The Constructive Role of the Internal Auditor With Emphasis on the Baton Rouge, Louisiana Area.

James Troy Hood

Louisiana State University and Agricultural & Mechanical College

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THE CONSTRUCTIVE ROLE OF THE INTERNAL AUDITOR
WITH EMPHASIS ON THE BATON ROUGE, LOUISIANA AREA

A Dissertation

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The Department of Accounting

by

James Troy Hood
B.S., Louisiana Polytechnic Institute, 1955
M.B.A., Louisiana State University, 1958
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# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>CHAPTER</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACKNOWLEDGMENTS</td>
<td>ii</td>
</tr>
<tr>
<td>ABSTRACT</td>
<td>vi</td>
</tr>
<tr>
<td>I. THE CHANGING CONCEPT OF INTERNAL AUDITING</td>
<td>1</td>
</tr>
<tr>
<td>- The Clerical Phase of Internal Auditing</td>
<td>2</td>
</tr>
<tr>
<td>- The Change to a Constructive Role</td>
<td>5</td>
</tr>
<tr>
<td>- Scope of the Study</td>
<td>8</td>
</tr>
<tr>
<td>II. ORGANIZATION OF THE INTERNAL AUDITING DEPARTMENT AS AN AID TO MANAGEMENT</td>
<td>11</td>
</tr>
<tr>
<td>- The Need for an Internal Auditor or an Internal Auditing Department</td>
<td>11</td>
</tr>
<tr>
<td>- The Place of the Internal Auditing Department in the Company Organization</td>
<td>15</td>
</tr>
<tr>
<td>- Four Levels of Internal Auditing</td>
<td>16</td>
</tr>
<tr>
<td>- Departmental Internal Auditing</td>
<td>16</td>
</tr>
<tr>
<td>- Staff Internal Auditing</td>
<td>16</td>
</tr>
<tr>
<td>- Managerial Internal Auditing</td>
<td>17</td>
</tr>
<tr>
<td>- Proprietorship Internal Auditing</td>
<td>17</td>
</tr>
<tr>
<td>- Centralization Versus Decentralization of the Internal Auditing Department</td>
<td>23</td>
</tr>
<tr>
<td>- Centralization</td>
<td>24</td>
</tr>
<tr>
<td>- Decentralization</td>
<td>27</td>
</tr>
<tr>
<td>III. SELECTION AND TRAINING OF THE INTERNAL AUDITOR</td>
<td>29</td>
</tr>
<tr>
<td>- Qualifications for Internal Auditing</td>
<td>29</td>
</tr>
<tr>
<td>- Sources and Selection</td>
<td>39</td>
</tr>
<tr>
<td>- Training of the Internal Auditor</td>
<td>46</td>
</tr>
<tr>
<td>- Orientation</td>
<td>47</td>
</tr>
<tr>
<td>- On-the-Job Training</td>
<td>52</td>
</tr>
<tr>
<td>- Reports on Training</td>
<td>54</td>
</tr>
<tr>
<td>- Staff Meetings</td>
<td>56</td>
</tr>
<tr>
<td>- Further Education</td>
<td>58</td>
</tr>
<tr>
<td>- Professional Organizations</td>
<td>59</td>
</tr>
<tr>
<td>CHAPTER</td>
<td>Page</td>
</tr>
<tr>
<td>------------------------------------------------------------------------</td>
<td>------</td>
</tr>
<tr>
<td>The Internal Auditing Department as a Training Ground for Future Administrative and Executive Personnel</td>
<td>60</td>
</tr>
<tr>
<td>IV. OPERATIONS AUDITS</td>
<td>62</td>
</tr>
<tr>
<td>Brief Distinction between Financial and Operations Audits</td>
<td>63</td>
</tr>
<tr>
<td>Effective Auditing Accomplished by Non-expert</td>
<td>66</td>
</tr>
<tr>
<td>Auditing Based on Controls</td>
<td>66</td>
</tr>
<tr>
<td>Advantages of Non-expert</td>
<td>68</td>
</tr>
<tr>
<td>Securing Cooperation</td>
<td>70</td>
</tr>
<tr>
<td>Approach to Operations Audits</td>
<td>72</td>
</tr>
<tr>
<td>Determination of Objectives</td>
<td>73</td>
</tr>
<tr>
<td>Gathering of Pertinent Background Material</td>
<td>74</td>
</tr>
<tr>
<td>Determination of Scope</td>
<td>78</td>
</tr>
<tr>
<td>Use of Operations Personnel on Audit Staff</td>
<td>80</td>
</tr>
<tr>
<td>Details Requiring Special Attention in Operations Auditing</td>
<td>81</td>
</tr>
<tr>
<td>Summary of Non-financial Areas Audited in the Baton Rouge, Louisiana Area</td>
<td>86</td>
</tr>
<tr>
<td>V. THE INTERNAL AUDITOR AND SYSTEMS AND PROCEDURES</td>
<td>89</td>
</tr>
<tr>
<td>Arguments against the Internal Auditor Working in Systems and Procedures</td>
<td>91</td>
</tr>
<tr>
<td>Arguments for the Internal Auditor Having Complete Responsibility for Systems and Procedures</td>
<td>95</td>
</tr>
<tr>
<td>Arguments for the Internal Auditor Having Modified Responsibility for Systems and Procedures</td>
<td>98</td>
</tr>
<tr>
<td>The Internal Auditor's Responsibility for Procedure Manuals</td>
<td>99</td>
</tr>
<tr>
<td>Distribution of Procedure Manuals and Bulletins</td>
<td>101</td>
</tr>
<tr>
<td>The Internal Auditor's Role in Procedure Manuals</td>
<td>102</td>
</tr>
<tr>
<td>Compliance with Manual</td>
<td>102</td>
</tr>
<tr>
<td>Preparation of the Manual</td>
<td>103</td>
</tr>
<tr>
<td>CHAPTER</td>
<td>Page</td>
</tr>
<tr>
<td>----------------------------------------------</td>
<td>------</td>
</tr>
<tr>
<td>Summary and Conclusions Concerning Systems</td>
<td>105</td>
</tr>
<tr>
<td>and Procedures</td>
<td></td>
</tr>
<tr>
<td>Employee Performance</td>
<td>107</td>
</tr>
<tr>
<td>Records Disposition</td>
<td>108</td>
</tr>
<tr>
<td>VI. THE INTERNAL AUDITOR'S COMMUNICATION WITH</td>
<td>111</td>
</tr>
<tr>
<td>MANAGEMENT: AN EFFECTIVE REPORT</td>
<td></td>
</tr>
<tr>
<td>Factual Information</td>
<td>114</td>
</tr>
<tr>
<td>Concise Wording</td>
<td>116</td>
</tr>
<tr>
<td>Clear Presentation</td>
<td>117</td>
</tr>
<tr>
<td>Objective Approach</td>
<td>125</td>
</tr>
<tr>
<td>Tactful Writing</td>
<td>125</td>
</tr>
<tr>
<td>Well-packaged Report</td>
<td>126</td>
</tr>
<tr>
<td>Prompt Reporting</td>
<td>128</td>
</tr>
<tr>
<td>Summary</td>
<td>129</td>
</tr>
<tr>
<td>VII. SUMMARY AND CONCLUSIONS</td>
<td>130</td>
</tr>
<tr>
<td>SELECTED BIBLIOGRAPHY</td>
<td>139</td>
</tr>
<tr>
<td>VITA</td>
<td>148</td>
</tr>
</tbody>
</table>
ABSTRACT

In approximately twenty years internal auditing has changed from an activity with no organization and with no formal standards of conduct to an organization of professional men located throughout the world. This drastic change was the result of research accomplished by outstanding men in the field, an expansion of activities outside the accounting area, and the formation of the Institute of Internal Auditors.

With the movement of the internal auditor into non-financial areas, several problems were encountered by management: the location of the internal auditor within the business organization, the selection and training of persons capable of performing this new broadened scope of activity, and the determination of the internal auditor's responsibility in operations, systems and procedures, and report writing. This study is concerned with these problems in the broad approach to internal auditing.

Primary data regarding the selection and training of the internal auditor and his responsibilities concerning operations and systems and procedures were gathered to show the actual practice of the four internal auditors located with principal industrial firms in the Baton Rouge, Louisiana area. These auditors and their firms prefer to
remain anonymous. Lengthy discussions were held with each of these internal auditors and much pertinent and interesting information was obtained for inclusion in this study. Intensive use was made of library materials available, especially the publications of the Institute of Internal Auditors.

In order to be of the most constructive use to management, the internal auditor should report to the top level of management—the president or vice-president. The internal auditing department should be staffed from several sources: persons transferred from other areas of the firm, persons who have experience in public accounting or internal auditing, and recent college graduates. The training program should include a rotation program covering various types of audit assignments under experienced auditors.

Financial auditing and operations audits are quite similar; they merely deal with different kinds of controls. The internal auditor is qualified to conduct operations audits, since he appraises controls and not technical operations.

The internal auditor should not be given the responsibility for the design and installation of systems and procedures, since he will have lost his independence if called upon to audit his own work. His responsibility is to audit for compliance and suggest any necessary changes. In order to make management as receptive as possible
to his recommendations in the written report, the internal auditor must follow contemporary principles of report writing.

Three factors appear to be hindering the growth of constructive internal auditing: in many companies the internal auditor is not reporting to the appropriate level of management, the title of "internal auditor," does not denote a comprehensive role, and there is a lack of understanding as to how a non-expert can effectively audit operations.

The future of internal auditing lies in broad, constructive assistance to management, and the internal auditor can fill this role adequately.
CHAPTER I

THE CHANGING CONCEPT OF INTERNAL AUDITING

Necessity created internal auditing and is making it an integral part of modern business. No large business can escape it. If they haven't got it now, they will have to have it sooner or later, and, if events keep developing as they do at present, they will have to have it sooner.\(^1\)

The entire history of accounting has been one of continuous changes and improvements, and the ability to remain cognizant of the changing needs of commerce has aided accounting in growing and developing and reaching the professional status which it has attained today. As commerce became more complex and more demanding on accounting, areas of specialization developed to meet the increased demands of business.

One of the most recently developed areas of accounting is the field of internal auditing. Today, it is generally recognized that there are two types of auditing—external auditing and internal auditing. External auditing—the review of financial records by an independent appraiser—has, of course, long been recognized as an

important phase of accounting and a necessity of business, whereas the area of internal auditing is still in the developmental stage.

Suffice it to say for the present that internal auditing is a review of important facts by an employee of the organization.

In theory, the function of internal auditing has always existed in one form or another. Even in a one-man type of operation, though no individual is designated as the "internal auditor," the owner himself performs certain inquiries, reviews, and appraisals in the normal course of keeping check on his business. Prior to 1900, some of the larger firms had set up separate internal auditing staffs. However, the realization of the potential value, scope, and objective of the internal auditor is, relatively speaking, very new. In fact, it was not until 1941 that a book was available which dealt comprehensively with the subject of internal auditing.

The Clerical Phase of Internal Auditing

Prior to 1941, internal auditing was an activity with no organization and with no formal standards of conduct. Since no literature which would provide an exchange of ideas was available,


\[\text{3V. Z. Brink, Internal Auditing, Ronald Press Company.}\]
each company making use of what might be called internal auditing developed the work to meet its particular needs and ideas. This being the case, there was little uniformity of practices and responsibilities among the internal auditors of the different firms.\(^4\)

Not too many years ago, much of the record keeping was done by hand, and it was necessary for someone to check the accounting work after it was done and locate the errors which frequently occurred in hand-kept records in recording transactions, postings, footings, and extensions. Also, in this same period, internal controls had not been developed to the extent that they are today, with the result that employees inclined toward fraud found it comparatively easy to effect misappropriations. It was therefore necessary to have some sufficiently skilled person perform this dual role of "checker" and "policeman," and the internal auditor fit this need because of his training in accounting. Thus, during these early years, internal auditing was largely limited to the verification of records and the search for dishonesty.\(^5\)

Over the years, some progressive internal auditors began to


reach beyond the limits of the clerical frontier of internal auditing. They conceived a broader scope of activities and a wider range of usefulness for internal auditing, but this individual pioneering was limited because of the lack of a formal organization which would provide a medium for exchange of ideas. The formation of the Institute of Internal Auditors in 1941 was the outgrowth of this desire for organization and was probably the greatest single factor contributing to the professional growth of internal auditing.

By 1947, this broadened viewpoint had gained sufficient momentum to be included in the first published "Statement of Responsibilities of the Internal Auditor." The following was a description of internal auditing as given by this statement:

Internal auditing is the independent appraisal activity within an organization for the review of the accounting, financial, and other operations as a basis for protective and constructive service to management. It is a type of control which functions by measuring and evaluating the effectiveness of other types of control. It deals primarily with accounting and financial matters but it may also properly deal with matters of an operating nature.

The wording of this statement is significant, as it indicates

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the stress upon internal auditing at the time. Note the sentence:
"It deals primarily with accounting and financial matters but may
also properly deal with matters of an operating nature." This
statement indicates the stand taken by the Institute was that the
primary responsibility of the internal auditor lay within the clerical
boundaries as previously discussed, but that in some supplementary
way it might be possible for the internal auditor to be of value in
areas outside of the accounting and financial areas.

The Change to a Constructive Role

Had internal auditing failed to grow and change in character,
it probably would have gone out of existence. As time went by,
machines began to replace the hand methods of keeping records.
The mechanical methods of record keeping provided automatic check­
ing procedures which obviated to a great extent the need for volumi­
nous hand checking by the internal auditor. Also, systems of
internal control developed to such an extent that there was much
less need and demand for the internal auditor to act as a "watchdog"
over the assets. Fortunately, at the same time that the clerical
phase of internal auditing was diminishing, the whole new approach
to internal auditing was being developed.

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8 The Institute of Internal Auditors, Inc., loc. cit. Underscores mine.
9 Thurston, loc. cit.
Internal auditing, like any special area of accounting, developed in response to the needs which arose. It was at this time that business in general was greatly expanded because of the all-out war effort and the following reconversion to peace-time operations; business assets were spread nationally and even internationally. This gross expansion brought with it the unavoidable separation of management from operations and made it impossible for management to keep in direct contact with all departments and activities. While the expansion and progress of business in general contributed greatly to the move to a broader approach to internal auditing, there were a few industries which gave the greatest impetus to the change. Railroads, utilities, chain stores, holding companies, distributing companies, and the large industrials were the companies with decentralized operations managed by delegated authority. These types of companies were most receptive to the wider scope of internal auditing which would provide qualified representatives of management to visit all locations of the companies and report their findings to management. During this time, management found itself in the public spotlight with increased responsibilities. Business was expanding rapidly, causing a loss of the personal contact which had been possible in the past, and someone was needed.

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10 Cunningham, loc. cit.
to fill the gap and aid management in maintaining control. Because of continued professional development and the availability of literature on the subject of internal auditing, management became aware of the potentialities of the internal auditor and began to utilize his services to assist in maintaining managerial control over the widespread business organization.

A definite change occurred in the objectives, methods, and status of the internal auditor; no longer was he classified as merely a better-than-average clerical employee.\textsuperscript{11} By 1957, the change in the whole concept of internal auditing was so pronounced that it warranted a change in the statement of the nature of internal auditing by the Institute of Internal Auditors. The following is taken from the revised "Statement of Responsibilities of the Internal Auditor" as published in 1957:

Internal auditing is an independent appraisal activity within an organization for the review of accounting, financial and other operations as a basis for service to management. It is a managerial control, which functions by measuring and evaluating the effectiveness of other controls.\textsuperscript{12}

In comparing this to the statement published in 1947, it can be seen that the content of the two statements is basically the same.

\textsuperscript{11}Arthur H. Kent, "The Internal Auditing Staff," The Controller, XV (July, 1947), 332.

The point that is important here is that the 1957 statement officially broadened the approach to internal auditing. In 1947, the stand was that the internal auditor's primary responsibility was with accounting and financial matters but that he might also deal with operating matters—a permissive but not necessary role. It should be noted that no such distinction was made in the 1957 revised statement, and the official stamp of approval was given to the broader approach to internal auditing. In fact, the revised statement declared explicitly that the internal auditor "should be concerned with any phase of business activity wherein he can be of service to management."  

Thus, while the rendering of protective service is still an important part of the work of the internal auditor, he is also expected to aid management in any way possible by providing important facts which otherwise would not be available. The modern internal auditor has a dual purpose—protective service and constructive service. The remainder of this study is concerned almost exclusively with the constructive service approach to internal auditing.

Scope of the Study

Because of the newness of the constructive service phase of internal auditing, much has yet to be done to establish the approach

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13 The Institute of Internal Auditors, Inc., loc. cit. Underscore mine.
and scope of this area of internal auditing. It is the purpose of this study to discuss thoroughly the selection and training of the internal auditor and his place in three important functions: operations, systems and procedures, and report writing.

