

# Internal auditor communications: an experimental investigation of managerial perceptions

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## Abstract

**Purpose** – The purpose of this paper is to examine potential determinants of management's agreement with internal auditor recommendations of an interim assurance engagement.

**Design/methodology/approach** – The experiment involved a  $2 \times 2 \times 2$  design with internal auditor gender, mode of communication and root cause variables randomly assigned to 228 experienced managers.

**Findings** – When the internal auditor includes a root cause for an identified deficiency in an internal audit report, management perceptions of the quality of that report improve. The gender of the internal auditor who communicates the audit finding with management does not significantly impact management's perceptions. Additionally, communicating the internal audit report via e-mail instead of videoconference results in improved managerial perceptions of the quality of the internal auditor. While improvements in perceptions of internal auditor quality lead to greater agreement with internal auditor recommendations, improvements in perceptions of report quality lead to greater implementation of internal-auditor-recommended remediation strategies.

**Research limitations/implications** – The operationalization of the manipulated variables of interest (communication mode, gender and root cause) may limit the generalizability of the study's results.

**Practical implications** – The paper includes managerial implications for internal auditors' choice of communication mode and inclusion of a root cause in interim internal audit reports.

**Originality/value** – This study provides evidence on the factors that could improve management's perceptions of internal auditors' work. The findings can help organizations, such as the Institute of Internal Auditors, to better understand how to address the needs of those who communicate with internal auditors.

**Keywords** Audit report, Internal audit function, Management perceptions, Audit recommendations, Internal auditor communications

**Paper type** Research paper



## Introduction

Good communication between the internal audit function (IAF) and management is crucial for an organization's success. Our study examines managerial perceptions of internal auditor attributes and report characteristics when internal auditors communicate their findings. [Sarens and De Beelde \(2006\)](#) identify management's response to internal audit recommendations as an integral part of the IAF–management relationship. Our study also examines the potential determinants of management's agreement with IAF recommendations of an interim assurance engagement. Internal auditors must communicate the results of its assurance engagement with senior management and other stakeholders to improve governance, risk and the control environment in an organization. Some of the attributes of communication between the IAF and management are clarity and timeliness, along with other communication quality characteristics such as accuracy, objectivity, conciseness, constructiveness and completeness ([IIA, 2012](#)). Even though communication at the conclusion of the audit typically involves a written report, communication of *interim* engagement results can vary in format, timing and content ([IIA, 2016](#)).

Internal auditors are encouraged to recognize areas of satisfactory performance in their communications to management ([IIA, 2012](#)). Often, though, internal auditor interim communications highlight issues that require corrective action that may not be perceived favorably by members of the management team who are tasked with mitigating the issues. Disagreement between management and the internal auditors over the results on an internal audit has been identified as the most frequent and “acrimonious” source of tension ([Chambers, 2017](#)). Sometimes management chooses not to implement internal audit recommendations. Richard Chambers, the President and CEO of the Institute of Internal Auditors, reflecting on his professional experience, summarizes the negative consequences of management resisting to implement auditor recommendations in the following:

When management says no and refuses to budge, you realize that it makes no difference how valid your recommendations are, or how hard you worked on the audit. Without results, you have accomplished nothing. The plain and simple fact is, if you can't bring people around to your point of view, the engagement will have been a waste of time, and important risks may remain unaddressed ([Chambers, 2014](#), par. 2).

Some internal auditors report being pressured to alter or leave out their findings ([Rittenberg, 2016](#); [Shumsky, 2016](#); [Monga, 2015](#)). In a world-wide survey of 14,518 internal audit professionals, 23 per cent indicated that they had experienced an instance where they were asked to suppress or substantially alter an internal audit finding or report that they considered to be valid ([Rittenberg, 2016](#)). An earlier report raises a similar concern by indicating that over 50 per cent of responding internal auditors report being approached with requests to change their findings ([Rittenberg and Miller, 2015](#)). This means that a considerable number of internal auditors report experiencing pressure as internal audit professionals.

This study is motivated by the need to more fully examine the nature of the relationship between company management and the IAF. [Soh and Martinov-Bennie \(2011\)](#) stress the importance of evaluating the IAF from the perspective of those relying on their work such as the audit committee, the external auditor and management. Studies focusing on the IAF have examined the relationship between internal auditors and the audit committee ([Goodwin, 2003](#); [Soh and Martinov-Bennie, 2011](#)) and between internal auditors and external auditors ([Abbot et al., 2010](#); [Prawitt, 2012](#); [Prawitt et al., 2009](#)). A few studies that explore management's perceptions of the IAF have evaluated management's reliance on internal auditors' consulting recommendations given their assurance reputation ([Tang et al., 2017](#)), management's assessment of IAF effectiveness in the South African public sector ([Erasmus](#)

and Coetzee, 2018) and internal auditors' ability to influence management based on internal auditor's interpersonal likability, argument organization and information used in support of their position (Fanning and Piercey, 2014). However, little is known about other potential determinants of management's perceptions of the IAF.

Gramling *et al.* (2004) call for more research identifying IAF characteristics that influence the relationship between the IAF and management. Lenz and Hahn (2015) emphasize the critical importance of interpersonal factors in determining the effectiveness of the IAF and encourage more research examining the attributes of the IAF that facilitate acceptance and ultimate resolution of internal audit findings by management. A survey of internal auditors conducted by Van Peurseem (2004) finds that communication and management intimidation through increased monitoring and follow-up investigations are critical to the role of internal auditors, with communication as the most prominent and distinctive characteristic of the role of the IAF. Kyburz (2016) calls for more studies to examine communication between the IAF and stakeholders, particularly management, by stating (p. 237):

The communication between internal auditing and its stakeholders (concerning management representatives in particular) presents an interesting field of research, which has not yet been thoroughly investigated. Studies could focus in-depth on the content, frequency, and type of communication, with the incorporation of behavioral aspects presenting another interesting research opportunity.

Boyle *et al.* (2015) also present the need for research to focus on internal auditor communication, with particular emphasis on report types and their influence on judgment of internal auditors and key governance members.

Because of the documented prevalence of resistance to internal audit findings, it is important to explore attributes that could impact management's decision-making when an internal auditor communicates a finding. The focus of our study is on three potential determinants:

- (1) mode of communication (e-mail vs videoconferencing);
- (2) internal auditor gender (female vs male); and
- (3) root cause presence in the audit report (explicitly stated vs not stated).

To address the objective of this study, we conducted an experiment in which corporate managers assumed the role of a manager of a hypothetical company. The managers received an internal audit report via e-mail or video (i.e. simulating a videoconference) from the chief audit executive (CAE). The CAE's gender was manipulated as female or male. The CAE either provided or did not provide the manager participants with the root cause of his or her audit finding. Finally, the CAE provided his or her recommendations to address the finding. Participating managers then provided their perceptions of the extent to which they agreed with the internal auditor's recommendations and the impact of the audit finding on the company financial position. Participants also chose which, if any, recommendations to implement.

