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Negotiating the role of internal audit: How directors situate audit in the governance process

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Context

Financial scandals like Enron and WorldCom have led to major changes in governance rules and practices. The role of directors was enlarged, and the responsibility for ensuring that solid governance rules are put in place now rests squarely on their shoulders.

To assume their role, directors must be able to rely on accurate, pertinent and timely information. In this context, internal audit can be a precious tool for directors in general and for audit committee members in particular.

Surveys conducted with internal auditors[1] and with the main users of the internal audit function[2] have shown that the role and expectations of internal audit have evolved significantly in recent years. Anderson (2009:21) summarizes the changes in an OECD report:

> *Over the last two decades, internal audit has undergone a transformation in its role, remit and attitudes. In many organisations internal audit has moved from being an extension of financial control, focussing on financial accounts and the operation of routine internal financial controls to becoming a function which perceives it has a role in assurance and internal consultancy, in relation to all risks, but especially those that have an impact at a strategic level, and which has a reporting line directly to the chair of the Audit Committee.*

Current knowledge is insufficient to let us pinpoint these new roles. After having surveyed over 300 chief audit executives in the United States, Grant Thornton (2011:2) had to acknowledge that:

> *Internal audit is evolving along the value creation dimension. Because of the changes in the profession, no single definition can capture the*

[1] See, for example, the results of six studies entitled Common Body of Knowledge (CBOK), published by the IIA Research Foundation between 1972 and 2011, or the State of Internal Audit Profession Studies conducted annually by the firm PricewaterhouseCoopers between 2005 and 2012. These documents are cited and commented on in Appendix 2 of this report.

[2] Examples include Korn/Ferry International, 2010; Moody's Investors Service, 2006; and the IIA Research Foundation, 2011a, cited in Appendix 2.

> *essence of what internal audit is. Internal audit is a little different for each organization and should be customized accordingly.*

It therefore seems that the role of internal audit is shaped by the needs of each business. The objective of my dissertation is to better understand how this role is constructed through interactions between the chief audit executive (CAE), senior officers and audit committee members. To this end, I met with several representatives of these groups to discuss the ways they define and negotiate, as needed, the role of internal audit within their respective organizations.

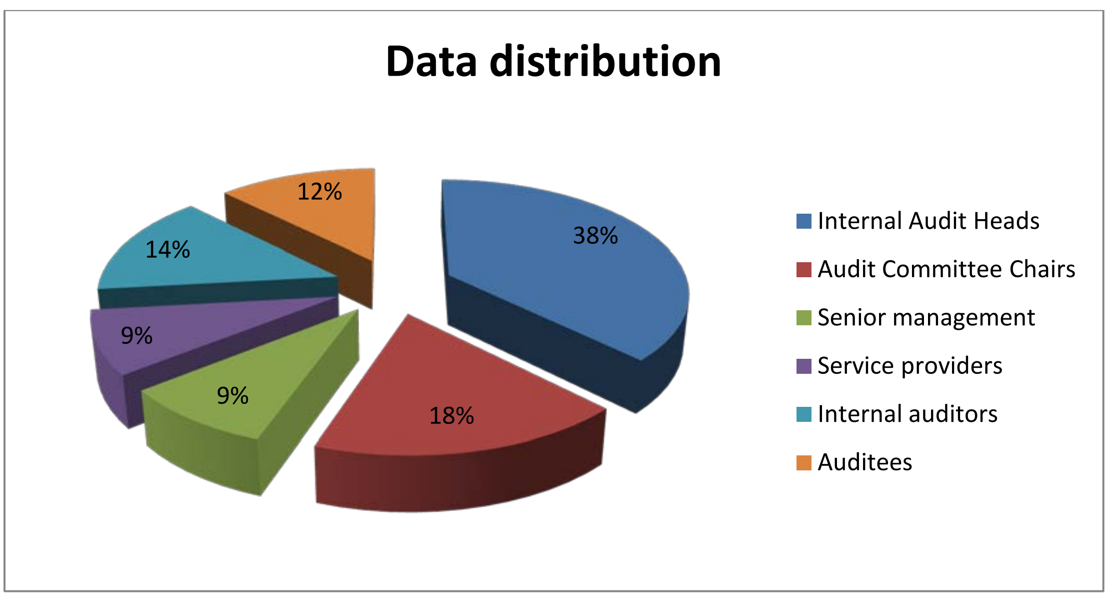
Based on these dialogues, in which experienced executives generously offered their thoughts about internal audit and shared the problems they encountered and solutions put forth, I wanted to write a synthesis of information that could be useful for directors. The goal was to give something back to the participants who had given me so much. This report is therefore not part of my dissertation. It is an opportunity I have taken to share with directors some thoughts on their links to the internal audit function and some ideas on ways to use this valuable tool. I can do so because of the richness of the data gathered for my thesis. Given the scarcity of guidelines in legislative frameworks and the scientific or trade literature to allow directors to plan and assess the development of the internal audit function within their organizations, I hope that this work will partly fill this gap.

The remainder of the report is organized as follows. The first section presents the methodology surrounding the data collection, along with pertinent information on the participants. In Section 2, I briefly outline my theoretical framework to clarify the structure of the analysis of the interview transcriptions. Sections 3 and 4 present the main findings of the data analysis, and the report concludes by summarizing the impact of directors on development and the use of internal audit. Appendix 1 contains the summary of this paper, prepared for the audit committee chairs who agreed to participate in the research, and Appendix 2 summarizes recent trade publications that may be of interest to directors.

Section 1: Methodology

My dissertation project aims to study how the new role of internal audit is being constructed, through all the interactions that surround the function within organizations, while taking into account the global context in which this role is evolving. Because the objectives of this research are to identify the context in which the role of internal auditors is negotiated, I deliberately met with some very experienced individuals who know and understand the changes that occurred in the global environment, rather than attempt to cover a vast sample.

Through the invaluable assistance from the Institute of Corporate Directors, the Collège des administrateurs de sociétés and the IIA, I gained access to audit committee chairs and chief audit executives recognized as leaders within the North American business community. Thanks to personal contacts and the snowball effect—participants who agreed to ask their boss or colleagues to participate in the project—I interviewed 56 people, distributed as follows:



Positions	Number	percentage
Internal Audit Heads	21	37,5%
Audit Committee Chairs	10	17,9%
Senior management	5	8,9%
Service providers	5	8,9%
Internal auditors	8	14,3%
Auditees	7	12,5%

The participants originated from Québec (66%), the other Canadian provinces (25%) and the United States (9%). Apart from the involvement of internal audit in the requirements of the American law SOX, no significant differences were noted. The data from the United States thus provided insight into the use of internal audit.

The directors encountered have chaired at least one audit committee. However, most have chaired several committees, in different sectors. Consequently, they could comment on the differences noted between the use of internal audit in a highly regulated and supervised context such as the financial sector, and its use in freer sectors in the North American economy.

Concerning chief audit executives (CAE), 21 agreed to participate in the research. Of this number, 6 work in the financial sector, 13 in other sectors and 2 worked in both the financial sector and other sectors. The other sectors are distributed as follows:

Other sectors	Number	Québec	Other provinces	USA
Manufacturing	4	2		1
Distribution/Retails	3	1	2	
Social	1		1	
Service Providers	3		2	1
Education	2	1	1	
Total:	**13**	**4**	**6**	**2**

The consultants’ profile is broken down as follows:

Service providers	Number
Internal audit service providers	2
Director's Education provider	1
IIA Audit Quality Evaluator	1
IIA Global representative	1

Interviews lasted between 60 and 120 minutes, and most were recorded and fully transcribed. In the case where it was not possible to record the conversation, detailed notes were taken immediately after the interview, while the discourse was still fresh in my mind. Several CAEs agreed to provide documents on their department, such as charters, examples of audit reports, annual plans or criteria used to assess the performance of their department. These documents were included in the data analysis.

Section 2: Reference framework

To facilitate the data analysis, it is important to choose a theoretical perspective that directs researchers’ attention to certain aspects and allows them to sort through the information gathered. I chose the analytical framework of negotiated order, introduced by American sociologist Anselm Strauss in his book ***Negotiations: Varieties, contexts, processes and social order*** (1988).

Strauss belongs to the school of Chicago stream. He studied the organization of work at American hospitals, particularly in psychiatry, during a vast rethinking of care offered to inpatients. His analyses are pertinent for internal audit, which has also undergone major transformations in the last few decades.

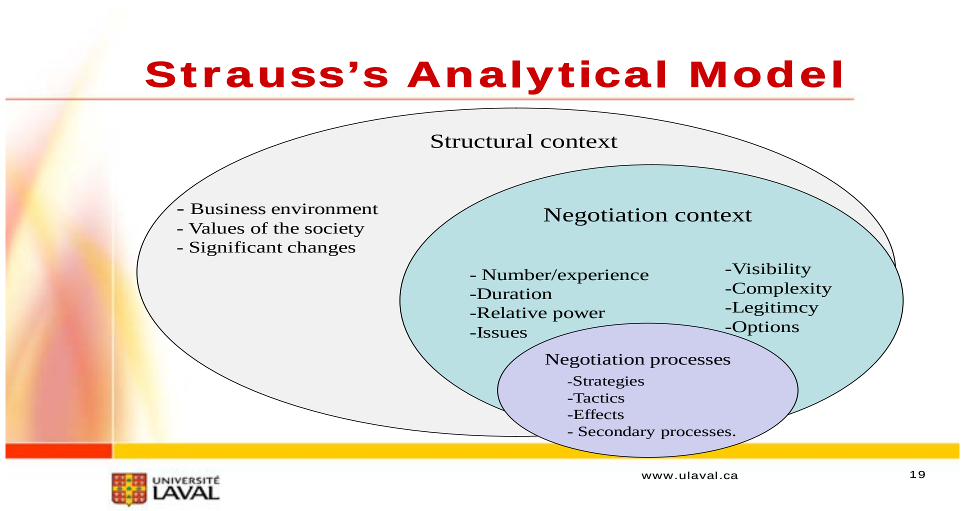
Strauss considers the social order a negotiated order. In other words, to ensure that work gets done, various people involved negotiate an agreement around rules established, and take the general context into account. One of the key elements of the negotiated order perspective is *the importance placed on the context* in which the exchanges take place. Strauss thinks it is crucial to grasp the global context of the organization, both internal and external.