The usefulness of internal auditing to management is directly related to the position of the internal auditing department in the organization structure of the firm and the quality of employee selected as the internal auditor. Chapters II and III are therefore spent in an analysis of how the internal auditing department can best be organized and staffed in order to provide management with the most efficient and beneficial service. Original research was done in the industrial firms in the Baton Rouge area to provide some of the information presented in Chapters III, IV, and V. Discussion in Chapters IV and V is centered along the lines of determining what should be done and what is being done by the internal auditors in the Baton Rouge area in order to aid managers in the functions of operations and systems and procedures.

Without an effective means of communicating with management, the work of the internal auditor would be valueless. The purpose of Chapter VI is to determine the principles of report writing which should be observed by the internal auditor in order to prepare a clear, complete, and action-securing report for management.

The final chapter presents a summary of the study and
conclusions as to the effectiveness of internal auditing in meeting the needs of management in non-financial areas. Obstacles which must be overcome if the internal auditor is to continue expanding in a constructive role are presented.
CHAPTER II

ORGANIZATION OF THE INTERNAL AUDITING DEPARTMENT
AS AN AID TO MANAGEMENT

The function of internal auditing is carried on in one form or another in all companies regardless of size. In a small operation, the owner himself acts as the internal auditor and performs inquiries and checks as he deems it advisable to do so. As the business becomes larger, it becomes impossible and inadvisable for the owner to spend his time performing the internal auditing function, and the task is assigned to an individual who performs the work and reports directly to the owner. In contrast to these simple situations in smaller companies, separate internal auditing departments with large staffs of a hundred or more operate as a direct aid to management in the large industrial organizations.

The Need for an Internal Auditor
or an Internal Auditing Department

It should be stated at the outset that an internal auditing group should be installed only if the need exists and not just because other, even similar, companies may be making use of such a group. The fact that firms of comparable size have internal auditors may be
an indication of a need, but this is not conclusive in itself. Any company which employs internal auditors without careful consideration of a number of factors risks wasting its money as well as the time of a number of high-caliber workers.

No precise formula can be developed that will indicate the necessity of having internal auditing in a business; each company must analyze its own requirements and reach its own conclusions. However, there are certain fundamental situations which may be observed in determining the need for an internal auditor or an internal auditing department:

1. Where the company's operations are conducted in more than one location.

2. Where the company's functions are diversified. For example, it may manufacture and sell its own products, maintain sales offices, and bill and collect from many customers over a wide area.

3. Where a company's salesmen act also as collectors, in such businesses as larger bakeries, distributors of dairy products, and department stores.

4. Where other companies of comparable size in the same or closely-related industries generally maintain internal auditing departments.

5. Where the company has a large number of employees. Large in most instances would mean several hundred, or even a thousand, unless coupled with problems of distribution and collection.

6. Where wage incentives of various types complicate payroll routines and resulting specific costs of products to the point where objective verification and appraisal is essential.
7. Where the system of internal check and control is inadequate to deal with the resulting potentiality of increased errors and fraud.

8. Where the public accountants find it necessary to perform internal auditing work before certifying the balance sheet, with resulting increases in costs.

9. Where management wishes maximum assurance that its plans, policies, and procedures are being carried out faithfully and efficiently, and that such plans, policies, and procedures are the most effective under the circumstances.¹

Some or all of the above may be applicable to the situation of a company, and management should give them careful consideration in deciding whether or not there is a definite need for internal auditing.

The size of the internal auditing department will depend upon the duties assigned to it by management and the needs of the particular business. For example, some companies carry on branch operations and will therefore need internal auditing done away from the main office, whereas this phase of internal auditing will not be required in companies without branch operations. Some managements will expect the internal auditor to do some activities of an operating nature, which will obviously affect the set-up and program of the internal auditing department. The number of special assignments to be given to the internal auditing department, the adequacy

of the system of internal check, and the nature and extent of the physical assets will also affect the size and structure of the internal auditing department.\(^2\)

The size of the department and the type of personnel to be employed should be specified only after a projection of the expected work of the internal auditing department for the next six months or year. This general projection, made as accurately as possible, should be presented and discussed with members of top management before determining the number and types of men to employ.\(^3\) This procedure will serve a double purpose. First, as has been indicated, it will assist in determining the structure of the department. Secondly, and possibly even more important, will be an indication by top management of the type of work expected from the department and a prediction of the backing to be received by the department from management.

In order for the internal auditing department to assist management best, the whole internal auditing program should be conducted separately from routine operations. There are two basic reasons for this: (1) if the same person does internal auditing and routine operations, it is usually the auditing work which takes second place and

\(^2\)Ibid., pp. 183-184 and 186.

\(^3\)Ibid., p. 186.
is done only if no routine operation work is waiting to be done, and (2) if the same person does both types of work, he will lack the detachment necessary for proper auditing and, therefore, most effective assistance to management, \(^4\) i.e., work will be done and audited by the same person.

**The Place of the Internal Auditing Department in the Company Organization**

Management should consider carefully the position of the internal auditing department within the company framework and organization, since this position will notably affect the efficiency and effectiveness of the work of the department. The type and range of work of the auditor will depend to a great extent on the organizational status of the internal auditing group with particular concern as to the person to whom the internal auditor reports. Brink and Cashin have stated that "the level of reporting authority determines the range of the services which can and will be rendered by any given internal auditing group."\(^5\)


Four Levels of Internal Auditing

There are different levels of internal auditing, and this fact causes no little confusion in discussions involving this operation. In many cases, the term "internal auditing" is applied to any type of verification activity, running the scale from such operational functions as bank reconciliations to complete and thorough audit programs somewhat comparable to those performed by public accountants. Internal auditing is sometimes divided into four distinct levels, each with its own objectives, scope, and standards of practice.

Departmental Internal Auditing

The simplest form or level of internal auditing is the work done by an auditor appointed by a particular minor department. This type of internal auditor is confined by the limits of the particular unit which appointed him and is responsible to the head of that unit. His work is limited to such tasks as the auditing of accounts payable, payrolls, and construction.  

Staff Internal Auditing

The staff internal auditor holds a position created under a vice-president, controller, treasurer, or some other person of comparable

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rank. Since he is appointed by a person in charge of a particular area, he is subject to the instructions and dictates of the person in charge, and his duties and responsibilities are confined to that area except as the person to whom he reports makes arrangements for him to move into other departments. As a rule, the internal auditor at this level lacks the freedom of movement and the detachment accorded to the next two levels of internal auditing. 7

Managerial Internal Auditing

If the internal auditor is appointed as a representative of top management—president, executive vice-president, or similar position—his duties and responsibilities automatically bridge all departments of the business, and he is known as a management internal auditor. 8

Proprietorship Internal Auditing

An internal auditor completely independent of all management personnel and appointed by the owner of a single proprietorship, the partners of a partnership, or the board of directors of a corporation is known as a proprietorship internal auditor. This level of internal auditing provides the greatest degree of independence and

7 Cunningham, loc. cit.
8 Loc. cit.
detachment, since the internal auditor is responsible directly to the owner(s) and may move anywhere in the organization as a representative of the proprietorship.  

Reporting Responsibility of the Chief Internal Auditor

Generally, all internal auditing of a particular organization is co-ordinated and controlled by one separate department of internal auditing, instead of having several internal auditing departments according to the different levels just mentioned. It is extremely important to make the right decision concerning the person to whom the chief internal auditor will report, as it will determine the whole course of thought and action of the entire internal auditing department. Careful consideration should be given to this point so that management may receive the maximum benefit from its internal auditing dollar.

One possibility is to have the internal auditor appointed by and therefore responsible to the board of directors. Concerning detachment and independence, this position would be the most advantageous, since it would subject the entire business organization to auditing appraisal. The internal auditor would be free to move

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9Cunningham, loc. cit.
anywhere in the organization, even to the point of appraising the work of the president. However, the basic point at issue here is whether the internal auditing department is to be designated as a check on management or as an aid to management. If it is purposed to have the internal auditing department serve as a representative of the proprietorship, then its responsibility should be to the board of directors. However, as it is generally conceded that the primary purpose of the department should be to serve as a constructive aid to management, it should be under the direction and control of management. It must be in a position to serve management in any way necessary in order to keep a current and constant check on operations of the business, and it should not be necessary for management to request that the board of directors place the internal auditors on a particular task. Of course, some type of compromise may possibly be effected with the chief internal auditor responsible to the board of directors for certain requirements and beyond these be subject to the control of management.\(^1\) This is merely offered as a suggestion which might be feasible depending upon the circumstances, since the situation of having two superiors—a member of top management and the board of directors—should be avoided in most cases. In a survey conducted by the Institute of Internal Auditors in 1957,.

\(^1\)Brink and Cashin, *op. cit.*, p. 44.
only 21 of the 317 respondents to the question answered that the chief internal auditor reported to the board of directors.\textsuperscript{11}

An arrangement which has worked out satisfactorily in some situations is to have the chief internal auditor report to the top ranking financial officer. In such a case the auditor is under the direction of the financial vice-president, treasurer, or controller.\textsuperscript{12}

It is necessary that this financial officer be in a high-level position, since he must be able to steer the work of the internal auditing department in all areas and yet provide the greatest degree of independence possible under the circumstances. For example, the operating head of the accounting department is at too low a level for the chief internal auditor to report to him. In the first place, an adequate degree of independence would not exist, since the internal auditor would be placed under the supervision of the person whose work he would be auditing. This situation would also exist, probably to a lesser degree, with the treasurer or controller. Secondly, the operating head of the accounting department would generally lack the position and stature within the company to be able to move upward or horizontally across the organization chart to assure that the internal


\textsuperscript{12}The Controllers Institute lists the internal auditing function as a responsibility of the controller.
The internal auditor receives cooperation in moving outside the financial area in order to perform necessary appraisals. However, if the person to whom the auditor reports is truly a top executive, it may be that this person can effectively co-ordinate the work of the internal auditor to the extent of making it possible for him to bridge the lines of the organization chart and serve constructively as an aid to management.

Many times it is advocated that the chief internal auditor should report directly to the president or executive vice-president. This situation also has its advantages and disadvantages, but as Ronald Woods indicates: "The closer the auditor is aligned to the president, the greater the independence, without loss of purpose." This position of being accountable directly to the president's office places the internal auditor in a position of detachment and independence away from those whose work must be appraised, and this independence is important for the internal auditor to feel free to evaluate all areas of the business without fear of reprisal. In this position the internal auditing department is best situated for being constructively helpful to management. It is not so far up in the organization (responsible to the board of directors) that sight is lost of the primary purpose of being of assistance to management, and neither is it suppressed.

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within one particular area of the business (reporting to the treasurer or a lower financial officer).

It is recommended that, if at all possible, the internal auditor should report to the executive vice-president rather than to the president. Following this procedure, the auditor will probably more easily receive the active support which is necessary and which the president would not have the time to give. In this position the internal auditor is at the "beck and call" of management, and he is in a situation where he can move anywhere in the organization to perform whatever appraisals that might be necessary without the complications which could arise if he were reporting to a financial officer and were asked to move outside the area of financial auditing. The internal auditor has more to offer than an appraisal of financial activity, and this propinquity to the president appears to be the situation in which the internal auditor can best serve in his role as an aid to management.

There is no final positive answer as to whom the chief internal auditor should report. Each company has its own organization, and the "scope or responsibility and supervisory authority of the officers differ."14 Thus, it becomes an individual problem for each company. There are cases where the controller is such a high ranking executive

14 lamperti and Thurston, op. cit., p. 185.
that the chief internal auditor could report to him and retain independence and free movement throughout the company; in such cases, it would be acceptable to have him supervise the internal auditor.\textsuperscript{15} As a safe rule, however, it appears that the procedure of having the chief internal auditor report directly to the executive vice-president or the president is the best plan.

Centralization Versus Decentralization of the Internal Auditing Department

Not many years ago, the operations of a company were confined to a relatively small geographical area. This was necessary because fast area-wide or country-wide transportation and advertising were not available to the extent that they are today. If all businesses were still conducted in one small area, the work of the internal auditing department would be greatly simplified. There would be the chief internal auditor, his assistant(s), and an adequate number of auditors to appraise the business operations at the location. However, as commerce progressed, a great number of businesses found it possible and advisable to expand their operations beyond a localized area, and co-ordination of the business became a greater

\textsuperscript{15} Victor Z. Brink, Managerial Control through Internal Auditing (Stamford, Connecticut: Brock and Wallston, 1943), pp. 76-77.
problem for the internal auditing department. In the companies which expanded their operations it was necessary to consider the advisability of decentralization of the internal auditing department in order for it to be of greater assistance. It had to be determined whether traveling auditors should be used to appraise operations at branches (a system of centralization) or whether a resident auditing staff should be employed at each branch (a system of decentralization). Careful consideration had to be given as to which procedure would be more effective for the particular business.

Centralization

Naturally, there are some companies which operate at one location or within a small area; these companies obviously lend themselves to a centralized form of operation of the internal auditing department. However, there are several additional factors which must be considered in determining the proper degree of centralization. The following seven factors are listed as having some bearing on this question by contributors to a survey:

1. Location or geographical dispersal of subsidiary operating units. Where closely concentrated geographically there would be a tendency to centralize the function while the reverse might be true if the units were widely scattered, because of travel requirements, etc.

2. Size of subsidiaries. Smaller subsidiaries, not large enough to require a full time auditing staff, would probably be covered by the parent organization, irrespective of location.
3. Type of business or nature of activities of both parent and subsidiaries. Where these are entirely dissimilar there might be less justification for centralization of auditing. Also there are statutory and regulatory requirements affecting certain industries that might have a bearing, . . .

4. General plan of organization in effect. This relates to the degree of centralization or decentralization of managerial responsibility in general as well as the accounting, record-keeping and control activities specifically. . . .

5. Nature of the internal auditing activities. Is the conception of the function limited largely to verification of records and accounts or does it encompass the higher grades of internal audit work, . . .

6. Availability to subsidiaries of qualified audit personnel. Difficulty in obtaining and retaining capable auditors or supervisors might serve to influence a centralized setup.

7. Custom or personal preference of top management. Resistance to change can be a practical even if illogical factor.16

Centralization should be considered carefully, since there are certain advantages to this form of operation. In the first place, it is generally assumed that there is a cost saving in a centralized operation. This applies only up to the point at which the cost of travel and other factors in order to keep a centralized operation may exceed the cost of decentralizing. If the internal auditing function

is centralized, it may be possible for the company to attract higher quality personnel to work out of the home office than it would be possible to secure for resident internal auditors at the various branches. Broader perspective and greater flexibility of the centralized internal auditing personnel promote a more efficient use of the staff. A centralized staff will usually follow a more uniform method of work than a decentralized operation, and this will result in a better basis for comparing results of audits.\footnote{Ibid., p. 49.} Also, the traveling auditor from the home office will not become as familiar with the branches he audits nor as well acquainted with the employees of those branches as would resident auditors. This situation should, therefore, make for a more thorough and objective audit if handled through a central office.\footnote{Lamperti and Thurston, \textit{op. cit.}, p. 188.}

The most objectionable disadvantage of the centralized type of operation of the internal auditing department is the travel involved--in terms of both time and money. Prolonged absences from home on extended out of town audits, sometimes lasting several weeks or months, will cause objection, especially from men with families. Some companies have tried various means of alleviating this drawback: more frequent trips instead of one of long duration, a team of
auditors instead of one auditor for a long period of time, weekend visits at home, and days off after each trip. Clearly, all of these expedients tend to raise the cost of auditing above the possibly already objectionable costs of traveling and living away from the main office.

Decentralization

Under any system of decentralization of the internal auditing department, the chief internal auditor should still be located at the headquarters of the company. This will provide the close contact with top management which is essential if the internal auditing department is to act effectively.

Decentralized operation of the auditing department will reduce the time and cost of travel to the various branch operations with the possibility of more frequent and more thorough audits by the resident auditor in charge. On the other hand, resident internal auditors at branch operations tend to become so familiar with the operations and the employees that they must be rotated among branches to avoid superficial audits. Also, problems of co-ordination and communication may develop with decentralization.\footnote{Ibid., pp. 188-189.}\footnote{Ibid., pp. 190-191.}
In many cases, both resident and traveling internal auditors are used when it is advantageous to decentralize the internal auditing department. The resident internal auditor serves the local management, whereas the traveling internal auditor is responsible to the headquarters management. The traveling auditor visits the location periodically and makes general overall audits, reporting the results to his superior, whereas the resident internal auditor will make detailed audits of each operation and report to the local management. This procedure provides assistance to the local management and still retains co-ordination with top management through the traveling internal auditor.

