Section I: Mandatory Guidance

This section is designed to help you:

- Identify and apply relevant ethical, practical, and legal standards to audit practice, including The IIA’s Code of Ethics, International Standards, and Practice Advisories, COSO, and relevant laws.
- Explain the International Professional Practices Framework categories of guidance.
- Define internal auditing.
- Describe compliance with The IIA’s Code of Ethics.
- Explain how the purpose, authority, and responsibility for an internal audit activity are documented, communicated, and approved.
- Understand the importance of securing the board’s approval of the internal audit activity charter and plan.
- Explain independence and objectivity and how to maintain both in an internal audit activity.
- Identify and describe the required knowledge, skills, and competencies for an internal audit activity and how an organization develops and/or procures them.
- Explain how to exercise due professional care in an internal audit activity.
- Describe the importance of professional development and formal certification for internal auditors.
- Describe elements of a quality assurance and improvement program.

The Certified Internal Auditor (CIA) exam questions based on content from this section make up approximately 35% to 45% of the total number of questions for Part 1. All topics are covered at the “P—Proficiency” level, meaning that you are responsible not only for comprehension and recall of information but also for higher-level mastery, including application, analysis, synthesis, and evaluation.

Section Introduction

The IIA’s International Professional Practices Framework

The Institute of Internal Auditors (The IIA) provides its members with an International Professional Practices Framework (IPPF) to guide their professional practice and ensure the highest-quality internal audit results in widely diverse environments.

In The IIA’s own words, “The purpose of the . . . IPPF is to organize The Institute of Internal Auditor’s . . . authoritative guidance in a manner that is readily accessible on a timely basis while strengthening the position of The
IIA as the standard-setting body for the internal audit profession globally.” Furthermore, by reflecting the evolution of current practice, the framework aims “to assist practitioners and stakeholders throughout the world in being responsive to the expanding market for high quality internal auditing.”

The IPPF consists of:
- The Definition of Internal Auditing.
- The Code of Ethics.
- The International Standards for the Professional Practice of Internal Auditing (the Standards).
- Practice Advisories (PAs).
- Practice Guides.
- Position Papers.

The Definition of Internal Auditing, the Code of Ethics, and the Standards are available to be read or downloaded from The IIA’s Web site (www.theiia.org), along with a great deal of other material relevant to internal auditors, whether or not they are IIA members. (Other materials available to the public for reading or downloading from the Web site include the monthly newsletter, ITAudit, and the continuously evolving Global Technology Audit Guide, both of which will be cited as authoritative sources in these study materials.) These materials enhance the knowledge and skills of internal auditors.

The Practice Advisories are intended for the use of IIA members and are password-protected. The full International Professional Practices Framework is available, however, in a printed version, known familiarly, and for reasons obvious to those who have seen it, as the “Red Book.” It can be ordered online. While the book includes all aspects of the framework—the Definition of Internal Auditing, the Code of Ethics, the Standards, and the Practice Advisories—it is not necessarily as up-to-date as the online version, which is subject to continuous review, revision, and addition. Internal auditors should be sure they are familiar with the most current version of the framework available at The IIA’s Web site. As the auditing environment evolves so will the Practice Advisories and, at a more deliberate pace, the Standards. For example, changes to the Standards effective January 1, 2013, included new language highlighting the importance of evaluating the achievement of the organization’s strategic objectives and reflecting the profession’s continued orientation toward evaluation of governance and risk management (in addition to controls) for some standards that did not yet have this language.
New topics will emerge, as, for example, the 2011 Edition of the IPPF (updated for 2012) added 2010.A2, “The internal audit activity’s plan of engagement must be based on a documented risk assessment undertaken at least annually. The input of senior management and the board must be considered in this process.” Finally, some standards will be deleted, as were 2130.A2 and 2130.A3 in the aforementioned edition. Note that this learning system is consistent with the revision of the Standards effective January 1, 2013, which can be viewed at global.theiia.org/standards-guidance/mandatory-guidance/Standards.aspx.

The IPPF is the “conceptual framework that organizes the authoritative guidance promulgated by The IIA.” Authoritative guidance comprises two categories: (1) mandatory and (2) endorsed and strongly recommended.

The Definition of Internal Auditing, the Code of Ethics, and the Standards make up the core of the IPPF, and abiding by them is mandatory for IIA members, practicing internal audit professionals, and Certified Internal Auditors. Mandatory guidance is denoted within the Standards by the use of the terms “must” and “should.” The IPPF Standards Glossary defines these words in the following manner:

- The word must specifies an unconditional requirement.
- The word should is used where conformance is expected unless, when applying professional judgment, circumstances justify deviation.

The introduction to the Standards goes on to clarify what is meant by mandatory guidance: “The Standards apply to individual internal auditors and internal audit activities. All internal auditors are accountable for conforming with the Standards related to individual objectivity, proficiency, and due professional care. In addition, internal auditors are accountable for conforming with the Standards, which are relevant to the performance of their job responsibilities. Chief audit executives are accountable for overall conformance with the Standards.”