Our results indicate that the gender of the internal auditor who communicates the audit finding with management does not significantly impact management's perceptions of the internal auditor or the audit report. Providing the reason why the audit finding occurred, i.e. the root cause, affects management's perceptions of the internal audit report's quality but does not affect whether management perceives the internal auditor as competent, independent and credible. Specifically, when the internal auditor provides the root cause of the audit finding, the internal audit report is perceived by management as more useful, clear, understandable and professional. Management also perceives that the internal auditor is

more competent and independent when the internal auditor communicates with management via e-mail rather than videoconference. Further, the attributes of the internal audit report and the internal auditor characteristics are significant determinants of management's agreement with internal auditor recommendations of an interim assurance engagement.

Prior research has examined the effects of the attributes of internal audit's recommendations on management's agreement (Burton *et al.*, 2012). Our study, however, focuses on the effect of attributes of the internal auditor (i.e. gender) and the internal audit report (i.e. communication mode and root cause). The results of this research shed light on facilitators and barriers to a more impactful auditor–manager communication, which ultimately leads to improved management reliance on internal auditors and greater internal audit effectiveness. Improving the communication between management and internal auditors is an important issue to investigate because there is evidence of management choosing not to implement internal audit recommendations after an internal auditor communicates a finding. Managers, internal auditors and standard setters can greatly benefit from understanding the attributes that affect management's perceptions of internal auditors' recommendations to develop strategies to mitigate the resistance to internal audit findings. Further, providing evidence on the factors that could improve management's perceptions of internal auditors' work can help organizations, such as the IIA, to better understand how to address the needs of those with whom internal auditors communicate. Thus, we focus our study on three potential determinants: mode of communication, internal auditor gender and the presence of an explicitly stated root cause in the audit report.

Our study answers Kyburz's (2016) call for more studies examining communication between the IAF and management. This study makes a contribution to the scarce accounting literature on gender of accounting professionals. While research has examined gender imbalance in promotion decisions in public accounting firms (Anderson-Gough *et al.*, 2005), examination of internal auditor characteristics, such as gender, is an overlooked area in internal audit research, and we hope to fill this void. Given the significant amount of research in psychology, which finds interesting female and male differences, it is noteworthy that we find no significant differences in how male vs female CAE is perceived by management. Few accounting studies examine the gender variable, but in different settings. Saiewitz and Kida (2018) find that results of their study do not vary by participant gender when gender is included as a control variable in their analyses. In the Saiewitz and Kida (2018) study, the external auditor communicating an inquiry was a male in all experimental conditions. However, in our study, we intentionally manipulate the gender of the internal auditor from whom the participant is receiving the internal audit report. As such, we cannot expect that prior research results will apply to our study. Therefore, exploring the communicator's gender remains an overlooked area.

Our setting also differs because we focus on the communication issues between managers and internal auditors, whereas several prior accounting studies examine the communication between managers and external auditors. For example, Saiewitz and Kida (2018) investigate an external auditing setting where managers interact with junior staff auditors, and Bennett and Hatfield (2018) focus on staff auditors interacting with a corporate controller.

As technology becomes more prevalent and widely used by firms, accounting research should also investigate how technology affects the communication and decisions among various parties. Prior research has investigated various communication modes such as text, video, face-to-face; however, prior research findings cannot be expected to apply to an accounting task, such as the one in our study. Though Saiewitz and Kida (2018) and Bennett

and Hatfield (2018) examine communication mode in auditing settings, the settings differ substantially from ours and the results are not conclusive on the effects of communication mode. Our study's intra-company communication setting is unique in that we examine managers' decisions in response to recommendations made by internal auditors employed by their own company.

Further, to the best of our knowledge, this study is one of the first to explore and test whether the inclusion of the root cause as part of the internal audit report influences managerial perceptions. The goal of communicating the root cause is to eventually eliminate the reappearance of the condition and improve organizational performance.

Our paper is structured as follows. Section 2 provides a detailed review of the relevant literature and develops our hypotheses. Section 3 describes our experimental design, followed by Section 4, which outlines the results of the study. Section 5 provides an overview of the results and discusses the implications of our findings.

## Background and hypothesis development

### *Research on managers' reliance on the internal audit function*

Even though studies focusing on the relationship between internal auditors and management are limited, a few recent studies examine issues related to managers' reliance on the recommendations of internal auditors. Sarens and De Beelde (2006) perform a qualitative analysis to broadly explore the relationship between the IAF and management, as well as their expectations of each other. They find that managers expect the IAF to provide assurance over the effectiveness of internal controls, to assist in improving those controls and to take part in the development of risk management systems. Burton *et al.* (2012) find that internal auditors can substantially influence managers when the auditor's recommendation is inconsistent with manager's initial position. Fanning and Piercey (2014) document that managers agree more with internal auditors who organize their arguments and are likable even if an auditor's position is unsupportive of management's position. Tang *et al.* (2017) report that internal auditor assurance engagement reputation has a positive impact on managers' reliance on consulting recommendations. No study, of which we are aware, has explored the role of internal auditor gender, communication mode and the inclusion of root cause in the communication of internal audit findings to management.

### *The mode of internal audit report communication*

To add value to an organization, it is critical for the IAF to use innovative technologies and tools to provide assurance (PwC, 2018). While only 14 per cent of IAFs have adopted advanced technologies, a significant number, 46 per cent, of IAFs are in the process of implementing technology (PwC, 2018). A recent article in *Internal Auditor* highlights the prevalence of remote internal audits and encourages auditors to use technological tools to increase internal audit efficiency, improve accuracy and gain deeper insights as the internal audit process "typically involves small teams traveling to various locations and setting up shop for one or two weeks. There, auditors pull team leads, directors, vice presidents, and even top executives away from their daily duties to evaluate the control systems and targeted processes. Teams then perform substantive tests, examine analytical procedures, hold direct interviews, and raise inquiries with various levels of management" (Suhovsky, 2018, paragraph 3). Many IAFs are using videoconferencing as a means of communication between the IAF and management (PwC, 2018). This approach allows internal auditors and managers to collaborate across offices and countries while reducing travel costs and improving efficiency and alignment with organizational objectives (PwC, 2018).

