

ESTABLISHING AN INTERNAL AUDIT DEPARTMENT: THE CASE OF THE SCHWAN FOOD COMPANY

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ABSTRACT

An effective internal audit department adds value to its organization in numerous ways. It helps the organization to achieve its objectives, improves risk management, strengthens internal controls, and enhances overall corporate governance. This case describes the steps that The Schwan Food Company took to establish its internal audit department, including finding a highly qualified chief audit executive, defining the internal audit department's mission, developing the audit charter, staffing the department, creating an overall audit strategy, and assessing the department's effectiveness. The exhibits provided in this case are used with permission straight from the company's files, and all the information in this case is factual. The case is appropriate for an auditing class or an internal audit class at the senior or graduate level.

* G. Randolph Just, CMA, CPA, CIA, CFE, CISA, CFSA, CCSA, was vice president, Audit Services, at Allina Hospitals & Clinics in Minnetonka, Minnesota, USA when he died in January 2006. He was previously chief audit executive for The Schwan Food Company.

BACKGROUND

The Schwan Food Company began in 1952 with one man and one truck. Marvin Schwan, the founder, was the son of German immigrants who came to the United States in 1920. He and his parents ran a creamery in Marshall, Minnesota, but were having trouble making ends meet. Marvin discovered that because of government pricing structures, he could sell ice cream for a few cents more in Yellow Medicine County, immediately north of Marshall. On March 18, 1952, he borrowed some dry ice bags and headed north in his used 1946 Dodge panel van with 14 gallons of ice cream. He knocked on farmhouse doors and sold all the ice cream. The next day he did the same thing again. Now, five decades later, The Schwan Food Company has gone from one man and one truck to 6,500 drivers in the Home Service business unit, and home delivery constitutes approximately 40 percent of the company's total revenues. The pale yellow trucks that the delivery people drive are the most recognized components of The Schwan Food Company's brand. Officially, the color is called "Inca Gold," and it was supposedly the founder's favorite color. "I think the legend is that he had a favorite tie with that color," explains Mike Gunderson, manager of corporate communications for The Schwan Food Company. Examples of home delivery items are listed in Exhibit 1.

In addition to home delivery, The Schwan Food Company's primary business units have grown to include its Global Consumer Brands unit and its Food Services group. The Global Consumer Brands unit manufactures, markets, and delivers frozen foods to grocery, warehouse, club, and convenience stores across the country. The Food Services group manufactures, markets, and distributes value-added frozen food products to public and private schools, universities, healthcare facilities, convenience stores, and chain restaurants. Today, The Schwan Food

EXHIBIT 1

Examples of The Schwan Food Company's Home Delivery Items*

Mini Deep Dish Cheese Pizza:

6 trays of 4 for \$9.99

Oven Ready Breaded Shrimp:

1.5 pound bag for \$12.99

Chicken Egg Rolls:

16 2-ounce portions for \$11.99

Chicken and Broccoli Express Bowl:

2 12-ounce bowls for \$7.49

Apple Cinnamon Flavored French Toast Sticks:

Approx. 40 sticks for \$6.79

Cheese and Herb Biscuits:

18 biscuits for \$5.99

Stuffed Potatoes:

8 5-ounce portions for \$8.99

Creamy, Rich Vanilla-Flavored Premium Ice Cream:

half gallon for \$5.69

Vanilla Sundae Cone:

24-count box for \$12.99

*A complete list of home delivery items is available at www.schwans.com.

Company's workforce consists of approximately 24,000 people, and grosses \$3.5 billion in annual sales.

IMPETUS FOR CHANGE

At The Schwan Food Company, the establishment of an internal audit department (IAD) was driven by personnel changes at the top executive levels. The first non-family-member CEO, M. Lenny Pippin, came on board with nearly 30 years experience in the food industry. At about the same time, David Kidwell, Dean of the Carlson School of Management at the University of Minnesota, began his service as the new audit committee chairman. Three years later, Tracy Burr, formerly a partner at Ernst & Young as well as at Deloitte & Touche, was hired as the new CFO. This new leadership helped the company to slowly make changes, such as an improved governance structure with the establishment of an IAD, but at the same time allowed it to retain the positive aspects of the company's corporate culture, including a high standard of ethics, values, and hard work. Thus, the creation of the IAD was part of a company-wide effort to improve the control and governance structures for a privately-held, but global, company that has the goal to double its size in five years.

