

Introduction

Work relationships can sometimes be tricky. What one demands or expects from a relationship can become complicated, and this can contribute to misunderstandings, inefficiency, and even resentment.

But a poor, strained, or superficial relationship between the audit committee and the chief audit executive (CAE) does more than create uncertainty. It can become a serious threat to good governance by contributing to misunderstandings, an inadequately resourced internal audit activity, undermined independence, superficial assurance provision, inefficiencies, missed opportunities, and less than optimal service to the detriment of the organization.

Internal audit should report functionally to the chair of the audit committee (or equivalent) and administratively to executive management, creating a direct line of communications between the CAE and the governing body. This unique partnership reflects the importance of proper management of the relationship. Indeed, this direct channel to the governing body initiates and nurtures the entire concept of independence and objectivity necessary for an effective internal audit activity.

It is imperative, therefore, for the CAE and the audit committee to have a clear understanding of their reporting and alignment responsibilities, including what they should expect and demand from each other. How each party interacts with the other also helps set baseline demands and expectations that are the building blocks of trust and support.

The CAE needs clarity when it comes to the demands and expectations among the audit committee, the chief financial officer, CEO, and other key internal stakeholders. A clear and healthy relationship where trust, transparency, and truth prevail is ideal in terms of establishing the demands placed on each other.

With respect to the audit committee, its responsibilities should be detailed within an audit committee charter. Its primary duty is to oversee the quality and integrity of the company's internal control environment including operational, financial, IT, accounting, and reporting practices.

Interestingly, numerous professional research papers eloquently describe best practices in the audit committee's oversight of the CAE and the internal audit activity. Yet there are relatively few that examine best practices of what the CAE should expect or demand from the audit committee.

KEY TAKEAWAYS

The CAE and the audit committee must have a clear understanding of their reporting and alignment responsibilities, including what they should expect and demand from each other.

The audit committee should demand and empower the CAE and internal audit to act independently and be willing to "speak truth to power."

The audit committee should be prepared to challenge the CAE and internal audit but also be willing to stand with them, rather than behind them.

The audit committee should demand the CAE and internal audit activity meet IIA Standards, be trusted advisors, and represent the audit committee in their efforts.

The audit committee should meet regularly with the CAE to discuss strategic and operational activities.

The IIA's position on the role of internal audit and, more specifically, the CAE is clear. Follow The IIA's *International Standards for the Professional Practice of Internal Auditing*. Be firm. Be strategic. Be courageous. Speak truth to power. Strive to become a trusted advisor.

Surveys indicate that most audit committees have healthy relationships with internal audit. But **The IIA believes there must be more transparency in terms of open demands from each other if assurance and governance are to be strengthened and improved.** Demanding relationships built on mutual respect should be sought out where each side pushes to improve performance.

What the Audit Committee Should Demand From Internal Audit

The Basics: Internal audit is most effective when it follows IIA *Standards*, and its resource level, competence, and structure are aligned with organizational strategy and core business competencies. The audit committee entrusts the CAE to operate the activity with integrity and competency to achieve its purpose.

The audit committee should demand:

- Adherence to IIA *Standards*.
- Internal audit staff obtain relevant certifications demonstrating professional acumen, knowledge, and competence.
- The CAE answers two key questions in an executive session:
 - Do management's actions/behavior conform to its words?
 - What should the audit committee do to help internal audit be more effective?

A Mature Internal Audit Activity: Mature internal audit activities should exhibit a high level of competency in data analytics, sophisticated audit programs, continuous risk coverage agility, an audit rotational model to develop talent, and an automated workpaper environment. Internal audit should be at the forefront of emerging risks, and have metrics that demonstrate the value it contributes to its organization. All of these will enable optimal and efficient operations that deliver maximum value to the organization.

The audit committee should demand:

- Development of a formal "IA Strategic Plan."
- Regular updates from internal audit on progress and changes to the plan.
- Feedback from executive management on internal audit findings and CAE engagement.
- An effective relationship between internal and external audit with evidence of real synergistic benefits occurring.
- A balance of traditional audit coverage and strategic objective reviews integrated with "new" coverage areas.
- The CAE obtain periodic 360-degree feedback reports from his/her direct reports and from management and submit a comprehensive report to the audit committee.

Lastly, the audit committee should expect the leader of a mature audit activity to be engaged in executive management meetings in which strategy and operations are discussed by raising relevant questions and providing appropriate insights. In other words, internal audit should have a seat at the table.