Typically, communications between internal auditors and managers consist of a series of e-mails or written reports. However, internal audit standards allow variations in format, timing and content of interim internal audit communications to management. A survey of IIA chapter members conducted in 2007 reported that 39 per cent of internal auditors' meetings occurred between attendees located in different offices (Lambing, 2008). The same survey reported that 15 per cent of managers and 16 per cent of directors have sometimes used videoconferencing (Lambing, 2008). Owing to the increasing availability, low cost and the ease of use of various types of communication technology, videoconferencing is increasingly being adopted for communication between the IAF and management. For example, as Accenture increased its global presence through acquisitions and increase in headcount, their IAF was challenged to identify risks and perform audits for an increasingly more complex global enterprise (Accenture, 2015). To address the needs of a rapidly growing business, Accenture's IAF had to increase the number and frequency of interviews and to shorten response times among audit teams around the world (Accenture, 2015). As a result, they used various technology tools, including videoconferencing (Accenture, 2015; p. 6):

Internal Audit makes use of these technologies to more effectively support its work, especially to collaborate with teams around the world virtually rather than through travel. [. . .] When travel is required to do field work, the extent of time needed to be on site can be reduced through the use of collaborative technology, helping to reduce travel costs and save employee time.

A chief internal auditor of Barclays also notes the use of videoconferencing technology to support the work of their IAF by stating the following (Protiviti, 2016; p. 12):

We are big users of videoconferencing technology, and we have our own intranet site that can be accessed by the entire team wherever they are based. [. . .] We use WebEx technology to train the entire department at times, sharing information much more efficiently while cutting down on travel.

Studies exploring the impact of using different communication modes find that managers perceive a CEO who communicates negative news such as a restatement through video, as opposed to written report, to be more worthy of trust and greater investment in the company (Elliott *et al.*, 2012). Chaiken and Eagly (1976) test the persuasiveness of written, audiotaped and videotaped communication modes. They find that with easy messages (those that consisted of sentences of 20 words or less, with one or two clauses per sentence, and with simpler vocabulary), video resulted in greater opinion change than in audiotape or written conditions. A recent study documents that compliance with requests communicated through e-mail (i.e. computer-mediated text) is often overestimated (Roghanizad and Bohns, 2017). The results of these studies confirm that videotaped messages tend to facilitate a more impactful communication.

Soo Suh (1999), however, finds no difference in decision quality across media – text, audio, video and face-to-face – in performing intellectual[1] and negotiation tasks. Soo Suh (1999) also reports that the video medium was closer to face-to-face than audio medium in task satisfaction and decision time. Other studies find that computer-mediated communication through text (i.e. two people typing information synchronously into a computer screen) is more successful, as it increases straight talk by reducing positive distortion of negative information found in face-to-face communication (Sussman and Sproull, 1999).

Saiewitz and Kida (2018) examine whether communication mode (e-mail, audio or video) of the audit inquiry impacts how clients respond to that inquiry, measured as the net items revealed or the difference between the number of items that support and do not support the

accounting position of a client. Though [Saiewitz and Kida \(2018\)](#) find that communication via e-mail (as opposed to audio or visual communication) biases client's responses toward their own position and away from the external auditor's position, communication mode does not have a direct effect on agreement with the external auditor's proposed audit adjustment. However, clients are less likely to agree with a proposed audit adjustment when they previously provide the auditor with a more biased information set ([Saiewitz and Kida, 2018](#)). Alternatively, [Bennett and Hatfield \(2018\)](#) find benefits to face-to-face communication relative to computer-mediated communication: staff audit professionals ask more follow-up questions, have greater back and forth interaction and make more relationship-building statements with a corporate controller in a face-to-face interaction.

Though these two studies examine communication mode in auditing settings, the settings differ substantially from ours and the results are not conclusive on the effects of communication mode. Our study's intra-company communication setting is unique in that we examine managers' decisions in response to recommendations by internal auditors who are employed by their own company.

In light of the increasing use of videoconferencing in internal audit, and because of the mixed findings reported in studies examining communication modes, it is important to explore whether managers possess different perceptions of an internal audit report delivered via e-mail as opposed to a video. Furthermore, the influence of the communication mode on managers' perceptions of the internal auditor are also important to examine. As a result, we hypothesize the following:

- H1a.* The mode of the internal audit report will influence managerial perceptions of internal audit report quality.
- H1b.* The mode of the internal audit report will influence managerial perceptions of internal auditor quality.

#### *Inclusion of root cause in the internal audit report*

Discussion of internal audit findings makes up a substantial portion of the report. It is desirable that recommendations are accompanied by the root cause ([IIA, 2016](#)). It can be defined as the gap between expectations based on policies (i.e. criteria) and actual evidence found during the engagement (i.e. condition) ([IIA, 2016](#)). The root cause addresses questions surrounding the reasons for the condition to be present. The goal of communicating the root cause of the observation is to eventually eliminate reappearance of the condition.

[Elliott et al. \(2007\)](#) state that understanding reasons for non-conformance by determining the underlying root cause is a critical activity in the evaluation of internal audit effectiveness. A survey of internal auditors and auditees identifies that the root cause analysis of audit deficiencies is an area that, if not properly addressed, could reappear and, therefore, diminish the impact and value of internal audit ([Elliott et al., 2007](#)). Moreover, their survey reports inconsistencies in the deficiency analysis process and low scores on quality improvement actions indicating that improvement actions are not performed when root causes are not fully examined. The authors emphasize that audit deficiency analysis and the quality of improvement actions are areas that are critical to internal audit improvement, even though they are underused in practice ([Elliott et al., 2007](#)).

Whether the inclusion of a root cause in an internal audit report indeed results in improved perceptions of internal audit report quality and/or internal auditor quality is an empirical question. Inclusion of a root cause in an audit report often provides more detail to a report. This additional detail is likely to be perceived by managers as superfluous and not

warranting particular attention. As such, management may not perceive an internal auditor or an internal audit report as higher in quality if a root cause is included in a report. Consequently, we examine whether the inclusion of the root cause as part of the report that communicates an internal audit finding has an influence on managerial perceptions. Therefore, we hypothesize the following:

- H2a.* Inclusion of a root cause in the internal audit report will influence managerial perceptions of internal audit report quality.
- H2b.* Inclusion of a root cause in the internal audit report will influence managerial perceptions of internal auditor quality.

### *Internal auditor gender*

Sarens (2009) states that examination of internal auditor characteristics, other than objectivity, is an overlooked area in research. Van Peursem (2005) calls for more research to explore the role of gender in communication between internal auditors and others. Moreover, Khlif and Achek (2017) point to the lack of studies exploring interactions between the gender of management and auditor. In this paper, we examine if gender of the internal auditor delivering the finding influences managerial perceptions. On one hand, because internal auditors are a non-random self-selected professional subgroup exposed to extensive socialization, we cannot assume that gender differences that have been documented among the general population will apply (Hardies *et al.*, 2011); Hardies *et al.* (2011) document no gender differences in the degree of overconfidence among auditors. On the other hand, Iyer *et al.* (2005) find gender differences, in that, women, reflecting on their actual work experience in public accounting, evaluate training and personnel in Big 4 accounting firms significantly lower than men. Also, studies focusing on gender relations in public accounting firms document gender imbalance in promotion decisions. Specifically, Anderson-Gough *et al.* (2005) state:

Male partners, senior managers, etc., will recruit, promote people with the same backgrounds and preferences as themselves, and hence reproduce organizational gender relations. Of course, we have noted in both firms deliberate policies of gender balance in recruitment and the use of seemingly neutral assessments, such as psychometric testing, with some effect, but such initiatives, necessarily, do not carry over to promotion (487).

