

SIAAB Guidance #05

Conforming with FCIAA and Standards in Small Audit Functions in the State of Illinois

Adopted December 8, 2015

Revised In Accordance with 2017 Standards – Effective January 1, 2017

**** Note: The terms “Chief Executive Officer” or “Agency Head” as utilized in this document are interchangeable and shall refer to the individual who has been designated by the Governor as the head of an agency under the Governor or the Constitutional Officer, in the case of those entities which do not fall under the direct jurisdiction of the Governor. The term “Agency” as utilized in this document, refers to an agency under the Governor or the Constitutional Office, in the case of those entities which do not fall under the direct jurisdiction of the Governor. Illinois Administrative Procedures Act (5 ILCS 100 Section 1-25) states, “‘Agency head’ means an individual or group of individuals in whom the ultimate legal authority of an agency is vested by any provision of law.”*

“Chief Audit Executive (or Chief Internal Auditor) describes the role of a person in a senior position responsible for effectively managing the internal audit activity in accordance with the internal audit charter and the mandatory elements of the International Professional Practices Framework. The Chief Audit Executive (or Chief Internal Auditor) or others reporting to the Chief Audit Executive (or Chief Internal Auditor) will have the appropriate professional certifications and qualifications. The specific job title and/or responsibilities of the Chief Audit Executive may vary across organizations.” [In Illinois, the Fiscal Control and Internal Auditing Act refers to this position as Chief Internal Auditor.]

SIAAB Interpretation

This guidance will address, on a high-level basis, key Auditing Standards (AS), and offer optional recommendations to assist small audit functions in conforming with the standards and complying with the Fiscal Control and Internal Auditing Act (FCIAA) (30 ILCS 10).

In April 2011, the Institute of Internal Auditors (IIA) published a practice guide titled Assisting Small Internal Audit Activities in Implementing the International Standards for the Professional Practice of Internal Auditing¹ (Guide). The Guide discusses the challenges faced by small audit functions, rates the level of challenge presented, and proposes remedies. This SIAAB guidance document will address the unique challenges for small audit functions in context of FCIAA.

The criterion for defining a small audit function varies by entity. For purposes of this guidance document, a *small audit function* is one that has a small number of audit staff in comparison to the overall agency headcount, budget size, programs, and mission. Ultimately, it is the

¹ <https://na.theiia.org/standards-guidance/recommended-guidance/practice-guides/Pages/Practice-Guides.aspx>

responsibility of each Chief Internal Auditor to determine whether its audit function is small and the level to which this guidance is applicable.

Auditing Standard 1000 – Purpose, Authority and Responsibility

AS 1000: *The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework (the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the Standards, and the Definition of Internal Auditing). The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.*

SIAAB Guidance:

Conformance with AS 1000 is independent of the size of the audit function and should not present unique challenges for small audit functions. The Chief Internal Auditor should obtain executive endorsement/approval of the audit charter from the chief executive officer, and governing board, as applicable, periodically. FCIAA requires the Chief Internal Auditor prepare a two-year audit plan for chief executive officer approval by the end of each fiscal year [30 ILCS 10/2003(a)(1)]. SIAAB recommends obtaining charter endorsement/approval in conjunction with annual approval of the audit plan.

Auditing Standard 1100 – Independence and Objectivity

AS 1100: *The internal audit activity must be independent, and internal auditors must be objective in performing their work.*

SIAAB Guidance:

The internal audit function must always perform its duties with objectivity and independence. The importance of the independence and objectivity should be discussed and reinforced, and real or perceived impairment should be disclosed to the chief executive officer and appropriate parties, at both the agency and engagement level (see also AS 1130 – Impairments to Independence or Objectivity). SIAAB recommends disclosing impairments in writing on at least an annual basis, in conjunction with the two-year planning process, and more frequently as warranted when impairments arise. The Chief Internal Auditor should exercise due care in ensuring that impairments are not perceived as excuses. When issuing a report where independence could not be satisfactorily achieved, the Chief Internal Auditor has an obligation to disclose the impairment and its related impact.

