

internal | audit **help packet**



Association of Credit Union Internal Auditors

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Thinking About Starting an Internal Audit Function?

The Association of Credit Union Internal Auditors takes pride in providing this internal audit information packet to interested credit unions.

This information is a compilation of ideas and documents provided by the members of ACUIA. We believe it will be beneficial to credit unions starting an internal audit function and to internal auditors themselves. This packet contains a variety of information and sample documents covering such topics as job descriptions, internal audit charters, audit plans, organization charts, publication sources, and much more. The documents included will provide useful guidelines, but do need to be adapted to fit the requirements and circumstances in each credit union.

While we have tried to anticipate your questions, we realize you may have some that are not covered in this information. We encourage you to contact ACUIA's Executive Office at (866) 254-8128 and they will provide you with a list of members who can answer any questions you may have regarding the internal audit function. Our members also have made personal visits to interested credit unions.

The Association of Credit Union Internal Auditors and its members hope this packet, offered as a free service, will help strengthen your credit union and the credit union industry through the promotion and support of internal auditing.

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What Is Internal Auditing?

The Institute of Internal Auditors (IIA) is an international association dedicated to the continuing professional development of the individual internal auditor and the internal auditing profession. Standards for the Professional Practice of Internal Auditing are issued by the IIA to provide guidance for internal auditors. The following are a definition and objective of internal auditing as described by the IIA. For more information contact the IIA at (407) 830-7600 or <http://www.theiia.org>.

Definition of Internal Audit

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.

Objective of Internal Audit

The internal audit activity should monitor and evaluate the effectiveness of the organization's risk management system.

The internal audit activity should evaluate risk exposures relating to the organization's governance, operations, and information systems regarding:

Reliability and integrity of financial and operational information.

Effectiveness and efficiency of operations.

Safeguarding of assets.

Compliance with laws, regulations, and contracts.

As contrasted with internal auditing of the past, today's profession is broad-scoped. It embraces not just the traditionally accepted view of internal auditing but also related services such as consulting, assurance, and control self-assessment. It thereby provides greater value by delivering accurate and reliable information to management and the audit committee.

How Do We Hire an Internal Auditor?

According to and reprinted with permission from the *National Credit Union Administration Supervisory Committee Guide*, Revised December, 1999:

Section 6.05 — There are several methods of employing an internal auditor. There are national, regional, and local organizations of internal auditors that may serve as resources for finding appropriate internal audit employees. Smaller credit unions with limited resources may want to consider sharing an internal auditor with other small credit unions on a consulting basis. Under these arrangements, you generally contract for a quantity of hours of the internal auditor's time. It is important that you hire a qualified individual to carry out this critical responsibility.

What Qualifications Should Our Internal Auditor Have?

Section 6.06 — Your internal auditor's qualifications should be commensurate with the size and complexity of your credit union. All internal auditors should possess:

Academic credentials and/or technical training and proficiency.

A commitment to continuing education and professional development.

Well-developed written and oral communication skills.

Independence.

Continuing Professional Development

Your internal auditor's continuing education is vital for ensuring efficient and effective audits with recommendations that enhance the overall operations of the credit union.

Sample Job Description

JOB TITLE: Internal Auditor

GRADE RANGE: 10/1 to 12/10

DIVISION: Internal Audit

REPORTS TO:

Supervisory Committee (Functionally), President (Administratively)

GENERAL SUMMARY:

Responsible for providing internal audit coverage of all credit union activities. Through continuous audits determines internal controls to provide adequate safeguards to ensure the credit union's general operating efficiency and compliance with laws, regulations, managerial policies, and generally accepted accounting principles.

MAJOR DUTIES AND RESPONSIBILITIES:

1. Develop and maintain a plan for auditing all credit union activities. Continually assess risks, member complaints, findings, and recommendations of outside auditors and National Credit Union Administration (NCUA) examiners, and changes in policies and regulations to effectively prioritize audit coverage. Solicit management for suggestions for audit and obtain supervisory committee approval of audit plans.
2. Develop and maintain audit programs for each audit area, continually evaluating the effectiveness of programs. Audit programs should identify objectives, planned scope of coverage, and procedures to be performed. Obtain supervisory committee approval of audit programs and revisions.
3. Gather and analyze data, and report audit results in accordance with Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.
4. Discuss audit findings and recommendations with president and supervisory committee. Prepare results of audits, communicating stature of operating conditions including recommendations for improvements to the president and supervisory committee.
5. Conduct special projects requested by supervisory committee.
6. Review planned changes in operating procedures and data processing conversions for audit integrity and adequacy of internal controls.
7. Identify training opportunities to improve staff understanding of control procedures.

SCOPE, PURPOSE, AND FREQUENCY OF CONTACT:

Within the Department:

N/A

Outside the Department:

Frequent contact with CU personnel

Direction of Others:

None

Direction Received:

Minimal supervision, exercising initiative within established guidelines and procedures. Confers with the supervisory committee and president as necessary.

Education Requirement:

College degree and a minimum of 24 college hours of accounting.

Experience Requirement:

Previous audit experience necessary with credit union exposure preferred.

8. Coordinate internal audit activities with that of the public and NCUA examiners.
9. Continue professional development through training and participation in professional organizations. Complete at least 40 hours of continuing education and training each year that contributes to professional proficiency.
10. All other duties that may be assigned.

Sample Job Description

JOB TITLE: Internal Audit Assistant

DIVISION: Administration

REPORTS TO: Internal Auditor

GENERAL SUMMARY:

The internal audit assistant will assist the internal auditor in providing internal audit coverage of all credit union activities. Through continuous audits determines internal controls to provide adequate safeguards to ensure the credit union's general operating efficiency and compliance with laws, regulations, managerial policies, and generally accepted accounting principles.

MAJOR DUTIES AND RESPONSIBILITIES:

1. Responsible for completing audits as assigned by the internal auditor.
2. Gather and analyze data, and report audit results in accordance with Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.
3. Responsible for interviewing credit union staff as needed to gather relevant information to complete assignments.
4. Communicate information, suggestions, and/or problems regarding audit status and critical findings throughout the assignments to the internal auditor.
5. Create all work papers to show what was done, the procedures and methods used, and the conclusion or the results of the work performed in an organized manner.
6. Support the efficient operation of the audit department as directed by the internal auditor, NCUA, and external auditors to expeditiously complete their assignments.
7. Submit recommendations for increasing or decreasing audit steps.
8. Maintains the confidential nature of all work papers and information obtained during an audit.
9. All other duties that may be assigned.

