COUNCIL’S PEER REVIEW PROGRAM

EXTERNAL QUALITY ASSESSMENT

OF

UNIVERSITY OF NORTH CAROLINA - GREENSBORO

INTERNAL AUDIT FUNCTION

March 2015
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INTRODUCTION

PURPOSE AND OBJECTIVES
As requested by the Internal Audit Director, we conducted a quality assessment of the internal audit function (IA) at the University of North Carolina at Greensboro (UNCG). The principal objectives of the Quality Assessment (QA) were to:

- Assess IA’s conformity to The Institute of Internal Auditors (IIA) International Standards for the Professional Practice of Internal Auditing (Standards)
- Evaluate IA’s effectiveness in carrying out its mission (as set forth in its charter and expressed in the expectations of the UNCG management)
- Identify opportunities to enhance IA’s management, work processes, and value to UNCG
- Identify noteworthy accomplishments

OPINION AS TO CONFORMANCE TO THE STANDARDS
It is our overall opinion that the UNCG IA activity - Generally Conforms. For a detailed list of conformance to individual Standards, please see Appendix A. While improvement opportunities exist in various areas, they did not preclude this assessment. The following major Standards were judged to Generally Conform to the Standards.

- 1000--Purpose, Authority and Responsibility
- 1100--Independence and Objectivity
- 1200--Due Professional Care
- 2000--Managing the Internal Audit Program
- 2100--Nature of Work
- 2200--Engagement Planning
- 2300--Performance of the Engagement
- 2400--Communication of Results
- 2500--Monitoring Progress
- 2600--Resolution of Senior Management Acceptance of Risk

The following Standards were judged as Partially Conforms to the Standards. See discussion under Recommendations and Observations.

- 1300--Quality Assurance and Improvement Program

The IIA’s Quality Assessment Manual suggests a scale of three ratings, “Generally Conforms,” “Partially Conforms,” and “Does Not Conform.” “Generally Conforms” is the top rating and means that an IA activity has a charter, policies, and processes that are judged to be in conformance with the Standards. “Partially Conforms” means deficiencies in practice are noted that are judged to deviate from the Standards, but these deficiencies do not preclude the IA activity from performing its responsibilities in an acceptable manner. “Does Not Conform” means deficiencies in practice are judged to be so significant as to seriously impair or preclude the IA activity from performing adequately in all or in significant areas of its responsibilities.
SCOPE AND METHODOLOGY
As part of the preparation for the QA, the internal audit function prepared an advanced preparation document with detailed information and sent out surveys to its staff and a representative sample of UNCG managers. A summary of the survey results (without identifying the individual survey respondents) have been furnished to the UNCG IA. Prior to commencement of the onsite work by the peer review team on March 2, 2015, the team lead worked with the Internal Audit Director to gather additional background information, select executives for interviews during the onsite field work, and finalize planning and administrative arrangements for the peer review. Extensive interviews with agency/university management and IA staff were conducted. We also reviewed IA’s risk assessment and audit planning processes, audit tools and methodologies, engagement and staff management processes, and a representative sample of IA’s working papers and reports.

RECOMMENDATIONS AND OBSERVATIONS
Recommendations and observations are divided into four groups:

- Recommendations that concern agency/management as a whole and suggest actions by senior management. Some of these are matters outside the scope of the peer review, as set out above, which came to our attention through the surveys and interviews. We include them because we believe they will be useful to agency management and because they impact the effectiveness of IA and the value it can add.
- Recommendations that relate to IA structure, staffing, deployment of resources, and similar matters that should be implemented within IA, with support from senior management.
- Observations that recognize best practices employed by IA leading to a level of performance beyond generally conforming to the mandatory guidance of the IIA.
- Observations of process improvement opportunities for IA to consider in its continuous improvement efforts. These observations do not indicate a lack of conformance to mandatory IIA guidance. They are offered as suggestions for the continued growth of IA’s successful practice.

Significant recommendations are set forth below.

PART I — MATTERS FOR CONSIDERATION OF UNIVERSITY

1. Observation: Lack of Resources

Impairment to organizational independence and individual objectivity may include, but is not limited to: personal conflicts of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations, such as funding. A scope limitation is a restriction placed on the internal audit activity that precludes the activity from accomplishing its objectives and plans. Internal auditors must determine the appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources. *(Standards 1130, 2030)*

Presently, UNCG has two internal auditor positions and one position is vacant. The vacant position is being reclassified to an advanced position with a focus on information technology. The position became vacant December 2014 and has yet to be filled.