For small audit functions in the State of Illinois, independence is enhanced by the FCIAA mandate for the Chief Internal Auditor to report directly to the chief executive officer, and to have direct communications with the governing board, as applicable, and by the FCIAA prohibition on internal audit performing operational activities. Chief Internal Auditors should

consider SIAAB Guidance 02: Internal Audit Independence - Interaction with Agency Head, Senior Staff and Placement within the Organizational Structure.

Auditing Standard 1200 – Proficiency and Due Professional Care

AS 1200: *Engagements must be performed with proficiency and due professional care.*

SIAAB Guidance:

Small internal audit functions are often faced with limited resources, and may not have the budget to invest in adequate training or hire personnel (including third-party specialists) necessary to do the work.

In order for a small audit function to have adequate *collective proficiency*, Chief Internal Auditors should, as permissible under hiring rules and agreements, seek staff auditors with complementary skills. Further, small audit functions have an increased need for auditors with sufficient experience to function with limited supervision. The level of independence and supervision auditors receive when performing functions should be commensurate with their experience and the complexity of the audit. Due professional care can still be achieved when utilizing less experienced staff by ensuring the appropriate level of supervision and oversight. The Chief Internal Auditor should seek guidance from peers, utilize reference materials (books, audit programs, internal control questionnaires, templates, etc.), and leverage training that is provided free of cost or at low cost (Web-based training, local SIAAB and IIA training, etc.).

Auditing Standard 1300 – Quality Assurance/Improvement Program

AS 1300: *The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.*

SIAAB Guidance:

Chief Internal Auditors should leverage the resources on SIAAB's Quality Assurance Review (QAR) Program page². Chief Internal Auditors and pertinent audit staff are encouraged to take the free QAR training provided by SIAAB (4 CPE), and small audit functions should also consider utilizing QAR checklists as part of their engagement planning and closeout process to promote reasonable, timely conformance with the Standards. The use of auditing software can also help provide quality assurance as the audit work is maintained in a central location and evidence of the completion and review of the audit objectives and steps is maintained within the software.

² https://siaab.audits.uillinois.edu/QAR_Program/

Auditing Standard 2000 – Managing the Internal Audit Activity

AS 2000: *The chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organization.*

SIAAB Guidance:

A significant challenge facing small audit functions in the State of Illinois is balancing the audit function's mandates under FCIAA and other Illinois statutes/rules with the expectations of senior management. The Chief Internal Auditor may have difficulty demonstrating the audit function adds value if management's priorities differ from the audit function's required mission. This disconnect, if unresolved, can worsen the challenge over time as management may not allocate sufficient resources to an audit function it does not view as adding value. Therefore, the internal audit charter should clearly define Internal Audit's mission and be endorsed by the chief executive officer [see AS 1000 (Purpose, Authority and Responsibility), above].

FCIAA requires the Chief Internal Auditor prepare a two-year audit plan for chief executive officer approval by the end of each fiscal year. While all audit functions should include its mandatory audits on the two-year audit plan, SIAAB encourages small audit functions to emphasize to the chief executive officer the mandatory nature of key items on the two-year audit plan. Resource limitations may result in non-mandatory engagements on the two-year plan being canceled or postponed, and, pursuant to AS 2020 (Communication and Approval), significant interim changes should be communicated to senior management and the governing board, as applicable.

Chief Internal Auditors should consider SIAAB Guidance 04 – Audit Plan Development and Amendment, and consult with their peers. SIAAB recommends small audit functions develop a two-year audit plan that prioritizes the activities required by statute. Managerial directives under FCIAA [30 ILCS 10/2003(a)(4)] should be added, postponed, or canceled based on resources and timing as to not interfere with mandatory engagements. Communication is essential so management does not view audit as having priorities contrary to the priorities of senior management, and so management will understand why prioritizing mandatory activities is necessary to ensure compliance with FCIAA and auditing standards.