SCOPE, PURPOSE, AND FREQUENCY OF CONTACT:

Within the Department:

Frequent contact with internal auditor

Outside the Department:

Frequent contact with CU personnel

Direction of Others:

None

Direction Received:

Moderate supervision, exercising initiative within established guidelines and procedures.

Education Requirement:

Accounting student who has completed at least 6 hours of college level accounting. Preferably has completed Intermediate Accounting I. Must meet all requirements in the College of Business Administration Internship Program.

EXPERIENCE REQUIREMENT:

Previous work experience necessary, with accounting or auditing exposure preferred. Working knowledge of Microsoft Word and Microsoft Excel required.

INTERNSHIP PROGRAM RESPONSIBILITIES:

Student's responsibilities include: Work a minimum of 240 hours per semester; Keep a daily diary of work activities; Write paper relating class studies to internship experience; complete an appraisal of the employer.

Credit Union's Responsibilities:

Verify the intern's work environment and duties.
Complete an appraisal of the intern's performance.
Possibly be visited once (at the place of employment) by the faculty internship coordinator.

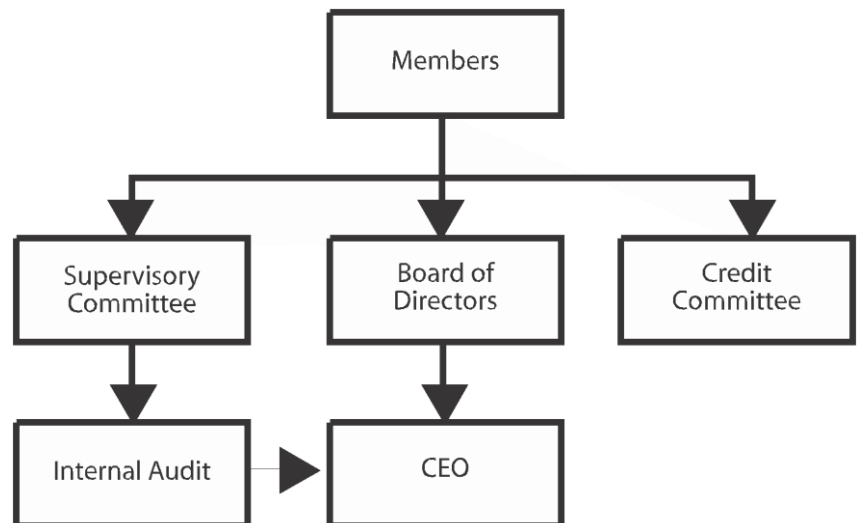
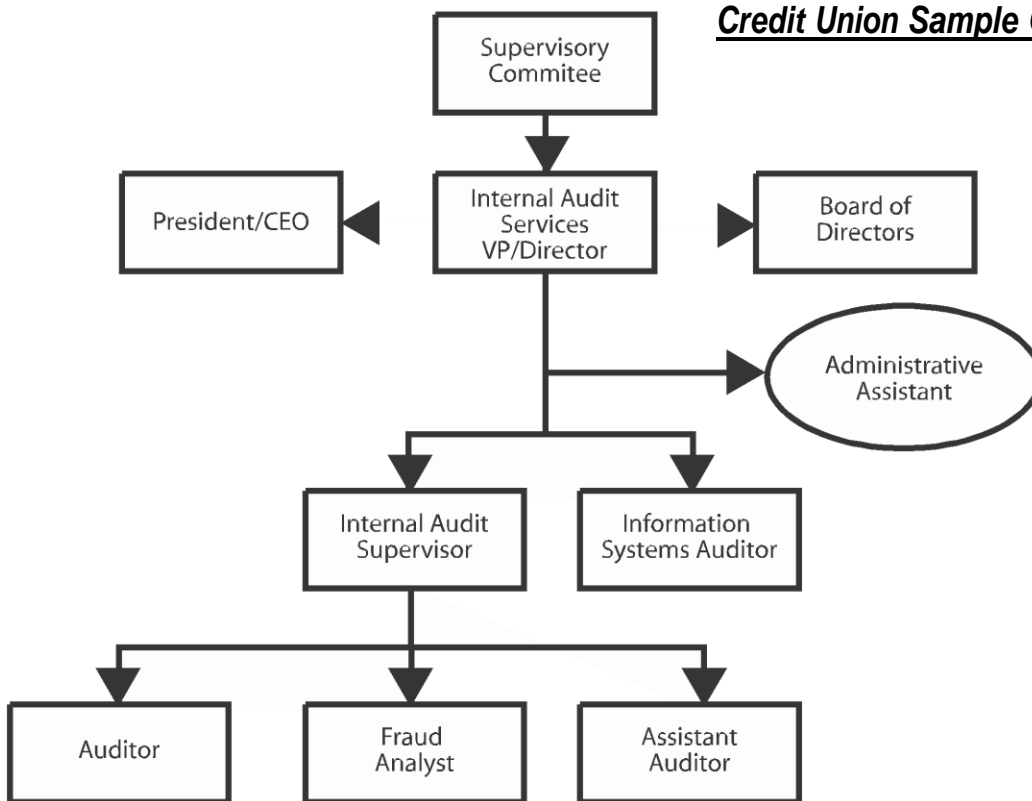
Organization Structure

According to and reprinted with permission from the National Credit Union Administration *Supervisory Committee Guide*, Revised December, 1999:

Independence. Independence is defined as “freedom from the influence, guidance, or control of another or others.” An internal auditor’s independence is vital to achieving reasonable assurance that internal controls are functioning properly, will safeguard the assets of the credit union and prevent and detect errors and irregularities.

One measure of an internal auditor’s independence is the auditor’s location within the organizational structure of the credit union. The internal auditor should report directly to you, the supervisory committee. The organizational status of the internal auditor speaks to objectivity. It is important to note the only way the internal audit function can operate effectively and add value to the credit union (in meeting regulatory audit and verification requirements) is by ensuring the reporting relationship is at a very high level.

Credit Union Sample Organizational Charts



Develop an Internal Audit Mission

In order to be effective, the internal auditing department must develop and implement an internal audit mission. Good planning in development of the internal audit mission will serve to reduce stress and increase management acceptance of the audit function.

