WORLD-CLASS INTERNAL AUDITING

Norman Marks
2019
AUDITING THAT MATTERS

Norman Marks
MATTERS TO........
Fewer than half of the 1,800 respondents are satisfied that internal audit delivers the value to the company it should (45%), and that the internal audit plan properly focuses on the “critical risks to the enterprise” (49%).
“... expectations have risen, and all internal audit functions need to rise to this new floor: providing assurance on a broader range of critical risks and clearly communicating deeper insights.”
Internal audit mission

“To enhance and protect organizational value by providing stakeholders with risk-based, objective and reliable assurance, advice and insight.”
WHAT MATTERS TO THE BOARD AND EXECUTIVES?
- Accounts payable
- Payroll
- Receiving
- Theft and fraud
"Almost all of IA findings are mundane operational compliance issues"

- July 2015
WHICH RISKS MATTER?

- Risks to the achievement of objectives
  - The objectives of the enterprise as a whole
  - The risks that matter to the board, CEO, and the executive team
ENTERPRISE RISK-BASED AUDITING
WHAT MATTERS TO THE BOARD AND EXECUTIVES? RISKS TO:

- Revenue targets
- Earnings targets
- Market share
- Major projects
- Reputation
- And so on......
UNDERSTAND THE BUSINESS
WHAT ARE THE RISKS THAT MATTER?

- What are the organization’s objectives?
- What are the risks to those objectives?
- What are the risks of today and tomorrow?
What are the risks that matter?

- What keeps you up at night?
- What could go wrong?
- What has to go right?
- Where do you spend your time?
- Are your objectives at risk?
- What is on the agenda of the board?
HOW TO IDENTIFY THE RISKS?

- ERM
- Executive interviews
- Operational reports
- Workshops
- IA brainstorming
- Listen and observe!
- Read and think!
A “Working” Inventory of Business Risks, for use by management and internal audit on a periodic basis

**Strategic**
- Strategic Planning
- Capital Investment
- Corp. Organization
- R&D

**Human Resources**
- Availability of Skilled Staff
- Perf/Rewards Alignment
- Workforce management
- Leadership
- Salary Inflation
- Communications
- Morale and Job Satisfaction

**Financial**
- Risk Management - Insurance
- Risk Management - Interest Rates
- Risk Management – Foreign Exchange
- Investments
- Financing
- Tax Strategies
- Debt Compliance

**Operations**
- Capital Projects
- Quality
- Customer Credits/Rebates
- Inventory Management
- Procurement
- Contract Compliance
- Capacity Planning
- Engineering
- Repair Services

**Information Technology**
- Access
- Availability
- Continuity
- System Integrity
- Technology Infrastructure
- Tech Development & Integration
- IT & Business Strategic Alignment
- Outsourcer Management
- Cost Control

**Suppliers**
- Supply
- Pricing
- Quality
- Relationships
- Billing
- Logistics

**Accounting & Reporting**
- SEC Reporting
- Management Reporting
- Statutory Reporting
- Financial Forecasts
- Tax Accounting & Reporting
- Performance Management
- Analyst Communications

**Technology**
- Product Obsolescence

**Rating Agencies**
- Maxtor credit
- Vendor terms (guarantees, advance payments)

**Integrity**
- Management Fraud
- Employee/Theft/Fraud
- Illegal Acts
- Resource Misuse
- Ethics
- Brand Image
- Tone At The Top
- Reputation
- IP Protection

**Customers**
- Customers’ sales
- Planning
- Reliability
- Relationships
- Contracts
- Standards and Expectations
- Customer viability

**Competitors**
- Innovation

**Suppliers**
- Customers’ sales
- Planning
- Reliability
- Relationships
- Contracts
- Standards and Expectations
- Customer viability

**Environment**
- Political
- Legal
- Regulatory
- Business Interruption
- External/Theft/Fraud/Illegal Acts
- Business Practices

**Compliance**
- Environment
CAN WE REACT WITH AGILITY?

- Flexible planning
- Flexible staffing
- Prompt information
- Short, quick steps
AGILE AUDIT PLANNING

- How often should we update the audit plan?
  - Update at the speed of the business
  - Update at the speed of risk
Auditing at the Speed of Risk!

“Internal auditors working from risk-based annual plans.... are increasingly finding themselves addressing yesterday's challenges.”

“Audit plans and coverage should constantly evolve as new, potential risks surface.”
HOW DO WE MONITOR RISKS?