FINDING A CHIEF AUDIT EXECUTIVE

The formation of The Schwan Food Company's IAD began when, after conducting a regional and national search through a recruiting firm, the management team hired G. Randolph Just as the Chief Audit Executive (CAE) who brought with him extensive Big Four public accounting and internal auditing experience.

Coincidentally, Mr. Just grew up on a farm only 24 miles north of The Schwan Food Company's headquarters in Minnesota, although he had no formal relationship with the company until his hiring. The well-known yellow delivery truck came to his farmhouse every week. "It was a great event for a kid on a farm to have this truck pull up full of pizza and ice cream. It was a wonderful thing!" he says. "I remember, as a young boy, having a toy truck and making roads around the farmyard, pretending that I was a Schwan route driver making stops throughout the countryside. I even drew a duckling on the Schwan truck! I always admired the company. So when the opportunity arose to join Schwan, I eagerly accepted."

DEFINING THE INTERNAL AUDIT DEPARTMENT'S MISSION

One of Just's first tasks as the new CAE was to develop the IAD's mission statement. The new CAE chose the following mission statement for the IAD which is almost verbatim from the Institute of Internal Auditors' (IIA) definition of the internal auditing function:

"To provide independent, objective assurance services designed to add value and improve The Schwan Food Company's operations. The internal audit department helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of the overall control environment and the network of enterprise business risk management control and governance processes."

The Schwan Food Company's overall mission, or defining goal, is that the company "will be the biggest, the best and the strongest provider of frozen food solutions on the face of the earth."

More specifically, its core purpose is “to enrich the quality of lives through our food solutions.” Thus, the IAD’s newly defined mission corresponds with The Schwan Food Company’s overall mission in that the department exists to help the company reach its goals and achieve its business objectives in an ethical, legal, and well-governed manner. This mission is accomplished by helping to improve controls, business processes, and business risk management.

DEVELOPING AN AUDIT CHARTER

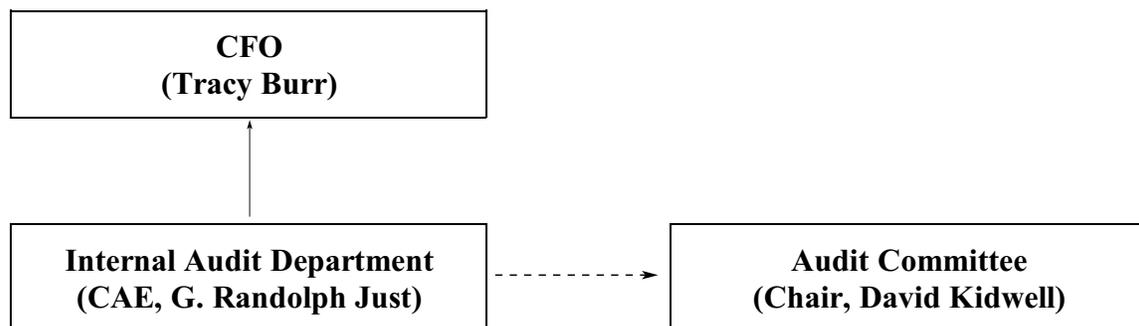
Crucial to the establishment of an IAD is the development of its written charter. The charter states the purpose, authority, and responsibility of the internal audit activity and establishes what senior management and the board of directors expect from the CAE and the internal audit staff. The Institute of Internal Auditors has developed *International Standards for the Professional Practice of Internal Auditing*, which begin with attribute standards, or standards that address the characteristics of organizations and parties performing internal audit activities. The first attribute standard states, “The purpose, authority, and responsibility of the internal audit activity should be formally defined in a charter, consistent with the Standards, and approved by the board.”

A charter, which should be approved by the audit committee on behalf of the board of directors, is critical for sending the message throughout the organization that internal auditing is viewed as a priority and has the endorsement of both executive management and the audit committee.

In addition to specifying the department’s mission statement, the charter should also clearly establish the independence of the department. It is critical that internal auditors be organizationally independent of management in order to enhance their effectiveness. This independence allows the auditors to perform their work objectively and without bias or concern that they will be unduly influenced by management on audit issues. The reporting relationships in The Schwan Food Company’s IAD are illustrated in Exhibit 2.

