

INTERNAL AUDIT – NEW DEVELOPMENTS & CHALLENGES BEFORE THE PROFESSION

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JB Nagar Study Circle Of WIRC
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Agenda

- History & Evolution of Internal Audit
- How IA changed over a period
- What place does Internal Audit have in Business today
 - *Around the World*
 - *In India*
- New Developments taking place
- Challenges Before the Profession
- Is IA geared to take on New Challenges



History & Evolution of Internal Audit*

- The history of Audit can be traced back to 4000 BC. Similar developments can be traced in China, Babylonia, Greece, the Roman Empire, the City States of Italy, etc., all of which developed a detailed system of checks and counterchecks.
- With the growth in size of business activities and complexity, a critical need for a separate internal assurance function that would verify the (accounting) information used for decision-making by management emerged.
- Management needed some means of evaluating not only the efficiency of work performed for the business but also the honesty of its employees.
- In due course, the internal audit function became responsible for “careful collection and interpretive reporting of selected business facts” to enable management to keep track of significant business developments, activities, and results from diverse and voluminous transactions

* Source- History Evolution of IA - The Institute of Internal Auditors Research Foundation -2003

History & Evolution of Internal Audit*

- Starting as an internal business function primarily focused on protection against payroll fraud, loss of cash, and other assets, internal audit’s scope was quickly extended to the verification of almost all financial transactions, and still later, gradually moved from an **“audit for management”** emphasis to an **“audit of management”** approach”(Reeve, 1986)
- In sum, the collective effect of growing transaction complexity and volume, the expertise required to review and summarize business activities in a meaningful way, need for organizational status to ensure independence and objectivity, as well as the procedural discipline necessary for being the **“eyes and ears”** of management all contributed to the creation of an internal audit department within business organizations

* Source- History Evolution of IA - The Institute of Internal Auditors Research Foundation -2003

Development of IA over the years

- Extension of external audit
- Internal check
- Probity Work
- Non financial systems
- Audit Committee

What do Internal Auditors Do

- Help solve problems
- Confirm accuracy of information
- Ensure assets are properly safeguarded
- Confirm compliance to laws & regulations
- Help improve the effectiveness and efficiency of processes
- Investigate fraud situations
- Provide a resource for skills

Source - www.iaa.org

Where are we now

- What *Image* do we have?
- What type of *Outputs* do we produce?
- What *Process* do we follow?
- What ability do we have to *control the future?*
- What *indicators* do we have of how we are doing?

Source – www.iaa.org

Institute of Internal Auditors (IIA) –the beginning of modern Internal Audit

- The IIA's rather humble origins – a small band of 24 charter members who held the inaugural IIA meeting in New York City on December 9, 1941 to around 185000 members world wide in 2017.
- It has metamorphosed having a worldwide expansion, continuing relevance, and increasing influence and recognition of The IIA and the internal auditing profession over the last 60 years constitutes remarkable growth and progress. Indeed, the internal auditing profession certainly appears poised for continued dynamic growth and promises to become “a profession for the 21st century.”
- IIA –CBOK – Largest Ongoing study of IA including Global Internal Audit Surveys
- IIA –IPPF® –International Professional Practices Framework (IPPF) ® - is the conceptual framework that organizes authoritative guidance promulgated by The IIA.
- IIA – Competency framework- is a tool that defines the competencies needed to meet the requirements of the International Professional Practices Framework (IPPF)® for the success of the internal audit profession.

How has IA changed

“Including Definition”

Old definition

Internal auditing is an **independent appraisal** activity within the organization **to check the accuracy and reliability** of the organization's record, promote **operational efficiency**, encourage **adherence** to policies, systems and procedures and to **safeguard the organization's assets**

New Definition

Internal auditing is an **independent, objective assurance and consulting** activity designed to **add value and improve** an organization's **operations**. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach **to evaluate and improve the effectiveness of risk management, control, and governance** processes

Source - IIA

How has IA Changed

Traditional Approach

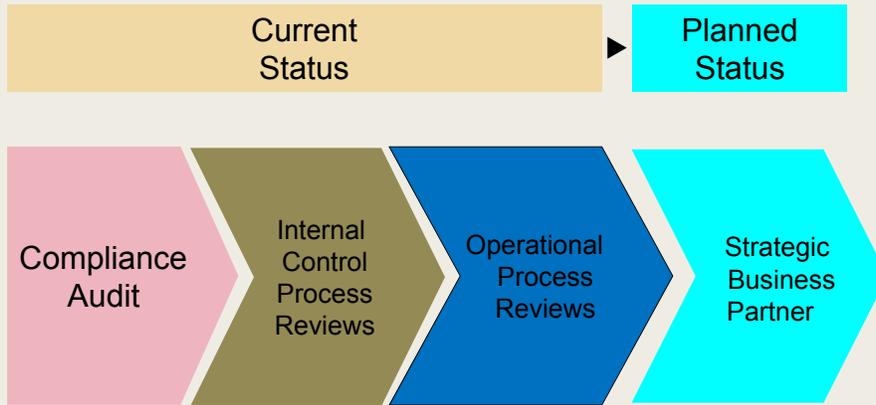
- Post Mortem
- Detection/Policing
- Silo Approach
- Financial
- Sample
- Periodical review
- Cyclical Audit Plans
- Manual
- Value Protector



