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# ACRONYMS AND INTERPRETATION

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<tr>
<th>Acronym</th>
<th>Interpretation</th>
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<tbody>
<tr>
<td>AC</td>
<td>Assistant Commissioner</td>
</tr>
<tr>
<td>ACCA</td>
<td>Association of Chartered Certified Accountants</td>
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<tr>
<td>ACL</td>
<td>Audit Command Language</td>
</tr>
<tr>
<td>AIE</td>
<td>Authority to Incur Expenditure</td>
</tr>
<tr>
<td>AICPA</td>
<td>American Institute of Certified Public Accountants</td>
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<tr>
<td>APM</td>
<td>Audit Planning Memorandum</td>
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<tr>
<td>ASCII</td>
<td>American Security Code for Information Interchange</td>
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<td>APSC</td>
<td>Air Passenger Service Charge</td>
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<td>The Authority</td>
<td>Kenya Revenue Authority</td>
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<tr>
<td>BSC</td>
<td>Balanced Scorecard</td>
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<tr>
<td>CA</td>
<td>Chartered Accountant</td>
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<tr>
<td>C A &amp; A</td>
<td>Corporate Affairs and Administration</td>
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<tr>
<td>CAATTs</td>
<td>Computer Assisted Audit Tools and Techniques</td>
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<tr>
<td>CAD</td>
<td>Current Audit File</td>
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<tr>
<td>CFE</td>
<td>Certified Fraud Examiner</td>
</tr>
<tr>
<td>CFS</td>
<td>Container Freight Station</td>
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<tr>
<td>CG</td>
<td>Commissioner General</td>
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<tr>
<td>CIA</td>
<td>Certified Internal Auditor</td>
</tr>
<tr>
<td>CID</td>
<td>Criminal Investigation Department</td>
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<tr>
<td>CISA</td>
<td>Certified Information Systems Auditor</td>
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<tr>
<td>COMESA</td>
<td>Common Market for Eastern and Southern Africa</td>
</tr>
<tr>
<td>COSO</td>
<td>Committee of Sponsoring Organisation</td>
</tr>
<tr>
<td>CPA (K)</td>
<td>Certified Public Accountant (Kenya)</td>
</tr>
<tr>
<td>CPE</td>
<td>Continuous Professional Education</td>
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<tr>
<td>CSD</td>
<td>Customs Services Department</td>
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<td>DC</td>
<td>Deputy Commissioner</td>
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<tr>
<td>The Department</td>
<td>Internal Audit Department</td>
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<tr>
<td>DTD</td>
<td>Domestic Taxes Department</td>
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<tr>
<td>EMU</td>
<td>Efficiency Monitoring Unit</td>
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<tr>
<td>EPZ</td>
<td>Export Processing Zone</td>
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<tr>
<td>FS</td>
<td>Financial Statements</td>
</tr>
<tr>
<td>GAAP</td>
<td>Generally Accepted Accounting Principles</td>
</tr>
</tbody>
</table>
GOK  Government of Kenya
HOD  Head of Department
HQ  Headquarters
HR  Human Resource Department
I & E  Investigation and Enforcement Department
IAS  International Accounting Standards
ICD  Inland Container Depot
ICPAK Institute of Certified Public Accountants of Kenya
ICQ  Internal Control Questionnaire
ICT  Information and Communication Technology
IDEA  Integrated Data Extraction and Analysis
IFRS  International Financial Reporting Standards
IIA  Institute of Internal Auditors
IS  Information Systems
ISACA  Information Systems Audit and Control Association
ISO  International Organization for Standardization
KACC  Kenya Anti-Corruption Commission
KNAO  Kenya National Audit Office
KRA  Kenya Revenue Authority
LAN  Local Area Network
Legal  Legal Affairs Department
LTO  Large Taxpayers Office
The Mission  Internal Audit Mission
MUB  Manufacture under Bond
NCF  Non-Conformity Forms
PAC  Public Accounts Committee
PAF  Permanent Audit File
PRWC  Payment Returns without Cheque
PSV  Public Service Vehicle
QMP  Quality Management Programme
R & CP Research and Corporate Planning Department
RTD  Road Transport Department
SA  Senior Internal Auditor
SDC  Senior Deputy Commissioner
TREO  Tax Remission Export Office
UK    United Kingdom
VAT   Value Added Tax
VFM   Value for Money
The Vision  Internal Audit Vision
WAN   Wide Area Network
PREAMBLE

Introduction

The Internal Audit Department was established under Section 13 of the Kenya Revenue Authority (KRA) Act, Cap 469 of the Laws of Kenya. Section 13(2) of the KRA Act states:

_The Commissioner General shall, subject to the approval of the Board, appoint the head of internal audit, the head of investigation, the head of research and training and other functional heads required by the Authority for the efficient performance of its functions._

The mandate of the department is spelt out under Section 19 of the KRA Act, Cap 469 which states:

_19(1) In addition to any other functions assigned to him by the Board or the Commissioner General, the head of internal audit shall be responsible for the internal audit of the Authority’s accounts and shall submit to the Commissioner General a report on the accounts in respect of every three months of a financial year._

_19(2) The Commissioner General shall submit every report referred to in subsection (1) to the Board for its consideration at the next meeting of the Board after he has received the report and shall also submit copies of the report to the Minister and the Controller and Auditor General._

The overall control, management and administration of the Authority is vested in the Minister of Finance through the Board of Directors and the Commissioner General of the Authority. The internal audit function is controlled by the Head of Internal Audit who reports administratively to the Commissioner General and functionally to the Audit Committee of the Board.

In line with its mandate, the Authority set up a vision statement “_to be the leading revenue authority in the world, respected for professionalism, integrity and fairness._”

The Internal Audit manual has been developed to provide direction, advice and information on the provision of internal auditing services to the Authority. The manual consolidates and brings up-to-date existing guidelines and supports the development of the internal auditing function in the Authority.
The manual is for use by the Authority’s auditors and is tailored to meet the Department’s needs in discharging its duties and responsibilities towards those being audited in the Authority. The manual also provides useful reference material to other stakeholders including accountants, IT staff and external auditors among others.

The manual reflects international best practices in internal auditing as promulgated by the Professional Practices Framework of the Institute of Internal Auditors (IIA Inc). The purpose of the manual is to:

i. Provide guidance to auditors so that they comply with audit procedures
ii. Assist auditors in achieving the highest possible quality
iii. Promote the highest level of professional competence among the auditors
iv. Provide a basis for measuring audit performance
v. Allow others outside the Department to gain a better perspective and understanding of the practices and professionalism of the Department
vi. Assist in the achievement of the strategic objectives contained in this manual and in other important documents adopted by the Authority including but not limited to:
   a. Performance Contracts
   b. The Balanced Scorecard
   c. The Taxpayers Charter
   d. The Corporate Plan
   e. KRA Internal Standards
   f. Anti-fraud and corruption policy
   g. Whistle blowing policy
   h. Human resource code of conduct

Hence, the Department is responsible for conducting an appraisal of all the Authority’s activities, financial and otherwise and giving assurance to the management on the adequacy and effectiveness of all control systems.

The Department also assists management by evaluating and reporting to them on the effectiveness of the controls and ensuring that the laid down regulations and procedures are adhered to. However, it remains the duty of management, not the Internal Audit, to operate an adequate system of internal controls.
Use of the Manual

The manual will assist management to appreciate the role of the Department in assisting the Authority to perform its duties. It will also assist management and other stakeholders to understand the role of the department in enhancing good governance, transparency and accountability in the utilisation of public resources.

Responsibility

Responsibility for ensuring compliance with the manual rests with the Head of Internal Audit.

The Head of Internal Audit is responsible for:

i. Keeping the manual up-to-date

ii. Defining the extent to which powers and duties vested in him may be exercised and performed by the auditors

iii. Giving direction to ensure the proper exercise of the powers and performance of the duties.

Management will be expected to:

i. Give full cooperation to the auditors to ensure their effectiveness in improving the financial management in the Authority

ii. Avail all documents, records and information relevant to auditing work

iii. Provide all the facilities required to enable the auditors to perform their duties effectively.

Exclusions

This manual does not cover procurement and financial procedures, which are the subject of separate manuals. Members of staff are advised to refer to these manuals where required.

Acknowledgements

I would like to appreciate the valuable contribution and roles played by the following in the production of this document:

a. The Board of Directors

b. The Audit Committee of the Board

c. The top management of the Authority

d. The following members of Internal Audit Department’s technical committee that produced this manual: Andrew K. Njoroge – Committee Chairman, Wilson K. Muraya –

Conclusion

It is intended that elements of this manual will be adopted over time as capacity within the department is developed. In order to ensure that the manual is current, the Department recognises that regular changes in the document will be necessary. Therefore, this manual in its entirety will be reviewed when necessary.

The Department is proud of this production. We will fully comply with its direction in the course of carrying out our duties. All new auditors will be required to read, understand and follow the guidelines contained in the manual.

However, the manual should be considered as a working document, subject to amendments as new regulations, rules and working practices are introduced. Suggestions for amendments, additions and improvements to the manual are welcome and should be directed to the Head of Internal Audit.

J.B.K KAMAU
Head of Internal Audit
CHAPTER ONE

100 INTRODUCTION

110 Background

The Internal Audit Department is established under section 13 of the Kenya Revenue Authority (KRA) Act, Cap 469 of the Laws of Kenya. The mandate of the Department is spelt out under section 19 of the same Act. The primary duty of the Department is to assist the management, through accurate and timely reports, to discharge their responsibilities with respect to financial reporting, internal controls and KRA operations, systems and procedures.

111 Management Control Policy

The Authority’s operating procedures and guidelines are contained in various operational, financial and administration regulations. Best practices and modern corporate governance require the adoption of a policy statement for controlling the Authority’s activities. The Management Control Policy is the foundation of all spheres of organisational control, and it is from this policy statement that the financial, operational and administrative regulations are drawn. The policy outlines the management’s responsibility for instituting effective internal controls to ensure that the Authority’s objectives are achieved efficiently.

112 Control Objectives

Management is charged with the responsibility of establishing a network of processes with the objective of controlling the operations of the Authority in a manner which provides the Board of
Directors with the assurance that:

i. Data and information published either internally or externally is accurate, reliable, and timely

ii. The actions of Heads of Departments, Deputy Heads, officers and employees are in compliance with the Authority’s policies, standards, plans and procedures, and all relevant laws and regulations

iii. The organisation’s resources (including its staff, systems, data/information bases and customer goodwill) are adequately protected

iv. Resources are acquired economically and employed efficiently and effectively, quality business processes and continuous improvement are emphasised

v. The organisation’s plans, programs, goals, and objectives are achieved.

113 Management Responsibilities

Controlling is a function of management and is an integral part of the overall process of managing operations. It is therefore the responsibility of managers at all levels of the Authority to:

i. Identify and evaluate the exposures to risk that relate to their particular spheres of operations

ii. Specify and establish policies, plans and operating standards, procedures, systems and other disciplines to be used to minimise, mitigate, and/or limit the risks associated with the exposures identified

iii. Establish practical controlling processes that require and encourage Heads and Deputy Heads of Departments, officers and employees to carry out their duties and responsibilities in a manner that achieves the five control objectives outlined above

iv. Maintain the effectiveness of the controlling processes they have established and foster continuous improvement to these processes.

120 The Internal Audit Charter

The Internal Audit Charter provides a formal definition of the Internal Audit Mission, Objectives, Accountability, Independence, Responsibility and Authority. The purpose of the Internal Audit Charter includes the following:

i. Formalisation of the internal audit function

ii. Documentation of the scope, authority and responsibility of the Department

iii. A blueprint that can be measured against the professional standards
iv. A basis for implementing policies, procedures and guidelines  
v. A basis for reliance by the external auditors  
vi. A marketing document to promote cooperation within the Authority

121 The Vision  
To be the best internal audit service in terms of professionalism, integrity and fairness in the public sector in Kenya and beyond.

122 The Mission  
The mission of the Internal Audit Department is to assist the management and the Board of Directors accomplish their mission by providing assurance and consulting services designed to add value and improve the Authority’s operations. The Department helps the Authority accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

123 Objective  
The objective and scope of the internal audit activity is to determine whether the Authority’s network of risk management, control, and governance processes, as designed and represented by the management, is adequate and functioning in a manner to ensure:

   i. Risks are appropriately identified and managed  
   ii. Interaction between various governance processes occurs as needed  
   iii. Significant financial, managerial and operating information is accurate, reliable and timely  
   iv. Employees’ actions are in compliance with policies, standards, procedures, and applicable laws and regulations  
   v. Resources are acquired economically, used efficiently, and are adequately protected.  
   vi. Programmes, plans and objectives are achieved  
   vii. Quality and continuous improvement are fostered in the Authority’s control process  
   viii. Significant legislative or regulatory issues impacting on the Authority are recognised and addressed properly.

Opportunities for improving management control and the Authority’s image may be identified during audits, and they will be communicated to the appropriate level of management.
124 Accountability

The Head of Internal Audit, in discharging his or her duties, shall be accountable to the Commissioner General and the Audit Committee of the Board: His or her duties are to:

i. Provide an annual assessment of the adequacy and effectiveness of the Authority’s processes for controlling its activities and managing its risks in the areas set forth under the Mission and scope of work

ii. Report quarterly on the significant issues related to the processes of controlling the activities of the Authority, including potential improvements to those processes.

iii. Provide quarterly information on the status and results of the annual audit plan and the sufficiency of the Department’s resources

iv. Coordinate with, and provide oversight of other control and monitoring functions (risk management, compliance, security, ethics and external audit).

125 Independence

To provide for the independence of the Department, the Head of Internal Audit reports administratively to the Commissioner General and functionally to the Audit Committee of the Board in the manner outlined in the above section on Accountability.

126 Responsibilities of the Department

The Department is charged with the responsibility of ascertaining that the ongoing processes for controlling the operations throughout the Authority are adequately designed and are functioning effectively. The Department is also responsible for reporting to the management and the Audit Committee of the Board of Directors on the adequacy and effectiveness of the Authority’s systems of internal control, together with ideas, counsel and recommendations to improve the systems.

The Head of Internal Audit and staff of the Internal Audit Department have the responsibility to:

i. Develop a flexible annual audit plan using appropriate risk-based methodology, including any risks or control concerns identified by the management and submit that report to the Audit Committee for review and approval

ii. Implement the annual audit plan as approved, including, as appropriate, any special tasks or projects requested by the management, the Audit Committee or the Board of Directors

iii. Maintain a professional audit staff with sufficient knowledge, skills, experience and professional certifications to meet the requirements of this charter
iv. Establish a system by which the Head of Internal Audit ensures the quality of internal auditing activities and processes

v. Perform consulting services beyond internal audit’s assurance services to assist management in meeting its objectives. Examples may include process design, training, and advisory services

vi. Evaluate and assess significant merging/consolidating functions and new or changing services, processes, operations and control processes coincident with their development, implementation and/or expansion

vii. Issue quarterly reports to the Commissioner General and the Audit Committee summarising the results of the audit activities

viii. Keep the Audit Committee informed of emerging trends and successful practices in internal auditing

ix. Assist in the investigation of significant, suspected fraudulent activities within the Authority and notify management and the Audit Committee of the results.

127 Authority

The Head of Internal Audit is authorised to:

i. Have unrestricted access to all functions, records, property and personnel of the Authority

ii. Have full and free access to the Audit Committee

iii. Subject to the budget ceilings approved by the Board, allocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish audit objectives

iv. In liaison with the Commissioner General, obtain the necessary assistance of personnel in units of the Authority where audits are performed as well as other specialised services from within or outside the organisation.

The Head of Internal Audit and staff of the Internal Audit Department are not authorised to:

i. Perform any operational duties of the Authority

ii. Initiate or approve accounting transactions external to the Internal Audit Department.

iii. Direct the activities of any KRA employee not working for the Internal Audit Department, except to the extent that such employees have been appropriately assigned to the audit teams or to otherwise assist the internal auditors.
128 **International Standards of Internal Audit Practice**

The Department will meet or exceed the International Standards of Professional Practice of Internal Auditing of the Institute of Internal Auditors (IIA) Inc and those of the Institute of Certified Public Accountants of Kenya (ICPAK).

129 **Code of Conduct**

An auditor is expected to be of the highest ethical and moral standard. Further, he or she must comply with the following:

i. Code of Conduct of the Authority
ii. Code of Professional Standards and Ethics of the Institute of Internal Auditors
iii. Code of professional standards and ethics of a professional association that he or she is a member
iv. The laws of the country, including the Public Officers Ethics Act, the Official Secrecy Act, the Economic Crimes Act.

130 **Audit Committee Charter**

At its 106th meeting held on the 23rd September 2003, the Board of Directors approved the establishment of the Audit Committee of the Board. The terms of reference of the Audit Committee are contained in the Audit Committee Charter, which includes comprehensive details of the purpose, authority, composition, meetings, and responsibility of the Audit Committee. Below is a summary of the Audit Committee Charter.

131 **Purpose**

The purpose of the Audit Committee Charter is to assist the Board of Directors in fulfilling its oversight responsibilities for the financial reporting process, the system of internal control over financial reporting, the audit process, and the Authority’s process for monitoring compliance with laws and regulations and the code of conduct.

132 **Authority**

The Audit Committee has authority to conduct or authorise investigations into any matters within its scope of responsibility. It is empowered to:

i. Retain outside counsel, auditors or others to advise the Committee or assist in the conduct of investigation
ii. Seek any information it requires from employees or external parties; all of whom are directed to cooperate with the Committee’s requests

iii. Meet with the Authority’s officers, external auditors or outside counsel when necessary.

133 Composition
The Audit Committee will consist of at least three and not more than five non-executive members of the Board of Directors. The Board will appoint the Committee members and the Chairperson. At least one member will have professional background in finance and auditing. Each Committee member will be independent as defined by the Board of Directors.

134 Meetings
i. The Committee will meet at least four times a year, with authority to convene additional meetings, as circumstances require. All Committee members are expected to attend each meeting in person or through approved representation

ii. The Committee will invite members of management, auditors or others to attend meetings and provide pertinent information when necessary

iii. The Committee may hold private meetings with the auditors

iv. Meeting agenda will be prepared and provided to members at least seven days in advance along with appropriate briefing materials

v. The Secretary shall prepare the minutes of the meetings.

135 Responsibilities of the Audit Committee of the Board
The Audit Committee is responsible for monitoring, overseeing and evaluating the duties and responsibilities of the management, the Internal Audit Department and the external auditors as far as those duties and responsibilities relate to the Authority’s processes for controlling its operations.

The Audit Committee is also responsible for determining that all major issues reported by Internal Audit Department, the Kenya National Audit Office and other outside advisors have been satisfactorily resolved. Finally, the Audit Committee is responsible for reporting to the full Board all important matters pertaining to the Authority’s controlling processes.

The Audit Committee has the following responsibilities:
**Financial Statements**

i. Review significant accounting and reporting issues, including complex or unusual transactions and highly judgemental areas, and recent professional and regulatory pronouncements, and understand their impact on financial statements

ii. Review with the management and external auditors the results of audits, including any difficulties encountered

iii. Review the annual and quarterly financial statements and consider whether they are complete, consistent with information known to committee members and reflect the appropriate accounting principles

iv. Review other sections of the Annual Report and related regulatory filings and consider the accuracy and completeness of information before release

v. Review with the management and external auditors all matters required to be communicated to the Committee under Generally Accepted Auditing Standards

vi. Understand how the management develops interim financial information and the nature and extent of internal and external auditor involvement

vii. Review the draft Annual Report with the management -- consider whether the report is complete and consistent with information known to the Committee -- before it is presented to the Minister for Finance and Parliament.

**Internal Control**

i. Consider the effectiveness of the Authority’s internal control over annual and interim financial reporting, including information technology security and control

ii. Understand the scope of internal and external auditors’ review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with the management’s responses.
Internal Audit

i. Review with the management and the Head of Internal Audit the Internal Audit Charter, audit plans, activities, staffing and organisation structure of the internal audit function

ii. Ensure that there are no unjustified restrictions or limitations in accessing documents and information within the Authority by the internal auditors

iii. Review and concur on the appointment, replacement or dismissal of the Head of Internal Audit

iv. Review the effectiveness of the internal audit function, including compliance with Standards for the Professional Practice of Internal Auditing of the Institute of Internal Auditors and those of the Institute of Certified Public Accountants of Kenya

v. On a regular basis, meet separately with the Head of Internal Audit to discuss matters the Committee or the Head of Internal Audit believes should be discussed privately.

External Audit

i. Review the external auditors’ proposed scope and approach, including coordination of audit effort with internal audit

ii. Review the performance of external auditors

iii. Review and confirm the independence of the external auditors by obtaining statements from the Auditors on relationships between the auditors and the Authority, including non-audit services and discussing the relationships with the auditors

iv. On a regular basis, meet separately with the Controller and Auditor General or his representative from the KNAO to discuss matters that the Committee or the Auditor believes should be discussed privately.

Compliance

i. Review the effectiveness of the system of monitoring compliance with laws and regulations and the results of the management’s investigation and follow-up (including disciplinary action) of any instances of non-compliance

ii. Review the findings of any examinations by regulatory agencies and auditor’s observations

iii. Review the process of communicating the Code of Conduct to the Authority staff/personnel and of monitoring compliance with the Code

iv. Obtain regular updates from the management and the Chief Legal Counsel regarding compliance matters.
Reporting Responsibilities

i. Regularly report the Committee activities, issues and related recommendations to the Board of Directors

ii. Provide an open avenue of communication between the Head of Internal Audit, the external auditors and the Board of Directors

iii. Review any other reports the Authority issues that relate to the Committee’s responsibilities.

Other Responsibilities

i. Perform other activities related to the Charter as requested by the Board of Directors

ii. Institute and oversee special investigations as needed

iii. Review and assess the adequacy of the Committee Charter annually and propose changes deemed necessary for approval by the Board

iv. Confirm annually that all responsibilities outlined in the Charter have been carried out

v. Evaluate the Committee’s and individual members’ performance on a regular basis.

140 Budgeting

The Department formulates its own budget which will fit in the overall annual budget of the Authority and in line with the corporate plan. To provide adequate time for thorough preparation before the start of a financial year on 1st of July, the budgeting process has to start early in the year.

The Head of Internal Audit should constitute and head an annual budgeting committee. The membership of the committee should be representative of the various sections and levels of seniority within the Department. To facilitate preparation of the budget in time, the Head of Internal Audit should constitute the committee by December every year. The committee should hold weekly meetings which should be recorded and the budget proposals work complete by February.

In preparing the budget, the committee should seek views from members of the Department and make budget proposals that are representative of the needs of the Department. The needs of the Department are those that will facilitate efficient and effective discharge of its Mission and therefore the proposals must endeavour to ensure optimal use of available resources. The Head
of Internal Audit should advocate for inclusion of the Department’s budget proposals in the Authority’s overall budget.

