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مركز أبوظبي للحوكمة  
Abu Dhabi Center for Corporate Governance



# The Role of Internal Audit in Strengthening Corporate Governance



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ABU DHABI CHAMBER OF COMMERCE & INDUSTRY

IIA Conference  
Abu Dhabi 13 April 2010

# What is Internal Audit?

- Definition of Institute of Internal Auditors:
  - Internal auditing is an **independent**, objective assurance and **consulting** activity designed to add value and improve an organization's operations.
  - It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and **governance processes**.



# The Evolving role of Internal Audit

- Initially, internal auditors were focusing on compliance of operations with the set policies and procedures.
- Then, the scope increased to cover the internal control environment.
- Then, internal auditors started assessing the risk within organizations (COSO ERM framework).
- Now, many stock markets require that public listed companies have internal auditing function within their organizations.
- Internal Audit's role is expected to widen and cover CG within their entities



# Corporate Governance

- Definition of CG by OECD:
  - Corporate governance involves a set of relationship between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined.



# Corporate Governance Components

1. Board of Directors & Committees.
2. Laws and regulations.
3. Business Practices & Ethics.
4. Disclosure & Transparency.
5. Enterprise Risk Management.
6. Monitoring.
7. Communication.



# Internal Audit role with CG Components

## 1. Board of Directors & Committees

- Assist board of directors in its self-assessment and best practices.
- Assess Audit committee effectiveness and compliance with regulators.
- Review audit committee charter with help of legal counsel.
- Be interactive of the subject of governance, bringing best practices ideas about internal controls and risk management processes to audit committee members.
- Establish accuracy of information used in compensation committee decision making.



# Internal Audit role with CG Components

## 2. Laws & Regulations

- Verify that the organization has identified assigned responsibilities and addressed all of the key legal and regulatory requirements.
- Look for opportunities to leverage compliance activities and capabilities to reduce long-term costs and improve performance.



# Internal Audit role with CG Components

## 3. Business Practices and Ethics

- Review code of conduct and ethics policies, making sure they are periodically updated and communicated to management and employees
- Perform a behavioral ethics review to assess the understanding and perception and compliance across organizational levels.
- Help management and audit committee hold people accountable (look at the actions not just words).
- Serve in the ethics oversight role or confer with the organizations ethics officer.
- Conduct annual audits and reporting results to the audit committee.
- Assess linkage of ethics to goal setting and performance evaluation process.



# Internal Audit role with CG Components

## 4. Disclosure and Transparency

- Conduct testing of financial disclosures and confer with the CFO.
- Understand concern for disclosure and transparency and align risk assessment with stockholder expectations.
- In the annual audit plan, address disclosure and transparency objectives.
- Understand the breadth and depth of disclosure and transparency possibilities and where the organization strives to be or should be on the spectrum.



# Internal Audit role with CG

## Components

### 5. Enterprise Risk Management

- Be proactive in advocating for participating in an organization's ERM efforts , including a commitment to common methodologies and tools.
- Facilitate identification of key risk areas for the organization as well as all key processes.
- Assist in the development of standards and processes flow documentation.
- Assist process owners in understanding assessing, designing and document controls.
- Inventory organizational risk compliance activities and strive to integrate them into a common methodology.
- Evaluate business and process owners on taking responsibility for ERM.



# Internal Audit role with CG

## Components

### 6. Monitoring

- Understand what monitoring activity is taking place in the organization for each of the other component of the governance framework.
- Facilitate the implementation of a common risk monitoring methodology across all corporate governance functions, feeding an integrated reporting system.
- Perform a strategic level corporate governance audit or ensure one is conducted.
- Incorporate tactical level corporate governance aspects into audit plans.



# Internal Audit role with CG

## Components

### 7. Communication

- Participate in ongoing dialogue with general counsel, chief financial officer, and other senior management officers.
- Maintain steady communication with audit committee members and oversight executives.
- Include information about corporate governance in audit reports.
- Assist establishing a corporate governance communications calendar and solicit input on needs and articles across the organization.



- When all the components of CG framework operate effectively and are well coordinated, corporate governance provides a platform to improve business performance and enhance stakeholders value.



# The Functions of Internal Audit within the Context CG

- Internal auditors operate in two capacities:
  - First, provide independent, objective assessment on the appropriateness of the organization's activities.
  - Second, act as catalysts for change, advising or advocating improvements to enhance the organization's structure and practices.



- Internal auditor's unique position in an organization allows him or her to observe governance structure and design, while not having direct responsibilities on them.
  - Advising the board and executive management on needed improvements and changes in structure and design
    - Not just whether established processes are operating.



- By providing assurance on the organization's risk management, control and governance processes, internal auditing becomes a key cornerstone for effective organizational governance.
- Support the audit committee in fulfilling its responsibilities.



# Challenges Facing Internal Auditors

- Remain independent and objective, yet being part of the organization.
- Require business knowledge, insight, good judgment and effective communications.
- Organizations to recruit and retain experienced auditors.
- Biggest challenge on organizations and auditors is that no one-size-fits-all method to improve corporate governance.



# Recent GAIN Report

- (A world in Economic Crisis: Key Themes for refocusing Internal Audit Strategy)
- Recent survey and roundtable conducted by the IIA in March 2009
- Participants comprised CAEs from fortune 100, US Public Company Accounting Oversight Board and other accounting firms



# Key Findings of the Recent GAIN Report

- Changing stakeholders expectations are prompting audit strategy revisions.
- A broader, more strategic focus on risks is developing.
- The focus of internal audit's coverage is shifting dramatically.
- CAE's and endeavoring to do more with less.



# 10 TAKE-AWAYS

1. Ramp up communication with management and the audit committee.
2. Place renewed focus on risk management and governance processes.
3. Strengthen your risk assessment process
4. Operate with a more flexible and adaptable audit plan.
5. Serve as a risk management educator.



# 10 TAKE-AWAYS

6. Focus on recession – related risks and activities.
7. Expand fraud testing in the audit plan.
8. Strength business knowledge
9. Strengthen your relationships and communications with the organization's other governance, risk, and control functions
10. Enhance the efficiency of your audit processes.



# Abu Dhabi Center for Corporate Governance



## Contact Us

P.O. Box 6700, Abu Dhabi

United Arab Emirates

Tel. +971 2 4474611

Fax: +971 2 4473630

[info@adccg.ae](mailto:info@adccg.ae)

[www.adccg.ae](http://www.adccg.ae)

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