The internal audit mission contains the mutually agreed upon responsibilities of the internal audit department. To be complete, the mission should include the following documents:

- *Departmental charter*
- *A set of internal auditing standards*
- *A set of procedures*
- *Audit guidelines*

Departmental Charter

The audit charter is the key document and becomes the job description for the internal audit function. It serves the following purposes:

- *Formalizes the internal audit department*
- *Documents scope, responsibilities, authority, and professionalism of the auditing department*
- *Can be measured against professional standards to determine the adequacy of anticipated internal auditing*
- *Forms the basis for implementing departmental policies, procedures, and guidelines*
- *Provides affected parties within the credit union with an explanation of the internal audit mission*
- *Provides the credit union's independent public accountants with a basis to evaluate the internal auditor's independence and possible reliance on their work*
- *Can serve as a marketing tool to promote cooperation within the credit union.*

Responsibility for Developing the Audit Department Charter

The internal audit director is responsible for preparing the audit charter. The charter should be prepared before any staff is hired. The following provides a checklist of items and issues to be addressed in this process:

1. Obtain management concurrence to develop a charter.
2. Gather the information needed to develop the charter.
 - 2.1. Acquire professional internal auditing documents.
 - 2.2. Examine copies of other internal auditing charters.
 - 2.3. Learn from other internal auditing departments.
3. Define the various parts of the charter.
 - 3.1. Scope.
 - 3.2. Authority.
 - 3.3. Responsibility.
 - 3.4. Guidelines for the conduct of audits.
4. Cross-reference the charter to the standards chosen by the department to follow.
 - 4.1. Do the standards encompass all the standards chosen?
 - 4.2. Can all items in the charter be cross-referenced to one or more standards?
 - 4.3. Do the wording and intent of the charter meet the wording and intent of the standards?
 - 4.4. Does the charter support the mandate and expectations of management and the board?
5. Final draft charter.
 - 5.1. As a rule, the charter should not exceed two pages in length.
 - 5.2. Should be subdivided into major parts.
 - 5.3. Must use clear, easy to understand language.
 - 5.4. Should be clear in respect to authority and responsibility.
6. Secure management and board approval of the internal audit charter.
 - 6.1. Approval must be included in the board minutes, and signed and dated by the chair and/or the audit committee chair.
 - 6.2. The audit director must be confident that senior management and the board fully support his mandate and are willing to state publicly that they are prepared to support the department with the resources and staff required to achieve the goals and objectives as outlined in the mandate.

2.3.1. Do not try to reinvent the wheel. When contacting other audit departments, you should try to interview the following:

Internal audit director;
The senior manager to whom the director reports;
Internal audit supervisors and senior auditors
Supervisory committee/audit committee members;
Public accountants.

Internal Auditing Standards

Internal auditing within the credit union should be measured against specific standards. For instance, the Standards for the Professional Practice of Internal Auditing as issued by the IIA.

The standards form the basis for measuring performance and audit quality. The standards adopted by the internal audit department should be the basis for implementing the charter.

Audit Procedures

Procedures explain what the auditor should do and how the auditor should perform these tasks.

Audit Guidelines

Guidelines contain suggestions for ways of accomplishing specific audit tasks. Guidelines are considered best practices.

Dealing with Senior Management and the Board

The following is a summary of a chapter found in *The New Internal Auditing* published by Roland press. It provides some interesting insights to dealing with the board and senior management.

- The first concern of every CEO is the smooth working of his top executive team.
- Management needs to be in charge in order to fulfill its responsibilities.
- Management's foremost challenge is leadership.
- Management dislikes surprises because surprises represent a loss of control over events.
- Internal auditing has become increasingly involved in corporate leadership without benefit of a positive theory to support its actions.
- Helpful auditing consists in allowing management to maintain the initiative.
- Internal auditors need to interface with management based on management time—not audit time.
- Management has its own peculiar definition of what constitutes a “problem.”
- Boards of directors are extremely hesitant to interface in the day-to-day management of the corporation.
- Board audit committees are a poor mechanism for solving problems. Their role is to ensure that problems are solved by management.

- There is a difference between working for someone and reporting to someone. Internal auditing reports to senior management and the board, but seldom works for them.
- The internal auditor is not the ultimate arbiter of what audit disclosure should be in the corporation. He must base his disclosure patterns on the “demand” for disclosure within the organization.
- Disclosure is a means - not an end in itself.
- Internal audit executives must see to it that disclosure practices fit the needs of the emerging environment. The official pronouncements of the IIA give audit directors considerable latitude in this area.

The new internal auditing proposes to make interaction with the audit function a more attractive proposition for operating management and auditees. It proposes to essentially cut off adverse disclosure at the point where assurance of corrective action is provided. Adverse disclosure to a higher level for purely informational purposes will be curtailed to the fullest extent permitted by management and the board audit committee.

Audit Charter Checklist

In order to be truly effective, the purpose, authority, and responsibilities of the internal audit department must be fully documented and agreed upon by audit management, senior

management, and the board of directors. This understanding is best documented in a well-crafted and articulate audit charter.

Audit Charter Checklist

	Y/N
1) Authority	
a) Does the charter clearly establish the department's position within the credit union?	
b) Does the charter define the scope of internal auditing activities?	
c) Does the charter authorize access to all record, properties, and personnel?	
2) Responsibility	
a) Does the charter outline responsibilities for serving management in a fashion consistent with the professional standards and code of ethics of the IIA or other professional auditing body?	
3) Independence	
a) Does the charter establish the reporting relationship of the department head?	
b) Does the charter require the department head report to a senior officer of the credit union, whose position and authority ensures the independent operation of the audit department?	
c) Does the charter require direct communication with the audit/supervisory committee on a regular basis? If so, does the charter require the following	
d) Attendance and participation in regular audit committee meetings?	
e) Submission of annual work plans, staffing requirements, and scope and objectives of major audit projects?	
f) Periodic submission of activity reports and significant audit findings?	
g) Does the charter require the concurrence of the audit/supervisory committee in the appointment or removal of the department head?	
4) Scope Of Work	
a) Does the charter provide sufficient flexibility for the department head to ensure that the nature, scope, and timing of audit activities are consistent with the standards of the appropriate professional audit body?	
5) Reporting	
a) Does the charter set forth standards as to the type and form and frequency of reports to be prepared by internal audit?	

Sample Audit Charter*

(a) Policy Statement

It is the policy of XYZ Credit Union to maintain an internal audit department as a means of providing the supervisory committee and all levels of management with information to assist in the control of operations and to assist senior management in reaching a conclusion concerning the overall control over assets and the effectiveness of the system of internal control in achieving its broad objectives. Additionally, the internal audit department will review the effectiveness and efficiency of operations and organizational structures.