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CHAPTER III

SELECTION AND TRAINING OF THE INTERNAL AUDITOR

Primary data were gathered for this chapter and the two following from the four internal auditors located with principal industrial plants in the Baton Rouge, Louisiana, area. Lengthy discussions were held with each of these internal auditors, and much pertinent information was gained for inclusion in this study. This information is interspersed throughout these chapters, but the persons and companies interviewed prefer to remain anonymous. Therefore, no specific names are mentioned, but appropriate reference is made to the fact that the information is primary data.

Qualifications for Internal Auditing

The effectiveness of the internal auditing department depends upon the men who make up the department; thus, it is especially important that new personnel be selected with care. The modern internal auditor has come a long way from being a clerical employee, merely recording and checking for the business organization. When internal auditing was restricted to a verification activity in the finance area, anyone trained in accounting could do the job; the prime (and many times exclusive) prerequisite was a thorough knowledge of
accounting. As the job of internal auditing broadened to encompass more and more of the entire business organization and tended to lose its restriction to the finance area, the work came to be such that more than a knowledge of accounting was necessary in order to carry out all the functions of internal auditing. Actually, since internal auditing changed very rapidly in a few years, many auditing departments found themselves unprepared to render the quality of service that management requested. The education which fitted a person for a financial verification activity was not sufficient for an internal auditor in the ever-widening scope of activity; the thought and perspective of the "new" internal auditor had to be different from those of an "accountant." Of course, this is not to say that the modern internal auditor should not be trained in accounting. In fact, all four of the companies interviewed require a college degree, preferably in accounting or business administration, for a person applying for a position in internal auditing. A specialized accounting background provides the basis for the work of the internal auditor, provided he has the mind that can grasp the concept of the broader viewpoint and that he can and does equip himself with any necessary additional education.

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Education for contemporary internal auditing falls into an "... area lying midway between business administration at one end, and accounting at the other."² A candidate for the position of internal auditor should have a thorough background in accounting, but his education should have given him breadth of knowledge rather than a high degree of specialization in accounting. Since the present-day internal auditor is expected to appraise the various business activities from the point of view of management, it is necessary that he be thoroughly versed in all functions of the business and be trained in the principles and functions of management. Rather than studying one particular area exhaustively, the person preparing for a career in internal auditing should strive for a good general knowledge in as many areas as possible. It is not necessary that the internal auditor have highly specialized training in all areas of business, but it is essential that he have a good working knowledge of the purpose, operation, and objective of each business function³ and the interrelationship of all business functions;⁴ otherwise, he will not be in a position to form an intelligent appraisal of


³Cunningham, op. cit., 57.

the procedures and controls of the functions he is to audit. The internal auditor must see how the business concern fits together as an integrated whole before he will be able to render the variety of service expected. This phase of education may be neglected even in the college trained internal auditor. In many cases college courses are highly compartmentalized, and only the exceptional student grasps the interrelationship between the different courses that are prescribed in his curriculum. An expertly planned course in internal auditing in the accounting curriculum can do much toward presenting these interrelationships and giving the student a broader concept in his education.

The contemporary internal auditor is expected to move throughout the organization as "the eyes and ears of management," and in his appraisals and reports he is to use a reasonable degree of managerial judgment. More and more, the internal auditor is moving into areas which are not commonly labeled as accounting or finance, e.g., advertising, traffic, insurance, real estate, engineering, and industrial relations. This formidable task requires an unlimited breadth of knowledge. Although he is not expected to be an expert in all phases of a business (especially in the areas outside of finance),

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the internal auditor must possess enough fundamental knowledge of such areas as human relations, business communications, scientific controls, organization, industrial relations, and engineering so that he may cultivate the management point of view in making his appraisals. Also, this fundamental knowledge places him on "speaking terms" with the administrators and workers in each of the areas, and he may contact the personnel on common ground and more readily obtain the desired information.

In his job which requires him to come into personal contact with many of the employees of the firm, it is vitally necessary that the internal auditor develop contact ability as well as technical proficiency. In fact, few positions demand better contact ability than that of the internal auditor. In a paper which he presented, Earle H. Cunningham, General Auditor of General Motors Corporation, stated that internal auditing is at the top of the list of professions requiring good contact ability composed of the sum total of one's personality and human relations.  

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Personality is of utmost importance in developing this contact ability of the internal auditor. Personality in business refers to "... a type of individual whose sum total of characteristics makes the person a good representative; ... well received by those whom he or she contacts." In the first place, the internal auditor must command the respect of his associates and those he meets on audits. This demands, in addition to technical ability, unquestionable character and conduct both in business relationships and personal contacts outside the firm. The internal auditor must create a good impression—be friendly, tactful, neat, and pleasant. It is necessary for him to convey a businesslike manner, but one that is an attitude of service rather than of cold efficiency.

The internal auditor must possess imagination, initiative, and a pride of workmanship which will aid him in setting higher standards for himself on each assignment. During the personal interviews in the Baton Rouge area, the importance of these characteristics were continually repeated and given as a most important consideration in the qualitative appraisal of any person being considered for an internal auditing position. As one internal auditor so aptly stated, the person must be a "self-starter," and "able to go

9Ibid., 46.

10Lamperti and Thurston, op. cit., p. 403.
off on his own," rather than having to be told in detail what each step of his work shall be. This requires much more than a technical knowledge of debits and credits and accounting procedures; it demands an interest in the work, the imagination to see beyond the surface, and the personal motivation to follow up along any avenues feasible to investigate--in short, an inquiring mind.

The internal auditor must possess a temperament such that he can work on details for extended periods of time when necessary without losing interest. Persistency is necessary in the gathering of what may, in some cases, appear to be insignificant facts for the formation of a very significant conclusion. Unless the internal auditor uses perseverance to secure all pertinent data, his conclusions may be incomplete or even incorrect.

High on the list of personal requirements are common sense and sound judgment. Throughout his work the internal auditor must continually call on his "good common sense" in choosing between alternatives. No amount of technical knowledge can substitute for

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12M. B. T. Davies, "Training the Individual Auditor," The Internal Auditor, X (June, 1953), 56.

13Mathias, loc. cit.
the instilled characteristics of good common sense and sound reasoning ability.

The majority of the time, the internal auditor will not be working alone; he will be in contact with members of his own staff, with management, or with the persons from whom he is securing information. Therefore, the internal auditor must be a type of individual who can work well with people as well as alone. It has been suggested by an educator in the field of business that the most important phase in the formal education of any internal auditor is the study of human relations—"... the study of people not as automatons but as human beings having mind, body and spirit, each of whom possesses a certain dignity and should, therefore, be treated accordingly."14

The internal auditor must have a personality which reaches out to those with whom he comes in contact. The better internal auditor will be one who is a natural "mixer"15—-one who knows what is going on around him, both in the firm and in the world in general, and is able to carry on a fluent conversation with his associates and the employees in the areas being audited; an introvert will find himself

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hindered in many instances when searching for information. The typical internal auditor will encounter a variety of personalities in the normal course of his work, and he will have to discuss many things during an examination or investigation. In order to solicit the cooperation of his contact, the internal auditor must be prepared to discuss a wide field of subjects, some not even remotely related to auditing. Each person has his own favorite topic of conversation, be it sports, taxes, or government, and expects the internal auditor to have at least a conversing knowledge concerning it. R. K. Arthur, Chief Accountant of the Standard Register Company in 1952, felt so strongly about this that he made the following statement:

What we expect is for our auditors to be able to discuss to some extent fishing, hunting, basketball as well as who is going to be nominated at this year's conventions, the trend of taxation, the trend of the cost of living, and labor and price control regulations... a normal knowledge of various phases of these subjects.16

Being a good conversationalist will help immensely in establishing a cooperative spirit between the internal auditor and his contacts through providing an attitude of interest in the opinions of other persons.

Diplomacy is also necessary in creating good contact ability for the internal auditor. The internal auditor must approach any audit with

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16R. K. Arthur, "Training the Auditing Staff," The Internal Auditor, IX (December, 1952), 47.
the assumption that conscientious and intelligent work is being performed in the area and that his responsibility is to justify this assumption with factual information. If the internal auditor enters an audit with such an attitude, he will convey a spirit of service to all audit points and create an atmosphere of cooperation which would be impossible if he were to assume the role of a "watchdog" constantly searching for fraud. Diplomacy can also be used in calling attention to errors in a constructive manner to the person committing or permitting them, rather than in a tone which infers that the error was uncalled for.

Contact ability—good personality and skill at human relations—is an attribute which the internal auditor can spend a lifetime developing. Every internal auditor should be conscious daily of ways to improve his contact ability. In developing along these lines, the person has the difficult task of constantly evaluating all his personal actions, which is always more difficult than determining deficiencies existing in other people. Every new internal auditor should be assisted in every way possible by his superior in developing this important attribute for success in the accomplishment of his work.

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17Arthur H. Kent, "The Internal Auditing Staff," The Controller, VI (July, 1947), 335.
Sources and Selection

Personnel form the very foundation of any internal auditing department, and high quality performance of the auditing function can be provided and maintained only by careful selection of the employees entering the department. This first step—selection—is probably the most important, since the new men determine the future potential of the department.

Basically, there are three groups from which men may be selected for the internal auditing department: current college graduates, men experienced in other firms, and men in other departments of the firm doing the selecting. There are differences of opinion as to the best source of supply, influenced by the size of the department, provision of a training program, and the personal preference of the person in charge of selection. It is of financial importance that careful consideration be given to the source and the selection procedure, since a rapid turnover of new employees can be a costly situation for all concerned.

Serious consideration should be given to men who possess the various qualitative characteristics previously mentioned and who are

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19 Loc. cit.
presently located in other departments of the firm. These men will already be familiar with the company, its products, many of its policies and procedures, and some of the personnel to be contacted on audits, and, therefore, will require less training along these lines, particularly if the prior experience has been in the area of finance, than someone from outside the business. Another advantage of transferring to the internal auditing department from within the firm is the benefit to be gained by observing the employee for the period of time desired before offering the position in the department, recommendations for transfer being made by executives and administrative personnel and observation being accomplished by the audit staff in the course of its work. ①

One of the Baton Rouge area firms indicated that new recruits for the internal auditing department came almost exclusively from the accounting division of the firm specifically for the reason that the employee could be observed and his aptitude for auditing work determined prior to his entering the internal auditing department. Another firm also indicated that the accounting department is a definite source for their internal auditors, although it was carefully pointed out that this was not the only source.

It must be mentioned, however, that there may be a possible
disadvantage to transferring within the firm. The advantage of know­
ledge of the firm and the other items previously mentioned may
possibly be offset by the necessity of reorientation of viewpoint to
achieve the broad impersonal and impartial approach of the internal
auditor.21 In spite of the possible disadvantage of this source,
however, the survey conducted in 1957 indicated that 48 per cent22
of the respondents considered transfers within the company as a
principal source of personnel for the internal auditing department.
It has been suggested that the following departments be given prime
consideration as sources of personnel: accounting, financial, in­
dustrial engineering, and methods-and-procedures.23

Some excellent men can be secured from the internal auditing
departments of other firms and from the public accounting field. These
men probably lack the detailed knowledge about the firm, but they offer
a knowledge of auditing, valuable experience in a variety of situations,
and a broader view than someone trained in another department of the

21Robert R. Crawford, "Internal Auditing and Public Accounting
as Training for Administrative Personnel," The Ohio Certified Public
Accountant, VI (Spring, 1947), 13.

22The Institute of Internal Auditors, Internal Auditing in 1957

23Lamperti and Thurston, op. cit., 191.
firm. In a paper presented before a chapter of the Ohio Certified Public Accountants, Robert R. Crawford, Division Auditor of Delco Products Division of General Motors, indicated that, in his opinion, the best training an internal auditor can receive is to be gained in a public accounting firm, since this position offers such a variety of experience.\(^\text{24}\)

In the personal interviews one very interesting fact concerning this was noted. One of the large industrials contacted hires men for the internal auditing department almost exclusively from the public accounting field--always from the same firm, the firm that performs the external audit for the company. Reasons given for this practice seem sound enough: 1. The person has at least two or three years of varied public accounting experience. 2. The man hired already has "experience" with the company in a type of auditing capacity, and because of this is familiar, to some extent, with the firm, locations of departments, personnel, and past records. 3. Based on the first two reasons, the man may be placed in charge of a complex audit from the beginning. The recruit comes to the internal auditing department having had experience in working with the internal auditor on previous external audits—a unique way of gaining experience for a position, but one which has apparently worked out well for this

\(^{24}\)Crawford, op. cit., 13-14.
company. Of the four companies interviewed, only one does not hire from public accounting firms into internal auditing; this is the one previously mentioned which receives all internal auditing personnel from the accounting department.

Many companies recruit personnel for the internal auditing department from the graduating classes of colleges and universities. Many schools are now offering courses in internal auditing, and often these graduates bring a fresh approach into the department. However, it should be remembered that the person hired will have no experience in any area, and, therefore, training will naturally be slower and require closer supervision than in the previously discussed categories in which the recruit had experience. But in hiring a recent college graduate (in contrast to hiring a non-college graduate) the firm should generally be acquiring a person whose college or university background will aid him in developing into the type of personality for internal auditing. "Self-reliance, poise, good appearance and effective speech are generally more clearly established in a college graduate. . . . my experience in hiring and training individuals leads me to believe that in general the college man is better educated from a personality viewpoint,"25 were statements made by R. K. Arthur, Chief Accountant of the Standard Register

25 Arthur, op. cit., 42.
Company, in a paper delivered at the Mid-West Regional Conference of The Institute of Internal Auditors in 1952. None of the plants in the Baton Rouge area hire recent college graduates; one internal auditor voiced a personal opinion against the employment of recent college graduates, since it was his opinion that these people have an inflated idea of what to expect, which is not apparent in a person with any degree of experience.

When practicable, it would appear to be desirable to have a blending of all three of the above categories in order to effect a well-balanced staff. People from other departments in the firm, public accountants and/or internal auditors from other firms, and a few recent college graduates, working together, should be able to learn a great deal from one another and, merging their knowledge and efforts, move toward the accomplishment of contemporary internal auditing. Two firms interviewed attempt some sort of this mixing of men from different sources, as they are the two firms which employ internal auditors from more than one source.

None of the firms interviewed used any examinations to test an applicant's academic knowledge of internal auditing, accounting, or any other area. Three used standard I.Q. and psychological written examinations, one receiving a written appraisal of the results of the examinations from the company psychologist. It would appear desirable for companies in their selections of proper individuals to
make use of the series of examinations prepared by the American Institute of Certified Public Accountants. The Level II Achievement Test is designed to test the accounting and auditing ability of persons with a college education (or its equivalent) in accounting. Level I Achievement Test is available to test accounting knowledge after only one year of accounting. An Orientation Test has also been prepared to determine the aptitude for business of men with no accounting education or experience. The Strong Interest Test is designed to determine the occupational interest of the person being tested. These examinations available to the internal auditor could be used as valuable guides in the selection of qualified and proper staff members.

As has been previously indicated, modern internal auditing requires a broad and varied knowledge, and this is evidenced in the amount and type of experience required of an applicant for consideration in the internal auditing departments of the companies interviewed in the Baton Rouge area. Experience required by these companies is summarized as follows: Company A--two to three years in public accounting or industrial accounting on a higher level or internal auditing for another firm; Company B--two years (type not

specified); Company C—one year as junior accountant with a public accounting firm or two years of diversified accounting with a large industrial firm; Company D—transfer in two accounting departments within the firm before coming into the internal auditing department. One interesting fact is that the chief internal auditor at one of the Baton Rouge plants entered the internal auditing department with five years of experience in time study and as superintendent of the job evaluation department of the plant; his accounting knowledge was obtained by correspondence study.

Training of the Internal Auditor

Having accomplished the task of selecting the new member of the internal auditing department, there is the job of grooming this recruit into an efficient employee of the organization. Regardless of his background, any new man coming into the internal auditing department will need some type of orientation to his new job. While many companies do not have detailed, formal training programs (probably because of the variety of background and experience of the new men), all companies must have at least some form of preliminary introduction and training for new employees, and either the chief internal auditor or a qualified member of his staff should be specifically designated as supervisor of all new men during this orientation or training period. Careful thought and consideration should go into
the selection of the person to be responsible for planning and conducting this orientation period. The person in this capacity must have the time and energy to devote to such a program without losing interest. This may be the sole responsibility of the supervisor, or it may be in addition to his other duties if there are not enough recruits to warrant full devotion of his time. However, it is most important that the supervisor of the program not be overloaded, with the training program as a mere "sideline" to his regular work. The supervisor should be able to spend as much time as is necessary in order to plan and conduct the training systematically and efficiently so the greatest benefit may be obtained by the company and the individual being trained.