- Listen
- Read management reports
- Read industry news
- Get out into the field
- What is on management’s agenda?
- What is on the board agenda?
- Think for yourself!
“Some people skate to the puck. I skate to where the puck is going to be”

WAYNE GRETZKY
WHAT IS AN EFFECTIVE AUDIT REPORT

- Communicates effectively
- Gets the message across to the speed-reading executive
- Eliminates the unnecessary to focus attention on the essential
- 1 page or less
- Multiple levels of communication
“The true worth of internal audit is not measured in the weight of after-the-fact recommendations, but in the ability to provide just-in-time advice and influence positive change.”

Protiviti
WHAT NOT TO DO....

- Write what you want to say rather than what they need to hear
- Use the audit report as documentation
- Waste time and money – yours and theirs
- Bury value in a mountain of waste
Internal Audit Report
of
<< Legal Entity name >>
Unit Location
Area: << name >>

Date of Report: October 23, 2015

<table>
<thead>
<tr>
<th>Distribution:</th>
<th>Audit Period:</th>
</tr>
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<tbody>
<tr>
<td>SCM Head</td>
<td>July 2014 to June 2015</td>
</tr>
<tr>
<td>Unit Head</td>
<td></td>
</tr>
<tr>
<td>Regional Sourcing Head</td>
<td>Audit Duration: September 4, 2015</td>
</tr>
<tr>
<td>Regional CFO</td>
<td></td>
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<td>Regional President</td>
<td>Closing Meeting: September 4, 2015</td>
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<tr>
<td>Chief Operating Officer</td>
<td>Management Response: November 21, 2015</td>
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<tr>
<td>Chief Executive Officer</td>
<td></td>
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<tr>
<td>Portfolio Head</td>
<td></td>
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<tr>
<td>Corporate Audit Head</td>
<td>Audit Team Member(s): abc</td>
</tr>
<tr>
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</table>

| : abc                              | Report Reference: ABG / CA / Business / year / Area / 001 |

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1. Executive Summary

- Internal audit team has completed review of << areas >> at << Unit >> for the period July 2014 to June 2015. Review of aspects like procurement planning and monitoring, Receipt of material, Quality check and Inventory management formed part of the audit scope.

- Based on the draft report issued on October 23, 2015, we have received the management response on November 21, 2015, which is appropriately incorporated in the report.

- Audit finding noted during review has been classified under moderate risk category and attributable cause being categorized under – ‘non compliance to laid down guidelines due to people’.

- Summary of key audit findings is as under -

### Table A: Risk categorization of audit findings

<table>
<thead>
<tr>
<th></th>
<th>Total</th>
<th>Major</th>
<th>Moderate</th>
<th>Minor</th>
</tr>
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<tbody>
<tr>
<td>Count of Findings</td>
<td>1</td>
<td>-</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>Cause Analysis</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Absence of process</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Design gap in process</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Non-compliance due to</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- People</td>
<td>1</td>
<td>-</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>- Technology</td>
<td>-</td>
<td>-</td>
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</table>

### Issue in brief

- Actual material load carried vis-à-vis RTO imposed load restriction (15 MT / tanker) is not monitored by the Supply Chain team. During the period July ’14 – July ’15, total of 102,498 MT of extra load (with a margin of 2MT over and above RTO limit) was carried, which, yielded the transporters possible extra earnings of Rs 12.9 million approximately. Load restriction was the primary reason for revising the base transportation rates in June 2014.

### Management Action Plan

Post audit, we started working on tanker overload issue and collected the permissible load limit for all the tankers mentioned in the RC book. We were informed that the overloading is due to the operational limitations at all loading terminals for liquid cargo. We have already started monitoring the loaded weight for the tankers against permissible load for all tankers on a daily basis. This will become part of our daily MIS which is visible to all stakeholders. Taking into consideration the operational realities (in absence of metering devices at terminals), we are going to bring down the variation within 1 MT for the time being. Appropriate actions has already initiated in this area.
### Risk Ratings:

- **High**
  - Absence of a key control (e.g., not measuring trucks) or detected failures of a key control greater than 20%.
- **Medium**
  - Detected failures of a key control between 5% and 20%.
- **Low**
  - Detected failures of a key control less than 5%.

### Control Descriptions

**On-Site Receiving:**
- **R.1 Authorization** – All trucks are authorized to enter the plant.
- **R.2 Inspection** – The gate visually inspects trucks when entering the plant. Necessary quality certificates are obtained or created.
- **R.3 Scaling (In/Out)** – All trucks are scaled in and out to determine the metal weight. Weighting tickets are entered into the system immediately.
- **R.4 Weight Determination** – Any containers and non-aluminum packaging materials are correctly deducted when determining the metal weight.
- **R.5 Scale Calibration** – All scales are regularly calibrated.