EXHIBIT 2

Reporting Relationships for The Schwan Food Company’s Internal Audit Department*



*A solid line indicates a direct reporting relationship, while a dotted line indicates an advisory reporting relationship.

The CAE reports directly to the CFO for administrative purposes. For purposes of governance, an advisory relationship is established between the IAD and the audit committee of the board of directors. These relationships, however, whether direct reporting or advisory, are flexible, depending on the management styles of individual managers. At present, The Schwan Food Company's audit committee chairman is very much a "hands on" chairman and views his relationship with the department to be as direct as the CFO relationship.

The audit charter protects the IAD's independence by ensuring full access by the CAE to the audit committee and protecting the CAE from removal without the approval of the audit committee. In addition, the charter of the The Schwan Food Company's audit committee establishes that the IAD is accountable to the board of directors through the audit committee. The Schwan Food Company's IAD charter is shown in Exhibit 3.

The Schwan Food Company's external auditor performed an analysis of the initial staffing level requirements for the IAD. Based on auditor recommendations, the audit committee and senior management decided to staff the department with 10 internal auditors supported by an annual budget allocation of approximately \$1.63 million, although the size of the function is expected to increase as the company grows. Ideally, the CAE wanted people at the senior and manager level with public accounting experience, as well as internal auditing work in industry. At the entry staff level, the CAE recognized that it was not possible to find people with that combination of experience. As a result, the IAD was staffed with a fairly broad-based assortment of expertise in financial, operational, compliance, and information systems auditing.

STAFFING

Initially, the greatest challenge faced by The Schwan Food Company in staffing its new department was convincing qualified people to relocate to corporate headquarters in Marshall, Minnesota – a community that is a three-hour drive from Minneapolis and with a population of approximately 12,000. While this is an attractive community for individuals with a family-based lifestyle, it was a hurdle to overcome in seeking to completely staff a new department. The company used industry contacts to recruit staff, in addition to receiving assistance from outside recruiting organizations. Within a few months, the company was able to fill all of its internal audit positions.

DEPARTMENT'S OVERALL STRATEGY

With the staffing completed, the CAE then worked with two of his audit managers in developing an appropriate overall strategy for the IAD. To determine the scope of the department's services, they decided to use: 1) a risk-based assessment methodology that is tied to the Committee of Sponsoring Organizations of the Treadway Commission (COSO) internal control framework and 2) a consumer products business process model that the CAE had previously used when he worked for KPMG LLP.

The consumer products business model describes how a company translates strategic objectives into business goals, processes and tactics to achieve those objectives. The model presented in [Exhibit 4](#) outlines the following factors:

First, **External Business Drivers and Stakeholders**, which are the outside factors and pressures that can prevent an entity from attaining its objectives. These may include the political and legal environment, actions of competitors, customers, trade regulations and others. The next factor is the set of various **Markets** that are relevant to the company's business. Finally, the **Business**

EXHIBIT 3**The Schwan Food Company Internal Audit Services Charter****PURPOSE**

The purpose of The Schwan Food Company's Audit Services department is to provide independent, objective assurance services designed to add value and improve the organization's operations. It helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of the overall control environment and the network of enterprise business risk management, control, and governance processes.

SCOPE OF WORK

The scope of work of The Schwan Food Company's Audit Services department is to determine whether the organization's network of enterprise business risk management, control (including reporting and disclosure controls), and governance processes, as designed and represented by management, is adequate and functioning in a manner to ensure:

- Risks are appropriately identified and managed.
- Interaction with the various governance groups occurs as needed.
- Significant financial, managerial, and operating information is complete, accurate, reliable, and timely.
- Employees' actions are in compliance with policies, standards, procedures, and applicable laws and regulations.
- Resources are acquired economically, used efficiently, and adequately protected.
- Programs, plans, and objectives are achieved.
- Quality and continuous improvement are fostered in the organization's control processes.
- Significant legislative or regulatory issues impacting the organization are recognized and addressed appropriately.

Opportunities for improving management control, profitability, and the organization's image may be identified during audits. They will be communicated to the appropriate level of management.

