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COSO Workshop

Workshop Objectives

- Describe the call-to-action that COSO presents to Internal Auditors

- Examine some of the key points in the framework

- Discuss the implications of the framework on an entity's plan

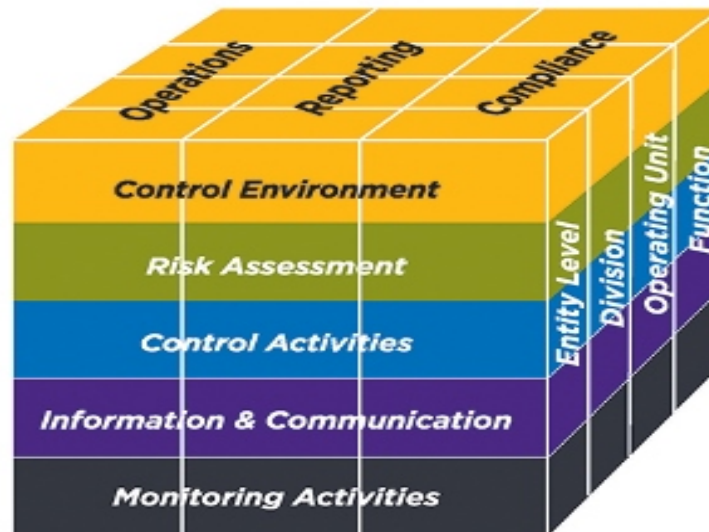- Discuss the implications of the framework on IA activities

The IIA Says that...

- Internal Auditors need to envision new ways to add value to their organization, and the profession as a whole.

Poll

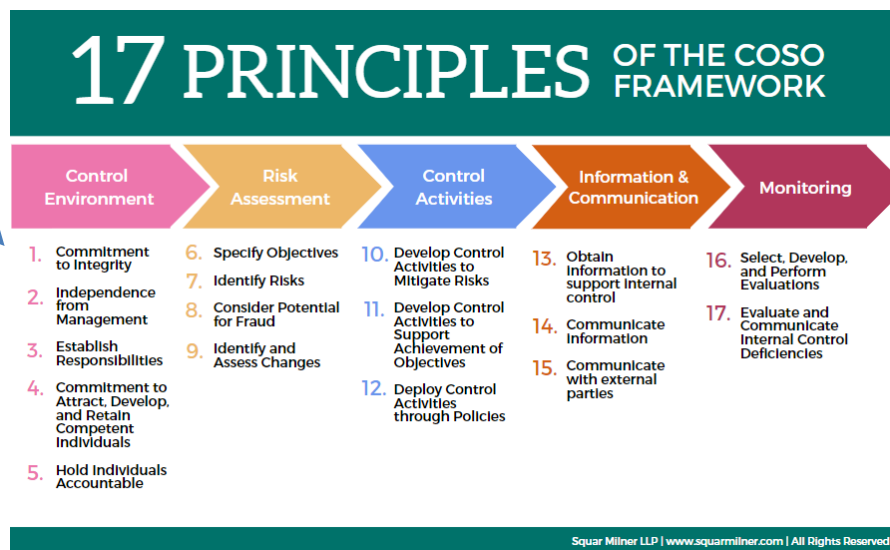**Do you use the COSO Framework when Planning your Audits?**

Yes or NO?

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These are your Risks
Which is the most important Component?

Do we really audit for this?

17 PRINCIPLES OF THE COSO FRAMEWORK

Control Environment	Risk Assessment	Control Activities	Information & Communication	Monitoring
1. Commitment to Integrity	6. Specify Objectives	10. Develop Control Activities to Mitigate Risks	13. Obtain Information to support internal control	16. Select, Develop, and Perform Evaluations
2. Independence from Management	7. Identify Risks	11. Develop Control Activities to Support Achievement of Objectives	14. Communicate Information	17. Evaluate and Communicate Internal Control Deficiencies
3. Establish Responsibilities	8. Consider Potential for Fraud	12. Deploy Control Activities through Policies	15. Communicate with external parties	
4. Commitment to Attract, Develop, and Retain Competent Individuals	9. Identify and Assess Changes			
5. Hold Individuals Accountable				

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CE, RA, CA, I/C, M

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COSO was established primarily for

1. External Auditors

2. Internal Auditors

3. Management

4. Shareholders

The Control Environment is best described as

A. The brain of the organization

B. The ethics and values of the organization

C. The heart of the organization affecting the other four components

D. The establishment of Internal Controls

Share Your Thoughts

Attitude

What is the attitude towards internal control within your organization?