**On-Site Shipping:**
- **S.1 Authorization** – All trucks leaving with aluminum are properly authorized (sales order or stock transfer order, etc.).
- **S.2 Scaling (In/Out)** – All trucks are scaled in and out to determine the metal weight. Weighting tickets are entered into the system immediately.
- **S.3 Weight Determination** – Any containers and non-aluminum packaging materials are correctly deducted when determining the shipment weight.
- **S.4 Scale Calibration** – All scales are regularly calibrated.

**Off-Site Storage:**
- **O.1 Receiving/Shipping** – Processes for receiving or shipping metal follow the same procedures as those used at Novelis owned facilities.
- **O.2 Movement Reconciliation** – Movements between warehouses, customer and Novelis plants are reconciled daily.
- **O.3 Physical Inventory** – Physical inventories or written confirmations are obtained regularly with appropriate oversight by Novelis management.

**Tolling:**
- **T.1 Movement Reconciliation** – Movements between tollers and Novelis plants are reconciled daily.
- **T.2 Physical Inventory** – Physical inventories or written confirmations are obtained regularly with appropriate oversight by Novelis management.
- **T.3 Recovery Reconciliation** – Contractually agreed recovery is reconciled against actual recovery on a monthly basis.
<table>
<thead>
<tr>
<th>#</th>
<th>AUDIT FINDING</th>
<th>RECOMMENDATION</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>On-Site Receiving</strong></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td><strong>Weighing of Inbound Shipments</strong></td>
<td>Management should require all metal entering and leaving the plant to be weighed. The scale weights should be used as the measurement to adjust inventory in the system.</td>
</tr>
<tr>
<td></td>
<td>Inbound coils from a third party supplier, [redacted], are not weighed. The scale at the plant is not build to handle coils from [redacted]. There is also no scale outside at the security gate. The weights on the bills of lading from [redacted] is entered in the system without verification.</td>
<td><strong>Owner:</strong> [redacted], Plant Controller</td>
</tr>
<tr>
<td></td>
<td>As a result, metal inventory balances may be inaccurate which could impact production planning and result in inaccurate inventory balances.</td>
<td><strong>Management Comment:</strong> Management will implement a random spot check by measuring width and build up to calculate weight vs. BOL. We have also begun the process to understand the cost and feasibility of installing scales.</td>
</tr>
<tr>
<td>2</td>
<td><strong>Visual Inspection at Gate</strong></td>
<td>Management should implement policies and procedures to randomly inspect truck trailers when entering and exiting the plant at the security gate. The policy should also include the requirements for documenting the inspection results.</td>
</tr>
<tr>
<td></td>
<td>Visual inspections of inbound and outbound truck trailers are not performed at the security gate.</td>
<td><strong>Owner:</strong> [redacted], EHS Leader</td>
</tr>
<tr>
<td></td>
<td>As a result, trucks could transport unauthorized items on and off the plant premises leading to lost or stolen metal and errors in inventory balances.</td>
<td><strong>Management Comment:</strong> Management will implement a random inspection.</td>
</tr>
</tbody>
</table>
WHAT IS AN EFFECTIVE AUDIT REPORT

- A communication that is read and \textit{acted on} right away
- A communication that \textit{matters}!
- Says what the stakeholder \textit{needs to know} and no more
Communicate what they need to know

January 15, 1995
Audit of Derivatives Trading

• Are there any risk issues of significance to the Audit Committee or executive management? YES/NO

• Are there any outstanding major internal control findings meriting Audit Committee or executive management attention? YES/NO

Distribution:
Audit Committee
Executive and Operating Management
“The AFE process does not meet the needs of the organization. Decisions are not timely and, as a result, business opportunities are lost – rendering null the original business justification. In addition, valuable executive time is expended at the cost of attention to business strategies and execution.”
OUR ROLE AS PRACTITIONERS

1. Focus on providing assurance that matters, on what matters, when it matters
2. *Enterprise* risk-based auditing
3. Communicate the results of our work in business terms, effect on corporate objectives
4. Skate to where the puck is going to be
5. Find a way to use technology ourselves
IIA Internal Audit Principles

- Provides risk-based assurance.
- Is insightful, proactive, and future-focused.
- Promotes organizational improvement.
CAN YOU HELP THE BUSINESS MANAGE AT SPEED?
You have yet to perform an audit I wouldn’t gladly pay for!
Norman helps us stay efficient
Internal audit provides Tosco with a competitive advantage.
PUNCH FEAR IN THE FACE

ESCAPE AVERAGE

DO WORK THAT MATTERS

START.

JON ACUFF
1. INSERT KEY INTO IGNITION
2. SHIFT INTO DRIVE
3. PRESS FOOT FIRMLY ON THE THROAT OF MEDIOCRITY
THANK YOU!

Norman Marks, CPA, CRMA
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OCEG Fellow; Honorary Fellow of the
Institute of Risk Management

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