

PORT OF SEATTLE
MEMORANDUM

DATE: January 10, 2012
TO: Audit Committee
FROM: Joyce Kirangi, Internal Audit Director
SUBJECT: Scope of Internal Audit Peer Review

The Audit Committee has requested information regarding a peer review by the Association of Local Government Auditors (ALGA).

Internal Audit organizations generally conduct audits under one of the following standards:

- Government Auditing Standards (commonly referred to as the Yellow Book) issued by the Comptroller General of the United States Government Accountability Office (GAO). Government Auditing Standards are used when conducting government audits and/or other non-profit organizations that receive federal funds.
- International Standards for the Professional Practice of Internal Auditing (commonly referred to as the Red Book) issued by the Institute of Internal Auditors (IIA). These standards are mostly used by private sector internal auditors.

Both professional auditing standards provide a framework for conducting high quality audits. There are many similarities between the Yellow Book and the Redbook, and there are also some key differences.

At the Port of Seattle, the Audit Committee oversees the activity of the Internal Audit Department. The Committee, under its charter, as adopted on October 26, 2010, requires audits to “be conducted under the United States Government Accountability Office’s Government Auditing Standards (Yellow Book).” Accordingly, the Internal Audit Department has been preparing its system of quality control in compliance with those standards. In addition to the Yellow Book requirements, Internal Audit has incorporated some of the Red Book elements (notably those associated with the annual work plan and risk assessments) as industry best practices to supplement the Yellow Book. Overall, the Internal Audit Department operates and conducts its activity in accordance with the Yellow Book.

Below are comments related to the scope of a Yellow Book and Red Book peer review. The scope refers to the activities and periods that will be subject to the review.

The way the process for engagement proceeds is that I request a peer review from the ALGA, and then they send me an engagement letter, rather than me sending them one, as the review elements are determined in their procedures. The elements for the engagement letters for both the Yellow Book and the Red Book review are as follows:

A. Government Auditing Standards (The Yellow Book)

Once an internal audit organization contacts ALGA and indicates it needs a Yellow Book peer review, ALGA will send a standard review engagement letter to the requesting organization, which establishes the overall objective of a Yellow Book peer review. The following is an excerpt of such a letter:

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The scope of the review will be to conduct a peer review following guidelines contained in the ALGA Peer Review Guide. The objectives of the review will be to determine whether during the period under review, the Audit Organization's internal quality control system was (1) suitably designed and (2) operating effectively to provide reasonable assurance of complying with applicable Government Auditing Standards issued by the Comptroller General of the United States.

Specific procedures to accomplish the stated objectives are established by the review team. ALGA's Yellow Book peer review in general covers the following areas:

- Auditor's Independence
- Organization Independence
- Professional Judgment
- Continuing Professional Education
- Staff Competence
- Quality Control and Assurance
- Audit Organization Policies and Procedures
- Monitoring Progress
- Planning
- Communication to management
- Follow up on Prior audits
- Audit Supervision
- Evidence
- Documentation
- Reporting

B. Professional Practice of Internal Auditing Standards (The Red Book)

Once an internal audit organization contacts ALGA and indicates it needs a Red Book peer review, ALGA will send a standard review engagement letter to the requesting organization, which establishes the overall objective of a Red Book peer review. The following is an excerpt of such a letter:

The scope of the review will be to conduct a peer review following guidelines contained in the ALGA Peer Review Guide for Assessing Conformance with International Standards for the Professional Practice of Internal Auditing. The objectives of the review will be to determine whether, during the period under review, the Organization Under Review's internal quality control system was (1) suitably designed and (2) operating effectively to provide reasonable assurance of conforming with applicable Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

Specific procedures to accomplish the stated objectives are established by the review team. ALGA's Red Book peer review in general covers the following areas:

- Independence and Individual Objectivity
- Proficiency, Due Professional Care, and CPE
- Quality Assurance and Improvement Program
- In/external Assessments
- Managing the Internal Audit Activity
- Communication and Approval
- Policies and Procedures
- Monitoring Progress
- Disseminating Results
- Reporting to Senior Management and the Board
- Governance, Risk Management, and Control
- Engagement Planning Considerations
- Engagement Objectives, Scope, Resource Allocation, Work Program, and Supervision
- Analysis, Evaluation, Recording Information
- Communicating Results
- Engagement Disclosure of Nonconformance with the Standards

The Internal Audit Department proposes a peer review starting in the 4th quarter of 2012. We anticipate the scope of the review will cover a one-year period, beginning in 2011 and extending into 2012.