Requirements for Effective Internal Control

- Components and principles are present and functioning

- Components operate in an integrated manner

- Additional points to consider:
  - *Components are suitable and relevant to all entities*
  - *Deficiencies that preclude conclusion*

- Other (management's process)

Roles and Responsibilities

- Board of directors

- Senior management

- Business-enabling functions

- Other personnel

- Internal auditor function

- External parties

Poll: An organization's directors, management, external auditors, and internal auditors all play important roles in creating a proper control environment.

Senior management is primarily responsible for

A. Establishing a proper organizational culture and specifying a system of internal control.

B. Designing and operating a control system that provides reasonable assurance that established objectives and goals will be achieved.

C. Ensuring that external and internal auditors adequately monitor the control environment.

D. Implementing and monitoring controls designed by the board of directors.

Deficiencies in Internal Control

🌐 *Internal control deficiency:* A shortcoming in a component or components and relevant principle(s) that reduces the likelihood that the entity can achieve its objectives.

Deficiencies in Internal Control

🌐 *Major deficiency*: An internal control deficiency or combination or deficiencies that severely reduces the likelihood that the entity can achieve its objectives.

- *A component and one or more relevant principles are not present or functioning or components are not operating together.*
- *A major deficiency in one component or principle cannot be mitigated by the presence of another component or principle.*

Deficiencies in Internal Control (continued)

- Management exercises judgment to assess the severity of a deficiency and may establish objective criteria for evaluation and reporting.

- Regulators, standard-setting bodies, or other third parties may also establish criteria for assessing the severity of internal control deficiencies.

Limitations of Internal Control

- Limitations may result from the following:
  - *Suitability of objectives as a precondition to internal control*
  - *Judgment (bias)*
  - *External events beyond the organization's control*
  - *Breakdowns due to human error*
  - *Management override*
  - *Collusion*

Share Your Thoughts

Limitations

What limitations in internal control have you witnessed or are you most concerned about at your entity?

Additional Considerations

- Judgment
- Points of focus
- Controls to effect principles
- Organizational boundaries
- Technology
- Larger versus smaller entities
- Benefits and costs of internal control
- Documentation

Internal control can provide only reasonable assurance that the organization's objectives will be met efficiently and effectively.

One factor limiting the likelihood of achieving those objectives is that

A. The internal auditor's primary responsibility is the detection of fraud.

B. The board is active and independent.

C. The cost of internal control should not exceed its benefits.

D. Management monitors performance.

Control Environment		
Principles	**Points of Focus**	
1 The organization demonstrates a commitment to integrity and ethical values	1	Sets the tone at the top
	2	Establishes standards of conduct
	3	Evaluates adherence to standards of conduct
	4	Addresses deviations in a timely manner
2 The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control	5	Establishes oversight responsibilities
	6	Retains oversight for the system of internal control
	7	Applies relevant expertise
	8	Operates independently
	9	Provides oversight on Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring Activities
3 Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives	10	Considers all structures of the entity
	11	Establishes reporting lines
	12	Defines, assigns, and limits authorities and responsibilities
4 The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives	13	Establishes policies and practices
	14	Evaluates competence and addresses shortcomings
	15	Attracts, develops, and retains individuals
	16	Plans and prepares for succession
5 The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives	17	Enforces accountability through structures, authorities and responsibilities
	18	Establishes performance measures, incentives, and rewards
	19	Evaluates performance measures, incentives, and rewards for ongoing relevance
	20	Considers excessive pressures
	21	Evaluates performance and rewards or disciplines individuals