150 KRA Structure

1600 Monthly Reporting

The Internal Audit Department maintains a formal process of communicating to the top management the audit findings and recommendations for all audits conducted. Monthly reports are submitted to the top management through the Research and Corporate Planning Department.

The monthly report shows the performance of the Department in terms of audit assignments completed during the month compared to the targeted performance. Collectively, the reports also show the department’s cumulative performance from the beginning of the financial year.
The report also shows details of audit assignments/reports for which audit recommendation implementation status reports have not been received from various departments.

The monthly report also outlines the progress made by the department in implementation of its balanced scorecard.

170 Compliance with the Law and Professional Standards

171 Internal Audits and the KRA Act Cap 469
Section 19 of the KRA Act states *inter alia* that in addition to any other functions assigned to him by the Board or the Commissioner General, the Head of Internal Audit is responsible for the internal audit of the Authority’s accounts and shall submit to the Commissioner General a report on the accounts for every three months of the financial year.

The report then becomes the guideline to the operation of the internal audit function within the Authority. The other duties that the Department discharges are defined in the Audit Charter. However, this section of the Act provides for all those other duties that the Board or the Commissioner General will direct the Internal Audit Department to do. These duties are not defined, but comprise what is commonly referred to as ad hoc audits.

172 Other Acts and Legal Notices Administered by the Authority
There are other Acts that do not have specific provisions relating to the internal audit activity within the Kenya Revenue Authority. However, since these acts are invariably used to enforce revenue collection, it is important that the auditors have proper working knowledge of them. They include:

i. The Income Tax Act (Cap. 470)
ii. The Customs and Excise Act (Cap. 472)
iii. The Value Added Tax Act (Cap. 476)
iv. The Road Maintenance Levy Fund Act 1993 (No. 9 of 1993)
v. The Air Passenger Service Charge Act (Cap.475)
vi. The Entertainment Tax Act (Cap.479)
vii. The Traffic Act (Cap.403)
viii. The Transport Licensing Act (Cap.404)
ix. The Second-Hand Motor Vehicle Purchase Tax Act (Cap.484)
x. The Civil Aviation Act (Cap.394)
xi. The Widows’ and Children’s Pension Act (Cap.195)

xii. The Betting, Lotteries and Gaming Act (Cap.131)

xiii. The Stamp Duty Act (Cap.480)


xv. The Parliamentary Pensions Act (Cap. 196)

xvi. The East African Customs Management Act, 2004

xvii. The Kenya Sugar Board Act, 2001

xviii. The Government Lands Act (Cap. 280)


173 International Standards for the Professional Practice of Internal Auditing

The Department is an integral part of the Authority and functions under the policies established by the management and the Board. The environment in which the assignment is carried, therefore, will govern the implementation of these standards. Compliance with the concepts enunciated by these standards is essential so that the responsibilities of internal auditors can be met. The purposes of these standards are to:

i. Impart an understanding of the role and responsibilities of internal auditing to all levels of the management, Board of Directors, public organisations, external auditors and related professional organisations

ii. Establish the basis for the guidance and measurement of internal auditing performance

iii. Improve the practice of internal auditing.

The standards consist of attribute standards, performance standards and implementation standards. The attribute standards address the characteristics of organisations and parties performing internal audit activities. The performance standards describe the nature of internal audit activities and provide quality criteria against which the performance of these services can be evaluated. While the attribute and performance standards apply to all internal audit services, the implementation standards apply to specific types of engagements. The detailed standards are available within the department and members of staff should always familiarise themselves with their provisions. The summary of these standards is as below:
i. **INDEPENDENCE** – INTERNAL AUDITORS SHOULD BE INDEPENDENT OF THE ACTIVITIES THEY AUDIT.

**Organisational Status** – The organisational status of the Internal Audit Department should be sufficient to permit the accomplishment of its audit responsibilities.

**Objectivity** – Internal auditors should be objective in performing audits.

ii **PROFESSIONAL PROFICIENCY** – INTERNAL AUDITS SHOULD BE PERFORMED WITH PROFICIENCY AND DUE PROFESSIONAL CARE

**Staffing** – the Internal Audit Department should provide assurance that the technical proficiency and educational background of internal auditors are appropriate for the audits to be performed.

**Knowledge, Skills and Disciplines** – the Internal Audit Department should posses or should obtain the knowledge, skills and disciplines needed to carry out its audit responsibilities.

**Supervision** – the Internal Audit Department should provide assurance that internal audits are properly supervised.

**Compliance with Standards of Conduct** – Internal auditors should comply with professional standards of conduct.

**Human Relations and Communications** – Internal auditors should be skilled in dealing with people and in communicating effectively.

**Continuing Education** – Internal auditors should maintain their technical competence through continuing education.

**Due Professional Care** – Internal auditors should exercise due professional care in performing internal audits.

iii. **SCOPE OF WORK** – THE SCOPE OF WORK SHOULD ENCOMPASS THE EXAMINATION AND EVALUATION OF THE ADEQUACY AND EFFECTIVENESS OF THE ORGANISATION’S SYSTEM OF INTERNAL CONTROL AND THE QUALITY OF PERFORMANCE IN CARRYING OUT ASSIGNED RESPONSIBILITIES

**Reliability and Integrity of Information** – Internal auditors should review the reliability and integrity of financial and operating information and the means used to identify, measure, classify and report such information.
Compliance with Policies, Plans, Procedures, Laws and Regulations – Internal auditors should review the systems established to ensure compliance with those policies, plans, procedures, laws and regulations that could have a significant impact on operations and reports and should determine whether the organisation is in compliance.

Safeguarding of Assets – Internal auditors should review the means of safeguarding assets and as appropriate, verify the existence of such assets.

Economical and Efficient Use of Resources – Internal auditors should appraise the economy and efficiency with which resources are employed.

Accomplishment of Established Objectives and Goals for Operations or Programmes – Internal auditors should review operations or programmes to ascertain whether results are consistent with established objectives and goals and whether the operations or programmes are being carried out as planned.

iv. PERFORMANCE OF AUDIT WORK – AUDIT WORK SHOULD INCLUDE PLANNING THE AUDIT, EXAMINING AND EVALUATING INFORMATION, COMMUNICATING RESULTS AND FOLLOW UP.

Planning the Audit – Internal auditors should plan each audit.

Examining and Evaluating Information – Internal auditors should collect, analyse, interpret and document information to support audit results.

Communicating Results – Internal auditors should report the result of their audit work.

Following Up – Internal auditors should follow up to ascertain that appropriate action is taken on reported audit findings.

v. MANAGEMENT OF THE INTERNAL AUDIT DEPARTMENT – THE HEAD OF INTERNAL AUDIT SHOULD PROPERLY MANAGE THE DEPARTMENT.

Purpose, Authority and Responsibility – The Head of Internal Audit should have a statement of purpose, authority and responsibility for the Department.

Planning – The Head of Internal audit should establish plans to carry out the responsibilities of the Department.

Policies and Procedures – the Head should provide written policies and procedures to guide the audit staff.

Personnel Management and Development – The Head should establish a programme for selecting and developing the human resources of the Department.
**External Auditors** – The Head should coordinate internal and external audit activity when necessary

**Quality Assurance** – The Head should establish and maintain a quality assurance programme to evaluate the operations of the Department.

174 International Financial Reporting Standards
The accounting process worldwide is guided by the International Accounting Standards, which give benchmarks on how issues in accounting are to be dealt with. The internal auditors, being accountants, are expected to have an understanding of the standards. These international financial reporting standards are available and the auditors should be conversant with their provisions.

180 External Auditors
External audits are periodic reviews of internal controls and performance of such tests to enable the expression of an opinion as to the reliability of the financial statements. The external auditor provides an independent opinion on the fairness of the financial statements contained in the annual report. It is a requirement of the State Corporations Act for the KNAO to carry out external audits on all State Corporations. Therefore, external audits for the Authority are carried out by the KNAO. A copy of the report is sent to the Public Accounts Committee (PAC).
CHAPTER TWO

200 STAFFING AND PERSONNEL

210 Organogram (KRA & IAD)

The organogram shows the approved relationship structure of the Internal Audit Department and the Commissioner General, the Audit Committee and the Board. The Board of Directors oversees the overall management of the Authority. Functionally, the Audit Committee provides the interface between the management of the Authority and the Board. It is also responsible for enforcing the implementation of the Audit Department’s recommendations.
**Staff Rotation**

The Department rotates staff regularly within the Units. The objective is to ensure cross-on-the-job training and reduce the risk of collusion with the auditees due to familiarisation. It also develops an internal check system and therefore ensures objectivity in dealing with the auditees.

**220 Duties, Responsibilities and Qualifications**

It is a requirement of the standards of professional practice that the internal auditors should possess the knowledge, skills and other competencies needed to perform their individual responsibilities. The Internal Audit Department collectively should possess or obtain the knowledge, skills and other competencies needed to perform its responsibilities. This guiding standard thus requires the Internal Audit Department to have a mix of skills, knowledge and competencies necessary to enable it perform diverse assignments with varying scope and complexities. The following are the duties, qualifications and experiences prescribed for officers in the department.

**Senior Deputy Commissioner – Internal Audit – (KRA 3)**

The Senior Deputy Commissioner is the head of the Internal Audit Department and reports to the Commissioner General administratively and functionally to the Audit Committee of the Board. His or her key responsibilities are as follows:

i. Establish and operate an efficient Internal Audit Department. This involves liasing with commissioners of the revenue departments and heads of departments

ii. Ensure that the internal audit systems, procedures and guidelines are prepared for approval by the Commissioner General and the Audit Committee of the Board

iii. Prepare work programme for the Department to ensure that audits are planned, managed and the quality of audit work maintained

iv. Ensure that the internal controls are reviewed and documented for their effectiveness and adequacy and that recommendations are made for improvements

v. Ensure that the accounting, administration and other operations comply with KRA management policies

vi. Prepare and submit audit reports to the Commissioner General and the Audit Committee of the Board

vii. Act as secretary to the Audit Committee of the Board (ex-officio)

viii. Liase with the KNAO and ensure the process of implementation of internal and external audit recommendations
ix. Any other duties that may be assigned by the Audit Committee of the Board, the Commissioner General, revenue commissioners and heads of departments.

The ideal officer should have the following minimum requirements:

i. University degree in commerce, accounting, finance, business administration or related field

ii. A Masters degree will be an added advantage

iii. CPA (K), CA, ACCA or acceptable equivalents

iv. Must have served as Deputy Commissioner in the Authority or equivalent position for at least three years

v. Must have an analytical mind with proven managerial and leadership skills

vi. Must be computer literate and proficient in the use of Computer Assisted Audit Tool and Techniques (CAATTs)

vii. Additional professional qualifications, i.e., CISA, CIA, CFE, will be an added advantage

viii. Possess good interpersonal and communication skills.

**Deputy Commissioner – Internal Audit – (KRA 4)**

The Deputy Commissioner reports to the Senior Deputy Commissioner and his or her duties include:

i. Deputising the Senior Deputy Commissioner

ii. Reviewing and updating the Internal Audit Procedures manual

iii. Conducting risk assessments, preparing work allocation schedules and staff training programmes

iv. Assisting in the review of the audit reports and files and supervision of staff in the department

v. Assisting in the preparation of department’s monthly reports

vi. Undertaking complex and special assignments requested by the KRA management

vii. Any other duties as assigned by the Senior Deputy Commissioner.

The ideal officers should have the following minimum requirements:

i. A university degree in commerce, accounting, finance, business administration or a related field

ii. A Masters degree will be an added advantage

iii. CPA (K), CA, ACCA or acceptable equivalents
iv. Must have served as Senior Assistant Commissioner in the Authority or equivalent position for at least three years

v. Must have analytical skills and clear understanding of taxation laws

vi. Must be computer literate and proficient in the use of Computer Assisted Audit Tools and Techniques (CAATTs)

vii. Additional professional qualifications, i.e., CISA, CIA, CFE, will be an added advantage

viii. Possess good interpersonal and communication skills.

**Senior Assistant Commissioner – Internal Audit – (KRA 5)**

The Senior Assistant Commissioner reports to the Deputy Commissioner and is responsible for the following:

i. Head of respective audit unit

ii. Organising audit teams for various audit assignments

iii. Supervising several audit teams working simultaneously

iv. Ensuring that audit files are organised in a systematic manner

v. Preparing specific audit assignment plans and programmes

vi. Reviewing audit files and reports prepared by auditors working under him/her.

vii. Assisting in the preparation of periodic audit work plans

viii. Carrying out any other duties as assigned to him/her by the Senior Deputy Commissioner/Deputy Commissioner.

The ideal officers should have the following minimum requirements:

i. A university degree in commerce, accounting, finance, business administration or a related field

ii. CPA (K), CA, ACCA or acceptable equivalents

iii. Must have served as Assistant Commissioner in the Authority or equivalent position for at least three years

iv. Must have analytical skills

v. Computer literate with hands-on experience with Computer Assisted Audit Tools and Techniques (CAATTs)

vi. Additional professional qualifications, i.e., CISA, CIA, CFE, will be an added advantage

vii. Must have a demonstrated ability of working in a multi-disciplinary team

viii. Possess supervisory and managerial skills

ix. Have good interpersonal and communication skills.
Assistant Commissioner – Internal Audit – (KRA 6)

The Assistant Commissioner reports to the Senior Assistant Commissioner and his/her duties include:

i. Assisting the Senior Assistant Commissioner in managing the unit
ii. Supervising several audit teams working simultaneously
iii. Performing initial reviews of the audit reports and audit files
iv. Assisting in preparation of specific audit assignment plans and programmes
v. Performing audit tests on the internal controls in accounting, administrative and operational procedures
vi. Any other work assigned by the Senior Assistant Commissioner – Internal Audit

The ideal officers should have the following minimum qualifications:

i. A university degree in commerce, accounting, finance, business administration or a related field
ii. CPA (K), CA, ACCA or acceptable equivalents
iii. Must have served as Principal Auditor in the Authority or equivalent position for at least two years
iv. Must have analytical skills
v. Be computer literate and familiar with Computer Assisted Audit Tools and Techniques (CAATTs)
vi. Have a clear understanding of taxation laws
vii. Possess supervisory and managerial skills
viii. Be a team player
ix. Have good interpersonal and communication skills.

Principal Auditor – (KRA 7)

The Principal Auditor reports to the Assistant Commissioner and his duties are as follows:

i. Assisting in the preparation of specific audit assignment plans and audit programmes
ii. Performing audit tests on the internal controls in accounting, administrative and operational procedures
iii. Ensuring that the audit findings are properly documented
iv. Preparing draft audit reports detailing audit findings
v. Any other work assigned by the supervisor.
The ideal officer should have the following minimum qualifications:

i. A university degree in commerce, accounting, finance, business administration or a related field
ii. Have CPA III or acceptable equivalents
iii. Must have served as Senior Auditor for at least two years
iv. Possess a clear knowledge of Kenyan taxation laws
v. Be computer literate and familiar with accounting packages
vi. Have good interpersonal and communication skills
vii. Must be a team player
viii. Must have supervisory skills.

**Senior Auditor - (KRA 8)**

The Senior Auditor reports to the Principal Auditor and performs the following tasks:

i. Carry out audit tests on internal controls in accounting, administration and operational procedures
ii. Ensures that the audit files are complete and well referenced
iii. Assist in the preparation of draft audit reports
iv. Any other work assigned by the supervisor.

The ideal officers should have the following minimum qualifications:

i. A university degree in commerce, accounting, finance, business administration or a related field
ii. Have CPA II or acceptable equivalents and be willing to pursue further professional qualifications
iii. Must have served as Auditor I or an equivalent position for at least two years
iv. Have knowledge of Kenyan taxation laws
v. Be computer literate
vi. Possess good interpersonal and communication skills
vii. Be a team player.

**Auditor I – (KRA 9)**

Auditor I works under the supervision of the Senior Auditor and his/her duties are:
i. Carrying out audit tests on internal controls in accounting, administration and operational procedures
ii. Ensuring that all working papers are documented and well referenced
iii. Ensuring that the audit file is complete and well referenced
iv. Any other work assigned by the supervisor.

The ideal officers should have the following minimum qualifications:

i. A university degree in commerce, accounting, finance, business administration or a related field
ii. CPA I or its acceptable equivalent and should be willing to pursue further professional qualifications
iii. Basic training in Kenyan taxation laws
iv. Computer literacy
v. Good interpersonal and communication skills
vi. Be a team player

230 Appointment, Promotion and Dismissal of Auditors

Appointments and promotions to the various levels will depend on a vacancy existing. The Department will inform the Human Resources (HR) Department of the vacancies existing which will be filled according to the Authority’s policy on appointments and promotions.

Dismissal of auditors from the service will follow the procedures applicable to all employees of the Authority.

240 Training and Professional Development

The Authority’s policy on recruitment is targeted at candidates who meet minimum academic qualifications in line with the position they wish to be considered. Each internal auditor is responsible for maintaining an adequate level and an understanding of the social economic and political environment within which the authority and its customers operate.

Each auditor should possess a body of specialized knowledge and should maintain a recognised, continuous process of education in order to sustain professional growth in the field of internal auditing. The auditor should be in compliance with the requirements established by the
International Standards for the Professional Practice of Internal Auditing of the Institute of Internal Auditors and the Institute of Certified Public Accountants (ICPAK). The auditor will also be expected to register with the professional bodies including ICPAK, the Institute of Internal Auditors (IIA) and Information Systems Audit and Control Association (ISACA) and adhere to their CPE requirements annually.

Ordinarily, the department runs an annual training budget and auditors are regularly taken for training seminars relevant to their job and grade. Therefore, the internal auditors will attend seminars and training as appropriate.

One aspect of professional development is obtaining professional certification such as a Certified Public Accountant (CPA), Certified Internal Auditor (CIA), Certified Information Systems Auditor (CISA) or Certified Fraud Examiner (CFE). To enhance the professionalism and credibility of the audit staff, the Authority supports employee’s efforts in achieving certifications by reimbursing 80% costs of sitting and passing exams. Professional certification is also a factor in the Departments’ annual employee performance appraisal.

In order for auditors to maintain an awareness and understanding of current developments in relevant business fields, the Department subscribes to periodicals and journals. These include:

i. Journal of Accountancy (A.I.C.P.A)
ii. Internal Auditor Magazine
iii. Taxation Magazine (UK).

Initially, new staff members will be exposed to various rules and regulations, copies of which are currently maintained in the office library. These include:

i. KRA Code of Conduct
ii. Public Officers Ethics Act
iii. Finance Procedures manual
iv. Procurement Policies and Procedures
v. Transport Policy
vi. Additionally, the Department’s Audit manual is accessible to each auditor.
CHAPTER THREE

300  THE AUDIT PROCESS

Although every audit assignment is unique, the audit process is similar for most engagements and normally consists of four stages: the audit planning, fieldwork, audit reporting and follow-up. The auditee’s involvement is critical at every stage of the audit process. Although the auditee may be distracted from the usual work routine by an audit, this is usually a worthy cost since the auditee benefits in the long term. Further, it is the intention of the Department to minimise time spent with the auditee and therefore maximum cooperation of both parties is of mutual benefit.

310 Audit Planning

311 Annual Audit Assignment Planning

The Department operates under an approved plan. The plan is developed in accordance with the Standards for the Professional Practice of Internal Auditing which requires internal auditors to plan for each audit. The plans will be developed after assessing the risks of auditable activities of the Authority as well as inputs received from the top management, the Authority’s Board of Directors, the Board’s Audit Committee and the external auditors.

Risk Assessment

Risk assessment of auditable activities is done by the Head of Internal Audit, the Deputy and the Heads of Units. The process involves identification and categorisation of risks. Management may be involved to provide information on the sources and importance of risks. The different risks are then evaluated on the basis of impact and probability of occurrence. Priority of audit assignments in view of the evaluated risks should then be given based on the planning team’s opinion of high, medium and low risk areas. The available resources should be prioritised to the areas of the highest risk.

The Balance Scorecard is the basis of preparation of the annual audit assignment-planning chart. The chart is based on the process of evaluation of internal controls and risk assessment process and shows the overall Department’s audit activities during a period of one year. For every department of the Authority, it shows the auditable units and the personnel assigned to carry out the audit. It also provides for annual leave and leaves some float time for any eventuality. This
is normally to allow for ad hoc and other investigative assignments, which are not planned for at the beginning of the year.

Upon approval by the Head of Internal Audit and the Board’s Audit Committee, the chart is availed to all audit staff members at the beginning of the year. Although the chart is followed in audit assignments, it is flexible and assignments ahead can be brought forward depending on the prevailing circumstances. Other factors that can necessitate the change of the chart include ad hoc assignments and staff changes. The chart forms one of the factors upon which the Department’s performance is evaluated against the assignments accomplished on an annual basis.

The audit plan will depict coverage, estimated resource requirements and the projected time frames for conducting audits. The plans shall be consistent with the Internal Audit Department’s charter and with the goals of the Authority. The planning process involves establishing:

**Goals**

The goals of the IAD should be capable of being accomplished within specified operating plans and budgets and to the extent possible should be measurable. They should be accompanied by the measurement criteria and time frame.

**312 Audit Work Planning Schedules**

Audit work planning schedules should include the activities to be audited, when they will be audited and the estimated time required, taking into account the scope of the audit work planned and the nature of audit work performed by others. The work schedules should be sufficiently flexible to cover anticipated demands on the IAD.

**Staffing Plans and Financial Budgets**

The staffing plans and financial budgets shall include the number of auditors and the knowledge, skills and discipline required to perform their work. This should be determined from audit work schedules, administrative activities, education and training requirements and audit research and development efforts. Overall adherence to the audit plan is best managed by tracking the components of individual audits in addition to each audit. Each audit is logically apportioned into audit-hours required for planning, preliminary survey, internal control evaluation, testing, reporting, supervision and review and final reporting.
Detailed time reporting is used as an incentive for auditors to perform efficiently since there is awareness that performance is being measured against expectations or set standards. The planning is documented and includes:

i. Establishing the audit objectives and scope of work
ii. Obtaining background information about the activities to be audited
iii. Determining the resources necessary to perform the audit
iv. Communicating with all who need to know about the audit
v. Performing as appropriate an on-site survey to become familiar with the activities and controls to be audited; to identify areas for audit emphasis and to invite auditee’s comments and suggestions
vi. Writing up the audit programme
vii. Determining how, when and to who the audit results will be communicated
viii. Obtaining approval of the audit work plan

The auditors submit regular activity reports to the management and to the Board of Directors. These reports compare the performance with the departmental goals and the audit work schedules and expenditures with financial budgets. They should explain the reasons for major variances and indicate any action taken or needed. It is important that the audit plan be adhered to as much as possible, so that a sufficient depth of audit coverage is accomplished.