Orientation

When the new employee reports for work, he should be carefully oriented to his job and introduced to the men with whom he will be working. It is important that the new man be made to feel "at home" from the beginning. The chief internal auditor or the person in charge of internal auditing at the particular plant location should certainly talk with any new recruits. The company organization and the place of the new employee within this organization should be explained immediately. This initial indoctrination period is an excellent time to discuss such things as company history, company operations,
company products, and company policies.\textsuperscript{27} Other topics to be covered might be responsibilities and standards of the internal auditing department, management expectations of the department, and the professional life of the internal auditor.\textsuperscript{28} This is the time to acquaint the new men thoroughly with the company layout and organization in general and with the internal auditing department specifically.

Only one of the Baton Rouge plants has what could be called a formal orientation program. This particular company has what they term a "formal indoctrination period" which lasts for five weeks. This is a carefully planned program to familiarize thoroughly the new members of the internal auditing department with the Baton Rouge plant. First, there is a talk on the Baton Rouge industrial complex (in Baton Rouge several plants are constructed on adjoining property which makes a virtual maze of industry) and walking tours of the plant are conducted. There is a series of lectures on employee relations, research and development, and safety. In addition to these, the new employees spend from a few hours to three days (the length of time being specified in each case) observing and studying

\textsuperscript{27}P. D. Lipscomb, "The Selection and Training of Internal Auditors," \textit{The Internal Auditor}, I (September, 1944), 32.

\textsuperscript{28}Arthur H. Kent, "The Selection and Development of an Internal Auditing Staff," \textit{The Internal Auditor}, IV (March, 1947), 50.
the processes in each of the following thirteen divisions: audit, purchasing, tabulating, industrial insurance, fixed assets, factory ledger, accounts payable, traffic, payroll, cost, production planning, data research, and engineering (a project is actually followed through the engineering process). The recruits spend sufficient time in each division to obtain a general understanding of the functions and processes of each division and to understand the relation and application of internal auditing to each division. They are introduced to the appropriate employees in each division and, in general, are made to feel "at home" in their new environment. The new employees finish the "indoctrination program" familiar with people, places, and locations which, it is hoped, gives them a feeling of belonging to the company organization and a general idea of the work expected of them.

From all indications the whole program seems well organized and certainly the most extensive of any found during the interviewing.

Another firm interviewed indicated that the whole training program covered a period of several weeks, but much less time was spent on general orientation and more time was devoted from the beginning to the coverage of actual internal auditing material. The program is certainly informal with no specified amount of time to be spent on any phase of orientation. A short period of time is devoted to having the new employee become familiar with people, operations, and the general type of audit he will be expected to conduct. There
are also discussions of the various written audit programs the recruit will be expected to cover—encompassing any angles, procedures, and key points deemed necessary. This is the company that hires only from the public accounting firm which performs the external audit, and this probably accounts for the lack of extensive general company orientation. The recruit will already be familiar with the company, people, and locations from his performance or participation in the performance of previous external audits for the company.

The third company is particularly interested in introducing the new recruit to the accounting personnel, and after this, the recruit broadens his contacts "as the situation presents itself" and as new projects develop. There are some short discussions of what internal auditing should be, how to approach people, objectivity, and the job of the internal auditor, but the department makes no pretense of having any sort of formal orientation program.

The fourth company (the one which hires basically from its own accounting department) stated that a new recruit already knows the finance personnel and that further introductions are made as needed. Also, in this company there are a few short discussions about the philosophy and the job of the internal auditor, but no extensive indoctrination period. Of course, since the new recruits in the internal auditing department come from within the company, it is expected that the new employees already know the general company information which
would be necessary to distribute to an employee coming from outside the firm.

During this orientation period before receiving any audit assignments, the new employee in the internal auditing department should receive some specific indication of the work which will be expected of him. This can best be accomplished at this point by having him read general company material, instruction manuals, and previous audit reports. These reports should not be read for detail but for information as to the type of reports prepared as a result of the auditing effort. He should be given the opportunity to ask questions necessary to clarify procedures and give him the information and confidence needed for accepting assignments. This reading should be kept at a minimum, as too much reading at this time will seem intangible and discouraging to the new employee. Only two of the companies in Baton Rouge had any kind of introductory reading material generally available for new employees. One of these companies provides first a brochure about the company and its product and how the two got together and developed. Then the new employee is expected to digest thoroughly the Controller's Policy Manual followed by other detail manuals pertaining to the

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30 Lombard, op. cit., pp. 74-75.
control divisions, e.g., *Fixed Asset Manual* and *Branch Reporting Manual*. Other reading is done as jobs are assigned. The second company had no general company reading material but did have the *Auditing Department Manual of Procedures* and a collection of *Divisional Operating Procedures* which the new internal auditor was required to digest. The other two companies had no suggested or required company related reading material. The new men are told of a few "textbook type" books which are available on internal auditing, and the inference is that the new employees will use these as reference books, reading them when the knowledge is needed.

**On-the-Job Training**

Most companies have discovered that the successful training program is based on the old adage "experience is the best teacher." Generally, trainees are rotated among various audit assignments (attempting a coverage of all assignments before repeating) while under the close supervision of an experienced auditor and the training program supervisor. Placing the trainee as an "assistant" to an experienced person in these various assignments and having him actually work on audit assignments will give him a sense of accomplishment in his work, remove to a certain degree the student-teacher relationship, and provide an atmosphere of two people working together on
In these various assignments the new employee will gain something from each of the more experienced auditors, e.g., their different characteristics, approaches to the audit and to the people with whom they come in contact, and these will fit into the pattern of ability, experience, and personality that the new employee is building for himself. The persons to whom the new employee is assigned must be impressed with the fact that they are acting as teachers; the recruits work with the older auditors in succession for the purpose of learning, and these senior men must fulfill their obligation to teach. Infinite patience is required in explaining methods and approaches again and again, slowly enough to be grasped by the new auditor; questions must be answered patiently and thoroughly.

If the program is designed properly, each succeeding assignment should give the new employee more experience, more knowledge, and possibly more responsibility. As the new auditor passes through the series of assignments under experienced auditors, he will become familiar with the methods and procedures of internal auditing, the manner of securing information, and the report writing procedure as

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31Ibid., p. 76.

32Kent, "The Internal Auditing Staff," op. cit., 334.

33Arthur, op. cit., 44.
the culmination of auditing work. All of these will be invaluable to the new employee when he is given his first assignment with complete responsibility.

In all of the companies interviewed, there were programs of informal rotation, but in no case was there a system of planned, scheduled movement. All indicated that there was rotation only as jobs came open. One internal auditor said that the criteria for rotation were ability, potential, and the need of the company. In another company men are rotated to assist in taking care of a backlog of work and to cover the jobs of men who are on vacation or ill. In some cases this movement is not considered a rotation procedure but a change of jobs, and in a few instances there is rotation from internal auditing to the accounting department—the person may stay in accounting or come back to the internal auditing department. This procedure of rotating through the accounting department does not appear advisable, as this could do much toward removing the independence and objectivity of the internal auditor. The person could conceivably at a later date be auditing some of his own work done while in the accounting department.

Reports on Training

In order to follow the progress of any trainee, there must be a procedure for reporting back to the training program supervisor. The
person to whom the trainee is assigned on each audit should issue a report on such items as:

1. Knowledge of the Job
2. Thoroughness
3. Contact Ability
4. Ability to Write
5. Alertness
6. Production
7. Potential for Development

Time spent on each assignment and type of work covered should also be reported. It would also be advisable to secure a report from the trainee after each assignment, obtaining his remarks concerning the training program and its administration at that particular phase. In order to secure the information desired, all reports should be made on prearranged forms to the extent practicable, but, of course, space should always be allotted on the form for the writing of comments, appraisals, and other information not specifically called for on the printed form. All reports should be addressed directly to the training program supervisor so he may ascertain the effectiveness of the training program, determine deficiencies and the need for more training, and

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36 *Loc. cit.*

better co-ordinate the training program of each new employee.

**Staff Meetings**

As the trainee rotates from assignment to assignment, a valuable part of his on-the-job training is in participation in discussions preliminary to the preparation of the audit report on each job. This cultivates a sense of "belonging" on the part of the new auditor and offers a feeling of satisfaction in seeing his work form a part of the report to management.\(^{38}\) The trainee should be expected and encouraged to offer comments during these discussions. All of the internal auditors interviewed indicated that post-audit conferences are conducted in which the job, the working papers, and the findings are discussed before preparation of the final report. All persons concerned with the audit are encouraged to make whatever statements and remarks that they consider pertinent and necessary for the discussion.

Periodic conferences and group discussions with the program supervisor should prove to be of benefit to both the supervisor and trainees. If carefully planned, these meetings should serve at least three purposes: (1) the gathering of trainees will give them the opportunity to discuss their experiences and knowledge and to exchange ideas, (2) the meeting should offer opportunity for the program supervisor

\(^{38}\)Smith, *op. cit.*, 27.
to give further instructions, and (3) conferences will enable the supervisor to maintain a personal contact with each man so that his progress may be more closely evaluated.\(^{39}\)

The above meetings may well be held in conjunction with the general staff conferences of the internal auditing department. Within the general staff meeting program, the trainees would have the opportunity of being together and with the program supervisor, as well as the opportunity to participate in many of the general staff meetings and discussion groups. Some companies have followed, as a part of their training program, the procedure of having different persons make oral summaries of required readings at the regular staff meetings.\(^{40}\) Participation in the presentation and in the discussions at the staff meetings should help keep the trainees current on information in the area of internal auditing, as well as give them a chance to develop their speaking ability and show their progress before a group.

Of the companies interviewed in the Baton Rouge area, only one has regular staff meetings of any kind; the meetings are not regularly scheduled, but are generally called every two weeks. All members of the staff attend, and discussions usually center around a consideration of progress, planning, and future assignments.

\(^{39}\)Lamperti and Thurston, \textit{op. cit.}, p. 405.

\(^{40}\)Kent and White, compilers, \textit{op. cit.}, p. 34.
Another internal auditor indicated that general staff meetings were held, but only infrequently and when needed. The third internal auditor disclosed that one national staff conference of all the internal auditors in the company had been held in the history of the company, but no meetings have been held in the Baton Rouge area. Indications were that the national conference was a most beneficial conference with good participation and speakers from both internal auditing and areas of the company related to internal auditing. Apparently the company has no plans for conducting any more of these national staff conferences, which leaves the regional internal auditor in the Baton Rouge area without contact with his colleagues. The fourth company has conducted no form of staff conferences for the internal auditing department.

Further Education

New employees should be strongly encouraged to take advantage of any special courses or conferences offered by the company which might be of value to them in their work. Several larger companies have formal, scholastic programs which must be successfully completed by the trainees after work hours before they are placed in a permanent position.\(^{41}\) If such an educational program is not provided

\(^{41}\)Horn, *op. cit.*, p. 23.
within the company, it is necessary for the training program supervisor to know what is available outside the company and to advise the trainees in selecting the professional courses which will increase their potential. Night school attendance should be recommended, particularly if a new employee's formal education is lacking at any point and a college or university is accessible. All the Baton Rouge companies encourage continuing formal education at a college or through correspondence study, if it will improve the potential of the employee. Three of the four companies have educational assistance programs whereby they refund a portion (50 or 75 per cent) of the costs incurred in securing additional formal education; the fourth company provides no educational assistance.

Professional Organizations

Attendance and participation at professional organization meetings of the Institute of Internal Auditors, American Institute of Certified Public Accountants, National Association of Accountants, and the State Society of Certified Public Accountants can be a source of training for the new as well as the older members of the department. Association with members of the profession from other firms can provide information and ideas not obtainable from books and day-to-day work in the firm. This type of association should help to keep the internal auditor informed as to what is going on in the profession in general and in the
Baton Rouge area specifically. Only two of the companies inter­viewed provide any sort of refund of costs incurred as members of a professional organization; one company provides 100 per cent refund on costs incurred as a member of the American Institute of Certified Public Accountants, while the other company covers only the cost of meals at a professional organization meeting. There is no chapter of The Institute of Internal Auditors in Baton Rouge.

The Internal Auditing Department as a Training Ground for Future Administrative and Executive Personnel

An internal auditing department which serves to aid constructively the management of the firm in its regular functions should serve management as a source of personnel for vacancies in positions of managerial responsibility. The personnel in the internal auditing department receive a type of training that would take someone in another department much longer to acquire. In the first place, the nature of the work of the internal auditor requires him to have a wide scope of knowledge. His work probably carries him into every de­partment of the firm, and he accumulates a vast knowledge of the operations of the company, the policies throughout the company, and even the problems confronting the company.\textsuperscript{42} He has been

\textsuperscript{42}Brink and Cashin, \textit{op. cit.}, p. 23.
accustomed to thinking with the mind of management, and his approach to his work has been with the viewpoint of a manager.

Furthermore, the work of the internal auditor causes him to make contacts throughout the strata of management, and, therefore, he is in a position to be able to impress a number of people throughout the organization with his abilities. It then becomes natural for management to consider the Internal auditor for a managerial position if they have been favorably impressed with his work and potential. Two of the companies interviewed indicated that the internal auditing department is a prime source of personnel for financial supervisory positions in other areas; the other two internal auditors said that no special consideration was given to personnel in the internal auditing department in the selection of men to fill managerial positions.

The internal auditing staff has been called "the best informed group in the company organization."43 This group is in a position to observe errors in management as well as the methods employed in successful management. This peculiar type of training has caused the internal auditing department to become more and more a source of supply of promising young men to move higher in the organization of the business, assume greater responsibility, and better serve the firm.

43Crawford, op. cit., 14.
CHAPTER IV

OPERATIONS AUDITS

Over the years internal auditing developed in the financial area to somewhat parallel the auditing standards and procedures followed by the public accountant in his outside audit of the firm. Financial accuracy, financial position, and consistent conformity with generally accepted accounting principles were the chief, and many times exclusive, concern of the internal auditor. Internal auditing developed rapidly in the financial area to encompass an audit for determining the adequacy and effectiveness of the various financial controls, such as the system of internal control, the accounting records, and the accounting procedures.

It was only natural for internal auditing to expand in the financial area. In the first place, financial audits have always been associated with accounting, and internal auditing evolved from an accounting background. Secondly, the financial audit is historical and thus an examination and evaluation of past occurrences rather than a more difficult evaluation of future proposals. Also, the bases for the financial audit—the accounting system and the system of internal control—are the creations of management for the control of financial operations. Management frequently considers past
compliance an indication of the success of the system.¹ Financial internal auditing was thus readily accepted and encouraged to expand investigations in the financial area almost immediately.

Growth of internal auditing outside of the finance area was certainly not so rapid. It has only been in recent years that any research and application of internal auditing has been made in the field of operations. It was the impression of many that the internal auditor—so typically associated with accounting and finance—would be moving beyond the scope of his responsibilities if he investigated the actual operations of the firm. The objection was that the internal auditor, being well versed in accounting, was qualified to conduct financial audits, but in the operational aspects of the business he was not an expert and therefore incapable of conducting an effective audit in this area.

**Brief Distinction between Financial and Operations Audits**

Actually, operations auditing is not a new kind of auditing, entirely unrelated to the methods of the more familiar financial auditing. A lack of understanding of operations auditing has resulted

in the opinion of many persons that operations auditing is something entirely new, different, and unrelated to financial auditing. Indeed, instead of being a new type of auditing, operations auditing is merely a new area of auditing having the same objectives as financial auditing with the basic difference being that one deals with financial controls and the other with operational controls. Thus, the subject matter under review is somewhat different, and a different basis for appraisement may be necessary. For example, the audit of the system of internal check in financial auditing calls for the checking of compliance with the system as established; whereas, in the audit of operations the internal auditor is checking for the accomplishment of objectives as established by management.

It is, in fact, difficult to separate entirely financial and operations internal auditing into two distinct categories, since in many financial audits the line is crossed into operations in performing the necessary verifications for the financial audit. For example, an audit of payrolls (a financial audit) leads to a check

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3 Charles N. Inman, "Managerial Auditing of Operations," *The Internal Auditor*, XI (June, 1958), 44.

4 Seiler, *op. cit.*, 11.

of the incentive pay which leads to a review of the time studies which support the incentive pay, and the internal auditor having begun on a financial audit ends up involved in the operational aspects of the business. Also, an audit of vouchers payable leads to a check of materials vouchers which leads to a check of materials requisitions, and the internal auditor again ends up in operations.\(^6\) Therefore, the internal auditor in following through on the verification of all aspects of financial audits will automatically be led into an audit of a great many aspects of operations, and it is difficult to draw a line separating financial and non-financial auditing. Actually, it is by this procedure of keeping a tie with familiar financial auditing and using it as a base that an auditor inexperienced in operations auditing can begin to broaden his scope and move more and more into the area of operations.

