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Review

Perceptions on the role of the internal audit function in respect of risk

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This research investigated the perceptions of chief executive officers, chief financial officers or chief operating officers, as well as chairpersons of the audit committees of the top listed companies in South Africa on the role of the internal audit function in respect of risk. These perceptions were compared with the views of chief audit executives. Data was obtained by means of personal interviews with the senior management and the chairpersons of the audit committees and by means of electronic questionnaires issued to the chief audit executives. Some interesting conclusions made are that communication regarding risk issues is lacking. Although the internal audit function's role is perceived as positive, the views of senior management and those of the chairpersons of the audit committees differ substantially. It is further concluded that these two parties expect an increase in internal auditing's involvement in risk-related issues. Senior management and audit committees can benefit by evaluating their organisations' risk maturities as compared to the top listed companies' risk management frameworks. Internal auditors can use the data to suggest improvements where needed as stipulated in the Standards of the Institute of Internal Auditors.

Key words: Internal audit function, internal audit risk assurance, internal audit risk assessment, risk-based internal audit engagement.

INTRODUCTION AND RESEARCH PROBLEM

Risk and its effective management is not a new phenomenon as is evident from the following statement made by President John F. Kennedy in the 1960s (IIA, 2009b): "There are risks and costs to a program of action. But they are far less than the long-range risks and costs of comfortable inaction."

Formalised risk management frameworks have been recognised by many as an effective tool in assisting management in running the company better. This formalised risk management is commonly referred to as corporate governance. In the last few decades, the incorporation of enterprise risk management into the business environment has grown as a result of many new developments, such as its inclusion in various corporate governance codes world-wide and the fact that it has come to be viewed as one of the cornerstones of sound corporate governance principles (IOD, 2009); the link between corporate scandals and risk management, for example, the recent credit crunch (Financial Stability Forum and Institute of International Finance sited in Baker, 2008:34; World Economic Forum sited in Lam, 2009:22); investors' requirements and the positive effect that risk management has on business performance (Moody, 2006:40; Standards and Poor's sited in Puccia, 2007; Lam, 2009: 24); and the numerous benefits it holds for the company (Beasley et al., 2008: 47; Storey, 2009: 42) such as the coordination of all efforts within the company to manage risks, the alignment of all terminologies and methodologies used, and managing risk on a proactive basis.

The above factors have forced management to revisit the roles and responsibilities of various parties related to risk managements (Merna and Al-Thani, 2005: 53; Gendron et al., 2007:105). One of these parties is the

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Abbreviations: CAC; Chairperson of the audit committee, **CAE**; Chief audit executive (head of the internal audit function); **CE**; Chief executive; **CEO**; Chief executive officer, **CFO**; Chief financial officer; **COO**; Chief operating officer; **IIA**; Institute of Internal Auditors, **IAF**; Internal audit function.

Internal Audit Function (IAF). At the same time the internal audit profession has realised that it will have to adapt to the changing environment in which it operates as reflected in a statement made by (PWC, 2008b) after a study performed on the perceived status of internal auditing in 2012 concludes:

> "The rapid growth of the profession and the many changes in the business environment makes it essential for the internal audit profession to adopt new mindsets if it wants to remain a role-player in the future."

As this is a new and dynamic field for the business environment, not much information is available on what is expected from the IAF with regard to enterprise risk management. Furthermore, it is uncertain whether the board and senior management are aware of what the potential role and function of internal auditing could be to assist in fulfilling their responsibilities. This paper investigates the perceptions of senior management, including the audit committee, on the role and responsibilities of internal auditing as well as the value that internal auditing add to the concept of enterprise risk management. These perceptions are compared with the activities currently performed by the IAF, as well as what the Standards of the Institute of Internal Auditors (IIA) expect from internal auditors.

Parties that should benefit from this study include role-players in the risk management framework, namely the board (including the audit committee) as overall responsible party, senior management as the day-to-day implementation coordinators, and the IAF as assurance providers. The study focuses mainly on the implementation of a risk management framework and determines where the top listed companies in South Africa stand with this process. Organisations can thus compare their current statuses and identify further areas for improvement.