313 Audit Teams and Time Budget

Audit Teams
This is a group of internal auditor(s) constituted by Head of Internal Audit to execute audit assignments. Ordinarily, an ideal audit team consists of the Head of Internal Audit, the Audit Manager, the Principal Auditor, Senior Auditor and an Auditor I. Where this is not possible due to shortage of staff, two or three auditors may be assigned to an audit. To enhance supervision of several audit teams, the Audit Supervisor normally accompanies the auditor(s) for the opening and exit meeting and ensures close supervision throughout the exercise.

An audit team is normally constituted taking into consideration such factors as educational background, experience, skills and level of training on particular areas, e.g., computer fraud. In the absence of certain expertise, the Head of Internal Audit, in consultation with the Commissioner General, can look for an external expert who is skilled in certain areas. This
should be done taking into consideration the professional competence and integrity of the external expert. For more complex assignment(s), audit teams are likely to consist of senior officers including the Head of Internal Audit.

**Time Budget**

An audit time budget provides an overall guideline for the performance of the audit. In addition, it enables the Audit Manager to control the audit work in process. It is essential that the audit time is controlled in order that it may be utilised in the most effective manner. The detailed time budget analysis should be completed at the conclusion of the preliminary review. Each audit assignment shall have a time budget that is approved by the Audit Manager, Deputy Head of Internal Audit and the Head of Internal Audit. This budget specifies all the time necessary to complete the audit from assignment through issuance of the final report. The budget process is broken down into the following phases (more may be used if warranted):

i. Planning, preliminary review and audit programme

ii. Fieldwork -- time allocated to the various tasks during fieldwork

iii. Preparation of audit report and approval

iv. Budget revisions -- any revision to the audit time budget shall be prepared by the Audit Manager, reviewed by Deputy Head of Internal Audit and approved by the Head of Internal Audit.

A time variance analysis shall be completed at the end of the audit, comparing the actual man-hours spent versus the budgeted man-hours as per the time budget analysis. An explanation should be provided for any variances.

Management should consider introducing time sheets to manage the audit process.

**314 Preliminary Review**

The objective is to gain sufficient knowledge of the unit being audited so that the auditor can design an audit programme that will accomplish the desired objectives. The review helps the auditor to determine if the assigned objectives are attainable within the allocated resources and what audit procedures to be performed based on assessed risks and exposures to achieve the audit objectives. The preliminary review work can be broken down into four distinct phases:

i. Familiarisation: This review shall normally include review of permanent and continuing audit file (if one exists), review of previous audit working papers, reports and management letters (if available), review of financial statements, review of organisational structure and staffing levels and review of rules and regulations and other manuals in use.
ii. Identification of potential problem areas -- This involves those programmes, activities and functions which are significant and have inherent risks.

iii. Evaluation of internal controls -- This entails the review of the unit’s internal control structure. A variety of techniques may be used such as use of internal control questionnaires, narratives, flow charts, interviews and data gathering and analysis techniques.

iv. Planning the detailed audit -- This stage enables the auditor to design tests to be performed in the fieldwork section of the audit.

315 Audit Programme

An audit programme outlines the necessary steps to achieve the objectives of an audit assignment within the defined scope. It is a detailed plan of the work to be performed during the audit. An audit programme will enable the following:

i. A systematic plan for each phase of the work that can be communicated to all audit personnel concerned

ii. A means of self-control for the audit staff assigned

iii. A means by which the Audit Supervisor/Manager can review and compare performance with approved plans

iv. Assist in training inexperienced staff members and acquainting them with the scope, objectives and work steps of an audit

v. Acts as an aid to the supervisor, making it possible to reduce the amount of direct supervisory effort needed

vi. Assist in familiarising successive audit staff with the nature of work previously carried out.

The audit programme consists of specific directions for carrying out an audit assignment. It contains a statement of the objectives of the operation being reviewed, the audit procedures to adhere to in order to meet the objectives and arrive at conclusions.

Departmental standard audit programmes are available (refer to Volume II of the audit manual) and should be used or modified to achieve the audit objectives. The Head of Internal Audit or Audit Supervisor reviews the audit programme and then discuss any concerns or proposed programme changes.
316 Announcement Letter

The auditee shall be informed of the audit assignment through an announcement letter from the Head of Internal Audit. However, the Internal Audit will not provide advance notifications for investigative audits. Additionally, the Department may not send an announcement letter for requested consulting services.

320 Fieldwork

The fieldwork concentrates on transaction testing and informal communications. It is during this phase that the auditor will determine whether the controls identified during the preliminary review are operating properly and in the manner described by the auditee. The fieldwork stage concludes with a list of significant issues from which the auditor will prepare a draft of the audit report.

321 Entrance Meeting

The auditee describes the unit or system to be reviewed, the organisation, available resources and other relevant information. During the entrance meeting, the auditor explains the audit process, identifies the auditee’s concerns and suggestions — generally opening the channels of communication that are necessary for a successful audit assignment. The Audit Supervisor, the lead auditor and any other team member may attend the entrance meeting. Issues to be discussed during entrance meeting are:

i. Discuss the purpose and objectives of the audit

ii. Discuss potential auditee’s problem areas within the audit scope. This communicates an intention of being helpful rather than critical

iii. Determine if the audit is considered neither appropriate nor timely and be open to discussing the auditee’s comments with your supervisor or Head of Internal Audit

iv. Discuss how audit concerns (observations) are handled

v. Discuss the business conditions and operations of activity being audited, including recent changes in management or major systems.

The opening meeting date, key attendees and substantive items discussed which are directly related to audit scope, objectives, timing or confidentiality should be documented in the work papers.
330 Conduct of Fieldwork

Audit Sampling
Audit sampling is performing an audit test on less than 100 percent of a population. In sampling, the auditor accepts the risk that some or all errors will not be found and the conclusions drawn (e.g. all transactions were proper and accurate) may be wrong.

Types of Sampling

Statistical (probability) sampling -- allows the auditor to stipulate with a given level of confidence the condition of a large population by reviewing only a percentage of the total items. In an audit context, the objective of statistical sampling can be defined as follows: to employ random selection procedures and statistical evaluation techniques in representative testing (whether for compliance or substantive objectives) so as to eliminate the risk of bias and so as to permit quantification of the sampling confidence achieved wherever this greater objectivity is warranted. Several sampling techniques are available to the auditor. Statistical sampling methods shall be used when any of the following criteria apply:

- Cost-benefit analysis supports the additional costs and time required
- The sample error or exceptions must be extrapolated to quantify for the population or a defensible expression of the test result is required
- The objective of the financial audit is to state an opinion on the reliability of the balances reported
- With the availability of computer software for sampling, they would be simpler to apply and or
- The risk of a sampling error must be quantified.

Attribute sampling --- is used when the auditor has identified the expected frequency or occurrence of an event.

Variable sampling --- is used when the auditor samples for values in a population which vary from item to item.

Judgment sampling --- is used when it is not essential to have a precise determination of the probable condition of the universe or where it is not possible, practical or necessary to use statistical sampling. The type of sampling used and the number of items selected shall be based on the auditors’ understanding of the relative risks and exposures of the areas under audit. All audit testing will include sampling. The type and sample size will be described in the audit
programme and will be approved by the Audit Manager/Supervisor. Judgmental sampling will be used when any of the following criteria apply:

i. They are designed to be equally or more effective and efficient as statistical sampling, while being less costly

ii. An auditor encounters a well designed, well controlled system, good management, well trained employees and feedback mechanism that highlights errors. It would therefore be extravagant to spend a great deal of time performing extensive substantive tests.

iii. An auditor encounters a system that is so weak (e.g. inadequate controls and or procedures, insufficiently trained personnel) that no reliance can be placed on the system of internal controls. It would therefore be extravagant to spend a great deal of time performing extensive substantive tests.

iv. The audit objectives are fully met by a non-statistical sample.

v. It is known that the population has no variability.

vi. Examples of deficiencies are needed to support the auditor’s contention that the system is weak and or

vii. Clues are needed as to whether to proceed with a statistical sample.

In all cases, the auditor needs to be experienced with the sampling process and alternative sampling techniques including statistical.

**Documentation of Audit Sampling**

Working papers detailing the sampling (statistical and non-statistical) techniques should include at a minimum, comments on the following items:

i. Identification of the controls or attributes being tested

ii. Sampling approach (e.g. attribute, variable, judgmental or other)

iii. Description of the population from which each sample is selected (e.g. size, homogeneity)

iv. For statistical samples, pre-determined confidence level and precision level

v. Calculation/determination of the sample size

vi. Sample selection method

vii. Records of the tests performed

viii. Analysis of the errors

ix. Conclusions.
According to IIA Performance Standard – 2320, internal auditors should base conclusions and engagement results on appropriate analyses and evaluations. The three types of audit tests that can be used to obtain audit evidence include:

i. **Analytical Reviews** – to test relationships between sets of data

ii. **Compliance Tests** – to test whether the operational, compliance and financial controls, both of the preventive and the detective nature, were operating effectively during a specified period

iii. **Substantive Tests** – to verify the accuracy of transactions, processes and account balances.

### 331 Analytical Review

This is the basic audit technique for considering systematically the consistency of such relationships and forming conclusions about the likelihood of weaknesses and errors in underlying systems. However, audit evidence provided by analytical review is circumstantial in that it only suggests whether the figures are reasonable. Analytical reviews alone rarely provide sufficiently reliable evidence on which to base an audit conclusion. However, analytical review provides an efficient tool for directing the focus of audit work. For systems or balances considered material, the auditor will need to obtain additional audit evidence. Therefore, analytical review complements rather than replaces other auditing techniques.

Analytical review may take the form of a comparison of related figures, trends and ratios, or an assessment of the overall reasonableness of the account figures. Analytical review procedures include the study of relationships such as:

i. Elements of financial information that would be expected to conform to a predictable pattern based on the audited units experience, for example the Authority’s payroll

ii. Financial and relevant non-financial information, such as a comparison of monthly payroll costs with the head count of employees together with a review of the average employee’s pay.

iii. A comparison of actual tax revenue to detailed budget plans indicating the number of taxpayers, tax rates and revenues in previous years.

The selection of appropriate comparisons and ratios, and the proper interpretation of results, requires a degree of experience and professional judgement. Proper use of analytical review techniques should help to reduce the level of detailed testing done.
Analytical review procedures are more effective when applied to balances or figures that have been broken down into smaller groups of related balances (e.g. an analysis of payroll costs by department and grade, split into basic salary and allowances). In general, the greater level of detail the more reliable the procedures are likely to be.

There are two stages during an audit where analytical review procedures may be used:

i. At the planning stage to assist in focusing the audit work

ii. During the detailed review of individual systems to provide substantive evidence towards meeting the general audit objectives.

**Analytical Reviews during Planning**

The detailed planning required for audit involves the analysis of financial information to identify areas of potential risk so that the auditor can determine the nature, timing and extent of audit procedures in order to provide a sound basis on which work can proceed. Such review/analysis will normally be conducted on the budget monitoring figures (e.g. forecast expenditure/receipts for the current year, compared to budget plans and compared to previous years' figures).

In addition to the identification of apparent abnormalities/inconsistencies, indicating the need for more intensive examination, the review can identify areas that conform to the auditor’s expectations and thus enable the level of details to be reduced. Analytical review at this stage also helps to improve the auditor’s understanding of the audited unit.

**Analytical Reviews during Detailed Audit Reviews**

Analytical review is often one of the principal sources of evidence to establish completeness, particularly in relation to receipts. Analytical review should be done before other substantive tests. The following points should be considered in planning analytical review tests:

i. The nature and objectives of the unit activities

ii. The knowledge gained during previous examinations, especially with regard to fundamental weaknesses previously reported

iii. Factors (both internal and external) that are likely to influence the Authority’s performance

iv. The availability of financial and non-financial information

v. The reliability of information;
vi. The management’s own use of analytical review procedures
vii. The type and degree of assurance required from the review.

In order to either confirm or refute the position indicated by the observed trends, the auditor should evaluate the explanations given. Depending on the degree of assurance obtained from analytical review procedures, the Auditor may be justified to lower the confidence level for detailed substantive testing, thereby reducing the sample size selected.

When deciding the level of confidence to place on the results of analytical review procedures, the auditor should consider the following matters:

i. The extent to which the testing is independent of the accounting system
ii. The relevance, reliability and comparability of the base information used in the calculations
iii. The likelihood of variations occurring in the base information
iv. The amount of other independent evidence available to support the analytical review tests
v. The expected results of the analytical review.

When analytical review is used as a substantive test, the following steps are likely to be common:

i. Compare the result being audited with the expected result
ii. Investigate the reasons for any significant discrepancy in either direction
iii. Record the results of the work carried out
iv. Confirm conclusions and impact on other tests in the working paper.

332 Documentation

The auditor should ensure that the working papers adequately document the planning, performance and results of, and conclusions from, the analytical review work.

Working papers should include:

i. An outline programme of the review work, e.g., account areas to be considered, overall review work on accounts figures, allocation of time
ii. A summary of significant figures and relationships
iii. The sources and dates of the acquisition of figures used
iv. Details of all significant variations considered
v. Details of the results of investigations into such variations including explanations obtained from the management and the steps taken to verify them
vi. The audit conclusions reached
vii. Information considered necessary for assisting in the planning of subsequent audit.

The auditor should consider the clearest and most cost-effective way of conveying the results of the analytical review (e.g. graphical illustrations, numerical tabulations). To identify trends, it may also be useful to draw up a schedule of ratios from period to period.

333 Compliance Testing
Compliance testing is primarily concerned with assessing the effectiveness of the unit systems of internal control. The different categories of internal controls are discussed in Chapter 4 of this manual.

334 Substantive Testing
Substantive testing is primarily concerned with the accuracy of transactions and balances. To provide a sound basis for audit findings and recommendations, auditing standards require that sufficient evidential matter be obtained through inspection, observation, inquiries and confirmation. To do this, the auditor's testing plan should consider the inherent control and detection risks applicable to a particular entity under audit.

The evidential matter required by auditing standards is obtained through two general classes of auditing procedures: (a) tests of details of transactions and account balances, and (b) analytical review of significant ratios, trends and the resulting investigation of unusual fluctuations and questionable items. These procedures are referred to as substantive tests.

In performing an audit, several substantive tests may be combined and performed in a single test. The following list includes the most common analytical review and test of detail procedures.

335 Comparison and Relationships
This involves comparing similar balances recorded in different periods. The auditors investigate unusual fluctuations because they may be indicative of errors in the account balance. If the auditor has become familiar with the business and with current activities, it is possible to make judgments that are more informed from these tests.
336 Predictive Tests
Predictive tests are similar to comparison and relationship tests since both are based on the premise that relationships exist among financial data. Predictive tests are a refinement of comparisons and relationships as they start with basic financial data and predict a result.

If the predicted result is significantly different from the recorded, additional audit procedures need to be performed until a reasonable explanation for the difference is obtained or the problem can be quantified.

337 Review of Detail for Unusual Items
This is the review of detail for unusual items, sometimes called an exception test. In this test, the auditor reviews a segment of the records or a work paper schedule to determine whether the details make sense (e.g. does the schedule present the information that it is supposed to? If a schedule should list all transactions over KSh 1,000, but it actually has only transactions over KSh 5,000, it may be incomplete).

338 Re-computation and Test of Clerical Accuracy
This involves testing the arithmetical accuracy, so the amount of adding and re-computing that the auditor does should be limited.

339 Inspection of Supporting Documents (Vouching)
This involves inspection of documents to support the recording of a transaction. For example, to support the purchase of a scanner machine, the auditor may examine the supplier's invoice, a receiving report and the purchase order. By examining these documents, the auditor can determine that the machine was received and that it cost KSh XX. The auditor would also review the description of the machine to determine that it was proper capital expenditure and is properly classified in the accounts as a property, plant and equipment.

3310 Confirmation
This test is a request to a third party, such as a customer or supplier, to confirm in writing directly to the auditor, some relevant information.
3311 Inspection of Assets
This test requires the auditor to physically observe certain assets in order to verify their existence. This test may not be practical or possible for all assets.

3312 Cut-off Tests
The auditor examines supporting documentation to determine that transactions are recorded in the proper period. For example, the auditor would review invoices paid after year-end to determine whether any of them were for goods/services supplied during the previous year and if so, whether the relevant expenses were accrued.

3313 Analysis of Accounts
The auditor reviews some or all of the entries that were processed through an account. This can be done on a summarised basis or can be done based on individual transactions.

An account may be analysed because the information obtained is intended to be a critical factor in reaching a conclusion about the propriety of the balances or the basis at which it is carried in the Financial Statements.

Another reason for analysing an account is to obtain information that will be useful in (a) applying analytical review procedures, (b) evaluating the management's accounting estimates or (c) testing the business' operations.

Based on the particular situation, the auditor may also examine critical documents to support the activity in the account. Also, the auditor may compare and relate this information to prior periods.

3314 Control Account Reconciliation
Control accounts should be reconciled to the subsidiary records and all unexplained differences investigated and resolved. This includes making any required adjustments to the recorded amounts.

Reconciling items are often a normal part of balancing individual balances and items with the control account. However, reconciling items can also indicate errors, irregularities and
breakdowns in systems and procedures. Therefore, the Auditor should be very cautious in evaluating the propriety and causes of reconciling items that do not arise from normal operations.

3315 The Degree of Risk, Materiality and Scope of Audit Testing

The selection of the type, timing and extent of testing is influenced by:

i. The degree of risk involved in the transaction – the concept of business risk is discussed in chapter 4 of this manual

ii. Materiality – substantive tests should be designed to detect errors that are considered to be material.

Scope of the Audit

The auditor needs to determine the level of compliance testing vis-à-vis the level of substantive testing that needs to be performed. Usually this is the decision of the Audit Manager and the lead auditor based upon their professional judgment supplemented by the core audit programme guidelines. Factors influencing the scope of work include:

i. **Processing environment:** Where the volume of transactions is high and the population is homogenous, the reliance on controls and compliance testing should be stressed e.g., cheque processing. Where transactions occur infrequently and each one is unique, then substantive testing should be stressed.

ii. **Auditable unit:** Where a unit entity is not responsible for a significant amount of asset/liabilities or capital, the auditor should not concentrate on substantive testing.

iii. **Control environment:** Where internal controls are considered to be ineffective during the planning stage, the auditor needs to expand the substantive testing. It would not be useful to perform compliance tests where controls are insufficient and ineffective.

iv. **Level of automation:** If the system review determines that reliance on system controls is appropriate, then compliance testing for controls should be limited.

3316 Direction of Testing

The direction of testing is important to consider for both substantive and compliance tests. In compliance testing, the auditor should select from a source that is complete bearing in mind the auditor's test objective (e.g. where the objective is to test for proper segregation of duties and adherence to proper approval requirements, the auditor should select from a list of system access rights to an authorized maintenance request form rather than the reverse).
Substantive tests rely on the objective of the test to determine the direction of testing. For example, to test for overstatement the auditor should select from the most final document. Conversely, a test for understatement should be selected from the initial document. For example, a test of overstatement of expenses should be selected from the general ledger and vouched to the invoices.

3317 Timing of Testing
The tests should be spread over the period under review and should cover a reasonable period. There can be exceptions, for example, where reliance can be placed on a recent review by the external auditors. This is appropriate when the scope and materiality thresholds are comparable.

Other factors to be considered in the timing of an audit:

i. Surprise versus advance notice audits depend on the risk. If the major risk is misappropriation of assets, (e.g., cash, securities) the auditor may opt for a surprise audit.
ii. Analytical review comparisons need to take into account the significance a business cycle has to the account balance. Comparisons may be performed monthly, quarterly or annually with comparisons of balances to prior month, prior quarter, prior audit, prior year end which ever is appropriate in the circumstances.

3318 Extent of Testing
This is a matter of professional judgment. The objective is to test the minimum amount necessary to obtain assurance that a control is functioning properly or that a transaction is properly reported. This objective is satisfied by using audit-sampling techniques. Factors that should be considered in determining the extent of testing include:

Compliance Testing

i. The frequency that the control is performed. In general, the more often the control is performed, the higher the level of compliance testing

ii. The degree of reliance on a control

iii. The materiality and risk of the transactions or balances involved

iv. The specific effect that an error resulting from a control weakness would have on the system of internal control or the financial statements

v. The risk that the error may not be detected.
Substantive Testing

The extent of substantive tests is affected by the degree of reliance on the system of internal control. In general, reliance on internal control reduces the extent of substantive testing while non-reliance increases the extent. The auditor will not be expected to place complete reliance on an internal control to the exclusion of substantive testing.

The extent of substantive tests is also affected by:

i. The materiality and relative risk of the items involved. For example, securities are likely to carry more risks than fixed assets in terms of control, valuation, etc., although both accounts may be material

ii. The extent to which exceptions are identified

iii. The account balance composition.

Normally the extent of substantive testing should be increased when the need for human judgment is an important consideration of the account balance e.g. adequacy of reserves.

3319 Audit Evidence

Audit evidence is the information internal auditors obtain through observing conditions, interviewing people and examining records. In adhering to the Standards for the Professional Practice of Internal Auditing regarding performance of audit work, auditors shall collect, analyse, interpret and document information to support audit results. The process of examining and evaluating information is as follows:

i. Information should be collected on all matters related to the audit objectives and scope of work

ii. Information should be sufficient, competent, relevant and useful to provide a sound basis for audit findings and recommendations

iii. Sufficient information is factual, adequate and convincing so that a prudent, informed person would reach the same conclusions as the auditor

iv. Competent information is reliable and at best attainable through the use of appropriate audit techniques

v. Relevant information supports audit findings and recommendations and is consistent with the objectives for the audit

vi. Useful information helps the organisation meet its goals.
To be familiar with the design and function of the accounting system, the auditor reviews evidence acquired from discussions with officials and with employees; evidence acquired by reviewing policy statements, procedures manuals and job descriptions and evidence acquired by observing the activities of the employees during the normal course of operations.

It should be obvious that in order to use internal accounting control as a form of evidence, many other types of evidence are also considered. The stronger the internal accounting controls, the less additional evidence the auditor needs to examine. Audit evidence has been categorized as physical, testimonial, documentary and analytical.

**Physical Evidence**
This is evidence obtained by observing people, property and events. It can take the form of photographs, charts, maps, graphs or other pictorial representations. Graphic evidence is persuasive. All observations should, if possible, be supported by documented examples. When the observation is the sole evidence, it is preferable to have two or more auditors make important physical observations. If possible, representatives of the auditee should accompany the auditors on such inspections.

**Testimonial Evidence**
This takes the form of letters or statements in response to inquiries or interviews. These standing alone are not conclusive and they should be supported by documentation if possible. The auditee’s statements can be important leads not always obtainable by independent testing.

**Documentary Evidence**
This is the most common form of evidence. It may be external or internal. External documentary evidence includes letters or memorandums received by the auditee, suppliers’ invoices and packing sheets. Internal documentary evidence originates within the auditee organisation. It includes accounting records, copies of outgoing correspondence, receiving reports and the like.
340 Work Papers

“Internal auditors should record relevant information to support the conclusions and engagement results.”

