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DIIR

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April 29, 2016

Exposure Draft: Proposed Changes to the Standards (IIASB) (February 1, 2016)

Dear Sirs and Madams,

We welcome and thank you for the opportunity to comment on the proposed changes to the International Standards for the Professional Practice of Internal Auditing (*Standards*).

While we know that many of our members are submitting their responses to the exposure draft by completing the survey questions provided by the IIA, we as the professional body of the Internal Auditors in Germany would like to supplement their input by submitting this comment letter.

General Remarks

In general, we support the objective of the International Internal Audit Standards Board (IIASB) to meet the challenges of today's evolving business environment by proposing changes to the *Standards*.

We also share the view of the IIASB expressed in the exposure draft that changes to the *Standards* were necessary as a result of the July 2015 changes to the International Professional Practice Framework (IPPF), such as the addition of Core Principles.

With respect to individual proposed changes to the *Standards*, we would like to submit the following comments:

Mitglied des
Institute of Internal
Auditors (IIA), Inc.

Mitglied der
European Confederation
of Institutes of Internal
Auditing (ECIIA)

Mitglied im
Wuppertaler Kreis e.V. –
Bundesverband betriebliche
Weiterbildung

Specific Remarks

Section “1. Change the Introduction of the Standards”

Use of the terms “internal audit activities”, “internal auditing activities” and “internal audit services”

In this section, the terms “internal audit activities”, “internal auditing activities” and “internal audit services” are used with a different meaning. In our view, this could result in confusion and therefore, we suggest to clarify the use of the terms.

The term “internal audit activity” is defined in the Glossary to the IPPF as:

“A department, division, team of consultants, or other practitioner(s) that provides independent, objective assurance and consulting services designed to add value and improve an organization’s operation. (...)”

Consequently, we agree with the following proposed changes to the introduction of the *Standards* and agree that the use of the term “internal audit activities” in plural is appropriate considering the definition of the Glossary:

Introduction to the ~~International~~ Standards

Internal auditing is conducted in diverse legal and cultural environments; within organizations that vary in purpose, size, complexity, and structure; and by persons within or outside the organization. While differences may affect the practice of internal auditing in each environment, conformance with *The IIA’s International Standards for the Professional Practice of Internal Auditing (Standards)* is essential in meeting the responsibilities of internal auditors and ~~the~~ internal audit ~~activity~~ **activities**.

However, the use of the term “Internal auditing activities” as proposed in the following paragraph seems to have a different meaning than the term “internal audit activity” as defined in the Glossary:

The purpose of the *Standards* is to:

- ~~1. Delineate basic principles that represent the practice of internal auditing.~~
1. Provide a framework for performing and promoting a broad range of value-added internal auditing **activities**.

In our understanding, “internal auditing activities” as used in this paragraph has the same meaning as the term “internal audit services” as used in a later paragraph of the introduction:

which the performance of these services can be measured. The Attribute and Performance Standards ~~are also provided to~~ apply to all internal audit services.

We therefore ask the IASB to consider replacing the term “internal auditing activities” with the term “internal audit services”.

Use of the term “Standards” in singular

Although the term “Standards” implies plural, the exposure draft proposes to use the term “Standards” in singular which results e.g. in the combination of the term “Standards” with “is” (rather than “are”):

The *Standards* is a set of ~~are~~ principles-based, ~~principles-focused~~, mandatory requirements consisting of:

As non-native speakers this wording is confusing. Also, in a German translation it will not be possible to copy this change to the *Standards*, i.e. we would have to continue to use “Standards” in connection with the German “are” (“sind”).

Therefore, we would ask the IASB to reconsider the proposed change.

Completeness of mandatory elements

The following change is proposed with respect to the conformance with mandatory elements of the IPPF:

The *Standards*, together with the Code of Ethics, encompass mandatory elements of the International Professional Practices Framework (IPPF); therefore, conformance with the *Standards* and Code of Ethics indicates conformance with mandatory elements of the IPPF.

In our view, this paragraph could imply that the mandatory elements comprise of the *Standards* and the Code of Ethics only. We suggest to also refer to the Definition and the Core Principles in order to have a complete listing of all mandatory elements.

Alternatively, we propose the following wording, implying that the conformance with the *Standards* and the Code of Ethics also results in compliance with the Definition and the Core Principle (as the rationale in section “8. Change to Standard 1300” suggests) (proposed adjustments are highlighted in yellow):

“The *Standards*, together with **the Definition, the Core Principles and** the Code of Ethics, encompass **the** mandatory elements of the International Professional Practices Framework (IPPF); **therefore, as the Definition and the Core Principles are embodied in the Standards,** conformance with the *Standards* and Code of Ethics indicates conformance with **the** mandatory elements of the IPPF”.

Section “5. Addition of New Standard 1112”

The exposure draft proposes the addition of the following standard:

1112 Chief Audit Executive Roles Beyond Internal Auditing

Where the chief audit executive has or is expected to have roles and/or responsibilities that fall outside of internal auditing, safeguards must be in place to limit impairments to independence or objectivity.

We agree that additional roles and/or responsibilities that fall outside of internal auditing (e.g., roles related to the second line of defense) do not necessarily impair the independence or objectivity of a CAE of the internal audit activity as required by the Code of Ethics and the *Standards* when appropriate safeguards are in place. Therefore, in principle we agree with the addition of the new standard 1112 as proposed.

