

October 12, 2021

Grigor Aramyan, Leader of the Risk Assessment and Audit in Practice Working Group, IAD, Head of the Internal Audit Service of the Ministry, Chairman of the Association of Internal Auditors and Accountants of Armenia

How to use this Guide

This methodological guide consists of five chapters:

Chapter 1. Understanding risk-based audit planning

Chapter 2. Categorizing the audit universe for risk-based planning

Chapter 3. Identifying risks and assessing their impact and probability

Chapter 4. Building risk-based strategic and annual plans

Chapter 5. Writing and updating strategic and annual plans

As well as many practical examples

Chapter 1. Understanding risk-based audit planning

What are risks?

- ❑ Risk
- ❑ Inherent risk
- ❑ Residual risks
- ❑ Acceptable risk



Chapter 1. Understanding risk-based audit planning

Understanding the differences between risk management and risk assessment in audit planning

- ❑ **Risk management** is (or should be) an integral part of internal control system and is the responsibility of management.
- ❑ **Audit risk assessment** is part of planning and a process where auditors consider both (i) individual events and related risks and opportunities re. the achievement of the objectives of elements of the audit universe and (ii) generic risk factors that help prioritize work to areas of highest risk.

Resources and targeted planning



Chapter 2. Categorizing the audit universe for risk-based planning

- ❑ An audit universe is a simple way of referring to all (or totality) of all things that an internal auditor could separately examine.
- ❑ **Attention!!! The plan should coincide with the goals of the organization.**
- ❑ Breakdown could be into the following categories:
 - ❑ **by organizational structure** (departments, divisions, units, individual projects);
 - ❑ **by common processes** (payments, receipts, asset management, procurement, contracting, inventory, human resource management);
 - ❑ **by location** (headquarters, regional offices, local offices);
 - ❑ **by operational programs** (issue of driving licences, collection of speeding fines, etc.);
 - ❑ **by service lines** (for example, services for the elderly, services for the handicapped, and childcare services that may be handled by several departments or units).

Chapter 3. Identifying risks and assessing their impact and probability

- **Impact** determines the financial and non-financial consequences for the organization in the event of a risk.
- **Probability** defines the chances that the risk may materialize.

Criteria for assessing impact

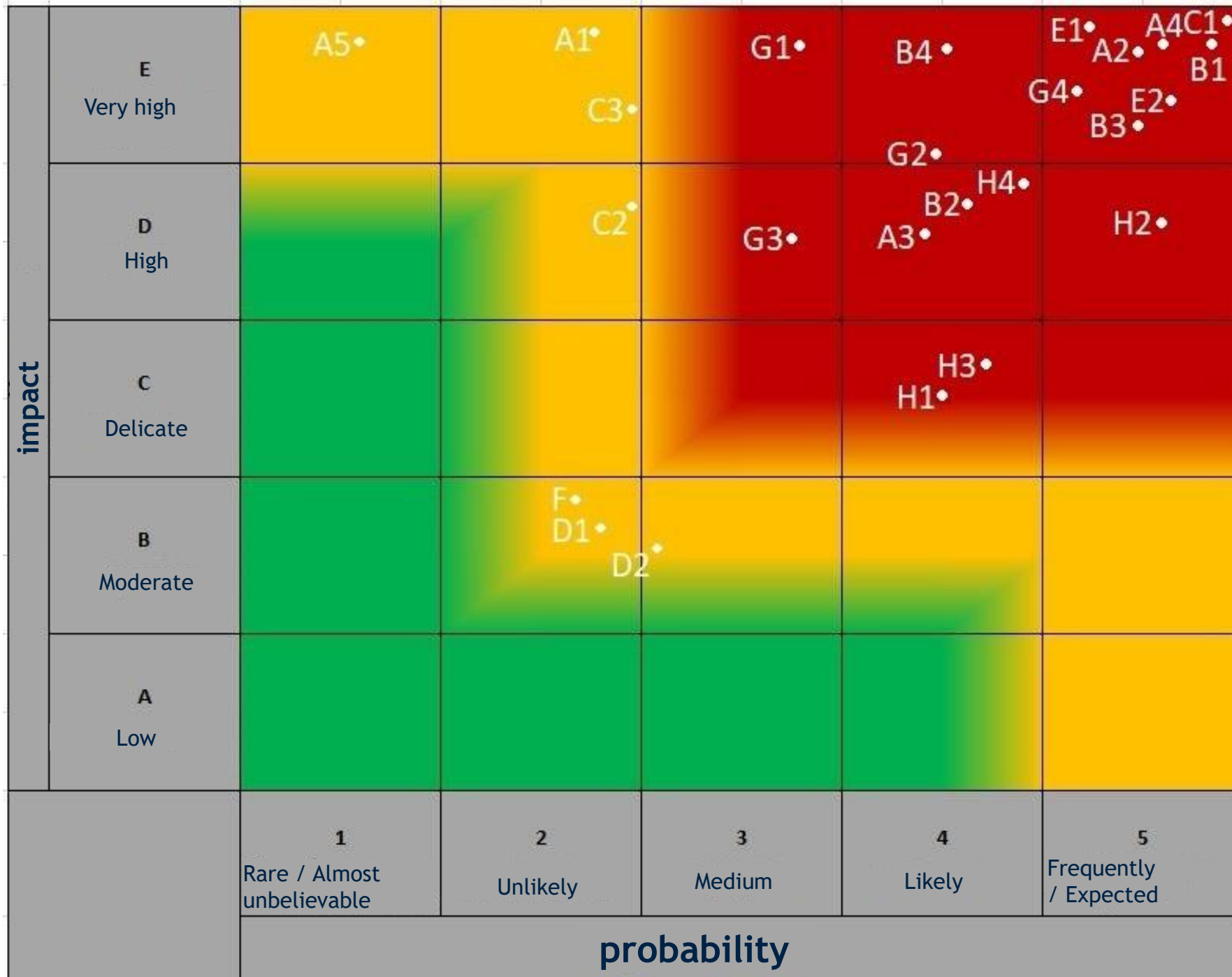
Financial impact.

