THE EVOLVING ROLE OF INTERNAL AUDIT IN A CONNECTED GRC ENVIRONMENT
INTRODUCTION

In today’s rapidly changing business environment, there is a marked increase in regulations, a greater focus on fraud and corruption and a heightened need for risk management. The end result is that executives, corporate boards and assurance professionals are under increased oversight and scrutiny by regulators, shareholders and external auditors. The consequence is that internal audit professionals are faced with a growing number of information requests, new compliance requirements, and the constant pressure to do more with less.

While many internal audit practitioners are currently concentrating on operational and compliance audits, auditing financial statements, and the evaluation of internal controls, the focus is rapidly evolving into other areas. In today’s regulatory and risk environment, there is a greater emphasis on risk management, fraud prevention, and corporate governance. With these changes, come the evolving role of the internal auditor and greater connection to the professions of compliance and risk management.
THE TRADITIONAL ROLE OF INTERNAL AUDIT

By definition, internal auditing is an independent, objective assurance and consulting activity. It is designed to add value and improve an organization’s operations by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Traditionally, internal audit provides management and the audit committee with assurance as to the design and operation of the governance, risk management and control processes in their organizations, which requires an unbiased view. In addition to conducting audits, internal audit is also involved in:

Assurance: The objective examination of evidence intended to provide accurate and current information to the stakeholders about the efficiency and effectiveness of its policies and operations, and the status of its compliance with the statutory obligations.

Assessment and Recommendations: Assessing and making recommendations on the effectiveness of the mechanisms that are in place to ensure that the organization achieves its objectives, and by performing this duty in a way that demonstrates informed, accountable decision making with regard to ethics, compliance, risk, economy and efficiency.

Oversight: Determining the basis by which decision makers achieve oversight and control of their organizations, apply sound risk management, target their attention to areas in need of improvement and demonstrate accountability. Accordingly, internal audit takes a disciplined, evidence-based approach to determining whether or not assurance can be provided that key systems and processes are appropriately designed and are functioning as intended.

Advisory Services: As an adjunct to the assurance role, and within their sphere of expertise, internal auditors will also provide advisory services to their organizations. In this respect, internal auditors are also expected to offer solution-oriented recommendations.

EVOLVING STAKEHOLDER EXPECTATIONS

Effective internal audit functions help organizations accomplish their business objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes. Based on changes in the business environment, the role of internal audit in the organization is continually evolving according to stakeholder and management expectations. Shareholders, board members and management are placing a greater emphasis on how internal auditors can play a role in evaluating and mitigating risks, IT and operations, managing fraud risk, as well as increasing their involvement in corporate governance.
INTERNAL AUDIT AND RISK MANAGEMENT

As outlined in the Institute of Internal Auditors International Professionals Practices Framework (IPPF), internal audit professionals are expected to play a central role in the enterprise risk management process. The IPPF Performance Standard 2120, states, “The internal audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes.” *

In this context, risk management refers to the design and implementation of actions and remedies to address risks through a consideration of potential treatments and the selection of the most appropriate course of action. This includes evaluating risk exposures relating to the organization’s governance, operations and information systems. According to this professional charter, internal audit then should be the primary owner of conducting the enterprise assessment of risk and the owner of the risk management function.

The core role of internal audit with regard to risk management is to provide objective assurance to the board on the effectiveness of an organization’s enterprise risk management activities. This will help ensure key business risks are being managed appropriately and that the system of internal control is operating effectively. As internal audit becomes more involved in the risk management processes, the discipline of performing risk assessments becomes a more emphasized job function. Risk assessment is a key analytical tool to identify and assess the extent of a likely hazard and to estimate the probability and consequences of negative outcomes for humans, property or the environment. Risk assessments are typically conducted on regulations, policies, processes, strategies and other attributes of organization.