Resembling issues encountered in public accounting, there are concerns of gender imbalance in the internal audit profession. Women represent approximately 31 per cent of CAEs, which is a larger gender gap than among directors or senior managers where women account for 33 per cent of auditors, 34 per cent of managers and 44 per cent of internal audit staff (Christ, 2015). Therefore, top internal audit positions within organizations are held predominantly by men. Female internal auditors could also be perceived as being less assertive, which can undermine their credibility, especially in situations where they might be met with resistance and where they need to take a firm stance (Christ, 2015). As a result, it is important to empirically explore whether internal auditor gender (i.e. being a female) plays a role in managerial decisions when they are presented with a finding that requires corrective action on their part. Therefore, we hypothesize the following:

- H3a.* The gender of the chief audit executive will influence managerial perceptions of internal audit report quality.
- H3b.* The gender of the chief audit executive will influence managerial perceptions of internal auditor quality.



*Internal audit report quality and internal auditor quality*

Measuring internal report and internal auditor quality is a complex and multi-dimensional process, which is also contingent on the needs of stakeholders such as management. At the heart of a high quality internal audit report is accuracy, objectivity, clarity, completeness and timeliness (IIA, 2012). It is reasonable to expect that an internal audit report quality will affect management's perceptions and will motivate them to take appropriate action. In a similar vein, internal auditors who are perceived by management to be competent, independent and credible will facilitate agreement with their recommendations and be successful at encouraging management to swiftly correct any shortcomings. Therefore, we hypothesize the following:

- H4a. Internal audit report quality will influence managerial agreement with internal audit recommendations.
- H4b. Internal audit report quality will influence managerial agreement with the negative impact of internal audit findings on the financial position and reputation of the company.
- H4c. Internal audit report quality will influence the number of internal audit recommendations management implements.
- H5a. Internal auditor quality will influence managerial agreement with internal audit recommendations.
- H5b. Internal auditor quality will influence managerial agreement with the negative impact of internal audit findings on the financial position and reputation of the company.
- H5c. Internal auditor quality will influence the number of internal audit recommendations management implements.

Thus, our theoretical model is displayed in Figure 1.

**Research design and method**

*Experimental design*

We conducted a 2 × 2 × 2 fully crossed between-participants experiment to test our hypotheses. We manipulated three independent variables – 1) gender: female vs male; 2) mode of communication: e-mail vs video; and 3) root cause: present vs absent. Participants were recruited with the assistance of a national research company called Qualtrics Panels.

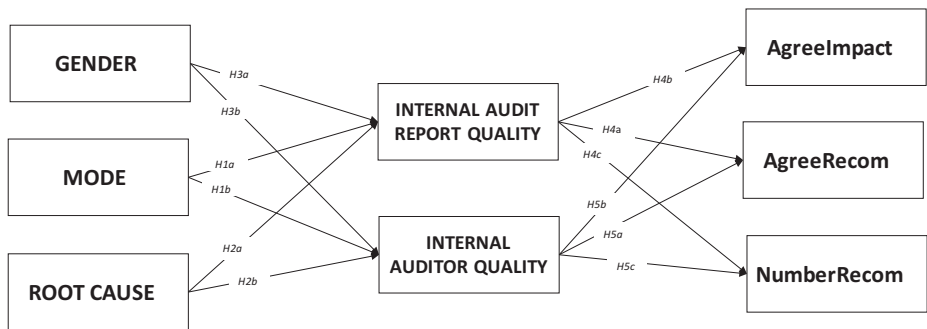


Figure 1. Theoretical model

The experiment was conducted online and was computerized to track time and to incorporate experimental controls. Participants were randomly assigned to one of the eight experimental conditions. Part of the experimental instrument is included in [Appendix](#).

We modeled the internal audit report included in our experimental materials after a large for-profit organization's internal audit report. We also discussed the experimental instrument with an external auditor from a Big 4 firm to draw on his experience with internal audit report observations and to ensure consistency of wording with firm terminology. Further, we received feedback on the experimental materials from fellow faculty with accounting information systems and auditing expertise to clarify any ambiguous sections of text[2].

### *Participants and experimental procedures*

To answer our research questions, a sample of managers was desired. To reach this population, we solicited the help of a national research company, Qualtrics Panels, and set the following specific criteria for participation:

- participants must be 18 years of age or older;
- participants must currently be mid- or upper-level managers; and
- participants must have at least one year of managerial work experience where they supervised employees.

Only individuals who met all these prescreening criteria were allowed to participate in the study.

Participants were asked to assume the role of a manager and were provided with case materials explaining that the CAE (i.e. female or male auditor) of their company's internal audit department provided them with the current internal audit report (i.e. via e-mail or videoconference) of the first quarter. Participants in the female (male) conditions received an e-mail from a female (male) CAE or saw her (him) on video[3]. The e-mail or videoconference recording covered the content of the internal audit report. All participants were given the internal audit report that contained a finding: three of the five accounts payable check requests (60 per cent) totaling \$125,000 did not have the proper approvals prior to disbursement. The internal audit report further explained the hypothetical company policy of having two approvals on checks over \$25,000. The internal audit report informed participants that the effect of this finding was that it could result in fraudulent disbursements, negatively impacting the financial position and reputation of the company. The internal audit report either contained or did not contain the root cause of this finding. The internal audit report concluded with the CAE's recommendations. All participants were exposed to the following recommendations:

As a result, we recommend that your department performs the following:

- Review all checks over \$25,000 to ensure payments are made for legitimate corporate expenses based on supporting documentation, including that appropriate approvals are obtained.
- Establish a formal training program within the department to ensure staff can properly execute their job responsibilities.
- To ensure employees in all areas of the company are aware of current policies, we also recommend that periodic reminders be sent directly to employees reminding them of the location of the policies, particularly when policies are revised.

Following the report, the dependent variable questions were asked. Participants were asked to indicate which recommendations by the CAE they would like to implement as managers in the company, to what extent they agreed with the recommendations and to what extent they agreed that the observation could negatively impact the company. The online application did not allow participants to leave the screen showing the case materials (experimental condition) and proceed to the next screen until 2 min had passed for the video conditions and 42 s for the e-mail conditions[4]. Next, participants were shown the manipulation check questions. Then, participants were asked additional questions about the characteristics of the internal audit report and the CAE. The post-experimental questionnaire followed.