Based on a staffing analysis performed by the NC Office of State Budget and Management, the
minimum staffing level at UNCG should be four internal auditors. The lack of resources exposes UNCG to risks that may be unacceptable to management. Without adequate coverage there is no assurance that controls are in place to mitigate the risk level related to accomplishments of business goals and objectives, safeguarding the University’s assets and compliance with laws, rules and University policy.

**Recommendation:** The UNCG Chancellor and Board of Trustees should provide additional resources to UNCG IA which will allow adequate coverage of high risk areas that will remove the scope limitation.

### PART II — ISSUES SPECIFIC TO THE INTERNAL AUDIT ACTIVITY

1. **Observation:** Enhance the Internal Audit Charter

   The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the *Definition of Internal Auditing*, the *Code of Ethics*, and the *Standards*. The nature of consulting services must be defined in the internal audit charter. The mandatory nature of the *Definition of Internal Auditing*, the *Code of Ethics*, and the *Standards* must be recognized in the internal audit charter. The IA Director must periodically review the internal audit charter and present it to senior management and the board for approval. The IA Director should discuss the *Definition of Internal Auditing*, the *Code of Ethics*, and the *Standards* with senior management and the board. (1000, 1000.C1, 1010)

   The IA activity has developed a charter defining the mission, authority, and responsibilities. While the charter addresses these areas at a high level, the IA Manual provides additional details. The IA charter was last updated in 2010 and is not signed by the most recent Audit Committee Chair.

   The IA Charter is the contract between management and the IA function and ensures a full understanding between the parties. The IA charter should clearly define the IA activity’s role and responsibilities, annual planning process, reporting process, monitoring duties, and quality assurance and improvement program. The charter should be signed by the appropriate stakeholders.

   **Recommendation:** Enhance the internal audit charter to fully define for its stakeholders the IA activity's role and responsibilities, including defining consulting service, referencing to the IIA Code of Ethics, and inclusion of the entire IIA Definition of Internal Auditing. Present the enhanced charter to the board for approval, discussing the *Definition of Internal Auditing*, the *Code of Ethics*, and the *IIA Standards*. The charter should be reviewed annually and signed by the current Audit Committee Chair, Chancellor and Internal Audit Director. A model internal audit charter was provided to the Internal Audit Director.

2. **Observation:** Confirm IA Activity Independence to the Audit Committee

   The chief audit executive must confirm to the board at least annually, the organizational independence of the internal audit activity. (1110)
The Director of Internal Audit meets quarterly with the Audit Committee of the Board of Trustees, and also meets in closed session with the Committee annually or as needed. However, there is not an indication the Director confirms to the Committee, at least annually, the organizational independence of the Internal Audit Office as required by the Standards.

**Recommendation:** Confirm to the Audit Committee at least annually, the organizational independence of the Internal Audit Office and develop a process for resolving conflicts.

3. **Observation:** Expand the Annual Risk Assessment and Audit Plan

The internal audit activity’s plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process. (2010.A1)

IA utilizes the Safety and Risk Management Division’s risk assessment and outcomes from the UNC-FIT program to develop an annual audit plan. Although these are two tools that can assist with the risk assessment, IA’s current annual risk assessment focuses only on financial risk. This approach omits critical areas such as information technology and reputational risk.

The first step to assessing risk is identifying the auditable universe. Each item in the auditable universe should be assessed against key risk areas such as: external oversight and influence, organizational governance\(^1\), compliance, reputational, campus safety, and information technology. The items with the highest risk scores should be included on the audit plan.

**Recommendation:** Expand the annual risk assessment and audit plan to: identify the auditable universe; identify key risk areas; assess the auditable universe against key risk areas; seek senior management and board input; and develop an audit plan based on high risk items. Also, the risk assessment should be formally documented.

4. **Observation:** Enhance the Information Technology Competencies and Develop a Long Range Education Plan for the IA Activity Staff

Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities. (1210)

The Director of Internal Audit has worked at UNCG for 30 years. He brings extensive experience however, no experience in the information technology (IT) area. Given the critical nature of IT to the business, knowledge of key IT risks and controls should be enhanced. The IA staff professional proficiency and the collective knowledge, skills, and competencies could be enhanced through obtaining further professional development in information technology. Additionally, it would be beneficial to supplement the quest for current professional certifications with two-three year continuing education plans for all future Internal Audit staff.

**Recommendation:** Based upon the expanded risk assessment that includes IT risks, develop a strategy to enhance the information technology related competencies of the IA activity and the information

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\(^1\) Includes operational, financial and fraud risk
technology scope of work. In the interim, management should enhance the current knowledge with the use of external service providers in a co-sourcing arrangement to conduct audit-related information technology activities.

