

▶ Internal Audit for Local Government Units

Principles and Concepts of Internal Control (IC)



Outline of Presentation

- ❑ Definition of Internal Control (IC)
- ❑ IC in the Philippine Government
- ❑ General Objectives of IC
- ❑ The IC Framework
- ❑ Components of IC



What is Internal Control?

Internal control is an **integral process** that is effected by an entity's **management and personnel** and is designed to **address risks** and to provide **reasonable assurance** that in pursuit of the entity's mission, the general objectives are being achieved.

(INTOSAI, 2004)



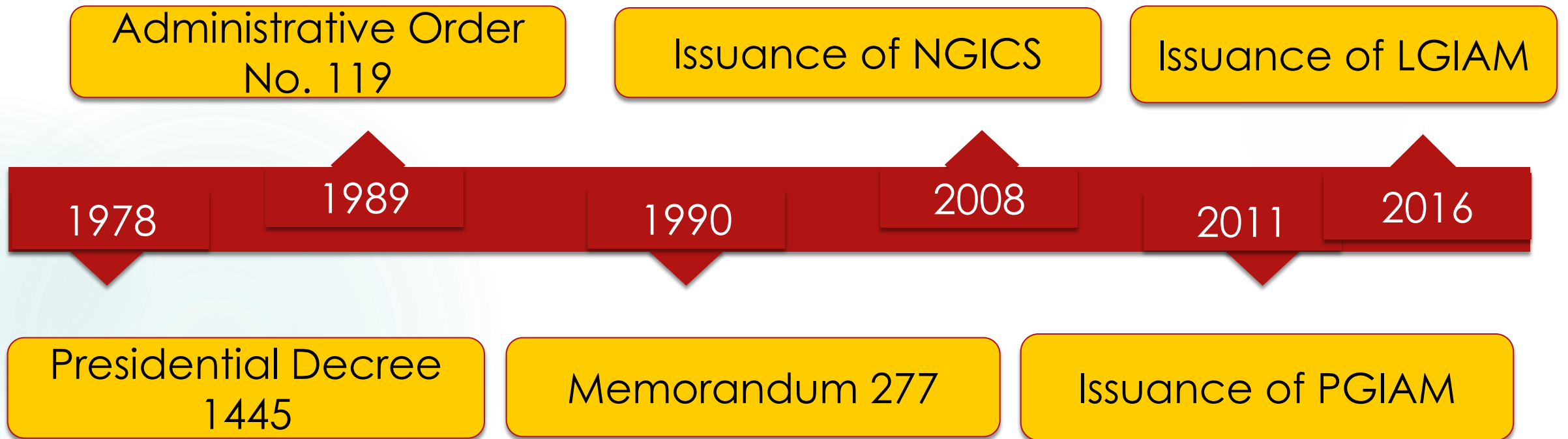
What is Internal Control?

Internal control refers to the plan of organization and all the coordinated methods and measures adopted within an organization or agency to **safeguard its assets, check the accuracy and reliability of its accounting data, and encourage adherence to prescribed managerial policies.**

(Section 123 of Presidential Decree No. 1445, as amended)



IC in the Philippine Government



National Guidelines on Internal Control Systems (NGICS)

An initiative taken by the national government to affirm its **commitment to the citizenry** towards accountability, effective operations, prudence in finances, and quality service. It unifies in one document existing Philippine laws, rules and regulations on internal controls to serve as a benchmark towards designing, installing, implementing and monitoring internal controls in the public service.



Philippine Government Internal Audit Manual (PGIAM)

A complement to the NGICS, explains and clarifies the nature and scope of internal audit in the Philippine public sector, including its institutional arrangements, as well as its protocols and processes. It aims to assist Departments, Agencies, and other instrumentalities of the government in establishing and developing internal audit to promote effective, efficient, ethical and economical operations in government.



Local Government Internal Audit Manual (LGIAM)

A complement to the NGICS, explains and clarifies the nature and scope of internal audit in the Philippine public sector, including its institutional arrangements, as well as its protocols and processes. It aims to assist **LGUs** in establishing and developing internal audit to promote effective, efficient, ethical and economical operations in government.



General Objectives of Internal Control

NGICS

- Safeguard assets
- Check accuracy and reliability of accounting data
- Ensure economical, efficient and effective operations
- Comply with laws and regulations; and
- Adhere to managerial policies