He therefore proposes a framework of analysis to identify and understand all negotiated order (whether it concern the work of medical teams in psychiatric institutions, as in his own research, or determination of the role of internal audit within contemporary organizations, which is the goal of my research). This analytical framework comprises two major axes:

First, the researcher must try to understand the global context in which negotiations around daily work occur. Strauss argues that this step is too often neglected. He insists on the need to analyze the structural context, which influences negotiations. He distinguished the structural context from the more specific negotiation context.

In addition, the researcher must capture the daily negotiation process and describe it as precisely as possible. The description should include interactions associated with negotiations, the types of actors involved, their strategies and tactics, and the consequences (foreseen or not) of negotiations. If applicable, the researcher should also provide explanations about the use (or not) of secondary negotiation processes such as barter or obtaining advantages in exchange for information.

The analytical model proposed by Strauss can be depicted as follows,



To better understand the impact of directors in determining the role of internal audit, it is useful to concentrate on the first two circles, namely the structural context and the negotiation context. The last subset, which concerns negotiation strategies, pertains more to internal auditors. If directors take too much of an interest in it, they may be criticized for engaging in micromanagement.

In the remainder of the report, I focus on the structural context and the negotiation context. The ***structural context***, discussed in Section 3, offers two main lines of analysis:

- 1) changes in the business environment with the coming into force of new laws on business governance, the diffusion of best practices, and higher education of directors;

- 2) actions the Institut of Internal Auditors (IIA) has taken to promote and regulate the internal audit profession.

These two main lines will shed light on facts that have driven changes in expectations of internal audit that continue to influence the negotiation of its role.

In contrast, the ***negotiation context*** refers specifically to organizations. This more restrictive context will be discussed in Section 4. Several factors can influence the way the role of internal audit develops, such as the organizational culture, social positioning placed on the internal audit function, the relationship of trust between audit and top management, and interactions between internal audit and other oversight and control functions. Directors have a role to play in each of these aspects, and can have a positive influence on the integration and hence the efficiency of the internal audit function.

Section 3: Structural context

Significant changes in the environment

Several participants described major changes in the business environment, which have impacted the development of internal audit. They include financial scandals that received intensive media coverage, new laws on corporate governance, pressure by monitoring organizations and training developed to help directors control their environment and companies more effectively.

Financial scandals that rocked the business world in the early 2000s focused public attention on the pressing need to rethink corporate governance. Massive media coverage of these events brought about significant changes in public expectations and forced regulatory authorities to intervene by adopting new standards. One of the participants offered these opinions on this subject:

> *Major scandals like ENRON or WorldCom and all that, well, these huge scandals undoubtedly changed the way organizations are managed, just like the events of September 11 transformed the aviation world. The authorities felt challenged and changed the rules...Companies, their executives, their boards of directors are more aware of risks. In fact, these events forced directors to be more aware of the importance of their role and responsibilities.*
> *Service provider, SP-5*

In response, several stakeholders demanded that boards of directors and officers apply recognized governance principles, ensure that the organization manage its risks appropriately and publicly demonstrate that they control operations and finances. Important reflection took place on various aspects of governance, leading to the writing of reports arguing for legislative reforms. The mandate and makeup of boards of directors was re-thought, and their responsibilities were often enshrined in more stringent regulations (for example, the Sarbanes-Oxley Act in the United States, and regulation 52-110[3] in Canada have reinforced the obligations of boards of directors and audit committees). Many of these regulations require that audit committees be formed to ensure adequate internal control, particularly regarding reporting of financial information. In both Canada and the United States, regulation now obliges executives to certify the quality of some of their internal control systems.

[3] Amid the cascade of financial scandals, several regulations were adopted under the Securities Act, to frame expectations of issuers. In this report, I refer specifically to Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings, and to Regulation 52-110 on the Audit Committee. For a more detailed presentation of issuers' permanent requirements, see the Autorité des marchés financiers website: http://www.lautorite.qc.ca/en/ongoing-requirements-issuers-insiders-autre.html.

In November 2003, the SEC approved new rules for the New York Stock Exchange, including the obligation to create and maintain an internal audit department. Listed companies had until October 31, 2004 to comply with this new requirement. However, no prescriptions concerning resources or functioning were added. The Institute of Internal Auditors (IIA) tried unsuccessfully to obtain this imposition during the tabling of Regulation 52-109 requiring Canadian public enterprises to tighten their internal controls. The commission in charge of analyzing comments on the draft regulation replied to the IIA as follows:

> *We think that management should be allowed to determine its staffing needs, in that they depend on the establishment, maintenance and evaluation of controls and procedures for reporting information, and internal controls.*
> *Notice of publication – Draft Regulation 52-109. January 2004, p 9.*

The question resurfaced in 2013, when the NASDAQ weighed the possibility of requiring all listed companies to have an internal audit function. Given the many protests the proposal raised, the organization withdrew the project on June 6, 2013. The main opponents argued that the cost of this function could be too onerous for small issuers, and that SOX already required independent certification of internal controls, which would make the mandatory creation of an internal audit function partly redundant.

Despite opposition to making internal audit mandatory, the usefulness of this function was increasingly felt in sectors that were highly regulated or that were characterized by complex business operations.

Several participants mentioned the necessary involvement of internal audit given new regulatory standards in both Canada and the United States. The following comments by audit committee chairs exemplify these views:

> *We were lucky to have a management team that wanted to play fair and that needed... and that clearly understands the role of internal audit and that understands even better, I think, like any other company since 52-109. You know, when like a CEO, like a CFO you have to sign in blood at the bottom of the page... You understand what*

internal controls are. And then it's easier than it was 15 years ago maybe, or even 10 years ago... So that, they understand. They understand there's a role to play, but they want to go beyond it too. That's fine.
Audit Committee Chair, AC-3

But I think the [internal audit] mandate will be to look at more and more the key and critical risks because of the fact that the CEO and the CFO are personally liable for the controls, to make sure that the controls are certified. Because of that certification, they will continue to be around...
Audit Committee Chair, AC-5

Well, even in Canada we have 52-109 and somebody's got to do that work. Even though the finance area and the operating people need to own those controls, somebody needs to check them. You can't have the monkeys running the zoo. You've got to have somebody who's independent looking at those things and pronouncing on whether they're good, bad or indifferent.
Audit Committee Chair, AC-7

Beyond the legislation aimed at public enterprises, i.e. that they require an internal audit function to be put in place or that make its presence practically indispensable, it is very evident from participants' comments that the sector and its particular framing will also have a great impact on the decision to put in place an internal audit function, and on the mandates given to this function. The more regulated the sector, the more the company will operate in several jurisdictions, and the more the internal audit function will be considered a major asset by executives and audit committee members alike.

And I think the role of internal audit is increasing rather than reducing, particularly when you get to a number of issues around regulatory and legal compliance...If you've got a company nowadays that operates in multiple jurisdictions... like in multiple countries. Or a company that is regulated, which more and more companies are being more heavily regulated by the government. There is a

significant role for internal audit to play, particularly if there is not a compliance group - and a compliance group may be part of internal audit or not – to ensure that they are proactively dealing with the world of regulation and some of the issues right now, if you look at SNC-Lavalin, some of the corrupt practices issues... So internal audit plays a very broad role in that.
Audit Committee Chair, AC-5

In some sectors, monitoring organizations have also realized the importance of internal audit, and some not only insist that the companies that they supervise have an internal audit function, but also seem to want to meddle in the role of that function. This situation was raised by several CAEs, who work mostly, but not exclusively, in the financial sector.

Because of all these things, the role of internal audit will also become more and more important. The regulatory authorities - especially in a sector as regulated as financial services - are beginning to recognize the importance of having a good internal audit function. The oversight authorities are also relying on the internal audit function. There is huge pressure on internal audit to do more and more auditing and to meet the expectations of more and more groups.
Chief Audit Executive, CAE-16

As an internal auditor we have a clientele. Who's the clientele? There are three clients. The first client is company management. The second client is the Board of Directors, through its audit committee, if you will, but it's the board. And the third client is the supervisory authorities. (...) Before, I had more of an influence on my annual plan. Now there is a requirement, from the supervisory authorities, that the plan be structured based on risk analysis that covers the universe of risks including weak risks, and that's so important that we also go audit places where risks are low, that if I listen to them, I would need to double my staff. I was saying before, one of my clients is the supervisory authorities. (...) This will add considerably to the burden of the internal audit department, in a company as regulated as a

financial institution, it’s that to protect themselves, the supervisory organizations require, in a lot of places, that things be audited by internal audit. Because it is them who are seen as independent, internally, and people responsible for going to see if the controls are done properly. So based on these two requirements, these two characteristics of the internal audit service, in a bunch of places, they're asking internal audit to show up and issue an opinion on something. This increases the work considerably.
Chief Audit Executive, CAE-21

It’s because compliance has become more complicated; there’s just more of it out there, and there’s more emphasis. Anti-corruption, you know, four or five years ago, we probably spent minimal time on that, nobody really dealt with it, and the law was always out there. Now we specifically test our policies, our guidelines, our payments and so on. What’s happened is the Department of Justice is enforcing more now on the actions around companies, with very, very heavy penalties and fines. (...) Nobody wants to be part of the headline, nor do they want to be part of a monitoring program by the Department of Justice if they are found to have made a bribe to a foreign official.
Chief Audit Executive, CAE-10

The last comment underlines the influence of the media in putting in place certain corporate governance practices. Top managers and directors alike are very intent on managing their organization's image. To this end, internal audit can be a valuable tool at several levels. First, in terms of content, internal audit can help executives and directors confirm that sectors or activities that the public view as critical are properly managed and that operations are controlled. Internal audit can also serve as a justification, its presence alone demonstrating that executives and directors take their responsibilities seriously.