5. **Observation**: Evaluate and Contribute to Improving the Governance Process

The internal audit activity must assess and make appropriate recommendations for improving the governance process in its accomplishment of organizational objectives (2110).

Internal auditors can act in a number of different capacities in assessing and contributing to the improvement of governance practices. Typically, internal auditors provide independent, objective assessments of the design and operating effectiveness of the organization’s governance processes. They may also provide consulting services and advise on ways to improve those processes.

**Recommendation**: Evaluate and contribute to improving the UNCG governance process. There are a variety of potential projects that meet the scope and intent of the Governance Standard including the following examples:

- Coordinating with management in administering an **employee ethics survey**;
- Participating as a presenter in **employee ethics training**;
- Providing information and training to management and staff members on the COSO model for internal control;
- Participate with the business and information technology strategic planning group; and
- Provide consultation regarding consideration of a **fraud hotline** for taxpayers, students, employees, and others to report suspected fraud, waste, and abuse within the University.

6. **Observation**: Strengthen the Quality Assurance Improvement Program (QAIP)

IA must develop a QAIP that includes both internal and external assessments. Ongoing monitoring of the performance of IA should include periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices. The QAIP must include both internal and external assessments. (Standard 1300, 1310)

Internal assessments must include: ongoing monitoring of the performance of the internal audit activity and periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices. Ongoing monitoring is an integral part of the day-to-day supervision, review, and measurement of the internal audit activity. Ongoing monitoring is incorporated into the routine policies and practices used to manage the internal audit activity and uses processes, tools, and information considered necessary to evaluate conformance with the definition of Internal Auditing, the Code of Ethics, and the **Standards**. (Standard 1311)

External assessments must be conducted at least once every five years by a qualified, independent assessor or team of assessors. These can be in the form of a full external assessment or a self-assessment with an independent external validation. The results should be communicated to senior management. Any nonconformance to the **Standards** should be disclosed to senior management. (Standard 1312, 1320, 1322)
An effective QAIP is the principal means of ensuring continuous improvement of IA. IA reports to the Audit Committee a breakdown of audits completed versus audits planned. However, IA has no process in place to provide reasonable assurance that IA is performing in accordance with the Standards, operates in an effective and efficient manner, and is perceived by stakeholders as adding value and improving the organizational operations.

IA has been in place at UNCG for over 30 years. This is the first external quality assurance assessment performed since its inception.

**Recommendation:** Adopt a process to monitor and assess IA overall performance and use this process to provide continuous improvements. This should include: a) an internal process which may include client surveys, key performance indicators, on-going monitoring and self-assessment; and b) an external process which includes a quality assurance review conducted by a qualified, independent assessor (or team) at least every five years. This process should be documented in the policy and procedure manual.

Results from the QAIP should be communicated to the UNCG senior management and the Audit Committee. Reporting such items such as allocation of audit resources by type of task or performance group, impact of resource limitations, level of risk associated with reported and outstanding and past due action plans, number of management requests, IA financial budget progress, etc., would more fully present past performance and ongoing activities.

**PART III — OBSERVATIONS AND POSITIVE ATTRIBUTES**

1. **Position and Governance**
   The Internal Audit Program is properly positioned within UNCG. The program is appropriately governed by the Chancellor and supported by senior management and the Audit Committee. There are opportunities to further strengthen the relationship of the Internal Audit Program with the university Chancellor and Audit Committee as described in this report.

2. **Audit Committee and Senior Management Support**
   The interviews conducted during this quality assurance review conveyed a high level of support from the university Chancellor, Audit Committee, and senior management.

**PART IV— OBSERVATION OF PROCESS IMPROVEMENT OPPORTUNITIES**

1. **Process improvement:** Use of computer-assisted audit techniques

Audit analytics and continuous auditing software can be of value to the IA activity and the entity as a whole. Powerful tools can help with data extraction and trend analysis to help in the area of fraud prevention and detection, tests of detailed transactions, analytical review procedures, and time and trend analysis.

**Recommendation:** Once IA has gained an IT skill set, IA should explore the possibility of the implementation of analytical tools for use in individual audits and continuous audit monitoring.
We appreciate this opportunity to be of service to the agency. We will be pleased to respond to further questions concerning this report and to furnish any desired information.

