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Center for Board Effectiveness

On the Audit Committee's Agenda

Governing a relevant, effective, and valued internal audit function

In January 2024, The Institute of Internal Auditors (The IIA) released the new Global Internal Audit Standards™ (Standards) to elevate the quality and effectiveness of an organization's internal audit function and its activities. The new Standards aim to elevate internal audit practices globally, enhance the credibility and relevance of internal audit functions, and support internal audit activities in providing greater value to organizations through improved governance, risk management, and control processes.

The new Standards represent an important evolution in the practice of internal auditing in consideration of increasingly complex and dynamic risk environments, rapid technological advancements, increased stakeholder expectations, and growing emphasis on strong organizational governance practices. At the same time, there is an expectation of increased accountability and performance from the internal audit function.

Internal audit functions need to evolve and adapt to remain relevant, effective, and of value in today's fast-changing business environment. For audit committees, understanding the new Standards is crucial to providing the necessary oversight of the internal audit function for their organization to be able to leverage internal audit more effectively.

The new Standards become effective January 9, 2025. Many internal audit functions have already assessed, or are in the process of assessing, their current practices against the new Standards to identify actions needed to prepare for their implementation and adoption. While more mature internal audit functions may be more aligned with the new Standards, many internal audit functions are finding that they need to take some action for conformance.

In addition, the new Standards have introduced the concept of "essential conditions" or activities of the board (typically the audit committee)[1] and senior management that are considered essential for the internal audit function to be effective. These essential conditions should be a foundation for dialogue between the audit committee, chief audit executive, and senior management and are discussed in more detail in another section.



[1] The Global Internal Audit Standards define the term "board" as the highest-level body charged with governance of the internal audit function, which in many organizations, is the audit committee.



Attributes of an effective internal audit function

The new Standards emphasize several important attributes (and related practices) that demonstrate an effective internal audit function and promote internal audit activities being conducted with a high level of professionalism, consistency, and quality—ultimately adding value to the organization. We have identified 10 attributes for audit committees to consider as their internal audit functions prepare to adopt the new Standards.

1 Independence and objectivity

The need for internal audit to be independent from the activities it audits remains. This is typically achieved by having a direct reporting line to the audit committee and safeguards in place when the chief audit executive has additional responsibilities outside of internal audit. In addition, internal auditors must maintain an unbiased mindset and avoid conflicts of interest to ensure that their assessments are impartial and credible.

2 Governance and oversight

The internal audit function should operate within a strong governance framework, with a clear mandate and support from the audit committee and senior management. Direct oversight by the audit committee enhances the function's independence and effectiveness.

3 Competence and professionalism

In today's evolving risk landscape, it is important that internal auditors possess the required qualifications, skills, and experience—not just for this year's internal audits, but for emerging risks and changing organizational needs. Ongoing training and professional development are essential to keep internal auditors updated on the latest emerging risks, industry trends, standards, regulatory requirements, and leading practices.

The new Standards also promote a high level of professionalism within the internal audit function, reinforcing the importance of ethical behavior, confidentiality, and due professional care.

4 A risk-based approach

Internal audit functions must have the required resources, skills, and methodologies to conduct comprehensive risk assessments and to identify, evaluate, and prioritize risks effectively in support of the organization's overall risk management framework.

Internal audit activities should be prioritized based on a comprehensive and dynamic risk assessment, focused on addressing the most significant risks of the organization and aligned with the organization's strategic objectives and risk profile. These activities should support the establishment and maintenance of robust governance, risk management, and control processes.

5 Balance of assurance and advisory services

The new Purpose of Internal Auditing statement within the Standards states that "internal auditing strengthens the organization's ability to create, protect, and sustain value by providing the board (i.e., audit committee) and management with independent, risk-based, and objective assurance, advice, insight, and foresight." This purpose can be achieved through a balance of both assurance and advisory services to comprehensively support achievement of organizational objectives and maintain robust governance, risk management, and control processes.

Assurance services:

- Provide independent evaluations of the effectiveness of the organization's risk management, control, and governance processes.
- Help ensure that the organization's risk management framework is functioning as intended and that controls are adequate and effective.
- Provide confidence to stakeholders that risks are being managed effectively.
- Support the integrity and accountability of the organization by helping ensure that governance structures and processes are effective and in compliance with regulatory requirements.
- Build trust among stakeholders, including the board, audit committee, regulators, and investors.
- Promote compliance with relevant laws, regulations, and standards, reducing the risk of legal and regulatory penalties.



