

# [The role of internal audit in meeting board accounting essay](https://assignbuster.com/the-role-of-internal-audit-in-meeting-board-accounting-essay/)

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This part of the report mainly focuses on the positive aspect of how audit committees of Silver Bird Group Berhad (SBGB) help to enhance the role of internal audit in meeting board of directors’ needs. With the increasing attention focused on the financial reporting by legislators, security analysts, institutional investors and regulators, the roles of audit committees have been stressed on their importance and responsibility by increasing the requirements in terms of audit committee membership and composition. The Malaysian Code of Corporate Governance (MCCG) best practice states that an audit committee should be comprising at least three members, a majority of whom are independent and all members of the audit committee should be non-executive directors. SBGB’s board of directors had fulfilled the stated requirement while forming the audit committee for the organization. The advantages of non-executive directors on the committee will allow the audit committee to obtain honest feedback on the performance of financial management easily. This is because the presence of executive directors may prevent the discussion of sensitive issues. Likewise, the non-executive directors may be able to see larger picture better for effective decision making as they are less likely to be informed in details. The Institute of Internal Auditors (IIA) states that the internal auditors are to perform their work with integrity, objectivity, confidentiality, professional competency and due care, and also professional behaviour at all times. Thus, the audit committee must ensure that the internal auditors perform their work in examining and evaluating the adequacy, efficiency and effectiveness of the organization’s internal control. Nevertheless, the audit committees have the authority to review and approve the internal audit plan, internal audit reports and ensure appropriate actions are taken by the Board of Directors on the recommendation of the internal auditors. Through this, the internal auditors was able to increase their accountability as their performance will be under greater scrutiny. Nevertheless, the advantage of having audit committee is that they are able to assess the suitability and independence of external auditors through various implementations of governing policies and procedures. This is because the independence of external auditors can be impaired by the provision of non-audit services to the company and threats to compliance with the fundamental principle. Thus, audit committee are there to establish policies governing the circumstances under which contracts for the provision of non-audit services can be entered into and procedures that must be followed by the external auditors in order to safeguard against the threat to compliance with the fundamental principle. Audit committees must review the external auditors’ reports and their audit findings to ensure more cost efficient and effective external audit will result, as this will benefit both the company and the auditor. Besides that, the Malaysian Code of Corporate Governance (MCCG) also states that the audit committee should works with the board of directors to establish a sound framework to determine the company’s level of risk tolerance and actively identify, assess and monitor key business risks to safeguard shareholders’ investments and the company’s assets. This is because internal controls are important for risk management and the board of directors should work with audit committee to formulate, implement and review the company’s internal controls system. An effective audit committee is able to ensure a company’s financial statement to be a reliable source of financial information through the compliance of applicable financial reporting standards, as this is integral to the reliability of financial statements. An audit committee has the right to full and unrestricted access to any information pertaining to the organization. As per the year 2011’s annual report, the audit committee of SBGB had frequently reviewed the unaudited quarterly report on the consolidated results for the each quarter ended. Through this, an effective audit comittee is able to help to create a climate of discipline and control which will reduce the opportunity for fraud. Thus, the objectivity and credibility of financial reporting will be strengthened. All in all, the purpose of audit committees is to act as a support and guidance that can help in focus on internal audit’s role. Therefore, by working closely with audit committee, the board of directors and internal auditors are able to develop and build mutual understanding and agreement with each other to help internal auditors to perform value added services and responsibilities that would help in identifying and managing the enterprise current and evolving risks.