Rating agencies and financial analysts may also influence the value of a company and public opinion of its reliability and outlook. Some participants mentioned the importance that rating agencies or financial analysts place on sound governance in their assessment of a firm. The fact of having a recognized and active internal audit team portrays the business in a better light. Moody's Investors services, for example, has even issued a guide to help audit committee members supervise their internal audit function more effectively.

Accounting firms have also been excellent ambassadors for development of internal audit. Already very present in the IIA, which they have supported and financed for several years, they have produced numerous studies of the profession, guides for directors to help them develop and supervise an internal function.[4] The impact of these studies and guides has been felt within boards of directors, as two participants explain:

> *It was the big accounting firms at the time, the Big 5 or Big 6, now Big 4, who had strongly advocated for internal audit, particularly because it's always been part of the external audit work plan to understand the control environment of their clients. In fact, external auditors have two options: they can rely on controls to reduce their work in coming to an audit opinion. Or they can basically not rely on the controls and do what is called a substantive audit or manual work audit. Lots more work. Irrespective of which approach they use, they are required to determine what the controls are, and the control environment. They always have that; that has always been a requirement of the external auditors.*
> *Back in the 80s and 90s, they wanted internal audit to be created in companies. It started with government but it slowly made its way into the private sector as well. Effectively, internal audit was the first way to make external audit fees lower.*
> *Audit Committee Chair, AC-4*

> *Accounting firms are heavily involved in development of internal audit. For one, a solid team of internal auditors can have an impact on internal control. It is often internal auditors who bring rigour and monitoring; they're responsible for the quality of audit trails. And they have the advantage, compared with external audit, of always being on the inside, of being close to business operations. If they can rely on a*

[4] For more details on this subject see Appendix 2, State of Internal Audit in Canada, which lists some of these guides and studies of the internal audit profession.

> *certain number of works by internal audit, it's a plus for them. There is also the global consultation aspect. Accounting firms have been very present with directors, either to advise them or to provide internal audit services or again to come audit internal audit every X years.*
> *Audit Committee Chair, AC-8*

Attention placed on sound governance by regulatory bodies, the media and the public, coupled with higher expectations of directors, has accentuated the need to rethink the profile and training of directors. The requirement of having within an audit committee at least one person considered a financial expert has led to an increase of accountants within this committee. Accountants are familiar with internal audit, which may partly explain audit committees' awareness of the value of this function. An experienced CAE clearly described this situation:

> *I think Sarbanes helped that. I think audit committee chairs are more aware of their responsibilities – I don't think their responsibilities necessarily changed. I think they're also more aware that they live in a much more complex and risky world. Therefore they need to make sure that they have good strong internal audit, of course, the entire world doesn't revolve around internal audit, but they need to make sure they have a good external auditor, a good internal auditor, and they need to make sure they have whatever else they need, and they've got to support them, and they've got to listen to them. So, I think if you think about the US in the post-Sarbanes world, I think it has elevated the focus of audit committees, and if you look at the US, you see a lot of changes of the audit committee chair, you see them upgrade the members of the audit committee.*
> *Chief Audit Executive, CAE-8.*

The early 2000s also saw the upsurge in training to help directors acquire knowledge and skills instrumental to the success of their work. This training apparently allows boards of directors and audit committees to better understand and play their role. In this training, internal audit is covered briefly. Several participants referred to this training, mentioning the importance of director development.

In short, several changes in society have influenced the development and role of internal audit. Public attention placed on sound governance following numerous financial scandals has prompted tighter regulation. New regulations such as SOX in the United States and Regulation 52-109 in Canada have heightened the need for an audit function. Internal audit has benefited from the deployment of new requirements to increase its visibility and in some cases to carve out an important place within organizations. However, the role of internal audit in highly regulated contexts may be limited to a compliance audit function, ignoring the wide range of value that this function could offer operations.

Expectations of directors are escalating, and their responsibilities are better understood. The growing complexity of organizations and of their competitive and regulatory universe is driving directors to seek tools to better gauge the status of their firm. Internal audit is clearly among the potential tools that could increase directors' comfort. Better trained, and more competent directors are increasingly familiar with the internal audit function, and many realize that this function can help them manage important risks related to their role.

Changes in the environment partly explain the development of audit. Another important factor is the IIA's efforts to alter the perception of this function, while seeking to adapt its role to current needs.

History and actions of the IIA

Internal audit, in its current form, is relatively recent and results from the financial crisis of 1929. At that time, the role of internal audit was limited to work done by employees of an organization to prepare for financial audits by external firms. The goal was thus to limit the cost of these audits. New recognition of internal audit in the 1930s was mainly linked to the creation of the *Securities and Exchange Commission* and the development of knowledge and new internal audit techniques. Originally, internal audit was created and developed to assist the external audit process. The early internal auditors were largely technicians who were assigned routine tasks of looking for clerical errors in financial statements on an ongoing basis.

Founded in 1941, the *Institute of Internal Auditors* (IIA) is a professional group that now has over 180,000 members distributed in 190 countries and territories. It was created by internal auditors to publicize the profession and improve its image. It has put in place a series of steps to position internal audit:

- the formulation of Standards to frame the work of internal auditors– the first *Statement of Responsibilities of the Internal Auditor* appeared in 1947, and after several revisions was replaced by the *Standards for the Professional Practice of Internal Auditing*, first published in 1978 and revised in 1981, 1999, 2008 and 2013;

-introduction of a code of ethics (1968);

- deployment of a training program leading to the title of CIA (1970); creation of the *IIA Research Foundation* in 1976;

- creation of trade publications such as *Internal Auditor,* launched in 1977;

- and vast international studies of the profession, including CBOK, a series produced between 1972 and 2010.

In the early 2000s, a vast questioning of the governance principles of public companies occurred in the United States. The IIA insisted on the role internal audit could play in the process of managing and reporting financial information. With the coming into effect of the Sarbanes-Oxley Act (SOX), and its Canadian equivalent (Regulation 52-109), the Institute positioned its members as the most qualified consultants to help top management and boards of directors meet the new (and costly) requirements of the legislation. It tried, with mitigated results, to have the mandatory creation of an internal audit department enshrined in the new regulations adopted in the wake of the financial scandals.

If it is true that the new legislation and positioning of internal audit as a control specialist benefited internal auditors in terms of job security or wage increases, this change in orientation of their work toward marked concentration on compliance has not had uniquely positive results.

The IIA was concerned that if internal audit spent too much time and energy on regulatory compliance, it could no longer fully assume its role of planning and carrying out a series of audits based on risk. The Institute argues that an internal audit program that did not take an organization's strategic and operational risk into account is an incomplete program that decreases the efficiency of internal audit and its value for companies. In addition, overinvolvement of internal audit in compliance tests limits the need for auditors to refer to their professional judgment, which can ultimately reduce the overall value and professionalism of internal auditors, and even undermine their expertise and skills.

In the second half of the 2000s, the IIA's discourse changed considerably. Abandoning the position of compliance expert, the Institute began trumpeting the added value of the function resulting from better control of the organization's major risks. It raised the topic of advancing the role of internal audit to involve it in assessing strategic risk management at companies and in the revision of the governance processes. The IIA thus developed a communication strategy around this added value and changed its Standards to take this new orientation into account. Were its efforts felt in the field? In other words, to what extent were its discourse and efforts reflected in the work of internal auditors?

In general, audit committee chairs interviewed seem to feel reassured when their internal audit function follows the IIA's Standards

> *I make sure that my CAE and the whole team follow the IIA Standards. I insist that they participate in the life of internal audit on the global scale, to make sure that we apply, here, global quality standards, that we are at the top of the profession.*
> *Audit Committee Chair, AC-2*

> *And we also have an external assessment done by an external firm. That is done every...three years, I think. I'm not that sure about that... I think it's three years... you'd have to ask our CAE. But there was one*

> *last year. So there was an external firm that came and did the department Assessment. They tell us if our team complies with all the IIA rules, if it all follows international standards. They evidently do comparisons, with other companies of similar size, to tell us where we are situated relative to the best practices they see. Where we can seek this comfort...Evidently, because of my experience, I saw many internal auditors, so it also lets me compare...*
> *Audit Committee Chair, AC-3*

> *One of the things you want to make sure is in place, is that your internal audit group is professionally trained, and that what they are doing is in compliance with the standards set by the Institute of Internal Auditors. They provide some level of standard setting and... So the role of the audit committee is quite significant, in my view, with respect to internal audit, because there is that reporting relationship.*
> *Audit Committee Chair, AC-5*

In fact, the audit committee chairs whom I interviewed are very experienced, and sit on boards of large public companies. Many CAEs expressed doubts about the knowledge of IIA Standards held by most audit committee members. The need for additional training in this area seems acute.

