The Institute of Internal Auditors Australia

Dear Q&A

Is it usual for an audit committee chair to instruct internal audit to increase observation risk ratings in an internal audit report and then re-issue the report?

Answer

It is not unknown for those charged with governance to have a different view of risk from the one held by management. The board would be expected to have a wider view of organisation objectives than management do and the audit committee is a direct adviser to the board. Ideally an audit committee will be a formal board sub-committee chaired by a board member or an independently appointed person. Under these circumstances the audit committee chair may be reflecting a specific sensitivity the board has when making the direction to internal audit to change a report.

The task of the internal auditor is to give a professional opinion to the audit committee. This involves the internal auditor forming their own view without undue influence from management, though management should be consulted about their view of observation risk ratings contained in a draft internal audit report. The opinion of management is valuable, but it should not determine the rating given by the internal auditor. Agreeing a rating with management is not essential; it may give the internal auditor confidence in their own assessment, but it may also reflect the result of negotiation and dilution of the internal auditor's conclusions.

A risk matrix is a guide rather than a constraint. It helps those who are assessing risk to scale risks in the same way, but it is not infallible. The internal auditor should always look at the result and ask themselves whether it looks right when compared to other risks. The risk matrix should reflect the risk appetite of the board. If it does not, then situations such as described may occur regularly.

If the chair of the audit committee does not agree with the internal audit report result, then the internal auditor should engage with the chair to find out why. This may lead to a valuable discussion that provides the internal auditor with greater insight into the thinking of the board and the board's risk appetite.

It does not seem appropriate for the audit committee chair to direct re-issue of an internal audit report unless the internal auditor has come to the conclusion the risk indicated in the original report is incorrect. If the internal auditor is not convinced, they should stand by their professional judgement. The audit committee can always formally determine that an observation be given a higher (or lower) risk rating than the internal auditor has recommended. This is within the authority of the audit committee. The internal auditor is an advisor to the audit committee and the committee is not obligated to take the internal auditor's advice. On the other hand, the internal auditor must be able to stand by their advice – the internal auditor's opinion should not be dictated by any member of an audit committee, even the chair.

Need an answer? Send your questions through to IAassist@iia.org.au