The Internal Control Framework

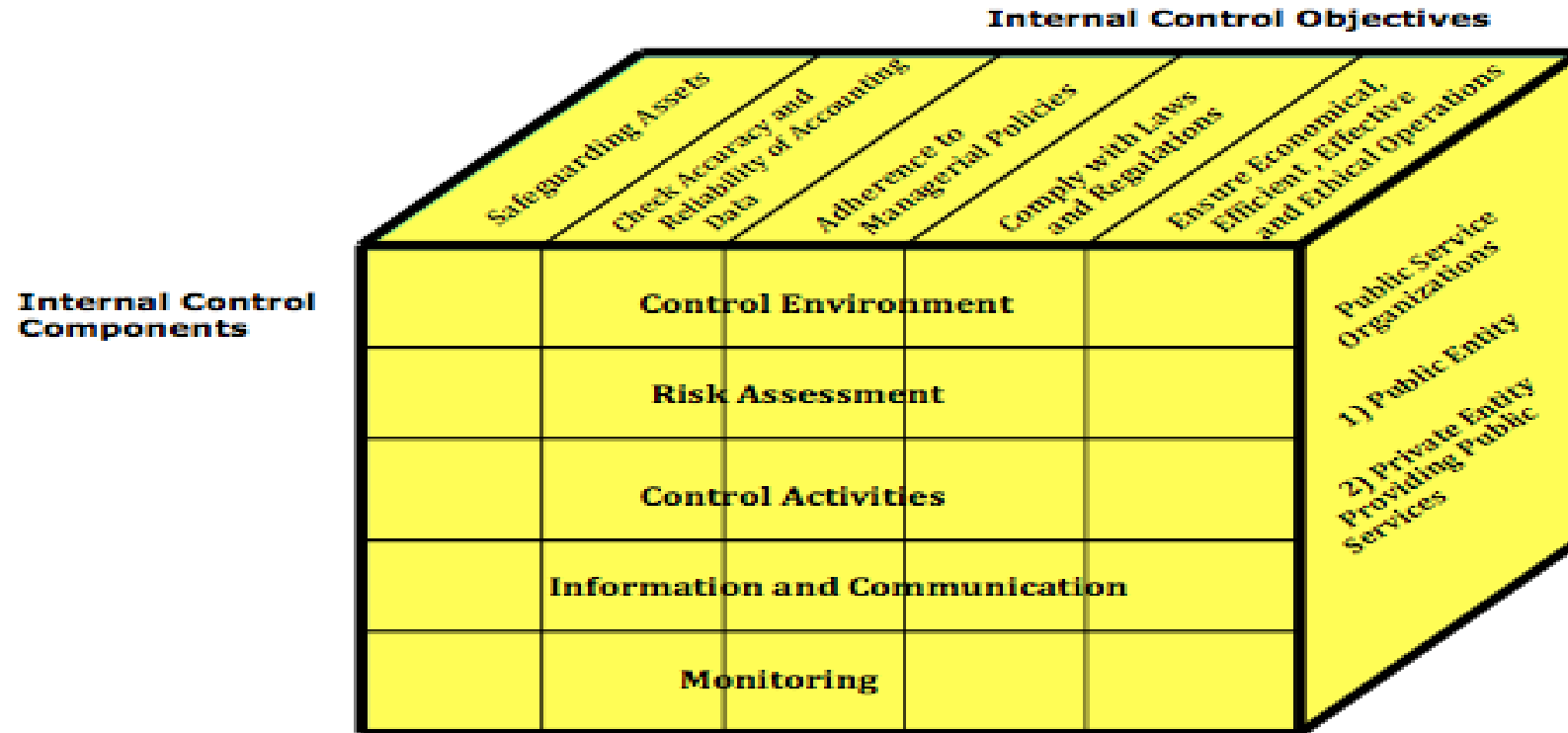


Figure 5 - Internal Control Framework

Components of Internal Control

- Control environment
- Risk assessment
- Control activities
- Information and communication
- Monitoring



Control Environment

Control environment is the general framework serving as basis for the other four components of internal control. It is the scope and coverage of an organization's internal control system which impacts on its structural and operational framework.



Risk Assessment

Risk assessment is the overall process of identifying, analyzing and evaluating relevant risks to the achievement of the control objectives and determining the appropriate response.



Control Activities

Control activities are the policies and procedures established to address risks and achieve the agency's mandate and objectives. Control is a measure that is modifying a risk. Control includes any process, policy, device, practice, or any other action which is intended to modify risk.

Once implemented, control activities are integrated into the control environment of the agency.



Information and Communication

Information and communication are vital in attaining the five control objectives. They go hand in hand and cut across all other internal control components. Information and communication include the records system which will ensure the transfer of required information to employees and top management, to the public it serves, to other public service organizations, and to its network of organizations and sectors that need the information.



Monitoring

Monitoring as a component of internal control is aimed at assessing the quality of the internal control systems' performance over time.



The Internal Audit



Outline of Presentation

- ❑ Definition of Internal Audit (IA)
- ❑ Legal Bases
- ❑ Scope and Functions of IA Unit
- ❑ Internal vs. External Audit
- ❑ Key Benefits and Value of IA to LGUs
- ❑ Principles and Standards of IA
- ❑ Types of IA

What is Internal Audit?

- ❑ We all operate internal controls e.g. when we follow management procedures for filing of documents;
- ❑ Internal audit is a means by which internal controls are checked to determine whether they are well designed and properly operated;

What is Internal Audit?

- ❑ It is not an adversarial function but a problem solving partnership to help LGUs achieve their objectives.
- ❑ The internal audit function provides an objective source detached from regular operating functions that can help LGUs continually improve the design and operation of internal controls.

