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CONCEPTUAL ISSUES OF INTERNAL AUDIT

Abstract: The characterization of internal audit and the scope of organizational functions are perceived differently by stakeholders. Formed much later than external auditing, internal auditing developed relatively quickly, and that too in several directions. Currently, the most common types of internal audit are operational audit, management audit and performance audit. Studies show that in practice, the listed types of internal audit overlap in their functions, which not only causes confusion among audit beneficiaries, but also takes additional resources from the organization.

The article clarifies the functions of operational, management and performance audit from the point of view of the beneficiaries. Operational audit pursues the identification of efficiency reserves in the implementation of various entrepreneurial functions, which are related to production, service provision. The task of management audit is to promote the functioning of the effective management system used in the organization. And the performance

audit is mainly related to the public sector organizations and aims not only to find out the reliability of the budgets of state finances, but also their effectiveness in terms of the expectations of the beneficiaries.

Therefore, the areas of operational, management, and performance auditing may intersect somewhere in organizations. And the smaller the scope of managerial, operational and performance audit functions, the more effective the organization of internal audit in organizations.

Keywords: internal audit, auditing standards, operational audit, performance audit, management audit, beneficiaries of audit

JEL classification: M40, M41

Research aim: to present ways of improving internal audit information provision.

Research novelty: from the beneficiaries decision-making point of view, managerial, operational and performance audit functions have been specified in the concept of internal audit.

Introduction

The requirement to form an internal audit is mainly related not so much to the assurance of information, but to the control functions of economic activity, with the aim of increasing the degree of efficiency of entrepreneurship. Consequently, the establishment of an internal audit institution is not at all an assessment of the reliability of the published financial statements, but rather an advisory and impartial opinion from an independent third party. In this regard, the business owner, shareholders and even the beneficiaries of public organizations feel the need to form internal structures that will function independently of the executive

management circles, will evaluate their work, will identify the weak points of entrepreneurship and will present recommendations for their elimination. However, at the same time, internal audit has its various manifestations in organizations. On the one hand, it reveals deficiencies in the implementation of specific functions (production, organizational) in the field of business, on the other hand, it helps to increase the efficiency of entrepreneurship management systems. And finally, in the public sector, internal audit pursues the evaluation of the performance of defined programs, both in terms of the fulfillment of budgets and the integrity of the intended results. And it turns out that in practice the internal audit is perceived differently by the beneficiaries, and gives rise to the clarification and interpretation of its functions.

Research Results

Internal audit experienced its development especially in the 80s of the last centuries, when the scope of functions of this structure was regulated. Subsequently, internal audit standards, internal auditors' codes of conduct, and internal audit implementation legislation came into force.

The internal audit operating in the organizations practically finds the edges of interactions with the external audit invited from outside. The regulation of such interactions is addressed by the international auditor standard 610 "Investigation of internal work", where it is stated that the role of internal audit is determined by the management of the organization and its objectives differ from the objectives of the external auditor, who is invited by organizations to present a conclusion on financial statements.

Therefore, the objectives of the internal audit functions change according to the requirements of the organization's management, and the main task of the external audit remains the same: to determine whether the published financial statements are free from material misstatements.

However, in achieving their respective objectives, the internal and external audit functions overlap to some extent, so some aspects of internal auditing may be useful in carrying out external audit procedures. At the same time, the international standard of external auditing emphasizes that the external auditor is responsible only for the expressed audit opinion and thus, does not reduce his responsibility at all when using internal audit work.

In this regard, internal audit standards are in practice along with external audit standards. Since 2011, the Republic of Armenia has had internal audit standards with the following groups:

- 1) characterizing standards (Attribute Standards).
- 2) operational standards (Performance Standards).
- 3) Implementation Standards.

Characteristic standards consider the main characteristic features of internal audit organizations and parties. Operational standards describe the nature of internal auditing and provide qualitative standards for evaluating internal audit activities.

While descriptive and operational standards apply to internal auditing in general, application standards apply to specific types of auditing activities. The applicable standards are different for different types of auditing activities. In particular, the applicable standards relate to audit assurance activities and consulting activities.

Operational auditing refers to the process of evaluating a company's operational performance, both day-to-day and over a wider time frame. It serves as a detailed overview of all internal departments and processes that make up business operations. While an external audit evaluates the reliability of financial statements, an operational audit examines how a company conducts its business with the goal of increasing the overall effectiveness of the business. Moreover, operational audits can be carried out by external specialists or an internal audit team.

The purpose of the operational audit is ultimately to identify reserves for increasing the efficiency of management. By auditing internal business policies and procedures, a company can identify problem areas and operate more efficiently. The results from the audit are most useful to the management team, who can consider these recommendations to streamline future processes. Let's present three of the main results of a successful operational audit:

- maximize entrepreneurial effectiveness by gaining a better understanding of how future policies and procedures can promote competitive business.

- identify and prevent risks as much as possible, as organizations face many operational risks, from health and safety issues to cyber threats.

- clear internal control system, examining each step of the operational process, delving deeper into the impact of any changes in internal control.