LITERATURE REVIEW

According to corporate governance guidance (COSO, 2004: 83; AS/NZS, 2004: 27; Spencer, 2005: 8-9; Atkinson, 2008: 42-45; IOD, 2009: 73-74), the responsebility for risk management lies with the board and senior management. Many companies implement a board risk committee to assist with this task (PWC, 2006:34-35; PRMIA, 2008; IIA Research Foundation, 2009b: 50). A further tendency is to set up a separate risk department and/or a chief risk officer to assist with this task (Beasley et al., 2005: 529; De la Rosa, 2007; PRMIA, 2008: 13; Hettinger, 2009: 49). This leaves the IAF independent to provide the board with assurance on the risk management framework and process.

The definition of internal auditing, being the cornerstone of the profession, is the ideal means to explain the evolution of the profession and its modern trends. One of the changes included in the current and relatively new definition (since 1999) is the activity to evaluate and improve the effectiveness of risk management (IIA, 2009a: 2). This reference in the definition to risk management has led to a change in how internal audit activities are performed. The Standards and Practice Advisories of the IIA (2009a) address three specific areas where the internal auditor should play such a role and incorporate risk into their activities.

Risk management framework and process

According to Standard 2120 (IIA, 2009a: 28-29) the IAF must evaluate the effectiveness of the risk management process. According to Practice Advisory 2120-1 (IIA, 2009a: 107-110) and a position paper (IIA, 2004), the ideal role for internal auditing is to verify the adequacy and effectiveness of the risk management process(es); that is verify whether management has planned and designed the process in such a manner that it provides reasonable assurance that the company's objectives and goals will be achieved. The activities can be divided into core activities (such as providing assurance on the risk management process, providing assurance that risks are evaluated correctly, evaluating the risk management process, evaluating the reporting of key risks, and reviewing the management of key risks); legitimate activities that may be performed with certain safeguards (refers to consulting activities that the internal auditor may undertake); and activities that are not appropriate to the IAF's role (such as taking responsibility for risk management). The extent of the involvement of internal auditing will be determined by the expectations that the board and senior management have of the IAF as well as the risk maturity of the company. Internal audit involvement may vary from no role, to auditing the risk management process, to actively and on a continuous basis being involved, or to managing and coordinating the process. No mention is made of the overall risk management framework.

Studies exploring the role of internal auditing with regard to risk management (McNamee and Selim, 1998: 13; Spira and Page, 2003: 656-657; Allegrini and D'Onza, 2003:198-199; Baker, 2004: 17; Beasley et al., 2005; Sarens and De Beelde, 2006: 73- 75; Gramling and Myers, 2006: 52-58; Roffia, 2007: 9; Fraser and Henry, 2007: 403; Deloitte and IIA (UK and Ireland), 2008: 8; PWC, 2008a: 9; Ernst and Young, 2008: 5-6; IIA Research Foundation, 2009a: 9) all indicate the growth of the implementation of risk management by companies. The studies also indicate that there is an increasing demand for internal auditing to be involved in risk management. This involvement varies from taking responsibility for the risk management process (not allowed according to the guidance of the IIA above), to auditing the risk management process as part of the internal audit plan, to actively and continuously supporting and being involved in the risk management process in a consulting role. The latter involves participation in risk committees, monitoring activities, status reporting, and managing and coordinating the risk management process. However, most studies do not refer to internal auditing providing assurance on the overall risk management framework, except for the recent study published by the IIA Research Foundation (2009a) on the trends for the profession in 2009 and beyond. In this study, the audit universe (IIA Research Foundation, 2009a: 9-10) includes the overall effectiveness of risk management within the company's risk environment, referring to both the risk management framework and the risk management process.

IAF's annual plan based on risk (also referred to as internal audit risk assessment)

The audit universe (Spencer, 2006:114-115; IIA, 2009a: 93) is a list of all possible auditable engagements that could be performed within a company and includes both strategic and operational activities. It is usually impossible to perform all these engagements due to a restriction of resources. Therefore, according to Standard 2010 (IIA, 2009a: 25-26) and Practice Advisory 2010-1 (IIA, 2009a:93-94), the chief audit executive (CAE) should base the IAF's annual plan on a risk assessment that is performed at least annually. One of the factors influencing this risk assessment is the outcome of the risk management process, ensuring that the most important auditable areas within the audit universe are focused upon.