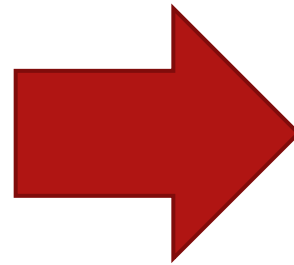


Internal Audit

- Evaluation of management controls and operations performance, and the **determination of the degree of compliance** with:
 - laws,
 - regulations,
 - managerial policies,
 - accountability measures,
 - ethical standards and
 - contractual obligations.

Internal Audit

Appraisal of the plan of organization and all the coordinated methods and measures



Recommend courses of action on matters relating to operations and management controls

Legal Bases of IA

No.	Issuance	Particulars
1	Presidential Decree No. 1	Abolished the IAS created under RA 3456, as amended by RA 4177, and transferred the function to the Management Division
2	Executive Order No. 292 or Administrative Code of 1987	Created an IAS in the Department of Public Works and Highways, and included the supervision of internal audit activities as one of the functions of the Department of Finance's Central Financial Management Office
3	Administrative Order s(AOs) 278 and 70	Provided authority for the creation of an IAS and its functions, duties and activities
4	DBM Budget Circular 2004-4	Highlighted the policy guidelines in the organization, staffing, positions and salary grades of the IAS

Legal Bases of IA

No.	Issuance	Particulars
5	DBM-CSC Joint Resolution No. 1, s. 2006	Provided for the creation of an IAS/IAU with its functions in line with Executive Order No. 366
6	DBM Circular Letter (CL) No. 2008-5	Provided the guidelines in the organization of the IAS and clarified its functions, and the rank and salary grade of the head of the IAS
7	DBM CL No. 2008-8	Provided that the IAS would be composed of a Management Audit Division and an Operations Audit Division, and specified the IAS/IAU's functions related to internal control
8	DBM LBC No. 110	Issuance of the LGIAM

Scope of Internal Audit

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Involves all matters relating to operations and management control:

- **Appraisal** of the adequacy of internal controls;
- **Conduct** of management audit; and
- **Evaluation** of the results of operations, focusing on the effectiveness of controls of operating systems and support services units/systems.



Functions of Internal Audit

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ADVISE the LCE on all matters relating to management control & operations audit

CONDUCT management & operations audit of LGU functions, progs, projs, activities & outputs & determine the degree of compliance with their mandate, policies, govt regulations, established objectives, systems & procedures/ processes & contractual obligations

Functions of Internal Audit Service/Office/Unit

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REVIEW and APPRAISE systems and procedures, organizational structures, asset management practices, financial & management records, reports and performance standards of the LGU

ANALYZE and EVALUATE management deficiencies and assist top management by recommending realistic courses of action

PERFORM such other related duties & responsibilities as may be assigned or delegated by the LCE or as may be required by law



Internal vs. External Audit

	INTERNAL AUDIT	EXTERNAL AUDIT
Function	<p>Advice LCE on matters relating to <u>management control and operations audit</u>;</p> <p>Review and appraise <u>systems and procedures</u>;</p> <p>Identify, analyze and evaluate management deficiencies and recommend courses of action</p>	<p><u>Examine, audit and settle accounts</u>;</p> <p>Conduct comprehensive audit and recommend measures and courses of action;</p> <p>Keep the <u>general accounts of government</u></p>



Internal vs. External Audit

	INTERNAL AUDIT	EXTERNAL AUDIT
Scope	Systems and Processes	All accounts, systems and processes
Approach	Controls-based	Risk-based
Types of Audit	Compliance Audit; Management Audit; Operations Audit	Comprehensive audit (financial and compliance audits); Performance Audits (Value-for Money Audits); Fraud Audit



Key Benefits of Internal Audit (IA) for LGUs

Oversight

- ▶ IA assists LCE by evaluating whether LGU is complying with policies & laws;

Insight

- ▶ IA independent findings on evaluating which policies, programs, projects are working well or not working as well gives unique position to identify better practices & recommend ways to improve service delivery, and

Foresight

- ▶ IA by looking ahead can play major role in identifying risks facing LGU and how to mitigate those risks & identify opportunities.

Value of Internal Audit

Improve the effectiveness of risk management, controls and governance processes.

Instill public confidence in the LGU's ability to operate effectively.

Strengthen the mechanism for ensuring the accountability of LGUs to their respective constituents

Principles and Standards of IA

❑ Conflict of Interest

The internal auditor should avoid conflict of interest at all times, thereby maintaining objectivity and impartiality and upholding public interest.

Principles and Standards of IA

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❑ Objectivity and Impartiality

Objectivity and impartiality requires auditors not to subordinate their judgment on audit matters to that of others.



Principles and Standards of IA

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□ Professional Competence

The internal auditor must maintain high standards of competence and professional integrity commensurate with his/her responsibilities and mandated functions.



Principles and Standards of IA

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❑ Authority and Confidentiality

This requires that the internal auditor acquires information in the course of the audit, with proper and specific authority and should not use or disclose any such information or appear to use the same for personal advantage or for the advantage of a third party.



