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partnership mandate
**A New Era in
Internal Audit**

Wee Hock Kee
President of IIAM

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THE GOVERNANCE PARTNERSHIP MANDATE

A New Era in Internal Audit

By Anuja Ravendran

In the past, internal auditors were always seen as the policemen guarding an organisation. Trends and developments within the profession today dictate that there is a need for the profession to transcend its traditional scope and move towards greater heights. Winds of change are already propelling the internal auditor towards assuming the strategic role of corporate governance partner within an organisation. Editorial Board Chairman, Raymond Liew spoke to Wee Hock Kee, president of the Institute of Internal Auditors Malaysia (IIAM) to gain a deeper insight into this shift in function.

Shifting roles

In the wake of corporate scandals such as Enron, Worldcom and Parmalat, the role of the internal auditor has significantly expanded from its traditional function of control checker to take on the newly emerged one of governance partner, offers Wee.

Last year during an Audit Director's Roundtable (a fraternity comprising well-known chief audit executives of multinational companies) meeting in the UK, the audit professionals met and defined the direction of internal audit for the next 10 years.

"They have come up with a vision that the profession needs to move towards the 'North East' direction where internal auditors are expected to provide governance partnership, moving away from the traditional role where they were expected to perform financial compliance," Wee explains.

This mandate, Wee says clearly points out that internal auditors are expected to support the board in discharging the governance responsibility.

In fact, even the Institute of Internal Auditors Malaysia, (IIAM) has been emphasising very strongly, throughout the last 24 months

that for internal auditors to effectively discharge their responsibilities, they need to work very closely with the other governance partners in the organisation.

The Four Cornerstones of Corporate Governance

Good corporate governance, says Wee, can be achieved with the coming together of the 'Four Cornerstones of Corporate Governance'. These cornerstones Wee explains, essentially refer to the partners within the governance process of an organisation.

It is based on a foundation that includes not only competent and ethical management but also a diligent board of directors/ audit committee, an independent external auditor and an effective internal audit function.

He further elaborates that the first cornerstone comprises the board, which provides leadership in governance through

the audit committee. The second cornerstone comprises the line function, headed by the CEO and his senior management team. They are expected to discharge governance and provide assurance back to the board in the form of proper internal control structures and sound risk management processes. Coming in third, are the external auditors who play a crucial role in understanding the governance structure within the organisation. The last cornerstone, is the internal auditor who is expected to work very closely with the three other governance partners to understand where the business control risk is within the organisation.

Wee believes that all partners play an equally crucial role in upholding good governance and should one cornerstone fail, the others would find it extremely difficult to cope.

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Establishing a good internal control structure

Internal auditors today must be at the forefront, working very closely with line managers and across the organisation, to establish a sound internal control structure. There are three levels of responsibility involved in achieving this.

“Level 1 comprises the business unit that builds up and establishes the internal control and risk framework within the organisation while Level 2 includes the oversight managers (the CEO and senior management) who are expected to perform close monitoring on the governance structure within the business unit.



Level 3 meanwhile encompasses the internal and external auditors who provide independent assurance to the organisation.”

While on one hand, internal audit provides the Level 3 support to the Audit Committee (and then back to the board), on the other hand it has to strike a very fine balance in working very closely with the line team in discharging governance. “This, in my opinion is the most challenging part of the internal auditor’s role,” Wee says.

Some internal audit departments take the stand that they do not want to be involved in Level 1 and Level 2 work as they say that it would impair independence but from Wee’s perspective and from his experience in the profession, it is equally important to support line functions to discharge governance.

“We have to be there to support them in establishing an effective internal control framework because no one else is better poised than us to do this. Internal auditors

have the cross functional and business experience that enables them to understand where the business risks of the organisations are and from that perspective they are able to jointly (with manage-

It should focus on providing that assurance and strategic risks are strategically managed. “For internal audit to do that, there must be good understanding of business. There is no way that they can extricate themselves from management in understanding where the strategic risks of organisations are.”