Impact on reputation.

Regulatory impact.

Impact on mission/achievement of objectives/operations.

Impact on people.



Chapter 4. Building risk-based strategic and annual plans

- ❑ Identification of risk factors
 - ❑ Financial materiality.
 - ❑ Complexity of activity.
 - ❑ Control environment.
 - ❑ Reputational sensitivity.
 - ❑ Scale of the changes.
 - ❑ Opportunities for fraud.
 - ❑ Political sensitivity.
 - ❑ Time elapsed since the latest audit.

Chapter 4. Building risk-based strategic and annual plans

Examples of scoring for risk factors		
For each risk factor, a score of 1 to five is given in accordance with the explanations below.		
Element	Description	Score
A. Materiality	The system accounts for less than 1% of the annual budget	0
	The system accounts for 5-10% of the annual budget	2
	The system accounts for 25-50% of the annual budget	3
	The system accounts for at least 75% of the annual budget	5
B. Control environment / Vulnerability	A well-controlled system with low risk of fraud or error	0
	A rather well-controlled system with some risks of fraud or error	3
	A system with little control in the past and a high risk of fraud or error	5

Chapter 4. Building risk-based strategic and annual plans

Examples of scoring for risk factors											
Step 1. Each of the risk factors is also weighted as per their relative significance.											
	<table border="1"> <thead> <tr> <th>Element</th> <th>Weight</th> </tr> </thead> <tbody> <tr> <td>A. Materiality</td> <td>3</td> </tr> <tr> <td>B. Control environment / Vulnerability</td> <td>2</td> </tr> <tr> <td>C. Sensitivity</td> <td>2</td> </tr> <tr> <td>D. Management concerns</td> <td>4</td> </tr> </tbody> </table>	Element	Weight	A. Materiality	3	B. Control environment / Vulnerability	2	C. Sensitivity	2	D. Management concerns	4
Element	Weight										
A. Materiality	3										
B. Control environment / Vulnerability	2										
C. Sensitivity	2										
D. Management concerns	4										
<p>Step 2. Then the factor scores and weights enter a formula to calculate the risk index.</p> <p>Risk Index = (A x 3) + (B x 2) + (C x 2) + (D x 4)</p>											
<p>Step 3. Each system is then categorized as High, Medium or Low based on the risk index score. For example:</p>											

Chapter 5. Writing and updating strategic and annual plans

□ Strategic plan

- Clearly defined objectives and performance indicators.
- Methodology.
- Information on how IA will work in the most important areas.
- The necessary and available resources to meet these needs.
- Assessment by internal audit of the risk of those events that may have an impact on the achievement of goals.
- Approach for providing follow-up recommendations.

Chapter 5. Writing and updating strategic and annual plans

- ❑ Annual audit plan
 - ❑ Assumptions in the strategic audit plan.
 - ❑ The latest action plan for the year.
 - ❑ Organizational and time constraints.
 - ❑ Resources that need to be reserved for unplanned work.
 - ❑ Alternative audit program on issues postponed to a later period.

Chapter 5. Writing and updating strategic and annual plans

- ❑ Constant updating of plans – regular monitoring of risks.
- ❑ Annual review of the strategic plan.
- ❑ Requests for additional audit during the year.

THANK YOU!