(Note: Adherence to the Standards is required even for those who are not IIA members or CIAs if the statement “conformance with the standards” is used in their work.)

The framework also includes strongly recommended forms of guidance that support the core. Each standard, for example, is generally supported by one or more Practice Advisories. There are also links, in some cases, to the growing
collection of Practice Guides and Position Papers. The Practice Advisories, Practice Guides, and Position Papers—unlike the Standards, the Code of Ethics, and the Definition of Internal Auditing—are optional, not mandatory. Practice Advisories and Practice Guides are The IIA’s version of “best practices.” Position Papers are IIA statements to assist a wide range of interested parties.

These strongly recommended forms of guidance are endorsed by The IIA and were developed using due process by an IIA international technical committee and/or institute. Rather than providing definitive answers, strongly recommended guidance is intended as a guide containing a wide range of possible solutions and methods of implementing the mandatory guidance.

The IIA’s Definition of Internal Auditing is covered in Chapter A, Topic 1, of this section. It is also posted on The IIA’s Web site. The Code of Ethics is discussed in detail in Chapter B, Topic 1. An introductory overview of the remaining parts of the framework—Standards, Practice Advisories, Practice Guides, and Position Papers—follows, along with a brief mention of some related supporting endeavors.

**Standards**

The Standards are principles-based mandatory guidance rather than a detailed set of rules and regulations. Some Standards include “interpretation” text to further explain the guidance description. This italicized text should not be overlooked, as it is part of the standard.

The purpose of the Standards can be broken down as follows:

- Delineate basic principles that represent the practice of internal auditing.
- Provide a framework for performing and promoting a broad range of value-added internal auditing.
- Establish the basis for the evaluation of internal audit performance.
- Foster improved organizational processes and operations.

The Standards employ terms that have been given specific meanings. The IPPF “Red Book” contains a brief Standards Glossary. Whenever these terms are defined in this learning system, they are identified as being from the Standards Glossary.

There are three types of Standards: Attribute Standards, Performance Standards, and Implementation Standards.
Attribute Standards
The Attribute Standards address the characteristics of organizations and parties performing internal audit activities. Attribute Standards apply to all internal audit services and internal auditors individually.

Attribute Standards are numbered in the 1000s range. The major sections of Attribute Standards are as follows:

- **1000—“Purpose, Authority, and Responsibility”**
- **1100—“Independence and Objectivity”**
- **1200—“Proficiency and Due Professional Care”**
- **1300—“Quality Assurance and Improvement Program”**

The following are examples of two of these Attribute Standards.

- **Attribute Standard 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 Definition of Internal Auditing, the Code of Ethics, and the Standards. The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.

- **Attribute Standard 1100—“Independence and Objectivity.”** The internal audit activity must be independent, and internal auditors must be objective in performing their work.

Each of the sections of Attribute Standards can have multiple subsections. For example, Standard 1100’s subsections (1110, 1120, etc.) all deal with some aspect of independence and objectivity. Similarly, Standard 1300 on quality assurance and improvement contains a subsection 1310, “Requirements of a Quality Assurance and Improvement Program,” which in turn contains two subsections, 1311, “Internal Assessments,” and 1312, “External Assessments.” The numbering system leaves room for additions in the future, indicating that this document will continue to evolve.

Performance Standards
Performance Standards describe the nature of internal auditing and provide quality criteria for evaluating audit performance. Similar to Attribute Standards,
Performance Standards apply to all internal audit services as well as internal auditors.

Performance Standards are numbered in the 2000s range. The major sections of the Performance Standards are as follows:

- **Performance Standard 2000**—“Managing the Internal Audit Activity.” The chief audit executive must effectively manage the internal audit activity to ensure that it adds value to the organization.

- **Performance Standard 2100**—“Nature of Work.” The internal audit activity must evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic and disciplined approach.

As you can see, the Performance Standards at this highest level address topics of general applicability; from 2200 through 2500, they trace the course of the well-constructed audit. Performance Standards also have more detailed subsections and are added to as the framework evolves over time.

**Implementation Standards**

Implementation Standards expand upon Attribute and Performance Standards and provide separate mandatory instructions for implementing the Attribute and Performance Standards depending on whether the engagement is to be for assurance (A) or consulting (C). The Standards Glossary defines an engagement as “a specific internal audit assignment, task, or review activity, such as an internal audit, control self-assessment review, fraud examination,
or consultancy.” The two types of audit engagements are described in the Introduction to the Standards as follows:

**Assurance**
Assurance services involve the internal auditor’s objective assessment of evidence to provide an independent opinion or conclusions regarding an entity, operation, function, process, system, or other subject matter. The nature and scope of the assurance engagement are determined by the internal auditor. There are generally three parties involved in assurance services: (1) the person or group directly involved with the entity, operation, function, process, system, or other subject matter—the process owner; (2) the person or group making the assessment—the internal auditor; and (3) the person or group using the assessment—the user.