## Negative Aspect of how Audit Committee can enhance the role of internal audit in meeting board of directors’ needs.

This part of the report mainly focuses on the negative aspect that the audit committee of Silver Bird Group Berhad (SBGB) failed to meet board of directors’ needs. In the case of SBGB, it was revealed that there was a lack of independence within the audit committee. The external auditors from Crowe Horwath, had refused to express an opinion on the financial statements because they were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. External auditor in the financial report had stated that, " During the course of our audit for Financial Year ended 2011, we expressed concerns to the audit committee and the board of directors over the validity and recording of certain transactions for which we were not able to obtain the sufficient and appropriate audit evidence and satisfactory explanations from management," It was not the responsible for external auditors to detect fraud as their role is to provide reasonable assurance that the financial statements are free from material misstatement, and to form an opinion on the financial statements whether they are of true and fair view. (External Auditor Role)As accordance to MCCG and IIA, audit committee must ensure that the internal auditors perform their work in examining and evaluating the adequacy, efficiency and effectiveness of the organization’s internal control and to review whether there are compliance of rules and regulations. However, stated in the financial report for year ended 2011; the internal audits conducted did not reveal weaknesses which would result in material losses, contingencies or uncertainties that would require disclosure in the annual report. Thus this indicated that the internal auditors had failed to detect the weakness of the internal control of the organization. In the case of SBGB, it was found that there were no proper internal controls to enforce the management team to have proper records kept under the requirements of the Companies Act 1965, thus making the financial records unreliable. Evidence found in the The Star News stated that there were no evidences or details recorded for the payments made amounting to RM7. 6mil for the refurbishment of an existing warehouse and factory as well as information to verify additions of plant and equipment amounting to RM4. 9mil. Nevertheless, the revenues and cost of sales amounting to RM31. 9mil and RM31. 3mil from the sweetened creamer business were also not able to be verified. Besides that, the external auditors also stated that they were not able to verify the sales transactions with six customers from the bakery businesses and telecommunication businesses amounting to RM149mil. (Internal Control problem)Also stated in Silver Bird Group Berhad’s financial report for the financial year ended 31 October 2011, there might be bad debts and additional allowance that needed to be made for impairment losses on receivables. This in fact revealed that the audit committee failed to perform their duties to work with the board of directors in establishing a sound framework to determine the company’s level of risk tolerance and actively identify, assess and monitor key business risks to safeguard shareholders’ investments and the company’s assets. Nevertheless the lack of proper internal control in the organization had lead to several circumstances that may render the values attributed to the organization’s current assets in the financial statement to be misleading as stated in the financial report. (Internal Control problem)The lack of independence in the audit committee had result in the failure to detect and to be alert of the frequent cash calls issued via private placements of shares, bonds or commercial papers and rights issues for working capital purposes over the years since SBGB’s listing in June 2002. Besides that, institutional investors such as Berjaya Group and Lembaga Tabung Haji which had 20. 6% and 22. 2% respective control over the company had failed to install Non-Executive Director in the audit committee to review the risk and internal control in the firm. The audit committee had also failed to use their voting rights to remove CEO Datuk Jackson for his regular demand of cash calls when the business is not expanding. Nevertheless, these threats had raised the awareness of the regulators to question the company, as these matters had cast a significant doubt on the financial performance and position of the company. (Audit Committee problem)All in all, the negative aspect of having poor corporate governance on both the board of directors and the audit committee may create many uncertainties which now surrounding the Silver Bird Group Berhad. Thus, an organization should maintain and uphold good corporate governance in order to strengthen the roles and responsibilities of the board of directors, audit committee and the internal audit function. Pending Data (Ignore)The suspension of three company officials consisting of the group managing director Datuk Jackson Tan, executive director Ching Siew Cheong and general manager for accounts & finance Lai Poh Mei from 24 February 2012 to make an internal inquiry would hopefully start to remove any doubt on this case. (pending)Furthermore, the director of internal auditing should have direct communication with the audit committee in order to help in assure the independence. Hence, the director of internal auditing should attend audit committee meetings and meet privately with the audit committee at least annually. (pending) Based on the annual report 2011 of Silver Bird Group Berhad, there was had 5 meetings held within 2011 and the internal auditors was invited by the audit committee of Silver Bird Group Berhad to those meetings. The frequency meetings of Silver Bird Group Berhad can bring the positive aspect of high level in detect the materiality risk, detect major fraud or irregularities as well as come out with immediate remedy action. It will assist in establishing and strengthening the independence and objectivity of the directors and the internal and external auditors. There will be improved communication and increased contact, understanding and confidence between directors, management and the internal and external auditors. (meeting) (pending) (might be positive if restructure)This would be the second time that the company stole the limelight, both for the wrong reasons. In September 2006, its High 5 bakery in Nilai, Negri Sembilan was shut down for two weeks and its halal certification was withdrawn following a raid by the authorities. The authorities had alleged that the bakery was unhygienic, employed illegal workers and used cooking oil without a halal certification. (pending, internal control)