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United States Government Accountability Office
Washington, DC 20548

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Subject: Exposure Draft of Proposed Changes to the *International Standards for the Professional Practice of Internal Auditing*

This letter provides the U.S. Government Accountability Office's (GAO) comments on the Institute of Internal Auditors' (IIA) Exposure Draft of Proposed Changes to the *International Standards for the Professional Practice of Internal Auditing (Standards)*. We appreciate the opportunity to comment on this significant proposal. We commend the IIA for taking on this project to update the *Standards* to align with the revised International Professional Practices Framework and to add clarity to the *Standards* using standard language to define auditor requirements.

While we agree with the overall approach of the exposure draft, we believe the *Standards* could be improved and have recommendations in the following areas:

- clarity of auditor requirements;
- citing conformity with the *Standards*;
- consulting engagements; and
- comments on specific standards.

Clarity of Auditor Requirements

Definition of terms

We are concerned that the definitions of “must” and “should” are not included in the *Standards* or the glossary. For purposes of commenting on the *Standards*, we are relying on the definitions of “must” and “should” from the instructions to the exposure draft. Clear definitions of the words used to indicate auditor requirements are essential for auditors to be able to properly understand and implement the requirements intended by the IIA. We noted the following points regarding terms used in the *Standards*.

- The terms “must” and “should” are not defined in the *Standards* or the glossary, although they are used to specify requirements throughout the *Standards*.

- The term “should” was previously defined in the glossary but has been removed in the exposure draft.
- From a definitional standpoint, it is problematic to use the word “must” in the explanation of the definition of the term “must.”
- The use of the phrases “must consider” and “should consider” is also problematic because the use of the word “consider” adds confusion to the requirement since it does not require a specific action. Also, it is not clear whether auditors need to document how they considered something. Other standards setters are using “determine” or “evaluate” in conjunction with “must” or “should,” and eliminating the use of “consider.”
- The word “ensure” does not tell an auditor the actions he or she is expected to take; rather it states an objective of an unstated procedure, which may or may not obtain the complete accuracy indicated by “ensure.”
- The phrase “is responsible for” also does not tell an auditor the actions he or she is expected to take.

We suggest including the definitions of must and should in the glossary and in the body of the *Standards* as an introduction preceding the attribute standards. We also suggest that the *Standards* not use the following terminology: “is responsible for,” “consider,” “ensure,” and “be alert to.”

In addition to the above concerns, we believe that another improvement would be for the IIA to consider applying clarity conventions along the same principles as those adopted by other standards setters – such as the International Auditing and Assurance Standards Board (IAASB), the American Institute of Certified Public Accountants (AICPA), the Public Company Accounting Oversight Board (PCAOB), and GAO – to define requirements for auditor actions in the standards. We noted a major inconsistency between the definitions used in the exposure draft instructions and those used by other standards setters. While the IIA has defined “must” as indicating unconditional requirements, which is consistent with other standards setters, the second sentence of the definition of “must” used in the exposure draft instructions indicates that – “The auditor must follow these requirements unless other procedures, which can be documented as sufficient and appropriate, could also satisfy the nature and intent of the *Standards*.” There is an inconsistency between stating that “must” indicates a mandatory unconditional requirement and then stating that other procedures can be substituted for a “must” requirement.

The second sentence of the “must” definition used in the exposure draft instructions is more aligned with the definition of “should” as used by other standards setters, including GAO. The definition of “should” as used by GAO, which is intended to be consistent with the definition used by the AICPA and the PCAOB, indicates a presumptively mandatory requirement and contains the following language: “...in rare circumstances, auditors and audit organizations may depart from a presumptively mandatory requirement provided they document their justification for the departure and how the alternative procedures performed in the circumstances were sufficient to achieve the objectives of the presumptively mandatory requirement.”

We suggest that the IIA move the second sentence of the “must” definition to the “should” definition. The definition of “must” needs to be clear that “must” indicates an unconditional requirement and that another procedure cannot substitute for a “must.” Also, we suggest adding language to the definition of “should” to indicate that substituting another procedure for a “should” requirement is allowed only if the auditors document their justification for the departure from the “should” and how the alternative procedures performed in the circumstances were sufficient to achieve the objectives of the “should” requirement. The IIA should review every “must” requirement in the *Standards* to determine whether there are acceptable alternatives to the procedure; if so, “should” is the appropriate word.

