

## FRAMEWORK OF REVIEWS INTERNAL AUDIT DIRECTIONS

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**Abstract:** The origin of internal audit was mainly conditioned by the strengthening of control activities within organizations, when the task was set to consistently assess the effectiveness of the asset maintenance process, the effectiveness of monitoring the results of financial and economic activities. Thus, internal audit acted as a tool to support corporate management. However, currently, the requirements for sustainable development of economic management have also had an impact on the directions of internal audit, which have already targeted the services of public interests. The study substantiates the requirement to review internal audit functions in the context of sustainable development of organizations.

**Keywords:** internal audit, control and monitoring functions, assurance and consulting functions, sustainable development assurance

**JEL codes:** M41, M42

**Research aims:** to rationalize and review the functions of internal audit, based on the contemporary problems facing the economic activities of organizations.

**Research novelty:** controlling functions aimed at serving the public interest have been proposed in the context of reviewing the traditional functions of internal audit, which are particularly related to ensuring the sustainability of organizations' development.

### **Introduction**

Traditionally, internal audit verifies and evaluates the effectiveness and reliability of the internal control system, the implementation of internal regulations, accounting policy requirements and top management decisions, the reliability of the information on the basis of which management makes decisions, the activities of various management levels, financial and tax accounting, as well as the preparation of financial statements, and the preservation of the organization's assets (Audit Committees in the European Public Sector 2019). However, currently, internal audit functions are also aimed at serving public interests, in particular, identifying opportunities for sustainable development of organizations and supporting their implementation, which forces us to reconsider the directions of internal audit functions (Hovsepyan H. 2020).

### **Results**

Internal audit, being a fairly new and modern specialty, is of serious interest in the current era of rapidly developing market economy and various changes. New challenges and imperatives are increasing the attention paid to the mentioned profession day by day. Although the roots of internal audit are quite deep, nevertheless it has acquired and formed its current appearance,

nature and essence, role and significance mainly in the last century and especially in the 3rd millennium.

Referring to the evolutionary development of internal audit, let us note that its roots date back to the period before our era. According to some sources, the roots of internal audit lie in BC. In the 3rd-4th millennia, when prototypes of accounting records were made on stones, which served as the basis for inspections. The historical basis for the development of auditing, including internal auditing, is also the so-called public finance and control that originated in Babylon, Greece, Ancient Rome, as well as the Middle East, which formed a new system of records, calculations and inspections (tax collection, payment, receipt of various funds) to prevent accounting errors and inaccuracies, as well as fraud and corruption. Audit has a long and noble history. Even in ancient Rome, a “hearing of accounts” was performed, when a responsible person compared the records. From here, the verbal inspection laid the foundation for the creation of the term “audit”, which arose from the Latin word “auditus” - hearing, listening”.

Despite its ancient roots, internal audit as a profession has generally begun to be recognized and developed since the 1930s. The founding of the Institute of Internal Auditors (IIA) in the United States in 1941 as an international professional association, whose mission is to provide dynamic leadership for the global profession of internal audit, was a turning point in this regard. Currently, IIA has more than 200,000 members from more than 170 countries around the world, as well as representations in the form of local institutes in different countries. IIA-Armenia, which is an affiliated

member of IIA, is also such a representation (Bruce Turner A., Andrew C. 2020).

It should be noted that at the initial stage of its recognition as a profession, internal audit was of an administrative-documentary nature, since accounting records were made in writing, and auditors had to perform inspections in their part, to exclude errors. Over time, internal audit has evolved from a checking, monitoring and inspection activity to the form it has today (The Future Auditor Has Arrived” 2019).

Internal audit is now defined as an independent, impartial assurance and consulting function to improve an organization's operations and add value. It helps the organization achieve its objectives by consistently assessing and improving the effectiveness of risk management, control and governance processes. Also, internal audit occupies a significant place in the improvement of the organization's activities and the overall control system. It is an important component of corporate governance (Zeitouny H.H. 2012).

