

Tutorial Letter 202/2/2018

The Internal Audit Process: Managing the Internal Audit Activity

AUI3704

Semester 2

Department of Auditing

IMPORTANT INFORMATION:

SUGGESTED SOLUTION TO ASSIGNMENT 02 OF 2018 FOR THE SECOND SEMESTER.

BARCODE

SUGGESTED SOLUTION TO COMPULSORY ASSIGNMENT 02 OF 2018

This tutorial letter provides feedback on compulsory Assignment 02. You need to study the contents of this tutorial letter carefully because it will provide you with valuable insight and assist you with your examination preparation. The study references are provided to assist you. Therefore, please refer to them to obtain a better understanding of the suggested solution.

QUESTION 1

30 marks

The chief audit executive's responsibility regarding the following:

1.1 Planning of the internal audit activity

References: Performance Standards 2010 & 2020
Practice advisories 2010-1, 2010-2 and 2020-1

This Standard dictates that the CAE (1) should establish risk-based plans (1) to determine the priorities of the internal audit activity, consistent with the organisation's goals. (1)

The suggested practice, where the need of audit projects (1) arises from the need of management at the regional offices, is unacceptable. (1)

The internal audit activity's plan of engagement should be based on a risk assessment (1) undertaken at least annually. (1) The input of senior management and the board must be considered in this process. This is the time when managers can make special requests (1) (P.S. 2010. A1).

The audit plan can also include consulting projects, if agreed upon; depending on whether there is potential for the work to ...

- improve management of risks (1)
- add value, or (1)
- improve the organisation's operations (1)

These internal audit plans and resource requirements, (1 including significant interim changes (1), should be communicated to senior management and the board for review and approval (1).
(Marks as indicated – maximum of 13 marks)

1.2 Resource management

References: Performance Standards 2030 & 2230
Practice Advisory 2030-1

The chief audit executive (1) and not the chief operating officer (1) must ensure that internal audit resources are appropriate, sufficient and effectively deployed to achieve the approved plan. (1)

The two internal auditors would probably not have the skills required to conduct the audit expected of them. (1)

The internal audit staff all has different skills, knowledge and competencies (1). Internal auditors must determine appropriate and sufficient resources to achieve the engagement objectives (1) based on an evaluation of the nature and complexity of each engagement, (1) time constraints

and available resources. (1)

The training needs of internal auditors should be considered because each engagement serves as a basis for meeting the developmental needs of the internal audit activity. (2)

Consideration should be given to the use of external resources in instances where additional knowledge, skills and other competencies are needed. (2).

(Marks as indicated – maximum of 11 marks)

1.3 Communication of engagement results

Reference: Performance Standards 2400 and 2410
Practice Advisory 2410-1

According to the scenario, only copies of the reports after they have been issued must be given to the CAE. (1) This can lead to non-compliance with the Standards because the CAE is responsible for the reports issued by his or her department. These reports must therefore be authorised by him or her before they are sent out (1½).

Internal auditors must communicate (1½) the engagement results promptly and include the engagement's objectives, scope and applicable conclusions (1½), recommendations (1½) and action plans. Where appropriate, the overall opinion should be expressed.

Although the CAE is ultimately responsible during supervision to ensure that communications are accurate, objective, clear, concise, constructive and timely (1½), audit reports can be provided by internal auditors, but the CAE is responsible for communicating the final results to parties who can ensure that the results will be given due consideration (1½).

(Marks as indicated – maximum of 6 marks)

QUESTION 2

30 Marks

2.1 Indicate whether the CAE may outsource the auditing of the human resources recruitment process to an external service provider, providing full reasons for your answer in terms of the Standards and the Practice advisories

Reference: Standards 1200, 1210, 1220
Practice Advisory 1210.A1-1

The CAE can outsource the audit if she complies with the Standards as follows: (1)

1. Standard 1200 states: Engagements must be performed with proficiency (1) and due professional care. (1)
2. Standard 1210.A1 states: The CAE must obtain competent advice and assistance if the internal auditors lack the knowledge, skills (1) or other competencies needed to perform all or part of the engagement. (1)
3. Practice Advisory 1210.A1-1 states: Each member of the internal audit activity needs not be qualified in all disciplines. (1) The internal audit activity may use external service providers or internal resources that are qualified in disciplines (1) such as accounting, auditing, economics, finance, statistics, information technology, engineering, taxation, law, environmental affairs, and other areas as needed to meet the internal audit activity's

responsibilities. (1)

4. Practice Advisory 1210.A1-1 states: An external service provider may be engaged by the board, senior management, or the chief audit executive (CAE). (1)
5. The supervisor should still maintain control/supervision over the quality of the work. (1)
(Marks as indicated. Maximum of 7 marks)

2.2 Evaluate, giving reasons, whether the CAE should accept the request to develop policies and procedures for the computer control environment. Base your answer on the IPPF and the information provided in this paper regarding All Yours Limited

References: Standards 1130, 1130.A2
Practice Advisory 1130.A2-1

1. It is stated that the board of All Yours Limited regards sound corporate governance as important. Therefore, the CAE **should not accept** (1) the responsibility for developing the policies and procedures for the computer control environment, because of the impact it can have on her independence and objectivity. (3)
2. At a minimum, the following factors need to be considered in assessing the impact on independence and objectivity:
 - Requirements of the code of ethics and the Standards – will she be responsible for auditing the policy and procedures within the next year? (2)
 - Allowances and/or restrictions contained in the internal audit charter – does it allow the CAE to take responsibility for management functions in the operational departments of All Yours Ltd? (2)
 - Disclosures required by the Standards – what must be disclosed and to who must the CAE disclose? (2)
 - Nature of the impairment – will this impair her independence and objectivity only or will it impair other principles? (2)
 - Length and duration of the assignment and scope of responsibility (1)
 - The CAE already had to outsource an assurance engagement on human resources. Does she or the department have the capacity to be involved in this project? (1)
 - Expectations of stakeholders – how will the audit committee react to the CAE rather being involved in drafting policies and procedures?) (1)(Marks as indicated. Maximum of 13 marks)

2.3 List the criteria according to which the CAE can assess whether the external service provider possesses the necessary knowledge, skills and other competencies, required to perform the audit of the human resources recruitment process, and explain how the CAE will go about doing this assessment in practice.

