

RISK-BASED AUDIT PLANNING - GUIDANCE FOR INTERNAL AUDITORS

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ABOUT ICPAU

The Institute of Certified Public Accountants of Uganda (ICPAU) was established in 1992 by the Accountants Act, Cap. 294.

The functions of the Institute as prescribed by the Act are to regulate and maintain the Standard of Accountancy in Uganda and to prescribe and regulate the conduct of accountants and practising accountants in Uganda. Under its legal mandate, the Institute prescribes professional standards to be applied in the preparation and auditing of financial reports in Uganda.

Vision

A globally recognized promoter of accountants for sustainable economies.

Mission

To develop and regulate accountants for professional excellence and sustainable impact.

Core Values

- 1) Professional Excellence
- 2) Accountability
- 3) Integrity
- 4) Responsiveness

International Affiliations

The Institute is a member of the International Federation of Accountants (IFAC) and the Pan African Federation of Accountants (PAFA).

DISCLAIMER

This paper is prepared to guide internal auditors in the preparation of risk-based internal audit plans. Internal auditors may utilize the paper in light of their professional judgment and the facts and circumstances involved in their organizations and each particular engagement. This paper does not intend to replace or be used as a substitute to the Global Internal Audit Standards or any relevant Practice Guides. Reference to conformance with relevant standards and guidance supports a discussion with senior management and the board about the importance of internal audit's risk-based plan as well as other aspects of planning (e.g., communication, coordination, and reliance).

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1.0 INTRODUCTION

The world is rapidly changing, which implies that many businesses today are grappling with emerging risks associated with these changes. To cope with this trend of events, internal auditors today have to master the ability to develop agile audit plans to address the rapidly evolving business risks. The implication of this is that internal auditors need to have the ability to assess risks frequently or even continuously. It is said that internal auditors should have the ability to assess risks at the speed of light.

This paper is prepared to support internal auditors during the process of preparing agile internal audit plans.

2.0 RISK-BASED AUDIT PLANNING

Risk-based audit planning is the process of ensuring that scarce audit resources are allocated to the riskiest areas in the organization. Risk-based internal audit planning provides a link between the internal audit engagements performed and the organization's overall risk management framework. According to the Global Internal Audit Standards, internal audit plans need to be prepared using a systematic, disciplined approach. Comprehensive risk-based audit planning enables internal auditors to properly align and focus the available limited resources to produce insightful, proactive, and forward-looking assurance and advice on the most pressing issues.

While traditional internal audits often follow a checklist approach, the constantly evolving business environment characterized by the emergence of new technologies requires a shift toward the risk-based paradigm. This means that internal audit plans today should focus on the most impactful risks. The risk-based approach therefore, enables internal auditors to provide the most impactful assurance in light of the continuously evolving risks. Risk-based internal auditing ensures that the scarce resources are concentrated on the highest-priority risks. Effective risk-based audit planning enables a more timely response to organizational risks, resulting in the customization of audit activities to match the specific circumstances of each organization.

Risk-based internal auditing enables internal auditors to master the ability to:

- a) Adopt a proactive approach to risk mitigation as risks are addressed before they materialize.
- b) Focus on macro-level risks while covering micro-level risks contributing to significant enterprise-level risks.
- c) Develop a vision of emerging risks.
- d) Leverage technology to monitor risks better and improve the quality, efficiency, and value of intelligence obtained through audits and continuous monitoring efforts.

3.0 THE RISK-BASED INTERNAL AUDIT PLANNING PROCESS

The process of establishing a risk-based internal audit plan generally involves the following steps:

3.1 Understanding the Organisation

According to Standard 9.1 of the Global Internal Audit Standards - Understanding Governance, Risk Management, and Control Processes, the development of effective internal audit plans requires the Chief Audit Executive to have an understanding of the organization's governance, risk management, and control processes. During this stage, therefore, internal auditors will seek to understand the organization's strategic objectives, strategies, and structure, especially the risk management processes and how the roles and responsibilities of risk management and governance are coordinated.

This stage is critical because it helps in identifying and assessing the risks that impact the organization. Understanding the organization in the context of risk-based internal audit planning involves the following:

- a) Evaluation of the organizational structure to appreciate responsibilities for risk management and governance structure including the board of directors, audit committee, and other governance bodies.
- b) Evaluation of the strategic objectives and review of the key performance indicators used in measuring progress towards the achievement of the strategic objectives.
- c) Review of key organizational documents such as the organizational chart, the strategic plan, annual reports, and minutes of meetings with those charged with governance.
- d) Consulting with key stakeholders especially senior management and the board to ensure the internal audit function shares a common understanding of the organisation's risk and assurance preferences.
- e) Conducting surveys, interviews, research, and brainstorming sessions to facilitate the identification of emerging risks and fraud risks. Researching industry news, trends, and regulatory changes may enhance awareness about emerging risks.
- f) creation or revising of the audit universe, which is essentially a list or catalogue of all potentially auditable units within the organization¹.

3.2 Risk Identification, Assessment, and Prioritisation

Organization-wide risk assessment enables the internal audit function to focus on risks rated as most significant. Critical risks are identified through understanding overall organizational and specific business objectives and the strategies used to achieve them.

¹ IIA Supplemental Practice Guide (2020): Developing a Risk-Based Internal Audit Plan, Institute of Internal Auditors, Inc, Lake Mary, Florida.

Standard 9.4 of the Global Internal Audit Standards- Internal Audit Plan requires organization-wide risk assessment to be completed at least annually. Risks represent the barriers to the achievement of organizational objectives.

However, the Chief Audit Executive should continuously be appraised with updated risk management information, to enable them to update the internal audit plan to ensure appropriate consideration of emerging trends accordingly. In situations of extremely dynamic business environments, the internal audit plan may need to be updated as frequently as every six months, quarterly, or even monthly. This will be done depending on the size and complexity of the organization concerning the governance, risk management, and control processes.