Auditing Standard 2100 – Nature of Work

AS 2100: *The internal audit activity must evaluate and contribute to the improvement of the organization's governance, risk management, and control processes using a systematic, disciplined, and risk-based approach. Internal audit credibility and value are enhanced when auditors are proactive and their evaluations offer new insights and consider future impact.*

SIAAB Guidance:

A small internal audit function should use a risk-based audit approach to ensure the depth, frequency, and nature of audit work are properly focused based on resources and risk. FCIAA

[30 ILCS 10/3002] references Internal Control Certification Guidelines that were established by the Comptroller in conjunction with the Department of Central Management Services. SIAAB recommends tracking the control areas documented in the Guidelines against their audits. Most audit engagements provide coverage over multiple control areas, and tracking the coverage promotes compliance with FCIAA as well as the Standards. A good tracking tool is a spreadsheet (or comparable resource) that cross references audit activities with related internal control areas.

The Comptroller guidelines list the following internal control areas that should be given consideration³:

- Agency Organization and Management
- Administrative Support Services
- Budgeting, Accounting and Reporting
- Purchasing, Contracting and Leasing
- Expenditure Control
- Personnel and Payroll
- Property, Equipment, and Inventories
- Revenues and Receivables
- Petty Cash and Local Funds
- Grant Administration
- Electronic Data Processing / Information Technology

See also SIAAB Guidance 04 – Audit Plan Development and Amendment for more detailed guidance on promoting compliance during the audit planning process. It is especially important for small audit functions to track any audit work planned or performed related to any areas of internal control to demonstrate all major systems of internal control are reviewed during the two-year audit cycle.

Auditing Standard 2200 – Engagement Planning

AS 2200: *Internal auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations. The plan must consider the organization's strategies, objectives, and risks relevant to the engagement.*

SIAAB Guidance:

Internal audit functions in the State of Illinois are required to conduct several recurring audits and engagements, typically on an annual or biennial basis. Chief Internal Auditors should consider obtaining or developing checklists and audit plan templates for common audits in order to streamline the process, and such resources should be tailored based on circumstances. Chief Internal Auditors should refer to SIAAB Guidance #4, Internal Audit Plan Development and Amendments in State of Illinois Government.

³ <http://www.ioc.state.il.us/index.cfm/resources/sams-manual-procedure-2-internal-controls/>

Further, SIAAB recommends leveraging the following resources:

- The annual internal control certifications required by FCIAA [30 ILCS 10/3003];
- Process narratives and flowcharts prepared by management and agency units;
- Information regarding management's risk tolerances or appetite;
- Historic internal and external audit findings⁴;
- Prior internal audit working papers;
- The agency's strategic plan and budget;
- A review of applicable statutes⁵ and rules⁶ pertaining to the auditable units and programs; and,
- Surveys, questionnaires, templates, etc. (IIA, ISACA, internally prepared, obtained from other State agencies, etc.).
 - The SIAAB website provides a "Resource" section to facilitate the sharing of information between State entities (<https://siaab.audits.uillinois.edu/Resources/>).

The development of work program templates by engagement type will reduce the time needed to complete engagements and will ensure that engagement objectives are appropriately incorporated into the work performed. The Chief Internal Auditor should revisit the templates periodically to ensure relevance and appropriateness in the context of the audit plan, risk, and the current environment. The Chief Internal Auditor should also ensure that sampling methods are sufficient based on the levels of risk and resources. Ideally, the most proficient auditors in the area(s) of testing should be assigned the most complex testwork, where possible.

External Audit Considerations in the Planning Process

According to AS 2050 (Coordination and Reliance), "*the chief audit executive should share information, coordinate activities, and consider relying upon the work of other internal and external assurance and consulting service providers to ensure proper coverage and minimize duplication of efforts.*" It is useful to consider the testing performed by external auditors and, where possible, to not duplicate their testing. In terms of risk management, it is prudent to audit what has not been audited, particularly for small audit functions seeking to optimize their limited resources. However, it is important to understand that testing by external auditors is not part of the internal audit program, and the fact that testing was conducted by external auditors does not alleviate internal audit's responsibility to perform audit testing.