____________________________________________________________
Barbara Baldwin, CIA, CPA, CICA
Team Leader
Office of State Budget and Management

____________________________________________________________
Monique Taylor, CFE, CICA, CRMA
University of North Carolina at Asheville
## ATTACHMENT A: Standards Conformance Form – Overall Evaluation Summary

<table>
<thead>
<tr>
<th>PART III: OVERALL EVALUATION</th>
<th>Standards</th>
<th>Major Standards</th>
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**Definitions**

GC – “Generally Conforms” means the assessor has concluded that the relevant structures, policies, and procedures of the activity, as well as the processes by which they are applied, comply with the requirements of the individual Standard or element of the Code of Ethics in all material respects. For the sections and major categories, this means that there is general conformity to a majority of the individual Standards or elements of the Code of Ethics, and at least partial conformity to the others, within the section/category. There may be significant opportunities for improvement, but these should not represent situations where the activity has not implemented the Standards or the Code of Ethics, has not applied them effectively, or has not achieved their stated objectives. As indicated above, general conformance does not require complete/perfect conformance, the ideal situation, “successful practice,” etc.
PC – “Partially Conforms” means the evaluator has concluded that the activity is making good-faith efforts to comply with the requirements of the individual Standard or element of the Code of Ethics, section, or major category, but falls short of achieving some major objectives. These will usually represent significant opportunities for improvement in effectively applying the Standards or Code of Ethics and/or achieving their objectives. Some deficiencies may be beyond the control of the activity and may result in recommendations to senior management or the board of the organization.

DNC – “Does Not Conform” means the evaluator has concluded that the activity is not aware of, is not making good-faith efforts to comply with, or is failing to achieve many/all of the objectives of the individual Standard or element of the Code of Ethics, section, or major category. These deficiencies will usually have a significant negative impact on the activity’s effectiveness and its potential to add value to the organization. These may also represent significant opportunities for improvement, including actions by senior management or the board.
PART I – MATTERS FOR CONSIDERATION OF UNIVERSITY

Recommendation: The UNCG Chancellor and Board of Trustees should provide additional resources to UNCG Internal Audit (IA) ...

One of two internal auditor positions is vacant due to retirement. The vacant staff position has been posted with Human Resources for applicants. The job description has been revised from a mid-level position to an advanced position, with an emphasis on information technology. The annual Internal Audit Activity report of the North Carolina Council of Internal Auditing, which includes staffing recommendations, is reviewed with the Chancellor.

PART II – ISSUES SPECIFIC TO THE INTERNAL AUDIT ACTIVITY

Recommendation: Enhance the internal audit charter ... should be reviewed annually and signed by the current Audit Committee Chair, Chancellor and Internal Audit Director.

Internal Audit will review IIA suggestions regarding the charter. The signature of the current Audit Committee Chair will be affixed to the internal audit charter prior to the May committee meeting.

Recommendation: Confirm to the Audit Committee at least annually, the organizational independence of the Internal Audit Office and develop a process for resolving conflicts.

Internal Audit will discuss organizational independence and conflict resolution with the Audit Committee at the May committee meeting.

Recommendation: Expand the annual risk assessment and audit plan ... Identification of an auditable universe and related risk responses of executive staff will be coordinated with the Office of Enterprise Risk Management and incorporated into audit planning. The Internal Auditor supplements risk identification as a member of the Internal Controls Assessment Committee chaired by the Internal Controls Officer. The audit plan is reviewed with the Audit Committee and approved by the committee.

Recommendation: Based upon the expanded risk assessment that includes IT risks, develop a strategy to enhance the information technology related competencies ...

The rewritten job description of the vacant staff position has been elevated to an advanced level, with an emphasis on information technology. The Director has scheduled a June workshop titled “IT Auditing for Non-IT Auditors” to assist in developing a strategy going forward.

Recommendation: Evaluate and contribute to improving the UNCG governance process ... Internal Audit will evaluate potential matters affecting governance. Information, e.g., internal control guidelines, will be shared with the executive staff. Currently, IA communicates risk
management and internal control via the reporting of external and internal audit activities to the Audit Committee and the Chancellor.

**Recommendation:** Adopt a process to monitor and assess IA overall performance and use this process to provide continuous improvements ...

This initial external quality assessment is the first step. Once the staff position is filled, the Director will enlist the individual’s assistance to identify and establish performance measurement processes.

**PART IV – OBSERVATION OF PROCESS IMPROVEMENT OPERATIONS**

**Recommendation:** Once IA has gained an IT skill set, IA should explore ... analytical tools for use in individual audits and continuous audit monitoring.

Internal Audit has redefined the vacant staff position with the goal of furthering information technology skills. Upon establishment of this resource, IA will evaluate the possibility of enhancing these skills with analytical tools and continuous monitoring.