

THE CURRENT STATUS OF AND DEMAND FOR INTERNAL AUDITING IN SOUTH AFRICAN LISTED COMPANIES

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An investigation by

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PREFACE:

The purpose of this preface is to explain the target audience of the book and the reviewing procedure followed:

1 TARGET AUDIENCE

- The information gathered in this research can be utilised by the users of internal audit services such as chief executive officers (CEOs), audit committees, the heads of internal audit functions (chief audit executives) as well as the managers of internal audit functions to improve their understanding of:
 - the evolution in internal auditing to a value added function;
 - the role of the internal audit function in risk management and corporate governance;
 - the increased demand for a wide variety of internal audit services
 - a corresponding increase in the expected skills and qualifications held by internal auditors.;
 - the value added services rendered by the internal audit function; and
 - the training needs of the various levels of entrants into internal auditing
- The improved understanding of the increased competency requirements can be used by peers, such as higher education providers, the Institute of Internal Auditors South Africa (IIA (SA)) and providers of continuing professional development (CPD) programmes to improve their products and services.

2 REFEREEING PROCEDURE BY EXTERNAL PEERS

- The research was conducted by 8 academics from 5 South African universities and the research report was submitted to the IIA (SA) for publication.
- The double blind peer review process was administered by the Research Foundation of the IIA Inc.
- Detailed review reports and comments were submitted by the external reviewers.
- The IIA (SA) accepted the final research report for publication.
- The IIA (SA) published the final research report as follows:
 - Full report in hard copy; and
 - Summary on IIA (SA) website.

The above information is also highlighted in the subsequent publishing statement from the IIA (SA), the publisher of this book.

01 November, 2010

This is to confirm that the Institute of Internal Auditors South Africa (IIA SA) is the publisher of the research report entitled 'The Current Status of and Demand for Internal Auditing in South African Listed Companies.'

The research was conducted by the iKutu research team comprising academics from the Departments of Auditing at the following South African institutions: University of South Africa (UNISA), University of Pretoria, Nelson Mandela Metropolitan University, Monash University (South Africa) and Tshwane University of Technology. The research project was supported by the Bureau of Market Research and sponsored by the IIA SA and KPMG.

Three different questionnaires were used as data collection instruments. The questionnaires were developed and finalised after extensive literature reviews had been undertaken, discussions with stakeholders had been held and pilot testing had been done in South Africa. To collect the data, questionnaires were completed using a combination of face-to-face interviews conducted by members of the iKutu research team and self-administrated personal and web-based questionnaires via emails and facsimiles. These responses were collated and analysed.

The research was conducted on 30 large companies listed on the JSE Limited. The report contains the purpose of the study, including the significance of the research to various parties, the research objectives, the literature review underlining the research objectives, the research methodology that was applied, the findings of the research, and the resulting conclusions and recommendations.

The final report was reviewed by two academic peer reviewers who are members of the IIA Research Foundation's Board of Research and Academic Advisors. The IIA Research Foundation is a (501)(c)(3) tax-exempt corporation (in the United States of America), formed to provide and expand research and education for the benefit of the internal auditor, the internal audit profession, and business and government communities. The Foundation publishes research and educational products that provide internal audit practitioners with current information and guidance.

The IIA SA accepts the above processes employed and believe the findings to be a fair and accurate reflection of the research objectives.

The information gathered in this research will be utilised to:

- determine fundamental statistics and related information for the use in skills development plans in keeping with skills development and higher education legislation,
- determine the size of the market demand and future potential for internal auditors in South Africa. The majority of the stakeholders in the internal audit environment, namely the tertiary institutions, SETAs, employers and the IIA (SA) will benefit from this information;



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- effectively plan educational needs, training interventions, conferences and continuing professional development activities;
- plan the growth, as well as resourcing of internal audit activities;
- create a greater awareness in the public domain of the critical need for internal audit as a value adding discipline in improving businesses operational efficiency and governance;
- highlight the value of research as a significant contributor to the promotion of the internal audit profession in South Africa; and
- develop curriculum by tertiary institutions.



Dr Claudelle von Eck
Chief Executive Officer



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ABSTRACT

To date, limited research has been conducted on the practice of internal auditing in South Africa. This lack of research is partly due to the fact that, as an academic discipline, internal auditing is still in its infancy. The main reason for undertaking this investigation into the current status of and demand for internal auditing in South Africa was to address this research vacuum.

This investigation builds on the global survey that was conducted by the Institute of Internal Auditors Research Foundation (IIARF) in 2006 to establish a common body of knowledge (CBOK) of the internal auditing profession. This investigation expands on the CBOK study in that it is not limited to the members of the Institute of internal Auditors (IIA) but includes the views and perceptions of both the chief audit executives (CAEs) and the main users of internal audit services. These users include the chairpersons of audit committees (CACs) and chief executive officers (CEOs), chief financial officers (CFOs) or chief operating officers (COOs) of 30 listed participating companies in South Africa that have the largest market capitalisation and could serve as a benchmark for other companies.

The aim of this investigation was to determine the current status of and demand for internal auditing in South Africa as perceived by the above-mentioned participants in a sample of the leading listed companies in South Africa.

The views and perceptions of the participants were obtained by means of three different structured questionnaires. One questionnaire was developed for completion by the CAE, a second for completion by the CAC and a third for completion by the CEO, CFO or COO. In order to ensure that all industries are represented in the cohort of selected companies, the selection was stratified to include at least one company from each industry. Descriptive analysis was used to present the findings of the investigation. It is envisaged that the findings of this project could provide a benchmark for South African companies with regard to internal auditing and that this investigation could be replicated for similar and comparative studies in other countries, over time in South Africa on listed companies and on Public sector entities.