(b) Responsibility of the Internal Auditor

The internal auditor is responsible for properly managing the department so that (1) audit work fulfills the purposes and responsibilities established herein; (2) resources are efficiently and effectively employed; and (3) audit work conforms to the Standards for the Professional Practice of Internal Auditing.

(c) Reporting and Relationship to the Supervisory committee

The internal auditor will report to the supervisory committee for approval on audit scope, policy, and administration. He/she will report in writing on all internal audits conducted in the credit union and will attend the committee meetings to report on significant recommendations and the operations of the internal audit function. The internal auditor will report to the president and CEO on all administrative matters.

(d) Independence

Independence is essential for effective operation of the internal audit function. It is the policy of the credit union therefore, that all audit activities shall remain free of influence by any organizational elements. This shall include such matters as scope of audit programs, the frequency and timing of audits, and the content of audit reports.

(e) Scope of Audit Activities

Audit coverage will encompass, as deemed appropriate by the internal auditor, independent reviews and evaluations of any and all management operations and activities to appraise:

Measures taken to safeguard assets, including tests of existence and ownership as appropriate;

The reliability, consistency, and integrity of financial and operating information;

Compliance with policies, plans, standards, laws, and regulations that could have significant impact upon operations;

Economy and efficiency in the use of resources;

Effectiveness in the accomplishment of the mission, objectives, and goals established for the credit union's operations and projects.

Assist management in conducting fraud investigations.

Audit activities will be coordinated, to the extent possible, with the public accountants so as to enhance audit efficiency.

(f) Access and Confidentiality

In accomplishing his activities, the internal auditor and his staff are authorized to have full, free, and unrestricted access to all credit union functions, activities, operations, records, data files, computer programs, property, and personnel. Under appropriate circumstances, the internal auditor is specifically authorized to communicate directly to the president, and/or the board of directors. It is expected that the internal auditor and his staff will exercise discretion in the review of records to ensure the confidentiality of all matters that come to their attention.

(g) Responsibility for Corrective Action

The manager or head of the division, department, unit, or site audited is responsible for seeing that corrective action on recommendations made or deficient conditions reported by the auditor is either planned or taken. The internal auditor is responsible for presenting a report on significant matters to the president, the supervisory committee, and the board of directors.

(h) Limitation of Authority and Responsibility

In performing their functions, the internal auditor and audit staff members have neither direct authority over, nor responsibility for, any of the activities being audited. Internal auditors will not develop and install procedures, prepare records, make management decisions, or engage in any other activities that could be reasonably construed to compromise their independence.

In connection with the complementary objectives of the audit function, internal audit will recommend accounting or other operational policies and procedures for approval and implementation by appropriate management. Therefore, internal audit review and appraisal do not in any way substitute for other activities or relieve other persons in the organization of the responsibilities assigned to them.

Approved this _____ day

of _____,
XXXX

Chairman, Supervisory Committee

Chairman, Board of Directors

*Note: Adapted from *Managing the Audit Function*; Michael P. Cangemi, CPA, CISA; 1996; John Wiley & Sons, Inc.

What is the Audit Plan and What Should it Include?

According to and reprinted with permission from the National Credit Union Administration Supervisory Committee Guide, Revised December, 1999:

Section 6.07 A sample supervisory committee work plan has been provided in Chapter 4, appendix 4A. The internal auditor's audit plan should generally be the work anticipated to be completed within the next year. However, the frequency of an audit of certain operational areas or functions should be based on the attendant risk factors. The plan should have a degree of flexibility to allow for audits of the adequacy of controls within new systems and/or significant changes to existing systems. An evaluation by the internal auditor should be part of

contemplated changes and modifications to systems and functions.

When determining the scope of work, the internal auditor must consider: (a) size and scope of the operation or function relative to the size and complexity of the credit union; (b) the existence of appropriate written policies and procedures; (c) the effect potential losses would have on the financial condition of the credit union.

Further information on risk assessment can be found in the "Internal Auditor Tool Kit: Risk Assessment," published in 1990 by the IIA.

Risk Based Audit Planning Checklist

The internal audit department is no different than any other efficiently run business. In order to ensure the efficient and effective and timely use of resources, the audit department

needs a plan. This includes the assessment of risk and the allocation of resources.

Risk Based Audit Checklist

Risk Based Audit Checklist	Y/N
1) Phase 1 - Assessment of Audit Risk	
a) Does the plan break the credit union down into logical business processes or units?	
b) Does the plan define the audit universe as a group of business process in a fashion similar to management?	
c) Does the plan include the development of appropriate risk criteria and assigned weighting for risks such as: <ul style="list-style-type: none"> i) Quality of internal control ii) Flow of funds iii) Asset liquidity iv) Public disclosure implications v) Management interest vi) Complexity of operations vii) Management viii) Results and time since the last audit ix) Audit plan of external auditors x) Changes in systems, processes, procedures, staff and management 	
d) Does the plan incorporate a risk-weighted evaluation/model for each process identified in a) above using the criteria in c) above?	
2) Phase 2 - Allocating Resources	
a) Has a risk strategy been developed enabling a broad-based audit approach?	
b) Does the plan divide the risk rated audit universe into high, sensitive, moderate, and low risk categories?	
c) Are all high-risk areas audited? Does the plan allow for annual coverage of 25% of the processes identified in Phase 1?	

Audit & Risk Management Services Mandate

General Policy

XYZ Credit Union has established the audit and risk management services department to assist members of management and the board of directors in the effective discharge of their responsibilities and to increase and enhance the effectiveness of XYZ's operational loss prevention efforts.

To this end, audit and risk management services provides an independent appraisal function to examine and evaluate company activities and furnishes the board and management with analysis, recommendations, counsel, and information regarding the activities reviewed.

For the purposes of this mandate, the vice-president of audit and risk management services is referred to as the vice-president.

Organizational Status

While audit and risk management services is an integral part of the company and functions within the policies established by senior management and the board of directors, it is essential for internal auditors and the vice-president to be independent of the activities reviewed. To enhance and ensure this independence, audit and risk management services have full, free, and unrestricted access to all relevant records, personnel, and properties.

The audit and risk management services department has an independent functional responsibility to the audit committee of the board of directors for the adequacy and effectiveness of internal and operational controls. The vice-president is expected to attend and provide counsel at all audit committee meetings, and as a senior manager, attends regular meetings of the board of directors. In addition, the vice-president meets in camera at least once a year with the audit committee.