When the internal auditor shifts to the field of operations auditing, he is the representative of general management and not merely financial management.\(^7\) There is more involved than the financial controls of financial auditing, and the internal auditor must remember that in operations auditing it is necessary that he assume the role of a direct representative of general management

\(^6\)Seiler, loc. cit.

\(^7\)Loc. cit.
with a broader outlook and audit scope than is required for a financial audit under the direction of financial management.

### Effective Auditing Accomplished by Non-expert

It is true that the internal auditor must be well qualified in accounting, as a great part of his work is in this area. However, to associate him completely with only this part of the business activities is not according to the contemporary concept of the internal audit function. Modern internal auditing is more than accounting, but certainly it cannot be expected that the internal auditor be an expert in every area that he audits.

### Auditing Based on Controls

For the type of evaluation performed by the internal auditor, expertness in operations is not necessary. There is one common thread running throughout the business organization from the board of directors down to the lathe operator and from the receiving department across the lines of the organization chart to the sales department. This common thread is the element of control. There are many forms of control among the various management levels and a variety of controls within each level. First, each level of management must exercise control over itself and over the level immediately below it in order to build an effective system of control over the
business as a whole. No unit of a business should function independently without some sort of established controls to direct the unit in fulfilling its function within the framework of the total business organization. These controls, established by management, serve as guides or, if necessary, restraints in steering each functional unit of the business toward effective performance of its objective within the total plan of the business.

As has been said by Donald E. Dooley, one of the directors of the Institute of Internal Auditors: "The audit of operating departments is simply the application of our regular techniques and our analytical abilities to widened areas of operations." Mr. Dooley sets forth two broad objectives of internal auditing, whether it be labeled financial or operations internal auditing:

A. Examination of the applicable control structure, and

B. Use of auditor's general knowledge of company operations in examination of the relation of departmental controls and operations to general company policies and to other departments.

These two general objectives do not confine the internal auditor to any particular area, except the area of controls which should be present in every facet of the business, in the production department.

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8 Dooley, op. cit., 60.

9 Ibid., 47.
as well as the accounting department. Thus, the internal auditor is not expected to be an authority in the actual operations of all the areas which he audits, but in the controls applicable to these areas.

Advantages of Non-expert

Actually, in many ways, it is better that the internal auditor not be an expert in operations. The man on the job each day, the expert, knows the job so thoroughly that it has become routine. He may become satisfied with the status quo and not consider changes which could be made to provide better control and/or a better procedure for accomplishing the task. The internal auditor, however, comes into the audit of operations with a fresh approach, and his lack of complete knowledge of technical operations can actually be a valuable attribute by causing him to ask penetrating—and sometimes revealing—questions concerning the operation. It may be found that long-continued use and accepted practice have caused many processes and procedures to be continued without any consideration as to possible changes. For example, basic questions were asked by a specialist in nuclear physics concerning the blast furnace process in Republic Steel in trying to determine the application of atomic energy in the steel industry. Surprisingly enough, in such a large and developed industry, many of these questions about the basic manufacturing process went unanswered by the experts. This appears to
illustrate the fact that no area of a firm is beyond penetrating, constructive questioning as to the processes involved and the procedures followed. Also, it very definitely points up the fact that a non-expert is sometimes able to take a fresh look at the situation and pose questions which actually set the experts to thinking.\textsuperscript{10}

Another advantage of the internal auditor over the expert is his constant move from one area to another or even from one plant to another in making his various audits. Moving about as he does, the internal auditor encounters similar problems in the same area in different plants or in different areas within the same plant. He has the opportunity to observe a variety of approaches to the solution of the same or a similar problem, whereas the expert is confined in his own department.\textsuperscript{11} Also, the roving internal auditor has the opportunity to observe the chain reaction of problems through the different areas of the company; in his unique position, he is familiar with tie-ins between departments.\textsuperscript{12} Problems sometimes arise which affect not only the operations of a particular area but of every area down the line through the business. The internal auditor, in his moving about, can

\textsuperscript{10}D. T. Noakes, "Auditing Techniques," \textit{The Internal Auditor}, XIV (June, 1959), 84-85.

\textsuperscript{11}Allen Howard, "Internal Auditing in a Large Corporation: A Constructive Approach," \textit{Accounting Papers of the Seventh Annual Conference of Accountants} (Tulsa, Oklahoma: The University of Tulsa, 1953), p. 66.

\textsuperscript{12}Ratliff, \textit{op. cit.}, 10.
foresee reactions in other departments, whereas this is generally beyond the concept of the expert confined to a particular specialized area.

It is important to emphasize at this point that internal auditing serves management in a staff capacity rather than in the line organization. This is significant to note since, being in a staff position, the internal auditor—a non-expert in technical operations—is not expected to decide on the correctness and effectiveness of any particular operational process. Being outside of the line organization of the business, he is not in a position to give instructions in the departments which he audits. The internal auditor makes his audits and reports his findings, but enforcement is left up to the line organization. Thus, the internal auditor has not usurped the authority and responsibility of the experts in deciding upon the feasibility of his report and recommendations.

Securing Cooperation

Ordinarily, the broad, general limits of the responsibility of the internal auditing function are settled by management upon the establishment of the organization. These limits become more clearly

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defined over the years partly by additional statements from management and partly by the development of customs relating to the work of the internal auditor in the particular firm. All of the internal auditors in the Baton Rouge, Louisiana area indicated that they were definitely encouraged by management to move into the non-financial areas, but only three of the four said that they had received an adequate degree of "backing" from management when they moved outside of the financial area. The fourth auditor was quite hesitant, saying that the situation was getting better, but that in some cases it was still a matter of opinion as to the adequacy of support by management.

In any case, expansion into the audit of operations must be handled carefully and with finesse. Only one of the auditors interviewed indicated that he had received complete cooperation from the non-financial personnel. Another auditor said that, in general, he had been well received and stated that most operations personnel demonstrated a lack of understanding of the internal audit since this was their first contact with the internal auditing function. The other two auditors revealed that some problems had been encountered--one indicated that he did not expect to be received as well in operations auditing as in financial auditing.

Certainly, it is imperative that the supervisors of the operations departments being audited be informed of the nature and objectives of the audit. A simple discussion in non-technical terms
concerning the nature and purpose of the audit should help immensely in gaining the approval, cooperation, and assistance of the supervisory personnel in operations. If approached with an audit program that is constructive and helpful and not simply a critical review, the personnel of operations areas will usually respond with helpful cooperation. Better acceptance will be obtained if the internal auditor "sells" his audit to operations rather than relying on an edict from top management to gain the cooperation of line personnel.

Approach to Operations Audits

When planning an audit of operations, it is important that the auditor consider the timing of the audit. The audit should be conducted at a time which will minimize the disruption of the normal flow of work through the department. If at all possible, the auditor should avoid conducting an audit during the peak work periods, insofar as this can be accomplished without conceding the objectives of the audit. The reason for this procedure can be seen by the application of good common sense. If the auditor performs the audit at a time when the operations supervisor is not rushing to meet deadlines, he will naturally find a better spirit of cooperation. For the accomplishment of the best audit, especially in the field of operations,

14 Dooley, op. cit., 54.
the auditor needs the cooperation of the personnel being audited, since there are many questions—certainly more than on a standard financial type audit—which the auditor will have to ask concerning the department during the course of the audit. By choosing the most opportune time for the department being audited, the auditor demonstrates a cooperative nature and thus commences his audit in an amicable atmosphere facilitating its performance.

Determination of Objectives

Before the auditor is prepared to begin even a preliminary investigation in the department to be audited, he must know the objectives which management has set for the particular department. In some departments these objectives are clearly defined by management and, therefore, easily determined by the internal auditor. For example, it might be said that the objectives of the production department are to produce the highest quality product possible at the lowest cost and in the shortest time.\textsuperscript{15} The objectives are tangible; success in their attainment can be counted and reported. The objectives of the public relations department cannot be so easily determined. The products of this department are intangible services contributing to the profit as a whole, but it is difficult to set

\textsuperscript{15} Selelter, \textit{op. cit.}, 12.
measurable objectives for this type of department. The internal auditor will have to spend some time in conference with the members of management to whom the different operations supervisors are responsible so that he can determine what is expected from the departments by management. The determination of objectives will be especially difficult for the first audit of many departments since the internal auditor will have the task of determining the expectations of management and the standards against which to match performance. These should be written down, because in doing so the internal auditor will tend to be more specific rather than continuing to work from hazy ideas.

Gathering of Pertinent Background Material

Once the objectives of the department are determined, the internal auditor may gather relevant background information concerning the specificities of the department to be audited. It is at this point that all details concerning the organization and operation of the department should be noted and studied carefully. This is the time for the internal auditor to study the department with the idea of acquiring a working knowledge of this particular phase of operations. Being in unfamiliar surroundings in an operations department, the internal auditor will have to spend more time in preliminary study than is necessary on an audit of a familiar area of finance. In each
personal interview conducted in the Baton Rouge, Louisiana area it was brought out that operations auditing requires a more extensive preparation period than does financial auditing. It was noted by those interviewed that financial controls are generally codified and well known, while non-financial controls are not nearly so clear; this lack of clarity of non-financial controls results in the necessity of a far more detailed study of organization, duties, and procedures in the operations departments. It was also brought out that, since in the operations departments the personnel are not, in general, conscious of figures, the internal auditor will require a longer period in which to secure information and develop material.

During this period of background study, the internal auditor must determine such information as the following: the organization structure of the department, the duties and responsibilities of the members of the department, the flow of work through the department, and the nature of all reports prepared for use within the department or to be issued from the department, when they are prepared, and who receives them. One author has stated that this process of familiarization very succinctly in the following four questions:


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16 Inman, *op. cit.*, 50.
There are several avenues of research which the internal auditor may follow in determining this preliminary information. One of the first things that he should always do is have a talk with those in charge of the department to be audited. This introductory discussion is most important since it sets the stage for the complete audit. If this is the first audit of this particular phase of operations, the internal auditor will be learning about the operations, and the operations personnel will be learning about internal auditing. It is imperative that this meeting be devoted to a time of understanding each other's position as well as a time of information exchange. The type of audit and the objectives of the audit should be explained in terminology which will be understood by the operations personnel. This discussion period offers one of the best opportunities for the internal auditor to gain the cooperation of the operations personnel, but this cooperation will not be forthcoming without an understanding of the purpose and objectives of the internal audit. Also, during this preliminary meeting the internal auditor should be able to gain much information about the particular area of operations, and some of the general questions mentioned above will be answered in the course of conversation. To obtain the necessary specific answers, the internal

17 F. E. Mints, "Operational Auditing," The Internal Auditor, XI (June, 1954), 35.
auditor should follow up this initial group meeting with individual discussions with members of the operations department.

Further information can be obtained from the written material concerning the department—department manuals, job descriptions, and reports from the department. Before starting the actual audit, the internal auditor should also take a tour of the department and observe the work being done.

In this gathering of information the internal auditor should attempt to cover and absorb as many phases of the departmental operations as is possible. He is, of course, in the position of learning the operational processes, and the more he can absorb at this time, the more competent he will be to perform the actual audit. Throughout this preliminary stage he should be constantly alert to means of control within the department. He should place himself in the position of the person responsible for the department and attempt to answer the overall question: "If I were responsible for the management of this project, what would I want to know about it?" This question should be the concern of the auditor throughout the audit from the first preliminary planning to the writing of the report. It is important that the auditor in a non-financial setting realize that his responsibility is to general management which calls

\[18\] Ibid., 28.
for a broader audit coverage since the appraisal is not limited to a financial approach. Thus, in every stage of the audit the auditor should have an interest in every operation in the department and not just that which has what is normally thought of as a financial application. In other words, the auditor should become absorbed in the work of the particular department to the extent of learning all that he can about its operations.

Pride should never stop the internal auditor from asking questions during this familiarization stage. The internal auditor is not expected to come to the operations departments with a complete knowledge of the operations. It is during this period of time that the internal auditor must ask questions and listen attentively to answers in order to assimilate all the new facts with which he is confronted. This period is his preparation for the work of the audit, and he should never try to convey the impression that he knows more than he actually does. It is much better to admit a lack of knowledge during this preliminary gathering of data than during the audit, and, too, the more facts gathered at this time, the more complete can be the audit.

Determination of Scope

Having performed the initial survey and observed the operational control problems, the internal auditor is in a position to outline the
tentative scope of the audit to be performed. Of course, it will not be possible to write all the various details to be performed on the audit, but the internal auditor should be able at this time to define some of the general areas of the audit coverage and the limitations of the review. It is important at this stage that the internal auditor actually write down an outline, as detailed as possible, of the audit program. Naturally, the outline should be left open for modification and extension, but it should serve to focus as clearly as possible the general objectives of the audit. Even in situations where it is possible to write only a brief and sketchy preliminary outline, this should be done, since the very act of trying to formulate and focus the review to be made may in itself center and channel the auditor's thoughts, bringing forth new areas and means of investigation.19 Particularly is this outline helpful in an unfamiliar area of operations. As the detail of the audit is conducted, this general outline will serve to remind the auditor of the general objectives and hinder him from dwelling on tangents which will not contribute to the effectiveness of the audit.

Of course, the internal auditor must not consider his outline of scope to be fixed and not subject to change. As so well stated by Arthur H. Kent: "His mental eyes are not to be immovably focused

19Arthur H. Kent, "Internal Auditing is an Appraisal Activity," The Internal Auditor, XVI (September, 1959), 41.
on a white line in the middle of the road. They must glance from side to side; and his mental antennae should receive messages from various directions.\textsuperscript{20} Therefore, it should be said that the purpose of this outline of scope is to guide the internal auditor, and it should not be permitted to stifle his imagination and initiative.

Use of Operations Personnel on Audit Staff

In the audit of operations, the internal auditor may find it advantageous to have the assistance of some of the personnel of the department being audited. This type of assistance should have two favorable results: (1) the personnel would provide the internal auditor with the technical assistance he may need while conducting the audit, and (2) with operations personnel working closely with him on the audit, the internal auditor may use psychology to his advantage and have the personnel of the department locate their own weaknesses.\textsuperscript{21} By knowing the technical aspects of the department, the operations personnel, when the auditor explains the controls necessary for the department, may actually locate weaknesses which might have gone unnoticed by the internal auditor. This "joint effort" by the internal auditor and a few operations personnel can lead to a

\textsuperscript{20}Kent, \textit{loc. cit.}

\textsuperscript{21}Seiler, \textit{op. cit.}, 16.
better understanding of the nature and purpose of internal auditing and to a realization that the internal auditor is there to help and not merely to act as a critical "watchdog."

Details Requiring Special Attention in Operations Auditing

As previously discussed, both financial and non-financial internal auditing are primarily concerned with the established system of control, if any. Thus, both financial and non-financial audits may be conducted by a similar general procedure of analyzing existing controls (or determining a lack of control) and checking compliance with these controls. However, there are a few specific items which will require special attention in operations audits.

First, in requesting information and records for inspection, as a general rule the internal auditor should channel his requests through the supervisor of the department. The supervisor will be able to supply the information himself and obtain the needed records for presentation to the internal auditor, or he is in the best position to designate which person in the department has the time available and will best be able to assist the auditor in locating the information which he needs with a minimum of disruption in the flow of work through the department.22

22A. J. Gregory, "The Internal Auditor--Friend or Foe?" The Internal Auditor, XV (December, 1958), 53.
Of course, this procedure should better the relationship between the operations department supervisor and the auditor. By working through the supervisor rather than going privately to an individual employee who may be heavily loaded at the time with jobs which must be completed, the internal auditor assumes the role of being cooperative and concerned with the work of the department as well as with his own job of auditing. Also, by working through the supervisor, the auditor conveys the attitude of working with the supervisor as opposed to the impression of a detective looking for errors.

In following this procedure, however, the internal auditor must be careful not to allow the supervisor to steer him from the objectives of the audit and thus weaken its effectiveness. Also, of course, the internal auditor may encounter operations supervisors who will not cooperate in this manner. If this occurs, then the auditor must resort to the alternatives of either contacting the supervisor's superior to encourage cooperation or securing the information he needs himself.

In general, internal auditors have learned that it is necessary for them to set an example in being neat and orderly during the course of an audit. Since the internal auditor will usually observe and report on the department as to the condition of the premises and records kept, it is imperative that he be an example for the operations department employees and at least leave things as he
finds them. In conducting the audit, the auditor will probably have occasion to examine correspondence and files; he should certainly leave these in good order.