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nal Auditors

Risk Assessment		
Principles		**Points of Focus**
6	The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives:	
	– Operations Objectives	22a Reflects management's choices
		23a Considers tolerances for risk
		24 Includes operations and financial performance goals
		25 Forms a basis for committing of resources
	– External Financial Reporting Objectives	22b Complies with applicable accounting standards
		23b Considers materiality
		26 Reflects entity activities
	– External Non-Financial Reporting Objectives	22c Complies with externally established standards and frameworks
		23c Considers the required level of precision
		26 Reflects entity activities
	– Internal Reporting Objectives	22a Reflects management's choices
		23c Considers the required level of precision
		26 Reflects entity activities
	– Compliance Objectives	22d Reflects external laws and regulations
		23a Considers tolerances for risk
7	The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed	27 Includes entity, subsidiary, division, operating unit, and functional levels
		28 Analyzes internal and external factors
		29 Involves appropriate levels of management
		30 Estimates significance of risks identified
		31 Determines how to respond to risks
8	The organization considers the potential for fraud in assessing risks to the achievement of objectives	32 Considers various types of fraud
		33 Assesses incentives and pressures
		34 Assesses opportunities
		35 Assesses attitudes and rationalizations
9	The organization identifies and assesses changes that could significantly impact the system of internal control	36 Assesses changes in the external environment
		37 Assesses changes in the business model
		38 Assesses changes in leadership

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Risk Assessment		
Principles		**Points of Focus**
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	– Operations Objectives	22a — Reflects management's choices
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		26 — Reflects entity activities
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		37 — Assesses changes in the business model
		38 — Assesses changes in leadership

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Control Activities		
Principles		**Points of Focus**
10	The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels	39 Integrates with risk assessment 40 Considers entity-specific factors 41 Determines relevant business processes 42 Evaluates a mix of control activity types 43 Considers at what level activities are applied 44 Addresses segregation of duties
11	The organization selects and develops general control activities over technology to support the achievement of objectives	45 Determines dependency between the use of technology in business processes and technology general controls 46 Establishes relevant technology infrastructure control activities 47 Establishes relevant security management process control activities 48 Establishes relevant technology acquisition, development, and maintenance process control activities
12	The organization deploys control activities through policies that establish what is expected and procedures that put policies into action	49 Establishes policies and procedures to support deployment of management's directives 50 Establishes responsibility and accountability for executing policies and procedures 51 Performs in a timely manner 52 Takes corrective action 53 Performs using competent personnel 54 Reassesses policies and procedures
Information and Communication		
13	The organization obtains or generates and uses relevant, quality information to support the functioning of other components of internal control	55 Identifies information requirements 56 Captures internal and external sources of data 57 Processes relevant data into information 58 Maintains quality throughout processing 59 Considers costs and benefits
14	The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of other components of internal control	60 Communicates internal control information 61 Communicates with the board of directors 62 Provides separate communication lines 63 Selects relevant method of communication

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Information and Communication (continued)			
Principles		**Points of Focus**	
15	The organization communicates with external parties regarding matters affecting the functioning of other components of internal control	64	Communicates to external parties
		65	Enables inbound communications
		66	Communicates with the board of directors
		67	Provides separate communication lines
		68	Selects relevant method of communication
Monitoring Activities			
16	The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning	69	Considers a mix of ongoing and separate evaluations
		70	Considers rate of change
		71	Establishes baseline understanding
		72	Uses knowledgeable personnel
		73	Integrates with business processes
		74	Adjusts scope and frequency
		75	Objectively evaluates
17	The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate	76	Assesses results
		77	Communicates deficiencies to management
		78	Reports deficiencies to senior management and the board of directors
		79	Monitors corrective actions

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▶ What challenges does your entity face related to the concepts presented?

▶ What principle do you feel most strongly is present and functioning in your entity?

▶ Is there a principle you feel may not be present and functioning?

▶ Are there one or more points of focus that your entity believes are not applicable to the entity?

Boeing Vision

1. Improving people lives **FAIL**

2. Global reach **FAIL**

3. High-quality products **FAIL**

4. People empowerment **FAIL**

According to COSO, which of the following is the most effective method to transmit a message of ethical behavior throughout an organization?

A. Demonstrating appropriate behavior by example.

B. Strengthening internal audit's ability to deter and report improper behavior.

C. Removing pressures to meet unrealistic targets, particularly for short term results.

D. Specifying the competence levels for every job in an organization and translating those levels to requisite knowledge and skills.

What Do You Know About Our Business?