The time allocated to an internal audit of a function generally allows for a more detailed scope of work than what external auditors are able to provide given their budget limitations and broad scope of work. The purpose of an internal audit is to provide reasonable, though not absolute assurance, that internal controls are appropriate and functioning effectively in regards to a particular function. An internal audit can identify significant control weaknesses if they exist however, it is not within the scope of an internal audit to discover all errors that may exist.

⁴ <http://www.auditor.illinois.gov/Audit-Reports/ABC-List.asp>

⁵ <http://www.ilga.gov/legislation/ilcs/ilcs.asp>

⁶ <http://www.ilga.gov/commission/jcar/admincode/titles.html>

Auditing Standard 2300 – Performing the Engagement

AS 2300: *Internal auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement’s objectives.*

SIAAB Guidance:

Small audit functions are faced with an increased workload challenge due to the lack of a sufficient number of auditors with the proficiency and experience necessary to achieve the engagement’s objectives. In small audit functions, the Chief Internal Auditor may be performing some engagements in addition to supervising, and there may be insufficient time to develop staff and related supervisory skills. An additional challenge may be that the Chief Internal Auditor is so involved in performing the engagement that it does not receive sufficient independent review.

SIAAB recommends, where possible, assigning staff to testwork based on their proficiency and experience. An auditor’s level of independence or supervision should generally be commensurate with the auditor’s experience and proficiency in the area of being tested, as well as the risk level of the area. The use of less experienced auditors requires an increase in oversight and supervision. AS 2020 (Communication and Approval) requires the chief internal auditor to communicate the impact of resource limitations to senior management.

Chief Internal Auditors should consult with peers throughout the State and share resources where appropriate. The SIAAB website provides a “Resource” section to facilitate the sharing of information between State entities (<https://siaab.audits.uillinois.edu/Resources/>).

Auditing Standard 2400 – Communicating Results

AS 2400: *Internal auditors must communicate the results of engagements.*

SIAAB Guidance:

The use of report templates can streamline the reporting process. Further, SIAAB recommends the reports include information regarding the major systems of internal control reviewed during the engagement [see section on AS 2100 (Nature of Work), above].

Auditors should be counseled and/or trained on providing meaningful and concise communications. SIAAB encourages the use of audit-finding templates to promote all required elements of findings are captured, to reduce oversight and supervisory overhead. The five required elements of a finding are:

1. **Condition:** Description of the problem identified (the “*what is*”).
2. **Criteria:** Description of the standard or benchmark not met (the “*what should be*”).
3. **Cause:** The reason the condition deviated from the criteria (the “*why*”).
4. **Significance/Effect:** Description on the risk, impact, and/or potential negative outcome (or opportunity foregone) because of the condition (the “*why it matters*”).
5. **Recommendation:** Suggested corrective action(s) to bring the condition into conformance with the criteria (the “*what should be done about it*”).

Chief Internal Auditors should also refer to the Practice Advisories for AS 2420 (Quality of Communications) and AS 2440 (Disseminating Results).

Auditing Standard 2500 – Monitoring Progress

AS 2500: *The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.*

SIAAB Guidance:

The internal audit procedures for small internal audit functions should document how to prioritize the findings on frequency and depth of follow-up. Because audit resources are scarce, audit follow-up work through actual fieldwork on all open findings is generally not feasible and to do so could restrict the ability of the audit function to provide audit coverage to areas not previously audited. Instead, the Chief Internal Auditor may require management representation that the matter has been addressed prior to expending resources on any further audit work. This is accomplished through periodic requests to auditees for updates to open findings that ask the auditee to provide evidence of the implementation of their corrective action plan. The auditors can review the representations and determine whether the action taken appears to satisfy the completion of the corrective action plan or whether additional information is needed, which may also include actual follow-up work if necessary. It should be made clear to management that although providing sufficient evidence may clear a finding, the only way for Internal Audit to determine with certainty that a Corrective Action Plan was fully implemented is to conduct a subsequent audit. Therefore, should internal audit conduct a subsequent audit of the area, management should understand that internal audit will utilize this information in ascertaining whether the appropriate action indicated was fully implemented and functioning as intended.

