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FOREWORD

Most organizations with an internal audit department also have some form of intellectual property rights. Whether the organization is a large privately held firm or a small governmental entity, there is likely intellectual property that has value worth tracking through management and auditing through the organization’s audit department. This book addresses some of the key concerns internal auditors should have when assessing key risks related to intellectual property and steps to consider when auditing the intellectual property process within their respective organizations.

For organizations that have a substantial amount of intellectual property, the internal audit team should audit intellectual property periodically to help ensure that the organization’s rights are captured, preserved, safeguarded, and valued properly. They must ensure that the staff performing the audit is qualified and the purpose of the audit is clearly articulated before they begin.

It would be prudent for the audit team to have a well-defined scope when auditing intellectual property to ensure that all resources are used efficiently and effectively. To this end, the preliminary review of the intellectual property process should be designed to provide insight regarding how to best employ audit resources and identify limitations imposed upon the audit staff when conducting the audit. To facilitate and enhance the audit process flow, charting the workflow often provides an overall view of how intellectual property becomes part of the organization and is subsequently managed.

The audit should include tests of controls and substantive tests, the timing of which will vary depending on the organization’s characteristics. Once the tests are complete, the internal auditors should be in a position to report findings to executive management. The report should be directed to a level that is high enough to ensure corrective action is implemented.
In summary, most organizations can conduct an audit of intellectual property in a reasonable amount of time and that, hopefully, yields meaningful findings.
ACKNOWLEDGMENTS

This project is the result of a tremendous amount of effort and support from numerous individuals. The list of everyone who had a direct or indirect effect on the outcome of this book is quite lengthy. I would like to thank my family and friends for their support. Also, I would like to extend my gratitude to the IIARF staff for their continuous encouragement and extensive editorial work.

This book is intended to assist organizations in assessing intellectual property and related operations. I am very grateful for all the comments provided since the first edition was published more than a decade ago. Many individuals provided valuable information and comments that influenced the outcome of this second edition.

I extend my thanks and gratitude to all who have contributed substantially to the development and implementation of this work. I am extremely grateful for your time and effort. I continue to encourage input and suggestions from readers inside and outside the audit community.
ABOUT THE AUTHOR

JAMES S. FARGASON, CIA, LLM, CMA, CPA, CFE, has published several works in the areas of law and accounting. He has been an active member of The IIA for more than 20 years and is a Certified Internal Auditor. He has presented at various IIA regional and international conferences on a variety of topics, including auditing contracts, auditing intellectual property, auditing legal counsel, and auditing fraud cases.

Fargason has extensive experience in the areas of law and auditing, and has served as a faculty member at three research universities. He holds a distinguished professorship at Louisiana State University (LSU), where he teaches in the MBA program and at the law school. He has a law degree from Tulane University, which involved studies in Siena, Italy, in comparative and international law. Before accepting a full-time faculty position teaching courses in law and auditing, he practiced law with several prominent law firms conducting litigation in numerous jurisdictions, including California, Washington, Texas, Louisiana, and Arizona.

He has done work for a variety of organizations, including the Federal Reserve, Chase, Deloitte, General Motors, Dow, International Monetary Fund, Microsoft, and Brunswick. He also offers onsite training and audit assistance to organizations throughout the world. Fargason can be reached via email at fargason@lsu.edu.
Chapter 1

INTRODUCTION

The purpose of this book is to provide a guide for internal auditors to perform an audit of intellectual property. Chapter 1 serves as an introduction. The second chapter covers types of intellectual property. The focus of the content is on four main areas: patent, trademark, copyright, and trade secrets. While there are other forms, these are the main types that should be included in an audit conducted on intellectual property.

Chapter 3 includes a discussion of the qualifications of the audit staff. The book stresses that they should collectively possess the knowledge, skills, and discipline to conduct the audit. The depth of the audit may vary depending on the qualifications of the auditors. Audit teams with limited technical expertise may still be in a position to perform limited testing.

Before beginning the audit, the team should consider the overall purpose, which is the subject of chapter 4. General purposes include an evaluation of the internal control structure related to intellectual property. The audit team also should look at substantive accounting issues to ensure that the organization is in compliance with Generally Accepted Accounting Principles (GAAP). The purpose of the audit may be expanded to include improving the efficiency and effectiveness of how the intellectual property process is organized and executed.

Chapter 5 examines the scope of the audit. The audit team may elect to narrow the scope on grounds of restricted subject matter or access to specific geographical locations. Such limitations do no constitute grounds to totally abandon the audit, though results could be qualified given such constraints.
Chapter 6 looks at the preliminary review. Internal auditors should conduct a preliminary review of the intellectual property process to gain a better understanding of how the organization handles new forms of intellectual property it acquires. Additionally, such a review may provide greater insight into which areas the audit resources should be concentrated.

While it is not imperative to flowchart the process, even a simple flowchart can provide great insight into how the intellectual property process is maintained and organized. Accordingly, chapter 7 discusses some of the considerations and concerns the team should contemplate.

It is highly recommended that the internal auditors perform control tests when conducting an audit of intellectual property. Such tests should include an assessment of how assets are safeguarded and protected against theft or loss. Other tests of controls are discussed in chapter 8.

The auditors should also conduct substantive tests to ensure that intellectual property is properly valued and placed on the financial statements in the appropriate period in accordance with GAAP. A variety of substantive tests are discussed in greater detail in chapter 9.

Once the audit is complete, the team should report findings to executives who have the power to implement change and take corrective action. Chapter 10 outlines some of the executives that may be on that reporting list, along with concerns such as confidentiality.

Auditing intellectual property is a worthwhile endeavor. The audit can be performed within a reasonable time and provide potential cost savings to the organization. Hopefully, this book will provide insight into some key audit steps to consider conducting when performing an audit on intellectual property.