CAEs have mixed opinions of the IIA Standards. If all recognize their usefulness and the need to regulate internal audit practice, several consider the standards too detailed to the point that they can stunt the development of the profession:

> The standards are very good. They have, over the last three years become too bureaucratic and they tend to be missing the wood for the trees.
> Chief Audit Executive, CAE-7

> It would certainly give the profession more flexibility. There, people interpret it... listen, there are 132 “musts” - or something like that – in the standards. It's something “must,” “have to” do. Listen, it's not... That's not what a profession is, as far as I'm concerned. That's not a profession, to say you must do 132 things to say you are doing your

> profession properly. Listen, soon they may start telling me how to turn the doorknob. You understand what I'm saying? Where does it stop, these things, to do a good job in internal audit? (...) It's not the method that makes a profession.
> Chief Audit Executive, CAE-11

Some participants emphasize that it can be difficult or even impossible for small internal audit teams to meet all the requirements contained in the Standards:

> *And a professional judgment, it is not limited to a series of standards. I will give you an example. At the conference I was on a panel: challenges, disadvantages and advantages of small audit teams. You can't meet all the requirements. The moderator asked me: how do you feel about that? Do you feel that you can't do your work? I said no. Me, I do my work as best I can, but I know that I am meeting the most important criteria. I'm independent, I'm objective, and I'm transparent, I have a relationship with the board, I have a relationship with the president, I have my charter. But do I have my quality insurance manual? No. Am I audited every five years? No. There are many like that. However, because I know that in the room, there are several who like paragraphs, and they know them - but me, what motivates and drives me is the 2000 [IIA Standards regarding Internal Audit Activities]. It's to give my client added value. That I will deliver at 100 miles an hour. The best sign that the work is appreciated is when you're always invited to the board of directors, that the time they give you always runs out, that your pay does not cause a problem, that you get a good annual assessment... Do you understand what I'm saying? There are many things that show you that people appreciate your work, which are worth more than saying that I met the 132 "must"s. I brought managers useful information that helped my client advance. So that's being professional. I'm quite eager for that day. Because there are many people who only live by the Standards and that's why, I think, there are people who are making internal audit pass for what it is... It's technicians who don't*

> *see the strategic role that they can play. The Standards, they're good, they're necessary, they're useful, it's a frame. But it's not a profession.*
> *Chief Audit Executive, CAE-11*

The interviews clearly show that the IIA Standards are important to frame the internal audit practice and to ensure the quality of audit reports. However, the audit committee plays a crucial role in determining the importance of internal audit's compliance with the practice standards. Audit committee members would therefore benefit from discussing this topic with their CAEs and adapting the application of the standards to the maturity and complexity of their organizations.

For example, the IIA requires that internal audit be certified by its quality review teams or by an external and independent accounting firm every five years. This quality review is intended to ensure compliance with IIA Standards. Slightly more than half of the CAEs interviewed said that their department was audited every five years (in most cases this mandate given to an accounting firm; only two companies were audited by the IIA itself). One CAE explained how his department did its own assessment, which was then validated by an external consultant. For others no external audit was done, either because the internal audit department is considered too young or too small to justify this exercise, or directors and officers had cut this audit because of cost issues.

In addition to the Standards, the IIA gives internal auditors many tools and models. Several participants mentioned that internal audit charters are fairly similar between companies because they are strongly inspired by the model proposed by the IIA, even if the role of each internal audit function varies significantly in practice. For example, almost all of the CAEs confirmed that their charter adopted the IIA's definition of internal audit, and specifically mentioned the need to provide assurance concerning internal control, evidently, but also risk management and corporate governance. Despite these comments, only two auditors claimed that they were involved in governance processes. Even in these case, their action was limited to compiling these processes. One participant with vast experience as a CAE for several large American companies mentioned:

> *I think there's a lot of confusion on the part of internal audit and their stakeholders about what internal audit could or should be doing relating to governance, and frankly that's why I was mentioning this one company where as general auditor, instead of doing an audit of governance, I went in and did a review and just tried to catalogue, here's what I think we're doing from a governance standpoint, here's some areas where you could maybe tweak it, and I kind of used that to get the audit committee and management comfortable with the idea that internal audit could be looking at something called governance, and help kind of ease into it.*
> *Chief Audit Executive, CAE-8*

The involvement of internal audit in risk management is not a fait accompli either. Several documents published by the IIA were cited by CAEs[5] to defend their role in risk management. One of the participants, involved with IIA Global, admits that few internal audit departments managed to perform assurance audits at the centre of risk management of their organization, and adds that:

> *(...) It's true that auditors will not always be able to audit processes deployed by the risk management team. Directors and officers are not always convinced that this is really the role of internal audit. As for me, I think that the biggest problem is that internal auditors themselves do not feel capable of doing these audits. It's out of their comfort zone. It's far from their "traditional work," and because they are not convinced, they can't convince management. We have a lot of work to do in this area.*
> *Service Provider, SP-4*

[5] Two documents in particular were cited by several participants: 1) *Internal Auditing's Role in Risk Management*, a White Paper published by the IIA Research Foundation in March 2011, which discusses activities that internal audit must perform to ensure sound risk management, activities it may undertake prudently, and the roles internal audit should absolutely not play in terms of risk management; 2) *The Three Lines of Defense in Effective Risk Management and Control*, a Position Paper published by the IIA in January 2013, which positions internal audit as the third line of defense in risk management, in charge of auditing the first and second lines of defense (namely 1) operational management, who control risk, and 2) centralized functions like risk management and compliance).

The IIA has made a formidable effort to advance and defend the role of internal audit both with legislators and in the business world. Nonetheless, even if formally the IIA discourse seems to be embraced by businesses, in the field internal auditors often lack the skills, experience and credibility necessary to take the full place they seek, particularly in risk management and governance.

Section 4: Negotiation context

Internal audit is part of the current vision of governance. Its significant development in recent decades is explained by many environmental factors including the IIA’s sustained efforts. We will now look at how the role of internal audit is determined, and the factors that can allow the function to be effective and useful. Specifically, we examine what occurs at the heart of organizations.

The participants all recognize that links between internal audit and the audit committee are important. Generally, CAEs attend meetings of the audit committee, have closed-door talks with members, and maintain fairly frequent contact with the audit committee chair. The audit committee receives and approves internal audit’s annual plan, assesses whether sufficient resources have been allotted to the internal audit function, receive reports and monitors the implementation of recommendations. The form of prescriptions recognized as sound governance practices is respected. However, it seems that greater involvement by the audit committees could help the recognition and efficiency of the internal audit function.

Many participants insisted on the fact that the role and use of internal audit varies considerably depending on the company’s sector, organizational culture, stage of development and maturity, officers’ philosophy, etc. Below I present points identified in discussions as key success factors for the creation of a positive negotiation context around the internal audit function. To help internal audit be more effective, the participants underlined the importance of respecting the organizational culture, even subtly advancing it if necessary, to allow acceptance of the audit internal function by top management and by operations. Companies operating in less regulated sectors are particularly sensitive to this question. In addition, directors can help reposition internal audit to ensure the credibility of the CAE and auditors, and thus favour the development and maintenance of a relationship of trust between managers and auditors. Directors also have an essential role to play in clarifying expectations of internal audit and of the other assurance functions such as compliance or risk management. Ensuring good risk coverage while avoiding duplication and redundancy not only protects the organization more strongly, but it also favours the development of synergy between these sectors, limiting turf wars and silos.

Adapting internal audit to the organizational culture

Many participants mentioned the importance of adapting the role of internal audit to the organizational culture. The role of internal audit, ways to address colleagues, and the content of reports differ greatly if the company is operating in a highly regulated and monitored sector like the financial sector, or if it operates in a freer context like manufacturing, distribution and retail sales, or services. In regulated sectors, the annual audit is largely determined by the context and is oriented toward compliance. In contrast, companies that operate in a more flexible environment and that are directed by managers with an entrepreneurial spirit must modify the internal audit approach and take into account the added value for operations and for management that internal audit can provide. One CAE described the importance of adapting to the organization as follows:

> *And I would say that it's the strength of a CAE to adapt to the economic reality, I would also say social, because it's human, very human... to all these dimensions of the company. Unfortunately, many internal auditors come from the same mould, they are former external auditors who come with a one-size-fits-all recipe. It's a work method and then when they come, well that's it. Either they break because they notice that they can't change the dynamics in which they operate. Or they will try to force their ideas internally, in an ecosystem that is completely unrelated to their approaches.*
> *Chief Audit Executive, CAE-11*

For internal audit to be accepted and fulfill its role in an entrepreneurial context, it is crucial to understand the expectations not only of the audit committee but also of top management. Added value and understanding the business is vital, as one CAE who served in the financial sector and in retail sales points out, along with an audit committee chair:

> *Q. And do you think that it influences the acceptance of the audit team within the senior management position when it's more or less regulated? Do you think it's harder or easier to have your work accepted?*
>
> *R. Well I don't think it's harder, I think it's different… it can be a different person you're looking for, so when it's less regulated, when it's more operational, I think you need a chief auditor who understands the business and understands being on the side of business. So I've been an auditor, I've been in risk management a long time, but I've also been CFO of the business, so I've been on the other side of management, you know, not in audit. And so I understand the complexities of being on management and the challenges that they face, so that helps me on the operational side. So I can give them some help, some useful business recommendations. In regulatory roles at the bank, it's less a concern because most of our audits are regulatory, I don't really have a choice, I have to do these audits every two years, that's what's dictated by the regulators so it doesn't matter if I understand or not the operational benefits, it's got to be regulatory in focus. So I'd say you could have someone running the regulated environment a little less business-oriented, yeah, because they have to understand the business in a regulatory environment, that's obviously very important, and probably more so important, you know, you can't, it's tougher to learn on the fly with a regulatory environment because you really do need to understand the regulations. But whereas you can cross industries if you're more operational. And bring other experience, another view on the business... (...) So I'd say that the expectations might be a little different in the requirements of the person being more understanding of regulatory versus kind of just more of a business person when it's more operational.*

Chief Audit Executive, CAE-20

[company name] is an entrepreneurial business, very entrepreneurial. So internal audit has a role... A statutory role but also a role where value added is important. It must fulfill their role of the 52-109, for example, a normal statutory obligation but they are constantly brought to the reality of very concrete questions by saying: of course, you make recommendations for me, it's perfect, but bring me added value. Bring me what would be... when you do (...) you spend lots of time at your work, you see lots of people, you see many things, many situations, bring me the recommendations too. Which go beyond statutory recommendations. Operational recommendations, efficiency recommendations, etc.
Audit Committee Chair, AC-3

The notion of added value is very important and varies between companies. Many respondents emphasized areas where internal audit can provide added value. Here are some examples:

- help identify places where revision of the processes can create efficiency gains or operational savings;

- prevent costly risks for the company while tightening internal control;

- increase efficiency while providing a more global vision of operations, which exceeds the scope of a single department;

- favour identification and promotion of ingenious ideas to allow them to spread throughout the business (for example if a productive site situated anywhere in the world finds an innovation to solve a recurrent problem that is also seen in other work plans. Internal audit is well positioned to diffuse and apply this innovation elsewhere in the company);

- provide indicators of best practices, on what is done elsewhere and what can be imported and adapted within the company;

- retain competent employees during periods of economic slowdown. These employees, from operations, add depth to internal audits while acquiring new skills. They remain available to the company when operations regain their momentum;

- contribute to the training of future leaders, by having them spend time in internal audit, which reinforces their understanding of risk management and gives them an overview of the business.