When auditing operations, the internal auditor must channel his criticism carefully. As is true with financial audits, the internal auditor should never criticize an employee directly and certainly he should never talk to an employee about the mistakes of another employee. If a situation which warrants criticism is discovered, the internal auditor should discuss the matter only with the supervisor of the employee involved and leave any criticism or disciplinary measures concerning the employee to the line supervisor. The auditor must work to acquire a reputation of being able to keep things to himself, as this type of approach will encourage the employees to feel free to discuss their problems with him.24 Also, as previously mentioned, the internal auditor serves in a staff capacity, and he must be careful not to assume a line relationship.

Biased opinion has no place in either financial or non-financial auditing, and the development of data to support a preconceived or biased opinion, while intentionally ignoring information which would tend to disprove the opinion, is indicative of a lack of professional

23 Gregory, loc. cit.
24 Loc. cit.
integrity. Complete honesty for everyone concerned and a willingness to consider the viewpoints and opinions of others is a must in the field of auditing.

When conducting operations audits, the internal auditor should use to the fullest extent possible his ability to ask questions. These inquiries should be directed along the line of control where the internal auditor is the expert. Examples of questions related to control are as follows:

What are company policies in this area? Are they adhered to? How does management know they are adhered to? What reports does management receive? Will such reporting effectively bring to management's attention any irregularities? . . . Are they still good policies or have they been established piecemeal over the years with the result that effectiveness has been lost and there is a lack of coordination in the way they are administered.25

It has been said that the ability to locate weaknesses is the internal auditor's peculiar "sixth sense" and requires much more inherent ability and insight than is required in the solving of problems once they are discovered and pinpointed.26 A word of caution should be included here, however, for the person who tends to magnify small errors which he discovers. This person actually creates a problem where none exists and does more harm than good on an operations audit.27 The internal auditor must have the insight to determine the

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25Noakes, *op. cit.*, 86.
26Seiler, *op. cit.*, 16-17.
27Loc. cit.
seriousness of the errors he discovers, overlooking those which are insignificant and spending his time fruitfully on the location and possible solution of significant problems.

The area of operations auditing requires a higher degree of adaptability than financial auditing. In operations auditing the internal auditor, as he moves from department to department, will be in constant contact with unfamiliar records, procedures, and personnel and will have to understand the problems of a variety of types of operations. Thus, the internal auditor who is involved with operations must be able to learn quickly and easily since he will be involved with many different kinds of control.

When moving into non-financial auditing, the internal auditor must be cognizant of the fact that generally he will not be trained to render opinions concerning the technical aspects of the operations. He is the expert in controls, and thus this is the area to which the major part of his investigation must be confined. Matters which concern the technical operations and deserve attention should be referred to a specialist in the technical field, and the internal auditor should not attempt to evaluate that which is beyond his training.

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28Gregory, op. cit., 52.
Summary of Non-financial Areas Audited in the Baton Rouge, Louisiana Area

All internal auditors interviewed indicated that they are actively engaged at the present time in auditing some procedures which may be considered to be of a non-financial nature. The following is a listing, designated by those interviewed, of the areas audited which they consider in this non-financial category (companies are indicated by the letters A, B, C, and D):

COMPANY A29
- Purchasing--Warehousing
- Traffic
- Advertising
- Public Relations
- Insurance
- Real Estate
- Engineering--All controls on contracts--particularly on compensation clauses
- Industrial Relations--All controls concerning employee benefits
- Production Control--Amount and quality of inventory produced

COMPANY B30
- Packing and Shipping
- Stores
- Product Movement
- Traffic
- Most other areas

(All areas are approached from the viewpoint of control)

29The first six areas in this list are regularly scheduled audits; the other audits are performed upon request of the specific department or management.

30None of these are regularly scheduled; all audits are performed upon request.
COMPANY C\textsuperscript{31}

Purchasing—Check purchase orders for competitive bidding, increase in costs over prior check, volume discounts, and discount terms

Insurance

Safety—One minor segment

Audit of the records of vendors with whom the company has contracts

New Construction

COMPANY D\textsuperscript{32}

Purchasing (Contracts)

Review of Personnel

Review of all departments except production areas to determine means of reducing costs

The following were listed as deterrents to the progress of non-financial auditing by those interviewed: the problem of gaining acceptance of the internal auditor's background training and common sense as being adequate to give him objectivity in auditing in the non-financial areas, a lack of understanding of the internal auditing function by operations personnel, and the greater difficulty of non-financial auditing when compared to financial auditing. These are all possible deterrents to the expansion of internal auditing in non-financial areas, but they are not permanent limitations. The more the internal auditor uses his initiative in performing operations audits in a variety of departments, the quicker he will receive complete

\textsuperscript{31}All of the areas listed are regularly scheduled audits.

\textsuperscript{32}All areas are audited on a continuing study basis.
support from management and cooperation from the operations personnel. Each job well done should be indicative of the fact that operations auditing is a service that management cannot secure elsewhere, and it should indicate to the operations department audited that the purposes of internal auditing are constructive and not merely a "policing function." When operations audits are based on control, the internal auditor is limited only by his own ability, initiative, and imagination.
In recent years much attention has been focused on the systems and procedures function, and many large companies, recognizing the importance of this function in maintaining control, have established systems and procedures departments. Small companies, their size not warranting a separate systems and procedures unit, have found it advisable to have one person charged with systems and procedures duties and responsibilities.

At first glance it might appear that the words "systems" and "procedures" are synonymous; however, from business usage two meanings have been derived. "Systems" is the general or inclusive term denoting overall plans for reaching a given objective.¹ In this category are, for example, the accounting system, the system of internal control, and the voucher system. Procedures are the routines followed within the system.² These are the rules by which the system


²Loc. cit.
operates to accomplish the desired results in a prompt and efficient manner. For example, in the voucher system there are procedures for completing, verifying, and recording each voucher. These procedures, when followed, aid in accomplishing the objectives of the voucher system.

Systems and procedures provide the nuclei around which the firm operates. A system should be established for the accomplishment of each phase of the business, and for each system established there should be well thought out procedures for the realization of the objectives of the system. The collection of systems and procedures, operating throughout the firm, provides basic control over the administration of the business and guides the firm.

For several years there has been considerable discussion concerning the extent to which the internal auditor should be concerned with systems and procedures work. It is interesting to note that the opinions relating to this reach opposite extremes. Some persons are of the opinion that the internal auditor should have absolutely nothing to do with systems and procedures work; others are just as expressive that systems and procedures are definitely a part of internal auditing and that the internal auditor is therefore shirking his duty if he does not avail himself of the opportunity to serve management in these areas. Some people, naturally, take a middle course, believing that some systems and procedures work is for the
internal auditor and other phases are definitely outside his area of effectiveness.

**Arguments Against the Internal Auditor**

**Working in Systems and Procedures**

There are many persons who feel that systems and procedures studies and installations are not within the responsibilities of the internal auditor and should not be undertaken by him. Those who have this opinion do not object to the internal auditor's appraisal of existing procedures and his evaluation of their adequacy and effectiveness; neither do they have any objection to his audit programs including checks of compliance with systems and procedures. These people, however, would "draw the line" when it comes to having the internal auditor design and install systems and procedures.

According to this group, the primary objection to the internal auditor's entering into systems and procedures work is: "For an auditor to initiate in detail and install a procedure upon which he subsequently must rely in a measure for the adequacy of his audit, places him in the position of being both accuser and accused in the event of any failure of the system."\(^3\) Work in designing and installing

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systems and procedures causes the internal auditor to perform an audit of his own work when he appraises the system. This audit of his own installation, it is said, causes the internal auditor to lose to some degree his independence and objectivity since he will naturally be hesitant to criticize the work he expended in initiating, designing, and installing the system. Loss of objectivity may cause the internal auditor to assign any failure of the system to inadequate supervision or incompetency, and, on the other hand, line management may blame the system rather than accepting responsibility for any failure. 4 All of the four internal auditors interviewed in the Baton Rouge, Louisiana area objected to the internal auditor having any responsibility (other than advisory) for the design and installation of systems and procedures. Three of the four interviewed specifically mentioned the inadvisability of having the internal auditor audit his own installations.

Another reason often advanced for keeping internal auditing separate from systems work is that the internal auditor is generally, by nature, training, and experience, an analyst. 5 This is not meant to infer that the internal auditor cannot do creative work but that his


5Salman, loc. cit.
major interest lies in appraisal and analysis and not in devising new systems and procedures.

Also, it is maintained by this group that the internal auditor does not have the type of knowledge required for developing and installing procedures.\textsuperscript{6} There is agreement that the internal auditor must have, in addition to his technical abilities, a fundamental knowledge of details in his company and a knowledge of the industry in which he is located. However, it is stated that:

This knowledge, for the most part, cannot be particularized. It can, at most, considering the limitations of even the best informed individuals, be in many instances a general knowledge of the fundamental facts and operations.\textsuperscript{7}

In most instances, detailed knowledge is required for the development of systems and procedures. A study of the minute details of operations must be made and considerable time spent in study of existing procedures which naturally must be considered before recommending new procedures. Controls must be checked, forms must be designed, and various types of possible mechanical recording equipment must be investigated in order to accomplish even an acceptable job in the design and installation of procedures. In addition to these details, the job may also involve writing clear and detailed instructions for correct performance, indoctrinating the staff that will execute the

\textsuperscript{6}Muschett, \textit{op. cit.}, p. 30.

\textsuperscript{7}Loc. \textit{cit.}
procedure, and being responsible for clearing up misunderstandings and wrong interpretations after the procedure is placed in operation.\textsuperscript{8}

Questions concerning a system or procedure will naturally be channeled to its author—in this case the internal auditor.

This type of work with its time consuming detail can cause a serious lag in the accomplishment of the internal auditor's audit program. Thus, those against having the internal auditor work in systems and procedures have a third reason, that of time. If the internal auditor spends so much of his time in the detail work of systems and procedures, then he will not have the time (nor staff) to maintain and conduct his appraisal audits in the depth nor with the timing desirable.

Also stated as a reason against the internal auditor becoming involved in systems and procedures work is the difficulty of administration. Many of the internal auditor's audits are coordinated with those of the public accountant, and it is contended that to add the creative detail of systems and procedures work to the analytical work of the internal auditor will disrupt normal schedules and make a coordinated effort with the public accountant virtually impossible.\textsuperscript{9}

\textsuperscript{8} Ibid., pp. 30-31.

\textsuperscript{9} Ibid., p. 30.
Arguments for the Internal Auditor Having Complete Responsibility for Systems and Procedures

Many persons hold the exact opposite view from the previous discussion. This group feels that it is entirely within the scope of duties of the internal auditor to design, develop, and install systems and procedures as well as to appraise their adequacy and effectiveness. The proponents of the theory that the internal auditor should actively engage in systems and procedures work refute the three arguments previously given against this procedure in the following manner.

To the argument that the internal auditor should never originate systems and procedures, this group retorts that the internal auditor is the one best qualified to initiate and install procedures since he is frequently the one who has, through his appraisal audits, located and determined the inadequate procedure which should be changed.\textsuperscript{10} The internal auditor is the one who discovers that a system or procedure is not functioning as planned, and in many cases he determines the exact cause of the failure. This group proposed that it is only logical for the internal auditor to follow through to design and install the necessary corrections to have the procedure functioning properly.

\textsuperscript{10}Salman, \textit{op. cit.}, 31.
To the position that the internal auditor is an analyst by nature and training and should not be considered a creator of systems and procedures, this group would reply that the internal auditor, upon location of an inadequate procedure, will automatically know the steps necessary to eliminate the inadequacy because he will have visualized the problem and, in many instances, the solution in his mind. Upon the location of the error or inadequacy, the solution many times is obvious. This group would maintain that the internal auditor should proceed from this solution created in the mind to the design and installation of the corrective measure.

These advocators for including systems and procedures as a function of internal auditing also have an answer for the proposition that this expansion of activities would be difficult to control and cause a lack of coordination with the outside auditors; they hold that this will not be a problem with an able administrator and good organization. Coordination with the external auditor is still accomplished by having the internal auditor carry through his appraisal audit as he would without any responsibility for design and installation of procedures; then, after completion of the audit the internal auditor can return to conduct the systems work determined necessary by him and/or the public accountant.

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11Salman, loc. cit.

12Loc. cit.
Naturally, the broadening of the scope of internal auditing to include systems and procedures work would require a larger auditing staff, but the proponents of extension indicate that the number of personnel required to do the combined work will not be as great as the total number required if these functions were separated and effectively conducted in two departments.\(^1\) Separation of the functions would naturally cause the employment of two higher paid department heads as well as other possible additions to the staff. Also, the separation can cause petty bickering which is sometimes prevalent when these two functions are not combined.\(^2\)

The following reasons, then, properly summarized, are given for combining systems and the internal auditor under one supervisor:

1. The similarity in nature and objectives of internal auditing and systems work.

2. The similarity in education, training, experience and personal characteristics of a good systems man and a good internal auditor.

3. The advantage of having one man carry through the job to completion.

4. The advantage of having one department head responsible for both functions.

5. A combined department produces better men for possible future executive positions.

\(^1\)Salman, \textit{loc. cit.}

\(^2\)Emil V. Kasman, "A Combined Systems and Internal Auditing Department," \textit{The Internal Auditor}, VI (September, 1949), 51.
6. The advantage of economy of operation.  

This group views procedures and performance as inseparable parts of an integrated whole and proceed on the theory that the work performed and the method by which it was accomplished are so closely related that they must be considered together and not as separate parts.

Arguments for the Internal Auditor Having Modified Responsibility for Systems and Procedures

There is a third group which would modify the contentions in each of the previous discussions. These people could be called the "middle of the road" group since they do not favor having the internal auditor responsible for all systems work, and yet they do not agree that systems and procedures work is never the responsibility of the internal auditor. These persons recognize that in regular audits the internal auditor will discover deficiencies in existing procedures, and he will be in the best position to initiate and install needed corrections. In order to accomplish the necessary coordination with the outside auditor, the internal auditor will first complete the audit and then return to conduct the systems and procedures work.

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At this preliminary investigation the internal auditor must estimate the time required and if it appears that it will require longer than the time allotted, the internal auditor must secure permission from his superior to continue. Many times the job will be of such length that the chief internal auditor will refer to it some designated person(s) outside the internal auditing department. Thus, the internal auditing department is not obligated for systems and procedures work, but if it has the time and feels that it is best qualified to do the job, then it has the option of choosing to conduct the systems work.

The Internal Auditor's Responsibility for Procedure Manuals

The procedure manual is a control device used by management to assist in correct interpretation and application of policies and procedures. Often it is thought by management that a certain policy or procedure exists to cover a particular function, and actually none has ever been formulated. Also, many times management believes that a certain policy or procedure is clear and that a specific interpretation is being made, whereas actually the course of action followed is quite different from the one expected by management. The use of procedure manuals can clarify much of the confusion which

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16 Salman, op. cit., 32.
may exist when policies and procedures are not written.

Procedure manuals are also useful in instructing new employees and promoted employees. Supervisors may not be able to instruct an employee in the details of a particular job, since they may never have performed the specific function themselves or it may have been a considerable period of time since they handled the details of the job. Of course, generally, the replacement on a job can be trained by the previous employee. However, this is not always possible and, too, continuous oral transferring of knowledge may lead to a procedure being followed which is quite different from the process intended. Written procedure manuals can be invaluable in maintaining standardized procedures over a period of time through several employees, or even assuming there were no changes in personnel, the manuals would serve to assure that present employees continue to perform the procedures as expected by management.

The effectiveness of a plan to develop and use procedure manuals will depend upon the support given the effort by management. The support backing the use of procedure manuals must be as broad as the areas which are to make use of them. In other words, if the procedure manuals are to be developed and used in

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17 William F. Martin, "Company Procedure Manuals and the Internal Auditor," The Internal Auditor, VII (September, 1950), 32.

18 Ibid., 33.
only one department, then approval and support must be obtained from the top supervisory position in the area, whereas, if the manuals are to be used throughout the business, then support should come from the top managerial position in the firm.

Distribution of Procedure Manuals and Bulletins

Some businesses follow the practice of preparing and distributing manuals which contain the procedures to be followed by every area of the firm. Depending upon the size of the firm, this type of procedure manual can become bulky and costly to publish, and, of course, each person receiving one of these complete manuals is obtaining a great deal of information which pertains to areas other than his own and in which he has very little or no interest. Only a very small part of the whole manual may apply to his particular area.

It would appear that a better method would be to plan the procedure manual by department and send to each department only that section which applies to it, with the exception, of course, of top executives who of necessity would receive copies of all sections. Following this method the procedure manual as distributed will not be so bulky (with specific procedures difficult to locate), and all

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19 Albert Dowell, "Developing Workable Methods and Systems," The Internal Auditor, V (September, 1948), 47.
information included will be applicable to the department receiving it. Revisions of procedures and new procedures can be handled by bulletins issued to the appropriate people for inclusion in their procedure manuals.

