Overall Internal Audit Opinions, Lessons Learned & Moving Forward

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Objectives of this session

I. Discuss requirements for internal audit opinions

II. Share UNDP OAI's experience

- Hear everyone else's experience

III. Formulate approach for an overall internal audit opinion

PART I

The Requirements

The Executive Board Decision, 2015
(For UNDP/UNFPA/UNOPS)

"Future annual reports should include an **overall opinion**, based on the scope of work undertaken, on the adequacy and effectiveness of the organizations' framework of governance, risk management and control."

IIA Std 2450: Overall Opinions

"When an **overall opinion** is issued, it must take into account the **expectations** of senior management, the board, and other stakeholders and must be **supported** by **sufficient, reliable, relevant, and useful information**."

IIA Practice Guide: *Formulating and Expressing Internal Audit Opinions*

- Scope of opinion
  - **Macro level** – based on the results of multiple audits over a period of time
  - **Micro level** – based on the results of a single audit or a few audits over a more limited period of time
- Types of opinion
  - **Positive** assurance
  - **Negative** assurance

Positive vs Negative Assurance Opinion

- **Positive** = *"reasonable assurance"*
  - Provides the highest level of assurance
  - One of the strongest types of audit opinions
  - Auditor takes a definite position; takes responsibility
  - Sufficient evidence gathered
- **Negative** = *"limited assurance"*
  - "Nothing came to the auditors' attention within the scope of their work that would indicate that controls are not effective"
  - Auditor takes no responsibility
  - Less valuable to stakeholders

Rating system for positive assurance

- Clear wording
- Appropriately defined
- Understood by all
- Consistent and sustained for years (to facilitate comparison)

For negative assurance opinion - a grading or rating system is not applicable.

Planning the expression of an opinion

- Decide on what opinion will be issued
  - Positive or negative
  - Macro or micro

- Formulate annual audit plan (basis for opinion)
  - For positive assurance – more evidence and broader scope required
  - Ensure adequate resources in place

- Establish criteria for the opinion
  - Governance
  - Risk management
  - Controls

PART II
The UNDP Experience

UNDP OAI practice

- Rates all audit results, except follow-ups, DIM financial audits, and limited scope audits

- Issues a graded positive assurance opinion at micro level using a *harmonized* rating system

- Issues a macro level opinion for some HQ functional & cross-cutting audits, with organization-wide scope

- Presents a conclusion (but not an opinion) in the annual report

Extract from Annual Report, conclusion:

"With the resources available in 2014, OAI was able to effectively carry out its mandate of providing internal audit and investigation services to UNDP. The collective results of the audits of headquarters units, corporate functions, country offices, Global Fund grants and DIM projects, as well as third-party audits of NGO/NIM projects, supplemented the other oversight mechanisms, from which the Administrator and the Executive Board derive assurance on the efficient use of UNDP resources and on the effectiveness and adequacy of governance, risk management and internal control systems. All offices concerned were responsive in implementing audit recommendations."

2014 OAI audit rating distribution

Audit Rating Distribution (2014)

5 (7%)

40 (57%)

25 (36%)

■ Partially Satisfactory ■ Satisfactory ■ Unsatisfactory
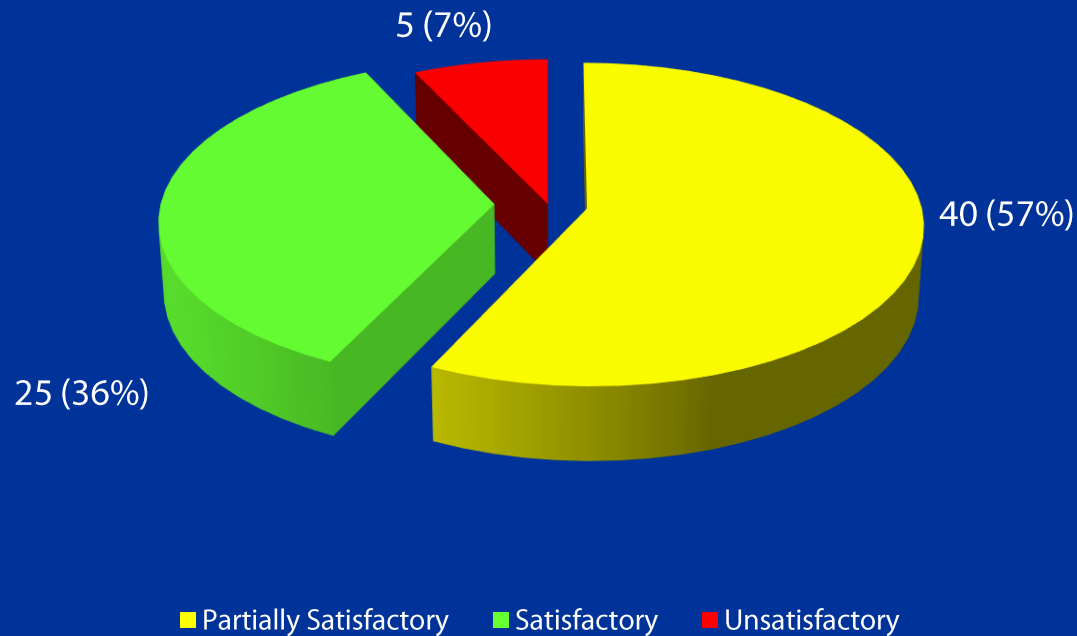
Harmonized audit rating system