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What is the Risk? The Chocolate Factory Candy Wrapping

- The company is a specialty chocolate company who prides themselves on quality
- Each piece of chocolate is wrapped by hand. Sales are $5 million
- There are 2 union employees that wrap 1,000 pieces of chocolate per day
- They are supervised by a manager who visits them periodically, instructs them and monitors progress.

Governance, Risk & Control:
Poll: Which of these do you care about?

A. Governance
B. Risk
C. Control
D. All of them

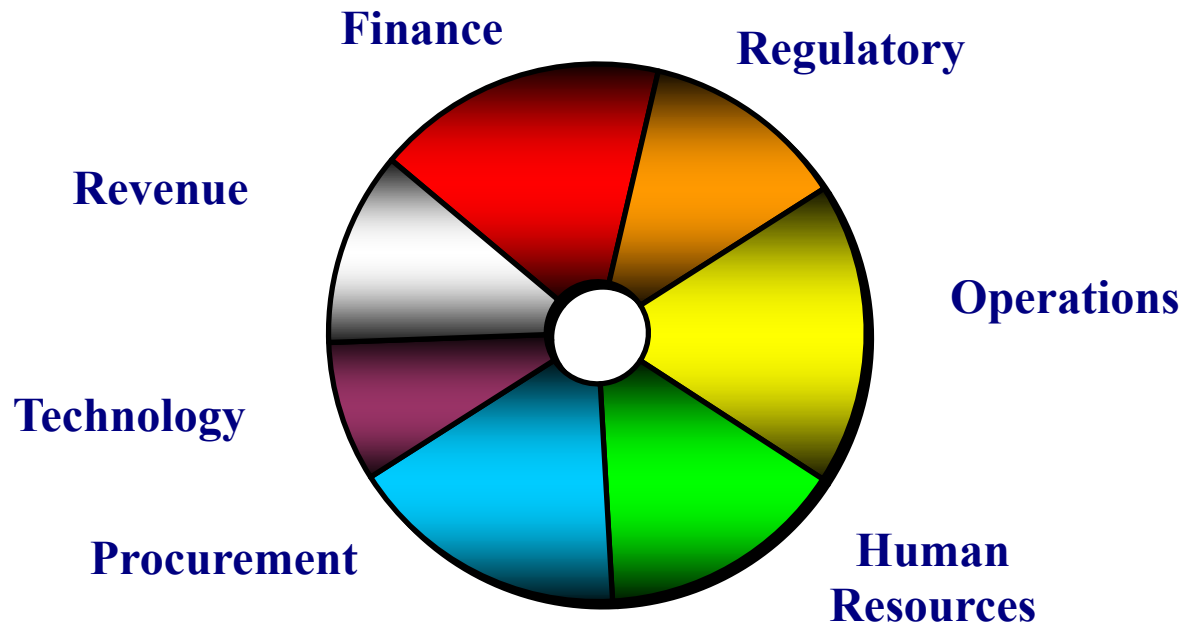# Notre-Dame's Safety Planners Underestimated the Risk, With Devastating Results

Do You have a seat at the table?

1. Yes, Definitely

2. Somewhat

3. Not Really

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What is a Company?
Where Can I Make An Impact

Finance

Regulatory

Revenue

Operations

Technology

Procurement

Human Resources

What is the Control Environment

| Integrity and ethical values | Management's philosophy and operating style | Organizational structure | Assignment of authority and responsibility | HR policies and practices | Competence of personnel |