INDEPENDENCE

To provide independence, the reporting relationships, authority and responsibility of The Schwan Food Company's Audit Services department are established by the Audit Committee on behalf of the Board of Directors. The chief audit executive reports to the chief financial officer for administrative purposes and also has full and independent access to the chief executive officer and the Audit Committee. Personnel in The Schwan Food Company's Audit Services department report to the chief audit executive. The approval of the Audit Committee is required for the removal or replacement of the chief audit executive. It is the policy of the Audit Committee to devote a portion of each meeting to an executive session at which only the chief audit executive is present. In at least two meetings per year, outside director members of the Audit Committee shall consult privately with

(continued)

EXHIBIT 3 (continued)

the external auditors and with the chief audit executive and report the results of the private consultations to the Board of Directors. In addition, the senior internal audit executive will have opportunity to meet with independent directors on the Audit Committee at each committee meeting.

ACCOUNTABILITY

The chief audit executive, in the discharge of his duties, shall be accountable to management and the audit committee to:

- Provide annually an assessment on the adequacy and effectiveness of the organization's processes for controlling its activities and managing its risks in the areas set forth under the purpose and scope of work.
- Report significant issues related to the processes for controlling the activities of the organization and its affiliates, including potential improvements to those processes, and provide information concerning such issues through resolution.
- Periodically provide information on the status and results of the annual internal audit plan and the sufficiency of department resources.
- Coordinate with and provide oversight of other control and monitoring committees and functions (for example, enterprise risk management, controllership, treasury, governance, finance, disclosure, ethics and quality committees; risk management, quality assurance, regulatory compliance, security, legal, environmental, and external audit functions).

RESPONSIBILITY

The chief audit executive and staff of The Schwan Food Company's Audit Services department have responsibility to:

- Develop a flexible annual internal audit plan using an appropriate risk-based methodology, including any risks or control concerns identified by management, and submit that plan to the audit committee for review and approval as well as periodic updates.
- Implement the annual internal audit plan, as approved, including as appropriate any special tasks or projects requested by management and the audit committee.
- Maintain a professional audit staff with sufficient knowledge, skills, experience, and professional certifications to meet the requirements of this Charter.
- Evaluate and assess significant merging/consolidating functions and new or changing services, processes, operations, and control processes coincident with their development, implementation, and/or expansion.
- Issue periodic reports to the audit committee and management summarizing results of audit activities, including significant audit issues and management action plans.
- Keep the audit committee informed of emerging trends and successful practices in internal auditing.

(continued)

 EXHIBIT 3 (continued)

- Provide a list of significant measurement goals and results to the audit committee.
- Assist in the investigation of significant suspected fraudulent activities within the organization and notify management, the external auditors and the audit committee of the results.
- Consider the scope of work of the external auditors and regulators, as appropriate, for the purpose of providing optimal audit coverage to the organization at a reasonable overall cost.

AUTHORITY

The chief audit executive and staff of The Schwan Food Company's Audit Services department are authorized to:

- Have unrestricted access to all functions, records, property, and personnel.
- Have full and free access to the audit committee.
- Allocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish audit objectives.
- Obtain the necessary assistance of personnel in units of the organization where they perform audits, as well as other specialized services from within or outside the organization.

The chief audit executive and staff of The Schwan Food Company's Audit Services department are not authorized to:

- Perform any operational duties for the organization or its affiliates.
- Initiate or approve accounting transactions external to The Schwan Food Company's Audit Services department.
- Direct the activities of any organization employee not employed by The Schwan Food Company's Audit Services department, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist internal auditors.

STANDARDS OF AUDIT PRACTICE

The Schwan Food Company's Audit Services department will meet or exceed the *Standards for the Professional Practice of Internal Auditing* of The Institute of Internal Auditors.

 Chief Audit Executive

 Chief Executive Officer

 Audit Committee Chairman

Processes define how work is done in the company and how outputs of one process become the inputs of the next. Business processes are broken down into three sections:

1. The **Strategic Management Process**, which defines the company's mission and objectives, as well as the risks that threaten the objectives, and establishes processes to monitor and manage those risks and achieve the objectives;
2. **Core Business Processes**, which develop, produce, sell and distribute the company's products;
3. **Resource Management Processes**, which support the other processes. These include functions such as human resources, information technology, accounting and others.

Included in the overall consumer products business model are lists of the company's **Alliances, Core Services/Products, and Potential Customers**.