Criteria	Practical measures (how)
1. Professional certification or other recognition (1)	1. CIA designation (1)
2. Membership of the external service provider of professional bodies (1)	2. IIA membership/adherence to code of ethics (1)
3. Reputation of the external service	3. Contacting other clients of the external

Criteria	Practical measures (how)
provider (1)	service provider (1)
4. Experience of the external service provider in the specific type of engagement (1)	4. Inspecting list of previous engagements (1)
5. Extent of education and training received by the staff members of the external service provider (1)	5. Inspecting the qualifications of the staff members in the specific area of expertise required (1)
6. External service provider's knowledge and experience in the specific industry (1)	6. Inspecting the experience of the staff members in the specific industry of All Yours Ltd (1)

(Marks as indicated. Maximum of 10 marks)

(One mark per a valid point, maximum **30 marks**)

QUESTION 3

21 marks

3.1 Discuss eight (8) different ways in which you as the CAE can help to alleviate specific concerns that hinder the audit committee members in exercising their responsibilities.

1. Legal actions: They can supply the committee with copies of audit reports or summaries of those reports. These can convey to the committee the problems being encountered and the action taken to correct identified defects and weaknesses. This serves as a potent defence against accusations of not being informed. (2)
2. Information systems: To comply with their responsibility internal auditors review the reliability and integrity of financial and operating information and the means to gather such information. They can give thorough assurance about the information systems and report weaknesses. (2)
3. Standards of Conduct: Internal auditors are responsible for complying with standards of due professional care. They are required to be alert to the possibility of intentional wrong doing, errors, ineffectiveness, etc. and must inform the appropriate authority in any such instance. They can also report to the audit committee where formal conflicts of interest which are prohibited, exist. (2)
4. Capital items: Internal auditors review budgeted and actual expenditures as well as capital budgets. If the audit committee is concerned about specific capital expenditures or proposals, internal auditors can provide relevant information. (2)
5. Compliance: Internal auditors should review the systems established to ensure compliance with policies, plans, procedures, laws and regulations which could have a significant impact on operations and reports. They can provide information on non-compliance if necessary. (2)
6. Performance: Internal auditors should review the accomplishment of established objectives and goals. In performing this audit activity; evaluation of the CEO's performance will also be done. (2)

7. Organisational background: Internal auditors can provide clear statements of what the entity does and how well or poorly it does it for those directors who lack insight into the organisation's background. (2)
8. Anticipating the question: Internal auditors should be sensitive to the questions an audit committee is likely to ask, and to bring certain information to their attention, even before questions are asked. (2)

(Marks as indicated. Maximum 16 marks)

- 3.2 A brochure about the internal auditing activity can be sent to each auditee manager prior to the commencement of the audit, thereby removing the mystery of internal auditing (1) and pointing out the support they can receive from internal audit activities (1).

(Marks as indicated. Maximum 2 marks)

- 3.3 Audit committees exercise responsibility in the areas of *financial reporting*, (1) *corporate governance* (1) and *corporate control*. (1)

(Marks as indicated. Maximum 3 marks)

QUESTION 4

16 marks

Criticise the CAE's decision, specifically with regard to adherence to the requirement of the Internal Auditing Standards regarding engagement supervision

Reference: Performance Standard 2340; Practice Advisory 2340 - 1

Engagements **must** be properly supervised to ensure objectives are achieved, quality is assured, and staff developed. (2) The CAE has overall responsibility for supervising the engagement, whether performed by or for the internal audit activity, but may designate appropriately experienced members of the internal audit activity to perform the review. Appropriate evidence of supervision is documented and retained. Supervision is the process that begins with planning and continues throughout the engagement. (2)

- The CAE should have provided supervision to the internal auditor in order to ensure that the final output meets the required quality standard. This will also assist the CAE to identify areas for improvements for the internal auditor. (2)
- The CAE should provide appropriate instructions during the planning of the engagement and approving of the engagement program. The CAE referred the internal auditor to the permanent file. (2)
- The CAE should see that the approved engagement program is carried out or should approve changes. The CAE only phoned but did not review the working papers. (2)
- The engagement working papers should be reviewed to determine that they support the engagement observations, conclusions and recommendations. The CAE did not review the working papers. (2)
- Communication should be accurate, objective, clear, concise, constructive and timely. Although it seems that the audit was done in time allocated, the other points were not addressed. (2)
- The CAE has to ensure that engagement objectives are met. No evidence of this being done is present. (2)
- The CAE must use the review of working papers as an opportunity for developing staff members. (2)

(½ mark for critique and 1½ for motivation; maximum 16)

Conclusion

It is important to review the feedback contained in this tutorial letter and compare it with your own answers.

You are welcome to contact us should you have any queries.

We wish you every success in your studies.