Principles and Standards of IA

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❑ Code of Conducts and Ethics

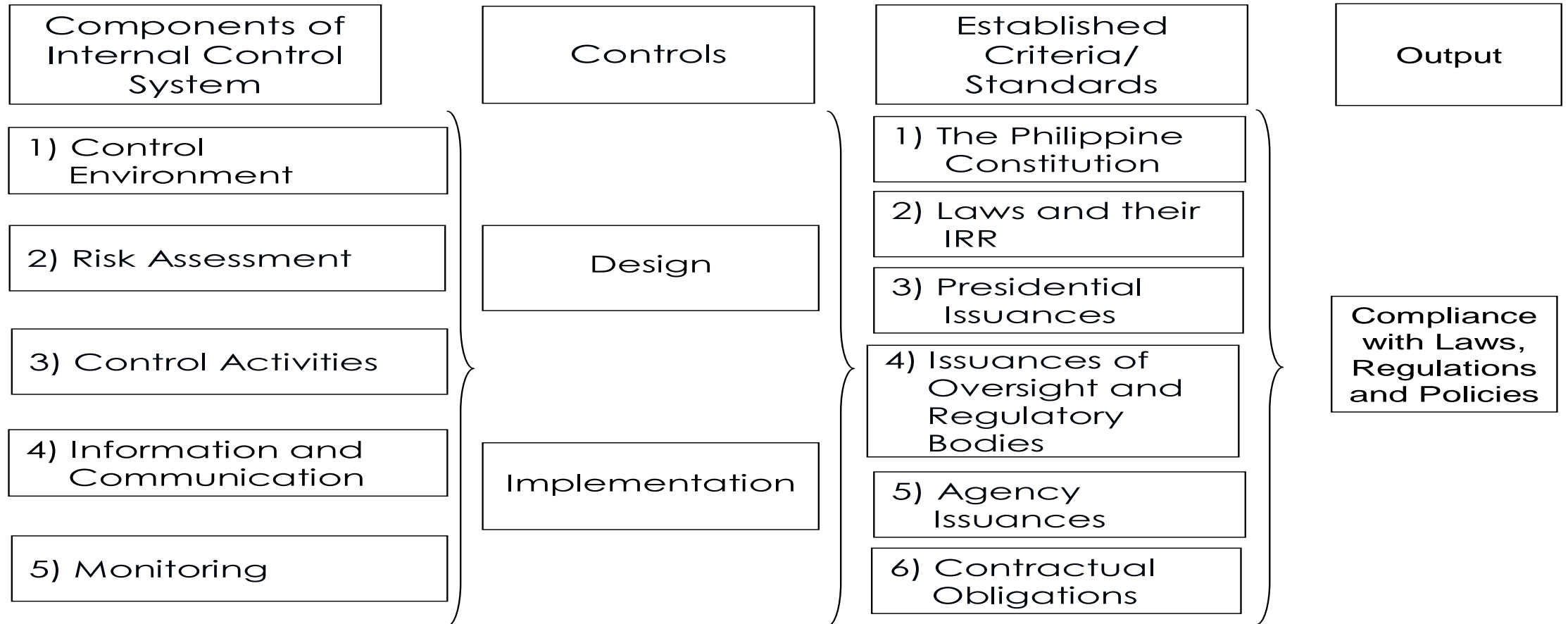
As public servants, internal auditors are bound to comply with the Code of Conduct and Ethical Standards for Public Officials and Employees (RA 6713)



Compliance Audit

Evaluation of the degree of compliance with laws & regulations, policies & procedures in the LGU