Internal audit must realign priorities to reflect merging needs of the audit committee and board as well as respond towards all the needs of stakeholders — proactively and consistently — without creating an environment of imbalance by saying that we only report to the Audit Committee, he states.

Internal audit must also have a strong link to the CEO and the board to elevate its authority and visibility — increasingly

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Discharging the governance partnership mandate effectively

There is increasing expectation that internal audit performs in a broader capacity and at world class standards. This is fuelled by three key pressures namely regulation, an evolving environment and corporate cost/value initiatives, Wee says.

“As such, it is imperative that a roadmap be established to discharge the new governance partnership mandate in an effective manner.”

reporting to the Audit Committee but not losing touch with the line functions so as to understand organisational risks better. Finally, internal audit must build a continuous improvement process to bolster the quality and productivity of the function through an effective Human Capital Management Strategy.

Human Capital Issues

However, with this shift towards becoming a governance partner, Wee voices his concern about the emerging trend of outsourcing and co-sourcing of internal au-

dit functions.

"The new set of regulations on governance have given rise to speculation that in order to have a good internal audit function within an organisation, more costs would be involved. In order to manage these costs these organisations may resort to outsourcing or co-sourcing internal audit."

While we are not against these concepts, there is much concern that there may be an influx of practitioners especially external auditors moving into this area of service. However, it must be noted that those offering these services must be well-qualified individuals.

"It is not all that simple to become an internal auditor. Having been an external auditor does not necessarily pave the way for an easy conversion process to becoming an internal auditor. It is a different ball game, firstly because of the different sets of skills required. While it is good to have a first degree in finance, (although it is not necessary), it may be better in terms of facilitating the understanding of financial governance. It also requires strong influencing, relationship, communication and also behavioural management skills." It is also highly encouraged for aspiring internal auditors to possess specialised skills like forensic accounting," Wee advises.

In addition, he says that certification is important. "As we continue to strive towards excellence, we continue to offer the Certified Internal Auditor (CIA) exam which is a post graduate qualification," he says adding that IIAM is now moving ag-



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gressively to promote the CIA qualification.

"Ultimately, we would like to see CIA as the license to operate for internal auditors," Wee says. At present there are over 300 CIAs in Malaysia. By 2010, the Institute hopes to have 1,500 CIAs to support the governance initiative in Malaysia.

Also, seeing as how governance is becoming one of the core functions of the internal auditor in this day and age, having high levels of integrity and ethics is also a key requirement. Towards this end, he says that members of IIAM are governed by the IIA International Code of Conduct, which requires them to practice the highest ethical standards.



Wee responds to a question from Editorial Board Chairman, Raymond Liew

Good governance for improved business

He acquiesces that the evolution of the role of the internal auditor to become a governance partner will not happen overnight, and neither is it an internal audit agenda alone.

"It is a joint effort between all four cornerstones, an area that we are continuously working on in terms of promoting good governance and I believe that internal audit has the ability to influence management by bringing in good practices, adopting some of the best practices.

We want to share this message of good governance with other public-listed companies. I believe that adopting best practices in this area will eventually give organisations good returns in business in terms of performance which will positively influence share prices," emphasises Wee.

Re-imagining Internal Audit

Within Malaysia, we are working very hard to re-image the internal audit profession. One of the ways of doing this is via the Best Internal Audit Practice Award (BIAPA), an annual event held in collaboration with the Malaysian Institute of Accountants (MIA).

These awards, it is hoped, will help spur local companies to strive for excellence in the area of internal audit. "The BIAPA is definitely the first move towards elevating internal audit standards in this country," he says.

"We received good response from corporate Malaysia during the inaugural awards held last year, but we believe more can be done. We want to bring this awareness to a wider group of people in the corporate field such as Audit Committee Chairmen, board members, CEOs and finance directors in Malaysia," he explains.

Also, this year there is a new award category for "Upcoming Best Internal Audit Practice Award, to spur smaller companies such as those listed on the Second Board of Bursa Malaysia Securities Berhad and on the MESDAQ to excel in the area of internal audit, Wee told *Accountants Today* during an interview in his office last month. **AT**