#### *Independent variables*

The following three independent variables were manipulated:

- (1) CAE's gender was manipulated by having a female or a male actor present the internal audit report to the participants. Actors in the videoconferencing conditions were both Caucasian and had no foreign accents. In the e-mail experimental conditions, participants were provided with a picture of the CAE to hold certain physical characteristics constant.
- (2) The mode of communication of the internal audit report was manipulated at two levels. Participants were told that they received the report in an e-mail format and were provided with the e-mail or participants clicked to play a video having the CAE read the same text that was provided in the e-mail condition. The content of the report, regardless of the mode of communication, was the same.
- (3) The only change in the content of the internal audit report was the root cause, our third independent variable, which was manipulated at two levels (i.e. present or absent).

The root cause variable is the reason for the CAE's finding/observation mentioned in the internal audit report. The observation was that a few of the accounts payable check requests tested did not have proper approval prior to disbursement. If managers were told the root cause of the observation, they were told the following: "So, what is the root cause of this observation? Although all company policies are available on the company's intranet accessible to all employees, the staff processing the payments indicated they were not aware of the approval policy and were never informed about policies applicable to their job during their training." If the root cause was absent, then the participants did not receive this information.

To ensure that results are not influenced by differences in actors, we conducted a short survey on Amazon Prime Turk with 53 participants who watched one of the two videos from our main experiment. We then compared the participants' responses regarding the female and male actors on important dimensions to make sure our study results are not caused by differences in actors. A total of 25 participants watched the video with a male actor, and 28 participants watched the video with a female actor.

Once participants reviewed the videos, they provided perceptions on a seven-point Likert scale, where 1 equaled "strongly agree" and 7 equaled "strongly disagree." The mean score to "The person in the video looks professional" for the female video group is 2.68 and for the male video is 2.28 ( $p$ -value = 0.352). The second dimension evaluated was whether the actor in the video was attractive. The mean score for the female video is 3.25 and for the male video group is 3.80 ( $p$ -value = 0.154). We also asked participants to agree or disagree with

the following statement: "The person in the video spoke with a foreign accent." The mean score for the female video group is 6.21 and for the male video, 6.68 ( $p$ -value = 0.194). The participants rated the statement, "I could understand what the person in the video was saying (i.e. the person spoke in a clear and understandable way)". The participants who watched the video with the female actor responded, on average, 1.86, and the participants who watched the video with the male actor responded, on average, 1.92 ( $p$ -value = 0.877).

Finally, participants were asked to indicate how "likable" the person seemed on a seven-point Likert scale, where 1 equaled "not at all likeable" and 7 equaled "extremely likeable." The means for the female video group (4.79) and for male video (4.92) are not statistically different ( $p$ -value = 0.722). We also compared the mean of each group to the scale mid-point of four. The results indicate that both female and male internal auditors were perceived to be likeable as they are both statistically greater than the neutral point of four on the seven-point Likert scale (female:  $t$ -statistic = 3.231,  $p$ -value = 0.003; male:  $t$ -statistic = 3.192,  $p$ -value = 0.004). Although there are inherent differences between the female and male videos, and we recognize this as a limitation of the study, there are no statistically significant differences on any of the five dimensions for our female and male actors. Thus, we conclude that the results of our study are not driven by differences in the attributes of the actors.

#### *Dependent variables*

The first dependent variable, *AgreeImpact*, asked participants: "To what extent do you agree that the internal auditor's observation (i.e. the lack of proper approval for check requests) could negatively impact the financial position and reputation of the company?" The second dependent variable, *AgreeRecom*, asked participants to indicate the extent to which they agreed with the CAE's recommendations. Both questions were measured on an 11-point Likert scale, where 1 represented "completely agree" and 11 represented "completely disagree." The third dependent variable, *NumberRecom*, asked participants which of the recommendations by the CAE they would like to implement. The first three answer choices consisted of the three recommendations mentioned in the internal audit report of the experimental materials. We also included a fourth answer choice which stated "I do not wish to implement any of these recommendations".

Additionally, we used various items to measure our two constructs of interest, internal auditor quality and internal audit report Quality. The internal audit report quality items asked participants to indicate on a seven-point Likert scale how they would describe the internal audit report based on five statements, where 1 represented "impossible to understand," "very unclear," "not useful at all," "not professional" and "not detailed at all," whereas 7 represented "very easy to understand," "very clear," "very useful," "very professional" and "very detailed," accordingly. The internal auditor quality variable was measured using three items. The first two questions asked participants to indicate whether they thought the CAE was competent and independent, where 1 represented either "extremely competent" or "extremely independent" and 7 represented either "not at all competent" or "not at all independent," accordingly. The third question asked whether participants thought that the information in the internal audit report was credible, with 1 representing "extremely credible" and 7 representing "not at all credible"[5].

## Results

### *Manipulation check questions*

To ensure that each participant was actively engaged and understood the case information, three manipulation check questions were posed regarding the relevant facts of the case. The first manipulation check question asked participants to select whether the CAE provided

them with the internal audit report over e-mail or via a Skype Web-conferencing call. The second question asked participants to select the gender of the CAE from the case materials (male or female). The third manipulation check question asked participants "What was specified by the chief audit executive's internal audit report as the root cause of the failure to properly approve check requests?" Participants made a selection between two answers:

- (1) explaining that the staff processing the payments indicated they were not aware of the approval policy and were never informed about policies applicable to their job during their training; or
- (2) explaining that the CAE's internal audit report made no mention of the root cause of the failure to properly approve check requests.

If a participant missed any of the three questions, these participants were dropped from the study by Qualtrics Panels and their answers were not recorded. Thus, the final sample of 214 participants consisted of participants who successfully passed all three manipulation check questions[6].

#### *Descriptive statistics and measurement model*

Our sample consisted of 214 managers. Their average age was 53.5 years. There were 128 male (56.1 per cent) and 100 female (43.9 per cent) participants in the sample. Of the participants, 140 (61.4 per cent) self-reported as mid-level management, 64 (28.1 per cent) as upper management and 24 (10.5 per cent) as C-level executives when asked about their current positions in their respective companies. The participants in the study had 32.5 years of general work experience and 20.2 years of managerial work experience where they supervised employees. Of the participants, 139 (61 per cent) indicated that the organization where they currently worked had an internal audit department, and 73.4 per cent indicated that they had read an internal audit report before. Of the participants, 39 per cent currently working in a company with no internal audit department indicated they had read an internal audit report before. Overall, 186 participants (81.6 per cent) had some type of experience in or with internal audit[7]. Participants were compensated by Qualtrics Panels with cash, gift cards or frequent flier miles. The means (standard deviations) of the dependent variables are as follows: *AgreeImpact* 3.328 (2.81), *AgreeRecom* 2.70 (2.48) and *NumberRecom* 2.46 (0.74)[8]. Descriptive statistics by experimental conditions are displayed in [Table I](#), Panels A and B, for the demographic information and in [Table II](#) for the dependent variables.

