Getting to the Point - Effective Audit Ratings

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Managing Director and Atlantic Region Leader | Risk Advisory Services

April 23, 2019
BDO and our Internal Audit Webinar Series
Polling Question 1

*From which time zone are you participating today?*

A. Eastern  
B. Central  
C. Mountain  
D. Pacific  
E. Other
Michael Vierheller, CPA  
Managing Director and Atlantic Region Leader | Risk Advisory Services

With more than 25 years of experience, Michael is a Managing Director of our Risk Advisory Services practice in the Greater Washington D.C. office and throughout the Atlantic region. He focuses on providing internal audit, risk advisory, Sarbanes-Oxley and financial and information technology consulting services, which includes performing risk assessments, conducting business process analyses and executing internal audit plans. He is also experienced in developing compliance review in accordance with the Sarbanes-Oxley Act, performing user acceptance testing on new system implementations, and assisting with the design, development and execution of regulatory compliance programs.

Michael advises clients on opportunities to increase the effectiveness and efficiency of critical business processes through providing feedback on the use and costs of controls and assessing the functional performance of people, processes and technology. He has assisted clients with the review and implementation of financial systems as well as the development and implementation of Enterprise Risk Management (ERM) programs.

Prior to joining BDO, Michael was a risk and advisory services partner with a big four accounting firm. Michael also has several years of experience in advising clients on the effective use and implementation of technology solutions to assist with achieving business objectives.
Today’s Learning Objectives

At the conclusion of this course, participants will be able to:

- Discuss the pros and cons of internal audit report ratings;
- Identify various audit report rating strategies;
- Discuss how to implement a report rating system and measure success.
How ratings are used throughout the Internal Audit lifecycle
Our goals as Internal Audit professionals

- Provide Third Party Assurance that an Organization is operating as management intends

- Identify and Prioritize Risk Factors that can be evaluated along with their controls and other mitigation factors

- Provide effective communication to various levels of the organization concerning those risk factors and the work performed
How do we deliver on our goals as Internal Audit practitioners?

Deliverables:

► Risk Assessment
► Internal Audit Plan
► Internal Audit Reports
► Status Reporting
► Yearly Internal Audit Summary

How do we tie these activities together? Audit Reporting!
Common audit ratings used throughout the Internal Audit lifecycle

- Risk Assessment
  - Risk Severity
  - Risk Likelihood
- Internal Audit
- Reporting/Follow-up
- IA Plan Development
- IA Execution
- Annual Summary Rating
- Audit Area Risk Rating
- Audit Objective Rating
- Audit Finding Rating
Polling Question 2

Does your Internal Audit Department use ratings throughout the Internal Audit lifecycle?

A. Always
B. Mostly
C. Sometimes
D. Never
E. Unsure
Building Effective Internal Audit Reports
Elements of Better Internal Audit Reports

- Background of Area Reviewed
- Scope of Internal Audit
- Audit Objectives (Tie Back to Risk Assessment)
- Individual Findings and Recommendations
- Audit Conclusions (Tie Back to Audit Objectives)
Writing an Impactful Audit Report: 6 Tips for Being More Persuasive*

- Keep it Short
- Keep it Simple
- Make Best Ideas Stand Out
- Do not Neglect the Basics
- Consider the Implications
- Remember the 5 Cs

The 5 Cs

- Criteria (what should be)
- Condition (the current state)
- Cause (the reason for the difference)
- Consequence (effect)
- Corrective action plans/recommendations

* Author - Richard Chambers, CIA, QIAL, CGAP, CCSA, CRMA, is president and CEO of The IIA. In Chambers on the Profession, he shares his personal reflections and insights based on his 40 years of experience in the internal audit profession.
# Audit Report Rating Systems - Pros and Cons

<table>
<thead>
<tr>
<th>Biggest Pros</th>
<th>Biggest Cons</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Helps Readers Differentiate the Severity of Issues</td>
<td>- More focus on Rating than Findings of Remediation Plans</td>
</tr>
<tr>
<td>- Helps Auditees prioritize corrective actions</td>
<td>- Close Down Communication for fear of consequences</td>
</tr>
</tbody>
</table>

*Important to know your audience and implement accordingly.*
Polling Question 3

Does your Internal Audit Department use ratings on Audit Reports?

