

Interaction Between Audit Committee and Internal Audit: Evidence from Tunisia

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The role of the audit committee and internal audit in corporate governance has grown in recent years. In this context, the audit literature and practice have underlined the increasingly important role of support and interaction between audit committee and internal audit with the aim to improve the corporate governance quality. The purpose of this paper is to examine the relationship between the audit committee and the internal audit as well as the impact of audit committee characteristics on this relationship in the Tunisian context. Data was collected by means of a questionnaire addressed to the chief internal auditors of 50 Tunisian firms. The regression results suggest that expertise and frequency of meetings of audit committee have a positive impact on audit committee interaction with internal audit, while the size of the audit committee affects negatively this interaction. However, audit committee independence has no effect on audit committee relation with internal audit.

Introduction

Recent corporate collapses in the United States as well as Europe have highlighted the role of corporate governance mechanisms and specifically that of audit committee and internal audit in restoring investor confidence in the capital markets.

In fact, audit committee is a key institution in the context of corporate governance which helps the board of directors in fulfilling their financial and fiduciary responsibilities to shareholders (Puri *et al.*, 2010). It is responsible for monitoring the company's financial statements and supporting the accounting department in the company. The audit committee should also evaluate the effectiveness of the internal control and monitor the internal and external audit. In its turn, the internal audit plays a major part in the corporate governance mosaic. Its main objective is to ensure that all business operations are controlled and that the company is managed effectively and transparently. Attached to Senior Management, the internal audit is in a good position to evaluate the effectiveness of risk management and internal control systems (Soh and Bennie, 2011).

Due to the increasing importance of internal audit and audit committees in ensuring corporate governance efficiency, this paper examines the relationship between audit committee

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and internal auditors as well as the impact of audit committee characteristics on this relationship in the Tunisian context.

Many corporate governance committees and regulators (Treadway Commission, 1987; Blue Ribbon Committee (BRC), 1999; Securities and Exchange Commission (SEC), 1999a; and Sarbanes-Oxley Act (SOX), 2002) point to a symbiotic relationship and interaction between audit committees and internal auditors to prevent internal control failure and ensure the integrity and quality of financial reporting.

Moreover, previous studies examining the relationship between audit committees and internal audit in Canada (Scarbrough *et al.*, 1998), Singapore (Goodwin and Yeo, 2001), the US (Raghunandan *et al.*, 2001), Australia and New Zealand (Goodwin, 2003) found that committees' interaction with internal auditing is affected by the composition of the audit committee such as the independence of committee members and their expertise in accounting or finance. Previous studies have concentrated solely on the independence of the audit committee (Scarbrough *et al.*, 1998; and Goodwin and Yeo, 2001), the separate influence of independence and accounting or finance experience (Goodwin, 2003) or the combined independence and experience of the committee (Raghunandan *et al.*, 2001). This paper extends prior studies in two ways. First, it examines the separate effect of all audit committee characteristics such as independence, financial experience, frequency of meetings and the size of audit committee on audit committee relations with internal audit. Moreover, the paper examines audit committee relations with internal audit in Tunisian companies. The paper is structured as follows: it provides a literature review on the relationship between audit committee and internal audit, followed by a description of hypotheses development. Subsequently, it outlines the data and methodology used in the study, followed by the discussion of the results. Finally, it offers conclusion.

Literature Review

The concept of audit committees is not a new issue. Audit committees were introduced in the US market even before 1978 (Spira, 2003). Their adoption was required by the New York Stock Exchange (NYSE) in the Treadway Report in 1987. It was also recommended by the Cadbury Committee (1992) in the UK to enhance public confidence after the crisis of 1980 (Hrichi, 2009). In 2002, the Sarbanes Oxley Act made the audit committee a body fully mandatory for all listed companies.

Regulators around the world have considered the audit committee as a critical element in corporate governance by virtue of its role in protecting the interests of the stakeholders by monitoring the actions of managers in terms of financial reporting, internal control and risk management (Chtourou and Ben, 2006). Moreover, the committee is regarded as a liaison between the Board of Directors and the internal and external auditors, which allows it to reduce the information asymmetry that exists between them.

The efforts of the Tunisian accounting and legal authorities to strengthen the role of the audit committees are expressed in the promulgation of Law No. 2005-96 of October 18, 2005

on strengthening financial relations securities. According to this law, the permanent audit committee is composed of at least three members designated as appropriate by the Board of Directors or the Supervisory Board from among their members, and it is prohibited for the Chief Executive or the Chief Executive Officer to be a member of the committee.

The audit committee is responsible for several issues relating to the audit and in particular the relationship of the organization with its auditors. As part of its responsibilities, it reviews the internal control procedures and the risk management system. These areas fall under the remit of the internal audit function, which means that an effective working relationship between the two parts is a key to sound corporate governance (Davies, 2009).

