

Chapter 30

Internal Audit in Ministries

1.0 MAIN POINTS

Internal audit is an important component of sound governance for public sector organizations. Internal audit provides value to governing bodies and senior management by providing an objective source of independent advice.

The Government of Saskatchewan funds a minimum of 30 internal audit positions in six ministries at an estimated cost of \$2 million. Government ministries in Saskatchewan are not legislatively required to have an internal audit function. The decision of whether to have an internal audit function is left to each ministry. The Ministry of Health and the Ministry of Education, which make up a significant portion of government spending, do not have their own internal audit function.

We evaluated whether six internal audit functions followed best practices—the Standards set by The Institute of Internal Auditors (IIA). We found that internal audit in ministries often focuses on financial transactions rather than on key ministry risks, financial or otherwise. While we observed some good practices, we found many areas where internal audit did not comply with the IIA Standards.

Based on the result of our assessments, we believe that improvements are needed to ensure that value for money is achieved through effective internal audit work. We note that many provinces have a centrally-coordinated internal audit function and we suggest that the Ministry of Finance evaluate centralization and other models for use in Saskatchewan. Our first recommendation on this point should be considered prior to the Ministry addressing the other recommendations. This chapter contains seven recommendations to improve internal audit.

2.0 INTRODUCTION

The Institute of Internal Auditors defines internal audit as follows:

Internal auditing is an independent, objective, assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control and governance processes.¹

The internal audit profession is governed globally by the IIA. The IIA publishes *The International Professional Practices Framework* (IIA Standards) for the work of internal audit. The IIA Standards outline both mandatory and strongly recommended guidance for internal audit.

In Saskatchewan, there is no legislative requirement for ministries to have an internal audit function. The decision of whether to have an internal audit function is left to each

¹ The Institute of Internal Auditors-*International Professional Practices Framework*, 2009, p. 2.



ministry. We identified where internal audit existed in ministries and evaluated whether they followed IIA Standards.

We determined that the ministries in **Figure 1** had internal audit functions as of May 25, 2012:

Figure 1 – Internal Audit Functions in Ministries

Ministry	Chief Audit Executive	Audit Committee Exists	Audit Committee Chair	Number of Internal Audit Positions	Type of Audit Work in 2011/12
Advanced Education	Director	Yes	Deputy Minister	5	Risk-based (e.g., audit of the skills training benefit program)
Central Services	Director	No ³	No ³	4	Partially risk-based
Environment	None ¹	Yes	Deputy Minister	2	Partially risk-based
Finance	Director	No ⁴	No ⁴	11*	Transaction focused (e.g., payments, payroll, revenue)
Justice	Unclear ²	Yes	Deputy Minister	4**	Transaction focused (e.g., revenue)
Social Services	Unclear ²	Yes	Executive Director	4	Limited - investigation

¹ – Environment does not have a CAE. There are only two internal auditors.

² – Ministry is unclear who CAE is. IA Charter was not clear.

³ – Audit Committee does not exist. CAE does not report to Executive or Audit Committee.

⁴ – Provincial Comptroller.

* – The Executive Director of the Financial Management Branch acting as Director of Internal Audit is included in this number.

** – A summer student position is included in this number.

The Ministry of Health has an internal audit position but does not conduct internal audit work.

The Ministry of Finance's internal audit function works under the Provincial Comptroller's Office as described in Section 8.3.2 below. Finance's internal audit function audits all ministries to assess financial and management controls.

The Ministry of Finance's mandate includes managing the financing, revenue and expenses of the Government in order to enhance the fiscal strength of the Province.² Therefore, improvements to the effectiveness of internal audit, risk management or internal controls for the Government would be the responsibility of the Ministry of Finance and we direct our recommendations accordingly.

3.0 VALUE OF INTERNAL AUDIT

Internal audit is an important component of sound governance for an organization. An independent and objective internal audit function provides a unique viewpoint and insights to senior management and the audit committee. Internal audit is able to provide

² <http://www.finance.gov.sk.ca/departments-overview> (accessed November 6, 2012)

this information because it is independent—that is, separate from operations—yet is part of the organization and able to understand the organization and its risks.