As part of this risk assessment methodology, the CAE reviews the strategic plans of the company and all the business units. The department's efforts are then targeted toward the key areas and objectives upon which the company and each of the business units are focusing. To accomplish this objective, the auditors meet with executives at the various business units and walk through a questionnaire that they have developed as part of the risk-based assessment approach (see Exhibit 5 for the questionnaire and the particular business risks and factors discussed).

EXHIBIT 5

Business Risk Assessment Interview Topics

The following questions and topics are intended as an overview of the type of discussion we would like to foster through our risk assessment interview process. Please use this information as a guide for our discussion. It does not have to be filled out in advance.

Overview

- 1) Discuss business strategies for your area of responsibility.
- 2) Discuss key business processes performed within your area of responsibility.
- 3) Discuss key business initiatives: current, upcoming, and/or ongoing.

Risks

- 1) What business risks do you see within your area? (See attached list of potential business risk factors.)
- 2) Can you estimate the likelihood of these risks occurring? (Example: high – very likely this will happen; medium; low)
- 3) Can you estimate the impact of these risks? (Example: high impact; medium; low)
- 4) Do you have a process for measuring and identifying these risks?

Controls

- 1) Briefly describe what controls are in place to protect against these risks.

Other Items

- 1) Do you have other areas of concern outside your immediate responsibilities?

(continue)

EXHIBIT 5 (continued)
Business Risk Categories and Risk Factors (for discussion)

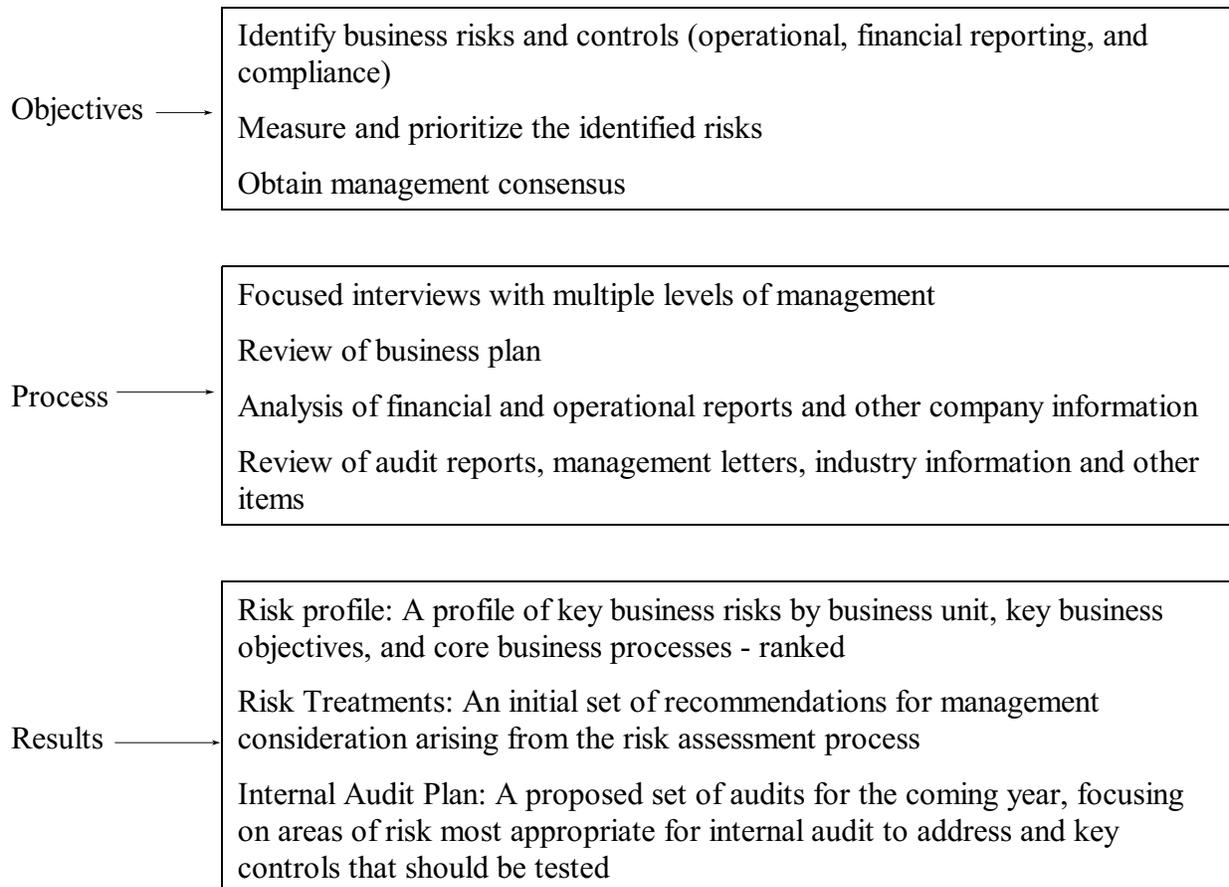
| <i>Risk Category</i> | <i>Risk Factors</i> | |
|----------------------|---|---|
| External Environment | <ul style="list-style-type: none"> • competition • financial markets • political • regulatory | <ul style="list-style-type: none"> • industry • owner relations • business interruption |
| Control Environment | <ul style="list-style-type: none"> • support • measurements | <ul style="list-style-type: none"> • legal • strategic |
| Infrastructure | <ul style="list-style-type: none"> • leadership • human resources | <ul style="list-style-type: none"> • information management |
| Marketing & Selling | <ul style="list-style-type: none"> • product branding • satisfaction • services • competition | <ul style="list-style-type: none"> • product development • products • marketing • distribution channels |
| Supply Chain | <ul style="list-style-type: none"> • purchasing • cost | <ul style="list-style-type: none"> • raw material management • vendor management |
| Liquidity | <ul style="list-style-type: none"> • cash flow • assets • cost of capital | <ul style="list-style-type: none"> • exchange rates • taxation • funding requirements |
| Operations | <ul style="list-style-type: none"> • processes • production cycle • capacity | <ul style="list-style-type: none"> • finished product management • contingency planning • incentives |