Added value can also be found in the type of assignments conferred on internal audit. All participants have emphasized the importance of doing - or relying on - good risk analysis to develop the internal audit plan. The more audits target important risks for the company, the more the value will be felt. Leaving auditors to examine compliance with petty cash and its impact can only have a minor impact. Subtly expanding the mandates of internal audit can let the audit committee improve the perception of this function within their organizations:

> *I think the other thing they can do is encourage them to take on broader assignments. If they've got the control thing well in hand, then the next thing is to broaden their mandate a little bit and to work with them to... whether it is in risk management or operating efficiency areas and to help them take on assignments which will be viewed positively by the rest of the company.*
> *Audit Committee Chair, AC-7*

The potential influence of internal audit on major initiatives was raised by all categories of participants:

> *Let me use one very specific example, which is if the company is embarking on a number of major initiatives, there would be a key role for internal audit right at the beginning of these projects, to make sure that all the risks are being managed and mitigated throughout the process. And they are kind of the independent eyes and ears around a number of big initiatives... the post-mortem reviews of whether a project delivered what it should or not...*
> *Audit Committee Chair, AC-5*

In certain circumstances, internal audit can give me a lot... For example, when there is a major project, in which we invested a lot of time and money, and which is supposed to yield a lot of savings, facilitate our operations, make them more fluid and certain... Well, even if the project manager tells me that it's all going well and that we achieved the expected savings, I really want to send internal audit to confirm this. Sometimes the result is surprising... There are sometimes nuances... And you can improve the results according to the recommendations of internal audit. At any rate, it gives me an accurate snapshot of the implementation of the project and its real consequences.
Senior Management, SM-1

Honestly, me I've seen it, real value, important value, a few years ago, when we were a bit disorganized, controls were not completely in place. So, there they did audits and really, the recommendations they made clearly improved controls. Today, I'm seeing less of that. They still do it, they will still make recommendation, but whereas before if it was 80% you'd say Wow! Now it's closer to 20%. So it's continuous improvement, really, rather than climbing a step. On the other hand, where I've seen value is in projects, when it doesn't go well. So go ask them: we have a problem there, check it out. I find that has great value because then usually the people who work on a project, an initiative, they want it to work. And when it doesn't work, generally they know why. So when internal audit goes at it, they confide a lot in that department.
Senior Management, SM-4

"I have a project assurance and advisory services group. It's a small group, there's only three people, but they look at all the big strategic projects and make sure that, you know, they look at a number of things, they look at, you know, the governance around the project, how well they're being managed and the right stakeholders are involved in the project, how executives are getting right reporting on the status of the project, they also look at, you know, various aspects

> *of project and solution management. So they can look at, you know, are we doing the right testing to make sure the systems are going to be ready before they go into production. They can look at operational readiness to make sure that, you know, when the system is put into production, we've trained all the people that are going to use this system and all the call centres, so when it goes into production the business is ready for it.*
> *Chief Audit Executive, CAE-13*

Therefore, several activities can help internal audit adapt to the organizational culture and provide added value. Directors may play a crucial role in this process. They can also help change mentalities, and develop an environment conducive to internal audit within their organizations. For example, a number of directors maintain that some managers might have an overly entrepreneurial vision of their company and therefore might be reluctant to put fixed structures in place. In their view, developing an internal audit function and hiring several full-time employees to ensure the function's effectiveness may hinder flexibility. In these situations, one option can be to hire an external consulting firm to carry out internal audit. The investment can thus be reviewed more easily. This approach lets officers see the possible contribution of internal audit and envision putting an internal team in place when they are convinced that the added value exceeds the recurring costs. Directors and officers can also decide to introduce an intermediate phase of co-sourcing, in which employees can be trained internally and specialists are hired to perform more complex or specific audits.

Co-sourcing is also often used to limit internal auditors' need to travel. External consultants, often large accounting firms, have offices in several regions around the world, which helps them overcome language and cultural barriers because they hire and train local staff. A CAE at one retailer mentioned that he relegated store audits, routine work requiring extensive travel, to an external firm; the team could then concentrate on centralized functions.

Another option consists of having an internal audit function made up of a minimum of permanent employees and putting in place a rotation process to allow operations staff to spend a few years in internal audit or even to participate in specific assignments where their operational skills are required (“*guest auditor*” program). This formula favours flexibility, and has several other advantages. For one, internal auditors improve their understanding of operations, which helps them submit more pertinent recommendations to managers. Second, people who spend time in internal audit develop new knowledge, and acquire a more global vision of the company, particularly regarding its business risks. They are therefore better positioned to face new challenges. This approach also has the advantage of publicizing internal audit within operations. When they return to their various sectors after working in the function, employees can better understand the value of internal audit and can serve as ambassadors to their colleagues.

At any rate, directors invariably have a very important role to play to ensure that a common vision of the role of internal audit develops within their company. The less regulated the sector, the more expectations can vary between top management and the audit committee. It is therefore essential that the audit committee chair encourage open discussions with internal audit and top management, to improve understanding of expectations:

> *When the company is a financial institution, highly regulated, or in some industries where some of their activities are also highly regulated, it is much easier to reconcile expectations. All the parties are much more aware of the importance of control processes and want the same type of assurance that rules are followed, that we are complying with the laws that govern us. In a more open context, you have to adapt. We may face an environment... I wouldn't say hostile to internal audit... but where people need to see us as business partners, who are there to assist them and not to report their weaknesses. We have to understand what is worrying them, where they have problems in their operations and help them. We have to discuss a lot to understand their expectations in terms of support we can provide. But also to help them better see where our presence can be very useful to them. The less the role of internal audit is fixed or defined by regulations, the more important discussion of the role is. The more we*

> *have to work to make sure that everyone has the same understanding, the same vision... and be sure that internal audit provides what people - officers and directors alike - expect of us.*
> *Chief Audit Executive, CAE-15*

It is therefore important that internal audit adapt to the needs of the organization and respect the business culture if it is to be accepted and fully play its role. When it comes to understanding and furthering the organizational culture, when necessary, directors can be a valuable asset for internal audit. This is not the only area where their involvement is crucial.

Ensuring the credibility of the function

If directors want to ensure that internal audit adapts to the organizational culture, and understands and meets the firm's specific needs given its sector, internal auditors must have enough credibility to play their role. This credibility is acquired partly because internal auditors possess the necessary skills to do their work, but also because they know the company operations well and can therefore provide valuable assistance to executives.

Much is expected from internal auditors, as an audit committee chair explains:

> *To speak the truth to the power, to be able to disagree without being disagreeable, to be skeptical without being suspicious of every action, to have the common sense to know what is important and what is not important and to have enough self confidence in their own ability to stick to their guns if necessary. You know, when all the rest of the world is saying you are wrong. Those are the qualities I would look for.*
> *Audit Committee Chair, AC-6*

The participants referred to two sets of knowledge: technical knowledge, on the way an internal audit is done, and knowledge of the business world in general and the company's operations in particular. In sectors other than financial, this business approach is crucial. The credibility of internal audit greatly rests on the way operations perceive its competence in this sector, its ability to make recommendations that improve or facilitate their work in the field. In this context, the presence of a multidisciplinary team can be a major asset. One CAE comments that:

> *Each individual can provide a complementary vision according to his experience and professional training. If audits were all financial, there would be only accountants. But for audits that require examination of concepts of efficiency, you have to develop a good operational understanding. You have to be able to evaluate how the parts come in and reach the workstations; compliance; occupational health and safety; inventory counts; organizing the assembly line, in terms of both safety and efficiency. To grasp all that it takes a mix of pertinent professions. A CA rarely goes out on the floor; he needs an engineer to evaluate the field. He's less familiar with legal terms and needs a lawyer to review the contracts and legal obligations. Then, enlightened by other professionals, the CA can "translate" the information into figures, into financial performance concepts. But to have the desired effect on operations, to understand all of the facets of their work, you need a multidisciplinary team.*
> *Chief Audit Executive, CAE-3*

It is essential that the audit team present a good mix of knowledge and skills to face its challenges. Auditors must be able to speak the same language as auditees, to pinpoint and understand their concerns, obligations and risks. Several participants mentioned the positive effects of being able to integrate people from operations in audit teams. These movements can improve the depth and impact of internal audit reports by providing a close link with operations, and by increasing the credibility of the function through cooperation with people recognized in their respective sectors.

> *Show me an internal audit function that has no movement between itself and the organization, and I'll show you a compartmentalized internal audit function that's not very good. You need some cross-fertilization and some linkage, and without that internal audit rarely has good credibility and a real strategic role.*
> *Chief Audit Executive, CAE-8*

Rotation of a portion of the internal audit team may also, many argue, allow auditors to preserve their critical perspective and avert the likelihood of being trapped in a routine, which could have adverse effects on the organization.

Extending the mandate of internal audit to allow auditors to transcend a purely technical role where their tasks are limited to performing compliance tests can also promote a more stimulating and attractive experience. In fact, the profile of people interested in spending time in internal audit is improving. In terms of recruitment, undoubtedly a major challenge related to the development and effectiveness of internal audit teams in the coming years, this aspect could be interesting:

> *The flavour of the month right now is to add new roles to that group – I think it makes the job more interesting for internal audit people and because it's not an easy role to recruit for in many companies and some companies haven't made it any easier, but the blend between internal control professionals and people who are cycling themselves through a bunch of financial roles and even financial and operating roles, it was different in every company, and so making that job more interesting for people who might not have a specific internal audit background is a good thing because it means that you're going to get a richer blend of people in the department and it's going to get easier to recruit folks, especially young people.*
> *Audit Committee Chair, AC-7*

Directors should therefore ensure that their internal audit teams are made up of competent people with good business knowledge - or at least easy access to it - to favour their credibility. Expansion of the mandates conferred on internal audit can also offer professionals interesting challenges, which makes it easier to recruit superior candidates.