Advisory services:

- Offer insights and recommendations to proactively improve processes, enhance efficiency, and mitigate risks, particularly those that are new or emerging.
- Proactively identify potential risk and control issues and suggest improvements before they become significant problems.
- Promote a culture of continuous improvement and strategic decision-making.
- Support strategic initiatives and provide insights that align with the organization's goals and objectives, enhancing overall organizational performance.
- Identify opportunities for enhancing governance and control processes, supporting the organization in being agile and responsive to changes in the external environment.
- Foster collaboration with management, leading to more effective implementation of recommendations and improvements—enhancing stakeholder confidence in the internal audit function.
- Identify areas where compliance processes can be enhanced, helping the organization stay ahead of regulatory changes and requirements.



A balanced approach provides an enterprise-wide view of the organization's risk landscape, combining the thoroughness of assurance services with the forward-looking perspective of and insights from advisory services. This integrated approach supports an internal audit function that can address both current and future risks effectively, as well as internal auditors who can provide more comprehensive insights to help the organization navigate complex and interconnected risks.

6 Resilience

The internal audit function should be adaptive and agile, capable of responding to changes in the organization's risk profile and external environment. A culture of continuous improvement and innovation of approaches and technologies is important to be resilient.

The dynamic nature of today's business environment requires resilience—and balancing assurance and advisory services can further allow internal auditors to respond effectively to emerging risks and changing organizational needs, as well as encourage the organization to adapt and innovate in response to new challenges and opportunities.

7 Use of technology

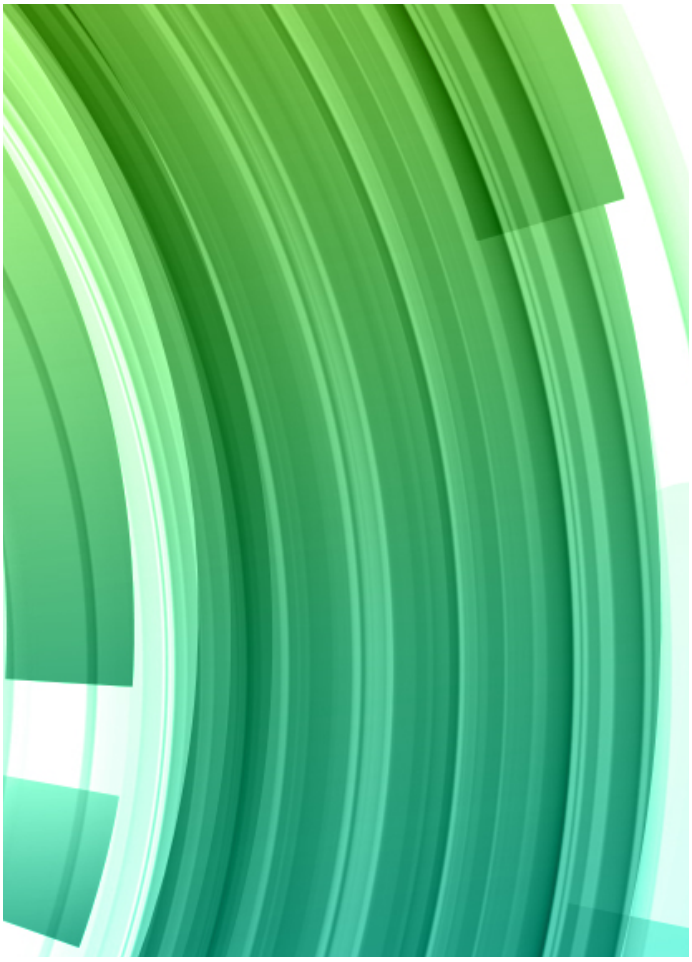
Embracing technology and digital capabilities within internal audit can enhance the efficiency and effectiveness of internal audit activities, as well as support the internal audit function's ability to help management better anticipate risks and control issues—including in the organization's own use of technologies.

Internal auditors should obtain the required competencies, training, and professional development to use technology effectively and efficiently in their internal auditing practices and to support risk management within their organization and its use of technology.

8 Effective communication and reporting, with a focus on value

Effective communication and collaboration with key stakeholders—including management, the audit committee, and external auditors—is critical for internal audit activities being responsive to the needs and expectations of the organization. Internal audit reports should provide valuable insights and recommendations to management and the audit committee. Reporting should be clear, concise, and actionable.

Internal audit activities should be aligned with the organization's strategic objectives and priorities and provide insights that help the organization achieve its goals and improve operations. By evaluating governance, risk management, and control processes and their ability to enable the achievement of the organization's objectives, the internal audit function can add significant value to the organization.



9 Quality assurance and improvement

The internal audit function should have a robust quality assurance and improvement program in place to evaluate the effectiveness of the function, assess achievement of the function's performance objectives, and continuously innovate and mature. Both internal and external assessments should be conducted, with periodic external assessments providing for an independent evaluation of the internal audit function's performance.