Procedure manuals must be kept up to date. Few items can be as useless as an obsolete manual in which it is not known which procedures are current and which are not. Actually, it has been stated that time is better spent in keeping the existing procedure manuals revised than in using the time to cover new procedures.20 Certainly, it is necessary to maintain lists of holders of procedure manuals so that as revisions are made and new procedures covered, it will be possible to send them to all persons who should receive them for inclusion in their procedure manuals.

The Internal Auditor's Role in Procedure Manuals

Compliance with Manual

It is generally accepted that the internal audit program should include an appraisal of existing procedures and the verification of compliance with these procedures. A well-written procedure manual can substantially reduce the time that the internal auditor must spend in the appraisal of procedures; it can be one of the best tools and

20 Martin, op. cit., 34.
sources of information for the internal auditor.\textsuperscript{21} A complete procedure manual which contains all bulletins issued to departments, if kept current, will include all acceptable procedures, and the internal auditor will have only to appraise those procedures and test for compliance. Without the procedure manual, the internal auditor would first have to determine the procedures and then conduct his audit to determine their effectiveness as a control medium. All internal auditors interviewed indicated that they use the procedure manual for checking adherence to procedure.

During the course of his audits, the internal auditor will naturally find certain areas for which the procedures have not been written in the procedure manual. If he feels that the procedures being followed differ from those which management believes are being followed, or if he suspects that misunderstandings and variations exist because of a lack of written procedures, then the internal auditor should recommend that the procedures be written and included in the procedure manual.\textsuperscript{22} By following this policy the internal auditor can act as the "trouble shooter" in locating those areas which are most pressing for written procedures.

\textbf{Preparation of the Manual}

Basically, the arguments for and against the internal auditor

\textsuperscript{21}Ibid., 37.

\textsuperscript{22}Martin, \textit{loc. cit.}
preparing the procedure manual are the same as those which were previously presented for and against the internal auditor having responsibility for systems and procedures. Naturally, the arguments against the internal auditor becoming involved in systems and procedures—loss of independence, lack of time, difficulty of administration, and lack of detailed knowledge—apply equally to the added detail of writing the procedure manual. Likewise, the same arguments given for having the internal auditor perform systems and procedures work also apply concerning his writing of the manuals.

One thing that should be mentioned, however, is that the internal auditor, even though he may not write the manuals, is certainly in an advantageous position to act in an advisory capacity to the one responsible for the preparation of the manuals. It would appear to be within his scope of operations to recommend changes which he observes are necessary in existing procedures and to recommend that new procedures be written. Also in an advisory capacity he may review the written procedure before it is promulgated in the procedure manual. The internal auditor's analytical training and experience places him in the position of being able to foresee many ramifications of the procedure, particularly in the area of control. Three of the four internal auditors interviewed indicated that they recommend and comment on procedures before they are included in the procedure manual. One auditor specifically mentioned that he
checked the new written procedures for any elimination of controls.

Summary and Conclusions Concerning Systems and Procedures

Considering the least problem first, the administrative and coordination difficulty could probably be overcome. As was suggested by one group in the previous discussion, the internal auditor could simply continue his appraisal audits as normally conducted in order to complete his work in time to coordinate with the external auditor. Later, at his own pace, he could return to conduct the systems and procedures installations. Therefore, it is felt that the problem here is not severe.

Another argument against having the internal auditor design and install systems and procedures was the lack of time. This problem can also be overcome by the addition of personnel on the staff of the internal auditor so that he will have an adequate staff for conducting all the investigations into systems and procedures installations. Thus, this problem could be virtually eliminated.

The third argument against the internal auditor doing systems and procedures work--lack of knowledge--is more difficult to solve. Actually, the internal auditor could probably do a fine job of prescribing systems and procedures in the area in which he was trained in detail. For example, the internal auditor trained in accounting
could probably do effective work in designing systems and procedures for the accounting area, but it is most doubtful that the accounting trained internal auditor could accomplish much in trying to derive detailed systems and procedures for the accomplishment of the engineering objectives of the firm. It is felt that there would always be a problem whenever the internal auditor attempted to use his "general" type knowledge outside of accounting and finance for the purpose of designing specific procedures.

The last problem, loss of independence, is the most difficult. As indicated above, the internal auditor could probably do a fine job of designing and installing accounting procedures, but there is still the problem of loss of independence. Criticism of one's self is always difficult, and the internal auditor cannot be expected to be able to analyze and criticize his own work objectively. Human nature is such that the internal auditor cannot remain objective in the appraisal of his own work, and thus any possibilities, indicated above, of having the internal auditor do systems and procedures design and installation have been eliminated.

The internal auditor may serve effectively in an advisory capacity, but the responsibility for systems and procedures installations and the writing of the procedure manual should be taken care of by someone other than the internal auditor.
Employee Performance

Beyond the question of properly designed and executed systems and procedures is the question of whether the persons responsible for the execution of the procedures are properly qualified and are performing efficiently. The internal auditor can be of assistance to management in judging the performance of employees.

Continuous appraisal of jobs and of people performing those jobs is absolutely necessary in assuring efficiency of operations. In normal audit appraisals it is impossible for the internal auditor to complete a comprehensive audit without some appraisal, at least mentally, of personnel as well as performance results. In the internal auditor's movement throughout the firm, he comes into contact with almost all the employees from the lowest to the highest position and gathers a wealth of information concerning the individual employees which can be used by management in the all important function of placing the right person in the right job.

It is necessary that the internal auditor exercise caution in appraising an individual's technical abilities, especially outside the areas of accounting and controls where the internal auditor is probably best informed. However, inefficiency in many cases is not

difficult to recognize, and the internal auditor is in an excellent position to observe it since he is familiar with almost all, if not all, positions in the firm.

**Records Disposition**

Many companies spend hundreds or even thousands of dollars each year for the storage of records. A certain amount of storage is necessary in any business, as particular records are needed for future use and reference, but it is surprising how much worthless material is kept and how many records, once valuable, are kept for a period of time which is far greater than their period of usefulness. Many companies are just not conscious of the accumulation of records, and neither do they appear conscious of the cost involved in filing and storing records.

When companies which have not become aware of record storage problems have used all available equipment for storage, they will usually follow one of two alternatives. If more floor space is available, the usual course will be to buy more filing equipment to provide more storage space without any regard to what is to be done with the present stored records. However, if all available floor space has been used, the business will generally follow the second course of action, that of discarding some of the oldest records. The person assigned to the job, generally without any knowledge of the problems involved
with records, usually will not have a plan of records disposition to follow and thus will arbitrarily choose and discard from the oldest records. This approach has several fallacies. First, age alone cannot be used in determining the value of records. Secondly, this procedure will not settle the problem, as records will again accumulate and the same action will have to be repeated. Also, if no record is kept of the records discarded, it is impossible to know which records have been kept and which were destroyed.

The solution to the records problem is the establishment of a complete "Records Plan" to cover the handling of every record from its preparation to its ultimate disposal. Surveys must be conducted and control over files must be established. A certain number of file drawers should be determined for each department, and the purchase of any additional files by any department should be approved by one appointed person. This procedure will force the retirement of records because of lack of filing space. Then some method of control must be established concerning the manner in which records are to be retired from the active files and placed in the records storage center, if such a place for the accumulation of inactive records is provided by

24 Paul G. Purington, "Records Disposition," The Internal Auditor, IX (June, 1952), 39.

25 Loc. cit.

26 Ibid., 40.
the firm. By adequate use of control numbers, etc., the records center can become a usable reference center; without adequate control it becomes merely a place to leave records which then cannot be found for further use. 27

Once all information is gathered on each record, appropriate data should be transferred to each department concerning the filing practices applicable to the department and the period of time each record is to be held in the active files before being transferred automatically to the records storage center of the firm.

It would appear that the internal auditor with his overall picture of the business should be the one to supervise the development of the records plan. The internal auditor in conducting his audits throughout the firm will have become more familiar with the various forms necessary for each department, with their use, and with their ultimate value than any other individual in the firm.

27 Ibid., 41-42.
CHAPTER VI

THE INTERNAL AUDITOR'S COMMUNICATION WITH MANAGEMENT:
AN EFFECTIVE REPORT

In today's expanding business organizations, the written report is replacing "over the desk" type discussion as a means of securing executive action. This change in the method of communication has caused many persons consternation in the writing of effective reports which will secure action in the manner intended. Many people are able to communicate effectively in an oral situation, but when they are forced to write a report, they seem to be at a loss for words and they have traumatic experiences in getting anything down on paper. On the other hand, there are those who appear to be prolific writers, but when they have finished writing a report it is neither understandable nor informative—not even interesting.

A lack of the ability to write effectively is often voiced as the major shortcoming of accountants, not only of those new in the field but also of the seasoned expert. The report is the result of a job involving many hours of time and many dollars of cost, and it is the evidence by which management judges the performance of the internal auditor. But more than this, the audit report is the document by which operations and personnel are judged and decisions are made. Thus,
the internal auditor presents a report upon which not only his work but also the performance of others will be judged. This important information must be well written. Although the internal auditor may work meticulously and accurately and prepare neat and complete working papers, he will be judged on the information delivered to management, and this information is delivered, generally, in the form of a written report.

Much has been said and written concerning the compilation, content, and presentation of the internal auditor's reports of activities. The major concern in this paper, however, is presentation and specifically with the style of writing the presentation. Of course, this limitation to style of writing is not meant to infer that other technicalities such as correct grammar and spelling are not important. By style of writing is meant the way of writing—word choice, sentence and paragraph length, and arrangement of words, sentences, and paragraphs to form the completed report.¹

There are basically three reasons why the internal auditor in many cases writes in a style which is not effective and does not secure the desired results. First, many internal auditors have "inherited" from the nineteenth century a style of writing which today is outmoded.

During that period speaking and writing included a certain amount of ornate frills, e.g., "exterminate the illumination" instead of "put out the light." Today, however, is an age of streamlined efficiency and accuracy accented by "straight to the point" simplicity, and writing must keep pace with the change.

Also contributing to an ineffective report is a desire to impress. Ordinarily this characteristic materializes in the use of words and composition which call attention to themselves rather than to the idea expressed. The use of unfamiliar words and phrases, causing the person who receives the report to read it with a dictionary in his left hand, merely detracts from the report, takes unwarranted time from the reader, and in general reduces effectiveness.

A third and natural reason for poor writing is "fuzzy thinking." It may be that in certain areas of the report the writer is unsure of the information included, and his unsureness may be reflected in a confused presentation.

The following discussions should by no means be considered to exhaust the list of report writing principles, but they can be considered as guides to effective report writing for the internal auditor.

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2 Dennis Murphy, "Let's Improve Our Reports and Letters," The Internal Auditor, X (March, 1953), 65-66.
3 Ibid., 66.
4 Loc. cit.
Factual Information

There is no doubt that information as important as that included in the audit report must be factual. A report which demands management's time in reading it and guides management in making decisions must be correct and representative of actual circumstances. There is no room in such reports for careless reporting of information.

One factor which will contribute to the accuracy of the report is for the internal auditor to write at least the first draft of his report at the location of the audit. Upon trying to commit his thoughts to paper, the internal auditor may discover several unanswered questions. If he is still at the location of the audit, these questions may be settled, saving the time-consuming return from his office, or, if this is not possible, the inclusion of vague information resulting in a non-factual report. Actually, the auditor should begin planning for the report at the time the audit is begun by maintaining files for the information to be included in the final report. This filing procedure will serve two purposes: (1) It will cause the internal auditor to plan ahead for the divisions of his report and the information to be included, and (2) It will provide a systematic means of accumulating data.

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To assure factual reporting, the conclusions of the internal auditor should be discussed with the supervisory line management in the area audited. The information and ideas which can be brought out in this discussion may throw new light on the observations of the internal auditor and alter his planned presentation in the report.\(^6\)

The reporting of data the internal auditor knows to be true poses no problem; the information is written without qualification. However, there is certain information which comes to the internal auditor in the form of explanations and descriptions, and this data may find its way into the report. To protect himself, the internal auditor must be careful to label this type of information according to its source and not represent it as factual information which he knows to be true.\(^7\) Only in this manner can the audit report be factual although references are made to nonfactual matters.

If the internal auditor on the audit had an assistant(s) who helped in the gathering of data and the preparation of working papers, the accuracy and completeness of their work must be ascertained.\(^8\) The supervisor on the audit is responsible for all information included in the audit report, and he must be certain of its accuracy.

\(^6\)Humphries, *loc. cit.*


\(^8\)Humphries, *op. cit.*, 28.
Concise Wording

The reader of the audit report will be much more receptive if he has read a concise report with all excessive wording removed. By conciseness is meant an expression "in the fewest words that will convey the complete idea to the mind of someone else."^9 The number of pages contained in a report does not measure conciseness; a long report may very well be a concise report if all the words used are necessary and any excessive wording has been omitted.

Of course, the report must be sufficiently comprehensive, and all relevant information must be included. During the course of the audit the internal auditor will observe and come in contact with much information which is either unrelated or far removed from the purposes of the audit, and if he is not careful, much of this detail will find its way into the report. After writing the first draft of the report, the auditor should start rewriting and removing the facts which are in no way related to the results of the audit. After the editing and rewriting stage, the resulting report should be concise--sufficiently comprehensive to convey all ideas but stripped of all unnecessary details and frills.

Naturally, conciseness should not be carried to the extreme

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^9Couperthwaite, op. cit., 57.
of causing the report to appear abrupt. Extreme conciseness can result in a lack of smoothness and clarity, a fault just as disastrous as being overly wordy. Properly used, conciseness is helpful in carrying the reader smoothly through the necessary detail of the report by the elimination of wording which does not contribute to the report.

Clear Presentation

The nature of clarity is to present ideas and information in an understandable manner—"to present, in vivid words, an orderly procession of ideas which will convey to the reader's mind the picture we want him to see." The report should be written so that each idea falls into place in logical sequence to lead the reader easily and without confusion to the conclusions and recommendations at the end of the report. The report should be written to a person and at all times the writing gauged to the particular reader so as to be coherent. If the report is not understandable to its reader, no communication takes place and the report serves no purpose. There are several pitfalls which must be carefully avoided by the internal auditor if he to present a report which has the intended effect upon

10 Couperthwaite, loc. cit.

11 Ibid., 54.
First, and a natural trap for any technical writer, is the internal auditor's use of the technical language of accounting and internal auditing. Naturally, the technical language of any profession usually is understandable only to those familiar with the terminology, and not everyone has a background in accounting and internal auditing. If everyone who reads the internal auditor's report had a college degree in accounting, a report written in the technical terminology would be understandable and would communicate information clearly. The internal auditor, however, must remember that several persons may read his report, even possibly including line personnel with no knowledge of the technical language of the profession. If it is impossible to eliminate technical terms from the report, they should at least be explained so that the report will be understandable to the reader.

Some persons have an inclination to demonstrate their knowledge of long and unfamiliar words when writing an audit report. A busy executive, however, will not be very favorably impressed if it is impossible for him to understand the report without frequent use of the dictionary. Certainly it is not advocated that an entire report should be written in one syllable words, as this would be just as poor as the opposite situation above. Proper judgment must be used in order for the report not to appear "showy" and yet not appear to have
been written in the vocabulary of a grammar school child. Often a long or an unfamiliar word is just right to convey the meaning intended, and certainly its use is entirely acceptable. The objection is using unfamiliar words with such frequency that they distract the reader from the ideas presented and call attention to themselves. The reader is actually diverted from the train of thought of the report as he tries to decipher the meanings of the complex words.

Ambiguous and vague wording must be eliminated from the internal auditor's report. Today's acceptable business writing has outdated ornate frills and veiled writing in favor of a direct and streamlined approach. For assistance in choosing words that will convey his thoughts precisely, the internal auditor should obtain and use a good dictionary and a thesaurus.

One of the major faults with many reports is the author's attempt at formality by using the passive voice. In a sense the internal auditor has inherited the use of the passive voice in report writing, since textbooks have begun only recently to present the active voice as being preferable. The report writer was taught to be impersonal and omit any personal references in his report in the belief that objectivity would best be obtained by omission of personalities involved. Frequently, the use of impersonal writing led to overuse of the passive

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12Severa, op. cit., 31.
voice and resulted in a dull writing style. However, dullness in writing style can be attributed to the writer rather than to the style of writing.  

In recent years a trend has developed toward the use of the personal style of writing in reports. The argument is that, since the internal auditor is writing to persons whom he knows, there is no reason for the written report to be drastically different from conversational exchange of information. Thus, the use of personal pronouns and references has been injected into reports.

Since both impersonal and personal styles of writing are acceptable in modern reports, the internal auditor must depend on each audit situation to dictate the style he must use. He should consider the desires and expectations of those to whom he is making the report and the formality of the situation. A formal situation would certainly lend itself to the use of the conventional impersonal style of writing, whereas in an informal situation the personal style would be appropriate.