Use of passive voice with “must” and “should”

The *Standards* frequently contain sentences using “must” or “should” in the passive voice. This usage implies that “things” must be a certain way without stating what the auditors are required to do or what actions the internal audit activity should take. This approach is also inconsistent with the usage of these terms by other standards setters. Usage of “must” and “should” in the passive voice does not indicate who is responsible for meeting the requirement. There are numerous examples of this usage throughout the *Standards*. One such example is in draft standard 1000 – “The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter...” Based on the second sentence of draft standard 1000 and Practice Advisory 1000-1, it appears that the intent is for this to be a responsibility of the chief audit executive. As an example, we suggest redrafting the standard in the following manner – “The chief audit executive must develop an internal audit charter that defines the purpose, authority, and responsibility of the internal audit activity.”

Language used in Interpretations

There is inconsistency with the language used in the interpretations. Some interpretations contain “must” or “should.” Others are written in the present tense or in passive voice. This inconsistency could result in confusion regarding the required actions to be taken to satisfy the intent of the interpretations, as well as confusion between the differing levels of auditor responsibility for complying with the actions outlined in a standard versus an interpretation. For example:

- Must – 1100, “Threats to independence must be managed...”
- Should – 1130, “The determination of appropriate parties to which the details of an impairment of independence or objectivity should be disclosed...”
- Present Tense – 2010, “The chief audit executive is responsible for developing a risk-based plan.”
- Passive Voice – “Sufficient knowledge of internal audit practices requires an understanding of all elements of the *International Professional Practices Framework*.”

Also, the degree of responsibility associated with interpretations is not entirely clear. By including the interpretations in the *Standards*, they are mandatory by definition,

but they are also considered to be guidance. The auditor's level of responsibility for complying with the guidance is not clear.

Citing Conformity with the *Standards*

The *Standards* do not require the use of a statement of conformity with the *Standards*, and the statement encouraging internal auditors to report that their activities are conducted in accordance with the *Standards* has been removed from standard 1321 (old 1330) of the exposure draft. Instead, the revised language contains a permissive "may." We believe that this revision weakens the *Standards*. We support the previous language that encouraged internal auditors to report that their activities are conducted in accordance with the *Standards*. However, the previous standard did not contain any requirements using "must" or "should." We believe that users of internal audit reports need to clearly understand whether the engagement and the internal audit activity conform with the *Standards*. Therefore, we believe that standard 1321 should require the chief audit executive to state that the internal audit activity conforms with the *Standards* and standard 2430 should require internal auditors to report for each engagement whether that engagement complied with *Standards*.

The "must" requirement for disclosure of nonconformance in 1322 and the "should" requirement for disclosure of nonconformance 2431 are inconsistent with the permissive "may" in 1321 and 2430. Specifically, standard 1321 states that the chief audit executive "may" state that the internal audit activity conforms with the *Standards* only if the results of the quality assurance and improvement program support this statement. However, standard 1322 states that when nonconformance impacts the overall scope or operation of the internal audit activity, the chief audit executive must disclose the nonconformance and the impact to senior management and the board. It is illogical for the disclosure of conformance with the *Standards* to not be required or even encouraged in standard 1321, yet the disclosure of nonconformance is a "must" requirement. Also, there is an inconsistency between the "must" requirement in 1322 and the "should" requirement in 2431.

In addition, it is unclear where or how standard 1321 intends for the chief audit executive to state that the internal audit activity overall conforms with the *Standards*. For purposes of individual engagements, the language in standard 2430 more clearly indicates that the statement of conformance with the *Standards* is to be included in the communication of the engagement results.