Through risk-based planning, effective internal audit focuses available resources on the areas of highest risk considering an organization's overall strategic objectives, operations and resources. Risk-based internal auditing should highlight opportunities to increase efficiency and confirm or identify weaknesses in the operation of key controls. Internal audit should have a positive impact on process improvement within the organization and provide relevant information on best practices for management decision making.

Internal audit provides recommendations to assist organizations in achieving their goals and objectives. Implementation by management of internal audit recommendations, and monitoring of management progress by internal audit, is part of effective oversight.

4.0 SCOPE OF WORK

The objective of this project was to assess whether internal audit within ministries followed best practices (i.e., IIA Standards). The assessment focused on internal audit in ministries for the period April 1, 2011 to June 30, 2012.

As noted in Section 2.0, we confirmed that only six ministries have internal audit functions. We assessed the six ministries' internal audit functions and practices against the IIA Standards using the IIA's External Quality Assessment criteria. These criteria are designed to permit consistent evaluation of compliance with IIA Standards. We outline the Standards in Section 5.0. We provided internal audit in each of these ministries with the detailed results of our assessment. We summarize the results of our work and provide recommendations in Section 8.0.

5.0 ASSESSMENT CRITERIA

Figure 2—Outline of IIA Standards

The IIA Standards specify basic requirements for the professional practice of internal auditing. These include:

- 1000 Purpose, Authority and Responsibility**
 - 1010 Recognition of the Definition of Internal Auditing, Code of Ethics and the Standards in the Internal Audit Charter
- 1100 Independence and Objectivity**
 - 1110 Organizational Independence
 - 1111 Direct Interaction with the Board
 - 1120 Individual Objectivity
 - 1130 Impairment to Independence or Objectivity
- 1200 Proficiency and Due Professional Care**
 - 1210 Proficiency
 - 1220 Due Professional Care
 - 1230 Continuing Professional Development
- 1300 Quality Assurance and Improvement Program**
 - 1310 Requirements of the Quality Assurance and Improvement Program
 - 1311 Internal Assessments
 - 1312 External Assessments
 - 1320 Reporting on the Quality Assurance and Improvement Program
 - 1321 Use of "Conforms with the International Standards for the Professional Practice of Internal Auditing"
 - 1322 Disclosure of Nonconformance

Source: The Institute of Internal Auditors-*International Professional Practices Framework*



6.0 OVERALL CONCLUSION

The Government of Saskatchewan funds a minimum of 30 internal audit positions in six ministries at an estimated cost of \$2 million. Based on the result of our assessments, we believe that improvements are needed to ensure that value for money is achieved through effective internal audit work.

The Internal Audit Capability Model is a framework that identifies the fundamental attributes required for effective internal auditing in the public sector (see **Figure 3** in Section 7.0). The results of our assessments found internal audit in ministries in Saskatchewan were at the early stages of the capability model. Moving towards uniform professional practices and oversight would increase effectiveness.

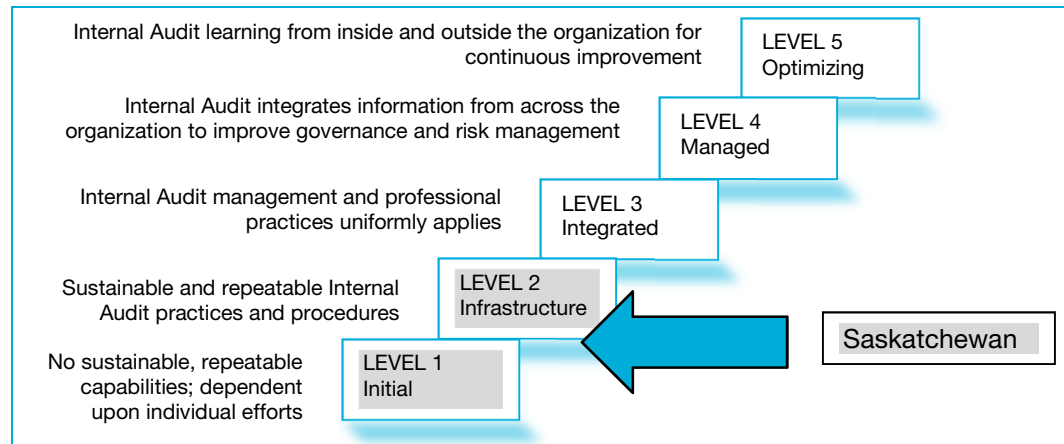
While we observed examples of good practices, we found many areas where internal audit did not comply with IIA Standards. We found examples, at the various ministries, of inappropriate reporting structures (such as a lack of independent chief audit executives and audit committees), absence of risk-based audit plans, untimely execution of audits, failure to complete audit plans, lack of supervision, limited reporting to audit committees (where these existed), and an absence of a formal quality assurance program. We found that internal audit activity in ministries focused on financial transactions. Also, two of the largest ministries, Ministry of Health and Ministry of Education do not have internal audit functions. We make several recommendations for improvements.