IIA Performance Standard – 2330

Audit evidence should be relevant, reliable and accurate. Audit work papers should record all audit evidence during the audit review. Work papers are contained in two types of files: the permanent audit file and the current audit file.

341 Permanent Audit Files

The Permanent Audit File (PAF) contains information that should be relevant to the current and future audits. Documents may include organisational charts, circulars, relevant regulations and manuals.

A PAF is useful for the following reasons:

i. It ensures that important documents are not overlooked, and it consolidates such documents at one location.
ii. It provides a basis for consistency in testing. Carry forward schedules, which compare ratios, averages, etc., can be used as an auditing tool.

To avoid the necessity to re-read the full documents during successive audits, a contract may be summarised or the significant sections of a contract may be underlined and included in the PAF for easy reference.

There is no standard organisational rule for the PAF. However, the following types of documents should normally be included in the file:

i. Organisational charts
ii. Description of business activities, systems, procedures and business plans
iii. Key analytical ratios
iv. Latest Corrective Action Plan
v. Legal and regulatory issues impacting the Authority
vi. Risk assessment
vii. Correspondence of continuing interest to future audits
viii. Updated audit programmes

342 Current Audit Files

The Current Audit File (CAF) contains schedules and documents relevant to the current audit. The CAF contains a record of all of the audit work completed and any conclusions reached. Current work paper files should have consistent organisation and documentation irrespective of the type of audit.

There is also no standard organisational rule for the CAF. However, the CAF should contain, as a minimum, following work papers:

i. Copies of the draft and final audit reports

ii. Significant findings and issues identified during the audit and how they were resolved

iii. Audit Planning Memorandum (APM) and related documentation

iv. Administration/Correspondence memos and documents

v. Follow-up of prior audit reports and matters that have not been resolved

vi. The tailored and updated audit programmes

vii. Analytical review. Any significant trends, material account balances and other conclusions reached in the course of the analytical review should be documented along with their effect on audit scope

viii. Detailed testing schedules.

The working papers should represent a clear record of the audit process, procedures, findings, conclusions and reports. Working papers should be capable of standing on their own without requiring any supplemental oral explanation from the Auditor(s) who did the work. Consequently, an independent reviewer should be able to understand all of the audit work performed, the findings and how exceptions and other issues were resolved and the conclusions drawn from the work.

The work papers are used for a number of important functions:

i. They demonstrate whether the audit was done in compliance with the relevant standards

ii. They aid in the organisation, control, administration and review of the audit work

iii. They form the evidence of the audit work performed and the conclusions drawn from that work

iv. They support the audit report.
While audit testing and audit findings must be adequately documented and supported in the work papers, auditors should ensure that clarity and functionality is not lost in the volume of data and supporting documents kept.

**Working Paper Techniques**

**Descriptive headings:** All working papers shall include the title of the audit, title of the working paper, preparer’s initials, signature, date prepared, source of the information and purpose of the working paper.

**Tick marks:** The auditor makes frequent use of a variety of symbols to indicate work that has been done. These symbols are commonly referred to as tick marks. As these ticks have no special or uniform meaning in themselves, an explanation of each tick mark shall be made on the schedule on which it appears.

**Cross-referencing:** Cross-referencing within the working papers shall be complete and accurate. Working papers shall be cross-referenced to the audit findings. Audit findings shall be cross-referenced to the exit meeting memo and or the audit report to indicate final disposition of the item. Cross-referencing shall be done in the margins of audit reports drafts. These references readily provide direct access to the working papers. At a minimum, work papers shall be cross-referenced to other related papers, the audit programme, summaries and the draft audit report. A copy of the final audit report, filed with the work papers shall also be cross-referenced.

**Indexing:** The system of indexing audit working papers shall be simple, yet leave room for flexibility. A capital letter shall be used to identify each segment of the audit and Arabic numerals used to identify schedules within the segments. The purpose of indexing is to facilitate the cross referencing of work papers to one another and to summaries of analysis and reports. It also indicates the relationship of the work papers to the particular areas or segments of the audit. The indexing system shall show the logical grouping of interrelated work papers. Appropriate grouping will not only contribute to ease of reference, but will also assist the auditor’s analysis, interpretation and summarisation of the results of the audit segments and facilitate supervisory reviews. The indexing should be simple and capable of expansion.
**Carry forward:** the auditor shall make full use of the working papers developed in the prior audit(s). Flow charts, system descriptions and other data may still be valid. Those papers that remain useful shall be made a part of the current working papers. They should be updated with current information, re-numbered, referenced, initialled and dated.

### 343 Review of Working Papers

> “Engagements should be properly supervised to ensure objectives are achieved, quality is assured and staff capacity is developed.”
> 
> *IIA Performance Standard – 2340*

All work papers should be reviewed to ensure that they properly support the audit report and that all necessary procedures have been performed. The review should be conducted at a level of responsibility higher than that of the preparer of the working papers. Work paper review is part of the quality control process. Evidence of supervisory review should be documented in the work papers. Such evidence should consist of the reviewer initialling and dating each work paper after it is reviewed.

The Head of Internal Audit should review selected audit files. Where appropriate, especially with more junior or inexperienced staff, this review should include spot checks on the relevant documentation to ensure that the work has been performed carefully and diligently.

When the Audit Manager visits an audit team on a review mission he or she should also review the work papers for all Internal Audit assignments (Systems Audit, Value for Money Audit, Risk Assessment etc) completed and discuss any issues arising from the review with the internal auditors on the job.

As a further quality check, a second level of review should also take place. This should include reviews by the Head of Internal Audit. The review should consist of a random spot check of work papers to ensure compliance with Internal Audit Standards and to identify areas where the reviewer's wider experience can be utilised to improve the audit process. Responsibility for first and second stage review will depend on the seniority of the auditor who performed the detailed audit work.
Irrespective of the person performing the first and second stage review, some key tasks must be performed at certain levels:

i. The Head of Internal Audit must vet all written Internal Audit reports

ii. All written Internal Audit reports, memos and letters must be reviewed and vetted by the Head of the Internal Audit Unit

When performing the first stage review, the reviewer should:

i. Ensure that work papers have been dated and appropriately initialled

ii. Undertake spot checks on the transactions checked by the Auditor to ensure that these checks have been undertaken properly and where appropriate the payments were correctly passed for payment.

Issues arising from the review, which are not resolved immediately, should be noted on a review sheet by the Audit Supervisor. The auditor concerned should answer the review questions. If satisfied with the response, the reviewer should sign off the review sheet. However, care should be taken to ensure that the work papers provide adequate evidence that questions raised during the review have been resolved. Acceptable alternatives with respect to disposition of review notes are as follows:

i. Retain the review notes as a record of the questions raised by the reviewer and the steps taken in their resolution

ii. Discard the review notes after the questions raised have been resolved and the appropriate audit work papers have been amended to provide the additional information requested.

The reviewers should use the review sheets to provide feedback to auditors and to ensure that lessons are learnt for future audits. To be effective, this feedback should be provided as promptly as possible.

344 Ownership, Custody and Retention of Working Papers

Work papers are the property of the department. They shall be in the custody of the Head of Internal Audit and accessible only to authorised officers. The Head of Internal Audit may give members of the management or the external auditors’ access to work papers. This type of access is necessary to substantiate audit findings because it allows the management to use the audit work for other business purposes and to permit coordination of internal audit efforts with
external auditors. Releasing audit work papers to any other outside organisations shall require the approval of the Commissioner General and or Legal Department as appropriate.

The Head of Internal Audit shall develop a retention requirement for work papers that are in keeping with the Authority’s guidelines or any other State Corporations’ requirements. At a minimum, a set of work papers shall be retained until the next audit of the particular unit is complete or five years, whichever is longer.

350 Exit Meeting

The results of an audit assignment should be discussed promptly with the principal officer of the institution/unit. This should be done immediately after the fieldwork has been completed. The Head of the Internal Audit Unit should attend this meeting and discuss the main findings and the proposed recommendations with the relevant officer.

The purpose of the exit meeting is to outline the Internal Auditor’s opinions and provisional recommendations, to ensure factual accuracy and clear any misconceptions that may have arisen during the audit. The opportunity should be taken to ensure that the proposed recommendations are a practical solution to identified weaknesses. The views of the officers obtained at this meeting should be taken into account when writing the internal audit report.

Auditors should ensure that when discussing or reporting their findings that they make clear to officers that the audit recommendations are not mandatory but advisory. However, if officers do not accept a recommendation they should explain how they propose to overcome the weakness identified by audit or explain why they do not consider the risk particularly significant. Where auditees do not implement audit recommendations, they have to accept the additional risks that may be involved.

A summary of matters discussed at meetings and any conclusions reached should be prepared, distributed to individuals, as appropriate and retained in the work papers.

After the discussion, auditors should determine the recommendations to be included in the draft report. These should indicate:

i. New or alternative controls to correct or mitigate any weaknesses that the auditors have identified
ii. Where controls are not being effectively applied, the action required to ensure compliance

iii. Unnecessary or redundant controls that should cease to be applied

iv. Any action which should be taken by the management to check that weaknesses in control
    have not been exploited or to rectify, recover or minimise any loss that may have occurred

v. Any Value for Money (VFM) suggestions or points of good practice that could be adopted.

The auditee’s views about audit conclusions or recommendations should also be taken into
account at the time of compiling the draft audit report. Auditors should also be prepared to
amend their recommendations, if appropriate, because of responses from the management.

As part of the discussions with the auditee, the Internal Auditor should try to obtain agreement
on the results of the audit and a plan of action to improve operations where needed. If the
Internal Auditor and auditee disagree about the audit results, the final audit report may state both
positions and the reasons for the disagreement. The auditee’s written comments may be included
as an appendix to the audit report. Alternatively, the auditee’s views may be presented in the
body of the report or in a cover letter.

360 Audit Quality

The establishment and implementation of a quality assurance and improvement programme for
Internal Audit is required by the Standards for the Professional Practice of Internal Auditing (the
Standards). The Head of Internal Audit shall establish and maintain a quality assurance
programme to evaluate the operations of the Department. The purpose of the programme is to
provide reasonable assurance that the internal auditing work conforms to the Standards for the
Professional Practice of Internal Auditing (the Standards), the Internal Audit Department’s
Charter and other applicable standards. A quality assurance programme shall include the
following elements:

i. Supervision

Supervision is a continuous process and focuses on individual audits. It also provides assurance
to both the Head of Internal Audit and the top management that auditors are doing what they are
supposed to be doing in their assignments. The assurance given shall include not only that
auditors conform to the Department’s policy as outlined in this manual (audit objectives are met,
working papers support findings and conclusions, and working papers provide adequate
information for a meaningful report) but also that the work is completed in accordance with the
standards adopted by the Department. Properly supervised audit assignments are the first and perhaps the most important step in the process of quality assurance.

ii. **Internal Assessments**

Internal assessments provide both quality assurance to audit management and training for the staff. Assessments are appraisals of how well auditors and supervisors have complied with the standards and the department’s policy. They encompass the work of both staff and audit management and are an evaluation of a sample of audit working papers and reports. The assessments shall also provide recommendations for improvement. The internal assessments shall typically be performed by a senior staff auditor (probably audit supervisor-Senior Assistant Commissioner), the Head of Internal Audit or combination thereof.

iii. **External Assessments**

The purpose of external assessments is to provide an independent assurance of quality to the audit management and staff, the top management, the Board of Directors and the Audit Committee and others such as external auditors who may rely on the work of internal auditors. The Commissioner General, in consultation with Head of Internal Audit, shall identify and appoint an appropriate body of person(s) from the private sector to carry out external assessments. In compliance with Institute of Internal Auditors (IIA) standards, the external assessments of the Department will be performed every five years to appraise the quality of its operations. Upon completion, the Department will receive a formal, written report expressing an opinion on the Department’s compliance with the Standards and will include recommendations for improvement as appropriate.

**Quality Assurance Review Process**

All working papers will be independently reviewed to ensure there is sufficient evidence to support conclusions, document the extent of audit work performed, ensure that all audit objectives have been met as well as substantiate compliance with applicable auditing standards. A review will be conducted by the Audit Manager for the assigned staff’s working papers. A further review will be conducted by the Head of Internal Audit or an assigned quality assurance staff person. Exception: If the Audit Manager is the only staff member assigned to the audit/task, then the detailed review will also be performed by the Head of Internal Audit or an assigned quality assurance person.
The Head of Internal Audit, the quality assurance person and the Audit Manager must sign the working papers (section summaries, audit programmes, draft reports) and complete the “Quality Assurance Review Form,” which will serve as documentation of the review process and will be filed with other working papers.

Auditors are encouraged to perform an “informal” self-review of their working papers. However, this review would be for their own benefit only and therefore this document WILL NOT be part of the working papers.

In performing the review, the reviewer shall:

i. Review working papers from audit programme steps to the referenced working papers, ensuring that cross-referencing is properly done, that the working papers support the steps performed and all steps have been completed (or why steps were not completed)

ii. Review working papers from the report to summaries and to the detailed working papers to ensure that all findings are stated, adequately documented and support the opinions, findings and recommendations

iii. Determine working papers compliance to the general Department’s working paper standards

iv. Determine report(s) compliance to the general departmental report standards

v. Determine permanent/continuing audit files’ (if any exist) compliance with departmental standards

vi. Record any deficiencies or comments on a working paper review notes form

vii. The auditor(s) who prepared the working papers will then respond (if necessary) to these points on the same format

viii. After the reviewer has “cleared” the points and completed (initialled) the Quality Assurance Review Form, the working papers will then be forwarded to the Head of Internal Audit

ix. The Head of Internal Audit will review the working papers and discuss the findings and review comments from the assigned Auditor, the Audit Manager and the Reviewer; then complete the relevant parts of the Quality Assurance Review Form and approve the draft report for the exit meeting

x. The Report Reviewer will perform a pre-exit meeting edit, check for spelling, and grammar and review consistency

xi. The assigned auditor will forward a copy of the draft report to the auditee prior to the exit meeting
xii. After exit meeting amendments, the Report Reviewer will perform a spell check as well as grammatical and consistency review, then print out the final version of the report.

xiii. The Audit Manager, the assigned Auditor(s) and the Head of Internal Audit will review and sign the final report.

370 Audit Reporting and Follow-up

Audit Reporting
As a result of conclusion of the fieldwork, the auditor will highlight areas of non-compliance which upon discussion with the auditee at the exit meeting will form the draft audit report. The final product of the review is the audit report in which the department will express its opinion, present the audit issues and action to be taken for improvements. Further details on reporting are discussed in Chapter 9 of this manual.

Auditee Surveys
As part of the Department’s self-evaluation programme, the auditee is asked to comment on the Department’s performance. This feedback is beneficial to the Department and can help make changes in the procedures. The prescribed format of the questionnaire is contained in volume two of this manual.

Audit Follow-up
The Department performs a follow-up audit to verify the implementation of the issues noted in the report. Actions taken are reviewed in order to determine if the desired results were achieved on the audit issues. The work of the Internal Audit follow up is further complemented by the work of the operations unit under the Commissioner General’s office.
CHAPTER FOUR

400 INTERNAL CONTROLS, AUDIT RISK AND MATERIALITY

410 Introduction

Internal control is broadly defined as a process that is implemented by the management to provide reasonable assurance regarding the achievement of objectives in the following categories:

i. Effectiveness and efficiency of operations
ii. Reliability of financial reporting
iii. Compliance with applicable laws and regulations.

Effectiveness and efficiency of operations includes the safeguarding of assets, that is, the prevention or timely detection of unauthorised acquisition, use or disposal of the Authority’s assets. It also includes responding appropriately to the business risks that face the organisation.

Internal control is control by management of what happens within the business. It is the totality of methods that management has introduced to provide reasonable assurance of the achievement of objectives and the avoidance of unwanted outcomes. Hence, internal control is the same thing as management control and, as such, it is an essential element of good management.

411 Management’s Responsibility for Internal Controls

The process of management comprises effective planning, organising, staffing, directing and controlling. Each of these must be done well if there is to be effective internal control. It is best to establish controls as early as possible within the system. Until control has been established, there is great possibility of error or loss that may go undetected.

Where control depends upon a reconciliation of figures, the reconciliation should be performed or supervised by someone who is (a) competent and (b) independent of the generation of any of the figures which are to be reconciled.

Where control depends upon supervision, it is important that this is taken seriously. Delegation is an important and valid management approach but it should not be abdication.
A well-designed system of internal control is worthless unless it is complied with. The semblance of control may lead to a false assurance. The top management should set a good example with regard to control compliance.

412 Elements of an Effective Internal Control System

There are five elements of an effective system of internal control.

Control Environment

i. Shared ethical values, including integrity, should be established, communicated and practiced throughout the Authority

ii. Human resource policies and practices should be consistent with the Authority’s ethical values and with the achievement of its objectives

iii. Authority, responsibility and accountability should be clearly defined and consistent with the Authority’s objectives so that the appropriate people take decisions and actions

iv. An atmosphere of mutual trust should be fostered to support the flow of information between people and their effective performance toward achieving the Authority’s objectives

v. People should have the necessary knowledge, skills and tools to support the achievement of the Authority’s objectives.

Identification and Evaluation of Risks and Control Objectives

i. Objectives should be established and communicated

ii. The significant internal and external risks faced by the Authority in the achievement of its objectives should be identified and assessed

iii. Objectives and related plans should include measurable performance targets and indicators

iv. External and internal environments should be monitored to obtain information that signal a need to re-evaluate the organisation’s objectives or controls.

Information and Communication
i. Communication process should support the Authority’s values and the achievement of its objectives

ii. Sufficient and relevant information should be identified and communicated in a timely manner to enable staff to perform their assigned responsibilities

iii. Plans to guide efforts in achieving the Authority’s objectives should be established and communicated

iv. Information needs and related information systems should be reassessed as objectives change or as reporting deficiencies are identified.

Control Procedures

i. Policies designed to support the achievement of the Authority’s objectives and the management of its risk should be established, communicated and practiced so that staff understand what is expected of them

ii. The decision and actions of different parts of the Authority should be coordinated

iii. Control activities should be designed as an integral part of the Authority, taking into consideration its objectives, the risks to their achievement, and the inter-related control elements.

Monitoring and Corrective Action

i. Performance should be monitored against the targets and indications identified in the organisation’s objectives and plans

ii. The assumption behind an organisation’s objectives should be periodically challenged.

iii. Follow-up procedures should be established and performed to ensure desired change or action occurs

iv. Management should periodically assess the effectiveness of internal control in its organisation and communicate the results to those to whom it is accountable.

413 Types of Internal Controls

Types of internal controls that auditors may find in the Authority include:

Organisational Structure

All the Authority’s departments should have a plan of their organisation, defining and allocating responsibilities and identifying lines of reporting for all aspects of their operations, including the controls. The delegation of authority and responsibility should be clearly defined.

An effective organisational structure should contain the following features:
i. The employment and training of competent personnel  
ii. The segregation of incompatible functions such as accounting and operating  
iii. The division of duties within the organization function  
iv. Well-defined responsibilities for all members of staff  
v. Defined and indicated reporting lines  
vi. Limitations and well defined responsibility at each level.

System Development Controls  
These internal controls relate to the introduction of new systems, or the modification of existing systems. Their purpose is to ensure that modifications are formally authorised, that adequate plans are made to cover a changeover period from one system to another, and that a new or modified system will still provide the required output. The auditor should note any major amendments or replacement systems being developed and then decide on the extent of audit involvement in the development of the new system.

Segregation of Duties  
One of the prime means of control is the separation of those responsibilities or duties that would, if combined, enable one individual to record and process a complete transaction. Segregation of duties reduces the risk of intentional manipulation or error and increases the element of checking.

Functions that should be separated include those of authorisation, execution, custody, recording and, in the case of a computer-based accounting system, systems development and daily operations.

Physical Controls  
These are concerned mainly with the custody of assets and involve procedures and security measures designed to ensure that access to assets is limited to authorised personnel. This includes both direct access and indirect access via documentation. These controls assume importance in the case of valuable, portable, exchangeable or desirable assets.

Management has a responsibility to safeguard the organisation's assets. Controls in this category are of significance to the auditor in relation to the occurrence and existence objectives. Restriction of access to the assets is a preventive control in this category. An example is by
having locked stores, or by keeping cash and easily convertible items such as instruments of payment in safes.

Periodic stocktaking is a detective control method in this category. The validity of the control depends on the segregation of the custodial and recording functions.

**Authorisation and Approval**

All transactions should require authorisation or approval by an authorised officer. Some transactions will require joint authorisation or approval e.g. signing of cheques. The limits for these authorisations should be specified. Such controls may involve either general or specific authorisation.

**General Authorisation**

There may be statutory authority for particular types of expenditures such as grant or the management may confer authority to acquire capital assets up to a certain value. Such authorisation is of a general nature and may affect the whole control environment.

**Specific Authorisation or Approval**

The responsibilities of the top management include accountability for incurring expenses and initiating activity. In these cases, expenditure cannot be incurred nor activity initiated without the approval of the authorised officer.

In some cases, approval levels for high value transactions may be with the Finance Committee or the Board of Directors.

**Certification**

The certification of documents by a responsible person, who has examined and checked them before any further processing takes place, normally relates to individual transactions and is therefore known as certification. An example of this would be where invoices for goods and services received are checked before payment is made.

Certification of the payment should be evidenced by the responsible officer's signature on the invoice. This is a common technique to ensure that all checking procedures have been completed and hence the validity of transactions before they are posted in the books of account.
Arithmetical and Accounting
These are the controls within the recording function which check that the transactions to be recorded and processed have been authorised, that they are all included, and that they are correctly recorded and accurately processed.

Such controls include checking the arithmetical accuracy of the records, the maintenance and checking of totals, reconciliations, control accounts and trial balances, and accounting for documents.

Personnel
Inevitably, the proper functioning of any system depends on the competence and integrity of those operating it. There should be procedures to ensure that personnel have capabilities commensurate with their responsibilities. The qualification, selection and training as well as the personal ethical characteristics of the personnel involved are important features to be considered in setting up any control system.

Supervision
Any system of internal control should include the supervision by responsible officials of day-to-day transactions and the recording thereof. Effective supervision will result from management involvement in supervision of the activities of the organisation by reviewing financial reports, budget variance analyses and monitoring the effectiveness of internal controls.

The Management
These are the controls exercised by the management outside the day-to-day routines of the system. They include the overall supervisory controls exercised by the management, the review of management accounts and comparison thereof with budgets, the Internal Audit function and any other special review procedures.

414 The Control Environment
The term internal "control environment" refers to the factors that have a significant impact on the selection and effectiveness of an organisation’s control procedures and techniques. The control environment has two distinct elements: control consciousness and general control mechanisms.
Control consciousness refers to importance the Authority attaches to its internal control procedures. The emphasis on strong and effective internal controls, when communicated and supported by the management, serves to instil a disciplined approach and prevent the entity's controls being circumvented.

