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1. Definition of Internal Audit

Internal audit is the evaluation of management controls and operations performance, and the determination of the degree of compliance with laws, regulations, managerial policies, accountability measures, ethical standards and contractual obligations. It involves the appraisal of the plan of organization and all the coordinated methods and measures, in order to recommend courses of action on matters relating to operations and management control.

2. Legal Bases for Internal Audit

The establishment of the internal audit function is based on Philippine laws and statutes. The creation of the Internal Audit Service (IAS) was first mandated under Republic Act No. 3456 or the Internal Auditing Act of 1962, as amended by Republic Act No. 4177 followed by the series of chronological issuances on the creation of IAS, to wit:

- A. Administrative Code of 1987 or EO 292
- B. AO 278 & AO 70
- C. DBM Budget Circular 2004-4
- D. DBM-CSC Joint Resolution No. 1, series of 2006
- E. DBM Circular Letter No. 2008-5
- F. DBM Circular Letter No. 2008-8


3. Scope of Internal Audit

3.1 Scope

- Internal audit is an integral part of the internal control system of public service organizations. The scope of internal audit is broad and involves all matters relating to operations and management control.
- Among others, internal audit encompasses the appraisal of the adequacy of internal controls, the conduct of management audit and the evaluation of the results of operations, focusing on the effectiveness of controls of operating systems and support services units/systems.

3.2 Functions of IAS

- Pursuant to the Administrative Code of 1987, and as reiterated in the National Guidelines on Internal Control Systems, the functions of the Internal Audit Services are as follows:

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- A. Advise the Management through the Audit Committee on all matters relating to management control and operations audit;
- B. Conduct management and operations audits, programs, projects, activities with outputs, and determine the degree of compliance with their mandate, policies, government regulations, established objectives, systems and procedures/processes and contractual obligations;
- C. Review and appraise systems and procedures, organizational structures, asset management practices, financial and management records, reports and performance standards of each of the company's units;
- D. Analyze and evaluate management deficiencies and assist top management by recommending realistic courses of action;
- E. Perform such other related duties and responsibilities as may be assigned or delegated by the Audit Committee in accordance with law.


4. Types of Audit

4.1 Compliance Audit

- It is the evaluation of the degree of compliance with laws, regulations and managerial policies and operating procedures in the company, including compliance with accountability measures, ethical standards and contractual obligations.

4.2 Management Audit

- It is a separate evaluation of the effectiveness of internal controls adapted in the operating and support services units/systems to determine whether they achieve the control objectives over a period of time or as of a specific date. It includes compliance audit.
- It is a review and appraisal of the systems and processes, organizational and staffing structures, operations and management practices, records, reports and performance standards of the company.

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- Control effectiveness refers to the achievement of control objectives. When these control objectives are achieved, it can be concluded that management controls are effective.
- Management audit should be distinguished from management review since the former's function is independent of the management.

4.3 Operations Audit

- It is a separate evaluation of the outcome, output, process, and input to determine whether government operations, programs and projects are effective, efficient, ethical and economical, including compliance with laws, regulations, managerial policies, accountability measures and contractual obligations.
- Work back approach is being used since the evaluation is based on results.


5. Principles and Standards of Internal Audit

5.1 Conflict of Interest

- The Internal Auditor should avoid conflict of interest at all times, thereby maintaining objectivity and impartiality and upholding public interest. He/she should maintain an impartial, unbiased attitude, characterized by integrity and an objective approach to work and be constantly conscious of and alert to factors which may give rise to conflict of interest.

5.2 Objectivity and Impartiality

- These are vital to the effectiveness of the internal audit function.
- Objectivity means an unbiased mental attitude and professionalism that allows an Internal Auditor to perform engagements with no quality compromises. Its principle imposes the obligation to be fair and intellectually honest.
- To be objective and impartial, the internal auditor shall at all times uphold public interest over and above personal interest.

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5.3 Professional Competence


- The Internal Auditor must maintain high standards of competence and professional integrity commensurate with his/her responsibilities and mandated functions. He/she should commit to the highest degree of professional competence, both in the technical and ethical sense, through empowerment and continuing self-development.

5.4 Authority and Confidentiality

- Based on the audit objectives and subject to compliance with the internal security policies of public service organizations, the Management should authorize Internal Auditor/s to have full, free and unrestricted access to all functions, premises, assets, personnel, records, and other documents and information that the Audit Committee considers necessary in undertaking internal audit activities.
- All records, documentation and information accessed in the course of undertaking internal audit activities are to be used solely for the conduct of these activities. The Internal Auditor should respect the confidentiality of information acquired in the course of performing the audit activities and should not use or disclose any such information without proper and specific authority, unless there is a legal or professional right or duty to disclose.
- Confidentiality is not only a matter of disclosure of information. It also requires that the Internal Auditor acquiring information in the course of the audit neither uses nor appears to use that information for personal advantage or for the advantage of the third party.
- The Audit Committee and the individual internal audit staff are responsible and accountable for maintaining the confidentiality of the information they receive during the course of audit.

5.5 Code of Conduct and Ethics

- As public servants, internal auditors are bound by the Code of Conduct and Ethical Standards for Public Officials and Employees in the performance of their functions.

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5.6 Hierarchy of Applicable Internal Auditing Standards and Practices


- The hierarchy in determining government internal auditing standards in the Philippine public sector, in the order of authority, is as follows:
 - A. Constitutional provisions;
 - B. Laws, rules, and regulations on public governance and accountability, and applicable jurisprudence;
 - C. Government policies, standards, guidelines, and regulatory issuances;
 - D. Standards and other issuances of intergovernmental organizations such as the United Nations' specialized committees and agencies;
 - E. Relevant or applicable standards and best practices in governance, accountability, and operations, both local and international, such as the International Organization for Standardization (ISO) and other officially recognized organizations and associations.

5.7 IAS Functions vis-à-vis Activities and Operations of Other Units

- The IAS should not participate in the activities and operations of another unit.
- The IAS is not responsible for or required to participate in procedures which are essentially part of regular operating activities or the primary responsibility of another unit in the organization. These include management and process improvement of operating and support services systems such as quality management, human resource management, and financial management, which are the responsibilities of the operating and support services units concerned.

5.8 Internal Audit in Government Not an Assurance and Consulting Activity (per PGIAM)

- Consulting activity is non-government service.
- Consulting activity is non-audit service.
- IAS in government is not an assurance service since the unit constitutes a separate component of internal control, the objective of which is to

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determine whether other internal controls are well designed and properly implemented.

- IAS does not undertake process or systems improvement. Instead, it conducts root cause analysis in cases where the controls are weak, and recommends courses of action (corrective or preventive measures) for top management to take.

5.9 Internal Audit Studies, Services, and Other Seminars by Private Persons or Firms

- The Administrative Code of 1987 specifies that no government agency shall enter into any contract with any private person or firm for services to undertake studies and services related to government auditing, including IAS, for a fee, seminars or workshops for government personnel on these topics, unless:
 - a. The proposed contract is first submitted to the Commission on Audit (COA) to enable it to determine if it has resources to undertake such studies or services; and;
 - b. COA shall have certified in writing its prior decision not to undertake such contract.