

Internal Audit Committee

(Following the Facilities and Property Committee)

Friday, February 15, 2013

Board Room

2nd Floor, J.S. Clark Administration Building

Southern University and A & M College

Baton Rouge, Louisiana

Agenda

1. Call to Order
2. Roll Call
3. Adoption of the Agenda
4. Public Comments
5. Action Items
 - A. Report from System Internal Auditor on SU System Employee Audit – Executive Session may be required (Braxton)
 - B. Revised Reporting Structure for SU Internal Audit Function (Lawson)
6. Informational Item
7. Other Business
8. Adjournment

Members

Mr. Myron K. Lawson, Chair; Mr. Calvin W. Braxton, Sr., Vice Chair;
Atty. Murphy F. Bell, Jr., Mr. Willie E. Hendricks,
Dr. Eamon M. Kelly, Mr. Mike A. Small, Dr. Leon R. Tarver II
Atty. Bridget A. Dinvaut – Ex Officio

Practice Advisory 1110-2: Chief Audit Executive (CAE) Reporting Lines

Interpretation of Standard 1110 from the International Standards for the Professional Practice of Internal Auditing

Related Standard

1110 – Organizational Independence

The chief audit executive should report to a level within the organization that allows the internal audit activity to accomplish its responsibilities.

Nature of this Practice Advisory: Internal auditors should consider the following guidance when establishing or evaluating the reporting lines and relationships with organizational officials to whom the CAE reports. This guidance is not intended to represent all the considerations that may be necessary during such an evaluation, but simply a recommended set of items that should be considered.

1. The IIA's *International Standards for the Professional Practice of Internal Auditing (Standards)* require that the chief audit executive (CAE) report to a level within the organization that allows the internal audit activity to fulfill its responsibilities. The IIA believes strongly that to achieve necessary independence, the CAE should report functionally to the audit committee or its equivalent. For administrative purposes, in most circumstances, the CAE should report directly to the chief executive officer of the organization. The following descriptions of what The IIA considers "functional reporting" and "administrative reporting" are provided to help focus the discussion in this Practice Advisory.
 - **Functional Reporting** — The functional reporting line for the internal audit function is the ultimate source of its independence and authority. As such, The IIA recommends that the CAE report functionally to the audit committee, board of directors, or other appropriate governing authority. In this context, report functionally means that the governing authority would:
 - Approve the overall charter of the internal audit function.
 - Approve the internal audit risk assessment and related audit plan.
 - Receive communications from the CAE on the results of the internal audit activities or other matters that the CAE determines are necessary, including private meetings with the CAE without management present.
 - Approve all decisions regarding the appointment or removal of the CAE.
 - Approve the annual compensation and salary adjustment of the CAE.
 - Make appropriate inquiries of management and the CAE to determine whether there are scope or budgetary limitations that impede the ability of the internal audit function to execute its responsibilities.