Continued Use of Consulting Terminology in the *Standards*

We remain concerned about the confusion that may result from the IIA's characterization of some forms of internal audit engagements as "consulting" engagements. In our earlier letters commenting on the *Exposure Draft of Proposed Changes to the Professional Practices Framework* (April 30, 2007), and the *Exposure Draft of Proposed New and Amended Standards for the Professional Practice of Internal Auditing* (May 20, 2003), we stated that the use of the term "consulting" services to cover internal audit work other than assurance services is problematic

because it provides a connotation that the internal auditor may not be independent. However, while we do have concerns with consulting terminology as stated above, we do commend the IIA for the addition of standard 2120.C3 regarding internal auditors not assuming management responsibilities for managing risks.

Comments on Specific Standards

We also have the following comments regarding specific standards included in the exposure draft.

Organizational Independence – 1110

The phrase “to fulfill its responsibilities” is too vague. We suggest combining this standard with standard 1110.A1, as follows: “The chief audit executive must report to a level with the organization that allows the internal audit activity to be free from interference in determining the scope of internal auditing, performing work, and communicating results fulfill its responsibilities.”

Impairment to Independence or Objectivity – 1130.A1

This standard should be expanded to also include current responsibilities. We suggest revising the standard to read: “Internal auditors must refrain from assessing specific operations for which they have current or were previously responsibilities. Objectivity is presumed to be impaired if an internal auditor provides assurance services for an activity for which the internal auditor had responsibility within the previous year.”

Also, a one year cooling-off period may not be sufficient in some circumstances, depending on the extent of auditor responsibility taken and the length of time impacted by the auditors’ actions. We suggest adding an interpretation to provide guidance on situations where more than one year may be needed for the cooling-off period depending on the facts and circumstances of the potential impairment.

Impairment to Independence or Objectivity – 1130.A2

This standard places a requirement on someone from outside the internal audit activity. We believe that the *Standards* should only include requirements for the chief audit executive, internal auditors, or the internal audit activity.

Impairment to Independence or Objectivity – 1130.C2

The definition of “the engagement client” is not clear. We suggest revising the standard as follows: “If internal auditors have potential impairments to independence or objectivity relating to proposed consulting services, the chief audit

executive must disclose these potential impairments must be made to the board and senior management engagement client prior to accepting the engagement.”

Proficiency – 1210.C1

This standard should be broadened to cover all engagements, not just consulting engagements. We suggest deleting standard 1210.C1 and adding the following to standard 1210: “The chief audit executive must decline to perform an engagement or obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.”

Due Professional Care – 1220.A1

Illegal acts, abuse, and violations of provisions of contracts or grant agreements are additional considerations for internal auditors in government audit organizations and we encourage the IIA to include those items in the standard. We suggest addressing this issue as an interpretation to provide guidance to internal auditors in government audit organizations, such as: “The exercise of due professional care by internal auditors in government audit organizations also includes considering the possibility of illegal acts and violations of provisions of contracts or grant agreements as appropriate, based on the audit objectives. Also, if during the course of the audit, auditors become aware of abuse that could be significant to the program under audit, they should ascertain the potential effect on the program within the context of the audit objectives.”

Due Professional Care – 1220.A3

The phrase “must be alert” is awkward and does not clearly indicate the intended requirement. We suggest deleting this standard and adding language similar to the second sentence of standard 1220.A3 to the end of standard 1220. Also, we suggest moving the concept of the first sentence to a new standard 2120.A3, which would be similar to the wording of 2120.C1. Our suggested wording for 2120.A3 is: “During assurance engagements, internal auditors must address risk consistent with the engagement’s objectives.”

Continuing Professional Development – 1230

The standard is too vague to be implemented consistently. It does not contain a requirement for a specific number of hours of continuing professional development or a description of the types of continuing professional development activities that would meet the requirements. Also, it is unclear whether the intent of the requirement is for auditors to complete only coursework or whether activities such as on-the-job training, reading, teaching, writing articles, or serving on professional committees would meet the requirement. Since there is no minimum amount of continuing professional development and no definitions of what qualifies, how does an internal auditor know whether he or she met the requirement?