Next, we simultaneously test the proposed path model by using partial least squares (PLS) ([Ringle et al., 2015](#)). The PLS analysis consists of two stages. In the first stage the reliability and validity of the measurement model is tested. To assess the adequacy of the measurement model, we analyze discriminant and convergent validities. In the second stage, the path coefficients and the fit of the structural model are analyzed ([Birkinshaw et al., 1995](#)).

We initially conducted an exploratory factor analysis for the five items of internal audit report quality construct. The means (standard deviation) of the five items are as follows: clarity 6.22 (1.15), understandability 6.28 (1.07), usefulness 6.07 (1.23), professional 6.12 (1.24) and detailed 5.27 (1.33). These measures are used as reflective indicators of the internal audit report quality construct. The individual factor loadings are greater than 0.73 and are deemed very good to excellent ([Comrey and Lee, 1992](#)), indicating that the convergent validity of this construct is satisfactory. Further, Cronbach's alpha is 0.906. The average variance extracted (AVE) for internal audit report quality is 0.730 and the composite reliability coefficient is 0.931. The recommended threshold values for AVE is 0.5 and for composite reliability coefficients is 0.6 ([Bagozzi and Yi, 1988](#)). Thus, we have a reliable measure.

Gender Mode	Male auditor				Female auditor				Overall <i>n</i> = 214	<i>F</i> -statistic ( <i>p</i> -value)
	E-mail		Videoconference		E-mail		Videoconference			
	Root cause <i>n</i> = 29	No root cause <i>n</i> = 27	Root cause <i>n</i> = 25	No root cause <i>n</i> = 25	Root cause <i>n</i> = 28	No root cause <i>n</i> = 25	Root cause <i>n</i> = 28	No root cause <i>n</i> = 27		
Panel A										
<i>Work experience (years)</i>										
Mean	34.66	33.41	30.2	31.12	30.32	32.72	31.21	36.85	32.60	1.259
SD	10.18	11.04	11.37	11.89	10.29	10.40	9.65	11.54	10.84	(0.272)
<i>Managerial experience (years)</i>										
Mean	23.17	20.74	19.6	17.92	18.5	17.76	19.57	23.3	20.14	1.259
SD	10.39	10.47	13.04	8.67	10.45	11.23	11.06	11.36	10.89	(0.372)
<i>Current position (years)</i>										
Mean	10.48	13.41	9.76	9.32	9.25	7.64	10.32	12.11	10.32	1.324
SD	9.21	8.88	6.73	7.05	7.14	6.20	7.41	10.00	8.01	(0.240)

(continued)

**Table I.**  
Descriptive statistics  
of demographic  
information

Table I.

Gender Mode	Male auditor				Female auditor				$\chi^2$ -statistic (two-sided <i>p</i> -value)									
	E-mail		Videoconference		E-mail		Videoconference											
Root cause presence	Root cause	No root cause	Root cause	No root cause	Root cause	No root cause	Root cause	No root cause	Overall									
<b>Panel B</b>																		
<i>Age</i>																		
25-34	1	3.4%	1	3.7%	1	4.0%	3	10.7%	1	4.0%	2	7.1%	1	3.7%	11	5.1%	21.464 (0.965)	
35-44	4	13.8%	3	11.1%	5	20.0%	5	17.9%	5	20.0%	3	10.7%	1	3.7%	31	14.5%		
45-54	6	20.7%	7	25.9%	7	28.0%	9	32.1%	7	28.0%	8	28.6%	7	25.9%	59	27.6%		
55-64	12	41.4%	12	44.4%	9	36.0%	8	28.6%	9	36.0%	13	46.4%	13	48.1%	86	40.2%		
65-74	6	20.7%	3	11.1%	3	12.0%	3	10.7%	3	12.0%	2	7.1%	5	18.5%	26	12.1%		
75-84	0	0.0%	1	3.7%	0	0.0%	0	0.0%	0	0.0%	0	0.0%	0	0.0%	1	0.5%		
<i>Gender</i>																		
Male	19	65.5%	13	48.1%	15	60.0%	12	48.0%	20	71.4%	12	48.0%	12	42.9%	15	55.6%	118	55.1%
Female	10	34.5%	14	51.9%	10	40.0%	13	52.0%	8	28.6%	13	52.0%	16	57.1%	12	44.4%	96	44.9%
<i>Position</i>																		
Mid-level mgmt	17	58.6%	18	66.7%	14	56.0%	15	60.0%	18	64.3%	18	72.0%	16	57.1%	17	63.0%	133	62.1%
Upper mgmt C-level exec	9	31.0%	8	29.6%	8	32.0%	8	32.0%	6	21.4%	3	12.0%	9	32.1%	8	29.6%	59	27.6%
	3	10.3%	1	3.7%	3	12.0%	2	8.0%	4	14.3%	4	16.0%	3	10.7%	2	7.4%	22	10.3%
<i>Internal audit experience</i>																		
Yes	13	44.8%	11	40.7%	11	44.0%	9	36.0%	9	32.1%	11	44.0%	10	35.7%	10	37.0%	84	39.3%
No	16	55.2%	16	59.3%	14	56.0%	16	64.0%	19	67.9%	14	56.0%	18	64.3%	17	63.0%	130	60.7%
<i>External audit experience</i>																		
Yes	10	34.5%	8	29.6%	2	8.0%	6	24.0%	6	21.4%	7	28.0%	6	21.4%	8	29.6%	53	24.8%
No	19	65.5%	19	70.4%	23	92.0%	19	76.0%	22	78.6%	18	72.0%	22	78.6%	19	70.4%	161	75.2%

Gender Mode	Male auditor			Female auditor			Overall n = 214
	Root cause n = 29	No root cause n = 27	E-mail n = 25	Root cause n = 25	No root cause n = 28	E-mail n = 27	
Root cause presence							
<i>AgreeImpact</i>							
Mean	3.24	2.96	3.04	3.60	3.00	4.15	3.28
SD	3.10	2.21	1.86	3.32	2.97	3.10	2.81
<i>AgreeRecomm</i>							
Mean	2.79	2.59	2.52	2.84	2.50	3.00	2.70
SD	2.56	1.89	1.76	3.15	2.55	2.65	2.48
<i>Number of recommendations</i>							
Mean	2.48	2.33	2.48	2.40	2.64	2.22	2.46
SD	0.79	0.62	0.77	0.82	0.68	0.97	0.74

**Notes:** Participants assessed AgreeImpact ("Observation will negatively impact company's financial position and reputation") and AgreeRecomm ("Agreement with recommendations") on a Likert scale ranging from 1 – completely agree to 11 – completely disagree. Number of recommendations reflects how many recommendations participants chose to implement

**Table II.**  
Descriptive statistics  
of dependent  
variables



We also conduct a factor analysis for the three questions of internal auditor quality construct. The means (standard deviation) of the three questions are as follows: competent 2.27 (1.41), independent 2.81 (1.45) and credible 2.07 (1.23). Cronbach's alpha is 0.822. The AVE for internal auditor quality is 0.739, and the composite reliability coefficient is 0.894. Thus, we have a reliable measure.