Compliance Audit



Source: LGIAM, page 40



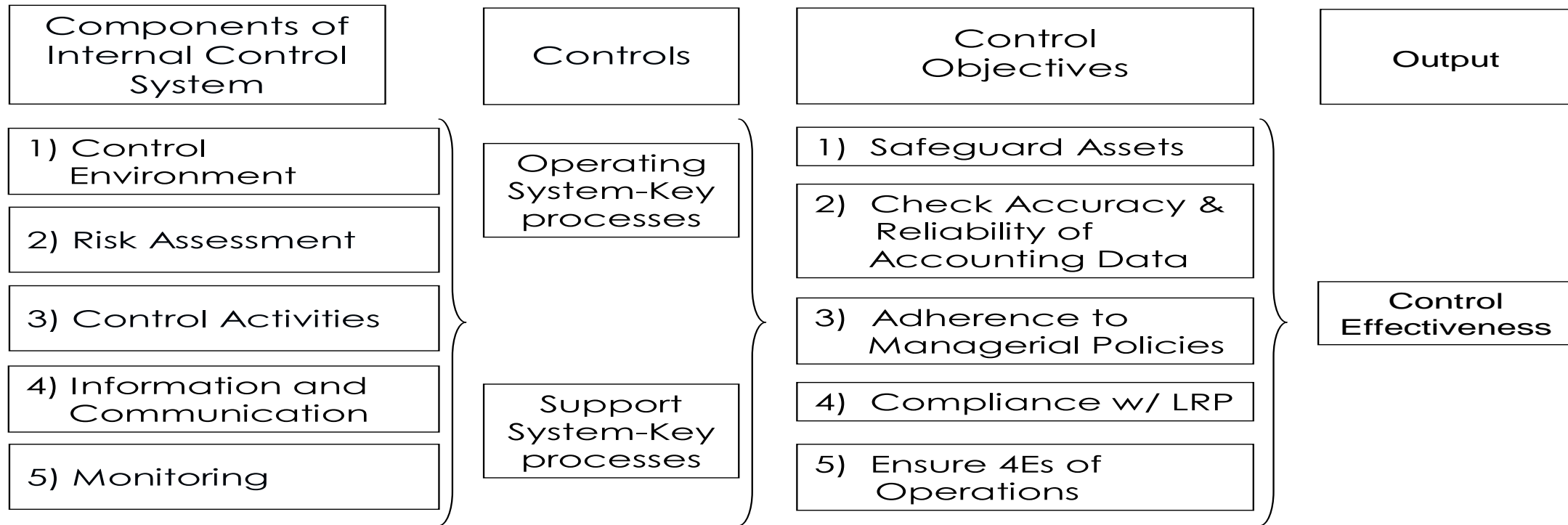
Types of Internal Audit

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Management Audit

Evaluation of the effectiveness of internal controls adapted in the operating & support services units/systems to determine whether they achieve the control objectives over a period of time or as of a specific date

Management Audit



Source: LGIAM, page 41



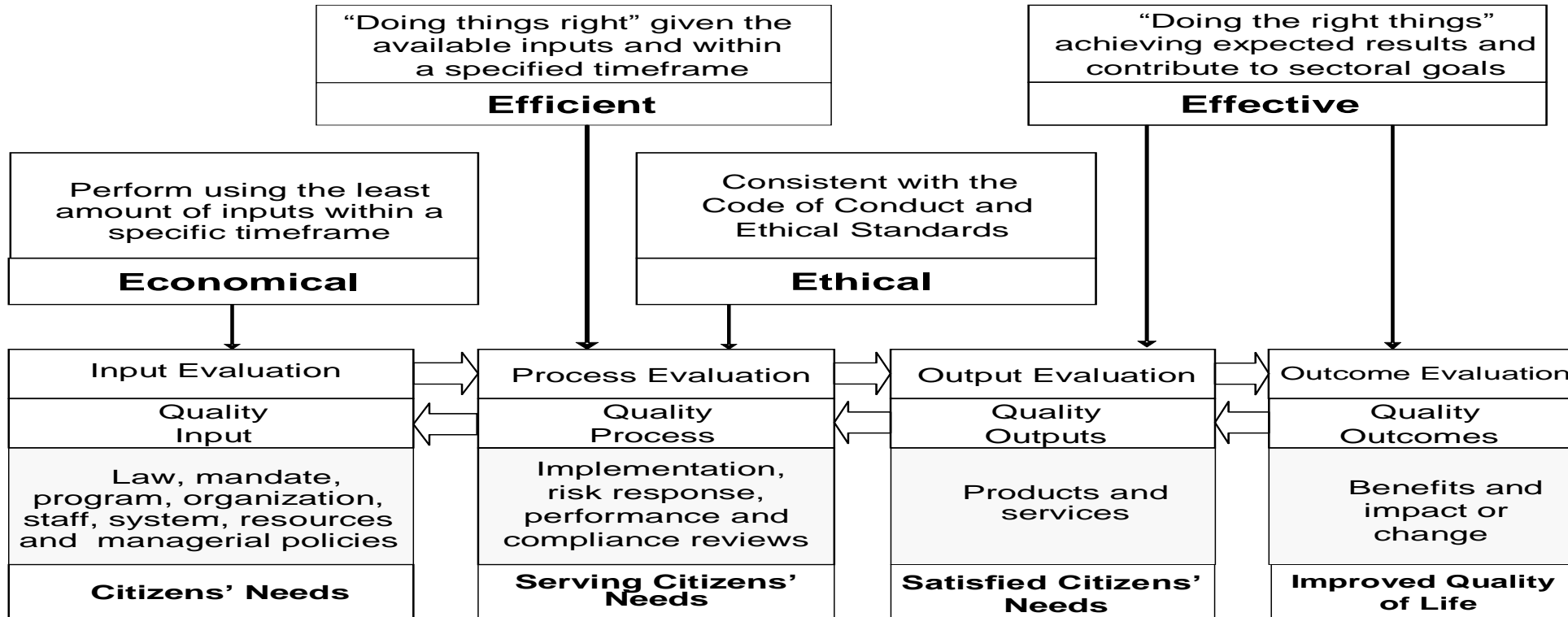
Types of Internal Audit

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Operations Audit

Evaluation of the outcome, output, process & input to determine whether government operations, programs & projects are effective, efficient, ethical & economical, including compliance with laws & regulations, managerial policies, accountability measures & contractual obligations