Most Canadian provinces have a central internal audit function. We suggest prior to addressing recommendations two to seven, that the Ministry of Finance consider recommendation one.

7.0 ASSESS ORGANIZATIONAL MODELS FOR INTERNAL AUDIT

We compared the results of our assessments of internal audit functions within the ministries to the Internal Audit Capability Model that is explained in more detail in **Exhibit 1** in Section 10.1. Our findings suggest that internal audit within ministries is at an early stage in the IIA Internal Audit Capability Model (**Figure 3**).³ For example, internal audit functions are not effectively structured, audits are focused on financial transactions and professional practices are inconsistent. There are limited sustainable, repeatable capabilities in only a few ministries.

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Figure 3—Internal Audit Capability Model—See Section 10.1 for Further Details

Source: The Internal Audit Capability Model for the Public Sector developed by the IIA Research Foundation

There is no current forum for regular meetings to promote collaboration among internal audit functions in ministries. As well, there is no central body to oversee internal audit work performed across ministries that considers the appropriate structure, focus and delivery of internal audit. Improved communication, cooperation, sharing of best practices and leveraging of expertise and resources would improve the effectiveness of internal audit.

Our cross-Canada scan indicated that except for Quebec and Saskatchewan, all provinces that have internal audit functions have centralized them (see Section 9.0). A centralized delivery can offer benefits. An overall view of government ministries, their objectives, risks, governance and controls would guide a complete risk-based internal audit plan across all ministries.

As previously noted, there are some ministries in Saskatchewan with significant risks that do not have an internal audit function (e.g., Ministry of Health, Ministry of Education). Also, there are a minimum of 30 internal audit positions in six ministries, representing about \$2 million in salaries. These internal auditors perform internal audit work focused on financial transactions, rather than carrying out internal audit projects based on key risks that would add value and help ministries achieve their objectives.

Centralization would reduce duplication of effort in some areas and provide audit services to ministries that do not have or cannot financially support an internal audit function. It would provide efficiencies as only one overall chief audit executive (CAE), one audit committee, and one risk-based audit plan would be needed. Centralization could promote consistency in quality of work and compliance with IIA Standards. In looking at centralization, there should be a thorough analysis of the pros and cons—keeping in mind that the current decentralized approach used is not working effectively.

- 1. We recommend the Ministry of Finance evaluate various organizational models for internal audit.**



At a minimum, if the Government determines not to centralize internal audit, consideration should be given to an internal audit committee that identifies opportunities for improving internal audit within ministries and facilitates information sharing.

8.0 KEY FINDINGS AND RECOMMENDATIONS

In this section, we outline key observations from our assessments and the resulting recommendations.

8.1 Purpose, Authority and Responsibility—Internal Audit Charters Need to Align with IIA Standards

1000 Internal Audit Purpose, Authority and Responsibility

IIA Standards outline the key pieces of an internal audit mandate in the form of an internal audit charter. In addition to defining the purpose, authority and responsibility, the internal audit charter should recognize the IIA definition of internal audit, code of ethics and standards.