Goodwin and Yeo (2001) argue that working relationship between the audit committee and the internal audit is beneficial for both parties. According to McHugh and Raghunandan (1994), Institute of Internal Auditors (IIA), (2003), Turley and Zaman (2004), and Gramling and Hermanson (2006), the audit committees often rely upon the internal audit, considered as an important resource for the audit committees to fulfill their responsibilities and perform their corporate governance duties effectively. In return, the audit committee is responsible for assessing the independence and the work performance of the internal audit (Schneider, 2010) and improving its status.

The US regulators have emphasized the importance of a strong working relationship between audit committee and the internal audit. According to the Sarbanes Oxley Act, "audit committees must make informed choices about the quality of work it receives from the auditors" (Rittenberg *et al.*, 2008). Similarly, the BRC (1999) outlines the importance of good relationship between the audit committee and internal audit in preventing misstatements in financial reporting.

In order to better understand the relationship between the audit committee and internal audit, we explain the role of internal audit in support of the audit committee, the audit committee's role in strengthening the internal audit, and the interaction between the audit committee and internal audit.

Role of the Audit Committee in Monitoring and Controlling the Internal Audit Function

Audit committees have a crucial role to play in providing oversight to the internal audit function. They should evaluate the effectiveness of the internal audit function (Schneider, 2010) by assessing the internal audit's organizational structure and ensuring that the function has sufficient staff to fulfill its mission (Bailey, 2007).

Moreover, an effective audit committee must improve and protect the independence of the internal audit (Marx, 2008) by approving the appointment, dismissal and remuneration of the chief internal auditor (Sarens and De Beelde, 2006). In addition, audit committee members are in charge of monitoring the work performance of the internal audit. They should review and approve internal audit reports such as internal audit charter, internal audit plan and programs, internal audit budget, and evaluate the internal audit results. Audit

committee is also asked to examine the cooperation between internal and external audit (Marx and Voogt, 2010).

The effort of audit committee members in supporting the internal audit function is emphasized by the National Association of Corporate Directors (NACD) (1999) which states that:

The audit committee can look into today's internal auditing function to provide independent, objective assurance and consulting activities designed to add value and improve the organization's operations.

Role of Internal Auditors in Supporting and Assisting the Audit Committee

A strong internal audit can increase the effectiveness of the audit committee in carrying out its tasks (Turner, 1999; and Bishop *et al.*, 2000). It is considered as an important resource that can assist audit committee in the evaluation of risks and frauds and provide important information about accounting and financial issues (Hermanson and Rittenberg, 2003).

Moreover, internal audit can provide comfort to audit committees, specifically, with respect to internal control and risk management system (Gendron *et al.*, 2004; Gendron and Bédard, 2006; and Sarens *et al.*, 2009). Indeed, audit committees feel uncomfortable about internal control in high-risk areas and risk management system because of the evolution in the company's risk management and internal control approach. Internal auditors, due to their specific knowledge and expertise in internal controls and their privileged position within the organization, can help audit committees to understand how internal auditors evaluate the system of internal control and the effectiveness of internal controls of the company (Rezaee and Zabihollah, 1993). Furthermore, the internal audit's role in formalizing the risk management system can also be a crucial source of comfort for the audit committee.

In addition, the internal audit function is seen as a mechanism that reduces the principal agency problems between the audit committee and the operational people in the organization, including management (Scarborough *et al.*, 1998; and Raghunandan *et al.*, 2001). In fact, the audit committee (principal) often lacks information about the status of specific questions of the organization, such as risk management and internal control, which are the responsibilities of operational people (agent) which may lead to uncertainty in their ability to fulfill their own supervisory role (Sarens *et al.*, 2009). Therefore, the internal audit, considered as a valuable resource that provides the information needed for audit committees, can reduce the problems of asymmetric information between the members of the audit committee and operational people within the organization (Bishop *et al.*, 2000).

Extent of Interaction Between the Audit Committee and Internal Audit

In order to ensure good corporate governance, audit committees should cooperate and interact with internal auditors (Scarborough *et al.*, 1998; Bishop *et al.*, 2000; and IIA, 2002). This interaction is, however, a broad concept and includes a variety of activities. Previous studies (Scarborough *et al.*, 1998; Raghunandan *et al.*, 2001; Goodwin, 2003; and Zain *et al.*, 2006) focused on three main aspects: (1) frequency of meetings between the audit committee and the

Chief Internal Auditor (CIA); (2) audit committee involvement in the dismissal of the CIA; and (3) review of internal audit work.