The Authority should be seen to be managing its affairs in an economic, efficient, and effective manner; ensuring good value for money in the services it provides for and on behalf of the taxpayers or other stakeholders. If the relevant officers have established a satisfactory control consciousness, internal controls that are cost beneficial should be able to survive inappropriate pressures to meet these goals.

The management's commitment to an effective control environment can be demonstrated through taking prompt action on feedback from auditors or other sources about internal control weakness. This demonstrates management's commitment and thus reinforces control consciousness throughout the Authority.

The effectiveness of the control environment is also dependent on whether prompt action is taken against those who circumvent or override controls.

To sum up, if control consciousness is to have the desired impact, there must be general control mechanisms to make it work. General control mechanisms provide the discipline necessary to cause specific controls to function effectively. They include:

i. Organisational structure
ii. Policies and procedures for establishing, amending and communicating policies and procedures
iii. Budgetary controls and financial reports
iv. IT/IS general controls
v. Integrity and competence of personnel
vi. Codes of conduct.

The existence of a satisfactory control environment does not guarantee the effectiveness of any control. However, its absence will undermine the effectiveness of controls generally.
415 Limitations on the Effectiveness of Internal Controls

People operate most control functions hence the effectiveness of controls may be affected by errors of judgement or interpretation, misunderstanding, carelessness, fatigue and distraction. Additionally, internal controls that depend on segregation of duties may be abused through collusion. Senior managers can also override controls.

Therefore, no internal control system, no matter how elaborate, can by itself guarantee efficient administration and the completeness and accuracy of records.

416 The Auditor’s Use of Internal Controls

The objective of the auditor's examination of a system is to arrive at an opinion on the operation of the system, and provide recommendations for improvements.

Auditors should:

i. Identify each control system within the organisation
ii. Identify the overall objective of each control system
iii. Identify the necessary control objectives for each system
iv. Identify the key internal controls that provide assurance on the operation of the control objectives
v. Evaluate the operational-effectiveness of the controls, identifying any gaps and recommending improvements in procedures where appropriate
vi. Ascertain that prescribed systems of control are properly implemented and operate in practice to achieve organisational objectives
vii. Report on opportunities for improving operational performance, systems' strengths and weaknesses, and significant loss, error or other variance from laid down standards.

If the auditor assesses the controls and finds them to effectively address the risks and exposures, then the level of substantive audit tests can be reduced. Conversely, where the auditor concludes that control system is not fully implemented or does not effectively address the key risk and exposures, a higher level of substantive testing should be done in order to determine whether errors or losses have occurred.
420 Audit Risk and Materiality

421 Introduction

An internal audit conducted in accordance with auditing standards is designed to provide management with reasonable assurance that the systems of internal control are designed and operating in the best possible way in order to help the organisation to achieve its objectives.

An understanding of the term reasonable assurance is central to the efficient conduct of audits conducted by the Department. The view given in audit reports is itself based on a combination of fact and judgment and consequently cannot be characterised as either absolute or correct. Therefore when an auditor reports, the level of assurance should be reasonable in that context and cannot be absolute.

One hundred percent checking of all transactions does not guarantee absolute accuracy or absolute assurance that the conclusion of the audit report is correct. Modern auditing calls for audit tests to be carried out on representative samples of transactions, and therefore there is always a risk of not detecting errors.

Hence, the objective of the Department should be to minimise the risk of drawing an incorrect conclusion in respect of all matters that are material to the organisation. There always exists a risk that an auditor will issue an incorrect report due to the inherent limitations of any audit. Such limitations include those arising from:

i. The impracticality of examining all items
ii. The inherent limitations of any accounting and control system
iii. The possibility of collusion or misrepresentation for fraudulent purposes
iv. Most audit evidence being persuasive rather than conclusive.

Therefore, in carrying out the audit procedures and in evaluating the results of those procedures, it is important to consider audit risk and materiality in determining the nature, timing and extent of audit procedures. By determining the level of risk and materiality, the auditor can obtain a reasonable degree of assurance about the effective design and operation of internal control systems and the correctness of the documents and records examined.
Audit risk is concerned with material weaknesses in the design and operation of systems, and as such the risk analysis can only be carried out in light of the materiality decision, a decision that ultimately affects the level of testing.

### 422 Definition of Audit Risk and Materiality

Audit risk is the risk that audit procedures will fail to detect an absent, inappropriately designed or ineffectively implemented internal control or management arrangement, which could result in an unacceptable level of business risk. Business risk is the risk of the organisation failing to meet its objectives.

Materiality is the degree of relevance or significance of an absent, inappropriately designed or ineffective control or management arrangement, in relation to the business risk of the organisation.

An item should therefore be considered as material to Internal Audit if the absence, inappropriate design or ineffective implementation of an internal control or management arrangement could result in an unacceptable level of business risk.

### 423 Components of Audit Risk

The three components of audit risk are:

- **i. Inherent risk** – the risk of material error occurring in the first place
- **ii. Control risk** – the risk of internal controls failing to prevent or detect material error
- **iii. Detection risk** – the risk of audit procedures failing to detect material error.

**Inherent Risk**

Inherent risk depends upon the nature of the system, transaction or item audited and whether it is susceptible to error. It indicates the amount of assurance required from audit tests. The higher the risk, the greater the extent of audit tests required in order to increase the likelihood of detecting errors if they exist.

Factors to be considered in determining the inherent risk may include:

- **i. The nature of the business**, for example, revenue collection
- **ii. The nature of the operation**, for instance, cash, stores, properties
iii. Likelihood of staff turnover affecting the accuracy of the financial statements
iv. Competence of staff
v. Presence of morale problems with staff
vi. Past experience of operation of control
vii. Time pressures on staff
viii. Unnecessarily high degree of management involvement in day-to-day operations
ix. Opportunity to manipulate the books of account
x. Management motive for manipulating books of account
xi. Recent allegations of misconduct or fraud against the audited body by third parties or regulatory bodies
xii. Evidence of significant errors in previous years
xiii. Complexity of activities in the system.

In order to assess these issues the auditor needs to discuss the relevant topics with staff in the Department being audited. A good background to the key issues facing each Department will also provide useful intelligence to help the auditor make the assessment.

**Control Risk**

Control risk depends on the strength of the audited unit’s governance arrangements and systems of internal controls, and whether there are effective controls operating to reduce the risk of the organisation failing to achieve its objectives.

Factors to be considered in determining the control risk include:

i. The management's philosophy and operating style
ii. The unit’s organisational structure
iii. Methods of assigning authority and responsibility
iv. The Management's control methods for monitoring and following up on performance
v. The effectiveness of internal audit
vi. Personnel policies and practices
vii. Influences external to the entity
viii. The management's control methods over budget formulation and execution
ix. The management's control methods over compliance with laws and regulations
x. The management's ability to promptly identify and react to changing conditions.
Where effective controls have been put in place, auditors should be able to rely on the implementation of effective control procedures, and hence use a systems-based audit approach. Where effective controls have not yet been put in place, the audit approach will tend towards substantive testing of a large volume of transactions.

**Detection Risk**
Detection risk is the risk that the auditor's tests will fail to discover material control weaknesses in accounting, financial and operational systems. There are two components of detection risk: sampling risk and non-sampling risk:

**Sampling Risk**
This arises from the fact that only a sample is selected for the audit tests, so that items in a population falling outside the selected sample may or may not contain material error. Therefore, conclusions might be reached which could have been different had the whole population been examined.

While it is impossible to reduce sampling risks to zero without testing 100% of transactions, it is possible to reduce the risk to an acceptable level through use of appropriate sampling techniques.

**Non-Sampling Risk**
This is the risk that the auditor fails to draw the right conclusion from an item that has been examined. Such a risk often arises from inadequacy of staff training, failure to exercise due professional care and diligence, inappropriate audit procedures, inadequate audit supervision, etc.

Proper planning, supervision and review minimises this risk.

**430 Minimising Audit Risk**
Internal auditors minimise the audit risk associated by exercising professional practice and care. Through diligent application of the Internal Audit Standards, auditors can overcome limitations in their technical familiarity with the business process/function or activity to provide meaningful information and assurance. The following elements are needed to minimise risk:
Audit Objectives - The objectives to be accomplished in any operational audit task must be approved by the management, stated in writing and understood clearly by the assigned audit team.

Standards or Criteria - The means by which the function, activity or operation will be measured must be formulated. If standards or criteria are not available, the audit team must recommend their development.

Effective Audit Plan - In the field, planning activities becomes much more focused on specific audit procedures than is possible during preliminary work. Field planning reasonably assures that the work can progress in a smooth, efficient manner towards the achievement of stated objectives. The following are additional suggestions on the subject of field planning:

i. Make plans realistic. Schedule only those items that can reasonably be accomplished within the envisioned timeframe

ii. Do not be too formal. Elaborate schedules or excessive details give the misleading appearance of precision. Even the best plans are subject to much uncertainty.

iii. Schedule and perform audit in order to minimise disruption of the auditee’s personnel and facilities

iv. Early during the course of the fieldwork, establish the date of the exit meeting. This date serves as a target and assures maximum attendance of all interested parties.

v. Obtain approval from designed individuals for significant changes in previously approved plans, whether such changes in previously approved plans occur in the audit programme, budget, or in some other aspect.

Competence, Supervision and Review - Work must be performed by persons with adequate technical competence, and they must be properly supervised. In some situations, the auditors may not possess the requisite knowledge of the audit area. In these cases, the auditor must seek assistance from organisational sources that possess such knowledge.

Clear Reporting - Reports should be clear and concise. For each reportable condition, the auditor must describe the condition encountered, identify the cause, cite the risks/exposures that are attendant as a result of the condition and recommend action that will mitigate the condition.
431 Operational Audit Performance

The Internal Auditor requires a certain level of knowledge and understanding to accomplish a quality examination. There is nothing quite so disastrous to the Department as to have an internal audit report prepared by untrained people who arrive at the wrong conclusions and to have the report discredited by the operating staff.

Most auditors have acquired a basic knowledge of the principles of accounting, auditing or internal control. To perform an operational audit one must learn the specifics of the system under review. The auditor is expected to have at least a general knowledge of the area being reviewed. This can be gained in part from reading books, periodicals and procedures manuals on the subject.

While the steps of an operational audit may be divided in any number of ways, the four basic ones are:

i. Familiarisation with the physical operations and basic objectives of the segment to be audited. This involves documentation of existing systems.

ii. Review and testing of the mechanisms used to plan and control the operations and achieve the objective

iii. Appraisal and evaluation of the adequacy and effectiveness of the control mechanisms

iv. Reporting of the findings, usually, with recommendations for improvements.

440 Materiality

441 Introduction

No system of internal control, however elaborate, can by itself guarantee the soundness and application of accounting, financial and operational controls; nor can it be proof against human error or fraud. Even if this were possible it would be unnecessary: the cost of implementing such controls would likely be greater than the benefits accruing from them.

Financial records rarely need to be absolutely correct and a small degree of imperfection in the design and operation of internal systems of control is to be tolerated. This tolerance is known as materiality and it underlies financial reporting, the external audit process and the internal audit process.
442 Materiality versus Sensitivity to Public Opinion

The management of the Authority has a duty to the public to ensure the effective stewardship of the Government’s resources. The Internal Audit Department therefore has a responsibility to review, report on and assist the management to improve its stewardship of these funds.

Having a clear idea of what is sensitive for each system within the Authority is important for the auditor in:

i. Assessing specific risks in sensitive areas at the planning stage

ii. Deciding what and how to report when exceptions are disclosed by the auditing process.

Standard descriptions of materiality tend to focus on the financial value of a transaction, property or risk of loss. However, some items can be material to the Authority because of public perception rather than their financial value.

443 Factors Affecting the Materiality Decision

The two main factors that have to be considered when determining whether a matter is material are its value and nature. Items may be material individually or in total, while certain systems and transactions may be of more interest than others to the management and the public.

**Materiality by Value**

Generally, the larger the value of transactions or properties dealt with by a system, the more material is the associated control system. However, materiality has to be judged in relative and not absolute terms. What is material in one instance or context may not be material in another instance or context.

**Materiality by Nature**

Regardless of the value, some systems are of significance in their own right. For instance the payment of staff’s allowances could be immaterial by value, but the controls and transparency of the system for determining and paying allowances is likely to attract a high level of public interest.

In addition, materiality by nature may arise in relation to statutory responsibilities or reporting requirements, where a higher degree of accuracy might be expected than the tolerance level derived from normal materiality-by-value considerations.
Impact of Materiality on Internal Audit

Materiality plays an important part at planning and reporting stages of the audit. The nature and value of systems will influence the determination of materiality in different ways.

Impact of Materiality at the Planning Stage

The auditor’s objective should be to have a reasonable expectation of detecting material weaknesses in the design and operation of accounting, financial and operational systems. Setting an appropriate planning materiality (coupled with the risk analysis and confidence levels) should satisfy that expectation.

Materiality by Value

At the planning stage, materiality by value is likely to be the main determinant of the focus and level of testing, although materiality by nature may also contribute. The level set is a matter of judgement, which should be agreed between the auditor and the auditee.

Sensitivity

In general, the more sensitive the system and the higher the potential impact the system poses towards the organisation meeting or failing to meet its objectives, the lower the materiality level and the greater the work necessary to provide adequate assurance to the management.

Sensitivity in this context should take account of, for example, high political profile, potential privatisation or probable use of figures by "action groups". The decision should not be influenced by the Department’s staff resource availability. [The ranges are for guidance but should only be departed from in unusual or exceptional circumstances, which should be clearly documented).

Local Sensitivities

There may be instances where one part of the audit scope is considered to be more sensitive than the rest. The Auditor should treat this as a separate area and operate to a lower materiality level than for the rest of the audit.

Lowering the materiality of an area to reflect sensitivity is a judgement taken independently of assessing the likelihood of the errors arising in that area. That judgement will be made at the
planning stage as part of the risk analysis for the audit as a whole. Operation of a lower materiality level results in more work being done in the area than would otherwise be necessary in the light of its basic significance to the audit as a whole.

**Continuous Review of Planning Materiality**

The auditor should be alert to changes in the underlying factors on which the materiality decision was based. Major changes in the base figures or inherent sensitivities should result in a reassessment of materiality.

**Impact of Materiality at the Reporting Stage**

At the reporting stage, materiality serves as a condition for evaluating the weaknesses uncovered and considering the need for issuing a report to the management. It also helps in prioritising the findings and recommendations, which ensures that the management attention and action are targeted to the material weaknesses.

Throughout the audit and at its conclusion, the auditor is required to evaluate the test results. Normally, all errors found in a system will be aggregated, and extrapolated if appropriate, to give the best estimate of total errors in the system. This quantifies to the management the potential cost of the existing control weaknesses and acts as an indication of the need to improve controls.

Decisions about levels of materiality by nature and content involve a larger range of considerations and therefore require much more subjective judgements. Where a system or transaction is politically sensitive, it may be that one or two errors or weaknesses would represent a risk to the organisation, and hence should be reported.

**450 Review of procedure manuals developed by the other departments**

Internal Auditors will review procedure manuals developed by the other departments to ensure that issues of internal controls and segregation of duties are adequately addressed. Further, the documentation of work done by tax auditors in the Revenue departments during tax audits and settlement of cases will be thoroughly reviewed.
CHAPTER FIVE

500 FINANCIAL AUDITS

510 Introduction

This chapter deals with financial statement (FS) auditing, an important area of internal auditing. The chapter provides an overview of the methodology of financial statement auditing in the Authority. It also describes how an auditor will ensure compliance with the Generally Accepted Accounting Principles (GAAPs), International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS). FS audit is carried out in accordance with Generally Accepted Auditing Standards and with a view to expressing an opinion on the truth and fairness of the KRA financial statements.

Section 19(1) of the KRA Act (CAP 469) provides for the internal audit of the Authority’s Financial Statements (FS) and submission of an audit report on the FS to the Commissioner General, who will then submit the report to the Board of Directors for discussion and adoption.

The overall purpose of performing FS audits include providing users with assurance as to whether the FS are reliable, internal controls are effective, and are prepared in conformity with Generally Accepted Accounting Principles. The FS audit is also intended to obtain assurance about whether the FS are free from material misstatements.

520 Financial Structure

The Finance Department is based at headquarters with branches in all revenue departments namely Customs Services, Domestic Taxes and Road Transport. It is headed by a Senior Deputy Commissioner assisted by a Deputy Commissioner. The Department is divided into the following sections: Revenue, Budgetary Control, Expenditure, Cash Office and Treasury Management, General Ledger and Financial Reporting and Payroll.

Accounting Systems in Use

There are two systems currently in use namely:

i. Scala version 5.1 for financial accounting and reporting
ii. Memory for payroll processing

530 Definition

FS auditing seeks to provide assurance regarding compliance with established systems and procedures comprising the processes by which financial products and services are rendered or their efficiency and effectiveness for the purpose intended and the extent to which products of those processes comply with some agreed upon or generally accepted criteria.

FS audit can be broadly categorised into two namely: revenue audit and accounts audit. Revenue financial audit entails accounting and reporting of revenue collected by KRA on behalf of GOK and it is related to operational audits discussed in Chapter 6 of this manual. A disclosure on the revenue performance is reported in the Authority’s financial statement. Accounts audits entail review of the Authority’s income, expenditure, assets and liabilities.

531 Objectives

The objectives of FS auditing relate to the objectives intended for prudent management of the finance function within the Authority. The principal objectives, financial rules and policies are highlighted in the financial regulations and procedures manual of the Authority.

However, there are common themes that form the basis for FS auditing objectives. These include:

i. An effective environment in which staff can carry out their activities with integrity and honesty

ii. The availability of policies, procedures, and systems that enable the finance functions to achieve their objectives with due regard for the safeguarding of assets

iii. The development of timely, accurate, and reliable financial information for internal and external use.

FS audits provide assurance to management and others that the internal controls systems are functioning as intended and financial information complies with established requirements for timeliness, completeness, and accuracy. The nature of the services rendered by internal auditing is aimed at minimising exposure to business and financial risk rather than fixing problems or situations that have gotten out of control.
Quarterly FS audits help ensure that financial data reported quarterly is reliable for use by the management. This is achieved by independently applying objectivity and financial reporting knowledge to significant accounting matters that come to the auditor’s attention during the review process.

532 Materiality Levels and Tolerable Error
Materiality is determined in the field and is dependent on the account balance. Unusual transactions that are more than 20% of the account balance are reviewed.

The auditor should consider audit materiality and its relationship to audit risk while determining the nature, timing and extent of audit procedures. While planning the audit, the auditor should consider possible weakness or absence of controls and whether such weakness or absence of control can become a significant deficiency or material weaknesses.

Weakness in control is “material” if the fact or the potential effect could influence the decisions of the users of the financial information. The higher the materiality level, the higher the audit risk and vice versa. However, the auditor’s assessment of materiality and audit risk may vary from time to time depending upon the circumstances and changing environment.

533 Timing
Quarterly FS audits are done one month after the quarter and reported to the Audit committee. Financial Statements audits for the year end has statutory requirements. The KRA Act states that FS must be submitted to the KNAO by or on 30th September of every year. However, commencement date of the FS audit is dependent on presentation of FS and related audit schedules by the Finance Department.

Auditing of the internal control structure within the finance department is a process where each identifiable process, transaction cycle, function and activity of consequence is evaluated and tested for compliance. The objectives pertain to providing reasonable assurance that the transactions of the subject process, activity, function or cycle are properly authorised, recorded, reported and safeguarded.

The detailed tests of control on compliance, substantive and audit programmes are discussed in earlier chapters.
540 Budgetary Control Process

A budgetary control process is reviewed to determine how the budgets are arrived at and whether the users of the budgets are involved in its development. Reviews of budgets involve checking whether it is supported by planned activities and carrying out variance analysis of 15% of the budget versus actual expenditure each quarter. It is important for the auditor to ensure that available resources are adequately and effectively allocated to various activities that are planned for by the Authority.

The budget expresses in financial terms the Authority’s plans for the financial year. The period covered by the official budget is the fiscal year 1st July to 30th June. In preparing the budget, the Authority takes into account the diversity of demands placed on the limited corporate resources to ensure that it continues to operate in a dynamic and progressive way. Monthly management reports are prepared comparing actual expenditure against budgets hence facilitating cost control.

541 Budget Preparation

i) Preparation of Annual Budget

This begins with the issuance of guidelines on budget preparation and budget formats. This is done by the Budget Section by 30th November in the period preceding that to which the budget relates.

The Authority has adopted the Activity Based Budgeting method in the preparation of its annual budgets. All the Authority’s departments and sections participate in the formulation of their respective budgets. Budget estimates are then presented to the Finance Committee of the Board and the Board of Directors for approval. The approved budget is submitted to the Treasury by the 31st March of the period preceding that to which the budget relates.

The final budget estimates are submitted to the Authority’s Board for final approval in June after the confirmation of funding from the Treasury. The approved figures are communicated to budget holders in form of Authority to Incur Expenditure (AIE). These are issued to the departments by 30th June.
ii) Revised Budget Preparation

In December, instructions are sent to Commissioners and Heads of Departments to prepare revised budgets. Officers responsible for the preparation of budgets ensure that the revised budget estimates are submitted to the Budget Section by the 31st of December. In January, the management presents revised budget estimates to the Finance Committee of the Board and the Board respectively for approval. The revised budget takes cognisance of the impact of changes in Income and Expenditure estimates.

iii) Budgetary Control

The control of income and expenditure, within an agreed budget, is the responsibility of a designated budget/AIE holder, e.g. a Head of Department /Region /Station. The AIE holders are responsible for the management of the income and expenditure items appropriate to their budget. All expenses incurred by the Authority pass through the Budget Section for commitment before being incurred. Further, the funding of purchase requisitions is confirmed before approval for procurement is granted.

Review of the budget is achieved by constant monitoring and feedback from devolved budget holders and monthly monitoring of performance as measured by the management accounts.

iv) Reports

The monthly budgetary control reports are presented to the top management and the Finance Committee of the Board to help them monitor financial performance of the Authority.

542 External Auditors

The Authority is audited by KNAO as provided in the KRA Act cap 469. The Department will permit the external auditors’ access to the FS audit reports and working papers/files.

External auditors provide an independent opinion on the fairness of the FS contained in the Authority’s annual financial report and submit the report to Parliament.

543 Audit of Financial Functions at the Regional Offices

There are five regional offices in the Authority, which have accounting centres at each region’s head office. The regions are: Central, Southern, Northern, Rift Valley and Western. The accounting offices are in charge of accounting, monitoring and reporting revenue collected and
expenses in the regions. Audits are carried out in these regions to review expenditure, payment processes and accounting systems in place. In situations where procurements have been done, the procedures are reviewed.

