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Comparing and Contrasting the Yellow Book and Red Book Standards

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Session Objectives

- Explain the primary differences between the two sets of standards
- Suggest ways for complying with both sets of standards

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Supplemental Guidance Issued by the IIA

- Supplemental Guidance: IIA International Standards and Government Audit Standards (GAGAS) - A Comparison, 2nd Ed.

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Issue 1 – Consulting

- **IIA Standards** and **GAGAS** the use the words “consulting” or “nonaudit services” to describe different services.
- The **IIA Standards** uses the term consulting within the definition of internal auditing, whereas **GAGAS** categorizes any service that is not an audit or attestation engagement as a nonaudit service.

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Issue 1 - Consulting

Consulting, as described by the **IIA**, is one of two major types of audit services internal audit organizations can provide. The **IIA** defines consulting services as “advisory and related client service activities...without the internal auditor assuming management responsibility.”

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Suggestion

- Audit organizations that follow both the **IIA Standards** and **GAGAS** in audit work should conduct such work in accordance with both sets of audit standards.
- Auditors should comply with **GAGAS** conceptual framework and requirements for nonaudit services, and auditors should not assume management responsibilities as provided for in the **IIA** definition of consulting services.

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Issue 2 – Independence in the Performance of Audit Services

- **IIA Standard** 1130.A1 states that an internal auditor's "objectivity is presumed to be impaired if the auditor provides assurance services for an activity the internal auditor had responsibility for within the previous year."
- **IIA Standard** 1130.C1 states that "internal auditors may provide consulting services relating to operations for which they had previous responsibilities." In addition, in October 2011 the **IIA** issued the **Practice Guide**, "Independence and Objectivity" which provides further guidance.

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Issue 2 – Independence in the Performance of Audit Services

GAGAS Conceptual Framework:

1. Identify threats to independence
2. Evaluate the significance of the threats identified, both individually and in aggregate
3. Apply safeguards as necessary to eliminate the threats or reduce them to an acceptable level
4. Evaluate whether the safeguard is effective

GAGAS Documentation Requirement:

When threats are not at an acceptable level and require application of safeguards, auditors should document the safeguards applied.

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Suggestion

Audit organizations should review the discussion of the **GAGAS** conceptual framework and the related threats and safeguards for independence to avoid the appearance of a lack of independence when a person is employed as an auditor and is subsequently assigned to audit an area for which the person had previous responsibility.

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Issue 3 – Performing Nonaudit Work

- **IIA Standard** 1130 notes that impairments to independence and objectivity, such as performance of nonaudit work by the internal auditor, must be disclosed to the appropriate parties.

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Issue 3 – Performing Nonaudit Work

GAGAS

1. Determine if there is a specific prohibition. Unless specifically prohibited, nonaudit services MAY be permitted but should be documented.
2. If not prohibited, assess the nonaudit service's impact on independence using the conceptual framework.
3. If the auditor assesses any identified threat to independence as higher than insignificant, assess the sufficiency of audited entity management's skill, knowledge, and experience to oversee the nonaudit service.

And...

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Issue 3 – Performing Nonaudit Work

GAGAS

4. If the auditor concludes that performance of the nonaudit service will not impair independence, document assessments in relation to both:
 - safeguards applied to eliminate threats or reduce them to an acceptable level, and
 - the auditor's consideration of management's ability to oversee the nonaudit services to be performed.

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Suggestion

Audit organizations should carefully review the **GAGAS** independence conceptual framework and standards for performing nonaudit services. The performance of certain types of nonaudit services by the audit organization or specific staff could impair independence on the assigned audit and significantly affect the ability of the audit organization to conduct the audits. Audit organizations should conduct all work in accordance with the more detailed **GAGAS** standards.

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Issue 4 – Reviewing the Organization’s Ethics Program

- **IIA Standard** 2110.A1 provides that “the internal audit activity must evaluate the design, implementation, and effectiveness of the organization’s ethics-related objectives, programs, and activities.”
- **GAGAS** does not require an evaluation of an organization’s ethics-related objectives, programs, and activities.

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Suggestion

To comply with the additional requirements of the **IIA Standards**, a periodic evaluation should be made of the organization’s ethics program, and that evaluation should be documented through a note or memos to the file or through an audit on the subject matter.

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Issue 5 – Risk Assessment for Overall Audit Planning

- **IIA Standard** 2010 states that “the chief audit executive (CAE) must establish a risk-based plan to determine the priorities of the internal audit activity, consistent with the organization’s goals.”
- **IIA Standard** 2010.A1 further requires that “the internal audit activity’s plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process.”