As evidence to the increased focus on risk management, the Institute of Internal Auditors (IIA) announced on August 29, 2011, that they will offer a new certification allowing audit practitioners to demonstrate their ability to provide advice and assurance to audit committees and executive management on whether key risk management and governance processes in their organizations are in place and effective. The Certification in Risk Management Assurance (CRMA) exam will be offered starting in mid-2013.

INTERNAL AUDIT AND FRAUD

The growing number of regulations and the successful expansion of multinational organizations into new markets increases compliance risk. Regulators expect thorough due diligence, oversight and background checks to be performed on partners, vendors, suppliers and others. Because fraud negatively impacts organizations in many ways – financial, reputational, and through psychological and social implications – it is important for organizations to have a strong fraud prevention program. It should include awareness, prevention, and detection programs, as well as a process to identify risks within the organization.

As organizations work to reduce the incidence of fraud, their anti-fraud programs continue to rely heavily on the internal audit activity. Over time as internal auditors review systems in the organization, they develop an overall knowledge of the organization’s processes, risks, control systems and personnel. These factors contribute to their effectiveness at detecting fraud.

The IIA provides mandatory guidance for internal auditors in its IPPF. Internal auditors are expected to have sufficient knowledge to evaluate the risk of fraud in their organizations, and are required to report to the board any fraud risks found during their investigations. As part of their oversight function, internal audit and compliance will find a greater connection between their roles.

Although internal audit and compliance are separate functions, it is clear that they share many common connection points. To ensure an effective coordination of activities between these two functions, these assurance groups should leverage a common language of risk and control, common methodologies, and leverage a common technology solution. A common methodology related to fraud and corruption for compliance and internal audit leads to an agreement about what information must be gathered and how it will be gathered. This includes defining the risk types that will be assessed and the risk thresholds that will drive the depth and quality of the review. An effective fraud and corruption compliance program will define the thresholds beyond which risks would require mitigation or additional management, what controls require testing, and rules governing the creation of issues for reporting and resolution.

CORPORATE GOVERNANCE

As a direct report and resource of the audit committee, the traditional remit of the internal audit profession has been driven by the focus of the audit committee. Charged with oversight of the organization’s audit and control functions, the audit committee responsibility includes the oversight of the processes and structures implemented by the board and monitoring the activities of the organization toward the achievement of its objectives.

In addition to exchange requirements, audit committee responsibilities are also highlighted in legislated rules including those listed in section 301 of the Sarbanes-Oxley Act, which states amongst other things that:

- “The audit committee must be directly responsible for the appointment, compensation, retention and oversight of the work of any registered public accounting firm engaged for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for the issuer, and the registered public accounting firm must report directly to the audit committee
- The audit committee establishes procedures for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls or auditing matters, including procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters
- The audit committee must have the authority to engage independent counsel and other advisors, as it determines necessary to carry out its duties.”

As the corporate governance requirements of organizations increase, it can be expected that the audit committee members will also work closer with internal audit and rely on the profession for their independent business insight.

THE CHANGING ROLE OF INTERNAL AUDIT

Whilst the role and responsibility of internal audit may vary in scope and authority between organizations, there is a clear trend that internal audit is taking on a more strategic and central role. With these changes, the increased interaction between the evolving internal audit function and its major stakeholders is an important area for organizations to focus on and develop. For many organizations, executive management will request more advisory involvement of internal audit, including performing reality checks on key management decisions.

It has become increasingly clear that GRC activities are by nature interconnected and rely on common information, methodology, processes and technology. By establishing a universal, integrated approach to legal, compliance, risk, audit, and control processes, leading organizations have demonstrated that they can better leverage information, gain operational efficiency, and provide greater transparency into overall business risks. Likewise, by establishing a common, integrated discipline around regulations, policies, risks, controls, and issues, leading internal audit practitioners have demonstrated that they can better leverage information, gain operating efficiencies, and provide greater transparency into legal, regulatory, operational, and overall business risks.
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