The audit committee should embrace the concept that its role is critical to the overall success of the organization's governance model. It must hold the CAE to account and expect the same performance of the CAE as it would from the CEO.

What Internal Audit Should Expect From the Audit Committee

The best relationships are partnerships, and the CAE must be equally open and clear with the audit committee about ways to enhance or improve its support of internal audit activities.

Internal audit activities should be clear in what they need and expect from the audit committee in terms of support and direction. This is especially crucial regarding concerns over management retaliatory overtures and the CAE's efforts to gain a seat at the management table. The CAE and internal audit should demand audit committees stand with them, rather than behind them.

The Basics: A CAE should expect to have the audit committee's time and attentiveness, just as it would from any superior guiding and leading staff development and success. What often works against such interaction is that audit committee members typically have limited time due to their other commitments. Despite such time restraints, supervisory oversight should not be limited to time allocated during audit committee meetings four to six times a year. Consistent and open dialogue is imperative.

The CAE should reach out quarterly for a minimum 30-minute phone call with the audit committee chair to discuss relevant items such as staff turnover, upcoming complex audits requiring cosourcing support, new or upcoming regulations affecting the profession, feedback from the chair on what they hear from management or within the committee, and emerging activities in the company that may impact the audit plan.

Time demands on the audit committee also can create the temptation to turn over to management its responsibilities for CAE review, remunerations, firing, and hiring. This practice in effect abandons much of the audit committee's oversight of the CAE and could jeopardize the integrity, independence, objectivity, and effectiveness of the CAE role.

Enhanced Audit Committee Support: Encourage the audit committee to commit to meeting on a regular basis — e.g., annually — with the CAE and internal audit's senior leaders to discuss:

- Audit strategy and methodology.
- Demonstrations of how internal audit performs data analytics.
- Risks affecting organizational success.
- Engagement in investigations of ethics and compliance matters.
- Feedback from the audit committee on their views of risk.
- Scope limitations and challenges faced with senior management.

Most importantly, take the time to further forge the strong relationship that must exist.

FIVE QUESTIONS

Building the right relationship between the audit committee and internal audit can make a significant difference in internal audit's ability to provide the best assurance and advisory services.

Here are five key questions the governing body should be asking:

1. *Does the CAE have unfettered access to the audit committee?*
2. *Does the CAE seek opportunities to strengthen his/her relationship with the audit committee?*
3. *Does internal audit have the ability to meet with the audit committee outside the presence of executive management?*
4. *Is the CAE being held to account to deliver the highest level of internal audit services that comply with IIA Standards and promote certification of staff?*
5. *What obstacles are keeping the CAE from earning a seat at the management table?*

The CAE, using video conferencing or other technology, may invite audit committee members to be available for questions during internal audit training or communication days. Visible engagement sets an immensely different tone within internal audit when the audit committee is approachable and available to the entire staff.

The audit committee also should demonstrate support for the internal audit staff. While there always will be a natural contention between internal audit and executive management, the audit committee should convey clearly that internal audit's role is critical to good governance. No member of the audit team should ever be penalized (in their career or otherwise) for asking the tough questions or approaching a sensitive topic in an audit.

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Conclusion

The relationship between the audit committee and internal audit is critical to good governance. An open relationship that pushes to improve communication and performance helps build an effective and efficient internal audit activity that is best positioned to help the organization reach its goals. But it requires the commitment of both parties to build that relationship into a trusting and dynamic partnership.

About Position Papers

The IIA promulgates Position Papers on key issues of interest to stakeholders and practitioners with the aim of advocating for sound governance and educating those involved in it. The positions outlined offer insights into various aspects of the governance process and internal audit's vital role in improving governance at all levels and adding value to the organization. Position Papers are developed and reviewed through a rigorous process that solicits input and critique from practicing internal audit professionals and other IIA volunteers who serve on The IIA's Global Advocacy Committee, IIA Standards Board, and The IIA's Professional Responsibility and Ethics Committee.

About The IIA

The IIA is the internal audit profession's most widely recognized advocate, educator, and provider of standards, guidance, and certifications. Established in 1941, The IIA today serves more than 190,000 members from more than 170 countries and territories. The IIA's global headquarters are in Lake Mary, Fla. For more information, visit www.globaliia.org.

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