In our view, however, the proposed new standard needs clarification of the nature of safeguards to be implemented and the level to which impairment of independence or objectivity does have to be limited to be acceptable. We acknowledge that in the past guidance has been issued by the IIA that addresses situations where the CAE may have assumed additional second line of defense responsibilities (e.g., Practice Guide “Internal Audit and the Second Line of Defense”, Practice Guide “Assisting Small Internal Audit Activities in Implementing the International Standards for the Professional Practice of Internal Auditing”). However, considering the addition of the new standard 1112, we suggest to issue Implementation Guidance that is specifically related to this standard and that gives guidance on the nature of appropriate safeguards and the level of impairment of independence or objectivity that may be acceptable under the *Standards*.

Section “10. Change to Standard 1312”

The exposure draft proposes the following change to the interpretation of standard 1312 External Assessments:

Interpretation:

External assessments enhance a complete quality assurance and improvement program and may be accomplished through ~~can be in the form of~~ a full external assessment, or a self-assessment with independent external validation. The external assessor must conclude as to conformance with the Standards; the external assessment may also include operational or strategic comments.

It is our understanding that an external assessment also includes the conformance of the internal audit activity with the Code of Ethics. We therefore suggest the following addition (highlighted in yellow):

“The external assessor must conclude as to conformance with the *Standards* and the Code of Ethics;...”

Section “19. Change to Standard 2100”

The exposure draft proposes changes to standard 2100 – Nature of Work including a reference to the new Core Principles that the internal audit activity needs to be “insightful”:

2100 – Nature of Work

The internal audit activity must evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic, ~~and~~ disciplined, ~~and~~ risk-based approach.

Internal audit credibility and value are enhanced when auditors are proactive and their evaluations offer new insights and consider future impact.

As already recommended in our comment letter dated October 29, 2014, to the exposure draft “Proposed Enhancements to the Institute of Internal Auditors International Professional Practices Framework (IPPF) (August 4, 2014), we strongly believe that, in order to support the internal audit practice and to help manage expectations with stakeholders, additional guidance should be developed and provided by the IIA on how “insight” and “insightful”, respectively, are defined and how this can be delivered.

Section “30. Change to Definition of Board”

The exposure draft includes an amended definition of the term “board”:

The highest level of governing body charged with the responsibility to direct and/or oversee the activities and hold senior management of the organization. Typically, this includes an independent group of directors accountable (e.g., a board of directors, a supervisory board, or a board of governors or trustees). If such a group does not exist, the “board” may refer to the head of the organization. “Board” may refer to an audit committee to which the governing body has delegated certain functions. Although governance arrangements vary among jurisdictions and sectors, typically the board includes members who are not part of management and is not solely comprised of members of management. If a board does not exist, the word “board” in the Standards refers to a group or person charged with governance. Furthermore, “board” in the Standards may refer to a committee or another body to which the governing body has delegated certain functions (e.g. an audit committee or risk committee).

We strongly believe that the use of the terms „board“ and „senior management“ in the Standards need to be clarified.

Under the current Standards and definition, it can be argued that the terms “board” and “senior management”

- a) either refer to two completely separate groups of people,
- b) or refer to two separate groups where one group (senior management) is a subset of the other group (board).

The proposed new definition seems to suggest that “board” and “senior management” are two completely separate groups of people:

*“The highest level of governing body charged with the responsibility to direct and/or oversee the activities **and hold senior management accountable** (e.g., a board of directors, a supervisory board, or a board of governors or trustees)”*

According to this definition, there is a “board” that directs and/or oversees, and there is a “senior management” that is held accountable by the “board” (i.e., two different groups of persons with different responsibilities).

However, under this view it seems to be unclear why certain actions and responsibilities with respect to the internal audit activity would be assigned to a level of management that is below the board level executives (such as approval of the audit charter by senior management and the board (1000), communicating the results of the quality assurance and improvement program to senior management and board (1320) or communicating the internal audit activity’s plans to senior management and the board for review and approval (2020)).

Therefore, in our view there is the possibility that regardless of the respective governance system in a territory (one-tier or two-tier board system)

- a) users of the *Standards* may have a different understanding of
 - i. the terms “board” and “senior management”, and
 - ii. what persons/groups and which levels of management the “senior management” is comprised of (i.e., executive directors and management board, respectively, or further levels of management)
- b) and hence, certain parts of the *Standards* that involve the terms “board” and “senior management” may not be applied consistently.

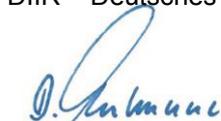
Therefore, we suggest to

- a) add a definition of the term “senior management” to the Glossary of the *Standards* and, under consideration of this new definition, clarify the definition of “board”,
- b) review and amend the *Standards* considering the clarified definitions of “board” and “senior management” as necessary in order to ensure a consistent understanding and application of the *Standards*, and
- c) develop guidance together with national institutes on how to apply the *Standards* with respect to the terms “board” and “senior management” in jurisdictions with a one-tier board system and two-tier board system, respectively.

We would be happy to discuss our views further with you. If you have any questions regarding this letter, please contact either one of us at d.mertmann@diir.de or c.scharr@diir.de.

Yours sincerely,

DIIR – Deutsches Institut für Interne Revision e.V.



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