Frequency of Audit Committee Meetings with the Chief Internal Auditor

The audit committee has to have effective communication with internal audit by having frequent meetings with the CIA to discuss and review specific issues on a timely basis (Scarborough *et al.*, 1998; and Raghunandan *et al.*, 2001). Regular meetings between audit committee and internal auditing help the audit committee to remain informed and knowledgeable about relevant issues regarding accounting, finance and auditing, thus enabling it to assist the internal auditors to resolve any problems identified. More frequent meetings also provide opportunities to undertake in-depth discussions on ways to improve an organization's financial reporting system (Zain *et al.*, 2006). From a regulatory perspective, the Treadway Commission (1987), the BRC (1999) and the IIA (2002) suggest that open lines of communication must be kept between internal audit and the audit committee to achieve maximum benefit for the organization. In addition, Bailey (2007) argues that the meetings between the audit committee and the CIA, without the presence of management, can help to improve communication between the two groups. Similarly, Braiotta (2000) points out that private meeting between the audit committee and the audit manager would improve and protect the independence of internal auditors as the auditor may provide more complete information to the audit committee because it is free from any influence of the directors. In this regard, the IIA issued a recommendation in 2002 to NYSE to demand audit committees to meet with the director of audit without the presence of management with a view to discussing sensitive issues.

Audit Committee Involvement in the Dismissal of the Chief Internal Auditor

The audit committee can interact with internal audit function through its involvement in the decision of dismissing the CIA which allows strengthening the authority and accountability of the internal audit function (Zain *et al.*, 2006) and reinforcing its independence (Scarborough *et al.*, 1998). Such involvement prevents the revocation of the CIA for raising sensitive issues related to management (Scarborough *et al.*, 1998) and encourages internal auditors to be more efficient and to communicate their findings honestly and objectively.

Audit Committee Review of the Internal Audit Work

The audit committee is required to ensure the effectiveness of the internal control system and internal audit program (BRC, 1999). To fulfill this responsibility effectively, audit committees are required to review the internal audit proposals related to programs and plans, internal audit budget, and internal auditors' coordination with external auditors. Further, the audit committee also has the responsibility of reviewing the internal audit results insofar as they relate to financial reporting, internal controls, and compliance with laws and regulations (Raghunandan *et al.*, 2001).

According to Zain *et al.* (2006), the greater is the extent of audit committee review of the internal audit programs and processes, the greater is the possibility of identifying weaknesses in the internal audit activities, and consequently of improving the internal monitoring function.

Bailey (2007) indicates that the best practices regarding audit committee review of internal audit work consist in reviewing the internal audit charter, plan, budget as well as the internal controls and the financial statements of the company.

Hypotheses Development

The specific objective of the study is to examine the association between audit committee characteristics and the committee's interaction with the internal audit function in the Tunisian firms. The hypotheses of the research focus mainly on four characteristics of audit committee: independence, financial expertise, frequency of meetings, and size of audit committee.

Audit Committee Independence

To fulfill its role of monitoring and protecting the interests of shareholders, the audit committee must be independent from the management. Independence has been defined as having "no relationship to the corporation that may interfere with the exercise of their independence from management and the corporation" (BRC, 1999). According to the SEC, independent audit committee members are more likely to "objectively evaluate the propriety of management's accounting, internal control and financial reporting advices" (SEC, 1999a). Increasing emphasis has been placed on the need for audit committees to be comprised solely of independent directors. In fact, the BRC and the Sarbanes-Oxley Act require all listed companies to have entirely independent audit committees (Bronson *et al.*, 2009). The Treadway Commission also recommends the US SEC to require all public companies to form an audit committee that consists solely of independent directors (Deli and Gillan, 2000).

Several empirical studies have explored the association between audit committee independence and interaction between audit committee and internal audit. Scarbrough *et al.* (1998) find in a sample of 72 Canadian manufacturing companies that committees comprising solely of non-employee directors are more likely to have greater interaction with internal audit than the committees comprising some executive directors. In fact, they show that they have more frequent meetings with the CIA; are more likely to provide private access to CIA and review the internal audit program and results of internal auditing. But they find no significant association between audit committee independence and committee involvement in decisions to dismiss the CIA. Likewise, the results of Goodwin and Yeo (2001) show that entirely independent audit committee meets more frequently with the CIA than those that are not totally independent. Based on responses from the CIA of 114 US manufacturing companies, Raghunandan *et al.* (2001) find that audit committees composed solely of independent directors and at least one member with accounting or financial expertise are more likely to have long and frequent meetings with the CIA, to provide private access to the internal audit manager, and to review proposals and results of internal audit. Further, Goodwin (2003) notes that fully independent audit committees are more involved in the dismissal of the CIA, and are more likely to meet privately the CIA than committees with non-independent members. However, the independence of the committee has no impact on the review of the audit committee of the internal audit work. Therefore, based on the preceding discussion, the following research hypothesis is proposed:

H₁: There is a positive relationship between the audit committee independence and audit committee interaction with internal audit function.

Audit Committee Financial Expertise

The effectiveness of the audit committee in fulfilling its mission depends significantly on the financial expertise of its members (SEC, 1999b). Indeed, financial expertise helps the committee to have a better understanding of the company's financial statements and audit risks and to communicate with internal and external auditors on internal control weaknesses and coverage of audit risks (Maines *et al.*, 2001). Financial expertise is defined by the Sarbanes-Oxley Act as having an understanding of Generally Accepted Accounting Principles (GAAP), financial statements, and audit committee functions (Robinson and Owens-Jackson, 2009).

