

## Report No. 08/2011 – 2nd Chamber

### “The internal audit function in the State Owned Enterprises”

This report deals with the findings of a performance audit entitled "The internal audit function within the State Owned Enterprises" for the year 2008 and covering 20 of such entities.

Sixteen of the respondents answered that their structure comprised an Internal Audit (IA) organic unit, while others expressed their intention to create one. However, only five companies knew about the full breadth of the Internal Audit concept and applied it, since the remaining limited their activity to simple monitoring internal control, neglecting aspects such as evaluation of the processes of risk management and governance.

It was found that in about half of the entities of the sample, the Internal Audit organic unit directly reported to the Board, thereby ensuring the independence of unrestricted access. However, because some of these Boards did not integrate non-executive members, the independence of those units may have been jeopardized.

The existing 199 internal auditors in the 16 companies with Internal Audit organic units represented an average of 12.4 internal auditors per organic unit. On the other hand, the auditor to employees ratio stood at 2.2 ‰, a value within the range of results found in surveys conducted by IPAI in Portugal (from 2.1 ‰ and 3.2 ‰ on average) and the average annual hourly each devoted to its internal auditor training was 45 hours, which fits within the benchmark set by the institutions of reference, which is 80 hours every two years.

These internal auditors were, in general (87%), hired internally. It turns out that 29 (15%) of those internal auditors had previously worked in management positions, and this is a situation that enhances the risks to the independence of the operations of Internal Audit organic units.

Of the 16 companies that had Internal Audit activity, 5 did not define indicators for measuring the performance of the respective unit, which did not allow for its quantification and qualification. In addition, as a rule, its activity was not subject to an independent external evaluation.

The cost of the Internal Audit function of the companies surveyed rose, in 2008, to 15.9 million euros. The average annual cost of each Internal Audit department was about 933.100 euros and an internal auditor 79.700 Euro / year, equivalent to 5.700 Euro / month.

Taking into account the results obtained, the Court of Auditors recommends:

#### **The State** as stakeholder / shareholder:

To enact and publicize, namely on the Internet, a script / letter of good practices to guide the entities on the SOE Internal Audit in order to enhance the role and contribution of IA systems in risk assessment and governance.

To encourage companies to change the paradigm of the Internal Audit function and integrate activity in the process of corporate governance, to strengthen the structure of internal control and risk management.

#### **Companies' Boards:**

To revive the Internal Audit function, giving it a greater responsibility of intervention in order to provide skills to enable them to play a role in evaluating the effectiveness of risk management, control and governance.

To comply with recommendations by The Institute of Internal Auditors, with regard to planning, human resources, skills, certification, training and evaluation of Internal Audit.

To ensure the independence, objectivity and technical competence of human resources of Internal Audit organic units, by increasing recognized certifications in the area and limiting the use of former managers to integrate the Internal Audit organic units, after their term/mandate comes to an end.

To establish a document measuring the performance of the Internal Audit organic unit in order to facilitate objectivity and transparency in the evaluation of internal auditors and its audit output. They should also be subject to external evaluation.