It seems that more IAFs are using risk methodologies to plan their activities (Allegrini and D'Onza, 2003; PWC, 2008a: 16) and that this tendency is growing (PWC, 2008b:31). Studies indicate that the use of the output of the risk management process (management's responsibility to identify high-risk areas) in the internal audit annual plan is not consistent. Some provide evidence (Ernst and Young, 2007: 10; PWC, 2007: 12; PWC, 2008a:18) that it is used to guide the planning of the IAF's activities, while others (Allegrini and D'Onza, 2003: 197; McCuaig, 2006: 4; Arena et al., 2006: 287; Sarens and De Beelde, 2006: 76) indicate that companies do not use this valuable source of information. A possible result linked to this is that CAEs world-wide (Ernst and Young, 2007: 10) indicated that they struggle to complete the internal audit annual plan due to various reasons (only 21% completed the entire internal audit annual plan and 24% completed up to 80%), one of these reasons being that the annual plan is not focused on the crucial issues identified by management. PWC (2008a: 3,16-18) highlights the importance of internal auditing focusing on strategic, operational and business risks in addition to financial and compliance risks as 80% of loss in external shareholders' value in Fortune 500 companies could be linked to the first set of risks. In spite of these statistics showing the importance of the risk management process outcome to effective internal audit planning, only 24% of CAEs indicated that their IAFs' annual plans are linked to the outcome of the process (Ernst and Young, 2007: 10).

Risk-based internal audit engagements

According to Standards 2200, 2201, 2210.A1 (IIA, 2009a: 31-32), when planning an internal audit engagement internal auditors must consider the significant risks to the activity under review, as well as the adequacy and effectiveness of the risk management process(es) that resides within the scope of the engagement. Practice Advisory 2210.A1-1 (IIA, 2009a: 125-126) elaborates on this by identifying that the internal auditor should consider management's risk assessment performed on the activity under review and if needed, perform an additional survey to obtain information on the activities, risks and controls.

After a comprehensive search, it seems that not much research information is available on the performance of a risk-based internal audit engagement. According to Allegrini and D'Onza (2003: 198) most internal auditors still perceive the identification of risks when planning the audit engagement as relatively unimportant (only 67% of the respondents perform some form of risk-based internal audit engagements) as they still follow the control paradigm. The study performed by PWC (2008a:4-5) suggests that audit committees are setting higher performance standards for internal auditing. These include shorter audit cycle times (from the commencement to completion of an audit engagement) due to the rapid changes within the business environment. To focus on mainly the high-risk areas within a specific engagement should shorten the audit cycle time as fewer audit procedures will be performed (for example, low-risk areas could be excluded). A study performed by Deloitte (2005: 9) amongst 800 executive members on the state of their companies' control programme confirms the need to move to a risk-based internal audit engagement approach. With regard to the control programme in their respective companies, 56.3% indicated that over-controlling on routine areas is a huge cause for concern, 29.1% indicated insufficient controls in high risk areas and 32.2% indicated insufficient focus on high risk areas in audit programmes. Only 13.9% indicated that their control programmes are lean and balanced.

RESEARCH METHODOLOGY

As this journal is a special edition focusing on the study performed on the standing of and demand for internal auditing in South African companies, the process followed to gather the information is explained in the foreword. Note that the population is the top 40 listed companies on the South African stock exchange, with a sample of 30 of these companies. Further cross analyses have been performed on the data, focusing on the three areas as discussed in the literature study. More emphasis is placed on the risk management framework and process. The reason being that

Table 1. CE and CAC respondents - Extent of contribution to the risk management process.