The major stock exchanges in the US (NYSE and National Association of Securities Dealers Automated Quotations, NASDAQ) as well as the SEC recommend that at least one financial expert should be present in the audit committee.

Previous researches show that the expertise of the audit committee is associated with the quality of the internal control process. The studies (Krishnan, 2005; Zhang *et al.*, 2007; Goh, 2008; and Naiker and Sharma, 2009) show that the presence of financial experts in the audit committee positively affects the quality of internal control. Similarly, Krishnan and Visvanathan (2007) and Naiker and Sharma (2009) show that the presence of expertise of the audit committee is positively associated with the quality of financial reporting.

Regarding the relationship between audit committee and internal audit, Raghunandan *et al.* (2001) find a positive association between accounting or financial expertise of the audit committee and the frequency of meetings between the committee and the CIA, private meetings with the CIA, and the committee's review of proposals and results of internal audit. Goodwin (2003) also finds a positive association between presence of audit committee expertise and private access of CIA and the audit committee review of audit work internally. However, it did not find a significant association between the presence of expertise and the committee's involvement in the dismissal of the head of internal audit. Thus, the research hypothesis is proposed as follows:

H₂: There is a positive relationship between the audit committee financial expertise and audit committee interaction with internal audit function.

Frequency of Meetings of the Audit Committee

The frequency of meetings of the audit committee is considered as a dimension of committee activity (Bedard *et al.*, 2004) and a potential indicator of its effectiveness (Menon and Williams, 1994). It is often used as a proxy for the diligence of the audit committee or the persistence with which the members of the audit committee perform their tasks (Menon and Williams, 1994; and DeZoort *et al.*, 2002). It is widely suggested by the regulators to have frequent audit committee meetings. For example, the Cadbury Committee (1992) and KPMG (1999) propose to have three or four meetings per year. The BRC recommends at least four meetings of the audit committee annually. Similarly, the NACD (2000) suggests a basic rule of four meetings of the

audit committee annually. Several studies (Zhang *et al.*, 2007; Goh, 2008; and Naiker and Sharma, 2009) show that firms with internal control problems are more likely to have frequent meetings of their audit committees. In addition, McMullen and Raghunandan (1996) show that frequent meetings of the audit committee may reduce the problems of the financial statements, while Barua *et al.* (2010) report a positive association between the frequency of meetings of the audit committee and the internal audit budget. However, previous studies fail to address the impact of audit committee meeting frequency on the relationship between audit committee and internal audit. Thus, the following research hypothesis is proposed:

H₃: There is a positive relationship between the frequency of meetings of the audit committee and audit committee interaction with internal audit function.

Audit Committee Size

The number of audit committee directors could be used as an indication or an approximation of the amount of resources available for such a committee. Best practices suggest at least three members (Cadbury Committee, 1992; and BRC, 1999). However, the NACD (2000) recommends confining the size of the audit committee to six members. Kalbers and Fogarty (1993) state that firms with larger audit committees tend to reinforce the status and authority of the audit committee within the organization. However, Abott *et al.* (2002) report no association between the size of the audit committee and misstatements in financial reporting. On the other hand, Goh (2008) finds that companies with larger audit committee are less likely to revise the internal control deficiencies, while Barua *et al.* (2010) find no association between the size of the audit committee and the internal audit budget. Hence, the research hypothesis is proposed as follows:

H₄: There is a negative relationship between the size of the audit committee and audit committee interaction with internal audit function.

Data and Methodology

Sample Selection

Data was collected by means of a questionnaire (see Appendix) addressed to the chief internal auditors of the Tunisian companies that have audit committees including banks, insurance companies and financial institutions. Because of the nature of the research population, i.e., Tunisians, to ignore postal questionnaire most of the time, the survey was conducted through face-to-face interviews. Initially, 74 companies were contacted, of which only 50 responded, giving an overall response rate of 67%. In fact, 13 companies (17%) did not respond because they do not have an audit committee, while 10 companies (10%) refused to answer. Details of respondents and response rates are shown in Table 1.

Definition and Measurement of Variables

The dependent variable in this hypothesis-testing model is the interaction between the audit committee and the internal audit function noted as *INTER*. As mentioned earlier, several studies (Scarborough *et al.*, 1998; Raghunandan *et al.*, 2001; Goodwin, 2003; and Zain *et al.*, 2006) define this interaction in terms of frequency of audit committee meetings with the CIA, audit committee

Industry Classifications	Sample Frequency	Sample Percent
Automotive Industry	2	4
Airline	1	2
Construction	3	6
Industry (Gas, Chemistry, Pneumatic, etc.)	5	10
Financial Sector (Banks, Insurance, Leasing, etc.)	34	68
Services	4	8
Communication	1	2
Total	50	100

involvement in the dismissal of the CIA, and the involvement of the committee in the review of the internal audit work. In pursuance of these studies, the paper first focuses on these three aspects and then tests the impact of audit committee characteristics on each of these aspects measured as follows:

Frequency of Audit Committee Meetings with the Chief Internal Auditor

Previous studies underline the importance of private meetings between the audit committee and the CIA (without management being present) with a view to providing for open discussions on issues of concern that may reflect adversely on the management. Therefore, two variables are defined here: the first one relates to the total number of meetings between the audit committee and the CIA, and the second to the private meetings between the audit committee and the CIA.