Favouring development of a relationship of trust

Credibility is only the first step in the development and deployment of an effective internal audit team. Internal audit needs to forge a relation of trust not only with the audit committee, but also with top management. The development of this dual relationship of trust is a formidable task. All internal auditors mentioned difficulties or, as they prefer to call them, major challenges in this area. The fact of reporting to both the audit committee and top management has several advantages, notably in terms of power, but this also creates tensions that must be recognized and addressed. Here again, directors can have a strong influence on harmonizing relations.

The audit committee must be involved in managing internal audit and ensuring that this function provides the committee with the support it needs to perform its duties. This support rests on the presentation of clear, pertinent and independent information on the company's situation regarding all of its major financial, operational and ethical risks. Internal auditors were asked for their views on what information to provide to the audit committee. While several auditors submit exactly the same reports, containing the same information, to all stakeholders, namely the unit audited, top management, the audit committee and when necessary the external auditor and monitoring bodies, others only reflected on the possibility of doing this. A distinction was made between full reports and summaries.

From the audit committee's perspective, transmission of full audit reports can be a heavy burden for directors. A summary of the main observations, important recommendations and an action plan follow-up can be sufficient. Evidently it is important that the substance remain the same and that directors receive an accurate picture of the situation.

If all findings, large and small, are transmitted systematically to the audit committee and the senior management, this creates major negotiations in the business units, which defend themselves by arguing that some points raised are not sufficiently important to be reported to the audit committee. All of the auditors mentioned that the formulation of reports is a sensitive topic that sometimes triggers in-depth discussions that can become very heated. To partly offset these difficulties, internal auditors have developed a number of strategies for transmitting the right information to the right hierarchical level. For example, an internal auditor can provide operations with a separate document containing less important findings that do not justify being reported to the audit committee, but that also should not be ignored. This complementary document can serve as an aid to managers and allow follow-up within the internal audit team. It is reviewed during the next audit in that sector, and auditors can observe how managers have corrected the situation. Another option is to hold informal meetings after the audit, to transmit important observations directly to operations. This approach seems to be greatly appreciated by officers because it lets them share complementary information with the internal auditor gathered from weeks spent in the field.

By paying attention to the level of information transmitted to the audit committee, directors can greatly decrease the tension that internal auditors face. By applying the “nose in, hands off” principle, directors ensure that they obtain the independent information they need to fulfill their mandate, while favouring a climate of trust between top management and the internal audit team, which boosts efficiency.

Repositioning internal audit

By ensuring the credibility of auditors, who demonstrate the necessary knowledge, skills and attitude, and by cultivating a relationship of trust between top management and internal audit, directors pave the way for a new positioning of the internal audit function. In recent years, expectations of internal audit have increased considerably. To become a strategic business partner for top management and a reliable and independent supplier of critical information for the audit committee, internal audit must be repositioned to gain the influence it needs to fulfill its new functions.

Discussions, negotiations and even conflicts are an inherent part of internal audit. To allow the function to be effective, not only must competent and courageous people be appointed, but they must be given sufficient authority to be able to impose, if necessary, acceptance of their recommendations.

> *Despite all the competence, efficiency, dynamism, leadership, and capacity to mobilize an internal audit team, at first, the evident support by top management and the audit committee is crucial. I remember the discussions I had with the audit committee chair on the importance he placed on internal audit, the message he planned to convey to all managers who go to the audit committee. But beyond that, it's the cooperation with top management that can bring about a change in mentality and facilitate the repositioning of internal audit.*

When I was appointed, the CEO met with the management committee and announced that he had appointed someone new to head internal audit. He insisted on the fact that he "believed in that person." This clear support, expressed openly, was a key element in the deployment of a new internal audit department and in its success.
Chief Audit Executive, CAE-1

CAE-1 is not the only chief audit executive to have stressed that support from the audit committee is very important, but it is often commitment by top management that lets the internal audit team work effectively. Officers are present in the company every day, and the signals they send to operations regarding the importance they place - or not – on internal audit often make a big difference. Officers are generally aware of the message they must convey, as one CEO explains:

Once we said that, what will the mission of internal audit be and how important will it be? It depends, in my view, on the CEO. Why? The first role of the CEO is "he sets the tone." Do you understand? He sets the tone, in the sense that it's he who establishes... It's like an orchestra conductor, do we play faster or slower? Louder or quieter? Do we... OK. And if the CEO greatly values internal audit... How do you do that? The quality of the person who will lead. The resources given to them. The role attributed to internal audit. For example, me I did it at other organizations, when I was CEO, to... I often did it... regularly in companies in which I was, I would do a quarterly review of operations. Then I was accompanied by... often the CFO, but regularly by internal audit. Why? Because all units and all unit leaders saw, at my side, the chief audit executive- who was often a woman. So, I put on the agenda: follow recommendations. Okay. Then it's crazy how it, as we say, it sets the tone, because people knew that in two weeks they would go see the CEO with their team to review all the operations and that the internal auditor will be there. And then if they were audited three months earlier, and the report sat on a shelf, well... he can't sleep anymore! So all that, it's little things but...
Senior Management, SM-2

The greater the relationship of trust between top management and internal audit, the more strongly officers will convey that internal audit is important to them. They will monitor reports, recommendations and action plans more carefully. If necessary they can insist that the business units cooperate or they can settle a dispute between them and internal audit. In daily management of the work of internal audit, full support of top management is essential.

The involvement of top management does not stop there. Once trust is established, it is critical that the CAE have access to important information concerning strategic planning, major initiatives done by the organization, the major risks it faces, etc. In other words, the CAE must "sit at the right table," and have frank and open discussions with the main officers, not only the CFO or the CEO. He must have access to the heart of the organization if his annual plan is to cover all of the most critical and strategic aspects, and have a real impact on the future of the company.

Directors must support this new positioning, and ensure that the CAE is considered a key player in the team. He can thus access the information he needs. He must also be granted sufficient support to prompt auditees to make the changes needed to improve processes and controls.

Clarifying the roles of each assurance function

Another important task is coordinating the various sectors that have assurance and control functions. Internal audit must often work with - or sometimes compete with - groups such as legal services, compliance, special investigations and risk management. Several participants specifically raised the topic of involvement of internal audit in the risk management process. Some comments imply competition between these sectors, which may represent a risk to the organizations affected. In fact, one of the strategies deployed to gain a competitive advantage concerns the retention of information:

> *You don't want internal audit to become a second-class citizen because the risk management department is taking up more room, and information does not circulate enough. It's crucial for internal audit to keep its place in the corporate universe. That's not always easy.*

Audit Committee Chair, AC-2

Well, I would say that Compliance, it's very clear what they have to do. It's really more Operational risk that's a new player, which in essence... which did not exist before and which inserted itself in everyone else's roles and responsibilities.
Chief Audit Executive, CAE-4

There absolutely needs to be cooperation, at least communication between risk management and internal audit... And it has to go both ways. I need to clearly understand what risk management finds important - even if sometimes the risk in question is not significant for internal audit, because it's not something that the company controls... – but if risk management finds it important, I need to understand why. Inversely, if I find something while doing my audits, something that risk management needs to know, I have to tell them. But these reflexes are not there yet. Everyone protects their territory and it's too bad...
Chief Audit Executive, CAE-15

In addition to creating a risk for the company by restricting the circulation of information, confusion between the different roles and the lack of cooperation between these functions inevitably leads to disagreements in operations. Managers complain of having to answer the same questions several times, which hinders their productivity. Some participants referred to "assessment fatigue":

Assessment fatigue it means plenty of people who come knock at your door and at some point they don't know who they spoke to any more. And what's symptomatic is that even internal auditors, regarding risk management, regarding regulatory compliance, it took time before they were able to understand - and I think it's not done yet in some cases. Yes there are some, it's a fact. I'd say that it's a perception, but it's a reality that there are perceptions of competition or functions that are on the defensive, who, of course, want to defend their turf and who see this as a threat because if someone else comes, he'll take my job. You know how it is. He'll do things that I can do.

Service Provider, SP-3

But this, all the risk analysis...Who would come to me with that? Because risk analysis, that's one thing ... There are so many people who do it... There, there may be some centralization possible... Because there is compliance risk, risk management does it, internal audit does it, everyone has their risk analysis, their template... In the end, it overlaps a lot... There was a lot of risk analysis. So I don't remember if... These functions would benefit from talking to one another anyway because there is at least an intersection on 80% of the equation. There is certainly synergy to be found there.
Senior Management, SM-5

Directors have a definite role to play in aligning all of these functions:

Today there are many people who proudly call themselves pillars of risk management and internal control. (...) We have a very evolved risk sector, very evolved risk management that not only does financial risks but really total risk mapping. There again there's a type of overlapping between what can be done in internal audit and what can be done by risk people. (...) I'll go sit down with these people. My main concern is that for one, I want to be sure there is no overlapping, that there is no duplication of work for the same risk sectors and at the same time I want to be sure we're not forgetting anything. We can't afford to have three pairs of eyes looking at the same activity, and forgetting about other activities. We have really reached a level where all these activities must be connected to be sure that the use of resources is optimal and effective at the same time.
Audit Committee Chair, AC-2

There are several ways to increase the synergy between internal audit and risk management. Apart from businesses operating in the financial sector – where regulation is very stringent and monitoring bodies favour a more conservative model with quite distinct and independent risk management functions and internal audit -- organizations have some flexibility in aligning these two functions.

On one side of the spectrum, internal audit can use the work of the risk management team as an "input" in its annual plan. According to some participants, this represents minimal interaction between the two functions. Without this minimum, work would be entirely duplicated and it is likely that an important activity may be overlooked. The CAE can also assist the management committee of the risk management team, as an observer, to gain an overview of the processes followed by this department, along with direct access to the results of their work.