Next, the CAE weighs and prioritizes potential projects across all the business units, while giving consideration to the volume of their activities and their importance to the company's overall strategic plan (see Exhibit 6 for a graphical representation of an overview of the risk assessment objectives, process, and results).

RISK-BASED METHODOLOGY

The risk assessment framework closely incorporates the concepts of risk and control. The Schwan Food Company establishes business objectives at all levels of the company, from the corporate level down through each business unit. To achieve these objectives, the company puts in place core business processes, which are groupings of related business activities (e.g., procure materials, manufacture products, distribute products, sell products, serve customers). The core business practices are upheld by support processes that provide resources and services to the core business processes. Risks threaten the achievement of business objectives at all levels, while

EXHIBIT 6
Risk Assessment Overview



controls are the activities Schwan puts into place to manage or mitigate the risks. Controls are often built into the core business processes and support processes (see Exhibit 7 for a graphical representation of the risk assessment framework).

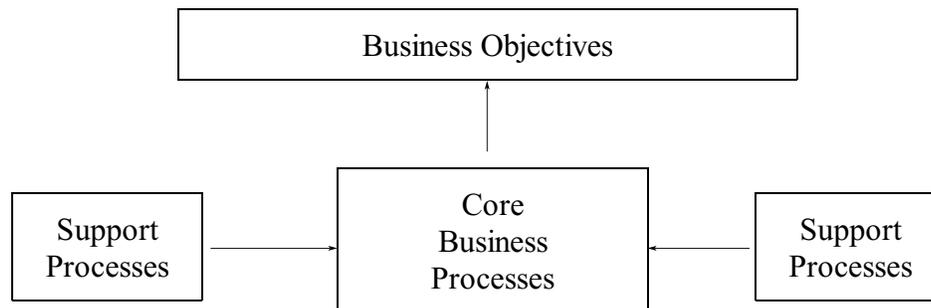
Within each process, the internal audit personnel assess gross risk (threats or impediments to the accomplishment of corporate or process objectives), the strength of relevant controls and of management's response to the identified risks, and residual risk (a re-evaluation of risk in light of controls and management's response). At the end of this process, residual risks are compared to gross risks for reasonableness. See [Exhibit 8](#) for a graphical representation of this risk assessment.