The internal audit charter is a formal document that defines the internal audit activity's purpose, authority and responsibility. The charter also establishes the positioning of internal audit within the organization thereby providing the authority for internal audit to access records and personnel in the course of its work. The charter also defines the nature of the activities of internal audit (e.g., assurance and/or consulting). It should be reviewed on a regular basis and approved by an audit committee.

We found that each of the ministries we examined with an internal audit function had an internal audit charter. However, the charters were not consistent. Review and updating of internal audit charters did not take place consistently across ministries. Where there was an audit committee in place, the charters had been approved. While the charters we reviewed defined internal audit, in most cases the definition was not consistent with the IIA definition of internal audit. Most ministry charters did not mention the IIA Code of Ethics. IIA Standards were noted in four charters but only one charter required an external quality assessment. The Ministry of Finance has recently begun developing a standard charter template for ministries to use.

- 2. We recommend the Ministry of Finance implement a standard internal audit charter that aligns with Institute of Internal Auditors Standards.**

8.2 Independence and Objectivity—Effective Audit Leadership Needed

1100 Independence and Objectivity

Internal audit independence and objectivity are required for internal audit to be able to carry out its responsibilities without bias or undue influence from management. Any impairment to either independence or objectivity must be disclosed to the appropriate parties.

Fundamentally, internal audit provides value to governing bodies and senior management by providing an objective source of independent advice. This is accomplished through effective reporting relationships and risk-based internal audit plans approved by audit committees.

The internal audit function should have a chief audit executive (CAE). The CAE is the lead internal auditor in the organization. A CAE will often be part of a unique reporting structure as this person will report functionally to an audit committee and administratively to a member of senior management. An audit committee for a ministry would typically be comprised of the deputy minister and assistant deputy ministers. Having external independent members is also reasonable. The audit committee would provide guidance and support to internal audit, including approval of audit plans and input into internal audit goals and performance. Administrative reporting includes the approval of timesheets, expense claims, space and equipment requirements.

Our assessments within ministries revealed challenges regarding internal audit leadership both from a functional and administrative perspective. There were two ministries where it was not clear who the CAE was. One ministry did not have a CAE. For these three ministries, administrative reporting of the internal audit function was to an inappropriate level of management in the organization. When internal audit does not report to an appropriate (i.e., senior enough) level within a ministry, internal audit may not have access to the right information to conduct its risk-based planning. Additionally, internal audit may not be able to function independently and may become management-driven.

Internal auditors should typically issue reports at the end of each audit that summarize their findings, recommendations, and describe any response or action plan by management. CAEs typically report to audit committees quarterly and provide management's progress toward resolving issues. Timely, formal reporting provides clear recommendations and action plans to resolve issues identified.

In two ministries, we found that there was no audit committee. In another ministry, the CAE did not report to the audit committee. In one other ministry, only verbal updates were provided to the audit committee. Verbal reporting makes it difficult to determine if critical issues are brought forward. It also makes it difficult to consistently address recommendations or understand complex subject matter. In ministries where internal audit reported to an audit committee, we found that the audit committees were not always meeting on a quarterly basis and audit results were not completed or reported on a timely basis. Three out of six ministries needed to improve their follow-up process for monitoring management's progress on addressing internal audit recommendations.



An internal audit functions should be evaluated by the audit committee. In four ministries, there was no evaluation of the CAE by the audit committee.

Other jurisdictions have implemented independent audit committees in a public sector setting. Some provinces have established one overall CAE and an audit committee that is made up of deputy ministers from various ministries. In these provinces, while internal auditors are still working within individual ministries, they report to the one overall CAE. The audit results are then reported to each ministry and as well as to an overall audit committee. This structure promotes the independence of internal audit and makes it less vulnerable to management influence.

3. We recommend the Ministry of Finance work with ministries to implement appropriate internal audit reporting structures to support effective internal audit.

8.3 Proficiency and Due Professional Care—Improvements Needed

1200 Proficiency and Due Professional Care

Internal audit engagements require knowledge and skills in order for the work to be performed with proficiency and due professional care.

8.3.1 Proficiency-Assess Internal Audit Competencies

Internal auditors must possess professional skills and competencies to perform quality work. They must also have adequate knowledge of the organization in which they work.