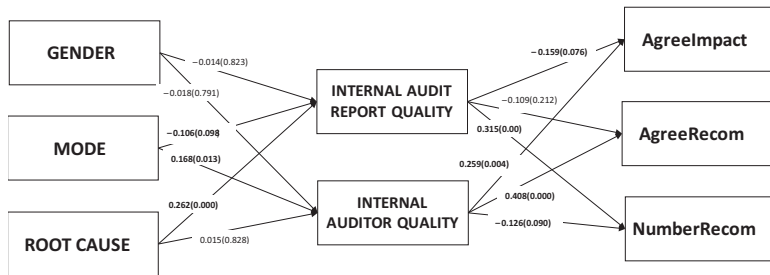
*Hypothesis testing*

Next, we estimate the model using PLS. PLS is a structural modeling technique that uses least squares parameter estimation to minimize the residual variances of all dependent variables (Chin, 1998). We chose PLS because of its robustness to produce estimates in smaller sample sizes, robustness to violations of multivariate normality and propensity to estimate complex models with a large number of variables (Klein and Rai, 2009; Henseler and Sarstedt, 2012). We follow Chin (1998) by using a bootstrapping method to obtain estimates of the standard errors, assessing the statistical significance of the path coefficients. The coefficients can be interpreted as  $\beta$ 's in OLS regression.

We use path coefficients and  $R^2$  jointly to test our structural model. The  $R^2$  value of 14.2 per cent suggests that our model explains a significant amount of variance in our first dependent variable, *AgreeImpact*. The  $R^2$  values for *AgreeRecom* and *NumberRecom* are 23.2 per cent and 16.3 per cent, respectively. Further, the model's path coefficients are represented in Figure 2 [9][10].

In our model, the five constructs are expected to play a significant role in the communication relationship between a manager and an internal auditor. We conclude that the model shown in Figure 2 is an overall good representation of the relationships among the modeled variables. The path between the mode of communication and internal audit report quality is marginally significant ( $p = 0.098$ ,  $\text{coef} = -0.014$ ), providing some support for *H1a*. Specifically, managers who read the internal audit report in an e-mail (as opposed to video) perceived the report as more useful, clear and professional. Also, the mode of communication significantly influences managerial perceptions of internal auditor quality ( $p = 0.013$ ,  $\text{coef} = 0.168$ ), lending support for *H1b*. Managers who saw the internal auditor on video perceived the internal auditor as possessing less competence and independence.

Including the root cause of the audit finding in the report significantly affects managers' perceptions of the quality of the internal audit report ( $p < 0.001$ ,  $\text{coef} = 0.262$ ) but does not significantly affect their perceptions of the internal auditor's competence and independence ( $p = 0.828$ ,  $\text{coef} = 0.015$ ). This finding suggests that managers perceive the internal audit report as more clear and useful when managers are provided with the reason of the audit finding. Thus, we find support for *H2a*, but not for *H2b*.



**Figure 2.**  
Path coefficients and  $p$ -values of model

The paths from auditor's gender to auditor's quality (attributes) and report quality are not statistically significant, suggesting that the gender of the internal auditor who communicates with management does not affect managers' perceptions of the auditor or the report. Thus, we do not find support for *H3a* and *H3b*[11].

As illustrated in [Figure 2](#), the path between managers' perceptions of the audit report quality and their agreement with the auditor's recommendations is not statistically significant ( $p = 0.212$ ), failing to provide support for *H4a*. However, managers' perceptions of report quality significantly influence the number of recommendations managers are willing to implement to correct the audit finding ( $p < 0.001$ , coef = 0.315) and managers' agreement with the negative impact of the audit finding on the company ( $p = 0.076$ , coef = -0.159), supporting our *H4b* and *H4c*. When we specifically examine the sign of the path coefficient, we find that as managers' perceptions of the quality of the audit report increase (i.e. more useful report), managers are willing to implement more of the auditor's recommendations.

In our model displayed on [Figure 2](#), we find support for *H5a*, *H5b* and *H5c*. Managers' perceptions of internal auditor's competence and independence significantly influence managers' willingness to implement auditor's recommendations ( $p = 0.09$ , coef = -0.126), agreement with the recommendations ( $p < 0.001$ , coef = 0.408) and agreement that the auditor's finding could negatively impact the company ( $p = 0.004$ , coef = 0.259). More specifically, these results suggest that as managers perceived the auditor as more competent and independent, managers agreed more with the auditor's recommendations.

## Discussion and conclusion

### Overview of results

Motivated by the need for an empirical examination of managerial perceptions of internal auditor communications, this study examines the potential determinants of management's agreement with internal auditor recommendations of an interim assurance engagement. Internal auditor interim communications highlight issues that require corrective action that may not be perceived favorably by managers who are tasked with mitigating the issues. Managers can be reluctant to agree to the internal auditor's recommendations. Thus, it is important to provide evidence on the factors that could improve management's perceptions of internal auditors' work.

The results of this study suggest that internal auditors should consider including the reason of the audit findings and observations in their interim report to improve their communication with management. Further, prior research has documented concerns of gender imbalance in the internal audit profession. This study, however, finds that the gender of the internal auditor communicating with management does not affect managers' perceptions of the auditor or the audit report quality, suggesting that a gender bias is not at play either consciously or subconsciously.

Internal auditors should also consider the mode of their communications. This study finds that managers who read the interim audit report as an e-mail perceived the report as more useful, clear and professional than when the report was provided to them via videoconference and were willing to implement more of the auditor's recommendations. Additionally, our results suggest that when the internal auditor delivered the report via e-mail, managers perceived the auditor as more competent and independent than when the report was provided in an e-mail format (over videoconference)[12]. Further, when managers perceived the auditor as more competent, they agreed more with the auditor's recommendations for remediating the issue identified by the audit.

*Implications*

The findings of this study can help organizations, such as the IIA, to better understand how to address the needs of those who communicate with internal auditors. Our findings suggest that inclusion of the root cause of an identified deficiency should be included in the internal audit report to improve the remediation of such deficiencies as recommended by the internal auditor.

Additionally, it is in internal auditors' best interest to maximize the effectiveness of their communications with others within the organization. Good communication is critical to success, but what defines communication to be "good"? Our study sheds light on how communication can be better received by management, demonstrating practical implications for internal auditors who can tailor their communications with management to better achieve their objectives. In addition to the benefit of providing a root cause in the internal audit report, it is also beneficial for internal auditors to communicate their findings via e-mail as this mode of communication results in improved management perceptions of the internal auditor's competence, independence and credibility relative to videoconferencing. This boost in management perceptions of the quality of the internal auditor can in turn improve management agreement with the internal auditor as well as the implementation of recommended remediation strategies.