Turning to the scientific and methodological foundations of the internal audit, which are an important element of its philosophy, it is necessary to state once again that, despite its ancient roots, internal audit is a fairly new profession, and as we have already noted, it was not recognized as an important process by organizations and their external auditors until the 1930s. The need for effective control processes is what, one might say, created the concept of internal audit. This recognition was largely due to the establishment of the US Securities and Exchange Commission (SEC) in 1934 and the change in the goals and objectives of external

auditing at that time. The United States, like the rest of the world, was going through a great economic crisis. As a legislative reform, the SEC required all organizations registered with it to provide financial statements certified by independent auditors. This requirement also prompted corporations to establish internal audit departments, but the primary goal was to support independent external auditors. At that time, external auditors were more focused on expressing an opinion on the reliability of financial statements than on detecting control problems, deficiencies and accounting errors. SEC rules accelerated the development of internal control processes, based on reliability auditing. At that time, internal auditors were mostly engaged in checking accounting records and detecting financial errors and deficiencies and often played the role of assistants or, in other words, “shadows” independent external auditors. The need to improve processes led to the realization that approaches should be changed and the potential of internal auditors should be used more effectively and purposefully. As a result, the NAI was founded in the USA, which, as we have already mentioned, later had separate representations in different countries of the world.

In recent decades, risk management has been recognized as a critical component of effective corporate governance. This circumstance has put additional pressure on organizations to identify all the business risks they encounter and explain how they manage them.

Since organizations are different, have different cultures, structures, strategies, different approaches to risks and various processes, in order to effectively apply the risk-based IA

methodology, internal auditors must take into account the above and other similar factors. They must align this methodology with the ideology, culture and values of the organization, without crossing the boundaries of professional ethics.

Regarding the importance and significance of internal audit, as well as its role in science and organizations, it should be noted that internal audit is an advisor and assurance provider for the highest levels of organization management, supporting the improvement of risk management, corporate governance and internal control processes, conducting an independent assessment and thereby providing additional guarantees for increasing the efficiency of the organization's management as a whole. The concepts of independence, impartiality, value addition and performance improvement that are the cornerstones here are of vital importance not only for the development of organizations, but sometimes for their further existence in general (Robert R. Moller 2016).

Presently, the functions of internal audit to identify the capabilities and opportunities of organizations for sustainable development are actively developing. The IFRS-S standards put into effect, require organizations to publicly disclose sustainable development strategies, risks, as well as opportunities. And the validity of this information is first of all assessed by internal audit, which, in addition to its functions aimed at corporate governance, carries out studies and conclusions related to the regular process of sustainable development.

The public interest encompasses the social and economic interests and general well-being of society and the organizations within it (including employers, employees, investors, the business

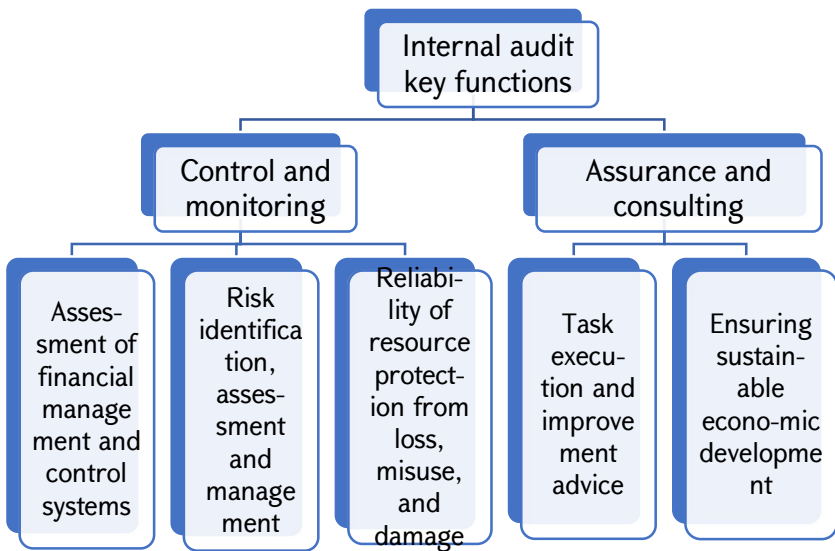
and financial community, customers, consumers, regulators, and government). Issues of public interest are context-specific and should take into account ethics, fairness, cultural norms, and values, as well as the potential for disproportionate impacts on particular individuals and subgroups of society (Khachatryan, N., 2024).