Is it possible to coordinate the work of internal audit and risk management to hold only one series of meetings with managers, attended by the directors of both of these sectors? Opinions on this topic are divided. CAE-15 thinks that people do not confide in the risk management director, who is part of the management team, to the same extent as they do in the chief audit executive, who is a control tool used by the audit committee, but CAE-20 expresses a different viewpoint:

> *They say that the executives, they won't tell you anything in risk if they think you're going to audit. That's up to the individual to establish trust, because that's going to be the same if you go alone: they're not going to talk to you either. So how are you going to establish a rapport with them and develop a risk assessment for your audit plan if they won't tell you the truth? So really the matter's with the order of risk audit and audit, if they don't trust you, they don't trust you. So that's just a poor auditor, a poor leader, quite frankly.*
> *Chief Audit Executive, CAE-20*

At the other end of the spectrum, internal audit and risk management functions can be combined into one department. The IIA has cast doubt on the effectiveness of this formula because it can hinder the independence of internal audit and make auditing risk management impossible, yet some CAEs see it as an interesting solution. Notably, it allows information to circulate more effectively while limiting duplication. If this formula is subtly emerging,[6] several measures should be taken to control it adequately.

[6] Of the 21 chief audit executives interviewed in this study, only one officially held this dual function. Four CAEs mentioned this possibility because they heard about it in the conferences or discussions with peers.

Notably, decisions related to risk appetite must be upheld at the management level; the CAE can express his point of view but he should not be a decision maker on this topic. In addition, the entire risk management process should be audited by an external consultant to ensure the independence of the audit. Lastly, the CAE's competencies must include solid knowledge of risk management in the company's sector.

In all cases, the audit committee should be mindful of the desired level of coordination, cooperation and synergy among all the functions that provide important information regarding the financial and global health of the business. It can thus ensure that the image it has of its organization, which shapes its decisions, is as complete and accurate as possible. The better the roles of each function are defined and understood, and the more clearly the directors express their expectations in terms of cooperation, the lower the likelihood of the alignment of the sectors causing problems:

> *There is no problem between risk management and my team. Why should there be? Our specific mandates are very clear. I know very well where my role starts and stops in the risk management context. And the Chief Risk Officer knows and understands my involvement. It's written in my charter. The fact that it is clearly written, that the charter of internal audit clearly mentions the limits of our involvement, it makes relations between the two departments much easier. For the audit committee that's important.*
> *Chief Audit Executive, CAE-22*

Conclusion

Given their heavy responsibilities, directors stand to gain by using internal audit as a valuable tool to help them play their role. Internal audit has evolved considerably in the past decades in an effort to meet the expectations of officers and directors. However, its role varies greatly between companies. This flexibility can be an advantage by allowing

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Some referred to greater or lesser involvement with the risk management function, notably regarding an advisory role.

the function to meet the specific needs of businesses, but these needs must be clearly defined and expressed.

Directors have a crucial role to play in determining the role of internal audit within their organizations. Their important influence goes beyond what many think is the responsibility of the audit committee, namely to protect the independence of the function. Granted, this independence is important and even essential to allow internal audit to provide directors with pertinent and reliable information, without undue pressure from officers. However, sufficient alignment of internal audit with company operations often demands more involvement from directors.

There are few guides to help directors reinforce their links with internal audit. Best practices indicate the form of these relations: frequent discussions between the audit committee chair and the CAE, the presence of the CAE at audit committee meetings, and closed-door talks, among other activities. They also suggest what should be done by the audit committee: approval of the charter and annual plan of internal audit, following internal auditors' recommendations and assessing their work. Participants confirmed that these guidelines are followed by most audit committees, which try to control the quality of information they receive.

Many directors seem to think that following these prescriptions is all it takes to optimize the performance of internal audit. Some mentioned that the value added of internal audit mainly concerned top management, that diversification of tasks lets the organization recruit better internal auditors and can serve managers, but does not concern them very much. However, directors can take on a broader role. They may find advantages in becoming actively involved in creating a climate that favours negotiation of the role of internal audit.

One participant rightly commented:

> *Q. Do you think that internal audit is more a management thing, or an audit committee thing?*
> *R: Well, it should be more a management thing, but as I say, the rules and regulations surrounding governance these days make it an audit*

committee thing regardless. Because it’s one of those functions that’s half management and half control, then it’s in a very funny position. It’s between management and the board a lot of times.
Audit Committee Chair, AC-7

It is possible for the audit committee to participate in developing the role of internal audit, to help integrate this function in the culture of their organizations and its repositioning, and thus increase its influence and added value. Directors can work on making internal audit a useful tool while helping auditors meet the company's needs. They can thus find the delicate balance that will allow internal audit to become a true contributor to organizational governance.

Appendix 1: Acknowledgments to audit committee chairs

Dear Sir or Madam,

First, I would like to thank you wholeheartedly for participating in my research project on determining the role of internal audit. You granted me the privilege of accessing vast expertise that made for a very rich data collection. A thousand thanks again.

As promised, I am sending you a short summary (in the appendix) of the practical findings that I reached during my research. I hope they will interest you and be useful to you as director. If you would like to read the detailed report presented to the Institute of Corporate Directors, it will soon be published on the Canadian Foundation for Governance Research website: http://www.cfgr.ca/research-reports/.

If you have any questions or comments, please do not hesitate to contact me. Thank you again for your invaluable participation.

Best regards,

Sylvie Harbour

Determining the role of internal audit

The role and expectations of internal audit have changed dramatically in recent decades. This role apparently varies between companies, depending on the context of each organization, its sector, maturity, complexity, and other factors. My research project therefore tried to clarify how this role is manifested within companies, which people are involved in discussions about this function, and what are their expectations, among other factors. The better we understand how expectations of internal audit are created and formulated, the better this function can play its designated role.

Methodology

Through the invaluable assistance from the Institute of Corporate Directors, the Collège des administrateurs de sociétés and the IIA, I gained access to audit committee chairs and chief audit executives recognized as leaders within the North American business community. Thanks to personal contacts and the snowball effect,—participants who agreed to ask their boss or colleagues to participate in the project—, I interviewed 56 people, distributed as follows:

Position	Number
Chief Audit Executive	21
Audit Committee Chair	10
Top Manager	5
Consultant	5
Internal Auditor	8
Auditee	7

The participants originated from Québec (66%), the other Canadian provinces (25%) and the United States (9%). The directors encountered have chaired at least one audit committee. However, most chair several committees, in different sectors.

Concerning chief audit executives (CAE), 22 agreed to participate in the research. Of this number, six work in the financial sector, 14 in other sectors and 2 worked in both the financial sector and other sectors.

Main findings

Several participants described major changes in the business environment, which have impacted the development and role of internal audit. They include financial scandals that received intensive media coverage, new laws on corporate governance, pressure by monitoring organizations and training developed to help directors control their environment and companies more effectively.

To understand the development of internal audit, we must also look at the efforts put forth by the IIA to advance and defend its role with both legislators and in the business world. Discussions indicate that even if the IIA's discourse seems to have been formally retained by companies, internal auditors actually often lack the skills, experience and credibility they need to take their rightful place, notably in risk management and governance. In addition, the organizational context does not always let the internal audit team meet all the criteria of the IIA Standards. Audit committee members should discuss with the CAE to determine what should be done about this within their organizations.

Concerning the functioning of internal audit in companies, participants confirm that in general, the links between internal audit and the audit committee are significant. Audit committees ensure that their internal audit department has an acceptable budget, they approve the annual work plans, and follow the implementation of recommendations. However, the interviews also indicated that directors have a crucial role to play in determining the role of internal audit in their organizations. Their influence is important and goes beyond what many think is the responsibility of the audit committee, namely to protect the independence of the function. Granted, this independence is essential to allow internal audit to provide directors with pertinent and reliable information without undue pressure from officers. In fact, adequate alignment of internal audit with business operations often demands greater involvement by directors.

To enhance the effectiveness of internal audit, participants underlined the importance of respecting the organizational culture, even advancing it subtly if necessary to allow acceptance of the internal audit function by both top management and operations. For example, for companies that operate in a less regulated environment, and that are run by managers with an entrepreneurial spirit, it is very important to adapt the internal audit approach to the company's particular situation. In this context, value added for operations and management is an important and sensitive issue that affects the acceptance of internal audit. The notion of value added varies between companies. Many respondents mentioned ways internal audit can provide value-adding assistance, such as reducing operating costs by identifying sub-optimal processes, diffusing best practices and notable innovations, and training future managers.

If directors want to ensure that internal audit adapts to the organizational culture, and understands and responds to the specific needs of the business given its sector, they must ensure that internal auditors have sufficient credibility to play their role. This credibility is acquired partly because internal auditors possess the necessary skills to do their work, and partly because they are very familiar with the business operations and can therefore give executives valuable help. The relationship of trust between top management and internal audit is essential to allow auditors to be considered important partners. By being trusted partners, auditors are more likely to be kept informed of the organization's major initiatives, projects and risks.

Directors also have a pivotal role to play in clarifying expectations of internal audit and of other assurance functions such as compliance and risk management. Ensuring good risk coverage by avoiding duplication and redundancy can not only better protect the organization, but it also favours the development of synergy between these sectors, thus limiting turf wars and silos.

Conclusion

Directors should strive to actively develop the role of internal audit, support the integration of this function within the organizational culture and facilitate its repositioning to increase its influence and added value. Directors can make internal audit the tool they need while helping auditors meet the company's needs. They can thus strike a delicate balance that will allow internal audit to be a real asset to sound organizational governance.

Appendix 2: State of internal audit in Canada

State of internal audit in Canada

In the wake of the Enron, WorldCom and other scandals, major changes have recently been made to Canadian Corporate Governance. Regulators charged directors with the herculean task of implementing and supervising a solid governance process, thereby expanding their roles and responsibilities. The audit committee has been a focal point of governance reform in recent years, with heightened attention paid to the integrity of financial reporting, internal controls, and compliance and risk management processes.