The risks are rated based on the magnitude of the impact to the organization of the risk occurring, as well as on the probability of occurrence. Residual risk assessments are conducted through focused interviews with multiple levels of management, a review of business plans, analysis of financial and operational reports, and a review of miscellaneous information (e.g., industry information, process documentation, etc.). For validation, the assessment results are discussed with the appropriate levels of management.

EXHIBIT 7
Risk Assessment Framework

RISKS

RISKS



RISKS

RISKS

For example, at The Schwan Food Company food quality and food safety are two areas of continual vigilance. The internal audit personnel will assess a gross risk of raw materials contamination at a certain level, but to control this very serious risk, every single batch of raw materials or product that comes into The Schwan Food Company's factories is tested for contamination. As a result of these very stringent controls that are in place, the residual risk is assessed as extremely low. For additional examples of residual risk ratings, see Exhibit 9.

Those business functions or processes with residual risk above a certain level are considered candidates for potential internal audit projects. The first question, however, is what expertise or resources are needed to best address the residual risk. Can management address the risk directly without an intervening internal audit project? In some cases, risks identified during the assessment process can be directly addressed by management. In other cases, either the legal department, the compliance department, or the external auditors, may be the most appropriate resource. Those functions or processes most appropriately addressed by the IAD are entered into the internal audit plan. That plan is reviewed with senior and business unit management and must be approved by the audit committee.

ASSESSMENT OF EFFECTIVENESS

The CAE reviews the status of the overall internal auditing plan with the auditing committee five times a year, on average. The success of the IAD is primarily measured against the criteria of whether the internal auditors are adding value to The Schwan Food Company. For example, are the major internal audit projects being completed? Is the IAD receiving requests from the business units for other projects? The CAE budgets approximately 80 percent of the internal audit staff time for projects identified through the risk assessment process, leaving 20 percent of their time open for

EXHIBIT 9
Examples of Residual Risk Ratings

Risks and controls are compiled by process. The average ratings per process are used to construct bar charts

| Description of Risk | Process | Gross Risk Rating | | | | | | Residual Risk Rating | | | | | | |
|--|----------------------|-------------------|---|----------|---|-----|------------------------------|----------------------|--|---------------------|----|----------------|----|-------|
| | | Probability | P | Impact | I | PxI | Control Effectiveness Rating | C | Description of Control/Response | Revised Probability | P2 | Revised Impact | I2 | P2xI2 |
| Uncertainty of exchange rates and volatility of oil price makes profit assurance difficult. | Treasury and Finance | likely | 4 | moderate | 3 | 12 | weak | 1 | No preventive controls are available. Management monitors profitability levels. Hedging is not performed by Sub. ABC Co. - US performs any hedging activity. | likely | 4 | moderate | 3 | 12 |
| Risk relating to the inaccurate forecast of volume requirements of ABC company. | Procure materials | moderate | 3 | major | 4 | 12 | strong | 3 | Specialize in the farm-to-fryer concept. Employs geographic diversification to help mitigate risk. | moderate | 3 | moderate | 3 | 9 |
| Poor visibility of inventory distribution chain can result in product stock-outs and oversupply. | Manufacture products | likely | 4 | minor | 2 | 8 | moderate | 2 | Moving from weekly to daily order processes and a more automated replenishment process. | moderate | 3 | minor | 2 | 6 |

emerging priorities. In its first year, the department received a large number of requests from the business unit customers for other projects, and that was clearly viewed by the audit committee as a substantial measure of success.

During the meetings with the audit committee, the CAE also reports the percentage of completion of the audit plan, although this is not the primary measure of the IAD's success since the department is intended to address risk as it arises. Consequently, the annual internal audit plan is considered to be flexible as it may be revisited on occasion throughout the year and changed as particular needs dictate.

Another major measure of success has been the open acceptance of the department by the business units and their willingness to work with the internal auditors. During the audits scheduled through the risk assessment process, company personnel were willing to offer ideas on areas that they thought they could use additional audits. Several personnel called the internal auditors for assistance as events occurred during the year. For additional monitoring of the effectiveness of the department, the CAE recently implemented a 9-question internet-based audit client survey that is used to gather input and feedback from the audit customers on each of their audit projects (see Exhibit 10).

As time passes and the IAD becomes more established, other metrics of success will probably be developed, such as the percentage of audit recommendations implemented by the various business units.