Operations Audit



Source: LGIAM, page



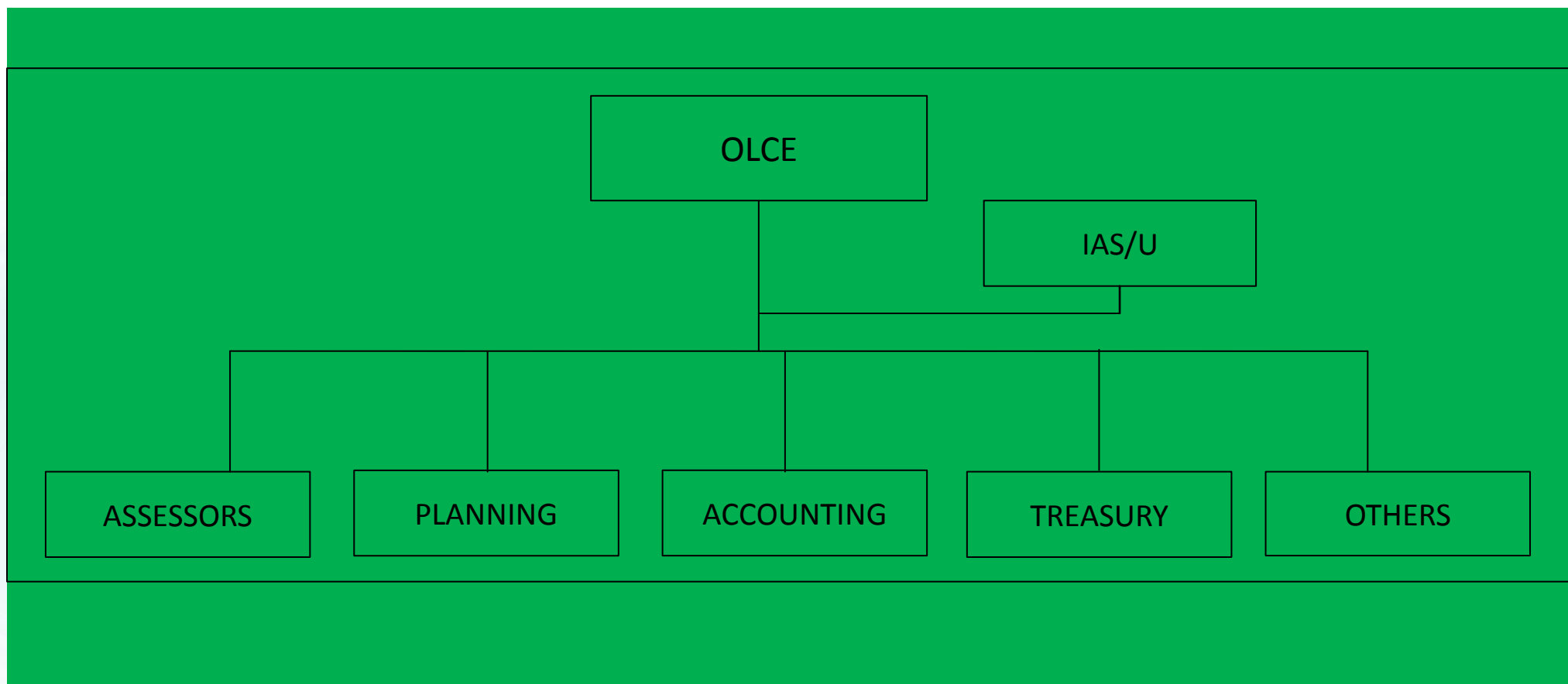
Organizing the Local Government Internal Audit Unit