Total Number of Meetings Between Audit Committee and the CIA: The meetings between audit committee and the CIA give some idea about the importance of audit committee relationship with the internal audit (Raghunandan *et al.*, 2001). Following Goodwin (2003) and Zain *et al.* (2006), the study uses a variable defined by the total number of meetings between the audit committee and the CIA per year and is noted as *FREQTOT*.

Private Meetings Between Audit Committee and the CIA: Referring to the study of Goodwin (2003), this variable is defined by the number of private meetings between the audit committee and the CIA per year and is noted as *FREQABS*.

Audit Committee Involvement in the Dismissal of the Chief Internal Auditor

Audit committee involvement in the dismissal of the CIA is measured by previous studies (Goodwin, 2003; Abbott *et al.*, 2003b; and Zain *et al.*, 2006) as a dummy variable that takes the value of 1 if the audit committee is involved in the dismissal of the CIA, or 0 otherwise. In this study, the same criterion is adopted. This variable is noted as *DISMISS*.

Audit Committee Involvement in the Review of the Internal Audit Work

The questionnaire includes six questions relating to the internal audit work. The first three questions relate to whether the audit committee reviews internal audit proposals relating to

programs/plans, budget and coordination of work with external auditors. The next three questions inquire whether the audit committee reviews the results of internal auditing relating to financial reporting, internal control and compliance with laws and regulations. Responses to these six questions were summed up to give a single variable ranging from 0 to 6, reflecting the amount of review work that the audit committee undertakes.

Regarding independent variables, they are the audit committee characteristics, and the measure of each of these variables is discussed in the following:

Audit Committee Independence

Following Raghunandan *et al.* (2001), Krishnan (2005), and Stewart and Kent (2006a and 2006b), independence of the audit committee (*ACIND*) is measured as the proportion of independent outside members in audit committee. Vienot (1995) states that outside director is a person who cannot be employed in the company or in a group company, or be a shareholder or trading partner (customer or supplier) or financial partner to the company. The study uses this definition, and the choice of this definition is justified by its simplicity and ease of application.

Audit Committee Financial Expertise

Bédard *et al.* (2004) define audit committee financial expertise as “having a professional certification in accounting or financial analysis or having experience in finance or accounting.” The authors exclude prior experience as a Chief Executive Officer in their definition and consider that the Chief Executive Officer position provides general financial literacy but not expertise. The same definition is adopted here because it is easy to understand by the survey respondents. Thus, following Abbott *et al.* (2003a) and Bédard *et al.* (2004), our variable *ACEXP* is measured as a dummy variable that equals 1 if at least one member of the audit committee has financial expertise and 0 otherwise.

Frequency of Meetings of Audit Committee

The frequency of meetings of audit committee is often measured as the number of audit committee meetings per year (Stewart and Kent, 2006a and 2006b; Zhang *et al.*, 2007; Goh, 2008; Sharma *et al.*, 2009; and Robinson and Owens-Jackson, 2009). In this study, the same criterion is used and the variable is noted as *ACMEET*.

Audit Committee Size

Following Raghunandan and Rama (2007), Goh (2008), Sharma *et al.* (2009), and Barua *et al.* (2010), the study measures the size of the audit committee (*ACSIZE*) as the number of directors in the audit committee.

Finally, the control variables relate to the firm sector, firm size and the size of the internal audit.

Firm Sector

Goodwin (2003) notes that the firm sector, in some ways, is linked to the relationship between the audit committee and internal audit, and more specifically with regard to the frequency of

meetings of the audit committee with the CIA. In fact, he finds that public sector companies have more frequent meetings between the audit committee and the CIA than the private sector. Based on the study of Goodwin (2003), the firm sector (*SECT*) is defined as a dichotomous variable, with a score of 1 for private sector entities and 0 for public sector entities. A negative impact of the sector on the relationship between the audit committee and internal audit is expected.

Firm Size

To measure this indicator, several studies (Abbott *et al.*, 2003b; Krishnan, 2005; Stewart and Kent, 2006a; Krishnan and Visvanathan, 2007; Zhang *et al.*, 2007; Bronson *et al.*, 2009; Sharma *et al.*, 2009; Abbott *et al.*, 2010; and Barua *et al.*, 2010) used the natural logarithm of total assets. Here the same measure is used, and the variable is denoted as *SIZE*.

Since the figures are approximate, we gave three scores: 1, if the log is between 0 and 5; 2, if it is between 5 and 10; and 3, if it is between 10 and 15.