Finally, improving the effectiveness of internal audit communications can only serve to help companies, especially those that have independent audits performed annually. If internal auditors are able to get management to correct identified deficiencies prior to annual external audits, companies could reap the benefits of lower external audit fees because of potentially lower assessed control risk. The implications of better internal audit communication, therefore, are not limited to the organization itself, but rather, are wide-ranging.

**Notes**

1. An intellective task "is a problem-solving task in which an evidently correct answer needs to be invented, selected, or computed, and then agreed upon" (Soo Suh, 1999, p. 296).
2. To keep our experiment concise, we did not provide participants with information on prior interactions with the internal auditor. Though this design decision may have impaired external validity, we believe it has resulted in a more internally valid instrument.
3. To improve both internal and external validity, we included an image of the female or male internal auditor in the e-mail above the "To:" and "From:" lines. The image was a screenshot from the videoconference participants in the other conditions viewed. Internal validity is improved because the salience of the manipulation does not get lost in the text. In reality, management would be well aware of the gender of the internal auditor, given prior interactions. Furthermore, including an image of the internal auditor improves external validity because many individuals have an image associated with their work e-mail addresses.
4. The difference in time spent on the manipulation page is an inherent limitation to our experimental design. However, the inclusion of time spent on the page as a covariate in our path analysis reveals that time differences do not impact our results. The time spent in seconds on the page with the manipulations for each experimental condition is as follows: 1) e-mail/no root cause/male: 121.52, 2) videoconferencing/no root cause/male: 153.49, 3) e-mail/root cause/male: 120.70, 4) videoconferencing/root cause/male: 232.69, 5) e-mail/no root cause/female: 113.56, 6) e-mail/root cause/female: 130.32, 7) videoconferencing/no root cause/female: 181.29 and 8) videoconferencing/root cause/female: 186.49.
5. We have created our two quality constructs based on measurements from prior research; however, we modified our measurements to fit the purpose of our study. The Internal Institute of

Auditors specifies that the communication between internal auditors and management should consist of quality characteristics such as accuracy, objectivity, conciseness, constructiveness and completeness (IIA 2012). Thus, we measure the report quality based on understandability, clarity, usefulness, professionalism and detail. We based our measurements of the internal auditor quality construct (i.e. competence, independence and objectivity) on the Desai *et al.* (2011) model of the strength of the internal audit function.

6. Though asked after our dependent variable questions (*AgreeImpact*, *AgreeRecom*, *NumberRecom*), we acknowledge as an experimental design limitation that the manipulation check questions were asked before other questions in the post-experimental questionnaire included in our path analysis.
7. Only 49 participants did not have or did not know if they had a current internal audit department and did not read a report. We re-performed the PLS analysis, excluding those 49 participants. Our results are robust, as there were no changes in the significance of the path coefficients of our model. Thus, we chose to include these 49 participants in our final data set.
8. Only two participants indicated that they did not wish to implement any of the recommendations. Of the participants, 97 per cent indicated they would implement recommendations sooner rather than later, with 53.8 per cent of all participants indicating the desire to implement the recommendations immediately. Of the participants, 86 per cent (11.2 per cent) indicated they were able to assess the internal audit report quickly (in an average amount of time). Thus, a total of 97.2 per cent of participants were able to assess the internal audit report in an average amount of time or quicker. Only 2.8 per cent of the participants indicated either slightly slow or extremely slow assessment of the internal audit report.
9. Unless otherwise noted, the *p*-values are two-tailed.
10. Cohen's  $f^2$  is calculated for all significant paths in the model. The largest effect size is for the internal auditor quality to AgreeRecom path (0.138). All other effect size measurements are between 0.01 and 0.076, indicating a small effect size.
11. We also conducted a multi-group analysis matching the gender of the participant with the gender of the auditor-actor in the experiment. We found no statistically significant differences in the path-coefficients for male vs female participants. Thus, it does not appear to matter whether the manager participant was female or male and exposed to a female or male internal auditor.
12. A total of 18 participants (8.4 per cent) indicated the use of videoconferencing by their internal audit function to communicate with management, showing that some respondents have had a first-hand experience using videoconferencing tools to communicate with their internal auditors. As technology becomes more available and easy to use in the future, we expect that the use of these communication tools will increase.

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#### Appendix. Part of Experimental Materials

**Condition 2 - Male/Video/Root Cause**

Please assume the role of a manager. You have received a Skype web-conferencing call from the Chief Audit Executive of your company's Internal Audit Department, Thomas Smith. The Chief Audit Executive provides you with the following Internal Audit Report for this year's first quarter. (Click on the video to play)



### Experimental Condition - Female/Email/Root Cause

Please assume the role of a manager. You have received an email from the Chief Audit Executive of your company's Internal Audit Department, Tiffany Smith. The Chief Audit Executive provides you with the following Internal Audit Report for this year's first quarter.



**From:** Tiffany Smith  
**Sent:** Tuesday, April 3, 2017 10:09 AM  
**To:** Company Manager  
**Subject:** Observation from Q1 2017 Internal Audit

Hello,

I hope you are doing well. While auditing accounts payable this quarter, Internal Audit made an observation we think needs to be brought to your attention.

**OBSERVATION:**

3 of the 5 accounts payable check requests tested (60%) totaling \$125,000 did not have the proper approvals prior to disbursement. Company policy requires checks over \$25,000 to have 2 approvals. One approval must be at a Vice President level or higher; however, these checks contained only one approval at the manager level. Internal Audit reviewed the support for each of the checks in question and found them to be legitimate charges.

**EFFECT/IMPACT:**

The effect or impact of failure to properly review and approve check requests is that it could result in fraudulent disbursements, negatively impacting the financial position and reputation of the Company.

**ROOT CAUSE:**

So, what is the root cause of this observation? Although all Company policies are available on the Company's intranet accessible to all employees, the staff processing the payments indicated they were not aware of the approval policy and were never informed about policies applicable to their job during their training.

**RECOMMENDATIONS:**

As a result, we recommend that your department performs the following:

1. Review all checks over \$25,000 to ensure payments are made for legitimate corporate expenses based on supporting documentation, including that appropriate approvals are obtained.
2. Establish a formal training program within the department to ensure staff can properly execute their job responsibilities.
3. To ensure employees in all areas of the Company are aware of current policies, we also recommend that periodic reminders be sent directly to employees reminding them of the location of the policies, particularly when policies are revised.

Shortly, you'll receive a brief survey questionnaire asking for your response to recommendations.

Thanks for your time.

Best, Tiffany Smith  
Director of Internal Audit

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