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Issue 5 – Risk Assessment for Overall Audit Planning

IIA Practice Guide, “Assessing the Adequacy of Risk Management,” issued in December 2010, provides further guidance.

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Issue 5 – Risk Assessment for Overall Audit Planning

GAGAS does not contain requirements pertaining to the overall audit planning for the audit organization. It focuses on planning associated with individual audits.

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Suggestion

To comply with the additional requirements of the **IIA Standards**, the audit organization should complete a plan of engagements at least annually that is based on a documented risk assessment.

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Issue 6 – External Quality Assurance Review

IIA Standard 1312: External assessments must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization. The CAE must discuss with the board:

- the form and frequency of external assessments, and
- the qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.

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Issue 6 – External Quality Assurance Review

IIA Standard 1320: Reporting on the Quality Assurance and Improvement Program (QAIP) requires the CAE to “communicate the results of the quality assurance and improvement program to senior management and the board.”

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Issue 6 – External Quality Assurance Review

- **GAGAS** requires that audit organizations performing work in accordance with **GAGAS** have a peer review performed by reviewers independent of the audit organization at least once every three years.
- **GAGAS** also requires internal audit organizations provide a copy of the external peer review report to those charged with governance.
- **GAGAS** requires an external audit organization make its most recent peer review report publicly available.

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Suggestion

Audit organizations conducting audits under the **IIA Standards** and **GAGAS** should have a peer review or an external quality assurance review conducted every three years designed to determine conformance with both the **IIA Standards** and **GAGAS**.

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Issue 7 – Quality Assurance Systems

- **IIA Standards** 1300 and 1310 state that the CAE must develop and maintain a QAIP that covers all aspects of the internal audit activity and includes both internal and external assessments.
- **IIA Standard** 1311 provides that the internal assessment must include ongoing monitoring of the performance of the internal audit activity and periodic self-assessments or assessments by other knowledgeable persons within the organization.

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Issue 7 – Quality Assurance Systems

- **IIA Standard** 1320 requires the CAE “communicate the results of the QAIP to senior management and the board.”
- **Practice Advisory** 1311-1 provides recommended guidance for performing internal assessments, including to report the results to senior management and the board at least annually.
- The **IIA’s Practice Guide** issued in December 2010, “Measuring Internal Audit Effectiveness and Efficiency,” provides further guidance.

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Issue 7 – Quality Assurance Systems

GAGAS requires a system of quality control designed to provide reasonable assurance that the organization and its personnel comply with professional standards and applicable legal and regulatory requirements.

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Issue 7 – Quality Assurance Systems

GAGAS requires audit organizations to document and communicate their quality control policies and procedures to collectively address:

- leadership responsibilities for quality within the audit organization;
- independence, legal, and ethical requirements;
- initiation, acceptance, and continuance of audits;
- human resources;
- audit performance, documentation, and reporting; and
- monitoring of quality.

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Issue 7 – Quality Assurance Systems

- **GAGAS** requires audit organizations to analyze and summarize the results of monitoring procedures at least annually.
- Summary to include identification of any systemic or repetitive issues needing improvement, along with recommendations for corrective action.

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Suggestion

Audit organizations should follow more detailed **GAGAS** requirements for the audit organization's quality assurance system and the recommendations in **IIA Practice Advisory** 1311-1 to report the results of its monitoring procedures at least annually.

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Issue 8 - Reporting Compliance with the Standards

- **GAGAS** paragraph 7.30 provides specific language the auditor should use to indicate work was performed in accordance with GAGAS.
- **Suggestion:** When reporting, use the **GAGAS** language and also make reference to the **IIA Standards**.

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Suggestion

To report compliance with **GAGAS** and **IIA Standards**:

We conducted this audit in accordance with Generally Accepted Government Auditing Standards and the International Standards for the Professional Practice of Internal Auditing. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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Issue 9 - Referencing the Standards

- In **IIA Standards** 1321 and 2430, the CAE may state that the internal audit activity conforms with the *International Standards for the Professional Practice of Internal Auditing* only if the results of the QAIP support this statement.
- Further, **Practice Advisory** 1321-1 states that initial use of the compliance phrase is not appropriate until an external review has been performed.

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Suggestion

- Until the audit activity has completed assessments that demonstrate the audit activity is in conformance with the **IIA Standards**, auditors should not report activities are conducted in accordance with the Standards—but should make the compliance statement as allowed under **GAGAS**, if applicable.
- If the audit activity complies with both sets of standards, **GAGAS** compliance statement may incorporate a reference to compliance with the **IIA Standards**.