- Administrative Reporting — Administrative reporting is the reporting relationship within the organization’s management structure that facilitates the day-to-day operations of the internal audit function. Administrative reporting typically includes:
 - Budgeting and management accounting.
 - Human resource administration, including personnel evaluations and compensation.
 - Internal communications and information flows.
 - Administration of the organization’s internal policies and procedures.
2. This advisory focuses on considerations in establishing or evaluating CAE reporting lines. Appropriate reporting lines are critical to achieve the independence, objectivity, and organizational stature for an internal audit function necessary to effectively fulfill its obligations. CAE reporting lines are also critical to ensuring the appropriate flow of information and access to key executives and managers that are the foundations of risk assessment and reporting of results of audit activities. Conversely, any reporting relationship that impedes the independence and effective operations of the internal audit function should be viewed by the CAE as a serious scope limitation, which should be brought to the attention of the audit committee or its equivalent.
 3. This advisory also recognizes that CAE reporting lines are impacted by the nature of the organization (public or private as well as relative size); common practices of each country; growing complexity of organizations (joint ventures, multinational corporations with subsidiaries); and the trend toward internal audit groups providing value-added services with increased collaboration on priorities and scope with their clients. Accordingly, while The IIA believes that there is an ideal reporting structure with functional reporting to the audit committee and administrative reporting to the CEO, other relationships can be effective if there are clear distinctions between the functional and administrative reporting lines and appropriate activities are in each line to ensure that the independence and scope of activities are maintained. Internal auditors are expected to use professional judgment to determine the extent to which the guidance provided in this advisory should be applied in each given situation.
 4. The *Standards* stress the importance of the CAE reporting to an individual with sufficient authority to promote independence and to ensure broad audit coverage. The *Standards* are purposely somewhat generic about reporting relationships, however, because they are designed to be applicable at all organizations regardless of size or any other factors. Factors that make “one size fits all” unattainable include organization size and type of organization (private, governmental, corporate). Accordingly, the CAE should consider the following attributes in evaluating the appropriateness of the administrative reporting line.
 - Does the individual have sufficient authority and stature to ensure the effectiveness of the function?
 - Does the individual have an appropriate control and governance mind-set to assist the CAE in their role?
 - Does the individual have the time and interest to actively support the CAE on audit issues?
 - Does the individual understand the functional reporting relationship and support it?
 5. The CAE should also ensure that appropriate independence is maintained if the individual responsible for the administrative reporting line is also responsible for other activities in the organization, which are subject to internal audit. For example, some CAEs report administratively to the chief financial officer, who is also responsible for the organization’s

accounting functions. The internal audit function should be free to audit and report on any activity that also reports to its administrative head if it deems that coverage appropriate for its audit plan. Any limitation in scope or reporting of results of these activities should be brought to the attention of the audit committee.

6. Under the recent move to a stricter legislative and regulatory climate regarding financial reporting around the globe, the CAE's reporting lines should be appropriate to enable the internal audit activity to meet any increased needs of the audit committee or other significant stakeholders. Increasingly, the CAE is being asked to take a more significant role in the organization's governance and risk management activities. The reporting lines of the CAE should facilitate the ability of the internal audit activity to meet these expectations.
7. Regardless of which reporting relationship the organization chooses, several key actions can help assure that the reporting lines support and enable the effectiveness and independence of the internal auditing activity.
 - Functional Reporting:
 - The functional reporting line should go directly to the audit committee or its equivalent to ensure the appropriate level of independence and communication.
 - The CAE should meet privately with the audit committee or its equivalent, without management present, to reinforce the independence and nature of this reporting relationship.
 - The audit committee should have the final authority to review and approve the annual audit plan and all major changes to the plan.
 - At all times, the CAE should have open and direct access to the chair of the audit committee and its members; or the chair of the board or full board if appropriate.
 - At least once a year, the audit committee should review the performance of the CAE and approve the annual compensation and salary adjustment.
 - The charter for the internal audit function should clearly articulate both the functional and administrative reporting lines for the function as well as the principle activities directed up each line.
 - Administrative Reporting:
 - The administrative reporting line of the CAE should be to the CEO or another executive with sufficient authority to afford it appropriate support to accomplish its day-to-day activities. This support should include positioning the function and the CAE in the organization's structure in a manner that affords appropriate stature for the function within the organization. Reporting too low in an organization can negatively impact the stature and effectiveness of the internal audit function.
 - The administrative reporting line should not have ultimate authority over the scope or reporting of results of the internal audit activity.
 - The administrative reporting line should facilitate open and direct communications with executive and line management. The CAE should be able to communicate directly with any level of management, including the CEO.
 - The administrative reporting line should enable adequate communications and information flow such that the CAE and the internal audit function have an adequate and timely flow of information concerning the activities, plans, and business initiatives of the organization.
 - Budgetary controls and considerations imposed by the administrative reporting line should not impede the ability of the internal audit function to accomplish its mission.

8. CAEs should also consider their relationships with other control and monitoring functions (risk management, compliance, security, legal, ethics, environmental, external audit) and facilitate the reporting of material risk and control issues to the audit committee.

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