Current (Modern) Approach

- Risk Focused
- Prevention
- Integrated
- Financial & Operational
- Complete Data & Process Driven
- Continuous
- Risk Based Audit Plans
- Technology driven
- Value Enhancer

Changing Status of IA



How IA changed – Global Perspective



Clause 49 & Companies Act
2013



How IA changed – Global Perspective

- Aftermath of Scams, Frauds etc led to SOX framework to be adopted in US
- A set of new regulations across the globe similar to SOX including Clause 49 in India
- COSO framework has been adopted as Internal Control Framework by most of the US companies.
- Focus on Risk & its management
- Audit Committees started taking active interest in audit findings
- From periodical to continuous audit
- Technological improvements in audit delivery
- Reporting of IA to Audit Committee

How has IA Changed – India Perspective

- Was a part of CARO, specific reporting on whether IA is commensurate with size of business
- Independent Directors in Audit Committee since enactment of Clause 49
- New Companies Act 2013- Special mention of IA u/s 138 read with Rule 13
- Concept of ICFR introduced u/s 134
- Regulators making IA mandatory inhouse in BFSI (Can be contracted/cosourced)
- Use of Data analytics has increased

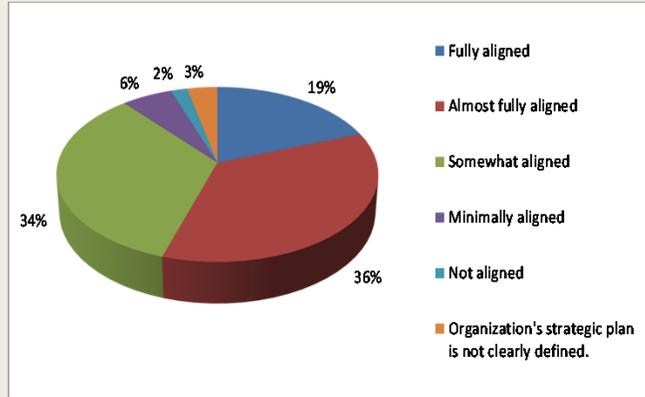
Where is IA in Business today

Serving more than one Master



✓ Is IA almost fully aligned with the strategic plan of the organization

Figure 1-1: Alignment of the Internal Audit Department with the Strategic Plan of the Organization



