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United States Government Accountability Office
Washington, DC 20548

May 20, 2010

Mr. Heriot Prentice
Director, Standards and Guidance
The Institute of Internal Auditors
247 Maitland Avenue
Altamonte Springs, FL 32701

Subject: Exposure Draft of Proposed Changes to the *International Standards for the Professional Practice of Internal Auditing*

This letter provides the U.S. Government Accountability Office's (GAO) comments on the Institute of Internal Auditors' (IIA) Exposure Draft of Proposed Changes to the *International Standards for the Professional Practice of Internal Auditing (Standards)*. We appreciate the opportunity to comment on this proposal. We commend the IIA for taking on this project to periodically review and update the *Standards*.

While we agree with the overall approach of the exposure draft, we believe the *Standards* could be improved and have recommendations in the following areas:

- impairment to independence or objectivity;
- external service provider and organization responsibility for internal auditing;
- risk management; and
- planning and criteria for communicating.

Standard 1130: Impairment to Independence or Objectivity

Standard 1130.C1 states that internal auditors may provide consulting services relating to operations for which they had previous responsibilities. We believe that the standard should also remind auditors of the impact consulting activities may have on their independence for providing assurance services. Accordingly, we suggest revising standard 1130.C1, as follows: “Internal auditors may provide consulting services relating to operations for which they had previous responsibilities. However, doing so may impair the auditor’s independence with regard to future audits of the operation.”

Standard 2070: External Service Provider and Organizational Responsibility for Internal Auditing

Chief Audit Executive

Proposed standard 2070 does not clearly indicate whether the entire internal audit activity, including the chief audit executive (CAE), may be provided by an external service provider or whether the CAE should be an employee of the audited organization.

In addition, the new definition of the CAE states that the “Chief audit executive describes a person in a senior position responsible for effectively managing the internal audit activity.” The prior definition stated that the “Chief audit executive is a senior position within the organization responsible for internal audit activities.” This revised definition also makes it less clear whether the CAE should be part of the organization.

We are concerned that the revised standard and definition of CAE could be interpreted to allow the entire internal audit activity of an entity, including the CAE, to be completely outsourced to an external service provider. While some government organizations may outsource or co-source the internal audit activity, oversight of the work, including the CAE function, should be performed internally. Maintaining this oversight role within the government is similar to the process used for any function that the government contracts to the private sector and is necessary to maintain effective control over the outsourced internal audit activity in the government environment.

We suggest revising proposed standard 2070, as follows: “When an external service provider serves as the internal audit activity, the chief audit executive ~~provider~~ must make the organization aware that it has the responsibility for maintaining an effective internal audit activity.”

In addition, we suggest changing the proposed wording of the definition of CAE, as follows: “Chief audit executive describes a person within the organization in a senior position responsible for effectively managing the internal audit activity in accordance with the internal audit charter and the *Definition, the Code of Ethics* and the *Standards*. Normally, the chief audit executive would be a *Certified Internal Auditor* or have *Certified Internal Auditors* reporting to them. The specific job title of the chief audit executive may vary across organizations.”

Quality Assurance and Improvement Program

We have concerns regarding the proposed interpretation to standard 2070. One concern relates to whether the quality assessment and improvement program applies to the organization, the external service provider, or both. Another concern relates to the lack of clarity on how the CAE would obtain sufficient evidence about the quality assurance and improvement program when an external service provider serves as the internal audit activity. In both these situations, clarification is needed about the process to be used for external assessments. In addition, the word “assessment” in the interpretation to the proposed standard should be changed to “assurance” for consistency with standard 1300.

To address these issues, we suggest revising the interpretation to standard 2070 to clearly indicate which party has responsibility for the quality assurance and improvement program and how the CAE would obtain sufficient evidence about the quality assurance and improvement program when an external service provider serves as the internal audit activity. In addition, we suggest revising the interpretation to standard 2070 to clarify the process to be used for the quality assurance and improvement program, including external assessments, when an external service provider serves as the internal audit activity. We also suggest replacing “assessment” with “assurance” for consistency with standard 1300.

Standard 2120: Risk Management

The addition made to the interpretation of standard 2120 suggests the internal audit activity’s assessment of the effectiveness of risk management is limited to the results of prior engagements. The narrow definition used in the proposed interpretation does not acknowledge that auditors may also need to focus on new or changed risks, such as risks related to new events and situations that have developed, in addition to those identified in prior engagements. Auditors may need to perform additional procedures beyond prior engagements, such as considering whether the organization has identified emerging trends and new risks in order to evaluate the effectiveness of the organization’s risk management processes. The importance of internal auditors being aware of these trends and risks is especially important in governmental entities, where early identification and corrections of deficiencies can help avoid unnecessary expending of resources and result in greater accountability to taxpayers.

We suggest changing the proposed addition to the interpretation of standard 2120, as follows: “The internal audit activity gathers the information to support this assessment from during multiple prior engagements. The results of these engagements, when viewed together, with the results of additional procedures, such as consideration of emerging trends and other risks, provide a basis for understanding of the organization’s risk management and its effectiveness.”

Standard 2410: Planning and Criteria for Communicating

For consistency with proposed standard 2010.A2, we suggest revising proposed standard 2410.A1, as follows: “Final communication of engagement results must, where appropriate, contain internal auditors’ opinion and/or conclusions. When an opinion and/or conclusion is issued it must address the expectations as agreed between the chief audit executive and ~~with~~ the board, senior management, and other stakeholders and must be supported by sufficient reliable, relevant, and useful information.”

We thank you for considering our comments on these important issues.

Sincerely yours,

A handwritten signature in black ink, appearing to read "James R. Dalkin". The signature is stylized and cursive, with a long horizontal stroke extending to the right.

James R. Dalkin
Director
Financial Management and Assurance