



# Factsheet: Chief Audit Executive Reporting

## Introduction

The definition of internal auditing is:

*An independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.*

This definition is contained in the 'International Professional Practices Framework' (IPPF) issued by the Institute of Internal Auditors (IIA).

If internal auditing needs to be independent and objective to effectively perform its role, what needs to happen for this to occur?

### How can internal audit be independent?

The assurance environment in organisations is generally structured as follows, but aligned to the specific assurance environment of individual organisations:

## 3 Lines of Assurance

1st Line of Assurance <i>Owns and manages risk</i>	2nd Line of Assurance <i>Monitors risk</i>	3rd Line of Assurance <i>Assures risk is managed</i>
<b>Management Controls</b> <i>Real-Time Focus</i> › Review governance and compliance › Implement improvements	<b>Management of Risk</b> <i>Real-Time Focus</i> + Review Focus of 1st Line › Confirm governance and compliance › Recommend improvements	<b>Independent Assurance</b> <i>Review Focus of 1st Line and 2nd Line</i> › Independently confirm governance and compliance › Recommend improvements
› Management controls › Internal controls › Project controls	› Risk management › Legal compliance › Technical compliance › Regulatory compliance › Security › Inspection activities › Quality activities › Work health safety › Environment	› Internal Audit

Internal Audit is a part of the organisation and therefore must be independent of management (1st and 2nd lines of assurance) if it is to perform its role independently and effectively without undue influence from management.

Internal audit independence is achieved by the chief audit executive reporting:

- › Functionally for operations to the audit committee through the chair.
- › Administratively to the chief executive officer.

Functional reporting generally involves the audit committee:

- › Reviewing and endorsing the internal audit charter.
- › Endorsing decisions regarding appointment and removal of the chief audit executive and contributing to the chief audit executive performance assessment.
- › Reviewing and endorsing the internal audit plan and any changes.
- › Reviewing reports on the results of internal audit engagements, audit-related activities, audit team capability, audit performance and other important

matters.

- › Monitoring compliance with standards, together with quality and improvement arrangements.
- › Meeting privately with the chief audit executive regularly without management present.
- › Making enquiries of the chief audit executive to determine any scope or budget limitations that may impede the execution of internal audit responsibilities.

Administrative reporting to the chief executive officer generally includes:

- › Internal audit resources and annual budget.
- › Provision of corporate services to internal audit including office accommodation, computers and equipment.
- › Human resource administration.

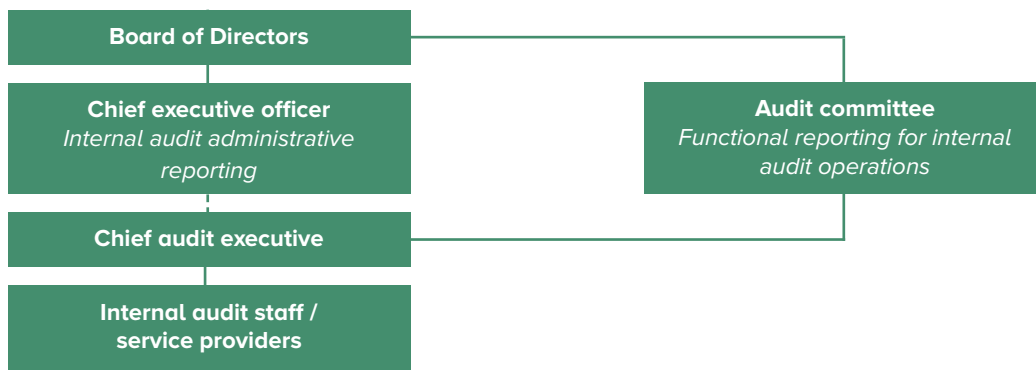
Where busy chief executive officers may decide to delegate administrative responsibility for internal audit, and this does not conflict with mandated requirements in their jurisdiction, it is usually to the next most independent senior executive who should be in an area where there is little internal audit activity,

for example general counsel or company secretary. It should not be the chief finance officer, chief operating officer or head of corporate services as those roles usually have a lot of internal audit activity and this leads to a perceived conflict with internal audit independence. In some organisations there is actual interference to internal audit independence and work by internal audit reporting to the chief finance officer, chief operating officer or head of corporate services.

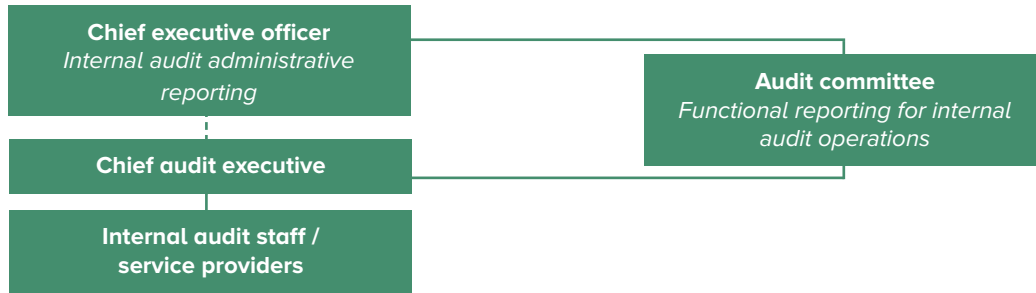
Should a chief executive officer decide to delegate internal audit administrative reporting, safeguards need to be built-in to the internal audit charter. This would include regular meetings with the chief executive officer so the chief audit executive can provide:

- › Independent and unbiased advice, assurance and support.

**Organisation with a board of directors**



**Organisation without a board of directors**



**Conclusion**

Organisations that take internal audit seriously will implement good practice independent reporting arrangements, regardless of whether this means internal audit does not report through a layered hierarchical organisation management structure that can lead to the very real risk of internal audit loss of independence. A loss of independence negates the core value of internal audit as the only independent voice at the table.

**Useful references**

- ‘Audit Committees – A Guide to Good Practice 3rd edition’, Australian Government Auditing and Assurance Standards Board / Australian Institute of Company Directors / IIA-Australia
- ‘Internal Audit in Australia’, IIA-Australia
- White Paper ‘Internal Audit Independence Arrangements’, IIA-Australia
- The 20 Critical Questions Series ‘What Directors should ask of Internal Audit’, IIA-Australia
- Factsheet ‘Chief Audit Executive’, IIA-Australia
- Factsheet ‘Evolution of Internal Audit’, IIA-Australia

- › Early warning of emerging issues.
- › A briefing following each audit committee meeting.
- › Advice on appropriateness of the internal audit resources and annual budget.

There should also be chief audit executive access to the chief executive officer any time the chief audit executive believes it may be warranted for important issues that may arise.

**What does good practice internal audit reporting look like?**

Good practice internal audit reporting arrangements can be shown diagrammatically as:

- APRA Prudential Standard CPS 510 Governance, Australian Prudential Regulation Authority
- ASIC Information Sheet (INFO 221) Internal Audit, Australian Securities and Investments Commission
- ‘20 Questions Directors should ask about Internal Audit’, Canadian Institute of Chartered Accountants
- ‘Core Brief for the Recruitment of Head of Internal Audit Posts in Central Government’, Her Majesty’s Government United Kingdom
- ‘King Code of Governance for South Africa’, Institute of Directors South Africa
- ‘Better Practice Guide: Public Sector Audit Committees’, Australian National Audit Office
- ‘Internal Audit and Risk Management Policy for the General Government Sector TPP 20–08’, NSW Treasury
- ‘Treasurer’s Instructions’, Government of Western Australia
- ‘International Professional Practices Framework’, IIA-Global