Party involved	Contribution to management of risk										Mean	
	1 None		2 Limited		3 Average		4 Above average		5 Significant			
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC
Audit committee	0	0	0	4	1	5	7	14	18	6	4.7	3.8
External auditors	0	0	0	2	1	11	11	9	18	2	4.6	3.5
In-house IAF	0	0	0	1	5	5	15	11	5	9	4.0	4.1
Outsourced IAF	0	0	2	0	4	5	2	1	6	2	3.9	3.6
Board of Directors	0	0	3	5	7	6	16	12	4	7	3.7	3.7
Management	0	0	3	0	13	4	8	12	6	14	3.6	4.3
Designated risk management division	0	0	3	0	4	0	5	8	0	19	3.2	4.7
Specialist risk consultant	0	0	6	0	11	3	7	10	1	6	3.1	4.2

these functions reflect directly on the risk maturity of the company as incorporated in many risk maturity models such as the one issued by the Risk and Insurance Management Society (RIMS, 2006). The risk maturity of a company could be a hampering factor with regard to the nature of internal audit services if the company is not on an acceptable level. Therefore, the extent of involvement of the IAF in the management of risk in the company is highly dependent on the risk maturity of the company.

DATA ANALYSIS AND FINDINGS

In this section data gathered by means of interviews and questionnaires are analysed. The parties involved are firstly either the chief executive officer (CEO) or chief financial officer (CFO) or chief operating officer (COO) - hereafter referred to as the chief executive (CE), secondly the chairperson of the audit committee (CAC), and lastly the CAE.

Risk management framework and process

This section focuses on the following areas:

(i) A brief overview of the utilisation of certain parties within the risk management framework.
(ii) The perceptions of the CE and CAC on the contribution of various parties to the success of the risk management process, risk management framework and risk communication.
(iii)The perceptions of the CE and CAC on the value added by the IAF to the comprehensive risk management framework.
(iv) The perceptions of the CE and CAC on the assurance provided by the IAF on the risk management process.
(v) The perceptions of the CE and CAC on the contribution made by the IAF to mitigating the top risks of the company.
(vi) The perceptions of the CAE on the services provided related to risk by the IAF.

When asked whether their companies have a separate board risk committee and chief risk officer, 90% of CE respondents indicated that these are in place. However, only 63.3% of CAC respondents indicated that their companies have a separate board risk committee even though both the risk committee and the audit committee are part of the board. It is thus clear that CEs do not necessarily have the same view as their CACs as to the existence of this role-player. Of the CE respondents 76.7% perceived their in-house IAFs as forming part of the risk management framework of their companies while 36.7% believed outsourced IAFs fulfilled this role. 85.7% of the CE respondents indicated that their companies have a separate risk management division that operates independently of their IAFs. Only 7% of these respondents were of the opinion that such risk management divisions decrease the importance of the IAF in risk management.

The CE and CAC respondents were requested to rate the involvement of various parties in the risk management process, that is the identifying and measuring of the impact and likelihood of significant risks (Table 1) on a scale ranging from no contribution to significant contribution. The CE respondents perceived the contribution made to this process in their companies by the audit committees (mean 4.7) as being the highest and that of a specialist risk consultant (mean 3.1) as the lowest. The CAC respondents in turn perceived the contribution of a designated risk management function as most valuable (mean 4.7) and the contribution of external auditors as the least valuable (mean 3.5). The contribution made by in-house IAFs was perceived as significant by both parties. This could be as a result of the in-house IAF being present on a full-time basis as part of the company; thus being more readily available to assist senior management and the audit committee, and that the in-house IAF probably has a greater understanding of the operations and risks threatening the company.

It is slightly concerning that the CEs' and CACs' mean perceptions of the various contributions, although both

Table 2. CE and CAC respondents - Extent of contribution to risk management framework.

Party involved	Contribution to management of risk										Mean	
	1 None		2 Limited		3 Average		4 Above average		5 Significant			
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC
Audit committee	2	0	3	3	8	11	14	7	3	7	3.4	3.6
External auditors	5	0	11	7	6	4	7	6	1	2	2.6	3.2
In-house IAF	1	0	2	1	3	3	11	10	8	8	3.9	4.1
Outsourced IAF	1	0	2	1	5	2	5	5	0	3	3.1	3.9
Board of Directors	1	0	4	7	10	6	10	8	5	7	3.5	3.5
Management	0	0	0	0	0	2	12	13	18	15	4.6	4.4
Designated risk management division	0	0	0	0	1	0	7	7	18	21	4.7	4.8
Specialist risk consultant	0	0	3	0	3	6	3	6	5	8	3.7	4.1

high differ. According to the literature, including corporate governance codes such as the King Report (2002 and 2009), the perceptions of the CAC respondents are more in line with current practices as those of the CE respondents, for example the contributions of the audit committee, external auditors, management and designated risk management division. However, the perceptions as to the contributions made to risk management by the board of directors and the IAF are closely related and, being that the King Report (IOD 2002) makes the board of directors responsible for the risk management process, the fact that the in-house IAF received such a consistent high rating is reassuring.