Administratively, the audit and risk management services department reports through the president and chief executive officer.

Scope Audit

The audit scope encompasses examining and evaluating the adequacy and the effectiveness of the company's system of internal and operating control, and the quality of operating performance against established standards in carrying out assigned responsibilities. The scope of the examination and evaluation performed in areas of the company includes the review of:

The reliability and the integrity of financial and operating information and the means used to identify, measure, classify, and report information.

The systems established to ensure compliance with policies, plans, procedures, laws, and regulations that

could have a significant impact on operations and reports, including determining whether the organization is in compliance.

The means of safeguarding assets and verifying their existence.

The economy, efficiency, and effectiveness with which resources are employed.

Operations or programs to ascertain whether results are consistent with established objectives and goals and whether operations or programs are being carried out as planned.

Organizations within the company at appropriate intervals to determine whether they are efficiently and effectively carrying out their functions of planning, organizing, directing, and controlling in accordance with management instructions, policies, procedures, and in a manner that is consistent with both company objectives and high standards of administrative practice.

The scope of the examination also includes:

Participation in the planning, design development, implementation, and operation of major computer-based systems to determine whether:

Adequate controls are incorporated in the systems;

Thorough system testing is performed at appropriate stages;

Systems documentation is complete and accurate.

The conduct of data center reviews and post-installation evaluations of major data processing systems to determine whether these systems meet their intended purposes and objectives.

The review of the adequacy and testing of the corporate and IS disaster recovery plans.

Participation in the planning and performance of audits of potential acquisitions with the company's external auditors and corporate staff.

Provision of professional assistance when required by the external auditors.

Risk Management

The scope of the risk management services includes, but is not limited to:

Identifying risk and security exposures in all operational areas and ensuring that the necessary corrective actions are taken;

AUDIT AND RISK MANAGEMENT SERVICES MANDATE CONTINUED

Ensuring that adequate risk management and security training programs including policies and procedures are available for all credit union staff;

Implementing and periodically updating the credit union's kidnap/extortion plan and business resumption plans;

Implementing and periodically updating the credit union's money laundering monitoring and reporting procedures;

Managing the corporation's insurance portfolio in an efficient and effective fashion;

Directing all claims-related activities;

Liaison with credit union employees on security-related matters and with local police forces, equipment suppliers etc.;

Fraud, robbery, and theft investigation and resolution;

Money laundering and mandatory suspicious transaction reporting;

Coordinating loss prevention programs administered in-house, by CUCO, and by casualty insurers (e.g. fidelity bond program, physical security program, certification program, etc.);

Developing corporate risk awareness throughout the credit union;

Fostering communications by receiving and disseminating all fraud warnings and other risk management briefs and communications.

external, forgery, counterfeiting, money laundering).

Money laundering investigation and resolution, including statutory compliance and reporting.

Robbery and theft investigation and resolution.

Design, installation, and maintenance of corporate and branch physical security devices including corporate card access, alarms, vaults, and video surveillance equipment.

Corporate document security.

Approved by the Audit Committee of the Board of Directors
(Insert Month, Day, Year)

Examples of Risk Management & Security Activities Covered Under This Mandate

The following list provides examples of risk management and security activities addressed by this mandate.

Fidelity bonding, robbery protection, officers', and directors' liability coverage.

Bonding certification programs and equipment certification programs.

Property and casualty coverage including credit insurance, business interruption coverage.

Kidnap and ransom coverage, policies & procedures.

Business resumption planning.

Fraud investigation and resolution (internal, member,

The Next Step in Risk Management

Auditors have been trained to make detailed examinations of the internal control system, recommend cost-effective actions for improving internal control, and focus their audit planning, testing, and reporting on internal controls in the business process. As a result, the natural inclination of most internal auditors is to start with the auditable unit's internal control system, rather than with its purpose. In other words, they audit from right to left. Unfortunately, when internal auditors start with controls, rather than from purpose, they are likely to be auditing the wrong things.

Control models such as COSO in the United States, Cadbury in the United Kingdom, COCO in Canada, and the King Report in South Africa have been huge milestones in the progress of internal auditing and governance. Adoption of the COSO framework marked the first time ever that all stakeholders came to agree on a definition of internal control. As a result, the major governance professions reached a common understanding and made integration possible.

These models now need to be extended, however, so that internal auditors can use them differently and take the next step in risk management. Risk-based auditing (RBA) can address some of the important questions that controls-based auditing leaves unanswered. RBA is a major step toward improved internal audit performance and organizational risk management. Internal auditors who have made the change to RBA have found increased management acceptance and greater integration of the internal audit with other governance elements of risk management.

The limitations of control-based auditing evaluating controls without first examining the purpose of the business process and its risks provides no context for the results. How can the internal auditor know which control systems are most important, which are out of proportion to their risk, and which are missing? Even the staunchest advocates of control-based auditing must admit to its limitations.

Organizational Plaque

When controls are the central theme of the internal audit, more and more audit reports and recommendations are generated for improving and strengthening internal controls. Over time, layer upon layer of controls are built up, creating a type of "organizational plaque." These excessive layers of control slow down business processes. Communication becomes more difficult, and too many people are employed in non-value-adding work. Drastic measures are usually necessary to remove the built-up layers of excessive internal control.

Out of Sync

Starting with the controls creates a bias for the present and past at a time when most organizations are oriented toward the future and constant change. Auditors are typically looking at control activities designed at some previous time to deal with issues that may have been long forgotten, which

means that the internal auditor is examining activities that may or may not be relevant to current risks. The controls could be extraneous because they monitor things that are no longer important or even in existence. What's worse is that essential controls could be overlooked; they do not yet exist because of changes in the business processes.

Managers now expect audit work to add more value, which they interpret to mean more anticipation of future events. What transpired six months ago has decreased in relevance as the pace of change quickens. Managers operate in the present and future, and internal auditors need to make changes to support management's efforts.

During times of rapid change, organizations need a fluid process built on the possibilities of risk. Static control structures based on limits tend to hold the organization back. IIA Chairman Jean-Pierre Garitte recently spoke about these types of issues. He noted that the future of internal auditing must include negotiating involvement early in the strategic planning process; advancing the timing of our involvement in the business process; and redefining the scope of our services to reflect alliances and cooperation with other service providers on the governance team.