The following suggested follow-up strategies are derived from the IIA’s practice guide for small audit functions:

Prioritized Audit Recommendations (Ratings)	Suggested Follow-up Strategy	SIAAB Guidance
High Risk/Priority	Validation by Internal Audit	Internal audit should consider reviewing the remediation plan and validating its results at completion.
Moderate Risk/Priority	Self-assessment, with Subsequent Validation	Internal audit should consider relying on validation by business process owners, and consider validating the remediation plan either at completion or during the subsequent audit.
Low Risk/Priority	Self-assessment	Internal audit should consider relying on validation by business process owners. Internal audit may also consider validation in the subsequent audit.

Internal Audit may consider requesting commitments from management and auditees regarding corrective actions and timeframes for addressing audit findings, and use the commitments to schedule follow-up activities. A good productivity tool is a spreadsheet (or comparable resource) that lists open issues, owners, due date, a brief summary of matter, and current status.

FCIAA requires the Chief Internal Auditor report on the status of internal audit findings and the extent of recommendations implemented annually by September 30 [(30 ILCS 10/2003)(a)(1)]. This deadline and reporting requirement should be discussed with key auditees. Awareness that reporting the status of findings to the chief executive officer is required by law may further motivate timely corrective action.

Auditing Standard 2600 – Management’s Acceptance of Risk

AS 2600: *When the chief audit executive concludes that management has accepted a level of risk that may be unacceptable to the organization, the chief audit executive must discuss the matter with senior management. If the chief audit executive determines that the matter has not been resolved, the chief audit executive must communicate the matter to the board.*

SIAAB Guidance:

The Internal Audit Charter for a small audit function may describe the resolution process in cases where management disagrees with internal auditing’s recommendation(s) or acceptable levels of risk. The Charter should be endorsed by the chief executive officer. Further, management’s acceptance of a level of risk the Chief Internal Auditor deems unacceptable should be communicated to management timely, and documented in the Internal Audit Annual Report (due by September 30 of each year, pursuant to FCIAA [30 ILCS 10/2003)(a)(1)]).

Chief Internal Auditors should also consider SIAAB Guidance 02: Internal Audit Independence - Interaction with Agency Head, Senior Staff and Placement within the Organizational Structure.

Fiscal Control and Internal Auditing Act (FCIAA)

Sec. 2001. Program of internal auditing.

Each designated State agency as defined in Section 1003(a) shall maintain a full-time program of internal auditing. In the event that a designated State agency is merged, abolished, reorganized, or renamed, the successor State agency shall also be a designated State agency. [30 ILCS 10/2001(a)]

Sec. 2002. Qualifications of chief internal auditor.

(a) The chief executive officer of each designated State agency shall appoint a chief internal auditor with a bachelor's degree, who is either:

(1) a certified internal auditor by examination or a certified public accountant and who has at least 4 years of progressively responsible professional auditing experience; or

(2) *an auditor with at least 5 years of progressively responsible professional auditing experience.*

(b) *The chief internal auditor shall report directly to the chief executive officer and shall have direct communications with the chief executive officer and the governing board, if applicable, in the exercise of auditing activities. All chief internal auditors and all full-time members of an internal audit staff shall be free of all operational duties. [30 ILCS 10/2002]*

Sec. 2003. Internal auditing program requirements.

