



“Dear Audit Committee Chair”

Over several years I have worked with Heads of Internal Audit (HIA / CAEs) to support their leadership of Internal Audit teams. Over the years a number of themes have emerged in relation to Audit Committees - those which have been instrumental in helping HIAs perform well and those which have not, with many others in-between.

What follows is a summary of a selection of key points, not intended to be exhaustive, effectively saying: “Dear Audit Committee Chair.... If the Audit Committee really wants to help Internal Audit (IA), here’s what you need to understand”.

- 1. If the working relationship between the Audit Committee and IA is going to be mutually productive, it is important that we don’t confine the contact that we have just to formal meetings.** Briefing meetings before each Audit Committee meeting are a start to deepening our working relationship. However, there is no substitute for spending time with the IA team, from time to time, to understand some of the challenges and dilemmas they face, and to directly communicate what is important. *Direct contact between the Audit Committee and IA team normally has significant benefits in terms of team morale. Furthermore, it will then be easier for the Audit Committee to highlight any points arising to senior management without it seeming as if the HIA has spoken “out of turn”.*
- 2. If you primarily see Internal Audit as a support to the External auditor, mostly in terms of helping to reduce the External Audit fee, you may be missing all you can get from Internal Audit.** Of course it’s sensible that IA can directly help to reduce External Audit fees, but with a limited amount of overall resource in the team, this will also reduce the work spent looking at more important business risks, operational processes and compliance obligations. In addition, External Auditors will typically not want to sub-contract the most important financial auditing areas to IA, meaning that the real value add from this work is reduced. So consider clarifying with the External Auditor how much extra financial control auditing they would have to do if IA did not do it, and how much that would cost?
- 3. Do you recognise that most senior managers and most line management don’t really want to be audited** and would much prefer IA to work on advisory assignments, supporting new business initiatives, designing new processes and finding cost saving and efficiency

opportunities? The IA team understands that assurance assignments will be valued by the Audit Committee, but the reality of organisational life is that IA will not get much real business engagement and respect if it is mostly seen as an evaluator or “policeman”. This is an awkward point for an HIA to raise and normally HIAs do their best to please both the Audit Committee and Senior Management. However, the truth is that with limited resources this is a challenging balancing act. So, *consider asking for the balance of IA work between advisory and assurance assignments and agree this with Senior Management.*

4. **Please ensure you have realistic expectations of the depth of and breadth of work that can be done by Internal Audit.** Sometimes IA will look at an area and later on, something may go wrong. At that point the Audit Committee may ask “Why didn’t IA spot the issue?” - this is a fair question, but perhaps the key point to focus on is: “Why didn’t management spot the issue?”! In addition, it is possible that the Audit Committee may have a rather optimistic view of how much depth IA is able to go to. All IA teams have to make judgments about the depth of work they do and auditing areas in a lot of depth will affect the breadth of coverage elsewhere. *So ask yourself how well you understand the depth versus breadth choices that the IA team is making,. Also develop a clearer understanding of the depth of assurance that IA is giving on key assignments, ranging from a “high level review” to a “detailed audit” to a “full investigation”.*
5. **Please don’t forget that Internal Audit does not have the prime responsibility to manage risks and operate controls.** It’s right that the Audit Committee should probe the work of IA and be interested in the IA view of remediation progress. However, this can sometimes result in de-emphasising that line management has the prime accountability for managing risks and operating controls, and that it is line management and staff that need to remediate processes and controls that are not working. *The Audit Committee should consider when was the last time that senior managers from the business were asked to attend the Audit Committee in person to explain what went wrong, and whether they are emphasising sufficiently the line management responsibility to drive remediation actions and the senior management role to keep track of progress and proactively address any slippage?*
6. **More generally, is there a clear and documented summary of how assurance activities are “joined up” in the organisation.** There are often a number of sources of assurance in an organisation that play a role in ensuring that risks are being managed and that processes and controls are working. This will include External Audit and the Finance function for financial reporting and financial controls; (perhaps) a Health, Safety & Environmental function, a Security function and other Product and/or

Service Quality functions. Being clear about how these roles fit together, alongside normal management oversight activities, is becoming an increasingly important priority for many organisations, to avoid governance fatigue, to streamline who does what and to identify and address any assurance gaps. Such a picture can also support consolidated reporting to the Audit Committee and board across the range of risk areas the organisation has. So, the *Audit Committee should consider whether the overall assurance picture for the organisation has been documented and ensure that they have reviewed this carefully*. Note that a rushed assurance map will not yield many benefits of value, whereas when this is done properly, it will reveal insights into the way specific key risks are being managed, formalising the accountabilities in the organisation and delivering actions that will streamline what is being done and also to address any key gaps.