**Consulting**
Consulting services are advisory in nature, and are generally performed at the specific request of an engagement client. The nature and scope of the consulting engagement are subject to agreement with the engagement client. Consulting services generally involve two parties: (1) the person or group offering the advice—the internal auditor; and (2) the person or group seeking and receiving the advice—the engagement client. When performing consulting services the internal auditor should maintain objectivity and not assume management responsibility.

Assurance and consulting are not mutually exclusive, so an audit activity can have both assurance and consulting (advising) components. A “blended” engagement may consolidate elements of consulting and assurance activities. In other instances, individual components of the engagement may be specified as assurance or consulting.

Internal auditors may conduct consulting services as part of their normal or routine activities or in response to management requests. An organization should delineate the types of consulting activities to be offered and develop necessary policies or procedures for each. The following are examples of consulting categories:

- **Formal consulting engagements.** Planned and subject to written agreement.
- **Informal consulting engagements.** Routine activities such as participation on standing committees, limited-life projects, ad hoc meetings, and routine information exchange.
- **Special consulting engagements.** Participation on a merger or acquisition team or system conversion team.
- **Emergency consulting engagements.** Participation on a team established for recovery or maintenance of operations after a disaster or other extraordinary business event or a team assembled to supply temporary help to meet a special request or unusual deadline.
In all situations, a consulting engagement should not be conducted in an attempt to circumvent assurance engagement requirements such as the need to provide an opinion at the end of an engagement. This is consistent with The IIA’s Code of Ethics. On the flip side—if deemed appropriate—services once conducted as an assurance engagement may be performed as a consulting engagement. However, such consulting activities should be coordinated with other internal audit assurance activities as well as external audit activities to minimize redundancy as per Standard 2050, “Coordination.”

The numbering format for Implementation Standards indicates their classification (assurance or consulting). For example, 1000.A1 and 1000.C1 are the Implementation Standards related to Attribute Standard 1000, “Purpose, Authority, and Responsibility,” whereby A indicates an assurance engagement standard and C indicates a consulting engagement standard. Implementation Standard 1000.A1 tells us, “The nature of assurance services provided to the organization must be defined in the internal audit charter. If assurances are to be provided to parties outside the organization, the nature of these assurances must also be defined in the internal audit charter.” Implementation Standard 1000.C1 states, in similar language, “The nature of consulting services must be defined in the internal audit charter.”

Exceptions to mandatory guidance of Standards
If laws or regulations prohibit internal auditors from complying with certain parts of the Standards, appropriate disclosures should be made. Internal auditors should comply with all other parts of the Standards.

Practice Advisories
The IIA’s Professional Issues Committee offers nonmandatory guidance in the form of Practice Advisories to help internal auditors put the mandatory Standards into practice. Practice Advisories are IIA-endorsed and provide concise and timely guidance to assist internal auditors in interpreting and applying the Code of Ethics and Standards and promoting best practices. Practice Advisories include practices relating to international, country, or industry-specific issues; specific types of engagements; and legal or regulatory issues. Some Practice Advisories are applicable to all internal auditors; others address the needs of a specific industry, audit specialty, or geographic area.

Practice Advisories address approach, methodology, and considerations but not detailed processes and procedures.

All internal auditors and other interested parties are welcome to submit suggestions to The IIA’s Professional Issues Committee to help in the continued development of the advisories. Practice Advisories have ongoing updates and
changes to provide new best practices to conform with the requirements of the Standards. All Practice Advisories are submitted to a formal review process by the Professional Issues Committee or other group designated by the Professional Practices Advisory Council. The most up-to-date versions of these and other parts of the framework appear at The IIA’s Web site (www.theiia.org). The Practice Advisories are intended for the use of IIA members and are therefore password-protected on The IIA’s Web site.

Practice Advisories will form the background of the presentation of many topics in this course.

As an example of how the Practice Advisories function, consider Standard 1110, “Organizational Independence.” The standard contains this mandate: “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.” How to put that into practice may not be immediately obvious to an organization’s chief audit executive (CAE). To get clarification, the CAE can bring up the Contents section of the online framework (assuming he or she is an IIA member), go to the section listing Practice Advisories, find an entry for Practice Advisory 1110-1, “Organizational Independence,” and read the further guidance provided there.

Even with the guidance of the Practice Advisories, the auditor will inevitably encounter challenging situations that aren’t specifically covered. When this happens, the auditor is still responsible for making decisions that are guided by the principles underlying the specific Standards and Rules of Conduct in the Code of Ethics. For The IIA’s members, these principles, and their animating spirit, cannot be overruled by a manager’s instructions or an organization’s contrary practices, policies, or culture. Only the law overrides the Code and the Standards.

**Practice Guides**

Practice Guides are another form of guidance provided by The IIA to help internal auditors incorporate the Standards into their practice. According to the Preface to the IPPF, the Practice Guides provide “detailed guidance for conducting internal audit activities” and include “detailed processes and procedures, such as tools and techniques, programs, and step-by-step approaches, including examples of deliverables.”

Like the Practice Advisories, these materials are listed only in the sections of The IIA’s Web site that require a password for access.