In respect of the risk management framework, that is the designing, operating and monitoring of an appropriate risk management strategy (Table 2), the designated risk management division was perceived by the CE and CAC respondents as making the most valuable contribution (mean 4.7 and 4.8 respectively). External auditors are perceived to make the least contribution (mean 2.6 and 3.2 respectively) to the framework. In both instances the CE and CAC respondents indicated that the contribution of the in-house IAFs (mean 3.9 and 4.1 respectively) is of more value in risk management than the contribution of the outsourced IAFs (mean 3.1 and 3.9 respectively). This corresponds with best practice as indicated by various corporate governance codes (refer to the King Report – IOD 2009:75-76) where management is responsible for the day-to-day implementation of risk management and could implement a risk management division to perform these tasks.

The level of contribution made to risk communication (that is the reporting of information on risk systems and processes, for example, maintaining a risk database containing the output of the risk management process) is reflected in Table 3. Both CE and CAC respondents indicated a mean of 4.7 for the value of the contribution made by a designated risk management function. In their opinion the external auditors make the least contribution (mean 2.7 and 2.8, respectively). In-house IAFs are perceived as making an average to above-average contribution while outsourced IAFs contribute on a limited to average level to risk communication.

CE and CAC respondents were requested to rate (from 1 – significant value, to 4 – no value, and 5 – not applicable) the current and expected future value added by the IAFs (Table 4). The results reflect either an increase in expected future value (as indicated in the increase in significant to moderate statistics), or for certain companies, that no current value was occurring and the CE and CAC did not expect a future value (as indicated in the consistence of no value/not applicable ratings). It seems that the CACs and CEs expected in-house IAFs to provide greater value-adding than outsourced IAFs (both current and future value adding). When focusing on the current value, the CEs had a lower perception of the contribution of the in-house IAF than that of the CACs. This is difficult to explain as it is expected that CEs work closely with their in-house IAFs.

Table 5 provides an illustration of the perceptions of CE respondents as to whether their IAFs provide assurance in respect of the risk management process. Of the 30 respondents 67% indicated that the in-house IAF provides assurance on the risk management process while 27% of the respondents were of the view that outsourced IAFs provide such assurance. The ‘not applicable’ results refer to certain companies having no in-house or outsourced functions and others using co-sourcing, thus having an in-house function but out-sourcing certain activities. The remaining two companies (making up almost 7% of the sample) have IAFs that do not provide any assurance on the risk management process. This is not in line with a moderate to high risk maturity level (RIMS 2006) as well as the new King Report recommendations (IOD 2009: 80), and should be addressed accordingly.

Respondents were requested to list the five most important risks to their respective companies and rank each one according to a 5-point scale (1 - no contribution, to 5 - significant contribution). The CE and CAC were

Table 3. CE and CAC respondents – Extent of contribution to risk communication.

Party involved	Contribution to management of risk										Mean	
	1		2		3		4		5			
	None		Limited		Average		Above average		Significant			
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC
Audit committee	4	3	3	1	8	8	13	8	2	8	3.2	3.6
External auditors	5	4	8	9	8	7	6	6	2	2	2.7	2.8
In-house IAF	3	1	2	3	1	4	14	9	6	9	3.7	3.8
Outsourced IAF	2	1	5	2	3	5	3	2	0	2	2.5	3.2
Management	0	0	0	1	5	4	15	10	10	15	4.2	4.3
Designated risk management function	0	0	0	0	0	1	8	6	18	20	4.7	4.7
Specialist risk consultant	1	0	5	3	3	3	1	6	3	5	3.0	3.8

Table 4. CE and CAC respondents – Current and expected value added by in-house and outsourced IAFs.