Internal Audit Size

Zain *et al.* (2006) show that internal auditor's perception of their contribution in the financial statements audit is positively related to the internal audit size. According to this study, a measure based on the natural log of the total number of staff in the internal audit department divided by the natural log of total assets is used. This variable is noted as *IASIZE*.

Model Specification

A cross-sectional regression model is used to examine the impact of audit committee characteristics on the interaction between the audit committee and the internal audit. The following multivariate regression equation is estimated:

$$INTER = \alpha_0 + \alpha_1 ACIND + \alpha_2 ACEXP + \alpha_3 ACMEET + \alpha_4 ACSIZE + \alpha_5 SECT + \alpha_6 SIZE + \alpha_7 IASIZE + \varepsilon$$

where the corresponding variables are as explained earlier.

Results and Discussion

Descriptive Statistics

As shown in Table 2, the audit committee meets with the CIA, on average, 3.78 times per year. This result compares favorably with those of previous studies where the number of meetings was 3.03 for Canadian audit committees (Scarborough *et al.*, 1998), 3.3 for the US and Singapore committees (Goodwin and Yeo, 2001; and Raghunandan *et al.*, 2001), 4.53 times for Australia and New Zealand (Goodwin, 2003), and 4.35 for Malaysian entities (Zain *et al.*, 2006). The results of the private meetings between the audit committee and the CIA show that the audit committee meets with the CIA without the presence of management, on average 2.24 times accounting to 60% of total number of meetings.

Moreover, the audit committee is involved in the dismissal decisions in 38% of entities. This is comparable to 48% in Canada (Scarborough *et al.*, 1998), 72% in Singapore (Goodwin and Yeo, 2001), 52% in Australia and New Zealand, and 80% in Malaise.

In terms of audit committee reviewing of the internal audit work, it is observed that the average committee review of proposals and results of internal audit is a mere 1.76 with a minimum of zero and a maximum of 6.

Furthermore, regarding the independent variables, the mean percentage of independent outside directors in the audit committee is only 36.3%. It should be noted that only 14% of the sample committees are composed exclusively of independent directors which is a very low percentage compared to the results of previous studies, such as 71% of Canadian audit consists solely of outside directors (Scarborough *et al.*, 1998) and 74% of audit committees in the US are completely independent (Raghunandan *et al.*, 2001). Regarding expertise among the audit committee members, an average of 76% of audit committees have at least one financial expert among their members, which is a good sign. Further, the audit committee meets on average 3.78 times per year with a minimum of 2 and a maximum of 6 meetings. The table also reveals that the average size of audit committee is about 4 members per committee. Finally, private sector companies are found to be more (64%) than the public sector (36%).

Table 2: Descriptive Statistics					
	Mean	Median	Maximum	Minimum	SD
<i>FREQTOT</i>	3.780	4.000	6.000	2.000	1.111
<i>FREQABS</i>	2.240	2.000	6.000	0.000	1.943
<i>DISMISS</i>	0.380	0.000	1.000	0.000	0.490
<i>REVIEW</i>	1.760	1.000	6.000	0.000	1.974
<i>ACIND</i>	0.363	0.333	1.000	0.000	0.373
<i>ACEXP</i>	0.760	1.000	1.000	0.000	0.431
<i>ACMEET</i>	3.780	4.000	6.000	2.000	1.055
<i>ACSIZE</i>	3.660	3.000	7.000	3.000	0.981
<i>SECT</i>	0.640	1.000	1.000	0.000	0.484
<i>SIZE</i>	1.720	2.000	3.000	1.000	0.572
<i>IASIZE</i>	0.178	0.210	0.470	0.000	0.130

Correlation Analysis

The Pearson correlation matrix for the variables in the model is presented in Table 3. It can be seen that multicollinearity is not a problem since the variables are generally not highly correlated with each other, especially the variables related to the audit committee characteristics. The correlation coefficient between *FREQTOT* and *ACMEET* is high ($r = 0.792$) which is not surprising because the audit committee meets with the CIA during the annual meetings of the audit committee.

	<i>FREQTOT</i>	<i>FREQABS</i>	<i>DISMISS</i>	<i>REVIEW</i>	<i>ACIND</i>	<i>ACEXP</i>	<i>ACMEET</i>	<i>ACSIZE</i>	<i>SECT</i>	<i>SIZE</i>	<i>IASIZE</i>
<i>FREQTOT</i>	1.000										
<i>FREQABS</i>	0.279	1.000									
<i>DISMISS</i>	-0.180	-0.119	1.000								
<i>REVIEW</i>	0.049	0.031	0.096	1.000							
<i>ACIND</i>	-0.092	0.230	0.064	0.088	1.000						
<i>ACEXP</i>	0.100	-0.027	0.150	-0.021	-0.049	1.000					
<i>ACMEET</i>	0.792	0.324	-0.150	-0.172	0.005	0.150	1.000				
<i>ACSIZE</i>	-0.013	-0.052	-0.319	0.0623	0.077	0.044	-0.014	1.000			
<i>SECT</i>	-0.149	-0.361	0.243	0.142	-0.239	-0.031	-0.118	-0.262	1.000		
<i>SIZE</i>	-0.034	0.116	0.023	-0.060	0.093	0.052	0.098	0.081	-0.223	1.000	
<i>IASIZE</i>	-0.011	0.268	-0.268	0.111	0.185	0.123	-0.089	0.241	-0.236	0.072	1.000