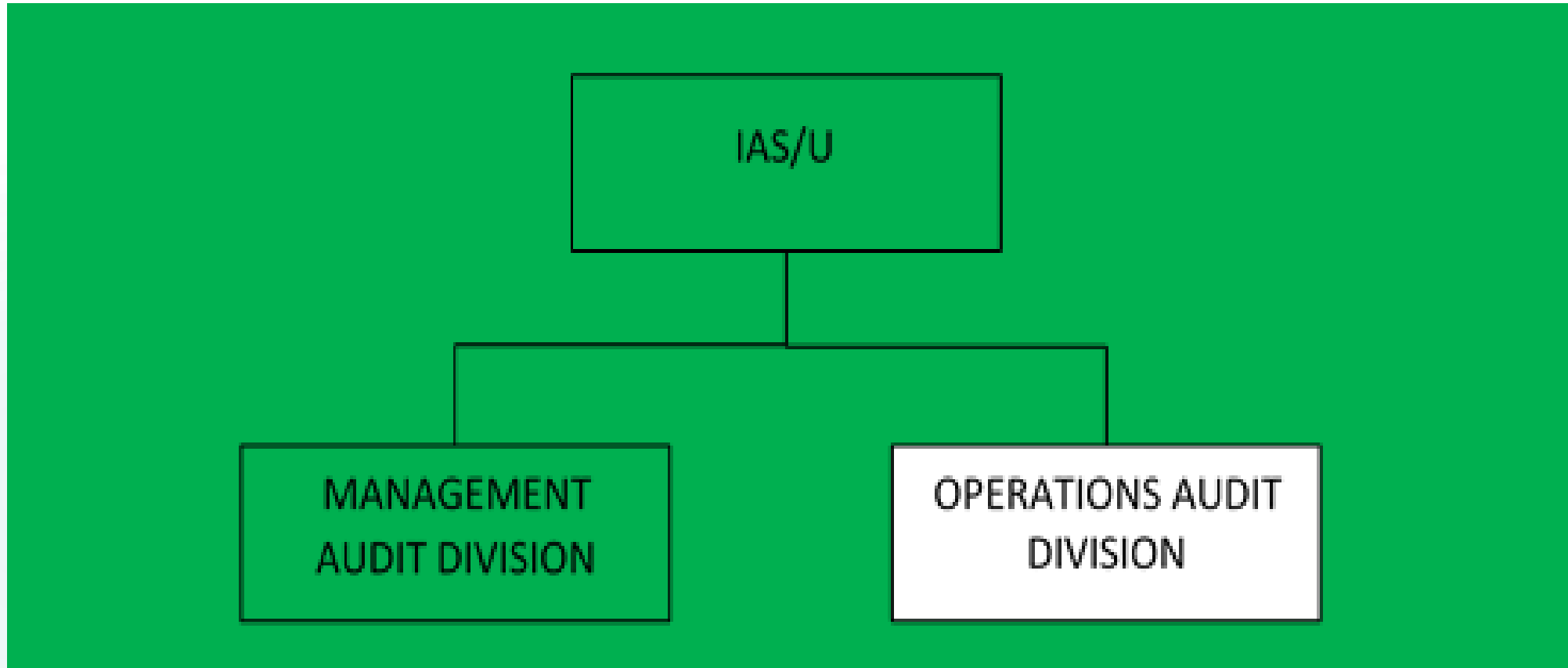
Outline of Presentation

- ❑ Organizational Structure of IA Unit
- ❑ Staffing the IAU
- ❑ Key Strategies for IA Function
- ❑ Key Attributes of the IA Function
- ❑ Roles and Responsibilities of Local Chief Executive, Sanggunian and Head of IA

Organizational Structure



Organizational Chart for IAS/U



Staffing the IAS/U

LGU

Organizational Structure and Head of the IAU

Provincial Government

The IAS/U in a provincial government may be a Department to be headed by a Provincial Government Department Head, SG-26.

City Government Special City

The IAS/U in a special city may be a Department to be headed by a City Government Department Head III, SG-27.

Highly Urbanized City

The IAS/U in a highly urbanized city may be a department to be headed by a City Government Department Head II, SG-26.

Component City

The IAS/U in a component city may be a department to be headed by a City Government Department Head I, SG-25.

Municipal Government Within Metro Manila

The IAS/U in a municipal government within Metro Manila may be a Department to be headed by a Municipal Government Department Head II, SG-25.

Outside Metro Manila

The IAS/U in a municipal government outside Metro Manila may be a department to be headed by a Municipal Government Department Head I, SG-24.



Options in setting up IAS/U for LGUs which exceeded PS Cap

LGUs may resort to full time designation of permanent employees of other units/departments until such time that the PS Cap is no longer exceeded

Key Attributes for Sound IAS/U

- Independent & objective;
- Clear roles & responsibilities;
- Compliant with the PGIAM professional standard of internal auditing;
- Sufficient resources & skills to carry out audit work;
- Regular & timely communication of findings & recommendations;
- Systematic conduct of follow-ups on audit recommendations;
- Continuous monitoring of internal audit effectiveness;
- Proactive auditing & advice;
- Comprehensive & balanced audit plans linked to LGU management of risks; and
- Presence of internal audit assessment mechanism.

Roles and Responsibilities

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- **Local Chief Executive**

- Has the direct responsibility to install, implement, and monitor a sound system of internal control
- Task the IAS/U to undertake the appraisal of the internal control within the LGU
- Disseminates managerial policies through the issuance of guidelines and standards, to guide the personnel in the proper execution of their individual and unit tasks that collectively contribute to the attainment of LGU goals



Roles and Responsibilities

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- **Sanggunian**
- Key role in establishing the IAS/U through the enactment of an ordinance creating the IAS/U
- Providing funding support in accordance with the provisions set out in existing Circulars
- Exercises operational responsibility over IAS/U in that the Head of the IA reports his findings to the Sanggunian.