Value added	CE				CAC			
	Current		Expected		Current		Expected	
In-house/Outsource	**IH (%)**	**OS (%)**	**IH (%)**	**OS (%)**	**IH (%)**	**OS (%)**	**IH (%)**	**OS (%)**
Significant/moderate	66.7	33.3	76.6	43.3	76.6	16.7	80.0	33.3
Limited	10.0	13.3	0	6.7	13.3	16.7	6.7	6.7
No value/not applicable	23.3	53.3	23.3	50.0	10.0	66.7	13.3	60.0
Total	100	100	100	100	100	100	100	100

Table 5. CE – The IAF provides assurance on the risk management process.

	Yes		No		N/A		Total	
In-house IAFs	20	67%	4	13%	6	20%	30	100%
Outsourced IAFs	8	27%	5	17%	17	57%	30	100%
Total providing assurance	28							

respondents listed a total of 203 risks. The 203 risks were categorised into the following seven risk areas:

(i) Finance;
(ii) Fraud;
(iii) Information technology (IT) related;
(iv) Operations;
(v) People;
(vi) Strategic; and
(vii) Other.

The number of responses per risk category, as indicated in Table 6, shows the number of times a specific risk category was chosen under each of the ratings. The risk category that was mentioned most by the CE and CAC respondents were the finance category (mean 1.67 and 1.27, respectively). The risk category chosen the least number of times was the fraud category (mean 0.04 and 0.13, respectively).

Table 7 illustrates the relative importance of the risks within a specific category. The CEs and CACs perceived the finance category as being the greatest risk (mean 3.5 and 2.7 respectively) to their companies and the fraud category as the least risk (mean 0.04 and 0.3 respectively). Tables 8 and 9 illustrate the responses of the CE and CAC respondents with regard to the contribution made by the in-house and outsourced IAF of their respective companies to mitigating these risks. When considering the mean of the responses, both the CE and CAC respondents were of the opinion that in-house IAFs make the most valuable contribution (mean 4.00 and 4.33 respectively) to the management of fraud-related risks. The perceptions of the CE respondents in respect of the outsourced IAFs revealed that the most valuable contribution is made in respect of the finance category (mean 3.80). CAC respondents were of the opinion that out-

Table 6. CE versus CAC - Number of responses per risk category.

Risk category	Contribution to management of risk										Mean	
	None		Limited		Average		Significant		Total			
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE*	CAC	CE	CAC
Finance	5	10	6	5	9	12	7	3	27	30	1.67	1.27
Fraud	7	10	9	13	11	7	0	0	27	30	0.04	0.13
IT-related	14	18	9	8	4	4	0	0	27	30	0.30	0.30
Operations	18	20	8	7	1	3	0	0	27	30	0.37	0.43
People	26	27	1	2	0	1	0	0	27	30	1.15	0.90
Strategic	19	23	8	5	0	2	0	0	27	30	0.63	0.53
Other	15	20	7	7	5	3	0	0	27	30	0.63	0.43

Note: Rating 4 - above average, was not chosen by any respondents for any of the risk categories. ***** Sample loss = 3.

Table 7. CE versus CAC - Importance of risk categories.

Risk category	Not mentioned		5^{th} (least)		4^{th}		3rd		2nd		1^{st} (most)		Total		Mean	
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE*	CAC	CE	CAC
Finance	5	10	0	1	3	0	1	4	5	7	13	8	27	30	3.5	2.7
Fraud	26	27	1	0	0	1	0	1	0	0	0	1	27	30	0.04	0.3
IT-related	19	23	4	2	1	0	2	4	1	0	0	1	27	30	0.6	0.6
Operations	15	20	3	2	0	0	1	1	3	5	5	2	27	30	1.6	1.2
People	14	18	2	1	5	1	1	6	1	1	4	3	27	30	1.4	1.3
Strategic	7	10	0	1	4	2	5	5	8	4	3	8	27	30	2.6	2.5
Other	18	20	1	1	3	2	2	0	1	4	2	3	27	30	1.0	1.2

*****Sample loss = 3

Table 8. CE and CAC – Contribution of in-house IAFs to top risk categories.

