

METHODOLOGY FOR CONDUCTING AN AUDIT OF THE INTERNAL CONTROL SYSTEM OF A BUSINESS PROCESS

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The purpose of this article is to demonstrate the possibility of improving the methodology for conducting an audit of the internal control system of a company's business process by developing an audit technology and providing practical recommendations for conducting an internal audit.

The results of this work can be useful to a wide range of people: from internal auditors - for using it as a manual - to company executives interested in conducting an assessment of the internal control system of business processes.

Modern trends in corporate operations are associated with the increasing role and importance of internal control in achieving company goals. Executives at large companies are beginning to understand that business success is only possible with a clearly structured and effective internal control system.

The goal of internal audit is to assess the effectiveness of a company's internal control system, but it should be noted that achieving this goal is a very labor-intensive and resource-intensive process. Therefore, auditors often evaluate the internal control systems of individual business processes or companies.

The assessment of the internal control system is carried out in accordance with the COSO IC model [7]. When conducting an audit of the internal control system, a comprehensive assessment of all elements that make up this system is carried out:

1. components of the IMS (control environment, risk assessment, control procedures, information and communication, monitoring);
2. goals whose achievement is monitored (operational goals, reporting goals, compliance goals);
3. four organizational levels (function (business process) level, operating unit (division) level, division (business line) level, organization (group) level).

According to the model updated in 2013, 17 principles are identified that help to cover the entire internal control system as fully as possible.

Thus, when auditing a business process, the effectiveness of the entire ICS as a whole and each element of the ICS in particular is assessed.

Regarding the methodology for conducting an internal control system audit, there is currently no standard methodology for this type of audit. This is not surprising, as internal auditing is primarily aimed at improving a company's operations. Therefore, a company has the opportunity to develop its own audit methodology that best suits the specific needs of its operations.

On the other hand, it's not worth assuming that there's no foundation upon which companies build their methodologies. In theory and practice, there are some common approaches to ICS auditing. For example :

- International professional standards of internal auditing define the general principles for conducting an audit [5];
- International Standards on Auditing ¹and PCAOB Standard ²(in particular, Auditing Standard No. 5, “Auditing Internal Control Over Financial Reporting That Is Integrated into an Audit of the Financial Statements”) [8];
- The methodology for conducting an internal audit review described in the article by I.A. Krasnova “Methodology for conducting an internal audit review of the effectiveness of the internal control system of business processes” [3];
- An alternative methodology for auditing the internal control system, most frequently used in the banking sector, is presented in the article by N.M. Zavarikhin, Yu.V. Potekhina “Methodology and methods of internal audit in commercial banks” [2] and many others.

Having analyzed existing auditing methods, as well as international auditing standards, we propose to highlight the following main stages of conducting an audit of the internal control system.

Let's consider the main elements of the methodology for conducting an internal control system audit.

1. Planning the audit

Audit planning is one of the key stages. The audit planning process includes analyzing information, creating an audit brief (defining process objectives, inherent risks, audit goals, scope of work, and audit schedule), sending a notification, and holding a meeting with the process owner.

When planning, please pay attention to the following points.

- Conducting interviews with consumers of a business process will allow you to learn more about the risks of the process.
- Identifying business process goals can be facilitated by using KPIs (if available in the company), regulations on structural divisions, and target indicators from information for operational meetings.
- Risk maps and previous internal audit reports can be used to identify inherent risks. To determine inherent risks, it is necessary to answer the following questions:

- What can prevent the process from achieving its goal?
- What factors influence the efficiency of the process?
- Where in the process is there potential for inefficient use of resources?
- What factors or events can lead to worsening or slowing down the process.
- To allow audit to optimally plan their time, it's best to send notification of the audit at least 10 business days before the on-site visit. The notification should include the title of the audit, a brief overview of the scope and objectives, the duration, and the contact information for the audit manager and audit team members. This will allow the process owner to assign responsible individuals familiar with the process and plan the time more effectively.
- The "Project Opening" meeting with the process owner should not be neglected. This meeting is crucial for establishing the scope and objectives of the audit and confirming a positive, long-term relationship between auditors and clients.
- Inspection planning should take up 20-30% of the inspection time. The better the planning, the more effective the results. As Abraham Lincoln, President of the United States, said, "If I had eight hours to chop down a tree, I would spend six hours sharpening the axe."