There were 30 internal auditor positions at various levels within the six ministries we assessed. The size and allocation of internal audit resources was not consistent. We found in risk areas where there was no internal audit expertise (e.g., information technology) there were no audits conducted.

Professional development is a key component to increasing knowledge and capabilities. We found that each ministry with an internal audit function supported continuous improvement through training.

There were differences in the experience levels of staff between the six ministries, and job descriptions and job classifications were not consistent. Some internal auditors were required to have a professional designation while others were not.

4. We recommend the Ministry of Finance work with ministries to ensure that internal auditors have appropriate competencies.

8.3.2 Due Professional Care—Internal Audit Plans Should be Risk Based

Risk management is a key component in effective internal audit planning. Risk management encompasses the identification, assessment, prioritization and mitigation of risks. Risks can be ranked by considering the likelihood and impact of events on an organization (e.g., financial, legal, reputational). Risk assessments allow an organization to make decisions to reduce, avoid or accept the risks identified.

The results of risk assessments are critical to internal audit. They support the development of risk-based audit plans that focus resources on the highest risk areas of the ministry. Without a risk-based internal audit plan, internal audit may be focusing its efforts in the wrong areas.

In some ministries, internal audit led the risk assessment/risk management process. Other ministries relied on another division within the organization to lead risk management. Yet other ministries contracted with third parties for risk identification and ranking assistance.

Overall, we found that there was no consistent risk management methodology used in ministries. This is an area where shared methodology and shared results could achieve efficiencies.

5. We recommend the Ministry of Finance and ministries collaborate on methodology and tools to support risk-based internal audit planning.

The Provincial Comptroller's Office of the Ministry of Finance assists the Legislature and the Government in controlling and accounting for the receipt and disposition of public money. The Provincial Comptroller's Office is mandated to verify that ministries maintain appropriate financial and management controls and are properly accounting for their revenues and expenses.⁴

The internal audit function in Finance works to support the statutory responsibility of the Provincial Comptroller. We found that the work conducted by internal audit in Finance mainly consisted of risk assessments and audits of financial controls in the areas of payroll, payments and revenue. There is little input from ministries on the scope of work done. Results were provided to ministries and reported to the Provincial Comptroller.

We found limited evidence of collaboration or coordination of efforts between internal audit in various ministries or with the Provincial Comptroller's Office. In some cases, the same financial risk area was audited by ministry internal audit and by the Provincial Comptroller's Office.

Some ministries had their internal audit functions conduct financial transaction audits rather than risk-based or operational audits. Other key risks may have related to controls over program delivery and major ministry projects, but these were not given audit attention. Internal audit plans should consider emerging risks and trends in government

⁴ <http://www.finance.gov.sk.ca/Default.aspx?DN=b7318a7a-f397-42fc-9245-dcc4c849c98a>.



as they pertain to the specific ministry and government as a whole. An effective risk-based audit plan integrates environmental scans, emerging issues, risk assessments and strategic goals into the audit plan. Internal audit can play a critical role in providing assurance to management in these key areas.

- 6. We recommend the Ministry of Finance work with ministries to develop risk-based internal audit plans.**

8.4 Quality Assurance and Improvement Program Required

1300 Quality Assurance and Improvement Program

Internal audit must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.

Internal audit should continuously monitor its effectiveness. Quality assurance assessments reduce the risk of inconsistent or unacceptable quality. The IIA Standards indicate the CAE must develop and maintain a quality assurance and improvement program that covers all aspects of internal audit activity. The IIA Standards also require that an external quality assessment take place once every five years. Assessment results must be reported to the audit committee.

We found that internal audit functions within ministries did not have formal quality assurance programs. For example, there were no formal surveys sent to managers after each audit engagement or annually to an audit committee. Surveys could evaluate such dimensions as professionalism, quality, timeliness, utility of meetings, and quality of status updates.

Prior to our assessment, no internal audit function within a ministry had received a quality assurance review. Quality assurance reviews would help ministries evaluate compliance with IIA Standards and identify opportunities to improve internal audit performance and services. Also, we found some ministries had internal auditors performing audits with no supervision or review of files.