Multivariate Analysis

A total of four estimations are carried out, and the results are reported in Table 4. The first estimation is done with the aim to test the impact of audit committee characteristics on the interaction between audit committee and internal audit in terms of frequency of meetings between audit committee and the CIA, *FREQTOT*. The overall model is significant [prob. (*F*-statistic) = 0.00], with an adjusted R^2 of 0.610 implying that the independent variables explain 61% of the frequency of meetings between the audit committee and the CIA. The second estimation tends to test the impact of audit committee characteristics on the private meetings of audit committee with the CIA, *FREQABS*, while the third tests the involvement of audit committee in dismissing the CIA, *DISMISS*, and the fourth tests the involvement of the audit committee in the review of internal audit work, *REVIEW*.

H_1 predicts a positive impact of audit committee independence on the interaction between audit committee and internal auditors. However, the study fails to find any significant association between audit committee independence and this interaction. This finding contradicts the results of previous researches (Scarborough *et al.*, 1998; Goodwin and Yeo, 2001; Raghunandan *et al.*, 2001; and Goodwin, 2003). The absence of such association can be explained by the low percentage of independent directors in the audit committees of Tunisian firms as compared to those of Canadian, American and Australian firms. This finding needs attention of regulators so that rules should be established with regard to the independence of the members of the audit committee in order to ensure better interaction with internal audit committee. Thus, H_1 is rejected.

With regard to H_2 presuming that the audit committee financial expertise positively affects the interaction between the audit committee and internal audit, results of estimation 3 indicate

Table 4: Regression Results					
Variable	Predicted Direction	<i>FREQTOT</i> t-Statistic (Probability)	<i>FREQABS</i> t-Statistic (Probability)	<i>DISMISS</i> t-Statistic (Probability)	<i>REVIEW</i> t-Statistic (Probability)
<i>ACIND</i>	+	-1.332 (0.189)	0.904 (0.370)	1.135 (0.256)	0.721 (0.474)
<i>ACEXP</i>	+	-1.332 (0.728)	-0.799 (0.428)	1.704* (0.088)	-0.027 (0.977)
<i>ACMEET</i>	+	8.749*** (0.000)	2.487** (0.016)	-1.254 (0.209)	-0.892 (0.377)
<i>ACSIZE</i>	-	-0.030 (0.779)	-1.427 (0.160)	-1.708* (0.087)	0.503 (0.617)
<i>SECT</i>	-	-0.234 (0.305)	-2.003* (0.051)	1.435 (0.151)	1.175 (0.246)
<i>SIZE</i>	+	-0.246 (0.174)	0.090 (0.928)	0.843 (0.398)	-0.187 (0.852)
<i>IASIZE</i>	+	0.669 (0.418)	1.949* (0.058)	-1.656* (0.097)	0.675 (0.502)
Adjusted R ²		0.610	0.208	0.2461	-0.073
Prob (F-Statistic)		0.000	0.016	0.0221	0.815
N		50	50	50	50
Note: *** Significant at 1%, ** Significant at 5%, and * Significant at 10%.					

that audit committee involvement in the decisions regarding the dismissal of the CIA is significantly related to the audit committee financial expertise. Indeed, the coefficient of the audit committee financial expertise (*ACEXP*) is positive (1.530) and significant in the involvement of the audit committee in dismissing the CIA. This implies that audit committees composed of financial experts are better involved in the dismissal of the CIA. Thus, H_2 is accepted. This can be explained with the fact that financial experts have extensive knowledge in the fields of accounting and auditing, and consequently, are more aware of misconduct, fraud or maneuvers made by the CIA which prompts them to fire him. However, Goodwin (2003) did not confirm an association between audit committee expertise and the dismissal of the CIA.

The coefficient related to the frequency of meetings of the audit committee (*ACMEET*) is positively and significantly associated with the frequency of total meetings between audit committee and the CIA (estimation 1) and private meetings between audit committee and the CIA (estimation 2). This result is logical as the CIA is present in all the meetings of the audit committee being a source of information to the audit committee on the developments of the organization, especially on the accounting and auditing matters. Thus, H_3 is accepted.

In H_4 a negative impact of the audit committee size on the interaction between audit committee and internal audit is foreseen. The regression results show that the coefficient related to the size of the audit committee (*ACSIZE*) is negative (-0.986) and significant in estimation 3, which implies that large-size committees are less involved in the dismissal of the CIA, thus confirming H_4 . This can be explained by the fact that audit committee comprising large number of directors can cause alliances and coalitions between members, divergence of interests and group conflicts, which make it difficult to have a common agreement on the decision of dismissing the CIA. Companies should decline the nomination of a large number of directors on audit committee so as to ensure that internal audit function is independent. Previous researches did not explore the association between audit committee size and audit committee interaction with internal audit.