Many internal auditors have started to use control self-assessment (CSA) as a way to address some of management's concerns. CSA attempts to capture the present state of the business process in terms of both risk and control. However, control models limit and define CSA; so CSA applications often start with controls—the "right-to-left" internal audit approach. Often risks are discussed only as a justification for the controls examined. CSA is typically an improvement over traditional internal auditing of past events, but it is limited as a tool for exploring the future.

Irrelevant

Business controls do not remain flexible and relevant simply because they are regularly examined, but because they are linked to current organizational objectives. Auditing from right to left is basically an examination of controls; risks are used to justify the importance of a control, rather than the other way around.

Audit reports that start with controls, end with controls. Selling the cost of additional control to managers is a tough job in rapidly changing business processes. Audit customers resent what they see as meaningless controls "tacked on" to their business processes, slowing them down. Control models and control-based internal auditing are not satisfactory responses to the needs of today's organizations.

Risk-Based Auditing Changes Everything

RBA changes the way internal auditors think and talk about control and risk. Suddenly, the internal auditor is anticipating change and examining how management is dealing with risks. Instead of focusing on history, audit reports address the present and the organization's level of preparedness to deal

with the future. Internal audit reports, “complete the loop” between assurance of control in current operational plans and input to risk assessment for the strategic plan. Management places much more value on risk-based internal audit reports than on traditional controls-based reports.

Risk-based auditing relies on the COSO approach except that the final step is managing risk instead of determining controls. RBA looks at all the ways managers deal with risks. For example:

- Controlling organizational activities still represents more than 90 percent of risk management strategies.*
- Avoiding risk involves redesign of the business process to change the inherent risk pattern.*
- Diversifying risk means spreading the total risk over a number of separate operations, such as sourcing critical raw materials from several suppliers.*
- Business continuity plans often utilize this technique.*
- Sharing and transferring risk usually involves a contractual arrangement with another party to accept some or all of the financial risk in exchange for a fee.*
- Insurance is an example of these techniques.*
- Accepting risk separates RBA from most other audit approaches. Allowing some risk is necessary for progress and profits, yet most internal auditors are reluctant to validate management’s acceptance of prudent risks.*

Risk-based auditing moves from left to right along the COSO sequence. There is no tendency, as exists in controls-based auditing, to jump prematurely to the control activities step. RBA starts with the auditable unit’s objectives, moves through the risks, and then addresses how those risks are managed.

Bob Skees, Vice President-Internal Audit for Lowe’s Companies, Inc. and an RBA advocate, relates: “Going from left to right, from objectives through risks to how those risks are managed, has made a big difference in the way our management relates to internal audits.” Skees also notes that RBA supports and is consistent with the CSA initiatives at Lowe’s.

Internal auditors all over the world are adopting various forms of risk-based auditing, as are most of the large public accounting firms providing internal audit services. The spread of RBA is an important next step toward improved internal audit performance and integrated risk management.

Mandates for Change

A clear sign of impending change is that what used to work doesn’t function so well anymore. All of the indicators are present for a paradigm shift. Negative indicators include growing dissatisfaction with the current definition of internal auditing, the recognized need for an expanded approach to IIA Standards, and the rapid rise of internal audit outsourcing as a common strategy.

Positive indicators of change include recent developments in risk management practices within corporate governance:

- Growth in the number of reports at conferences and in the literature citing great results from risk-based audits.*

Successful integration of governance resource in internal audit and risk management planning in a number of companies worldwide.

Elevated positions for risk managers, including an officer-level chief risk manager in many organizations.

Changes are already under way for many fundamental documents of the internal audit profession. The risk management concept first appeared in the draft definition of internal auditing that will replace the IIA Statement of Responsibilities. Even with the current changes in the definition of internal auditing and a new framework for IIA Standards, more work remains to take the profession to a level beyond COSO and the other control models.

The Need for a Risk Model

As the century draws to a close, internal auditors have seen the zenith of internal control as a basis for managing organizations. They are now exploring the new risk-based practice of internal auditing as the way of the future. The internal audit profession is poised for a dramatic breakthrough as a vital force in corporate governance. All we need to do is to take the next step.

What the internal audit profession needs more than anything is a business risk framework that encompasses all of our notions about risk and risk management. This framework is the next step in an integrated internal audit and risk management process.

In 1995, the Australia/New Zealand Joint Standards Board issued the world’s first consensus national standard on risk management, AS/NZS 4360. The Canadian Standards Association followed in 1997 with CAN/CSA Q850-97, Risk Management: Guideline for Decision Makers; and the Japanese and the International Standards Organization are both rumored to be working on separate drafts of similar standards.

Experience in Australia has shown that these standards cannot be directly used to provide a risk framework for internal auditors, but they do provide a building block. To complete the next step, the assurance and risk management stakeholders in corporate governance will need to come together, as the control specialists did under COSO, and build a new and broader foundation for the profession of internal auditing based on the risk management principles.

*Reprinted from Internal Auditing Alert
By: David McNamee and Georges Selim*

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McNamee and Selim are co-authors of a new book, Risk Management: Changing the Internal Auditor’s Paradigm, published by The Institute of Internal Auditors Research Foundation.

Sample 200X AUDIT PLAN

Calculation of Available Hours:

365 days x 8 hours =	2,920
Less weekends (104 X 8) =	(832)
Less holidays (10 X 8) =	(80)
Total hours per individual (full 12 months) =	2,008

	Employee #1 (start 03/15/XX)	Employee #2 (start 01/01/XX)	Employee #3 (start 03/12/XX)	Employee #4 (start 04/25/XX)
Available hours	1,476	2,008	1,690	1,411
Less Paid Time Off (PTO)	128	200	160	152
Less Schools & Conferences	-150	-100	-100	-100
Subtotal	1,454	2,108	1,750	1,463

Continuing Audit Work:

Meetings	265	150	100	100
Special Projects, to include:	175	100	165	245
- XP Report Writer Training				
- CUSO Audits				
- Emerging Issues & Training				
Compliance Program Administration	135	20	50	170
Security Program / Administration	100	20	210	0
Administrative Tasks *	120	150	200	20
Report Review **	60	223	200	100
Accounts Verification (as of 12/31/00)	39	40	20	20
NCUA Exam Assistance	20	40	20	10
Annual External Audit Assistance	40	60	5	5
CIA Test Review	0	150	0	0
Subtotal	954	953	970	670

Additional Audit Hours Available	500	1,155	780	793
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Targeted Audits:

Branches (10)	60	395	170	100
Quarterly Loan Review (4)	30	0	280	203
First Mortgage Review	30	0	0	60
Fraud Prevention	60	20	80	0
Call Center	25	80	0	0
Collections Department	25	0	0	120
CUMIS / IT	15	15	0	0
Indirect Lending	5	90	0	10
Accounting Bank Accts & Central Ops	30	100	0	10
Credit Cards/ ATM Department	5	60	0	0
Corporate Credit Cards	5	40	0	0
Travel & Conference	5	40	0	0
Insurance Claims (Death & Disability)	5	45	0	15
Titles & Insurance Department Review	5	0	0	60
General Ledgers	100	200	100	90
Compliance Audit	15	0	0	75
Fixed Assets Audit	10	10	150	0
ACH Audit / Wire Transfer Review	10	60	0	40
Southeast Switch Audit	60	0	0	10
Subtotal	500	1155	780	793

Time Remaining	0	0	0	0
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* Includes writing reports, employee reviews, dormant accounts, and general administrative work.

** Includes 90 days paid ahead report, daily member activity report, supervisory override report, money laundering report, general ledger, and ATM card issuance log report.

Sample Audit and Risk Management Services Status Report

Audit Area	Audit Pri.	Audit Budget	Current Time	Previous Time	YTD Time	Est. Var.	Est. TTC	Audit Status	Est. Start	Est. Finish	Report Date	Overall Opinion
Branch Audits:												
Sample City 1	M	85	-	-	-	85		N				
Sample City 2	H	85	-	-	-	85		N				
Sample City 3	M	80	-	-	-	80		N				
Sample City 4	M	80	-	-	-	80		N				
Sample City 5	M	80	-	-	-	80		N				
Sample City 6	M	80	-	-	-	80		N				
Sample City 7	H	80	-	-	-	80		N				
Sample City 8	H	80	-	-	-	80		N				
Sample City 9	H	80	-	-	-	80		N				
Sample City 10	H	85	-	-	-	85		N				
Sample City 11	H	80	-	-	-	80		N				
Sample City 12	M	80	-	-	-	80		N				
Sample City 13	M	85	-	-	-	85		N				
Sample City 14	M	80	-	-	-	80		N				
Sample City 15	M	80	-	-	-	80		N				
Total Branch Audits		1,220	-	-	-	1,220						
Corporate & EDP Audits:												
Staff & Director Loans	M	50	-	-	-	50		N				
Commercial Lending	H	150	-	-	-	150		N				
Treasury Internal Control	H	50	-	-	-	50		N				
DICO - MISAR	L	50	-	-	-	50		N				
RRSP/RRIF Processing	H	100	-	-	-	100		N				
Mutual Fund Compliance	H	320	-	-	-	320		N				
Disaster Recovery	H	70	-	-	-	70		N				
Change Control	M	35	-	-	-	35		N				
Data Centre Security	M	35	-	-	-	35		N				
Telecommunications	L	32	-	-	-	32		N				
Software Licenses	L	35	-	-	-	35		N				
SQL Database Balancing	M	35	-	-	-	35		N				
Interac Compliance	H	70	-	-	-	70		N				
Capital Expenditures	L	70	-	-	-	70		N				
Lan Administration & Access	M	70	-	-	-	70		N				
Internet Access Control	H	70	-	-	-	70		N				
Total Corporate & EDP Audits		1,242	-	-	-	1,242	-					
Operational Audits:												
Key Controls Review	M	70	-	-	-	70		N				
Delinquency Control	H	70	-	-	-	70		N				
Payment Processing	M	70	-	-	-	70		N				
Facilities	H	300	-	-	-	300		N				
Total Operational Audits		510	-	-	-	510	-					
Ongoing Audits:												
External Audit	L	100	-	-	-	100		N			NA	NA
Special Projects - Task Force	M	850	-	-	-	850		N			NA	NA
Special Projects - Program	L	150	-	-	-	150		N			NA	NA
Total Ongoing Audits		1,100	-	-	-	1,100	-					
Administration:												
Risk Management	NA	200	-	-	-	200						
Administration:	NA	600	-	-	-	600						
Vacations	NA	588	-	-	-	588						
Total Administration		1,388	-	-	-	1,388	-					
Grand Total		5,460	-	-	-	5,460	-					

Opinion

V Very Good
 S Satisfactory
 N Needs Improvement
 U Unsatisfactory
 NA Not Applicable

Status

N Not Started
 F Field Work Started
 R Draft Report Issued
 C Completed

Priority

L Low
 M Medium
 H High

Note:

TTC = Time To Complete
 Var = variance = YTD time + TTC - Budget

Sample — Employee #1

Audit Area	Curr. Time	Prev. Time	YTD Time	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Branch Audits:															
Sample City 1	0	0	0												
Sample City 2	0	0	0												
Sample City 3	0	0	0												
Sample City 4	0	0	0												
Sample City 5	0	0	0												
Sample City 6	0	0	0												
Sample City 7	0	0	0												
Sample City 8	0	0	0												
Sample City 9	0	0	0												
Sample City 10	0	0	0												
Sample City 11	0	0	0												
Sample City 12	0	0	0												
Sample City 13	0	0	0												
Sample City 14	0	0	0												
Sample City 15	0	0	0												
Total Branch Audits	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Corporate & EDP Audit															
Staff & Director Loans	0	0	0												
Commercial Lending	0	0	0												
Treasury Internal Control	0	0	0												
DICO - MISAR	0	0	0												
RRSP/RRIF Processing	0	0	0												
Mutual Fund Compliance	0	0	0												
Disaster Recovery	0	0	0												
Change Control	0	0	0												
Data Centre Security	0	0	0												
Telecommunications	0	0	0												
Software Licenses	0	0	0												
SQL Database Balancing	0	0	0												
Interac Compliance	0	0	0												
Capital Expenditures	0	0	0												
Lan Admin & Access	0	0	0												
Internet Access Control	0	0	0												
Total Corp. & EDP Audits	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Operational Audits:															
Key Controls Review	0	0	0												
Delinquency Control	0	0	0												
Payment Processing	0	0	0												
Facilities	0	0	0												
Total Operational Audits	0	0	0												
Ongoing Audits:															
External Audit	0	0	0												
Special Projects - Task Force	0	0	0												
Special Projects - Program	0	0	0												
Total Ongoing Audits	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Administration:															
Risk Management	0	0	0												
Administration:	0	0	0												
Vacations	0	0	0												
Total Administration	0	0	0												
Grand Total															