10 Adherence to ethical standards

The new Standards emphasize the importance of integrity and objectivity in internal audit activities, which helps establish trust among stakeholders, including the board, audit committee, management, and external parties. Internal auditors should adhere to a code of ethics that promotes integrity, confidentiality, and professional behavior. The internal audit function should also promote an ethical culture within the organization and support ethical decision-making and behavior.

Essential activities of the audit committee (and senior management) that support an effective internal audit function

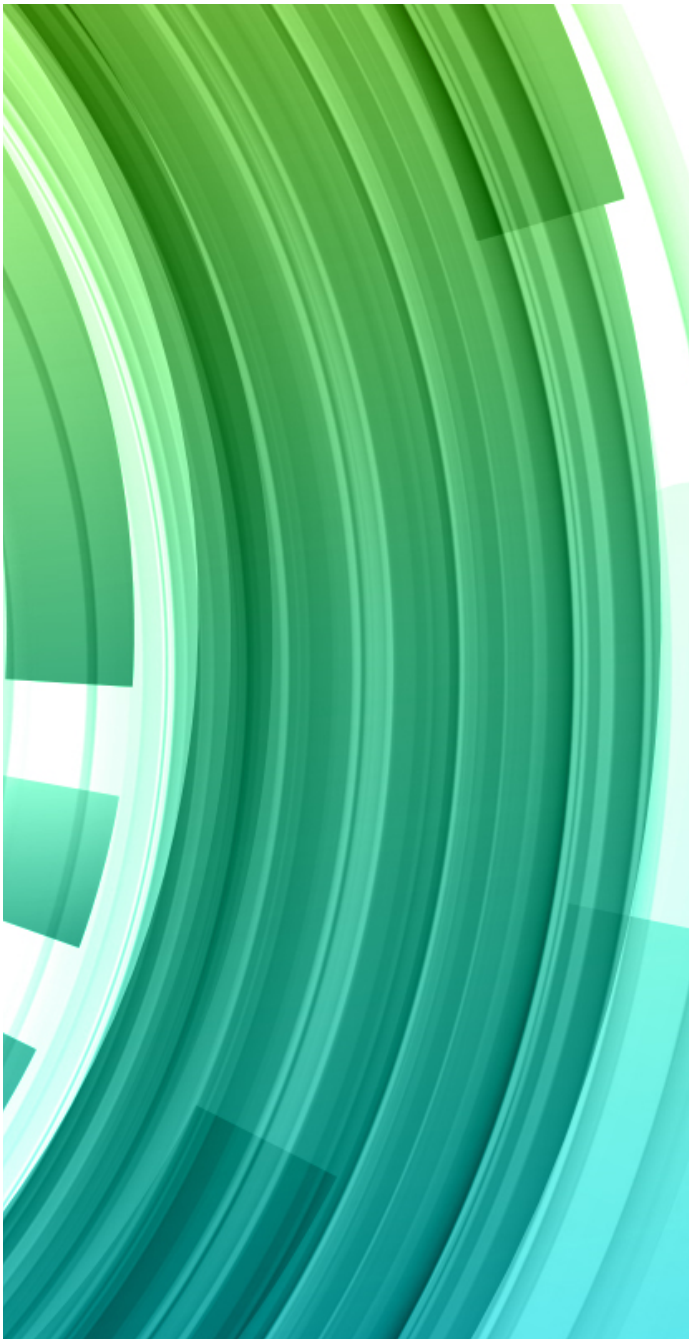
Boards, and specifically audit committees, play a critical role in overseeing the internal audit function and supporting its effectiveness. The chief audit executive is responsible for the internal audit function's implementation of and conformance with the new Standards and related principles—and the new Standards outline the requirements of the chief audit executive.

However, in developing the new Standards, there was also recognition by The IIA that there are essential governance activities performed by the board (typically audit committee) and senior management. These activities are believed to be necessary for the internal audit function to be most effective and enable the audit committee and senior management to champion and promote internal audit within the organization. They are labeled "essential conditions" and are contained within the new Standards in Domain III: Governing the Internal Audit Function.

Essential conditions in summary

Each standard within Domain III includes the essential conditions for the board (i.e., audit committee), and separately for senior management, that should exist for appropriate governance in support of an effective internal audit function. The new Standards outline the requirement for the chief audit executive to have a dialogue with the audit committee and senior management about the importance of the essential conditions and to gain alignment (or understand the potential impact on the effectiveness of the internal audit function if there is disagreement about the support outlined in the essential conditions).

As Domain III states, it is important for the chief audit executive to receive input from both the audit committee and senior management. The audit committee has the ultimate responsibility for governance as outlined in Domain III; however, senior management plays a significant role in supporting, championing, and promoting the internal audit function.