544 Audit of Procurement and Stores Systems

Major procurements of goods and services in the Authority are done at the Authority’s Headquarters. The procurement procedures are generally guided by the provisions of the Public Procurement and Disposal Act and an audit will be carried out to ensure compliance. The stores procedures will also be audited to ensure that procured goods are properly accounted for.

545 Payroll Payment and Information Systems Audit

The Authority runs two payrolls namely:

i. The senior management payroll – This is contracted to a 3rd party.

This payroll is prepared by consultants on behalf of the Authority and caters for staff in grade KRA 1 to KRA 4. Every month, a schedule of changes in the payroll (derived from source documents received) is prepared by Senior Assistant Commissioner, Budget and Payroll. This is forwarded to the consultants through the Senior Deputy Commissioner, Finance. It is done by the 15th of every month.

The consultant processes the changes and submits a copy of the payroll for authorising. Final payslips and payroll reports are issued after the draft payslips are checked/authorised.

ii. The General payroll.

This is processed internally using the memory payroll system. A payroll audit shall be conducted as a systems audit. This will also include month-to-month comparisons of the number of staff factoring issues such as additions, deletions due to retirements and death.

545 Reporting and Audit Opinion

Section 19 of the KRA Act (Cap 469) provides that the Head of Internal Audit will submit to the Commissioner General a report on the Authority’s accounts in respect of every three months of financial year. The Commissioner General in turn submits the report to the Board for its consideration with copies to the Minister for Finance and KNAO.
CHAPTER SIX

600 OPERATIONAL AUDITS

610 Introduction

According to the American Institute of Certified Public Accountants, an operational audit engagement is a distinct form of management advisory service that may have some characteristics of financial audit engagement. It involves a systematic review of the organisation’s activities, or a section activities in relation to specified objectives. The purpose of the engagement may be:

i. To assess performance
ii. To identify opportunities for improvement
iii. To develop recommendations for improvement and further action.

For the purpose of internal auditing, operational audit is defined as a systematic review and evaluation of an organisational unit for the purpose of determining its effectiveness and efficiency. It includes a review of the management control system for any business activity/process/function, and identification of factors that may hinder efficiency and effectiveness of the function.

Operational audits share much in common with financial auditing. Areas of similarities include planning, evidence gathering and reporting. However, operational audits are devoted to assessing the efficiency and effectiveness of operations within the Authority. It should be noted that even with the best plans, intentions, resources and skills, management and their supporting staff, the Authority may not perform as expected. There is always room for improvement. It is this improvement in operations that operational auditing seeks to contribute.

The operations areas in the Authority are functionally defined on the basis of departments. These include Domestic Taxes, Customs Services, Road Transport, Support Services, Information and Communication Technology, Human Resources, Administration & Corporate Services, Finance, Investigations and Enforcement and Internal Audit. In all these operational areas there are business processes designed to achieve specific business objectives. An operational audit is
generally aimed at evaluating how well these departments’ processes can achieve the set control objectives.

620 Nature of Operational Audits

The statement of responsibilities of Internal Audits, published by the Institute of Internal Auditors (IIA) outlines six activities involved in attaining the overall objectives of operations audit. These are:

i. Reviewing and appraising the soundness, adequacy and application of operating controls, for a business process

ii. Ascertaining the extent of compliance with established policies, plans and procedures

iii. Ascertaining the reliability of reports issued to management

iv. Appraising the quality of performance in carrying out assigned responsibilities

v. Recommending operating improvements

vi. Accounting for and safeguarding assets

For public sector organisations, operational audits consists of these additional elements:

i. Financial and Compliance - Determines whether (i) financial operations are properly conducted (ii) the financial reports of an audited entity are presented fairly and (iii) the entity has complied with applicable laws and regulations.

ii. Economy and Efficiency - Determines whether the entity is managing or using its resources in an economical and efficient manner and determines the causes of any inefficiencies or uneconomical practices, including inadequacies in Management Information Systems, administrative procedures, or organizational structures.

iii. Programme Results – determines whether the desired results or benefits are being achieved, the objectives are being met, and the management has considered alternatives that can yield desired results at lower cost.

630 Operational Audit Performance

The Internal Auditor requires a certain level of knowledge and understanding to accomplish a quality examination. Most auditors have acquired a basic knowledge of the principles of accounting, auditing or internal control. To perform operational audit, one must learn the specifics of the system under review. The auditor is expected to have at least a general
knowledge of the area being reviewed. This can be gained in part from reading procedures manual, books and periodicals on the subject.

While the steps of an operational audit may be divided in any number of ways, the four basic steps are as follows:

i. Familiarisation with the physical operations and basic objectives of the segment to be audited. This involves documentation of existing systems

ii. Review and testing of the mechanisms used to plan and control the operations and achieve the objective

iii. Appraisal and evaluation of the adequacy and effectiveness of the control mechanisms

iv. Reporting of the findings usually with recommendations for improvements.

640 Performance Audit /Value for Money

The term “Value for Money” (VFM) is commonly used to describe the combination of economy, efficiency and effectiveness within an organisation. Improving VFM is a major objective of the Authority. This chapter is to clarify the Department’s role in these two tasks – performance audit and VFM -- and to give guidance on the approach that auditors should take to these issues.

The primary responsibility for achieving VFM lies with management who should institute appropriate arrangements for securing value for money and for monitoring its achievement in the operations they manage.

The management may appraise the achievement of VFM by instituting special reviews of particular policies, programmes, activities or units. Such reviews may be carried out by senior officers, inspection and review services (including Internal Audit), specialists, external auditors or consultants, or by joint teams made up of staff selected from these groups.

641 Role of Audit in VFM

The role of Audit in the Authority in relation to VFM is two-fold:

i. As an integral part of its responsibility to evaluate the internal control system, Internal Audit examines and evaluates the controls established by the management to secure good value for money

ii. Auditors may conduct, or participate in, special VFM reviews.
642 Value for Money and Systems Auditing

The primary objective of Internal Audit is to provide an opinion on the adequacy, reliability and effectiveness of the systems of internal control, and to advice management on required improvements. The evaluation of controls over economy, efficiency and effectiveness of procedures, programmes and processes is essential component of this responsibility.

The concepts of economy, efficiency and effectiveness are central to an understanding of value for money. They define the relationships between plans (including objectives and targets), inputs and outputs:

i. Economy is concerned with minimising the cost of resources used for an activity, having regard to appropriate quality

ii. Efficiency is the relationship between output, in terms of goods, services or other results, and the resources consumed

iii. Effectiveness is the extent to which the objectives of an activity are achieved and the relationship between the intended impacts and actual impacts of an activity.

These concepts can be applied to policies and programmes as well as to intermediate activities such as administration and control. The economy, efficiency and effectiveness of parts of a system can be evaluated separately from the system as a whole.

Economy, efficiency and effectiveness are closely inter-related. They can be judged in isolation but should normally be considered together, as one element may be traded off against another. For example, a system may become more effective if more resources are put into it, but may then fail to meet the desired standard of economy. Consequently, the term ‘value for money’ is often used to describe the combination of economy, efficiency and effectiveness.

In performing VFM reviews, auditors should:

i. Clearly identify and appraise the framework of controls associated with the Authority’s VFM strategy. This framework may consist of any organisational strategy, reporting systems, or parts of individual systems, which have been (or should be) established by officers to ensure that resources are employed with due regard to VFM

ii. Emphasise VFM considerations when planning the audit work. This may include taking account of indications of poor VFM
iii. Consider the need to adopt a particular approach to appraising VFM in resource-intensive systems
iv. Ascertain the Accounting Officer's requirements for VFM audits, and whether the Department has adequate resources to meet those requirements
v. Clearly demonstrate the way in which Internal Audit will address VFM when planning its work
vi. Make clear the extent to which they intend to comment specifically on VFM issues within their statement of assurance.

These measures will allow the provision of a more fully informed statement of audit assurance on those systems or parts of systems that are critical for the attainment of VFM. The approach and methodology to be employed in the appraisal of VFM will vary according to the type of audit conducted. The types may include:

i. Systems audit -- which may focus on VFM control systems and the implementation/maintenance of a VFM strategy
ii. Modified systems audit - enlarged to increase the level of substantive testing and provision of detailed cost recommendations
iii. Special VFM audits - investigating signs of possible waste, the effect of important projects, the efficient conduct of standard managerial operations, or small-scale reviews designed to foster cost consciousness.

643 Why the Department should be involved in VFM Reviews
Auditors are particularly suited for conducting VFM reviews because of their independence and professional expertise in review and analysis. Possible benefits for Internal Audit include:

i. Internal auditors' knowledge and expertise may be improved through experience of types of work outside those normally encountered in the Internal Audit Department
ii. Reviews may present an opportunity for Internal Auditors to deepen their knowledge of the activity reviewed, and to look closer at the effects of internal control in operation
iii. Involvement in high profile reviews, recognised by officers to require a high level of expertise and professionalism, can enhance the prestige and status of internal auditors
iv. Closer involvement of auditors with operations may encourage officers to see auditors as helpful and so encourage a participative approach to audit work
v. Involvement in team work requires closer working with other consultancy, inspection and review services and should lead to better understanding and relationships.
The Department may contribute to VFM reviews without serious consequences for its independence by:

i. Limiting its participation to the evaluation of control in the area specified thus enabling the results of the work to be integrated with normal Internal Audit activity

ii. Seconding auditors to participate in or carry out the VFM review.

Where auditors do form part of a multidisciplinary review team, they should protect their professional independence by reserving the right to report independently if there is any disagreement over findings. Auditors can minimise the effects of possible compromise to audit objectivity by ensuring that they do not audit areas where they have been involved in VFM reviews.

The primary tool for VFM audits is process mapping (flowcharting or narratives). VFM audits consist of basically four steps:

i. Understanding the process - The difference in VFM audits is that in addition to control concerns, the auditor should identify business objectives, identify high-risk procedures, identify gaps in the process, and develop audit objectives and scope to focus on VFM issues. By focusing on the business, and by working with the auditee, value can be added to the business process activity.

ii. Identifying process gaps - These gaps may include the identification of new controls needed for changing business requirements or improving the design of existing controls. They also include gaps in the process that are not control related and excess steps (including controls) that could inhibit efficiency. It may be necessary for the auditor to prepare "should be" process maps in addition to the "as is" process maps. This step requires a thorough understanding of processes and working with the auditee.

iii. Validating process performance measures and assess controls - as opposed to testing controls, more time is spent on judgmental, but value-added analysis of process design. This will include validating the performance measures management relies on

iv. Make process improvement recommendations - Recommendations that come out of VFM audits should help management improve the effectiveness and efficiency of the business process as well as controls.
CHAPTER SEVEN

700 INSPECTION

710 Introduction

Inspection is a special form of audit that aims at identifying operational weaknesses and inadequacies in physical facilities that can hamper effective and efficient discharge of the Authority’s mission. Inspection emphasizes on the work environment and staff morale as opposed to ordinary internal audits which concentrate on examination of records and review of the internal control systems.

711 Inspection Strategies

Inspection strategies covers areas like staff matters, office accommodation, transport and other administrative matters.

720 Staff

721 Objectives

i. To assess the human resource capacity, both technical and support, at the station or department.

ii. To assess frequency of staff transfers as an internal control measure and as a strategy of ensuring continuously revitalised staff

iii. To assess fairness in the basis of staff promotion and discipline

iv. To assess fairness in work allocation to the officers in the station or department

v. To assess the performance of the officers

vi. To identify problems encountered by staff in meeting their objectives

vii. To review the position of staff leaves.

722 Procedures

Establishment

The establishment for a station/department will be as per the approved structure. The information on the station/department’s establishment will be collected for both the technical and support staff. Casual employees working at the time of inspection will be included in the inspection. The
information collected should include their names, employee numbers, designations, age, date of posting to the station and date of promotion to the present position.

**Work Allocation**
The information on work allocation schedules and organisation charts for all staff and programmes in the station will be obtained from the station manager or the unit head. This will be compared with the staff list and the attendance register to ensure that all staff is fully engaged. The auditor will check for any biased allocation of work and plans for continuity in programmes which are currently being handled by officers who are about to retire.

**Targets and Performance**
Targets for all the technical staff in respect of each programme in the station will be obtained. The level of performance of each officer will be obtained from the management reports and compared with the targets. This will provide an independent appraisal of the technical staff. It will also assist in identifying the officers who require further training or refresher courses. The station head and the affected officers will explain major shortfall or variance in expected performance.

The following will be the rating (achieved proportion of the target)

- Very good - 80% and above
- Good - 60%-79%
- Average - 40%-59%
- Poor - below 40

**Attendance**
The main objective of reviewing attendance is to ensure that the officers adhere to the Authority’s rules and regulations governing official working hours and leaves. The auditor will examine the daily attendance register and daily absence reports. Auditors will ensure that the attendance registers are appropriately signed and agree with leave roster and sick leave reports. Sick leave reports will be supported by sick sheets or similar documents. The auditor will examine management file for any disciplinary action taken for unauthorized absence from duty, inadequate performance and check for warning letters in the officers’ confidential files.
723 Office and Staff Accommodation

Objectives

i. To assess the level of physical security at the station including fire prevention appliances, locks, keys allocation and general office security

ii. To check adequacy and efficiency in the use of office equipment, furniture, communication facilities, stationery and other general office facilities

iii. To check the state, condition and adequacy of office accommodation and staff houses in the station.

Procedures

i. The auditor will check security arrangements, conditions, adequacy and sufficiency, fire precaution and appliances, cleanliness and state of repair of the roofs, offices, staff houses, registries, archives and libraries. In addition, auditors will check office accessibility/location to the taxpayers in view of the current and future trends in business activities in the station and its environs.

ii. The auditor will check condition of furniture, state of repair and sufficiency. Working conditions of equipments, like typewriters (whether manual or electric), computers, faxes, calculators and cabinets will be identified and their conditions will be inspected.

iii. The auditor will check if the required stationery is requisitioned on time (check re-order level), received without undue delay, properly recorded and used for purposes intended.

iv. Efficiency in reply of mails from traders without delay will be checked by examining complaints files, suggestion box contents, observation of operations and interviewing the staff. Acknowledgement of every letter should be done within two weeks of receipt. Issues raised in the normal letters should be cleared within one month. Exceptional cases should however be cleared within a reasonable time. Cases of long delays will be examined and explanations sought from the station head and the officer concerned.

v. The auditor will confirm that a key register is maintained and updated when an officer is transferred or ceases to be an employee of the Authority. This will guard against loss of the Authority’s assets in case un-surrendered keys are mishandled.
vi. The auditor will check that a register of trunk calls is maintained and the calls are properly authorised. Further, checks will be made to ascertain if payments are made for all unofficial (private) calls.

730 Transport

731 Objectives

i. To assess the adequacy of the transport facilities in the station

ii. To assess the condition of transport facilities

iii. To assess the adequacy of the drivers in relation to motor vehicles, boats, bicycles, motorcycles and other means of transport

iv. To assess the level of adherence to the Authority’s policy on use of transport facilities.

732 Procedures

The auditor will find out the number of vehicles, condition and the current state of vehicles. From the work tickets, the auditor will check if the vehicles are being used in the official duties and in the delivery of programme in the station. The auditor will note any misuse of vehicles and disciplinary measures taken thereof. Physically inspect the vehicles to confirm their existence and check for any un-reported damages. Further, find out the condition and the current state of boats, bicycles, motorcycles and lifts then document all the findings. The auditor shall also ensure that the vehicles were appropriately allocated to the station and will note excesses or deficiencies and recommend appropriate action.

740 Administrative Matters

741 Objectives

i. To examine the administration procedures used at the station and their consistency with the Authority’s policy and other relevant statutory requirements.

ii. To assess the administration procedures used to serve customers and assess their adequacy.

iii. To assess any weaknesses in administration which can affect the performance of the staff and the station in general.
742 Procedures
The auditor should find out whether circulars, routine orders and work instructions are received in good time for immediate implementation. The auditor will find out whether the management briefs the officers on how to implement the instructions. The auditor will review level of compliance with the circulars and work instructions issued.

The auditor should hold separate discussions with the management, technical staff and support staff. The auditor should document complaints from both technical and non-technical staff and the suggested solutions. The auditor should discuss shortfalls in performance with the station manager and the affected officers and document all the explanations. Assess the inter-personal relationships in the station by interviewing staff, observation of activities and examination of communication made to or by staff to management. For confidentiality, the auditor should not identify the officers with the complaints on another officer. If necessary, discussion on sensitive matters should be done with the concerned officers in their respective offices or in the office allocated to the auditor. This will ensure open discussion and non-victimisation. The auditor will record all the traders’ complaints identified in the review of inward mail/correspondence.

The auditors should inspect any other aspect of the station, for instance, staff welfare, morale, officers cleanliness, staff housing, the record of accidents within the station and any resulting claims for damages by staff or the public, neatness of the files and filing of the same, the record of meetings by station head and his/her staff and document the findings.

The auditor should discuss all the inspection findings with the station manager and the officers assessed and seek their comments as per the standard audit practice.
CHAPTER EIGHT

800 OTHER TYPES OF AUDITS

810 Quality Management Programme (QMP) Audits

Quality Management Programme (QMP) audits should be planned as part of the overall work plan of the Department. The aim of the QMP audits will be to determine whether the quality management system conforms to the best practices as stipulated in the ISO Standards and the quality management system is effectively implemented and maintained.

811 Audit Strategies

i. QMP audits should be conducted as provided by the Authority’s Quality Policy and Quality Management manual

ii. The auditor should use the quality management systems requirements of the International Organization for Standardization (ISO) as benchmarks to compare the Authority’s planned and actual measures

iii. The auditor should also compare the Authority’s promises to its customers through the Taxpayers’ Charter with the actual performance.

812 QMP Audit Objectives

The QMP audits should be aimed at ensuring that the Authority’s management system follows the Plan – Do – Check – Act cycle. That is, plans are devised and followed for appropriate activities; actions are checked for compliance with the plans and corrective and preventive actions taken.

Specifically, the objectives should be to obtain assurance that:

i. The management has identified, documented, implemented and maintained the processes necessary for a quality management system and offer of quality services to its customers

ii. The top management has provided evidence of commitment to development, implementation and continuous improvement of the quality management system for it to be effective

iii. The Authority has determined and provided the resources needed to implement, maintain and continuously improve the quality management system and to meet the customers’ requirements
iv. The Authority ensures that its personnel are competent on the basis of appropriate education, training, skills and experience 

v. The Authority plans and implements the monitoring, measurement, analysis and improvement processes needed to demonstrate conformity to the tax laws, the quality management system and the continuous improvement of the quality management system.

820 Investigative Audits

821 Introduction

Investigative audits are performed when fraud is suspected in the Authority. The audits focus on alleged civil or criminal violations of the Kenyan laws, Authority’s policies and procedures. Internal theft, white collar crimes (cheques and credit cards fraud, cyber crimes etc), misuse of the Authority’s assets and conflict of interest are examples of reasons for carrying out investigative audits. The audits may result in prosecution or disciplinary action taken on the offender(s) or both.

Webster’s Ninth New Collegiate Dictionary defines fraud as “deceit, trickery, and intentional perversion of truth in order to induce another to part with something of value or to surrender a legal right.” In accounting or auditing literature, the term “fraud” has been clearly defined as follows: an intentional deception, misappropriation of a company’s assets or the manipulation of its financial data to the advantage of the perpetrator.” The Institute of Internal Auditors (IIA), in Statement on Internal Auditing Standards (SIAS) No 3, “Standards for the deterrence, Detection, Investigation, and Reporting of Fraud,” defines fraud as follows: “Fraud encompasses an array of irregularities and illegal acts characterized by intentional deception.”

“Computer Fraud” is defined by Brandt Allen in his article “The Biggest Computer Frauds: Lessons for CPS” Journal of Accountancy, 143 No. 5, May 1977, p. 52”: any defalcation or embezzlement accomplished by tampering with computer programs, data files, operations, equipment or media and resulting in losses sustained by the organization whose computer system was manipulated.”

822 Fraud Audit Procedures

Sources of Fraud Information

The major sources of fraud information include:

i. Detection during routine or other investigative audits
ii. Report from third parties like members of staff, informers, the media, e.t.c.

iii. Instructions from the Commissioner General (CG), Commissioners and Heads of Departments on suspected fraud cases or areas

iv. Board of Directors through the CG.

Role of the Internal Audit Department in Fraud Investigations

The Department shall investigate frauds which arise as a result of the following:

i. Fraud which is discovered by auditors during their routine audit procedures of functions and systems within the Authority. However, this will only be done after completion of the audit assignment of which a recommendation shall be made for investigations to be carried out

ii. Fraud cases which have been referred to the Department by Board of Directors, Commissioner General, Commissioners and Heads of Departments.

Auditors appear as expert witnesses in case the fraud investigations lead to court prosecutions. Court prosecutions are handled by the Investigations and Enforcement Department who will also act as a link between the Authority and other Government investigative agencies on all fraud cases.

Audit Procedures

Detection in the Course of Audit

i. The auditor should report the matter to the immediate supervisor who in turn reports to the Head of Internal Audit. The Head of Internal Audit immediately informs the CG and the SDC-Investigation and Enforcement

ii. The suspected fraud may call for change in audit plan and strategy to concentrate on the area of suspected fraud. In addition, Investigation and Enforcement Department may be involved if necessary

iii. Where it is a member of staff involved in the fraud, the reporting of the fraud information should flow throughout the chain of command up to the Commissioner General before the audit is commenced.

iv. Staff members subject to the complaint shall not be initially advised of any inquiries as this may prejudice future investigations. Members of staff and auditors who get privy to fraud information are required to maintain confidentiality with respect to complaints or
matters referred to them. Care shall be taken to avoid unnecessary or prematurely alerting individuals against whom allegations have been made.

v. Once suspicion has been aroused, the suspect may not continue to operate as before. Immediate action will be taken to seek legal advice on whether there are sufficient grounds to suspend the employee. If a decision is made to suspend the suspect, then the timing shall be done to prevent the suspect from destroying or removing evidence that may be needed to support disciplinary or criminal action. All access rights to the premises and computer systems shall be withdrawn. Further, any authority the suspect may have on behalf of the Authority shall be terminated. The suspect shall be supervised by the security personnel at all times if a decision is made not to suspend the suspect(s).

vi. Any breach of confidentiality by officers to whom fraud has been reported to may result to disciplinary action being taken against them.

vii. Any communication with the external parties as regards the results of the investigations i.e. the media shall be with prior approval of the CG as enshrined on the code of conduct of the Authority.

**Instructions from the CG, Commissioners, Head of Department (HOD) and Fraud Information from Members of Staff**

The information should be in written form or verbal. It should be precise and evidence, if any, should be attached. It should also include the following where possible:

i. Name(s) of suspected fraudster(s) and the staff number(s)

ii. The Department, Station, Section and/or office of the suspect

iii. Date(s) or period when the fraud was committed or suspected to have been committed

iv. Estimated amount of revenue loss suffered by the Authority as a result of the fraud

v. Brief description of the nature of fraud

vi. Available documentary evidence

vii. Any other information that may assist in investigation

viii. The report must be signed.