Risk identification, assessment, and documentation may be done using the following approaches:

3.2.1 Specific-risk Approach

This approach involves identifying risks associated with each specific auditable unit in the audit universe. Auditable units may be any topic, subject, project, department, process, entity, function or area that due to the presence of risk may justify an audit engagement². Risks are identified, analysed, and assessed concerning particular business objectives, activities, or processes.

3.2.2 Risk by Process Approach

Similar to the Specific-risk approach, the Risk by Process approach involves the identification and mapping of risks to business processes. Additionally, processes that play key roles in achieving the business objectives are determined and risks associated with such key processes are prioritized for consideration in the internal audit plan.

3.2.3 Risk-factor Approach

This approach is commonly used when performing a comprehensive organization-wide risk assessment to identify factors common to all auditable units that affect the ability to achieve organization objectives. Risk factors are elements that increase the impact or likelihood of risk to the related auditable unit.

3.3 Estimation of Resources

This stage involves the estimation of the resources needed to implement the internal audit plan. Resources may include people (labour hours and skills), technology (audit

² IIA Supplemental Practice Guide (2020): Developing a Risk-Based Internal Audit Plan, Institute of Internal Auditors, Inc, Lake Mary, Florida.

tools and techniques), time, and finances. The Chief Audit Executive must estimate the scope of the engagements and the skills, time, and budget needed to perform the identified engagements.

The estimation of resources needed to perform the identified engagements will be influenced by the nature and complexity of engagements, resources spent on comparable engagements that were performed previously, and the date of the most recent audit of the area or process.

3.4 Coordination with other Providers of Assurance and Consulting Services

Internal audit functions are most impactful when they provide assurance and consulting services where the highest residual risk exists. In mature and highly regulated organizations, the high-risk areas are controlled effectively by the first line and may have sufficient assurance coverage by the second line such as risk management and compliance functions as well as the external auditors.

To make the best use of the available resources, internal auditors should coordinate activities, share information, and consider relying upon the work of other internal and external assurance and consulting service providers. This minimizes the duplication of work and maximizes the efficiency with which assurance is provided.

Standard 9.5, Coordination and reliance requires that while the internal audit function may place reliance on the work of other assurance providers, the Chief Audit Executive must document the basis for that reliance and is still responsible for the conclusions reached by the internal audit function.

3.5 Drafting the Internal Audit Plan

All the work in the preceding sections should be performed to have a draft internal audit plan, which is then presented, discussed, revised, and finalized for approval by those charged with governance. An internal audit plan may include the sections indicated in Appendix 1. Standard 9.4 - Internal Audit Plan requires that the internal audit plan include:

- Consideration of internal audit mandate and the full range of agreed-upon internal audit services.
- Specification of internal audit services that support the evaluation and improvement of the organization's governance, risk management, and control processes.
- Consideration of coverage of information technology governance, fraud risk, the effectiveness of the organization's governance, risk management, and control processes.
- Identification of the necessary human, financial, and technological resources necessary to complete the plan.

- Consideration of changes in the organization's business, risks operations, programs, systems, controls, and organizational culture.

Once the draft risk-based internal audit plan is developed, it is discussed with senior management before eventually being presented to the Audit Committee which may suggest additional adjustments to the plan based on its view of the organization's risk appetite.

3.6 Communication of the Finalised Internal Plan

After the Audit Committee's approval, the finalized plan is presented to the board. The typical presentation will summarise the engagements in the plan, and explain the risk assessments behind the selections. Once the board formally approves the plan, all affected business areas in the organization typically receive a copy.

Once the final plan is approved, the Chief Audit Executive, senior management, and those charged with governance should agree upon the criteria that may be applied to define significant changes (resulting from emerging and/or unprecedented occurrences among others) that may necessitate revisions to the audit plan. The criteria should be incorporated into the internal audit function's methodologies.

4.0 CONCLUSION

Risk-based internal audit planning is a strategic approach that enhances the effectiveness and efficiency of the internal audit function. Risk-based internal audit planning ensures that all internal audit activities are aligned with the organization's risk management strategy, ultimately contributing to better governance, risk management, and control processes. This ultimately contributes to the achievement of organizational objectives.

APPENDIX 1

A typical internal audit plan will have the following sections:

- a) Executive Summary - Summary of the most significant risks, the planned engagements and basic schedule, and the staffing plan.
- b) Policies and Processes - Basic description of the processes used to establish the audit universe, perform the risk assessment, coordinate assurance coverage, and the staffing requirements.
- c) Risk Assessment Summary - Description of the risk assessment process and results
- d) Overview of Planned Engagements - This section should show a list of proposed audit engagements, the scope and objectives of the engagements as well as the timing and duration of the proposed engagements
- e) Assurance Coverage and Exclusions - This section includes an assurance map, summary or other tool to communicate assurance over significant risk areas. The section should also include an acknowledgment of auditable units or risk areas that are not addressed as well as recommendations for assurance via co-sourcing or outsourcing options.
- f) Rationale for inclusions and exclusions - This explanation includes information such as changes in risk rating, length of time between audit engagements, and management changes.
- g) Resource Plan - This section contains a description of the type and quantity of resources needed to execute the plan. This description may include the number of staff required to complete the audit plan (capacity), the number of support staff needed, a summary of the results of the skills assessment, and a plan of action to address the skill gaps.
- h) Financial Budget Requirements - The plan should include a financial plan to cover the payroll of internal audit staff, the cost of co-sourced or outsourced services (if any), audit tools and technology, training, and other expenses.
- i) Approval Sign-off Area - The plan must be approved by senior management and the board.

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