Risk category	Contribution to management of risk												Mean	
	None		Limited		Average		Above average		Significant		Total			
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC
Finance	6	5	5	3	2	4	4	5	0	2	17	19	2.24	2.79
Fraud	0	0	0	0	0	0	1	2	0	1	1	3	4.00	4.33
IT-related	2	1	0	0	2	2	0	0	4	1	8	4	3.50	3.00
Operations	3	5	1	0	3	2	1	0	4	2	12	9	3.17	2.33
People	3	5	3	1	5	2	2	1	0	1	13	10	2.46	2.20
Strategic	5	3	3	2	3	6	5	7	2	0	18	18	2.78	2.94
Other	2	5	0	1	4	0	1	3	1	0	8	9	2.88	2.11

sourced IAFs make the most valuable contribution to risk management in respect of fraud-related risks (mean 2.33). The perceptions of the CE and CAC respondents of the in-house IAFs (Table 8) reveal similar views; whereas this is not the case with their perceptions on the outsourced IAFs (Table 9). For example, for the risk category finance, the perceptions are respectively 2.24 and 2.79 for the in-house IAFs, but differ substantially for the outsourced IAFs with respective means of mean are 3.8 and 1.47.

Tables 6 to 9 above indicate that according to the perceptions of the CEs and CACs, the IAF is not in the ideal position to assist with the mitigation of the top risk area, namely finance. However, the respondents believed that the in-house IAF can contribute significantly to the mitigation of fraud and IT-related risks. Furthermore, the perception was that the in- house IAF can contribute more to the mitigation of the top risks than the outsourced IAF, probably due to the fact that the in-house team are part of the company structure and thus understand the operations

Table 9. CE and CAC – Contribution of outsourced IAFs to top risk categories.

Risk Category	Contribution to management of risk												Mean	
	None		Limited		Average		Above average		Significant		Total			
	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC	CE	CAC
Finance	14	14	1	2	1	2	1	1	0	0	17	19	3.80	1.47
Fraud	0	2	0	0	1	0	0	0	0	1	1	3	0.60	2.33
IT-related	6	3	0	1	1	0	1	0	0	0	8	4	0.80	1.25
Operations	10	5	0	0	0	2	2	1	0	1	12	9	1.80	2.22
People	11	6	2	2	0	1	0	1	0	0	13	10	2.00	1.70
Strategic	15	11	2	1	1	4	0	1	0	1	18	18	3.60	1.89
Other	7	8	0	0	1	1	0	0	0	0	8	9	1.80	1.22

Table 10. CAE – Current and future risk-related services rendered/to be rendered by IAFs

Service area	Current		Future	
	No of respondents	(%)	No of respondents	(%)
Risk management	8	26.7	7	23.3
Risk assurance	12	40	30	100

Table 11. CAE – Descriptive statistics of internal audit services provided to the company (average annual hours) with regard to risk management.

	In-house				Outsourced			
	Current		Expected		Current		Expected	
	Framework	Process	Framework	Process	Framework	Process	Framework	Process
N	8	12	7	12	8	12	7	11
Mean	1183.8	2247.1	1302.7	2760.0	109.4	37.9	125.0	34.01
Standard Deviation	1056.9	3607.7	1441.4	4392.0	205.3	108.6	216.2	113.1
Minimum	150	100	200	200	80	375	375	375
Median	880	1003	500	1500	290	438	438	438
Maximum	3000	12800	4000	16000	500	375	500	375

N = Number of respondents.

and risks better.

The perceptions of the CAE respondents on the risk-related services that IAFs provide to the company are indicated in Table 10. The respondents indicated that currently 26.7% of IAFs are rendering services (probably consulting activities as indicated by the literature) related to the risk management framework and/or process and 40% render risk assurance services. The CAE respondents perceived the future risk management and risk assurance services rendered to change to 23.3% (decrease = 4%) and 100% (increase = 77%) respectively, being more in line with the guidance provided by the IIA (2004).

Table 11 provides descriptive statistics of the perceptions of the CAE respondents on the average annual hours spent on risk-related internal audit services provided to their companies. The table compares the time spent currently on the risk management framework and risk management process by in-house and outsourced IAFs (refer to the mean distribution). In-house IAFs were perceived to spend substantially more hours per annum on the risk management framework than outsourced resources. Furthermore, the CAEs expected that in-house IAFs will increase their involvement even further in the future.

IAF's annual plan based on risk

CAE respondents mostly perceived the incorporation of risks in the annual audit plan at a rating of above average to significant (93%). Only 7% of respondents chose a rating of average involvement. This is a much higher tendency than is revealed by global studies as reflected in the literature.