The Head of Station or Section should ensure that evidence is secured by locking up documents in a safe or secure office. If related to a fraud on data in the computer database, backup should be made and secured.
Conducting Fraud Investigation

The management is normally responsible for deciding whether or not to pursue a fraud investigation. However, if the Department believes management itself may be involved in the fraud, the Board of Directors will be notified and they are then responsible for approving further action. If either management or the Board of Directors makes the decision to investigate possible schemes, extended procedures shall be performed to follow up on the fraud indicators first noted by the internal auditors. These are:

i. Planning of the audit/investigation should be carried out immediately. During planning stage, the internal auditors shall evaluate the extent of the fraud scheme and the level of personnel involved. In addition, planning shall be done to encompass matching the knowledge, skills and disciplines required to conduct an investigation with the technical expertise of available Internal Auditors and other specialists. The Head of Internal Audit shall allocate a suitable auditor to lead the audit team, preferably of rank not lower than Principal Auditor, and the audit should commence immediately.

ii. Auditors should proceed as quickly as possible to the place of suspected fraud. Careful consideration shall be taken to ensure that managers and employees who may be involved are not inadvertently tipped off.

iii. Interviews should be conducted and documented with the Head of Station/Section and all other officers (including suspected officer(s)) who may provide necessary information. The suspected officer, where possible, will be preferably interviewed before the close of the investigations.

iv. Documents and written information and any other evidence should be secured.

v. Confirm the information provided on the fraudulent activity and establish the extent of the fraud.

vi. Prepare weekly progress reports for the Head of Internal Audit who should brief the Commissioner General as appropriate. In certain cases and usually at the initial stages of the investigation, reporting can be more frequent as dictated by facts on the ground. The frequency will vary from case to case and the lead auditor can have discretion on this.

vii. The use of internal and external experts on MIS, Legal, Investigation and Enforcement will be considered. In addition, cases may be referred to Kenya Anti-Corruption Commission (KACC), Criminal Investigations Department (CID), and Efficiency Monitoring Unit (EMU) if required. If specialists outside the Authority are included in the investigation, their credentials shall be evaluated by checking appropriate licenses and certifications and making inquiries regarding the professional reputation of the
specialists. The Department shall also ascertain that no relationship exists between the unit or persons being investigated and the specialists.

viii. Fieldwork and interviews will be dictated by the circumstances of the case and the auditor should determine the amount of work to be done. Several audit teams may also carry out similar audits but at different locations simultaneously.

ix. The audit work shall be reviewed by the immediate supervisor (Preferably the Manager in charge of the unit) or Deputy Head of Internal Audit depending on the extent of the fraud.

x. Consider the need for revision of the plan as the case progresses.

xi. Consider extending the investigations to related areas in other offices of the Authority.

xii. Audit procedures and progress reports shall not be shared with the auditees. In fact, the objectives of the investigation may be masked so that the potential for losing evidence is minimised.

xiii. During the investigation, any auditor suspected to have been complacent should be dropped from the audit team and a suitable replacement made.

xiv. The auditors may consider using appropriate computer programmes to detect or substantiate fraud.

xv. The fraud investigations may be a pointer to systems weaknesses and the auditors may then consider amending the audit schedule to incorporate a regular systems audit in the affected area (s).

xvi. At the conclusion of the fraud investigations, the Auditors will utilise the information obtained to help the Authority to be more secure and robust in future. From details of the scheme, the Auditors may be able to develop recommendations for controls that should be implemented in future to prevent similar frauds from occurring. Also, from knowledge of actual fraud cases, audit tests shall be designed to detect similar schemes in other units. Finally, information on recent frauds adds to the Department’s database of knowledge and helps in identifying future indicators of fraud.
**Reporting Procedures**

In the course of the investigative audit, the Head of Internal Audit will keep the CG informed on the progress of the investigation. It is important to maintain confidentiality in all investigations to protect the integrity of the investigation results and those involved. An auditor’s report on fraud may be made at an interim point (for example, after the detection phase) or at the conclusion of the work. The interim report may be in writing or may be made orally. However, the report at the end of the investigation phase, encompassing findings, conclusions, recommendations and corrective action taken, must be in writing. If a report is made at the conclusion of the detection phase, the communication shall present the Department’s recommendation as to whether an investigation is warranted, along with support for that recommendation.

i. The report should be addressed to the CG but where the investigation was sanctioned by another party (Commissioners or HODs) other than the CG, a copy shall be made to the other person(s).

ii. Two reports are produced; one for the Court stating the facts of the fraud and the second for the management detailing weaknesses, recommendations and the way forward. The audit supervisor or any other auditor in the team (where applicable) shall sign the Court report. A draft of the court report shall be reviewed by the Legal Services Division before its issuance.

iii. The audits will be done in accordance with the Authority’s policy on fraud and corruption. The policy should describe the activities that constitute fraud, state signs of fraud, outline the methods of reporting fraudulent activities, specify who to report to and provide protection for whistle blowers and the investigators. It should also state whether or not the suspected officer should be suspended or forced to take leave during the investigations. This will ensure all staff members are aware of procedures of reporting suspected fraudulent activities.

iv. However, two situations relating to fraud call for quick reporting by the Department. In the first case, if a significant fraud has been discovered and the details have been established with reasonable certainty, the management or the Board of Directors shall be informed without delay. The second case relates to a fraud that impacts on issued Financial Statements of previous periods. If such a scheme is discovered, the Department shall inform management as well as the Audit Committee of the Board of Directors.
830 Third Party Audits

831 Introduction
In the course of audit, it sometimes becomes necessary for the auditors to seek information from third parties. The third parties may include agents (as in withholding tax), banks, airlines for APSC revenue and other taxpayers. This situation may arise in the course of routine, investigative or ad hoc audits.

832 Guidelines to Third Party Audits
These guidelines are developed to govern/guide interactions between the department and third parties (outside the Authority) so that no confusion arises as far as the mandate of the Internal Audit Department as opposed to other departments’ roles.

Sometimes Auditors find it necessary to corroborate evidence gathered internally from the Authority’s records with third party information or get more evidence directly from the taxpayers’ records. Situations, which demand this kind of confirmation from third parties, include the following:

i. Where the Authority is interested in knowing whether all the revenues paid into the banks have been remitted to the main collection accounts

ii. Where the Authority is interested in knowing whether the withholding agents are remitting all revenues collected

iii. Where scanty information on transactions exist within the Authority records and systems. Auditors may wish to corroborate this with third party information relating to those specific transactions

iv. Where documents supporting specific transactions cannot be traced from within the Authority, the auditor may wish to seek such information from the taxpayer concerned

v. Where the management has specifically requested an audit of particular third party transactions with the Authority.

Procedures
When such situations arise, the following guidelines should be employed to govern interactions between internal auditors and the concerned third parties.

i. All communication with outsiders should be approved by the Commissioner General.

ii. A letter requesting for specific information has to be written to the taxpayer and signed by the Head of Internal Audit or the Commissioner General
iii. Occasionally when time is of essence, a phone call to the taxpayer with the permission of the Head of Internal Audit would suffice
iv. A visit to the taxpayer can then be arranged by appointment, where necessary, for purposes of collecting data or verifying specifics from the taxpayers’ records or premises
v. The auditor is expected to conduct himself professionally at the taxpayer’s premises and stick to relevant issues
vi. A report will be done on the findings of the visit, which will form part of the overall report on the audit
vii. Such reviews will not absolve the taxpayer from subsequent audits by other departments
viii. In case entry is refused, the auditor in consultation with the Head of Internal Audit should seek the assistance of the Investigations and Enforcement Department.

840 Consulting Services

Internal Audit is an independent, objective and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objective by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

The definition of Internal Auditing gives cognisance to consulting activities in the organisations within which the internal audit activity takes place. The International Standards for the Professional Practice of Internal Auditing gives guidance on how the consulting activity is to be carried out. Below are the salient features of the standards:

i. The nature of the consulting activity should be defined in the audit charter
ii. Auditors may provide consulting services relating to operations for which they had previous responsibilities
iii. If auditors have potential impairments to independence or objectivity relating to proposed consulting services, disclosure should be made to the engagement client prior to accepting the engagement
iv. The Head of Internal Audit should decline the consulting engagement or obtain competent advice and assistance if the internal audit staff lacks the knowledge, skills or other competencies needed to perform all or part of the engagement
v. The Auditor should exercise due professional care during a consulting engagement by considering the:
• Needs and expectations of clients, including the nature, timing and communication of engagement results
• Relative complexity and extent of work needed to achieve the engagement objectives
• Cost of the consulting engagement in relation to potential benefits.

Consulting Services that Internal Audit may provide:
The Department may provide the following consulting services provided that appropriate safeguards are in place:

i. Facilitating the identification and evaluation of risks by making available to the relevant officers the tools and techniques used by the Department to analyse risks and controls
ii. Using the Department’s expertise in risk management and control, and overall knowledge of the Authority’s operations and objectives to champion the establishment of a risk management framework
iii. Providing advice and facilitating workshops on risk and control
iv. Providing advice, facilitating workshops, and coaching the management on risk and control
v. Supporting the officers in identifying the best way to mitigate risk.

The appropriate safeguards include:

i. Ensuring that it is confirmed in writing that the management retain overall responsibility for risk management
ii. Ensuring that management decide the most appropriate responses to risk. The Department should advise and offer critique without assuming responsibility.
iii. Ensuring that Internal Audit does not perform any roles that constitute risk management.

The procedures to be followed in carrying out such consulting activities will depend on the circumstances of the individual cases

Consulting Services that the Department should not provide
The Department should not undertake any of the following consulting activities:

i. Imposing the risk management processes in the Authority;
ii. Providing assurance on the operation and effectiveness of risk management processes on behalf of the management
iii. Implementing the risk management programmes
iv. Managing the risk management process
v. All activities where the competence of the auditor is in doubt.

850 Information Systems (IS) Audits

851 Introduction

Information Systems (IS) audit can be defined as any audit that encompasses review and evaluation (wholly or partly) of automated information processing systems, related non-automated processes and interfaces between them.

Information Systems audit processes collect and evaluate evidence to determine whether the information systems and related resources adequately safeguard assets, maintain data and system integrity, provides relevant and reliable information, achieve organisational goals effectively, consume resources efficiently, and have in effect internal controls that provide reasonable assurance that business operational and control objective will be met and that undesired events will be prevented, detected and corrected in a timely manner.

The following are the major information systems in use in the Authority:

i. SIMBA 2005 (GAINDE)
ii. Income Tax Information System
iii. VAT Information System
iv. RTD Information System
v. KRA Intranet, LAN and WAN
vi. Memory for Payroll Processing
vii. SCALA for Financial Accounting and Reporting

An auditor should be familiar with internationally recognised standards and guidelines on Information Systems such as Information Systems Audit and Control Association (ISACA) and International Organization for Standardization (ISO).

IS audit is similar in approach to Financial and Operational Audits in that it require adequate planning, audit organizations, assessment of overall risks and developments of an audit programme that consists of objectives and audit procedures that will satisfy the audit objectives.
852 Information Systems Control Areas

IS Security Controls
The Authority’s Security Policy should stipulate how the data, hardware and software should be made secure. The auditor needs to acquaint himself or herself with the International Standards that give the best practice for security management such as ISO 17799. In addition to security the auditor shall be required to ensure that the accountability of assets is kept up to date.

System access controls are fundamental in an information system and the auditor is required to ascertain the logical and physical system access controls. The most common logical system access exposures are Trojan horses, Salami techniques, virus, worms, logic bombs and trap doors. Further, mandatory and discretion access controls must be instituted to enforce the Authority’s security policy and rules.

The management’s privacy policy that takes into account considerations of the applicable privacy laws and regulations in Kenya and abroad is a fundamental area to consider in IS auditing.

Care should be taken to ascertain whether computer crimes and exposures/threats are adequately prevented and controls are put in place to counter such threats resulting from hackers/crackers, script kiddies, employees, IS personnel, end users, former employees, taxpayers and casual employees.

The auditor should familiarise himself or herself with the Authority’s information technology environment, the security layers, path of logical access, general points of entry, logical access controls in the operating systems, databases and/or application access controls. The methods of access controls include; identification and authentication processes, logon IDs and passwords, biometrics used and controls, access rules applied, remote access security controls and audit logging to monitor system access.

Encryption protects data in transit over the network from unauthorised interception and information stored on the computers from unauthorised viewing or copying. It is also used to deter and detect accidental or intentional alterations of data and verifies authenticity of a transaction or document received electronically. There are various methods of encryption of data
and the auditor needs to know and understand their use in the Authority. Some encryption methods are inbuilt in the software and others use key cryptographic systems. A message that has been encrypted twice, first by the sender’s secret key and secondly by the receiver’s public key achieves both authentication and confidentiality. Digital signatures are intended to verify the integrity of the message and confirm the identity of the sender.

The auditor should have knowledge and adequate tools to analyse the audit trail. Such tools include: audit reduction tools, trends/variance detection tools and attack signature detection tools. Cost consideration is paramount when deciding on the tools to use.

Anti-viruses are preventive control tools and the auditor should be familiar with the types, their implementation and effectiveness. The auditor should also confirm the procedures for updating anti-viruses.

Hardware and Software Configuration

Hardware relates to the technical and physical features of the computers. The auditor shall review the technical infrastructure documentation of the system, hardware components, processing and input and output components. Types of computers used and their common roles, and the types of appliances and their roles (firewalls, intrusion detection system, switches and routers). It is important to consider hardware acquisition procedures and ensure they are in line with laid down procurement procedures.

Hardware must be routinely cleaned and serviced to work effectively. The auditor should review hardware maintenance programme and also review downtime reports to ascertain their effectiveness.

Software relates to programs and supporting documentation that enable and facilitate use of the computer and controls the operation of the hardware. System software is a collection of computer programmes used in the design, processing and control of all computer applications used to operate and maintain the computer system and must be compatible with its operating system. Operating systems contain programmes that interface between the user, processor and application software. Application software contains programmes that perform the processing of records for a specific function. Database management system is a class of system software that
aids in organising, controlling and using data needed by application programs. The auditor shall review the logical paths of the programs in the Authority and their documentations.

In addition to the above the auditor shall audit the information systems network infrastructure, telecommunication links, types, network protocols and standards used in the Authority.

**Application Controls**
The objectives of application controls are to ensure the completeness, accuracy of the records and the validity of the entries made therein resulting from programmed processing.

The IS auditor tasks include the following:

i. Identifying the significant application components and flow of transaction through the system and gaining a detailed understanding of the application by reviewing available documentation and interviewing appropriate personnel

ii. Identifying the application control strengths, and evaluating the impact of the control weaknesses on the development of a testing strategy by analysing the accumulated information

iii. Testing the controls to ensure their functionality and effectiveness by applying appropriate audit procedures

iv. Evaluating the control environment to determine that control objectives were achieved through analysing the test results and audit evidence

v. Considering the operational aspects of the application to ensure its efficiency and effectiveness by comparing the system with efficiency programming standards, analysing procedures used and comparing them to management’s objectives for the system.

**Input, Processing and Output Controls**
Input control procedures must ensure that every transaction to be processed is received, processed and recorded accurately and completely. These controls include the following: input authorization, batch controls and balancing, error reporting and handling, and batch integrity in online or database systems.

Processing procedures and controls ensure the reliability of application program processing and include: data validation and editing procedures, processing controls that ensure the completeness
and accuracy of accumulated data, and data file control procedures that ensure that only authorised processing occurs to stored data.

Output controls provide assurance that the data delivered will be presented, formatted and delivered in a consistent and secure manner. This also includes report distribution. The auditor should be aware of existing controls in the application and should test this existence. This can be achieved with the help of the system administrator and users. Most controls are embedded and designed into the application that supports the processes. These controls may be a combination of management, programmed and manual controls.

Testing the effectiveness of application controls involves analysing computer application programmes; testing computer application programmes controls, or selecting and monitoring data processing transactions.

**Techniques for Analysing Computer Applications Programmes include:**

i. Recording the flow of designated transactions through logic paths within the programmes, called snapshot

ii. Identifying specific programme logic that has not been tested and analysing programs during execution to indicate whether program statements have been executed, this is called mapping

iii. Tracing shows the trail of instructions executed during an application. Tagging involves placing an indicator on selected transactions at input and using tracing to track them (Tracing and Tagging)

The above techniques require knowledge in application program and programming.

**Techniques for Testing Computer Application Controls include:**

i. Test data/desk where simulated transactions are applied through a real programme

ii. Base case system evaluation – uses test data sets developed as part of comprehensive testing of programmes

iii. Parallel operations – Actual production data is processed through both existing and newly developed programmes at the same time and results are compared. It is used to verify changed production prior to replacing existing procedures

iv. Integrated testing facility – creates a fictitious file in the database with test transactions processed simultaneously with live data.
v. Parallel simulation – production data is processed using computer programmes that simulate application programme logic
vi. Transaction selection programmes – use audit software to screen and select transactions input to the regular production cycle.

Techniques for Selecting and Monitoring Data Process Transactions include:

i. Embedded audit data collection where a software embedded in host computer applications screens and selects both input and generated transactions during production, such as system control audit review file or sample audit review file.

ii. Extended records – gathers all data that have been affected by a particular program.

To facilitate the evaluation of application system tests, the auditors may use Computer Assisted Audit Tools and Techniques (CAATTs)

Computer Assisted Audit Tools and Techniques (CAATTs)
CAATTs are important tools for the auditor in gathering, analysing and manipulating data. It enables an auditor in performing audits to gather information independently. The reliability of the source of the information used provides a reassurance on findings generated.

CAATTs include many types of tools and techniques, such as generalized audit software, utility software, test data, application software, tracing and mapping, and expert systems.

The auditor, in liaison with the ICT Department, shall obtain the soft data for audit from the relevant parties. Generalised audit software refers to standard software that has the capacity to directly read and access data from various database platforms, flat files systems and ASCII formats, Examples are Audit Command Language (ACL) and Integrated Data Extraction and Analysis (IDEA).

Business Continuity and Disaster Recovery Plan
The purpose of the business continuity/disaster recovery is to enable a business to continue operations in the event of a disruption and to survive a disastrous interruption to their information systems. The auditor’s task among others include understanding and evaluating business continuity strategy, its effectiveness, adequacy and its connection to business objectives
Programmes Development (In-house Business Application)

The Authority commits significant resources to develop, acquire and maintain application systems that are critical to the effective functioning of key business processes. Software development must be approached in a systematic and sequential manner. It begins with a feasibility study and progresses through requirements definition, design, development, implementation and post implementation. The series of steps or phases have defined goals and activities to perform with assigned responsibilities, expected outcomes and target completion dates.

The auditor’s task is to monitor the system development process to ensure that controls are implemented, users and business requirements are met, and the best methodologies are being followed.

Configuration management system provides control over programming maintenance activities and involves procedures that identify, defines and base line software items in the system. Since software is subject to ongoing changes during and after development, identification of the items that are likely to change is crucial.

Users of the system convey system change requests to the system management using some type of formal correspondences. All requests for changes and related information should be maintained by the system maintenance staff as part of the system’s permanent documentation. The auditor should review the overall change management process. Library control software can be used to separate test from production libraries to ensure that all program changes are authorised.

860 Project Management Audit

The auditor shall ensure that there is a clear project management process and major deliverables are defined. The following are possible stages and activities in a project management process:

861 Project Definition

At this stage the auditor will ensure that the following activities are properly and adequately done.

i. Defining of the scope and ensuring that the stakeholders have a common understanding of the project
ii. Developing the management plan and defining of the project objectives, scope, benefits, and risks. This should give the project implementation approach, high level estimates, resources, infrastructure plan and the project control approach.

iii. Developing the project organisation stating the project sponsor, steering committee and management team in addition to their roles and responsibilities defined

iv. Managing the subcontracts if any include defining work product, time frame and monitoring of work carefully

v. Defining the approach to organisation change. This will involve identifying the key change control role and managing change using a collaborative approach

vi. Developing project communication plans, that is, defining frequency, timing and purpose of meetings and information to be communicated

vii. Developing project control procedures that include: quality management procedures, risk and issue management procedures, configuration management procedures, control and reporting procedures, detailed work planning methodology and administrative handbook.

862 Project Plan

The auditor shall ensure that the work plan includes the following activities:

i. Documentation of objectives, scope and assumptions

ii. Determine tasks dependencies and estimate efforts of each task

iii. Identify support, overhead and contingency tasks and assign specific resources

iv. Formal agreement and base line work plan

v. Undertaking communication and training.

863 Project Management and Control

The auditor shall audit the major deliverables in this stage, which are: progress reports, updating of the detailed work plans and management plans, cost schedules and performance reports generated at this stage. The main activities the auditor shall be concerned with at this stage are:

i. Management of quality, risk, issues, change controls and configuration

ii. Management of critical activities and achievement of set project objectives

iii. Management of project staff, subcontractors, organisation change and expectations.

864 Close of Project

The auditor shall review the major activities in this stage, which include:

i. Review and update management plan
ii. Development of detailed work plan for closing
iii. Closing of contracts with subcontractors
iv. Assessment of project performance and documentation of lessons learnt
v. Conducting of final performance reviews
vi. Documentation and archival of project deliverables, disposal of project infrastructure
vii. Disbanding of project organisation and formal close of the project.
viii. Commissioning of projects and handing over

865 Post Implementation Review
At this stage, the auditor will review the planning and conduct of post implementation review and performance of agreed actions.

866 Staff IT literacy audit
The auditor will assess the staff IT literacy levels with a view of ensuring that staff are adequately trained to handle the operations and that staff are not placed in the wrong areas e.g. programmers being allowed to handle the business processes.
CHAPTER NINE

900 REPORTING AND FOLLOW-UP

910 Introduction

The Department maintains a formal process for communicating to the Board and the management the results and recommendations for all audits conducted. Our principal product is the final report in which we express our opinions about the audit findings and discuss our recommendations for improvements. Therefore, in order for the Department to be effective, the reports clearly and persuasively convey the results of the audits to enable readers to recognise the validity of the findings and the benefit of implementing any recommendations. It is therefore important to structure the report to emphasise the most important findings.

920 Structure of the Report

The audit report should inform the management and other potential users of the performance of a function or an area. A logical assembly of the contents will give the reader a clear and complete understanding of the information being presented. The minimum required details for an audit report are described below:

Audit Report Numbering – The audit report number will be allocated after the head of internal audit has reviewed the report. The audit report number will appear on the cover page after the title and on the right hand footer on all pages of the report. It will also appear on the forwarding memo after the title of the audit report. An automated register of the audit report numbers will be maintained at the Deputy Head of Internal Audit’s office. The format of the report number will be; IAD/Unit or Department/Year/Serial number.

Forwarding Memo - This is the covering letter signed by the Head of Internal Audit and used to send the audit report to the management.