The auditor develops a report on their findings and includes recommendations for improvement. Depending on those recommendations, the auditor may also develop an implementation plan to help the company make the necessary changes. They discuss

these recommendations with the appropriate managers, ensuring that the management team accepts unfavorable findings and solutions. Organizational management may agree to follow all suggestions or discuss why some changes cannot be implemented.

After completing the operational audit, the auditor organizes a follow-up meeting with the relevant management team and staff, discussing the changes made in the processes and evaluating their results. They measure these results against the objectives set by the audit and determine whether they are meeting the stated objectives and making some progress towards them. Participants in public services and the wider non-profit sector regularly evaluate their activities in terms of the mission, goals and objectives for which they were created. In international practice, among such approaches and tools, performance audit (CA) is particularly important. In this regard, performance audit (CA) finds its active application in public sector organizations. A performance audit is an independent, impartial and reliable study that shows whether government initiatives, systems, operations, programs, activities or organizations are operating in accordance with the principles of economy, target effectiveness and cost effectiveness and whether or not there is room for improvement. The principles of economy, target efficiency and cost efficiency can be defined as follows. The principle of economy means minimizing the cost of resources, when the resources used must be available at the right time, in the right quantity and in the right quality, as well as at the best price. The principle of cost-effectiveness means getting the most out of available resources. This refers to the relationship between the resources used and the output in terms of quantity, quality and time. Target effectiveness relates to the achievement of defined

goals and the achievement of intended results. The main purpose of performance audit is to constructively promote economical, targeted and cost-effective management. It also promotes accountability and transparency. Performance auditing promotes accountability by helping those with management and supervisory authority improve performance. This is done by analyzing whether the decisions of the legislative and executive bodies are effectively developed and implemented from a goal and cost point of view, and whether the best combination of price and quality is provided to citizens and taxpayers. It does not question the goals and decisions of the legislator, but analyzes whether any gaps in laws, legal acts or any deficiencies related to their implementation hinder the realization of individual goals. A performance audit focuses on areas where it can create the most value for citizens and areas with the greatest potential for improvement. Performance auditing creates constructive incentives for responsible parties to take appropriate action.

Management audit is also a variety of internal audit and has been in use since the recent past. It does not aim to establish the credibility of the organizations' reports, but to identify weak links in management and improve management functions. A management audit is an analysis and assessment of the competencies and capabilities of a company's management to achieve corporate goals. It is aimed at an independent and systematic analysis and evaluation of the company's overall activity, considering the effectiveness of the company's management, functions and achievements. Therefore, a management audit assesses the extent to which an organization's management team is utilizing its strategic and tactical capabilities and resources.

A management audit also finds out whether the principles and policies formulated by the organization's management have been successfully implemented or not. It analyzes the causes of management inefficiency and non-fulfillment of objectives, presents suggestions for improvement, e.g. production, sales, purchasing, finance, human resources, administration, etc.

In fact, business owners hire management auditors who provide valuable suggestions to improve business performance, examine and evaluate the organization's management objectives and strategic policies, and judge whether planning and policies are being properly implemented. A management audit helps to increase profitability by making recommendations to maximize the efficient use of an organization's resources. Management audit also helps to coordinate management activities. identifies interrelationships between activities, assesses authority and responsibility, and provides valuable suggestions for improving coordination between activities and employees. In this case, the weak points of various levels of management are identified and valuable advice is given to the top management regarding various policies and further actions.

A management audit is a process that allows a company to determine the effectiveness of its current management team. It may include analyzing current department processes, reviewing team member leadership strategies, and reviewing performance and inventory reports. This can help a company understand how its management teams use available resources and implement strategies to achieve organizational goals. A management audit focuses on the performance of the management team as a whole rather than auditing individual management team members.

A management audit is a systematic study of management decisions and actions to analyze performance. Unlike an external audit, a management audit primarily examines non-financial data to assess management performance. In a way, the audit tries to find the answer to how well the management is managing the company's business. Is the management style suitable for business operations? A management audit focuses on results, evaluating the effectiveness and adequacy of controls by challenging the underlying rules, procedures and methods.

Auditors analyze the structure of the organization with various competitive aspects. This can help them determine whether the current structure benefits the organization or whether a different structure could increase the company's competitiveness. In the case of an audit, the communication system operating within the management framework becomes a matter of discussion. The more confusing or complex the organizational structure, the more likely the consultant will suggest simplifying the structure of management information flows and feedback loops. Having a simple organizational structure can help improve communication flows and help resolve issues faster.

After the management audit is completed, the consultants prepare a detailed report on what they observed during the audit. Once management teams receive a report from the third-party consultant, they can begin developing plans to implement the action items from the audit. Implementation of these changes may vary from organization to organization, as company change management programs likely differ. However, some general steps a company can take to implement the changes recommended by a management audit include:

- ratification of the proposed changes,
- definition of intended changes,
- adaptation of changes to the company's goals,
- determining the impact of the intended changes,
- communicator.