Roles and Responsibilities

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- **Head of IA (HoIA)**
 - Accountable to the LCE and the Sanggunian, as the case may be, for the efficient and effective operation of the internal audit function
 - Has direct access to the LCE and meets regularly to provide the LCE the opportunity to seek the comments of the HoIA on management control and audit functions, quality of the audit effort and internal controls, and other areas of control as appropriate
 - Provide inputs to the LCE in the following areas:



Roles and Responsibilities

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- Head of IA (HoIA)
 - a) Maintaining accountability for results, norms of conduct, and transparency
 - b) Promoting self-assessment and adherence to professional and ethical standards
 - c) Ensuring that funds are properly utilized in order to attain objectives
 - d) Enhancing management controls to ensure that control objectives are achieved; and
 - e) Ensuring that the 4E's of operations are achieved



Strategic Internal Audit Planning



Outline of Presentation

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- Strategic Internal Audit Planning
 - Definition
 - Importance



Strategic Internal Audit Planning

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- This is the process of identifying the key audit strategic direction of the IA Unit for a three-year period.



Importance of Planning the Audit

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- ❑ Understanding the control environment and the organization;
- ❑ Outlining the scope and objectives of the audit;
- ❑ Establishing the basis for budgeting (time, cost, personnel);
- ❑ Identifying the evidence required to develop the audit findings;

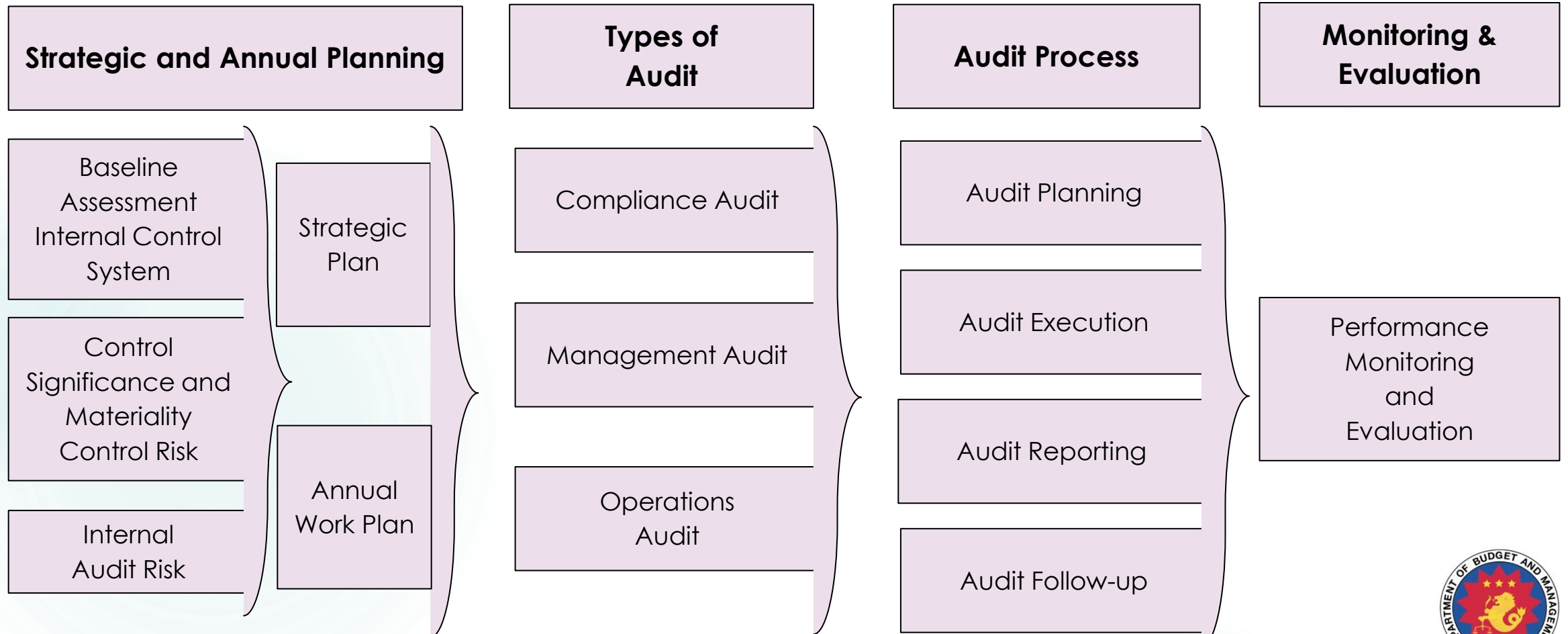
Importance of Planning the Audit

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- Assisting in choosing/determining the audit procedures (nature, extent and timing); and
- Establishing the basis for coordinating the staff.

Planning & Internal Audit Key Process



3 Levels of Audit Planning

Strategic Planning

Annual Work
Planning

Audit Engagement
Planning



Performance Monitoring and Evaluation

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- This is the periodical assessment of internal audit performance and addressing opportunities for improvement which can help maximize the efficiency and effectiveness of the internal audit function.



Performance Monitoring by the Head of IA Unit

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- Review of Progress Assessment Report
- Review of Completion Assessment Report



Performance Evaluation by the LCE

64

- Review of Internal Audit Report
- Review of the IA Unit's Performance Report



Oversight over IA Unit

	COMMISSION ON AUDIT	DEPARTMENT OF BUDGET AND MANAGEMENT
Oversight	Adequacy of IAU as part of internal control system (ICS)	Efficiency and effectiveness of IAU as part of ICS