Risk-based internal audit engagements

A substantial majority of the CAE respondents indicated that internal audit engagements are performed with an emphasis on risk. The frequency distribution of the responses to two different questions addressing a risk-based approach when performing internal audit engagements revealed a perception that 93.1% of IAFs do follow a risk-based approach.

Conclusion

Both the risk committee and the audit committee are board committees. It is therefore a concern that CACs in some instances are unaware of the existence of a board risk committee in the company as indicated by the CE responses (90% compared to 63.3% of CAC responses). This concern is further substantiated by the fact that the contribution to risk communication is rated the lowest by both the CE and CAC respondents when compared with the risk management process and risk management framework (refer to Tables 1, 2 and 3). This raises a question as to the effectiveness of risk communication in general, and specifically risk communication between the audit committee and the risk committee. These two committees, one assisting the board with their responsibilities for the governance of risk (risk committee), and the other being responsible for providing assurance on risk (audit committee) should at least have some form of communication in order that they may effectively execute their duties.

With regard to the current and expected value that IAFs can add in respect of risk, the perceptions of the CE and CAC respondents is that the IAFs' future contributions should increase. This is an indication that the CEs and CACs expect greater utilisation in respect of risk of the IAF, which is evident of a higher status and level of acceptance of the function within the company. This supports the guidance in the third King Report (IOD, 2009:97) that stipulates that IAFs should enjoy the respect and cooperation of the board and management.

In light of changes in the global environment, such as the increase in corporate scandals, the demands as a result of changing technology, the scarcity of competent and skilled people in key positions, the increased competition due to globalisation, the global economic meltdown, to name but a few, it is concerning that both CEs and CACs rate finance as the most important risk category. Although not covered by the scope of this study, this raises the question whether CEs and even CACs have mostly financial backgrounds. This is further highlighted by the fact that CEs identified outsourced IAFs (mostly Big4 audit firms) as contributing the most to the mitigation of the finance risk category (refer to table 9 - Mean = 3.8).

According to 93% of the CE respondents the IAF is providing assurance on risk (Table 5). However, table 10 shows that only 40% of the CAEs agreed with this statement. This difference is inexplicable and raises the question as to whether the CE respondents have indicated that assurance is provided because they wish to prove adherence to governance principles or simply because they are uninformed.

The CAE respondents perceived that future internal audit activities performed with regard to risk will increase substantially. Whether this will occur is, however, another matter as a high number of ad hoc management requests as well as limited resources could prevent this from happening.

A last concern is the fact that there is a material difference between the perceptions of the CE and CAC respondents with regard to risk-related matters. This is best highlighted in Table 9 where differences in mean perceptions are material.

What is reassuring is the results of this study highlight that management regard internal auditing as an important component of the risk management framework. Furthermore, internal auditing is optimally utilising the incorporation of risk into their activities as is evident from the statistics on the incorporation of risks in IAFs' annual plans and internal audit engagements based on risk.

Further research should focus on the comparison of this South African scenario with global best practices. The public and private sectors in a South African as well as a global context should also be compared. Studies should specifically focus on the risk maturity levels of companies as this is an indicator of what is currently in place and assists in identifying further areas of improvement.

Terminology

Risk management(*): refers to the dynamic process and other structures in place to identify and deal with risks that impact certain objectives on a micro level, usually within a silo, for example, it will only focus on a business unit or process.

Enterprise risk management (*): refers to the extension of risk management across the company on a macro level by integrating all the risk management initiatives including strategic and operational levels.

Risk management process (*): the process that is used by management to identify, assess, treat, monitor and report risks. This is usually a structured and systematic set of tasks.

Risk management framework(*): the totality of the structures, processes, systems, methodologies, individuals involved, *et cetera*, that a company uses to implement its risk management strategy.

Risk assessment (*): the analysis, measurement and evaluation of each risk identified.

Risk maturity (*): provides role players with a way to combine all the various elements of a risk management framework to best suit the needs of their company. The more elements that are implemented and successfully executed, the more risk mature the company is. (*) As risk management is a relatively new field, its terminology differs widely from company to company - the definitions given here are specific to the context of this paper.

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