2. Performing the check

Performing a review involves describing the business process, analyzing the process objectives, identifying risks and controls, evaluating the design, and testing the operational effectiveness of the controls.

The main practical recommendations for performing the check are as follows.

- Conducting an analysis of the audited process's objectives will provide insight into significant deficiencies in the process's internal control system. The analysis can be conducted to ensure that the objectives are formulated in accordance with SMART criteria, determining the balance between long-term, medium-term, and short-term goals, and the relationship between the objectives of the audited unit and the corporate center.
- One of the effective ways to validate the design of control procedures is the walk-through method. To do this, you need to select specific transactions or documents and trace their path from start to finish.
- The design of a control procedure is a set of elements that make up a control procedure: risk coverage by control, location of control execution, control performer, information and resources, conditions of execution, scope of control, control method, control evidence, control regulations.

To evaluate control design, it is necessary to establish the connection between business objectives and risks, and between risks and the control procedures that respond to the corresponding risk. A control procedure design is ineffective if the control is absent, the control

does not fully address the risk (the residual risk is higher than acceptable), or there is a conflict of authority.

The presence of control procedures for which no specific risks exist should be further analyzed. It's possible that the control procedure is redundant. The ratio of one risk to one control procedure is not necessarily optimal: one control procedure may cover several risks.

- Testing operational effectiveness involves answering the following questions:
 - How was the control procedure applied?
 - The consistency with which it was applied during the review period?
 - By whom (or through what) was it used?

To conduct testing, it is necessary to determine the testing type (observation, survey, study, or replication). To achieve a higher degree of confidence, it is recommended to test the same procedure using different testing types.

Determining the time period for selecting testing depends on:

- from the presence of assumptions about the presence of inconsistencies;
- testing of this control in previous periods/reports;
- the size of the testing period (quarter, year, etc.);
- frequency of control procedures (daily, monthly, quarterly, etc.);
- control environment.

Determining the test (sample) size depends on:

- from the size of the general population;
- the number of deviations that may occur;
- assessing the risk of ineffective control.
- When selecting a sample, it's important to check the population for homogeneity, completeness, and accuracy. Using statistical sampling methods will allow the obtained results to be generalized to the entire population.
- Since test results are a critical element in the preparation of the audit report, all tests must be properly documented. Working papers must contain sufficient evidence to substantiate the internal audit's observations and/or justify the strengths of the business process (if the internal audit results do not identify any deficiencies or opportunities for improvement in the internal control system of the business process). However, working papers should only reflect the information necessary to support this justification.

All references must be correct: documentation must allow links to be drawn from observations to supporting working papers and, if necessary, to primary documents.

3. Generating a report, completing the audit

At this stage, a conclusion is reached regarding the effectiveness of the internal control system. To reach a conclusion on the effectiveness of the internal control system, it is necessary to evaluate each component of the COSO model for all objectives.

To evaluate a group's business process, it's necessary to evaluate the business process at each company and draw a general conclusion. If the group is divided into divisions based on product category, then it's sufficient to evaluate the business process at a single company within the division.

Basic practical recommendations for writing a report:

- The internal audit report contains two parts: introductory and substantive. The introductory part of the "Audit Report" provides general information about the audit, such as :
 - purpose, object and subjects of verification;
 - composition of the audit team, timing of the audit.

The descriptive part of the Audit Report is the most voluminous and informative block, containing all the results of the audit.

- Typically, the final version of the "Audit Report" is presented to: the audit client – the person who initiated the audit; the owner of the business process being audited ; and other interested users at the discretion of the head of the company's internal audit department.
- Don't neglect the "Project Closure" meeting with the process owner. The purpose of this meeting is to discuss the strengths and weaknesses of the internal control system and discuss any corrective actions taken or planned based on the internal audit findings.

Internal auditing of internal control systems is currently the subject of debate among academics and practitioners in this field. The practical significance of this article lies in demonstrating that having a methodology for conducting an audit facilitates the internal control system audit process and improves its effectiveness. The methodology developed and described in this article is not mandatory for all companies. Each company is free to develop and implement its own methodology.

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