Regulatory Agencies

Rulemaking Agencies for US Credit Unions

Equal Employment Opportunity Commission (EEOC) -
Discrimination in Employment
Environmental Protection Agency (EPA) - Environmental
Hazards
Federal Emergency Management Agency (FEMA) - Flood
Disaster Protection Act and Flood Insurance
Federal Reserve System
Federal Trade Commission (FTC) - Joint Policy on
Discrimination in Lending and Privacy Act
Internal Revenue Service (IRS)
National Credit Union Administration (NCUA)
Securities and Exchange Commission (SEC) - Bank
Secrecy Act

State Agencies

U.S. Department of Housing and Urban Development
(HUD) - Lending
U.S. Department of Justice - Fair Lending Reviews
U.S. Department of Labor - Employment
U.S. Department of Transportation - Americans with
Disability Act
U.S. Department of the Treasury - Bank Secrecy Act

Federal Reserve Board

Regulation A - Advance to Member Banks on Their Notes
Regulation B - Equal Credit Opportunity Act (ECOA)
Regulation C - Home Mortgage Disclosure Act (HMDA)
Regulation D - Reserve Requirements
Regulation E - Electronic Fund Transfer Act
Regulation G - Securities Credit by Persons Other Than
Banks, Brokers, or Dealers
Regulation J - Collection of Checks and Other Items by
Federal Reserve Banks and Funds Transfers through
Fedwire
Regulation M - Consumer Leasing
Regulation T - Credit by Brokers and Dealers
Regulation Z - Truth-in-Lending
Regulation CC - Expedited Funds Availability Act
Federal Reserve Operating Circular #9 - Commercial
Payments Through Automated Clearing Houses

Internal Revenue Service

Backup Withholding - Forms W-9/W-8
Depositing Backup Funds Withheld
Depositing Employee Funds Withheld
Discharge of Indebtedness - Form 1099C
Dividend/Interest Reporting - Form 1099INT
Employee Withholdings - Form W-2
Federal Insurance Contribution Act - FICA
Federal Unemployment Tax
Foreclosures and Abandonment of Security - Form 1099A

Individual Retirement Accounts - Form 5498
Magnetic Media Reporting - Forms 1098/1099
Mortgage Interest Reporting - Form 1098
Original Issue Discount Reporting - Form 1099OID
Property Subject to Levy
Real Estate Transaction Reporting - Form 1099S
Record keeping Requirements for Employment Taxes

Department of Labor/ Equal Employment Opportunity Commission

Affirmative Action
Age Discrimination in Employment Act
Americans with Disabilities Act
Civil Rights/Equal Employment Opportunities
Employee Retirement Income Security Act (ERISA)
Employment Practices Record Keeping
Employment-Related Group Health Care Plan -
COBRA Family and Medical Leave Act
Minimum Wage/Overtime
Occupational Safety and Health Act (OSHA)
Polygraph Protection Act

Department of the Treasury

Bank Secrecy Act
Book-Entry Transactions Involving Treasury Securities
Counterfeit and Mutilated Currency
Currency Transaction Reporting
Federal Payments Through Automated Clearing Houses
Fiscal Agents and Treasury Tax and Loan Depositories
Savings Bonds
Federal Trade Commission
Fair Credit Reporting Act
Fair Debt Collection Act
Holder in Due Course Rules

Others

Anti-Discrimination Data Collection
Credit Unions on Military Bases
Employment of Aliens
Environmental Lender Liability
Food Stamps
Federal Family Education Loan Provisions
Housing Counseling
Privacy Act
Real Estate Settlement Procedures Act (RESPA)
Signature Guarantees
Soldiers' and Sailors' Civil Relief Act
Title I Property Improvement and
Manufactured Home Loans
Veteran's Reemployment Rights Act

Mentoring Program for New Credit Union Internal Auditors

The Association of Credit Union Internal Auditors (ACUIA) is an organization of credit union internal auditors. Our mission is to serve the credit union industry through the following objectives: to facilitate the exchange of information and ideas among the membership; to provide internal auditing guidelines, resources, and educational materials; and to promote internal auditing in the credit union industry. Internal audit programs, website, membership directory, mentoring program, bulletin board, and quarterly publications are some of the services that we offer to our membership.

ACUIA is committed to providing resources to all internal auditors at member credit unions. However, our mentoring program is devoted to supporting new credit union internal auditors in developing or enhancing their audit function. These individuals may be new to the credit union industry, new to internal auditing, or new to both. The mentoring program, which is administered by the best practices committee, matches new internal auditors with a “seasoned” ACUIA member/auditor at a comparable credit union. Support and assistance for the new internal auditor will include, but not be limited to, the following areas:

Development of a charter

Development of an annual audit plan

Development of audit programs and administrative procedures

Interacting with the supervisory committee, board, and/or senior manager

Although all ACUIA members are entitled to assistance in these and numerous other areas as a result of their membership, the mentoring program provides a more personal introduction to the many benefits and resources available through ACUIA. This program is intended to help facilitate ACUIA’s goal of being the primary source of credit union internal auditing information for its members.

Contact ACUIA

Please contact ACUIA’s Executive Office if you are interested in this program, either to request a mentor or to volunteer to serve as a mentor. ACUIA can be reached at (866) 254-8128 or email to acuia@acuia.org.

What Is The ACUIA?

ACUIA is incorporated under the laws of the state of Wisconsin as a non-profit organization, but our design is not limited to state boundaries. Indeed, members of ACUIA are found across the United States and worldwide. Regional chapters have been established in order to provide maximum benefit to our members through the promotion of personal contact and networking.

Membership is open to credit union personnel concerned with the audit or accounting operations in credit unions. Nonvoting memberships are also available to non-credit union organizations. All memberships call for an annual membership fee.

Currently, the membership meets regionally on a periodic basis, in addition to an annual national conference. Members are encouraged to volunteer for a variety of projects that are implemented each year.

The ACUIA thanks the volunteer committee who dedicated their time and experience to the development of this help packet. Those members were: Terry McEachern, committee chair person, Royal CU; Donald Bernat, Hepcoe CU; Jake Malasig, Community First Guam FCU; Dorothy Roessler, Heritage Trust FCU; and Chan Singh, Eastern Financial FCU.

We hope you find this information packet useful and anticipate that you will find value in supporting your internal auditor’s membership in our organization. To learn more about the Association of Credit Union Internal Auditors, contact us at:

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