Currently internal audit plays a critical role in enhancing an organization's ability to serve the public interest (Internal Audit transformed 2021). While internal audit's primary function is to strengthen corporate governance, risk management, and control processes, its impact extends beyond the organization. Internal audit contributes to the overall stability and viability of an organization by providing assurance about its operational efficiency, reliability of reporting, compliance with laws and/or regulations, safeguarding of assets, and ethical culture. This, in turn, fosters public trust and confidence in the organization and the broader systems of which it is a part. Towards (Anderson U. L., Head M. J., Ramamoorti, C. Riddle, M. Salamasick, Sobel P. J. 2017).

The RA Law "On Internal Audit" defines a number of functions aimed at improving the activities of organizations, such as:

- 1) assisting the head of the organization in identifying and assessing the risks existing in the organization.
- 2) assessing the effectiveness of financial management and control systems and their compliance with the following conditions:
  - a. identification, assessment and management of risks by the organization's management,

- b. compliance with the legislation of the Republic of Armenia and other conditions related to the organization's activities (contracts, departmental normative acts, etc.),
- c. economical, efficient and useful functions,
- d. reliability and integrity of information,
- e. reliability of protection of assets and resources from losses, abuses and damages,
- f. performance of tasks and achievement of objectives.



**Figure 1. Directions of key internal audit functions<sup>8</sup>**

2. Internal auditing is performed through the provision of assurance or consulting services aimed at ensuring specific audit tasks.

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<sup>8</sup> Composed by author



3. An audit performed for assurance services consists of an objective evaluation of evidence by the internal auditor in order to present an independent position or conclusion on the process, system or other component being audited (RA Law "On Internal Audit" 2010).

However, the law does not clearly state the functions of internal audit aimed at ensuring the sustainable development of organizations, which we consider important in the current competitive business environment. For this reason, when classifying internal audit functions, we consider it appropriate to include assurances aimed at sustainable development (see Figure 1).

### **Conclusion**

Internal audit in the current competitive situation should serve not only corporate, but also public interests. The principles of sustainable development of organizations require audit accountability in the areas of social justice, green business, risks mitigations of economic activity negative impact on the environment, and resource conservation. The role of internal audit in this area is increasing, which not only ensures the reliability of such information flows, but also assists in identifying opportunities for sustainable business development. Therefore, there is a need to review the traditional directions of internal audit in the context of sustainable development.

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### Ջուլիետա Քալաշյան

Հայաստանի պետական տնտեսագիտական համալսարան,  
ասպիրանտ

**Բանալի բառեր** – ներքին աուդիտ, վերահսկողական և մշտադիտարկման գործառույթներ, հավաստիացման և խորհրդատվական գործառույթներ, կայուն զարգացման հավաստիացում

Ներքին աուդիտը, հանդիսանալով բավականին նոր և ժամանակակից մասնագիտություն, լուրջ հետաքրքրություն է ներկայացնում ներկայիս խիստ արագ զարգացող շուկայական տնտեսության և բազմատեսակ փոփոխությունների դարաշրջանում: Նոր մարտահրավերները և հրամայականներն օրեցօր ավելի են մեծացնում ուշադրությունը նշված մասնագիտության նկատմամբ:

Ավանդաբար, ներքին աուդիտը ստուգում և գնահատում է կազմակերպության վերահսկողական համակարգի աշխատանքի արդյունավետությունն ու հուսալիությունը, ներքին կանոնակարգերի, հաշվապահական հաշվառման քաղաքականության պահանջների և բարձրագույն ղեկավարության որոշումների իրականացումը, տեղեկատվության արժանահավատությունը, որի հիման վրա մենեջմենթը որոշումներ է կայացնում, կառավարման տարբեր օղակների գործունեության, ֆինանսական և հարկային հաշվառման, ինչպես նաև հրապարակվող հաշվետվությունների կազմման, կազմակերպության ակտիվների պահպանման ուղղություններով:

Սակայն ներկայումս ներքին աուդիտի գործառույթները ուղղվում են նաև հանրային շահերի սպասարկմանը, մասնավորապես կազմակերպությունների կայուն զարգացման հնարավորությունների բացահայտմանը և դրանց իրագործման օժանդակմանը, որն էլ ստիպում է վերանայելու ներքին աուդիտի գործառույթների ուղղությունները:

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