(a) *The chief executive officer of each designated State agency shall ensure that the internal auditing program includes:*

(1) *A two-year plan, identifying audits scheduled for the pending fiscal year, approved by the chief executive officer before the beginning of the fiscal year. By September 30 of each year the chief internal auditor shall submit to the chief executive officer a written report detailing how the audit plan for that year was carried out, the significant findings, and the extent to which recommended changes were implemented.*

(2) *Audits of major systems of internal accounting and administrative control conducted on a periodic basis so that all major systems are reviewed at least once every 2 years. The audits must include testing of:*

(A) *the obligation, expenditure, receipt, and use of public funds of the State and of funds held in trust to determine whether those activities are in accordance with applicable laws and regulations; and*

(B) *grants received or made by the designated State agency to determine that the grants are monitored, administered, and accounted for in accordance with applicable laws and regulations.*

(3) *Reviews of the design of major new electronic data processing systems and major modifications of those systems before their installation to ensure the systems provide for adequate audit trails and accountability.*

(4) *Special audits of operations, procedures, programs, electronic data processing systems, and activities as directed by the chief executive officer or by the governing board, if applicable.*

(b) *Each chief internal auditor shall have, in addition to all other powers or duties authorized by law, required by professional ethics or standards, or assigned consistent with this Act, the powers necessary to carry out the duties required by this Act.*

IIA Glossary of Definitions:

- **Board** - The highest level of governing body (e.g., a board of directors, a supervisory board, or a board of governors or trustees) charged with the responsibility to direct and/or oversee the organization's activities and hold senior management accountable. If a board does not exist, the word "board" in the *Standards* refers to a group or person charged with governance of the organization. Furthermore, "board" in the *Standards* may refer to a committee or another body to which the governing body has delegated certain functions (e.g., an audit committee).
- **Charter** - The internal audit charter is a formal document that defines the internal audit activity's purpose, authority, and responsibility. The internal audit charter establishes the

internal audit activity's position within the organization; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities.

- **Chief Audit Executive (Chief Internal Auditor)** - Chief audit executive describes the role of a person in a senior position responsible for effectively managing the internal audit activity in accordance with the internal audit charter and mandatory elements of the International Professional Practices Framework. The chief audit executive or others reporting to the chief audit executive will have appropriate professional certifications and qualifications. The specific job title and/or responsibilities of the chief audit executive may vary across organizations.
- **Code of Ethics** - The Code of Ethics of The Institute of Internal Auditors (IIA) are Principles relevant to the profession and practice of internal auditing, and Rules of Conduct that describe behavior expected of internal auditors. The Code of Ethics applies to both parties and entities that provide internal audit services. The purpose of the Code of Ethics is to promote an ethical culture in the global profession of internal auditing.
- **Compliance** - Adherence to policies, plans, procedures, laws, regulations, contracts, or other requirements.
- **Conflict of Interest** - Any relationship that is, or appears to be, not in the best interest of the organization. A conflict of interest would prejudice an individual's ability to perform his or her duties and responsibilities objectively.
- **Engagement** - A specific internal audit assignment, task, or review activity, such as an internal audit, control self-assessment review, fraud examination, or consultancy. An engagement may include multiple tasks or activities designed to accomplish a specific set of related objectives.
- **Engagement Objectives** - Broad statements developed by internal auditors that define intended engagement accomplishments.
- **Impairment** - Impairment to organizational independence and individual objectivity may include personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations (funding).
- **Independence** - The freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner.
- **Internal Audit Activity (Internal Audit Function)** - A department, division, team of consultants, or other practitioner(s) that provides independent, objective assurance and consulting services designed to add value and improve an organization's operations. The internal audit activity helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes.

- **Objectivity** - An unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others.
- **Risk** - The possibility of an event occurring that will have an impact on the achievement of objectives. Risk is measured in terms of impact and likelihood.
- **Risk Management** - A process to identify, assess, manage, and control potential events or situations to provide reasonable assurance regarding the achievement of the organization's objectives.
- **Standard** - A professional pronouncement promulgated by the Internal Audit Standards Board that delineates the requirements for performing a broad range of internal audit activities, and for evaluating internal audit performance.