Quality Assurance and Improvement Program – 1300

GAO, the AICPA and the IAASB have developed guidance and standards on quality control systems. These systems are much more extensive than internal and external assessments. For example, the policies and procedures included in a quality control system under GAO standards address: (a) leadership responsibilities for quality within the audit organization, (b) independence, legal, and ethical requirements, (c) initiation, acceptance, and continuance of audit and attestation engagements, (d) human resources, (e) audit and attestation engagement performance, documentation, and reporting, and (f) monitoring of quality. We suggest using this material or that of the AICPA or IAASB to provide more robust standards on quality control systems.

Managing the Internal Audit Activity – 2000

We suggest revising this standard to delete the use of the word “ensure.” As discussed above, we do not agree with using the word “ensure” in the *Standards*. We suggest revising the standard as follows: The chief audit executive must effectively manage the internal audit activity so that ~~to ensure~~ it adds value to the organization.”

Communication and Approval – 2020

We disagree with this standard because it requires senior management to approve the audit plan. Because senior management is often the auditee, the standard would lead users to conclude that the auditor lacks independence from senior management. Even if only the board approved the audit plan, the *Standards* should not include requirements for actions to be taken by boards. We believe the phrase “for review and approval” should be deleted.

Internal auditors in government audit organizations have a duty of accountability to the public. Including a requirement for them to gain the approval of senior management for their audit plan is not consistent with their duty of accountability to the public. If the standard is not changed in accordance with the above, we suggest addressing this issue as an interpretation to provide guidance to internal auditors in government audit organizations, such as: “Since internal auditors in government audit organizations also have a duty of accountability to the public, it is important for the chief audit executive to be sufficiently removed from political pressures to conduct audits and report findings, opinions, and conclusions objectively without fear of political reprisal. Consequently, for these types of internal audit activities, management approval of the audit plan is not required.”

Risk management – 2120.A3 (suggested new standard)

Please see comments under standard 1220.A3 above.

Risk management – 2120.C1

We suggest deleting the phrase “and be alert to other significant risks” for consistency with the suggested addition of standard 2120.A3 and our comments under standard 1220.A3 above.

Engagement Objectives – 2210.A3

If management has not established adequate criteria to determine whether objectives and goals have been accomplished, internal auditors may need to develop appropriate criteria to use in their evaluation. However, internal auditors need to be careful that they do not make decisions for management regarding the appropriate criteria for management’s use.

Identifying Information – 2310

Other standards setters, including the IAASB, AICPA, PCAOB, and GAO have revised their evidence standards to state “Auditors must obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions.” We suggest revising this standard to be consistent with other standards setters.

Quality of Communications – 2420

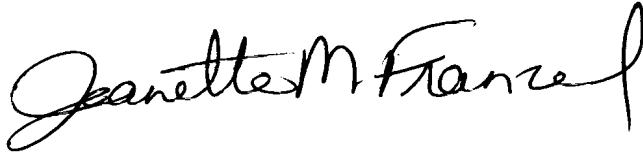
The qualities for communications listed in standard 2420 are not appropriate requirements for inclusion in a standard. GAO has moved similar language from being part of the requirements in the standards to being included as supplementary guidance material in the latest revision of the standards. This change was made because the qualities for communications do not indicate requirements for auditors or audit organizations, and it would be impossible to document compliance with these “requirements.”

Disseminating Results – 2440.A1

This standard does not contain a “must” or “should” requirement, but rather uses the phrase “is responsible for” which is not consistent with the description of requirements in the remainder of the *Standards*. We suggest revising this standard to be a “must” requirement for consistency with other standards of comparable importance and using the phrase “those charged with governance.” We suggest the following as revised wording for the standard: “The chief audit executive must ~~is responsible for communicating~~ the final results to those charged with governance and to parties who have the authority to give ~~can ensure that the results are given due~~ consideration.”

We thank you for considering our comments on these important issues as we work together on issues of mutual interest to the accountability profession.

Sincerely yours,

A handwritten signature in black ink that reads "Jeanette M. Franzel". The signature is fluid and cursive, with the first name being the most prominent.

Jeanette M. Franzel
Director
Financial Management and Assurance

cc:

Mr. Harold Monk, Jr., Chair
U.S. Auditing Standards Board

The Honorable Mark W. Olson, Chairman
Public Company Accounting Oversight Board

Mr. James M. Sylph, Technical Director
International Auditing and Assurance Standards Board