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Issue 10 – Fraud

- **IIA Standard** 2120.A2 requires an evaluation of the potential for the occurrence of fraud and how the organization manages fraud risk.
- **IIA Standard** 1210.A2 requires internal auditors to “have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud”.
- **IIA Standard** 1220.A1 requires internal auditors to “exercise due professional care by considering... the probability of significant errors, fraud, or noncompliance.”

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Issue 10 – Fraud

- In addition, the **IIA Practice Guide** “Internal Auditing and Fraud” (2009) contains comprehensive guidance for internal auditors relative to fraud awareness, responsibilities during engagements, risk assessment, prevention and detection, investigation, and communication.
- **Planning:** **GAGAS** paragraphs 6.30-6.32 and **IIA Standards** 2120.A1 and 2120.A2 both require an assessment of potential fraud risk during planning.
- **Reporting:** **IIA Standard** 2060 states that the CAE must periodically report risk exposures and control issues, including fraud risks, to senior management and the board.

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Issue 10 – Fraud

- **GAGAS** requires reporting fraud that either has occurred or is likely to have occurred, which is significant within the context of the audit objectives.
- **GAGAS** also requires communication in writing to audited entity officials of fraud that is not significant within the context of the audit objectives, but warrants the attention of those charged with governance.

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Issue 10 – Fraud

GAGAS paragraphs 6.30-6.32 and 7.21-7.26 include additional requirements in the area of fraud, such as:

- discussing fraud risks factors among the team,
- performing additional audit procedures should factors or risks related to fraud be identified,
- extending audit steps and procedures, as necessary, when information comes to the auditor's attention that fraud may have occurred, and
- additional detailed requirements for reporting of fraud.

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Suggestion

- Both **IIA Standards** and **GAGAS** provide guidance in the area of fraud.
- Auditors should follow the more detailed **GAGAS** requirements and also comply with the additional requirements of **IIA Standard 2060** to report periodically to senior management and the board.

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Issue 11 – Follow-up on Previous Audits

- **IIA Standard 2500** states that the CAE “must establish and maintain a system to monitor the disposition of results communicated to management.”
- **IIA Standard 2500.A1** provides that the CAE “must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.”

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Issue 11 – Follow-up on Previous Audits

- **GAGAS** requires auditors to evaluate whether the audited entity has taken appropriate corrective action to address findings and recommendations from previous engagements that are significant within the context of the audit objectives.
- Auditors use this information in assessing risk and determining the nature, timing, and extent of the current audit work, including the extent to which testing the implementation of the corrective actions is applicable to the current audit objectives.

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Suggestion

- The **IIA Standards** require follow-up activities on each audit to ensure accountability, whereas **GAGAS** requires follow-up on previous audits to the extent that such management actions could affect the planning of the current engagement.
- Audit organizations should establish a follow-up process that meets the requirement of the more detailed **IIA Standards**, while not assuming management's responsibilities.

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Issue 12 – Continuing Professional Education (CPE)

The **IIA Standards** do not specify the number of hours recommended per year or biennially for auditors who are not certified. Internal auditors not presently holding certifications are encouraged to pursue CPE that supports efforts to obtain professional certification.

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Issue 12 – Continuing Professional Education (CPE)

GAGAS has more specific requirements:

- Minimum of 24 hours of CPE every 2 years
 - Directly relates to government auditing, the government environment, or the auditee's unique environment
- Additional 56 hours of CPE for auditors involved in
 - Planning, directing, or reporting on **GAGAS** assignments; or
 - Charge 20 percent or more of time annually to **GAGAS** assignments
- Minimum of 20 hours of CPE each year

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Suggestion

Audit organizations should follow the more detailed CPE requirements of **GAGAS** for all auditors and internal specialists performing work in accordance with **GAGAS**, whether certified or not.

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Conclusion

- For organizations either required to or that elect to use both **GAGAS** and the **IIA Standards**, the Comparison Tool can enhance the quality of internal audit activities and provide direction for implementing both standards.
- When differences arise, the Comparison Tool provides suggestions for appropriate action.
 - The tool demonstrates that the standards can be compatible.


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Questions ?



Comparison Tool:
<http://www.theiia.org> > Search: "IIA GAGAS Comparison 2nd Edition"



Red Book:
<https://na.theiia.org/standards-guidance/mandatory-guidance/Pages/Standards.aspx>



Yellow Book:
<http://gao.gov/products/GAO-12-331G>

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