IIA Standards require disclosure to the audit committee of nonconformance with the IIA Code of Ethics or Standards. As noted above, ministries did not always fully comply with the IIA Standards; however, there were no disclosures made by ministries of nonconformance.

- 7. We recommend the Ministry of Finance implement effective quality assurance programs for internal audit.**

9.0 INTERNAL AUDIT ACROSS CANADA

Figure 4 shows the structure of internal audit in other Canadian provinces. Seven of the nine provinces in Canada that have internal audit have centralized this function. Five of these seven provinces have a central audit committee.

Figure 4—Internal Audit Across Canada

Province	Internal Audit Model Structure	Chief Audit Executive	Audit Committee Exists	Audit Committee Chair
British Columbia	Centralized	Assistant Deputy Minister Internal Audit and Advisory Services	Yes	Minister of Finance
Alberta	Centralized	Chief Internal Auditor	Yes	Deputy Minister
Saskatchewan	Decentralized	Varies across ministries	Varies	Varies
Manitoba	Centralized	Director Internal Audit and Consulting Services	Yes	Deputy Minister
Ontario	Centralized	Chief Internal Auditor and Assistant Deputy Minister	Yes	Deputy Minister
Quebec	Decentralized	Varies across ministries	Varies	Varies
Newfoundland	Centralized	Director of Professional Services and Internal Audit	No	No
Nova Scotia	Centralized	Executive Director Internal Audit	Yes	Deputy Minister
New Brunswick	Centralized	Comptroller acts as the provincial CAE	No	No
Prince Edward Island	No Internal Audit	N/A	N/A	N/A

Source: Information collected by Provincial Auditor Saskatchewan, Fall 2012

10.0 EXHIBITS

10.1 Internal Audit Capability Model

The capability levels in the Internal Audit Capability Model provide a road map for continuous improvement within an internal audit activity.



Exhibit 1—Internal Audit Capability Model for the Public Sector⁵

Description of the Capability Levels	
5—Optimizing	<ul style="list-style-type: none">—IA is a learning organization with continuous process improvements and innovation.—IA uses information from inside and outside the organization to contribute to achieving strategic objectives.—World-class/recommended/best practice performance.—IA is a critical part of the organization's governance structure.—Top-level professional and specialized skills.—Individual, unit, and organizational performance measure are fully integrated to drive performance improvements.
4—Managed	<ul style="list-style-type: none">—IA and key stakeholders' expectations are in alignment.—Performance metrics are in place to measure and monitor IA processes and results.—IA is recognized as delivering significant contributions to the organization.—IA functions as an integral part of the organization's governance and risk management.—IA is a well-managed business unit.—Risks are measured and managed quantitatively.—Requisite skills and competencies are in place with a capacity for renewal and knowledge sharing (within IA and across the organization).
3—Integrated	<ul style="list-style-type: none">—IA policies, processes, and procedures are defined, documented, and integrated into each other and the organization's infrastructure.—IA management and professional practices are well established and uniformly applied across the IA activity.—IA is starting to align with the organization's business and the risks it faces.—IA evolves from conducting only traditional IA to integrating as a team player and providing advice on performance and management of risks.—Focus is a team building and capacity of the IA activity and its independence and objectivity.—Generally conforms to the Standards.
2—Infrastructure	<ul style="list-style-type: none">—Key question or challenge for Level 2 is how to establish and maintain repeatability of processes and thus a repeatable capability.—IA reporting relationships, management and administrative infrastructures, and professional practices and processes are being established (IA guidance, processes, and procedures).—Audit planning based principally on management priorities.—Continued reliance essentially on the skills and competencies of specific persons.—Partial conformance with the Standards.
1—Initial	<ul style="list-style-type: none">—Ad hoc or unstructured.—Isolated single audits or reviews of documents and transactions for accuracy and compliance.—Outputs dependent upon the skills of the specific person holding the position.—No professional practices established other than those provided by professional associations.—Funding approval by management, as needed.—Absence of infrastructure.—Auditors likely part of a larger organizational unit.—Institutional capacity is not developed.

Source: The Internal Audit Capability Model for the Public Sector developed by the IIA Research Foundation.

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