Title Page – This describes the business process audited, logo of the Authority, date of dispatch, origin and the department audited.

Table of Contents - This is on line of topics/contents in the report with their corresponding page numbers.
Executive Summary - This part of the report consolidates the overall result, key findings, recommendations and management’s views (where applicable), in brief and concise paragraphs. It is important that this section is brief and that each individual point is numbered, ranked in order of importance and is representative of the body of the report.

Introduction - This outlines and defines the scope, purpose and period of the audit, review or special investigation. The nature and extent of work performed should be described and related activities not reviewed should be identified if necessary. Introduction will cover the following details described below:

i. BSC focus – This outlines the perspective, strategic objectives and initiative of the assignment.

ii. Background information - This briefly indicates the present position of the particular area/activity under review and provides any other information related to the audited area/activity. In addition, the status of the management’s actions on prior audit report findings, recommendations, and conclusions may be included in this section.

iii. Objectives of the audit - This states the purpose of the audit and should be simple and clearly stated. The reason for conducting the audit and what it is expected to achieve should be stated.

iv. Audit strategy - This describes the audit techniques used, such as interviewing, reviewing records, testing transactions, analytical auditing procedures, etc.

Audit Findings/Observations, Recommendations and Management Comment(s) - This section forms the main body of the report and provides the basis for the executive summary. Specific examples observed and visual aids such as diagrams may be appropriate to emphasise or summarise key findings. This states the areas of weaknesses noted, implications, specific examples, the corrective action required and the management comment.

Conclusions and Acknowledgements - The conclusion is a reasonably brief summation of the overall audit or review. The summary of findings and recommendations provides ample coverage of the report and for this reason the conclusion need only reflect the main points of the report. Normally, an acknowledgment will include a statement of appreciation from the audit staff for the cooperation and hospitality extended to them during the audit.

Appendices - These include all material necessary to support and prove audit findings and recommendations that would otherwise interrupt the flow of the report but would assist the reader. This can take the form of copies of documents, a summary or listing of audit results.
930 Audit Findings/Observations, Recommendation and Management Response

All audit findings must be documented in the Non-Conformity Forms (NCFs) in the working papers. Unfavourable findings will be summarised on the working papers whether or not they are to be included in the audit report. All findings shall be documented immediately by the auditor discovering the situation.

931 Stating Findings and Conclusions

Upon conclusion of the fieldwork, the auditor will summarise the audit findings, conclusions and recommendations necessary for preparation of the draft audit report. Each audit finding will have documented the following attributes:

Statement of Condition

The condition identifies the nature and extent of the find or unsatisfactory condition. It often answers the question: “what was wrong?” Normally, a clear and accurate statement of condition evolves from the auditor’s comparison or results with appropriate evaluation criteria.

Criteria

This attribute establishes the legitimacy of the finding by identifying the evaluation criteria and answers the question: “by what standards was it judged?” In financial and compliance audits, criteria could be accuracy, materiality, consistency or compliance with applicable accounting principles and legal or regulatory requirements.

Effect

This attribute identifies the real or potential impact of the condition and answers the question: “what effect did it have?” In operational audits, reductions in efficiency and economy or not attaining the programme objectives are appropriate measures of effect.

Cause

The fourth attribute identifies the underlying reasons for unsatisfactory conditions or findings and answers the question: “why did it happen?” If the condition has persisted for a long period of time or is intensifying, the contributing causes for these characteristics of the condition shall also be described.
Recommendations

The final attribute identifies suggested remedial action and answers the question: “what shall be done?” The relationship between the audit recommendation and the underlying cause of the condition shall be clear and logical. The recommendations in the audit report shall state precisely what needs to be changed or fixed. How the change will be made is the auditee’s responsibility. Unless benefits of taking the recommended action are obvious, they should be stated. The cost of implementing and maintaining recommendations shall be compared to risk. Recommendations shall be directed to an individual capable of taking action. For any recommendation made for the management, a finding would need to be identified within the body of the working paper.

932 Management Response

Upon the completion of the audit fieldwork, Non–Conformity Forms (NCFs) will be sent to the auditee immediately either as paper copy or electronically requesting the department’s written response to audit queries. The management is expected to respond on how report findings will be resolved and include an implementation timetable. In some cases, managers may choose to respond with a decision not to implement and to accept the risks associated with an audit finding. Returned NCFs will be recorded and summarised.

Written management responses to draft findings and recommendations are required within five working days from the date the findings are presented to management. The management responses should express explicit concurrence or non-concurrence on all elements of a finding (on the facts, conclusions, and recommendations) in a language clear and simple as possible with emphasis on improvement. A separate response will be provided for each finding. Electronic templates are encouraged.

Concurrence with a recommendation should be accompanied by specific actions that will be taken to implement it. If any disagreement responses are submitted, the department, upon request, will schedule and conduct a meeting with the auditee to discuss potential resolution. The Internal Audit Department may decline responses from the auditee that are incomplete or inadequately supported.

After fieldwork is completed and the management's comments on the discussion Audit Report at the exit meeting have been considered, an audit report is prepared. The report will normally be
issued with a request that the management provides written comments on implementation within two months from the date of the report.

**940 Report Timeliness**

Reports should be issued as soon as practical following the completion of the audit work. The Head of Internal Audit should establish the processes for ensuring the timely issuance of audit reports. Reports should be reviewed in draft form with the responsible Audit Supervisor on a timely basis following completion of audit work.

A management response should be obtained during fieldwork or within one week after completion of fieldwork in order to ensure timely issuance of the final report. The audit report may be issued without the response in the event of undue delays by the management in submitting the responses.

**950 Qualities of good Internal Audit Reports**

The following are qualities of a good report:

i. **Objective:** Objective reports are factual, unbiased, and free from distortion. Findings, conclusions, and recommendations should be included without prejudice. If it is determined that a final audit report contains an error, the Head of Internal Audit should consider the need to issue an amended report which identifies the information being corrected. The amended report should be distributed to all individuals who received the audit report being corrected. An “error” is defined as an unintentional misstatement or omission of significant information in a final audit report.

ii. **Clear:** Clear reports are easily understood and logical; avoiding unnecessary technical language and providing sufficient supporting information can improve clarity.

iii. **Concise:** Concise reports are to the point and avoid unnecessary detail. They express thoughts completely in the fewest words possible.

iv. **Constructive:** Constructive reports are those which, as a result of their content and tone, help the auditee and the organization and lead to improvements where needed.

v. **Timely:** Timely reports are those that are issued without undue delay and enable prompt, effective action.
960 Distribution of the Reports

The audit report is issued to the management and to the Board. The CG’s approval is required for the release of reports outside the Authority. The Head of Internal Audit should review, approve, and sign the final audit report before issuance and should decide to whom the report will be distributed. A record of report distribution should be kept.

Audit reports should be distributed to those relevant officers who are able to ensure that audit results are given due consideration (i.e. those who are in a position to take corrective action or ensure that corrective action is taken). The final audit report should be distributed to the officer in charge of the unit. Certain information may not be appropriate for disclosure to all report recipients because it is privileged, proprietary, or related to improper or illegal acts. Such information, however, may be disclosed in a separate report.

If auditors discover weaknesses that may be symptoms of general themes across the Authority, this should be reported promptly to the appropriate level of management. The aim is to ensure that action to rectify the problem is taken promptly before auditors review individual systems at each department.

There may be circumstances when auditors should provide additional written or oral reports. For example, if particularly significant/material findings are made during the audit, especially if they involve suspected fraud/irregularity, these should be reported immediately to senior officers and, through the Head of the Internal Audit, to the Commissioner General.

970 Report Security and Confidentiality

Attention to the security of all audit reports is the responsibility of each auditor. Care should be taken to ensure that reports are stored in a locked file cabinet as directed.

Although the Department’s reports are exclusively for the use of the Authority’s management, certain reports especially investigative audit reports will contain information that should not be disclosed to unauthorised persons. Audit reports will be classified as confidential if they meet the following criteria:

i. Report discloses a weakness (potentially resulting in a loss) which has not been corrected at the time of distribution
ii. Report discloses sensitive information, which could prove an embarrassment to the Authority (if made public)
iii. Report discloses information classified as "restricted data"
iv. At the discretion of the Head of Internal Audit.
v. Audit reports classified as confidential will be marked with the words “CONFIDENTIAL REPORT” on the title page and the footnote. Soft copies of confidential audit reports shall be password protected and access shall be limited to authorised personnel only.

980 Implementation of Audit Recommendations

It is the responsibility of the management to ensure that appropriate action has been taken on reported audit recommendations and that such action is achieving the desired results, or that the management has assumed the risk of not taking corrective action on reported findings. Implicit in the management’s response to audit recommendations is the responsibility to ensure that all actions, activities and functions are conducted within the established Authority’s policies and procedures. Implementation of audit recommendations is determined through follow-ups after a period of two months from the date of issuance of the audit report. The role of follow up of implementation of audit recommendations is vested with the Operations Unit in the Office of the Commissioner General.

990 Follow-ups

Follow-up is defined as a process by which auditors determine the adequacy, effectiveness, and timeliness of actions taken by the management on reported audit issues/findings/observations and recommendations/action plans, including those made by external auditors and others.

The Head of Internal Audit is responsible for assessing that corrective action has been taken and is achieving the desired results or that senior management has assumed the risk of not taking corrective action on reported issues. The matters raised in the audit reports are followed up during the next visit to the area unless there is a specific need for interim follow-up. When a follow-up audit is conducted, a separate report is to be prepared and issued in conjunction with the report for the current audit.

Where a response to an audit report is not received within three months, a follow-up letter is sent to the auditee. If a response is not received, the matter is reported to the Audit Committee. The
nature, timing, and extent of follow-up will be determined by the Head of Internal Audit. Factors that will be considered in determining appropriate follow-up procedures are:

i. The significance of the reported issue or recommendation (certain issues may be so significant as to require immediate action by the management and may require monitoring, until corrected, because of the effect they may have on the organisation)

ii. The degree of effort and cost needed to correct the reported condition

iii. The impacts that occur should the corrective action fail

iv. The complexity of the corrective action

v. The time period involved

vi. There may be instances where the management’s oral or written responses shows that action already taken is sufficient when weighed against the relative importance of the audit issue or recommendation, and in these instances, follow – up may be performed as part of the next audit.

Follow-up activities will be considered and incorporated as part of the Department’s annual audit plan. The inclusion of follow-up activities in the plan will be based on the risk and exposure involved and also, the timeframe indicated by the management to correct the reported issue/observation and recommendation.

The Head of Internal Audit is responsible for establishing a process for follow-up. In this connection, the following elements will be included as part of the Department’s follow – up process, as appropriate:

i. A timeframe within which the management’s response to the audit issues and recommendation is required

ii. An evaluation of the management’s response

iii. A verification of the response

iv. A follow-up audit

v. A reporting procedure that identifies unsatisfactory response/actions, including the assumption of risk, to the appropriate levels of management

The techniques to be used to effectively monitor progress are:

i. Addressing audit issues and recommendations to the appropriate levels of the management for corrective action
ii. Receiving and evaluating responses to audit issues and recommendations during the audit or within a reasonable time period after the report is issued

iii. Receiving periodic updates from management in order to evaluate the status of the management’s efforts at correcting previously reported conditions

iv. Receiving and evaluating information from other organisational units assigned responsibility for procedures of a follow-up nature

v. Reporting to senior management or the Board on the status of responses to audit issues and recommendations.

Unresolved findings will also appear in the follow-up report and will include a brief description of the finding, the original audit recommendation, the auditee response, the current condition, and the continued exposure of the Authority. The follow-up review results will be circulated to the original report recipients and other officials as deemed appropriate.
CHAPTER TEN

1000 ADMINISTRATIVE PROCEDURES

1010 Performance Evaluations

Performance evaluation shall be based on the performance contracts signed with Management. Performance evaluation of staff should take account of the time budget, quality of work and attitude towards work. It is vital that officers keep track of and manage their time. Officers shall complete the time variance schedule upon completion of an audit assignment and hand it over to the audit supervisor. A copy shall be filed at the appropriate section of the file.

The Head of Internal Audit or the Audit Manager should do quarterly reviews and prepare a documented evaluation of the auditor’s performance. Strengths and weaknesses should be noted and be supported by specific instances. In this way, the auditor should receive the most objective assessment and at the same time focus on specific areas for improvement.

The evaluation will be based on the officer’s overall performance and the quality of the work that was accomplished. Some of the items considered when making the evaluation for auditors are:

   i. The ability to identify and raise quality issues in an audit
   ii. Good and well reasoned audit recommendations
   iii. Audit completion dates versus the promised completion dates
   iv. Deportment
   v. Communication skills
   vi. Report writing skills.

If the evaluator identifies weaknesses, an action plan shall be developed to assist in making the necessary improvements to achieve a satisfactory level of performance. Training needs shall also be identified to address areas to be strengthened.

Standard Workday

The Authority’s working hours are from 8.00 a.m. to 5.00 p.m. with a one hour lunch break. However, due to pressure and urgency of some assignments, staff members may be called upon to work extra hours to complete urgent assignments on time. While working in the field, working hours should conform to those of the station being audited.
Attendance Register
As per the Authority’s policy, all staff (KRA grade 8 and below) must sign in and out on the time sheets provided on all working days. When leaving the office for more than fifteen (15) minutes, staff members shall request for permission from the immediate supervisor/unit head or Head of Internal Audit.

Absenteeism
Those individuals absent due to sickness or other reasons not cleared in advance should telephone the office within the shortest time possible and explain the reason.

Annual/Maternity Leave
This will be in accordance with the Authority’s annual/maternity leave policy. However, due to the work arrangements and some unforeseen circumstances, staff members’ annual leave may be delayed to enable conclusion of urgent/emergency assignments. For this purpose, the staff members shall be informed in advance of the intended delay.

1020 Storage and Security of soft and hard copies of the Audit Reports
Audit files include audit working paper files and general office files, manual or automated, which contains memos and general correspondences. These shall be reviewed on an annual basis and be purged as per the Authority’s record retention policy.

Auditors should remember that desktop Windows “passwords” provide no security over any data on the computer should physical security in the office be compromised. Highly confidential data should be saved directly to a removable media.

To provide physical security over the data and computing resources, the locks at the entrances to the office should be secured when the office is unattended. Sensitive data on removable storage media and hard copies of sensitive data should be locked appropriately, secured and properly destroyed when disposed off. Audit reports shall only be accessible to authorised individual (s).

Auditors are responsible for maintaining backups of their desktop files on separate media. Auditors may wish to back up non-sensitive data to the ‘audit’ folders on the shared drive on the Authority’s server, relative to the need for security of the files.
For fraud investigation, the level of security goes a notch higher since the degree of confidentiality required is quite high. All information concerning allegation(s) of fraud must be protected and kept confidential by all auditors.

Hard copies of the audit report shall be kept by the Head of Internal Audit, the Deputy Head of Internal Audit and the Secretary to the Head of Internal Audit. A copy of the report shall be filed in the audit file. This will ensure that in case of loss of any copy of the report, a copy can be obtained from other sources. This is in addition to the soft copy which shall be kept on the floppy disk/flash disk. A soft copy of the report shall also be kept under a separate log maintained by the Head of Internal Audit in his/her personal computer. Every audit team leader shall maintain a folder in a designated computer for storage of audit reports and related correspondences.

**Record Keeping**

Each departmental unit has been allocated cabinets for filing of audit files. The files should be labelled to indicate the station or section audited, the date of report and the process audited. The arrangement of the files in the cabinet should be such as to ensure protection of the documents and ease of retrieval. The keys to the cabinets are under the custody of the Head of the Unit. Old files should be kept in the department’s archive.

**File Indexing**

The Department has a file index for all files which is maintained by the secretary to the Head of Internal Audit. File indexes are issued serially and should be communicated to all members of staff.

1030 **Office Facilities (Computers/Laptops, Telephones and E-mails)**

**Laptop and Desktop Computers**

Laptops assigned to staff are the responsibility of the staff person until returned. Staff members will be required to sign in the register for the laptop borrowed.

The following procedures should be followed when using and storing laptop computers:

i. Laptops should be transported in their protective carrying cases at all times

ii. Laptops should be protected from temperature extremes, precipitation (rain and direct sunlight) and dampness

iii. Staff members should refrain from placing drinks or foods near laptops and in places where spills could cause damage to the laptop
iv. Staff members should note that insurance cover has been purchased for the office’s laptops. However, the coverage provides only reduced, or no coverage in the following instances:
   • Theft, vandalism or pilferage of a laptop
   • Disappearance of a laptop (i.e. a laptop turns missing during the performance of a physical inventory, or vanishes without any signs of a break in)
   • Damage caused by insects, vermin, corrosion, rust, dampness, dryness, freezing or extremes of temperature
   • Damage caused by rough handling.

v. The laptops are provided with all the necessary software. Do not download any software to the laptop, or install any software to the laptop without the approval of the Head of Internal Audit

vi. Laptops should be secured when not in use

vii. A designated member of staff will be responsible for the safeguarding of and accountability for any laptops not assigned to a particular staff member

viii. Doors to offices with laptops should be locked over lunch hours or any other time the auditor is away from his working area (e.g. while interviewing auditees)

ix. A sign-out sheet/register must be filled out before removing the laptop from the storage area.

Software Licenses
The Head of Internal Audit will be responsible for the acquisition of software licenses in liaison with ICT department. Renewals of the licenses shall also be monitored by the Head of the Department who will also be in charge of storage.

Computer Protocol
Computer viruses: Staff members should be aware of the seriousness of the threat posed by computer viruses. To make sure that computers are not infected with viruses or transmit viruses, all diskettes received from outside the office should be scanned. Diskettes that are sent out of the office should also be scanned for viruses prior to sending. Be careful with files that are downloaded from other systems especially programme files. Antivirus software shall be installed on all computers and auditors should be familiar with its use.

Passwords: Passwords should be easy to remember, difficult to guess and should not be given to others (at least others outside the office). It is required that periodically, passwords be changed.
Software piracy: The Department shall not tolerate software that has been pirated. All software used in the Internal Audit Department should be acquired legally and registered.

**Telephone Usage**

When answering the telephone within the office state: “Internal Audit” and identify yourself by name. Always request the telephone number of the party calling, even if they indicate they will call back. Phones should be answered within three (3) rings. If the incoming call is for an auditor who is out of the office, a message will be taken and given to the auditor when they return.

Auditors should check for telephone messages each time they return to the office. It is an offence to use telephone in the offices for private business unless in exceptional circumstances as stated in the Code of Conduct. Official telephone conversation with the auditee must be adequately recorded and filed. This will form part of audit workings.

**E-Mail**

The Department supports the use of e-mail to assist in communication with auditees and other related parties. In order to efficiently use the office’s computer resources, the auditors shall adhere to the following rules regarding the retention of e-mail:

i. When e-mail is used as part of an audit assignment and is to be included in the working papers, it should be printed out and filed

ii. If the communication is not to be included in working papers, it should be deleted from the e-mail system once the matters covered by the e-mail have been resolved.

**Internet/intranet Audit Tools**

Members of staff are expected to uphold high discipline and integrity while using the internet/intranet facility. Staff members are allowed to surf the Internet for information related to their field. Members are not allowed to surf undesirable sites during working hours.

**1040 Communication within and outside the Authority**

The communication shall be in accordance with the Authority’s Code of Conduct. The relevant clauses are reproduced below.

i. The chain of command shall be respected at all times when communicating internally and externally
ii. Staff shall not intrude into the privacy of another staff member’s life so long as such matters do not affect the member’s performance.

iii. Phone tapping or eavesdropping on telephones or any other communication media is strictly prohibited as this constitutes invasion of an individual’s privacy.

iv. Staff shall not give information to unauthorised parties in response to requests for information on technical subjects related to the duties and activities of their departments.

v. Staff shall not, under any circumstances, communicate with the mass media either in writing or by granting an interview and making statements on matters affecting the Authority’s programmes or policies without the prior approval of the Commissioner General.

vi. Staff, whether on duty or on leave of absence, should not allow themselves to be interviewed on questions of public policy affecting Kenya or any other country without the permission of the Commissioner General.

vii. Staff members who have access to confidential matters in the course of their duties have an obligation to keep such matters strictly confidential.

1050 Standardised Audit Forms

Several forms shall be used during the audit process. The various forms approved for use in Internal Audit include:

i. Non conformity forms (NCFs)

ii. Records/documents request form

iii. Working papers (different columns)

iv. Analysis forms (14 column)

The use of these forms ensures proper communication and documentation of workings. They also promote uniformity in recording. Refer to volume II for detailed samples of working papers. These forms are subject to change and will only be amended after approval has been given by the Head of Internal Audit.
1060 General Matters

Information Security
Security of information in Internal Audit should be in line with the Authority’s information security policy. The following security guidelines should be followed to ensure information security in the Department.

Restricted information: All information reviewed in the course of an audit and information that auditors have access to should be considered strictly confidential.

Working papers: Upon completion of the audit, working papers should be maintained in locked file cabinets within the Department. Access to audit files shall be granted to individuals representing outside audit interests only by the Head of Internal Audit. However, files should not leave the Internal Audit office.

Data ownership: All data kept on the office of the Department’s computers should pertain to the Authority and related professional duties of the auditor. As such, these files are considered the property of Internal Audit, rather than the property of the individual who has created them. All files, whether paper, electronic or fiche may need to be accessed from time to time. It is the policy of the Department that such information will be freely accessible to those who need it. Passwords on official documents should be communicated to the Head of Internal Audit in a sealed envelope that can be opened when there is need to access or print the files for official use. As stated elsewhere in this manual, sensitive information require a password to limit access.

These standards are designed to allow efficient access to information by those who have a reason to use it as well as to protect the integrity of the original files.

No Smoking Policy
The office of internal audit has adopted a no-smoking policy.

Dress and Deportment
Auditors are expected to conduct themselves in a professional manner in both dress and deportment. Auditors should be smartly dressed and should carry themselves with dignity.
1070 Internal Audit Meetings

The Department shall hold quarterly audit staff meetings. The meetings shall be scheduled and called by the Head of Internal Audit in consultation with the Secretary (who shall be appointed annually on rotational basis). At the meeting, audit assignments shall be discussed and any other problem encountered by auditors in the course of their work. The minutes of such meetings shall be recorded and confirmed at the next meeting. All members of staff shall receive a copy of the minutes.

1080 Decision Making Procedures in Internal Audit

To enhance the efficient running of the Department, there is need to have a clear communication system. The following decision making procedures shall be followed:

i. The Head of Internal Audit shall constitute an internal committee in which all Unit Heads will be members

ii. The Head of Internal Audit shall be the chairman to this committee which shall hold meetings on need basis

iii. The committee will deliberate on issues relating to administration, operations and functions of the department.

The final authority however is vested on the Head of Internal Audit. The Unit Head shall also hold meetings with their unit staff regularly to communicate decisions made in such meetings.