CONCLUSION

An effective IAD adds value to its organization in numerous ways. It helps the organization to achieve its objectives, improves risk management, strengthens internal controls, and enhances overall corporate governance. In short, a well-designed and functioning IAD advances the business. As such, the motto of The Schwan Food Company's IAD is "advancing the business."

DISCUSSION QUESTIONS

1. Why might a company decide to establish an internal audit department (IAD)?
2. Why was The Schwan Food Company, a private company, motivated by the Sarbanes-Oxley Act of 2002 (legislation pertaining only to public companies) to install an internal audit function? List specific factors (both internal and external) that may have caused The Schwan Food Company to change its internal control practices and corporate governance structure.
3. Given The Schwan Food Company's particular situation and set of circumstances at the time that their internal audit function was implemented, what essential characteristics and qualifications should their new Chief Audit Executive (CAE) have possessed?
4. Exhibit 3 includes The Schwan Food Company's Internal Audit Services Charter. Briefly discuss why each of the sections of this charter is necessary and appropriate.
5. Undoubtedly, many non-audit employees at any organization might be initially intimidated at the thought of the establishment of an internal audit department and having to answer questions from internal auditors. What might The Schwan Food Company's new Chief Audit Executive have done to alleviate these initial fears and concerns? What steps could the new CAE have taken to reduce the "us vs. them" relationship between The Schwan Food Company's non-audit employees and the staff of internal auditors?

EXHIBIT 10
The Schwan Food Company Audit Services Client Satisfaction Survey

| | <u>Strongly</u> <u>Agree</u> | <u>Agree</u> | Neither Agree or <u>Disagree</u> | <u>Disagree</u> | <u>Strongly</u> <u>Disagree</u> | No Basis to <u>Respond</u> |
|--|---------------------------------|--------------|--|-----------------|------------------------------------|----------------------------------|
| 1 I was pleased with Audit Services’: | | | | | | |
| a. Knowledge | _____ | _____ | _____ | _____ | _____ | _____ |
| b. Professionalism | _____ | _____ | _____ | _____ | _____ | _____ |
| c. Communication | _____ | _____ | _____ | _____ | _____ | _____ |
| Please provide comments: | | | | | | |
| 2 Audit Services respected my existing workload: | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 3 The objectives, purposes, and scope were clearly communicated to me: | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 4 Communication of results and status was timely and adequate. | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 5 My business concerns and perspective were adequately considered: | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 6 The action items made business sense: | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 7 Overall, this audit or project provided value to me: | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 8 I consider The Schwan Food Company’s Audit Services to be a valuable business partner: | | | | | | |
| Please provide comments: | _____ | _____ | _____ | _____ | _____ | _____ |
| 9 Please provide recommendations that would improve the process: | | | | | | |

6. It is critical that an organization's IAD be independent. How might a charter ensure this goal is accomplished? How did The Schwan Food Company's IAD charter contribute toward ensuring independence?
7. Read the executive summary of Internal Control – Integrated Framework by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission (see http://www.coso.org/publications/executive_summary_integrated_framework.htm) and summarize its main points. Critique and evaluate The Schwan Food Company's initial efforts to implement their internal audit function using the five internal control components as a rubric. How well were each of these five internal control components initially established? Assign scores from 0 (worst) to 5 (best) for each component. Ask students to compare and justify their scores.
8. Read the article entitled, "Does Your Control System Pass the COSO Test?" *Tone at the Top*, The Institute of Internal Auditors, March 1998 at the following link: <http://www.theiia.org/download.cfm?file=57080>. Use the contents of this article to evaluate whether the newly installed audit function at The Schwan Food Company passes the COSO test.
9. Read the article entitled, "Struggling to Incorporate the COSO Recommendations into Your Audit Process? Here's One Audit Shop's Winning Strategy," by Applegate and Will, *Internal Auditor*, December 1999, at the following link: http://www.coso.org/audit_shop.htm. Contrast the two strategies taken by The Boeing Company and The Schwan Food Company in incorporating the COSO recommendations into their respective audit processes. What can the new IAD at The Schwan Food Company learn from the COSO-based internal audit function at The Boeing Company?

TEACHING NOTES

Teaching notes are available from the editor. Send a request from the "For Contributors" page of the journal website, <http://gpae.bryant.edu>.