

Raising the game: The Audit Committee - Internal Audit Relationship

Audit committees are no doubt shouldering heavier responsibilities than ever before. In light of growing expectations from shareholders, regulators and other stakeholders, audit committees need to forge closer ties and maximise the value they get from an already established pool of resources.

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The internal audit function is an example of a key resource. Naturally, greater scrutiny from stakeholders these days have audit committees developing higher expectations of internal audit functions and requiring them to deliver value more efficiently and effectively.

So how should audit committees oversee and monitor the effectiveness of internal audit?

There are several elements that underpin the relationship between the audit committee and internal audit function. This strategic partnership is not only critical to ensuring the audit committee delivers accurate and transparent information but also in providing valuable insight to understanding how effectively the company is managing its business and financial reporting risks.

Building a trust-based relationship

The audit committee and internal audit function should not work in silos. In overseeing internal audit, audit committees must demonstrate visible support when needed. If audit committees value the insight that internal audit provides, they must communicate this to the entire organisation and ensure other Board members appreciate the importance as well as the level of comfort it gives.

When such support is extended to the internal audit function, empowerment is likely to follow. Sometimes this can mean having the courage to raise sensitive matters to the audit committee and creating awareness at Board level. When this happens, proposed recommendations are more likely to gain acceptance and be implemented instead of negotiating a watered-down approach.

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In action, this could mean:

- Regular one-to-one meetings between the internal audit Head/Chief Audit Executive and the audit committee chair.
- Inviting department heads whose departments have received a poor internal audit rating to an audit committee meeting so that he/she may provide explanations and how the situation can be re-mediated.
- Reviewing of significant internal audit recommendations that have not been implemented in accordance to a specified time line.

Clarifying roles

What role do Management and the audit committee want internal audit to play?

An internal audit function may be performing a wide spectrum of work but not all of its efforts are being channeled to the right places. This could sometimes be a result of poor communication and/or different perceptions between the different levels of hierarchy within the organisation.

The roles and responsibilities of internal audit should be clear and understood by all. The Board, as well as management should have collective agreement on where internal audit efforts should be channeled to (i.e. internal audit's priorities/areas of focus). Only then can expectations be communicated and resources directed to the intended areas of focus.

In action, this could mean:

- Evaluate if the audit committee is sending a clear, one-voice message to the rest of the organisation on internal audit's plan, approach and priorities.
- Discuss and agree on the expectations that the audit committee has of internal audit - this should be made known to both Management and the Chief Audit Executive.

Establishing clear reporting lines

Ideally, internal audit should report directly to the audit committee. It is crucial for internal audit to attend audit committee meetings as well. These measures instill empowerment within the internal audit function to report directly to the audit committee should any issues warrant it.

Communicating effectively

This relates to effective reporting. Typically, an effective internal audit report demonstrates a succinct manner of reporting, as well as at an appropriately summarised level.

The Chief Audit Executive should have a good level of understanding of Management's expectations and therefore exercise reasonable judgment to identify only the findings that pose significant impact to the company.

Audit committees can consider periodical meetings with internal audit to discuss the amount and type of information that is appropriate for submission to Management.

Taking this relationship to the next level clearly is not the easiest of tasks. In a landscape of growing scrutiny and expectations from stakeholders, audit committees and internal audit functions will be put to a test but strengthening this relationship will help companies mitigate their overall risks better and more efficiently too.

Further reading

11th Annual State of the Internal Audit Profession Study

The 2015 issue of the State of the Internal Audit Profession Study talks through how internal audit functions that are aligned with a business' new direction and are operating at the forefront of the companies' most relevant risks, are highly valuable contributors to the organization. The study highlights four key areas that enable internal audit to contribute to their organizations' strategic and transformational initiatives.

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