Sentence and paragraph construction must be carefully planned. Many times it is not the content but the length of the sentence which determines the difficulty of understanding. When several bits of

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14 Ibid., p. 171.
information, along with supporting data, are all included in one sentence "package," the mind of the reader will probably not be able to grasp the complete thought without rereading. The mind accumulates information within a sentence, then stops at the end of the sentence and begins to accumulate more information with the beginning of the next sentence. Only a certain amount of data can be absorbed easily from each sentence package.\textsuperscript{15}

Naturally the length of sentence that the mind can absorb with ease varies with the mental capacity of the reader. It is generally agreed that sentences written for the middle level of adult American reading ability should average no more than sixteen to eighteen words.\textsuperscript{16} However, it has been indicated that the internal auditor's report can be written in sentences averaging twenty words in length.\textsuperscript{17} This variance is probably due to the fact that in directing his report to management, the internal auditor is aiming his writing at persons with above average mental capacity and reading ability. Of course, in limiting the internal auditor to sentences averaging twenty words, it does not mean that he should strictly avoid the use of longer sentences as long as these are well constructed and convey the

\begin{footnotes}
\item[15]\textit{Ibid.}, p. 188.
\item[16]Lesikar, \textit{loc. cit.}
\item[17]Murphy, \textit{op. cit.}, 72.
\end{footnotes}
meaning simply. However, several long sentences should not be permitted to follow in succession, allowing the reader no break in complex construction.

Short, well-organized paragraphs contribute to the clearness of the report. Long paragraphs give the impression of being difficult and are less inviting to the reader. Each topic of a report should be covered in a separate paragraph, and the length of the paragraph will depend upon the topic covered. The general rule is that paragraphs should average about eight or ten lines. Variations will naturally occur depending upon the topics to be covered. Lengthy paragraphs should be analyzed to see if more than one topic is covered and additional breakdown of the paragraph is warranted.

Many writers make use of a topic sentence method of writing. In following this procedure, there is one most important sentence in each paragraph, and all other sentences in the paragraph expand, supplement, or qualify the central topic. The topic sentence may appear at the beginning of the paragraph (the most common practice), within the paragraph, or at the end somewhat as a summary or conclusion.

Findings included in the audit report should be presented in a

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18 Lesikar, op. cit., p. 197.

19 Loc. cit.
logical order, e.g., by functions audited or by location audited. An orderly arrangement provides the reader with a chain of thought and enables him to comprehend more quickly and easily the message of the report.

Headings for the various divisions of the report should be used skillfully and appropriately. The few words for use in each caption should be carefully chosen to command the attention of the reader and to be informative concerning the material in the section to follow. In addition, the general appearance of the report will be enhanced. A report which is appropriately sectionized, giving the reader mental breaks in his reading, will be much better received and easier read than one of page after page of closely typed narrative and hard-to-locate information.

To assure clear communication the internal auditor must be careful to place emphasis where it belongs in order to convey the proper impression to the reader. Some information included in the report is of major importance; other data is of a supporting nature. In the written report, the internal auditor should construct the narrative in order to make the important points obvious to the reader so he will have no problem of evaluating data.

Accounting schedules can also serve useful purposes in breaking the monotony of narrative as well as in presenting the material succinctly. However, any type of columnar information should be condensed and used infrequently, as many readers are prone to skip this type of data and read only the prose presentation.

Bar charts, line charts, pie charts, and other means of graphic presentation aid in holding the interest of the reader by providing an interesting appearance to the report.

As a final note on clearness, one photograph can be much more effective than many pages of writing. A picture included in the audit report can be quite effective in describing the physical condition of a branch location. For added emphasis the internal auditor might also include a picture of the physical plant of a competitor at the particular location. This procedure will certainly arouse more interest than several pages or even several audit reports could have generated.

Clear reports eliminate doubt and confusion resulting in more efficient communication and a saving in both time and money.

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21 Couperthwaite, *op. cit.*, 56.
Objective Approach

Another essential characteristic of a good report writer is objectivity—the ability to approach each new audit problem with an open mind and an unbiased viewpoint. The internal auditor must be careful to include all relevant facts in his report and not just the facts which will support his conclusions. It is the receiver of the report, not the internal auditor, who makes the decisions as to courses of action, and this person is entitled to know all relevant facts before reaching his decision. The internal auditor will certainly not build up confidence in his work if he purposely omits facts from his report because they do not coincide with some pre-conceived idea.

Alternatives that merit attention should be given objective consideration. The present method of accomplishing a particular job should never be considered as the absolute "best" or as infallible even though it has been functioning satisfactorily for years. There may be several alternatives which would produce as good or even better results. Objectivity demands that they be considered.

Tactful Writing

The audit report must be written with dignity and tact. The internal auditor must keep constantly in mind that there is a possibility of his offending two persons or groups of persons—the
person(s) audited and the receiver of the report. It is difficult to believe that any internal auditor would purposely set out to be tactless, but many times this can occur unintentionally. First, the internal auditor may omit sufficient background material necessary for the reader of the report to make an intelligent decision. There is no deliberate attempt to hoodwink the reader, but the internal auditor feels that the conclusion is so obvious that his recommendation should automatically be followed. The reader, however, may not have such strong convictions, and he should be provided with all necessary background information for reaching his decision. The internal auditor should not be so tactless as to assume that the reader will accept the recommendations in the report without knowing all background facts.

Secondly, the persons audited may be offended by careless wording in the internal auditor’s report. Of course, where criticism is warranted, it should be brought out in the report, but it should be constructive and in a diplomatic language. There is no place in the internal auditor’s report for the use of sarcastic criticism or emotional language which could destroy the amenity of personnel to subsequent audits.

Well-packaged Report

The internal auditor must recognize that impressions are important and give serious consideration as to the opinion which will
be formed by the recipient the instant the completed audit report is placed on his desk. The internal auditor has a product to sell—his constructive service to management—and this product is presented in a package—the internal audit report. As has been said by the auditor in one large firm: "Even though we . . . have the best products in the industry, we wouldn't dare try to sell them in milk bottles wrapped in newspapers." The same is true in internal auditing. The internal auditor prepares a professional report, and it should look professional when presented to its reader. First impressions are important, since they set the stage for the reading of the report. If the first impression is poor, then the report itself will have to cancel this opinion. If the report receives a favorable reaction, this obstacle will not have to be overcome.

The report presented in some type of cover will receive a much better reception than a few sheets of paper stapled or paper-clipped together. The cover selected should protect the report and enhance its appearance. Color and design of the cover should contribute to the professional appearance of the report.

The report should be well typed on good quality paper, probably of standard 8 1/2" x 11" size. The arrangement of material

22Alfred L. Pilson, "Internal Auditors' Reports," The Internal Auditor, X (December, 1953), 53.

23Loc. cit.
on the page should be pleasing to the eye, and indentation and caption form should be consistent throughout the report. Generally, the report should be double spaced and, if length warrants it, a table of contents included.

**Prompt Reporting**

The internal auditor loses no time in reporting a defalcation. In this case, the reason for prompt reporting is obvious. The reasons for prompt reporting of information not concerned with fraudulent employees should be just as obvious to the internal auditor. There are two groups interested in the results of the audit—management and the division audited.

First, the audit report provides management with material for decision-making purposes, and decisions must be based on the most current information, not data from last month or last year. If the internal auditor takes too much time in preparing and submitting the audit report, the information included may not even be factual, since circumstances and conditions may have changed since the appraisal was performed. Using out-of-date information can result in erroneous decisions.

In addition to the reaction of management toward a delayed report, the response from the division or department audited must also be considered. After the audit, the auditee is waiting for
either directions for changes to be made or a clearance—notification that everything was found in order. If there is much delay, interest lags, discussions are forgotten, and the auditee is apt to remember only the nuisance aspects of the audit, and this will possibly result in a decrease in cooperation on subsequent appraisals. The internal auditor has probably disrupted schedules and taken the time of the supervisor in the division audited. The least that can be done is to give a prompt report on findings.

One of the best ways to decrease the time required to complete the report after the audit is to begin writing the rough draft of the report while still conducting the appraisal. This procedure was also mentioned as a means of assuring factual reporting.

Summary

It is doubtful that anyone can ever attain perfection in writing, but everyone can strive to improve by the study of accepted principles and by observation of reports which others have prepared. By constantly improving the method of communication—the audit report—the internal auditor can be of even greater assistance to management.

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24 Humphries, op. cit., 30.
CHAPTER VII

SUMMARY AND CONCLUSIONS

It has been the purpose of preceding chapters to present discussions concerning certain aspects of internal auditing. Though not labeled as internal auditing, this function has always existed in some form in all businesses. Even in the smallest concern, the role of "internal auditor" is filled by the owner in conducting his checks and appraisals of business operations.

Over the years, as firms became larger and required a greater amount of detailed record keeping, internal auditing developed as an important function, preventing fraud and assuring management as to the accuracy of the records. During this period internal auditing was limited to the finance and accounting area of the business. With the refinement of record keeping, the use of machines, and the development of better internal control features, the verification activity became less time consuming, and it was not necessary for the internal auditor to act exclusively in a clerical capacity.

At the time the clerical phase of internal auditing was diminishing in importance, a whole new area of internal auditing was being developed. In 1941, two events occurred which gave
internal auditing the added impetus which was needed at that time.

First, the Institute of Internal Auditors was founded, which was probably the greatest single factor contributing to the growth of the profession of internal auditing. This organization provided a means of communication among internal auditors. Also occurring at this time was the publication of V. Z. Brink's book *Internal Auditing*, the first comprehensive work dealing with that subject.

As a result of additional research in the field, some progressive internal auditors began to move outside the accounting area of their firm and attach a broader significance to internal auditing. With the Institute meetings and publications to disseminate information to members, the profession grew in non-financial areas.

With the internal auditor's increased movement outside the financial area of the business, firms were faced with the problem of designating the echelon of management to whom he would report. There are four possible levels of internal auditing, each with its own scope and objectives. The level of internal auditing which provides the greatest degree of independence is the proprietorship level. The proprietorship internal auditor is appointed by the board of directors. If appointed by the top management, his scope encompasses all departments of the business, and he may be called a management internal auditor. Next in line would be the staff
internal auditor who is confined principally to a particular area by virtue of his appointment by the controller, treasurer, or other person of comparable rank. The simplest form of internal auditing is departmental internal auditing. This internal auditor is appointed by a minor department, and his work is limited to that particular unit.

If the auditor is to be available to serve management constructively, it would appear that he should report to and be under the direction of the top level of management--the president or executive vice-president. At this level of reporting, the internal auditor has direct authority to cross departmental organization lines and move throughout the firm in conducting constructive auditing in any non-financial areas.

As the work of the internal auditor changed, so did the characteristics and education required for internal auditing. When internal auditing was only a financial activity, a thorough specialized background in accounting was all that was necessary for internal auditing. The modern internal auditor, however, must have breadth of knowledge, perseverance, good contact ability, and excellent personality, to name only a few of the prerequisites. No longer does the internal auditor have the single function as a "watchdog;" he must be able to take the managerial viewpoint on each audit.

Since the persons working in internal auditing form the very
foundation of the department, it is most imperative that careful thought and consideration be given to the selection and training of high-quality, capable personnel. In order to accomplish contemporary internal auditing, it is desirable to have a group of internal auditors composed of persons transferred from other departments in the firm, of public accountants and/or internal auditors from other firms, and of recent college graduates. This blending of personality, experience, and knowledge should result in the effective accomplishment of modern internal auditing.

There seems to be general agreement that there should be some type of training program for the internal auditor, and companies have various types of programs differing in coverage and in length of time. Applying the adage "experience is the best teacher," companies many times rotate new internal auditing employees among various audits and assign them to work with different experienced auditors.

The personnel in the modern internal auditing department receive a type of training by their movement throughout the firm, a program which is not available to people who are stationary in a particular department. The internal auditor accumulates a vast knowledge of information concerning the firm, since his work probably carries him into every department of the business organization. This peculiar type of training has caused the internal auditing department to be favorably considered as a source of promising young executives.
It has only been in recent years that the internal auditing function has begun to expand into the operations of the firm. Because he was not an expert in operations, there was objection to the internal auditor moving outside the financial area. A lack of understanding of operations auditing has resulted in the opinion of many that financial auditing and operations auditing are entirely different and unrelated. Actually, they are quite similar, with the basic difference being that financial auditing deals with financial controls whereas operations auditing is concerned with operating controls. Expertness in operations is not necessary, since audits are based on controls. Indeed, it may even be better that the internal auditor is not an expert in operations. The non-expert does not have the biases or preconceived ideas of the expert, and the non-expert can often ask penetrating questions of the expert.

It is generally conceded that operations auditing is more difficult than financial auditing, because in many cases the operations controls are not well codified. It may be an arduous task in some cases to determine the objectives established by management for some departments. Only after conducting an initial survey of the department, observing operation control problems, and gathering background data, can the internal auditor determine the scope of the audit.

In some cases it may be advisable for the internal auditor to
use some operations personnel on his staff. This procedure should serve a dual purpose: (1) technical assistance is provided the internal auditor, and (2) operations personnel can be led to a better understanding of internal auditing and its functions.

There is no question but that the internal auditor is responsible for determining compliance with the systems and procedures as established by the firm. However, there is a complete divergence of opinion as to the internal auditor's responsibility for systems and procedures studies and installations. One school of thought is that the internal auditor should have complete responsibility for systems and procedures studies and installations, whereas the opposite viewpoint is that this function does not fall within the scope of the internal auditor's services. A third group maintains that the internal auditor should assume limited responsibility for this activity.

Several arguments are given for and against each of the above policies, but there appears to be one most important determining factor—loss of independence. Human nature makes it impossible for the internal auditor to remain objective concerning his own work, and thus, he should never be given the responsibility for designing and installing any system or procedure if there is the possibility he will ever be called upon to perform an audit in the area. The internal auditor may advise concerning systems and practices design and installation, but he should not be given responsibility for the task.
Records disposition is a problem which the internal auditor can help solve in many companies. Many businesses do not appear to be cognizant of the cost of record storage and therefore they have no systematic plan for the removal and disposition of records. In order to avoid the accumulation of worthless records which occupy valuable space, a records disposition plan must be formulated, adopted, and followed. The person responsible for the formulation of such a plan must be one who is familiar with the records required and used throughout the firm. Through his various audits the internal auditor will have become more familiar than any other individual in the organization with the value of the forms completed in each department. It would thus appear that, because of his company-wide experience, the internal auditor should be the one to devise such a records disposition plan.

Upon completion of an audit the internal auditor submits the results of his appraisal in the form of a written report. This document is most important, since it is the means by which the work of the internal auditor will be judged by management. Valuable hours of time may have been spent in meticulous detail and investigation and in the preparation of accurate working papers, but management sees only the final report on the audit. This final presentation is used as the basis of judging not only the work conducted by the internal auditor but also the performance of personnel and the results
of operations. Such an important document warrants all possible attention to detail in its preparation. In order to make management as receptive as possible to the contents and recommendations of the report, the internal auditor must follow a style of writing which contributes to, rather than detracts from, the report. The following guides to effective report writing by no means exhaust the list, but they are indicative: factual information, concise wording, clear presentation, objective approach, tactful writing, well-packaged report, and promptness. By improving the communication of information to management, internal auditing can be even more useful.

Great strides have been made in internal auditing, especially in recent years. Within approximately twenty years internal auditing has grown from a disorganized group of clerical "policemen," to an organization of professional men located not only in the United States but throughout the world.

There appear to be three hindrances to the growth of internal auditing in a constructive role. First, in a number of companies the internal auditor is not reporting to the level where he would be best situated to serve management. Bounded by departmental lines, his growth and the expansion of his activities are suppressed, and all his auditing remains of a financial nature.

The second obstacle which must be overcome by the internal auditor is the fact that the title "internal auditor" does not indicate
to the persons outside the profession the true nature of his duties. To the layman the term "auditor" denotes a narrow, limited verification activity. Since there has been no change in title, the layman does not realize the drastic change that has come about in this area.

The third hindrance to growth in non-financial areas is the lack of understanding of the growth and expansion of scope which have already occurred in internal auditing. People, not realizing that the audit is based on controls, fail to understand how the internal auditor, a non-expert, could possibly audit an operations department.

These interferences are not drastic, and they can be remedied. The opportunity for internal auditing lies in this broad, constructive role of the internal auditor. Internal auditors who have the proper perspective and initiative will always be able to find unlimited opportunities to render service to management.
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PUBLICATIONS OF LEARNED ORGANIZATIONS


VITA

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Title of Thesis: The Constructive Role of the Internal Auditor with Emphasis on the Baton Rouge, Louisiana Area

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