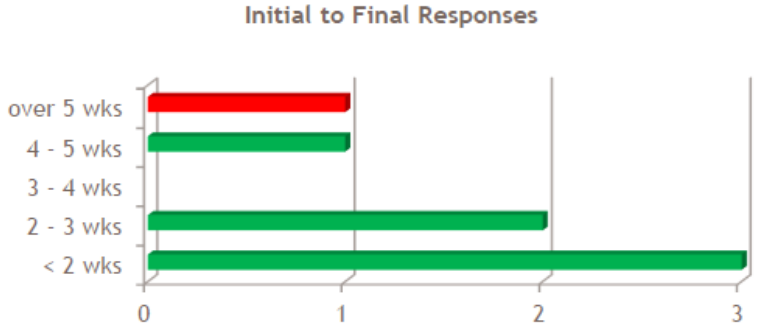
- Management responses received within four weeks in 75% of cases.



- All reports issued within one week.



- Responses for Health & Safety & Asset Management are three days after target date.



- Over 70% of reports signed off within 3 weeks of initial responses. Only one report took more than five weeks to finalise after receiving initial responses, being Network Control & Management.

Qualitative performance indicators

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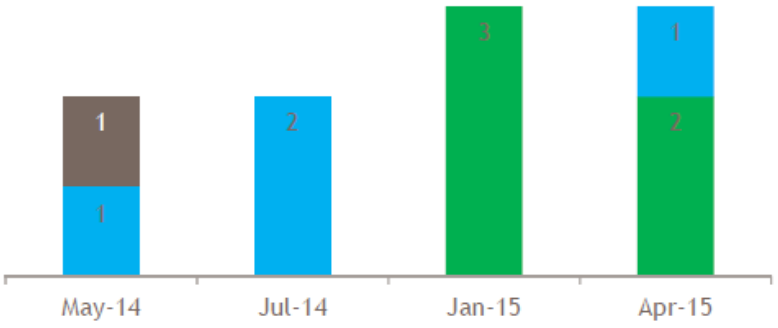
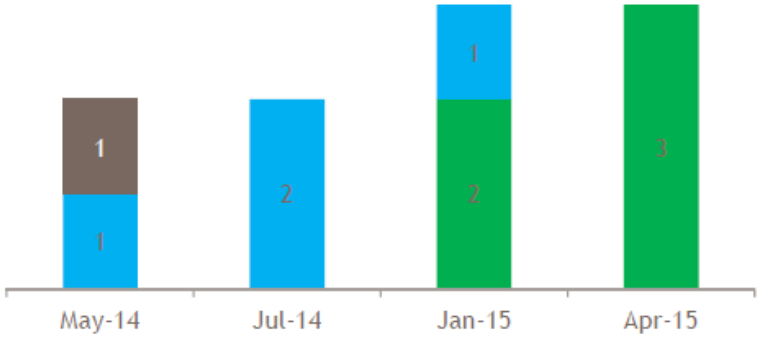
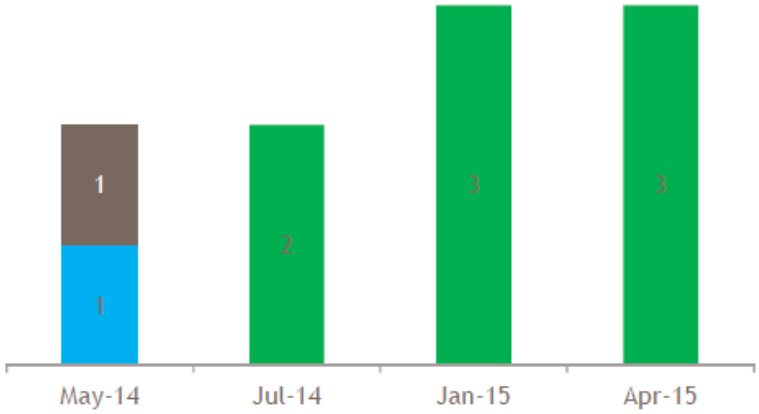
1. Internal audit understand the business and processes of the organisation.



2. Risks identified for each assignment were appropriate for the organisation and the area under review.



3. The staff undertaking the internal audit assignment asked informed, relevant questions to identify the controls against the risks already identified above within the audit area



Key

The bar graphs show the responses to each question with the colour of the bar reflecting the response received and the numbers representing the quantity of responses. The colours of the bars reflect the responses received as follows:

Very satisfied

Dissatisfied

Denotes where a question has not been answered.

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Chartered Institute of Internal Auditors

Communication with the board, top management and the auditee.

Chief Audit Executive Forum – Oslo 12 November 2018

Presented by:

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