- 7. Please recognise that what the Internal Audit function finds will often give you important insights into the leadership and culture of the organisation.** Of course all organisations have room for improvement in relation to risk management and process effectiveness, and sometimes audit findings will just be a function of staff or management short-comings in a specific area. However, what IA finds will sometimes reveal deeper insights into the culture and leadership of the organisation. Thus if a process was not working: Was part of the problem a lack of clear accountabilities in relation to what needed to be done? (which may apply to other risks also); Or was the problem symptomatic of a lack of training? (which may apply in other areas as well); Or a lack of management interest and oversight in the nature of the risks the organisation faces and what is being done to manage this?; Or a tendency to underestimate the resources required to manage a risk area properly? It is not easy for IA to open up these thematic and cultural issues, since senior management will naturally be nervous about the cost and time implications of wide-scale improvements. As a result, there are many occasions when HIAs feel that Senior Management will be reluctant to take action on a risk theme, or emerging issue, until after things have gone wrong (by which time real damage has been done). The Audit Committee can play an important role in asking IA what themes are emerging from past audits, and what emerging themes are coming up, and also encourage Senior Management to consider the wider lessons to be learned, so that problems can be headed off in advance, rather than when it is too late.

- 8. Recognise that whilst it is common to talk about the way the Internal Audit team can be used as a centre for talent development and the spreading of risk and control skills across the organisation, only a few achieve this.** In many organisations staff don't really understand the role of IA and even for those who do understand the role, it's rare for IA to be seen as a good and proven way of developing your career. Whilst most senior managers say they want to support IA as a career choice, the reality is that most staff regard working in a front-line or business facing role as a better career choice and most managers will prioritise filling such a "delivery" role over an IA role. Audit Committee members can play an invaluable role in paying close attention to the experience and potential of staff joining the IA team. They should be interested in understanding the extent to which guest auditors and guest advisors are being obtained from the wider organisation. Finally, understanding the mobility of IA staff into other roles will also be a key indicator to in relation to whether IA is genuinely a good career option.
- 9. Pay close attention to what is being measured by the Internal Audit team; since many traditional metrics are becoming outdated.** It is common for the IA team to be measured on the delivery of the audit plan and keeping costs to budget. Other common metrics concern themselves with the audit delivery process; such as the time taken to issue an audit report. Whilst all of these metrics have a place, they can take up a good deal of time to collate and report and many not give particularly good insights into the extent to which the IA team is contributing to the organisation. A focus on "key outcomes" may ensure that IA is being measured at the right level, but – again – care needs to be taken with what is being proposed; for example, a focus on "cost saving opportunities identified" needs to be tempered by recognising that some IA findings may require additional resources to be deployed (but with a reduction in the compliance or reputational risk that the organisation may have). In addition, management feedback on the work done by IA needs to be distinguished carefully between the feedback of those who have just been audited (which may vary depending on the results of the audit), and the feedback of more senior managers, who may judge IA according to the wider contribution to business objectives and priorities. There should also be a clear place for the Audit Committee to express and communicate what they value from IA, so there is a proper appreciation at the Senior Management level of the Assurance role that the IA team is being

asked to perform, and how well it is performing in that regard. Audit Committee members are reminded that “what gets measured, gets done”, and should support and encourage the Head of Internal Audit to ensure that the current IA metrics are appropriate.

- 10. Recognise that the stakes are high for both the Audit Committee and the HIA, so mutual trust and respect will be key.** Of course Audit Committee members have a high profile role and will be concerned to ensure no significant issues arise while the organisation is being overseen “on their watch”. By the same token, the role of the HIA is high profile in the sense that the most difficult risk and assurance issues the organisation faces will need to be resolved by them in conjunction with senior management. *On key points it is very important that there is “no daylight in between” what the HIA proposes and what the Audit Committee is going to support. If an HIA perceives that Audit Committee support can waver, this will act as a limit on their authority and the likelihood of them pushing on certain issues. Note that most HIA’s (and the IA team) will be looking to pursue careers in the organisation and will therefore be reluctant to “stick their neck out” if they are unsure if they are going to get support. Moreover, if they do take a stand on a point and feel they are not supported by the Audit Committee, they will be less likely to take a stand in the future.*

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