- Agreed in 2007 with UNFPA, UNICEF, UNOPS, WFP
- Updated in 2010
- UNICEF recently moved away
- 3-tiered rating

  - Satisfactory
  - Partially satisfactory
  - Unsatisfactory

Harmonized rating definitions

Satisfactory -- Internal controls, governance and risk management processes were adequately established and functioning well. No issues were identified that would significantly affect the achievement of the objectives of the audited entity.

Partially Satisfactory -- Internal controls, governance and risk management processes were generally established and functioning, but needed improvement. One or several issues were identified that may negatively affect the achievement of the objectives of the audited entity.

Harmonized rating definitions (cont'd)

Unsatisfactory -- Internal controls, governance and risk management processes were either not established or not functioning well. The issues were such that the achievement of the overall objectives of the audited entity could be seriously compromised.

Criteria for internal audit opinion

- Internal controls, governance and risk management processes
  - Adequately established
  - Functioning well

- No significant issues that impact on objectives
  - Can be discerned from the priority of recommendations
    - ✓ Promptness of action needed
    - ✓ Severity of potential risk
    - ✓ Consequence on UNDP

Lessons learned from having audit ratings

PROS

- Help managers and Audit Advisory Committee assess audit results quickly
- Provide basis for prioritizing follow-up attention
  - On-site follow up audit for "unsatisfactory" audit the following year
- Offer useful comparative info on severity of issues or trends across UNDP
- Allow OAI to communicate potential risks for not implementing recommendations from unsatisfactory audits
- Motivate managers to perform better as audit rating is used as a performance indicator

Lessons learned from having audit ratings

CONS (counter productive)

- Management focuses on audit rating rather than on the criticality of audit issues and on actions needed to address them.

- Audit rating leads to disagreement; causes delay in report issuance.

- Audit rating can create friction between auditors and clients, who become more reluctant to share known weaknesses with auditors.

- Auditors are sometimes challenged with regard to the basis and the consistency of audit ratings.

PART III

The way forward

Neutralize the cons!

- Explain the audit rating at the entrance meeting; reiterate at the exit meeting.

- Consider sending the draft report with no rating.
  - Once management comments are in, re-assess and decide on the audit rating, which should now be acceptable.

- Definition of internal audit ratings displayed on organization's website (public disclosure)

- Develop an SOP for auditors to ensure consistency in providing ratings

Coming up with an overall opinion: a 4-step approach

1. Review distribution of ratings during the year.

2. Re-assess audit issues with high priority recommendations.

3. Consider current implementation status of recommendations.

4. Consider status of any investigation cases.

Reassess audit issues
with high priority recommendations

(from "partially satisfactory" and "unsatisfactory" audits)

- Materiality threshold
  - ✓ Pervasiveness of deficiencies
  - ✓ Significance of amount (if quantifiable)

- Impact of risk at the global/corporate level
  - ✓ Prevents achievement of strategic goals
  - ✓ Affects reputation of organization

An option - Limited macro opinion

- Insufficient evidence to support all areas supposed to be covered by a macro opinion

- Significant scope limitation

- Audit results cannot be extrapolated to represent the whole audit universe.

Opinion statement must adequately describe reasons why the opinion being issued is limited.

Proposed overall opinion statements, retaining existing rating system

Satisfactory	**Overall, the governance, risk management and control processes were adequately established and functioning well. No issues were identified that would significantly affect the achievement of the objectives of (the organization).**
Partially Satisfactory	**Overall, the governance, risk management and control processes were generally established and functioning, but needed improvement. One or several issues were identified that may negatively affect the achievement of the objectives of (the organization).**
Unsatisfactory	**Overall, the governance, risk management and control processes were either not established or not functioning well. The issues were such that the achievement of the overall objectives of (the organization) could be seriously compromised.**

Thank you!

comments may be sent to
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