Risk: <u>That</u> will never happen

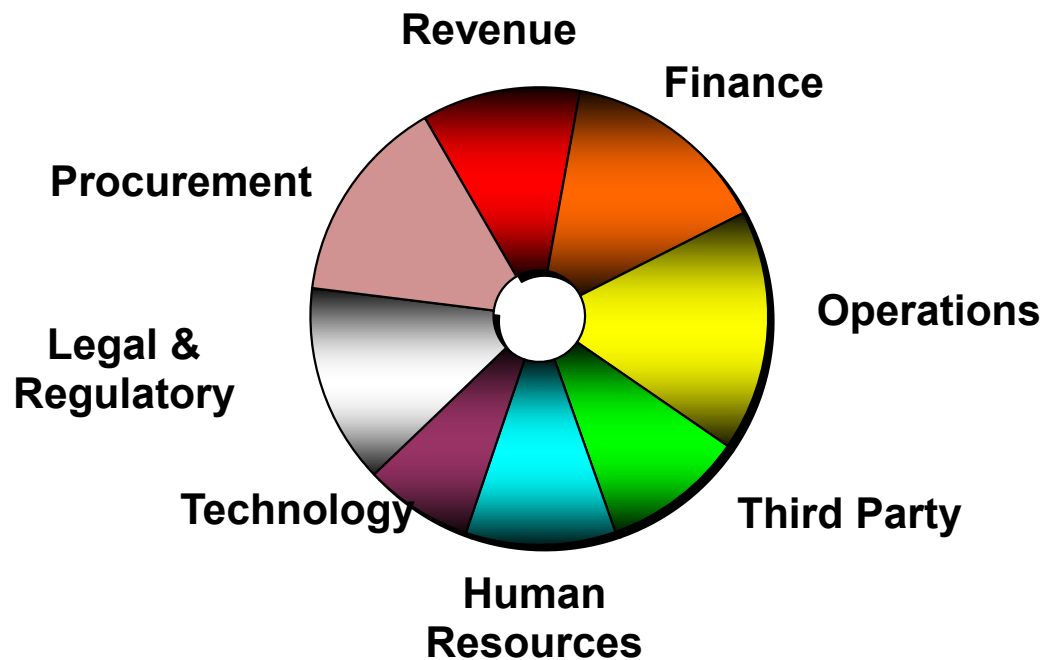The Control Environment Minimizes Risk

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What have we been up against?

- 1999: "Bull Market" and Y2K

- 2001: Terrorism, BCP, and disaster recovery

- 2002: Enron, WorldCom, and Cynthia Cooper

- 2002-2003: Sarbanes-Oxley and PCAOB

- 2004-2007: SOX, SOX, and SOX

- 2008: Implosion of the economy

- 2010: Economic crisis; realignment of coverage

- 2021 Covid 19

What is a Company?
Where is Governance, Risk and Controls?
Think the Unimaginable!!!

Revenue
Finance
Procurement
Operations
Legal & Regulatory
Third Party
Technology
Human Resources

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Auditing Control Environment

⚠️ Start with risk assessment.

📅 Take into account planning considerations.

✓ Require assessment criteria.

⚙️ Require selection of tools/techniques to use.

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The Definition of Internal Auditing
Poll: What is the most important word?

Assurance

Accomplish

Value

Systematic

Internal auditing is an <u>independent</u>, <u>objective assurance and consulting activity</u> designed to <u>add value</u> and <u>improve an organization's operations</u>. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to <u>evaluate and improve</u> the effectiveness of risk management, control, and governance processes.

The Definition of Internal Auditing states the fundamental purpose, nature, and scope of internal auditing.

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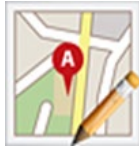
How to Audit the Control Environment- Examples