In terms of control variables, it is observed that the sector variable is negatively and statistically significant (estimation 2) in private meeting between the audit committee and the CIA. This implies that private sector firms are less likely to have audit committees that meet with the CIA in the absence of management than the public sector enterprises. Goodwin (2003) found no significant association between the sector and the frequency of private meetings between the audit committee and the CIA. In addition, the coefficient of the internal audit size is positive (3.978) and significant (estimation 2) in the private meetings between audit committee and the CIA, which implies that companies with a large internal audit are more likely to have meetings between the audit committee and the CIA in the absence of management. However, Zain *et al.* (2006) also found that internal audit size positively affects the assessment of internal auditors of their contribution to financial statement audits.

Moreover, the coefficient of the internal audit size is negative (-5.110) and significant (estimation 3) in the involvement of the audit committee in dismissing the CIA, indicating that companies with large internal audit are less involved in the dismissal of the CIA. Finally, the results show that the size of the company has no impact on the relationship between the audit committee and internal audit.

Conclusion

This study extends the present literature by examining the impact of audit committee characteristics on the relationship between the audit committee and internal audit in the Tunisian firms.

The findings of the study have important implications for regulators who seek to improve corporate governance quality. First, the results indicate that audit committee independence has no significant impact on audit committee interaction with internal auditors. This contradicts the findings of the previous studies that focused on the positive impact of the independence. This result is attributed to the lack of independency of audit committee members in Tunisian firms, which needs the attention of regulators to establish rules in terms of independence of audit committee members to ensure better interaction with internal audit. Moreover, it is observed that financial expertise and frequency of meetings are all positively and significantly associated with at least one of the dependent

variables explored. Therefore, companies are recommended to appoint at least one financial expert in their audit committee and to convene annual meetings more frequently with a view to improving the interaction between audit committee and internal audit. Finally, audit committee size has a negative and significant impact on the interaction in terms of involvement in the decision to dismiss the CIA. Therefore, companies should avoid the nomination of a large number of directors on audit committee in order to ensure the independence of the internal audit function.

There are some limitations to the present study. First, the unavailability and non-publication of information relating to the audit committee characteristics as well as aspects of interaction between the audit committee and internal audit forced the authors to conduct a survey through face-to-face interviews with the CIA. This procedure was time and cost consuming, making it very difficult to visit all the firms. Second, only a few companies in Tunisia have an audit committee. Third, the small sample size is due to the disinclination of many companies to give responses.

Given the limitations of the studies dealing with the relationship between audit committee and internal audit function, it will be interesting to go further into the nature of this relationship and investigate in future research the impact of audit committee effectiveness on the internal audit quality. □

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Appendix

Questionnaire

1. Which sector does your company belong to?
 - Private Sector
 - Public Sector
2. How many members are there in your audit committee?
 - 3 members
 - 4 members
 - 5 members
 - Others (please specify)-----
3. What is the number of your audit committee meetings per year?
 - Two meetings
 - Three meetings
 - Four meetings
 - Others (please specify)-----
4. Each year, how many times does your audit committee meet with the chief internal auditor?
 - Twice
 - Three times
 - Four times
 - Others (please specify)-----
5. Does your audit committee meet privately (without the presence of management) with the chief internal auditor?
 - All meetings are entirely without management present.
 - All meetings have some private time.
 - Not all, but ____ meetings per year are without management present.
 - No meetings without management present.
6. Since outside director is a person who cannot be employed in the company or in a group company, or be a shareholder or trading partner (customer or supplier) or financial partner to the company, what is the number of independent outside directors in your audit committee (have no relation to the firm other than their position as directors)?
 - One director
 - Two directors
 - Three directors
 - Others (please specify)-----

Appendix (Cont.)

7. Since audit committee financial expertise is defined as having a professional certification in accounting or financial analysis or having experience in finance or accounting, what is the number of financial experts in your audit committee?

No expert

One expert

Two experts

Others (please specify)-----

8. Does your audit committee review internal audit proposals related to:

Programs/plans	<input type="checkbox"/> Yes	<input type="checkbox"/> No
Budget	<input type="checkbox"/> Yes	<input type="checkbox"/> No
Coordination with external auditors	<input type="checkbox"/> Yes	<input type="checkbox"/> No

9. Does your audit committee review internal audit results related to:

Financial Reporting	<input type="checkbox"/> Yes	<input type="checkbox"/> No
Internal Control	<input type="checkbox"/> Yes	<input type="checkbox"/> No
Compliance with Laws and Regulations	<input type="checkbox"/> Yes	<input type="checkbox"/> No

10. Is your audit committee involved in the dismissal of the chief internal auditor?

Yes

No

11. What is the total number of staff in your internal audit department?

12. Approximately, what is the total amount of your assets (in millions of dinars)

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