In discharging their duties, boards can only be as good as the information that is provided to them, or to which they have access. From this perspective, the internal audit function might prove to be crucial for directors in general and members of the Audit Committee in particular.

In this context, a review of recent studies can highlight current reflection on the Audit Committee's role in overseeing internal audit. The purpose of this paper is to provide directors with food for thought on this topic and to succinctly summarize several professional publications that they may find informative.

Current positioning of internal audit in Canada

There is scant data on internal audit in Canada, mainly because up until recently Canadian internal auditors were part of the North American division of the Institute of Internal Auditors. In autumn 2010, Canadian auditors voted to create an independent Canadian Institute. The two-year transition process that followed will culminate on January 1, 2013 with the founding of the new institute.

The internal audit function in North America has been the subject of several reports. Although they do not address the Canadian situation in particular, they are worth consulting because recent research shows that there are few differences between Canada and the United States regarding the organization and use of internal audit. The context of market globalization and the fact that many large companies operate in both countries reinforce the plausibility of this finding. Therefore, I present North American information and distinguish Canadian data where possible.

Most studies that examine internal audit positioning, the makeup of audit teams or the role of audit within organizations have involved questionnaires transmitted directly to internal auditors, for example IIA members for studies of this organization, or chief audit executives (CAE) for surveys done by accounting firms. Although results vary depending on the respondents, the following elements emerge:

- Although the vast majority of internal auditors working in the private sector are hired by publicly traded/listed companies, the IIA has noted a significant increase, in recent years, in the number of teams deployed within privately held/non-listed companies;

- In terms of positioning, most internal audit teams report functionally to the audit committee. This committee, or its chair, is generally consulted during the hiring or dismissal of the CAE, although the final decision is generally made by senior management. Administratively, internal audit tends to report to the CEO or CFO. Other models exist where the CAE reports to another member of the executive suite, such as the Chief Risk Officer or General/Legal Council, although this structure is much less common. Statistical data seem to point to an industry effect in the choice of administrative supervisor.

- According to IIA data, internal North American auditors are generally older than their colleagues in other regions of the world. 71% of North American auditors are over age 44. The profession attracts equal numbers of men and women, according to the 2010 survey. The level of education of internal auditors is rising: most now hold a university degree. Lastly, internal auditors have more varied career profiles and work experience than before. Although most of them have training and experience in accounting, backgrounds in finance, management, IT, engineering and law are also present;

- The debate over outsourcing of the internal audit function seems to have faded since the 2000s. In general, companies engage in co-sourcing by hiring consultants with particular knowledge that the team lacks (according to IIA figures, nearly 60% of companies in North America use this technique).

Relations with other members of the organization

With auditees: the role of the internal auditor seems to have changed profoundly, evolving from that of “police officer” to one of “collaborator.” The audit committee must ease this transformation by focusing on the way the team builds relations with other members of the organization. Internal auditors are expected to develop trust-based relationships with management and auditees. It is important for the audit committee to ensure that the CAE is well connected to the executive branch to keep abreast of the activities and strategic initiatives of the organization.

Staffing internal audit teams with people who have experience in other departments (including operational areas) helps improve business knowledge.

Members of the audit committee must be prudent and ensure that internal audit has the recognition and independence it needs to carry out its duties. On a preliminary basis, all auditors met with as part of my research mentioned having often solid, even heated discussions with auditees concerning both the attribution of the overall rating and the presentation of some findings. In the most recent IIA survey (2010), 15% of North American CAEs mentioned that they experienced coercion to change a rating or assessment or to withdraw a finding in an internal audit report.

With the audit committee: links between the audit committee and internal audits are much closer than in the past. CAEs regularly attend meetings of the audit committee, and most of them confirmed that they have had informal discussions or meetings with the chair of the audit committee. Moody's Investors Service published an interesting guide in 2006 describing the audit committee's five central functions with respect to internal audit oversight. This report underlines that, together with management, the audit committee plays a critical role in communicating the importance of internal audit across the organization. This support from the audit committee grants internal auditors essential maneuvering room and powers they need to work effectively. Lastly, the audit committee or its chair is being consulted more and more often in the hiring, evaluation and rewarding of the chief audit executive.

With external auditors: as mentioned above, collaboration between internal and external audit is increasingly sought after by directors. The audit committee must ensure that the scope of each group is well defined, complementary and not overlapping. To achieve efficient coordination, the audit committee must also make sure that, while preserving the independence they need, both groups cooperate closely and discuss all problems openly.

Role of the internal audit function

Internal audit plays diverse roles in companies. Involvement in the processes of the Sarbanes-Oxley Act and its Canadian equivalent has apparently diminished considerably. Internal audit plans reflect much more balanced coverage among operational, financial, and compliance risks than was noted for much of the past decade. Nonetheless, the IIA and some accounting firms are dismayed that internal audit does not help assess the company's major risk management.

Because the role varies greatly between organizations, it is essential that the CAE, the audit committee chair and management have a consistent view of internal audit's role, level of audit coverage needed and, consequently, adequate funding of the department.

The following points often emerged in the professional literature:

- *Determination of audit scope:* this point is a major concern for audit committee members. Audit committee chairs increasingly expect internal and external auditors to have closer contact and to cover the organization's audit needs sufficiently, without overlapping. Some still hope that the work of internal auditors can reduce external audit costs, particularly regarding internal control certification, but this trend appears less significant than the will to ensure sufficient risk coverage.

- *Planning*: it is important for the audit committee to ensure that internal audit define a coverage plan to protect the organization. Although most works recommended that annual planning take into account the important risks for the company, many also insist on complete coverage over a determined period (for example every three or five years). Because risks and opportunities may change rapidly during the year, the plan must be flexible enough that it allows the internal audit team to adapt to a changing environment. Evidently, any significant variance relative to the initial plan must be explained to the audit committee, which typically must approve it. In addition, the IIA underlines the possible variance between audit plans and expectations of different stakeholders, notably the audit committee. Statistics show that internal auditors and audit committee members do not consistently identify the same risks as posing threats to the organization. In this context, it is crucial that the audit committee ascertains that the CAE grasps its vision and shares its risk assessment. The committee must then ensure that the annual plan prioritizes actions in line with this assessment.

-*Talent development*: The literature raises a major question: should internal audit serve as a training ground for the organization's future managers? This question has sparked many debates. In a recent survey of about 200 internal audit stakeholders[7] (audit committee member or chair; board chair; CEO, CFO or other executive to which the CAE may report administratively—the research was conducted in the United states only), the IIA found that almost 50% of respondents said that internal audit did not play this role. It is therefore very important to ensure that the stakeholders within the organization have a shared perception of this

[7] Institute of Internal Auditors Research Foundation (2011). *A Call to Action: Stakeholders' Perspectives on Internal Auditing*. Altamonte Springs, FL

role. If they decide that internal audit should provide training, particular coaching for future managers could be developed, related to objectives, training and supervision, for example. It may also be useful to develop separate key performance indicators that would reflect performance in this area, such as a target number of transfers to be achieved in a certain time period, or assessment of the performance of new managers trained by internal audit when they take on new positions;

- *Balance between assurance and advisory functions* is another area of significant debate. If some see internal auditors as advisors who should be enlisted in the organization's development projects, the majority disagree. Many seem to fear that if internal auditors offer advice about operations, their independence would be jeopardized, and they might not be able to objectively audit a project after the fact. However, internal auditors are generally invited to give advice,--especially regarding best practices--when they present their reports at the end of assurance engagements. It is in this context that the advisory aspect of auditors' work seems to be developing;

- *Involvement of internal audit in risk management and corporate governance assessment*: despite what the IIA and some accounting firms[8] insist, many maintain that internal audit, although it can become more strategic, should not participate in major risk management. Coordination between internal audit and other assurance departments such as Risk management, Compliance or Corporate strategy is a matter of concern for directors. My preliminary research results tend to affirm this problem. Because coordination between these functions is difficult, the members of the organization do not clearly understand the role of each function, feel that several teams ask them for the same information, and do not see the added value of one function compared with another. For members of the audit committee, this concern is twofold: they want to ensure that all the elements, in particular major risks, are well covered and managed, but they also want to avoid overlapping. Unfortunately, although it recognizes this problem, the professional literature offers few suggestions for how directors can address and solve these difficulties.[9] Developing this research topic could certainly help directors fulfill their coordination and supervisory role.

Evaluation of the internal audit function

[8] See PriceWaterhouse Coopers (2012). *Internal audit 2012: A Study Examining the Future of Internal Audit and the Potential Decline of a Controls-centric Approach*.
[9] Moody's (2006) and PriceWaterhouse Cooper (2012) arguably offer the best perspective on this question.

Studies tend to demonstrate a gap between the objectives of internal audit and the way its performance is evaluated. The main tools used to assess internal audit are:

- Typically, audit committee members have relied on the percentage of the annual plan achieved in the specified time frames to determine their level of satisfaction with the internal audit function;

- Another traditional way to evaluate the efficiency of internal audit is to look at the level of acceptance of internal auditors' recommendations and the rate of implementation of recommendations by the units audited. Yet this assessment method can have perverse effects in that auditors may be tempted to dampen their report or change their recommendations to obtain a better acceptance rate. However, the audit committee evidently plays an important role in ensuring that the recommendations are studied and implemented with full support from management;

- Increasingly, surveys and comments by different parties involved in internal audit (senior management/board members/audit committee members) are used to assess the auditors' work and improve their effectiveness. Auditees' views are being increasingly solicited to better determine the quality of work and interactions with internal auditors;

- Organizations, albeit a minority, are beginning to use a balanced scorecard to examine all the facets of the internal audit team's work. This balanced scorecard notably takes into account the development objectives of internal auditors and of team members who are training to hold managerial positions within the organization, along with relations with different organization members, the process of formulating the annual plan, etc.;

- Lastly, some companies consider the criterion of external auditors' reliance on internal audit.

In conclusion, the IIA recommends that internal audit be subject to periodic external assessment, either by a consultant (such as an accounting firm or internal audit consultant such as Protiviti) or by the IIA directly.

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