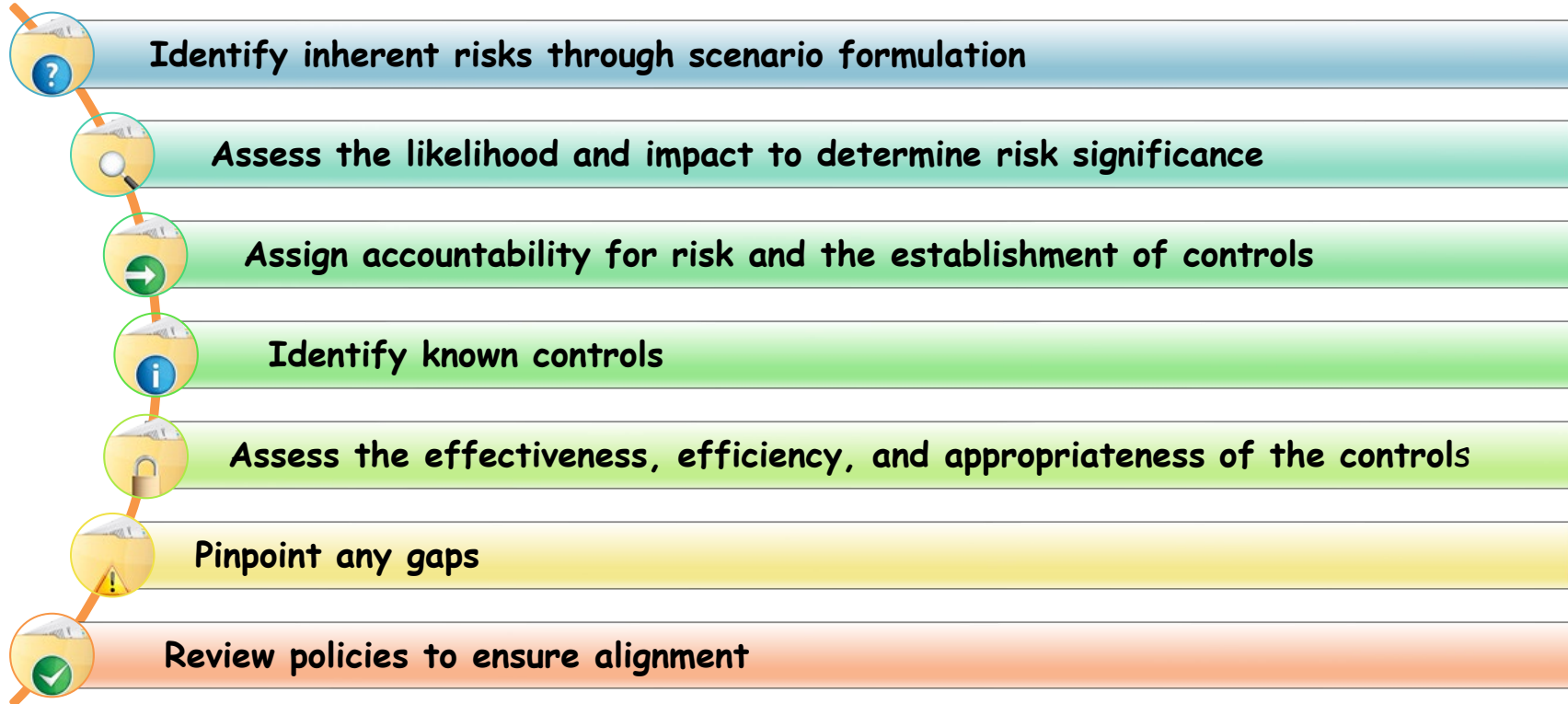|				
Hire and grow ethical employee base	Employees will conduct themselves in an ethical manor	Only authorized employees will have access to assets	Cash payments will be properly accounted for	Cash at point of sale will be secured
Checking activities will be safeguarded	Security over acceptance of cash will be preserved	Purchasing & Billing activities will have oversight	Authentic employees will be paid at agreed to rate and for actual hours worked	Payments will be made for legitimate expenses
Inventory and assets will be protected	Intercultural property will be protected	Employees will not engage in corruptive activities	Conflicts of interest will be reported	Financial reporting will be accurate

Key Steps to Audit the Control Environment

- Identify inherent risks through scenario formulation
- Assess the likelihood and impact to determine risk significance
- Assign accountability for risk and the establishment of controls
- Identify known controls
- Assess the effectiveness, efficiency, and appropriateness of the controls
- Pinpoint any gaps
- Review policies to ensure alignment

5. What Sampling Techniques do you primarily use?

Judgmental

Statistical Sampling

100%

AI

Your Company's Mission

How can you help Your Company accomplish its' Mission

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Who Wins?

Audit the Control Environment
Keep your eyes open, ask questions

What if we Don't

Audit Departments

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Agile Internal Audit to Evaluate Control Environment

Focused on **business value**.

Increased **audit quality** and **reduced cost**.

Accelerated audit **cycles** and **efficient** and **effective** delivery.

Outcome and **value driven**, focused on **risk**. Continuous **prioritisation** of focus areas.

Increased collaboration between **audit team** and **auditee**, improving expectation management and increasing productivity.

Increased and **continuous communications**.

Improved **project visibility** and status **transparency**.

Timely insights delivered by **brief and just in time reporting**.

Reduced waste and **reduced documentation** requirements.

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The IIA Says that...

- Internal Auditors need to envision new ways to add value to their organization, and the profession as a whole.

Q&A

What final questions do you have?