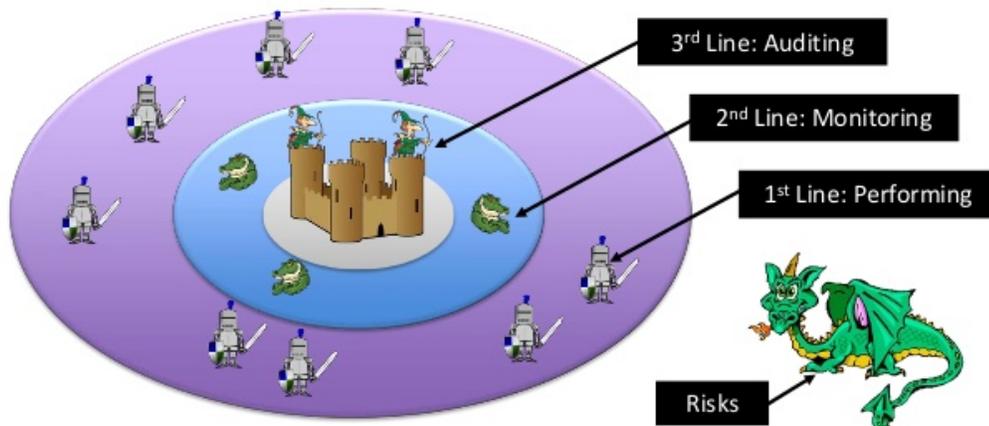
Source: IIA RF - CBOK Study

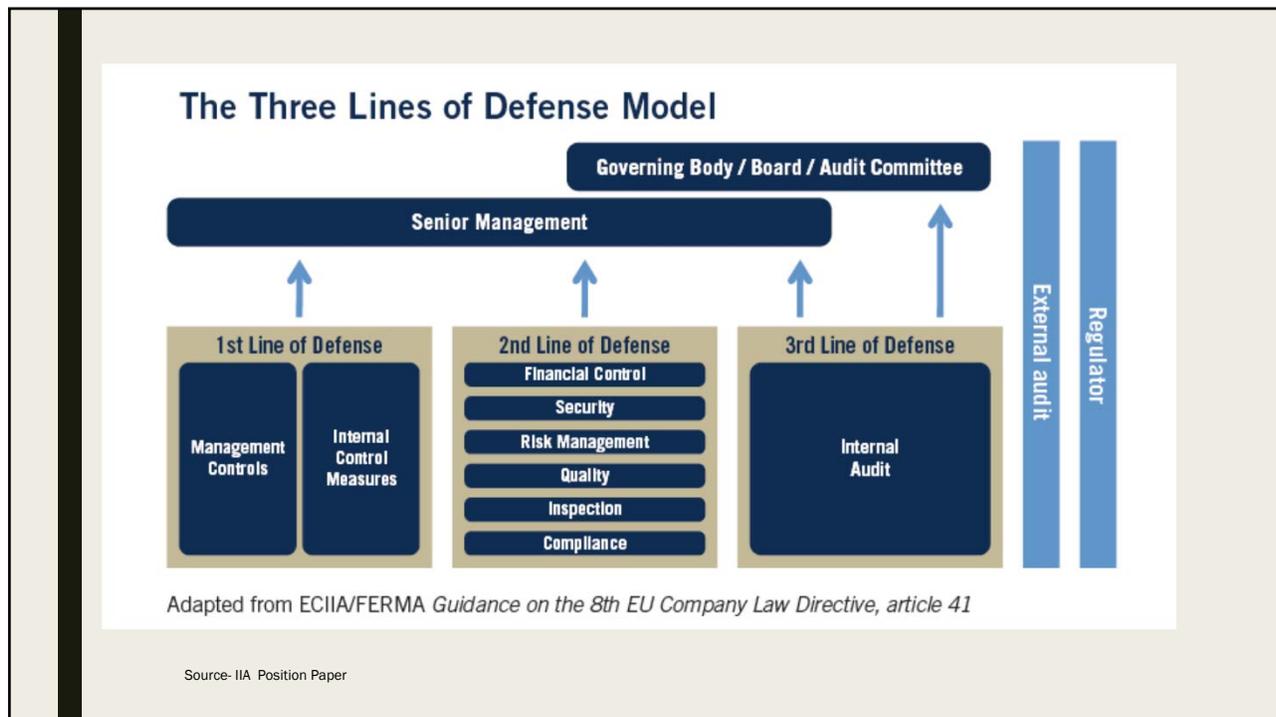
Where is IA in Business today

■ Expectations of Stakeholders

- *Understanding Businesses*
- *Need for a business partner*
- *Continuous Assurance*
- *Help in review of Business Strategy*
- *Help Organisation stay ahead of the curve*
- *Move from Value protection to Value Enhancement*

The Three Lines of Defense





Future Internal Auditor-^{*}

An Internal Audit Department is mature if it has the following attributes:

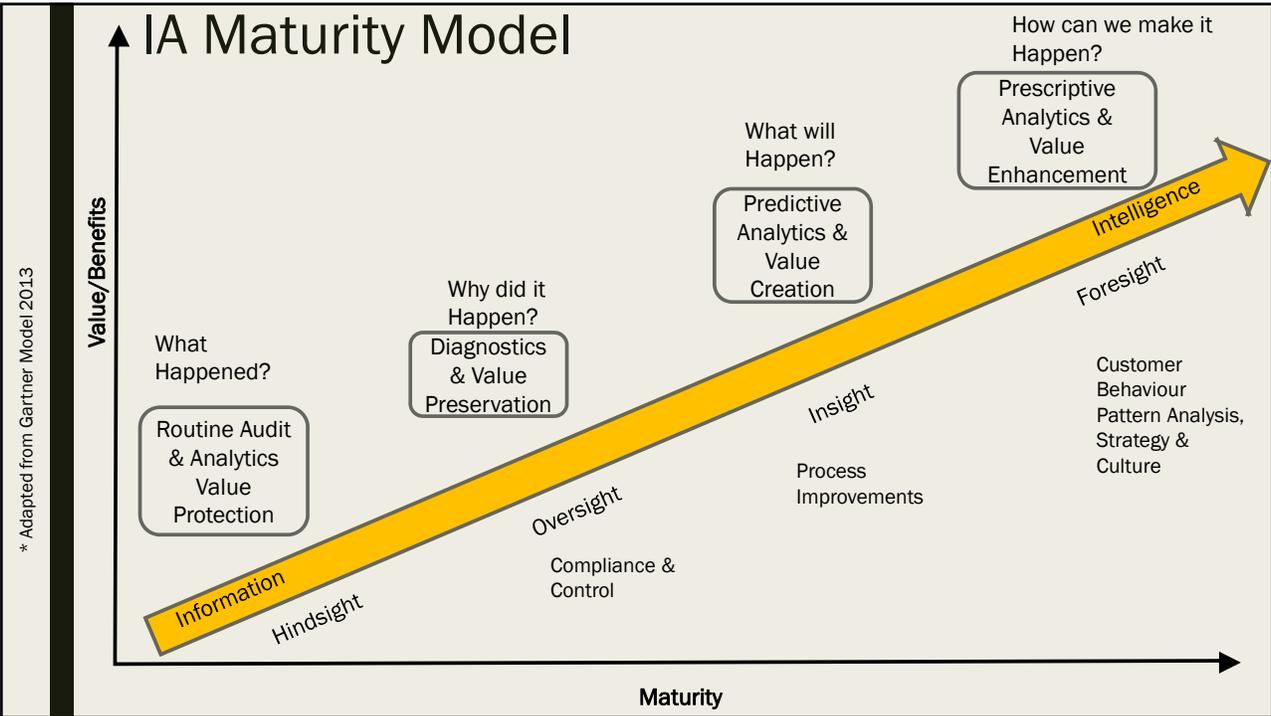
- Is almost fully aligned with the strategic plan of the organization
- Demonstrates agility and flexibility to adapt the internal audit planning to changes in the strategic objectives
- Relies on a holistic risk assessment
- Has an internal audit staff with mixed skills and industry knowledge
- Provides structured, documented, and diversified training programs for the staff

^{*}
Source – IIA CBOK Maturity Benchmarking Study

Future Internal Auditor- *

- Documents and continuously monitors audit procedures
- Makes the internal audit strategy explicit and translates the strategy into key performance indicators (KPIs)
- Uses leading technology across the entire audit process
- Has a Quality Assurance and Improvement Program (QAIP)

* Source - IIA CBOK Maturity Benchmarking Study



Current Standing of Internal Audit in India -

- Limited spread of internal audit
- Promoter driven small, medium size companies not keen, look at it as extra cost.
- Majority of them focus only on financial records and most of them get this done to avoid a auditors remark in the Balance Sheet
- Companies are at different internal audit maturity levels.
- Scope is not well defined
- Internal audit is evolving with new IT tools (ACL,IDEA etc)
- Internal Audit now also looks at Technical Stuff like Production efficiency, BOM configuration, Product assessments, Technology etc

Current Standing of Internal Audit in India

- It needs collaborations of various professionals since we as CA's do not have these technical skill sets
- Companies Act 2013 has also broadened the scope of Internal audit as well
- Now Auditor also has to mention on “effectiveness of controls”
- Who can be an internal auditor- Act does not specify it states “CA/CWA or any other professional”.
- Further, the Act/Rules do not define “any other professional”
- So lot of potential for work *but competition from “others” as well.*

Questions to be Answered – Is Audit having the relevant standing in the organisation

■ Audit Principles

– Internal Audit

- Independence ?
- Resources ?
- Risk focused ?
- Qualitative Adequacy ?



Questions to be Answered - Is there justice to IA

■ Board of Directors and Top Management

- *Fees/Commission – Are they paid effectively ?*
- *Audit Committee Time – Do they allot sufficient time ?*
- *Independent Members of the Board – Are they Really Independent ?*
- *Corporate Governance – Is it actually happening?*

New Developments

- Business Model Disruptions on the rise
- Increase in Digital footprint of business
- Understanding Automation & Analytics
- Integrated Assurance
- Business Culture Audits
- Cyber Audits
- Business Strategy Audits

KPMG Global Audit Committee Survey -2017



Necessary Investments for a Successful Internal Audit

- Human Resources
- Knowledge
- Technology
- Methodology
- Communications

Key Challenges for Internal Audit

- Audit “all business risks”
- Report on effectiveness of Business Process
- Understanding Business Risks and their Mitigation
- Understanding continually changing legislations
- Keep a Tab of Fraud metrics in the organisation
- Understanding Technology
- How to create value and enhance value for organisations
- Analysing Big Data
- Continuous Audit

Challenges for the Profession

- Recognising there is a paradigm shift
- Understand nature of the shift
- Taking the lead
- Be proactive
- Upgrading ourselves
- Upgrading our teams

Challenges for the Profession

- Harnessing Technology
- Educate/Understand the Board
- Emphasis on assurance
- Focus on key risks
- Improve Communication

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Thank You