The essential conditions outlined in Domain III specific to the board address:

Governance framework

- **Clear mandate:** Ensure that the internal audit function has a clear and appropriate mandate (i.e., the authority, role, and responsibilities of the internal audit function) documented within the internal audit charter.
- **Independence and objectivity:** Safeguard the independence of the internal audit function (and objectivity of its internal auditors) by ensuring the function has direct access to the audit committee and is free from undue influence.

Resource allocation

- **Adequacy of resources:** Collaborate with senior management to provide the internal audit function with sufficient resources—financial, human resources (talent, as well as continuing training and professional development), and technology. Consider the impact of insufficient resources on the internal audit function's ability to fulfill the internal audit mandate and achieve the internal audit plan.
- **Competency development:** Invest in the continuous professional development of internal audit professionals (or access to sourcing) to support the internal audit function in having (or being able to obtain) required skills and knowledge for today and the future.

Communication and reporting

- **Transparent communication:** Support open and transparent communication between the internal audit function, management, and the audit committee. Promote effective communication and collaboration between internal auditors and key stakeholders. Set expectations for communication, including frequency and escalation criteria and process.
- **Alignment with organizational objectives:** Share information (or involve the chief audit executive) in strategic planning processes to better align internal audit activities with the organization's goals.
- **Actionable reporting:** Require internal audit reports to be clear, concise, and actionable—providing valuable insights and recommendations for improvement.





Support of the internal audit function

- **Championing internal audit:** Support and promote recognition of the internal audit function throughout the organization to enable the internal audit function to fulfill its purpose and effectively pursue its strategy and objectives.
- **Positioning and authority:** Demonstrate support through internal audit's positioning (i.e., administrative reporting line) within the organization and authority (i.e., its mandate).
- **Quality and performance:** Provide perspective on the organization's strategies, objectives, and risks to assist the chief audit executive in developing the internal audit function's strategy, performance objectives, plan, and priorities. Ensure there is a quality improvement and assurance program in place to support internal audit activities being conducted in accordance with the standards and continuously improved. Monitor the quality and assess the efficiency and effectiveness of the internal audit function (including collaboration on the external quality assessment, required every five years per the Standards.

The essential conditions are foundational elements that should be in place to support the internal audit function's ability to operate effectively and in accordance with the new Standards. It is important that audit committees understand these essential conditions and their implications in order to effectively oversee the internal audit function and help it add significant value to the organization.

Considerations for the audit committee in supporting adoption of the new Standards

Audit committees play a critical role in oversight of the internal audit function's implementation and adoption of the new Standards. We have identified some specific responsibilities below.

1 Oversight and guidance

Provide oversight and guidance to the chief audit executive as to implementation of the new Standards and to determine alignment with the related essential conditions and information needed from the chief audit executive.

2 Resource allocation and readiness preparation

Determine if the internal audit function has the required resources, including budget and personnel, to implement, adopt, and conform with the new Standards. Discuss with the chief audit executive any resource constraints, as well as expected implementation areas that may require a higher level of effort or time. In order to adopt and conform with the new Standards in early 2025, internal audit functions should be performing a readiness assessment and identifying and prioritizing required actions to be taken. In addition, internal audit functions should invest in training and development programs for internal audit staff to confirm that they are well-versed in the new Standards and expectations.

3 Stakeholder communications

Communicate and collaborate with key stakeholders, including management and the external auditors, about the changes and implications.

4 Monitor performance and progress

Understand the internal audit function's progress toward implementation and adoption of the new Standards. Provide input to the chief audit executive as to the function's strategy, performance objectives, and performance measures, considering the new Standards as the baseline for expected performance.





5 Maturity expectations

Communicate expectations to the chief audit executive of areas in which the audit committee prioritizes maturity of the internal audit function beyond just conformance with the new Standards. Discuss with the chief audit executive the strategic activities required to advance from current to desired state—and the resources needed to achieve this. Ensure that those considerations are incorporated into the internal audit function's longer-term strategy, performance objectives, and performance measures.

Conclusion

The new Global Internal Audit Standards™ represent a significant step forward in the evolution of internal auditing and opportunity to continue to elevate and mature the internal audit function. They serve as a benchmark for internal audit functions to measure their performance and effectiveness against globally recognized standards and promote continuous improvement and delivery excellence. The new Standards also serve to support internal audit functions in remaining relevant, effective, and valuable in an increasingly complex and dynamic business environment.

For audit committees, understanding the new Standards and their implications is crucial to helping ensure that their organization is leveraging the internal audit function effectively. By staying informed and proactive, audit committees can help their organizations navigate the complexities of the new Standards and achieve greater value from their internal audit activities.

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