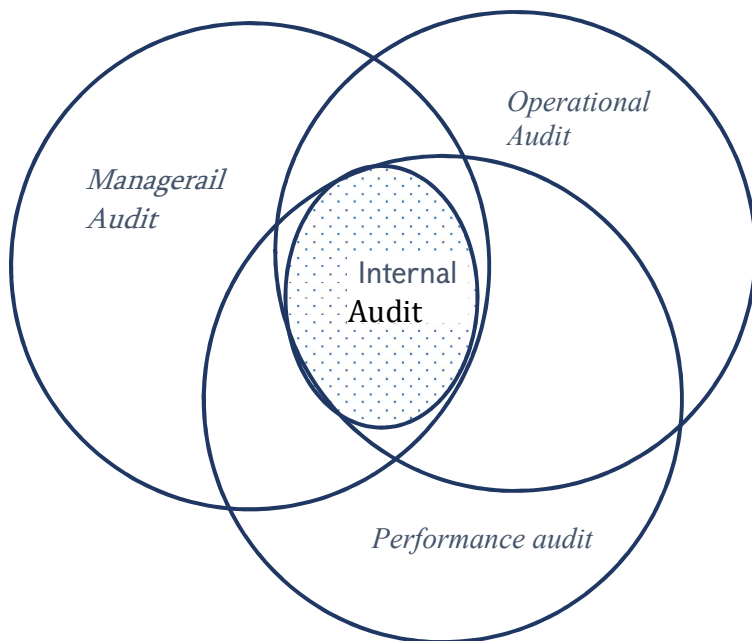


Figure 1. The place of internal audit within the management, operational and performance audit functions²

² Composed by author

Conclusion

Thus, the functions of operational, managerial and performance audits derive from the direct objectives of internal audit. Both management and operational audits operate within the organization and their functions often overlap with internal audit (see Figure 1). If the performance audit is carried out to evaluate the effectiveness of the management functions within the organization, then the operational audit is organized with the aim of optimizing and improving the management functions. And performance audits promote transparency by providing parliament, taxpayers, other funding sources, and the media with insight into the management of various government activities and their ultimate outcomes. In all cases, these three areas of internal audit may overlap in their functions, which in practice requires clarification of their objectives, to avoid repetitions and ineffective spending of audit resources. And the smaller the scope of managerial, operational and performance audit functions, the more effective the organization of internal audit in organizations.

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Գյուլյո Արաբյան
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ՆԵՐՔԻՆ ԱՈՒԴԻՏԻ ՀԱՅԵՑԱԿԱՐԳԱՅԻՆ ՀԻՄՆԱԽՆԴԻՐՆԵՐԸ

Բանալի բառեր – ներքին աուդիտ, աուդիտի ստանդարտներ, գործառնական աուդիտ, կատարողականի աուդիտ, կառավարչական աուդիտ, աուդիտի շահառուներ

Ներքին աուդիտի բնութագրումն ու կազմակերպչական գործառույթների շրջանակը տարբեր կերպ է ընկալվում շահառուների կողմից: Ձևավորվելով արտաքին աուդիտից շատ ավելի ուշ, ներքին աուդիտը համեմատաբար արագ զարգացավ և, այն էլ, մի քանի ուղղություններով: Ներկայումս ներքին աուդիտի առավել տարածված տարատեսակներն են հանդիսանում գործառնական աուդիտը, կառավարչական աուդիտը և կատարողականի աուդիտը: Ուսումնասիրությունները ցույց են տալիս, որ գործնականում ներքին աուդիտի թվարկված տարատեսակները իրենց գործառույթներով հաստատվում են, որը ոչ միայն

շփոթմունքի առիթ է տալիս աուդիտի շահառուների շրջանում, այլև կազմակերպությունից խլում է լրացուցիչ ռեսուրսներ:

Հոդվածում հստակեցվում են գործառնական, կառավարչական և կատարողականի աուդիտի գործառույթները՝ շահառուների տեսանկյունից: Գործառնական աուդիտը հետամուտ է լինում ձեռներեցության տարբեր գործառույթների իրականացման արդյունավետության ռեզերվների բացահայտմանը, որոնք վերաբերում են արտադրությանը, ծառայությունների մատուցմանը: Կառավարչական աուդիտի խնդիրը կազմակերպությունում կիրառվող կառավարման արդյունավետ համակարգի գործունեության խթանումն է: Իսկ կատարողականի աուդիտը հիմնականում առնչվում է հանրային ոլորտի կազմակերպություններին և նպատակ է հետապնդում ոչ միայն պարզելու պետական ֆինանսների նախահաշիվների ծախսման հավաստիությունը, այլև դրանց արդյունաբերությունը՝ շահառուների սպասումների տեսանկյունից:

Հետևաբար, գործառույթների իրականացման տեսանկյունից գործառնական, կառավարչական և կատարողականի աուդիտի ոլորտները կարող են կազմակերպություններում ինչ-որ տեղ հատվել: Եվ որքան փոքրանում է կառավարչական, գործառնական և կատարողականի աուդիտի գործառույթների հատույը, այնքան կազմակերպություններում ներքին աուդիտի կազմակերպումը համարվում է արդյունավետ:

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