A. Always
B. Mostly
C. Sometimes
D. Never
E. Unsure
Using different types of ratings within your Internal Audit reports
How to effectively use ratings within audit reports

Audit Objectives Ratings
How did the Auditee fair against the Audit Objective?

Audit Findings Ratings
How Significant is the issue that was identified?

Audit Report
Rating against audit objectives

Keep it Simple

- Met Objective
- Mostly Met Objective
- Did Not Meet Objective

<table>
<thead>
<tr>
<th>Category</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Met Objective</td>
<td>Green</td>
</tr>
<tr>
<td>Mostly Met Objective</td>
<td>Yellow</td>
</tr>
<tr>
<td>Did Not Meet Objective</td>
<td>Red</td>
</tr>
</tbody>
</table>

Allows the Auditor to tie back to the following:

- Why was this area selected for audit?
- What was important to test?
- What needs to be tracked and reported against?
Ratings for specific findings

Typical Scales

- 3 or 5 level scale
- Definitions should be established and communicated
- Consistently Applied

<table>
<thead>
<tr>
<th>Level of Severity</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>♠</td>
</tr>
<tr>
<td>Medium</td>
<td>♦</td>
</tr>
<tr>
<td>Low</td>
<td>♣</td>
</tr>
</tbody>
</table>

Allows the Auditor to do the following:

- Communicate the auditor’s judgement on severity?
- Prioritize importance of remediation activities?
- Guide readers/users of reports to focus on more important items?
Polling Question 4

Does Your Internal Audit Department rate audit objectives?

A. Always
B. Mostly
C. Sometimes
D. Never
E. Unsure
Polling Question 5

What type of scale does your IA team use on rating audit Findings?

A. Three Point Scale
B. Five Point Scale
C. Other Scale
D. No Scale
Building an Annual Internal Audit Summary Report
## Annual Summary Report for Internal Audit (Better Practice)

<table>
<thead>
<tr>
<th>Risk Assessment</th>
<th>• Identified Key Risks (and related Audit Themes) for the Organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit Plan</td>
<td>• Identified Individual Process Areas and Selected Mitigation Activities to Review as Part of Audit Plan</td>
</tr>
<tr>
<td>Individual Audits</td>
<td>• Performed Individual Audits and Issued Specific Audit Reports Related to the Areas Reviewed</td>
</tr>
<tr>
<td>Annual Summary Report</td>
<td>• Summarize all Audit Activities tied to Annual Risk Assessment Key Risks and Audit Themes</td>
</tr>
</tbody>
</table>
Elements of an Annual Summary Report

- Key Risk Themes Identified in Annual Risk Assessment
- Types of Audits performed against those themes
- Results of Individual audits
- Overall results of audit activities as it relates to Key Risk Themes
Rating Annual Summary Areas

Make Ratings Relevant to Themes

► Categorize Effectiveness
► Consider number of needed Categories
► Did Not Meet Objective

<table>
<thead>
<tr>
<th>Category (3-5 Levels)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Effectively</td>
</tr>
<tr>
<td>Opportunities for Improvement</td>
</tr>
<tr>
<td>Needs Improvement</td>
</tr>
</tbody>
</table>

Allows the Auditor to do the following:

- Summarize results of audits collectively?
- Comprehensive results for Senior Management and Audit Committee?
- Feeder for future Risk Assessments?
Polling Question 6

Does Your Internal Audit Department Prepare Annual Audit Summary Reports?

A. Yes
B. No, but Good Idea for your organization
C. No, and not a Good Idea for your organization
Determining success
Typical success factors related to audit ratings

- Increased Risk Awareness
- Better Alignment on Significance of Issues
- Prioritization on Remediation Efforts
- More Concise Audit Reporting
Key factors in implementing rating systems

- Open and on-going communication with Management and Auditees
- Documentation of Definitions and Categories
- Linkage of Audit Activities to Risk Assessment
- Consistent and objective reporting
Concluding thoughts
Concluding thoughts

- The use of ratings can be a valuable tool
- Know your stakeholders and align ratings to their needs
- Create objective definitions for ratings
- Apply ratings as consistently as possible
Questions

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Coming Soon

May 13-15, 2019
North America CACS/ISACA Conference
Anaheim Convention Center - Visit us at Booth 604

June 25, 2019
2019 Internal Audit Webinar Series - Course 3
Audit Speed - Opportunities for Enhancement

July 7-10, 2019
IIA International Conference
Anaheim Convention Center - Visit us at Booth 715