This investigation found that the internal audit functions (IAFs) have a fairly high status. The high status applies especially to in-house IAFs. It was also found that there is a demand for highly skilled internal auditors, especially female internal auditors from previously disadvantaged groups.

List of companies included in the research

The following companies were included in the research:

- 1 ABSA Group Ltd
- 2 African Bank Investments Ltd
- 3 African Rainbow Minerals Ltd
- 4 Anglo American Plc
- 5 AngloGold Ashanti Ltd
- 6 Anglo Platinum Ltd
- 7 Barloworld Ltd
- 8 Dimension Data Holdings Ltd
- 9 Discovery Holdings Ltd
- 10 Exxaro Resources Ltd
- 11 FirstRand Ltd
- 12 Gold Fields Ltd
- 13 Harmony Gold Mining Company Ltd
- 14 Impala Platinum Holdings Ltd
- 15 Investec Ltd
- 16 Kumba Iron Ore Ltd
- 17 Liberty Group Ltd
- 18 Massmart Holdings Ltd
- 19 Mittal Steel South Africa Ltd (ArcelorMittal South Africa Ltd)
- 20 MTN Group Ltd
- 21 Nedbank Ltd
- 22 Old Mutual Plc
- 23 SABMiller Plc
- 24 Sanlam Ltd
- 25 Santam Ltd
- 26 Sappi Ltd
- 27 Standard Bank Group Ltd
- 28 Steinhoff International Holdings Ltd
- 29 Telkom SA Ltd
- 30 The Bidvest Group Ltd

CHAPTER 1: INTRODUCTION AND BACKGROUND

1.1 INTRODUCTION

The internal audit function (IAF) is enjoying a level of prominence and attention unlike ever before (Carcello, Hermanson & Raghunandan 2005:118). Its role has evolved over time and given the significant changes organisations are facing, such as regulatory environment and new technologies, it is likely to be subjected to considerable changes in the future. Recent highly published corporate scandals, such as Enron, WorldCom, Parmalat and other companies have led to an intense focus on corporate governance, effective oversight and sound internal controls which further impacted the role of the IAF within an organisation. These changes resulted in expanded opportunities and challenges to the IAF, emphasising its role in corporate governance.

The increased recognition of internal auditors has resulted in the services of the IAF being expanded from essentially an accounting-orientated service, to a much broader management-orientated service. Recent demands by stakeholders of organisations for greater accountability from management, be it the board of directors, audit committee, executive management or other levels of management, will likely further augment the services of IAFs.

Despite all of the above, internal auditors in practice may be falling short of expectations. Previous research identified many concerns regarding the standing of internal auditors. Essentially, two key issues appear to be the professional status of the IAF within an organisation, and the demand for competent (skilled and knowledgeable) internal auditors.

During 2006, the Institute of Internal Auditors Research Foundation (IIARF) conducted a global survey in respect of the common body of knowledge (CBOK) of the internal audit profession (IIARF 2007). The CBOK study aimed to broaden the understanding of the practice of internal auditing throughout the world. The overall objective of the CBOK study was to develop a comprehensive database to capture a current view of the global state of the internal audit profession. The database includes information such as compliance with the Institute of Internal Auditors' (IIA) *International Standards for the Professional Practice of Internal Auditing* (hereafter referred to as *Standards*) and the state of the IAF world-wide, including staffing, skills and competencies required (IIARF 2007).

It is important to note that the CBOK study was based on and limited to the perceptions and views of the members of The IIA globally. This study obtained the views and perceptions of the members of the internal audit profession in South Africa as well as the users of the services of the IAF. The perceptions and views of the Chief Audit Executives (CAEs), Chairpersons of Audit Committees and the Chief Executive Officers (CEOs), Chief Financial Officers (CFOs) or

Chief Operations Officers (COOs) of the top listed companies in South Africa were obtained to determine the standing of and demand for internal auditing.

This research is the first phase of a comprehensive research study conducted by academics from the auditing departments of the University of Pretoria (UP), the University of South Africa (Unisa), the Tshwane University of Technology (TUT), Monash University – South Africa (MSA) and the Nelson Mandela Metropolitan University (NMMU), together with the Bureau of Market Research (BMR) at Unisa. The second phase of this study will be conducted on the standing of and demand for internal auditing in the South African public service.

The remainder of this research report discusses the purpose of the study, including the significance of the research to various parties as well the research objectives, the literature review underlining the research objectives, the research methodology that was applied, the findings of the research conducted, and the appropriate conclusions and recommendations.

1.2 PURPOSE OF THE STUDY

The main purpose of this study is to determine the standing of and demand for internal auditing within 30 large listed South African companies. In order to reach such a determination, this research report will consider

- Data on the profiles of the CAEs of the IAFs, and audit committees;
- The perceptions of the respondents or users of the functions and activities of the South African Institute of Internal Auditors (IIA (SA));
- The perceptions of the stakeholders on the IAFs' structure,
- The perceptions of the respondents on the IAFs' services rendered and approaches followed as well as the demand for services;
- The perceptions of the respondents on the IAFs' status,
- The perceptions of the respondents on the IAFs' role in respect of risk assessment and risk management;
- The perceptions of the respondents on the IAFs' role with regard to corporate governance and fraud; and
- The views of the respondents on the composition of the IAFs' staff complement and their perceptions on the demand for internal audit staff.

The objective of the research reported on here is twofold, namely to firstly determine the standing of internal auditing within 30 large listed South African companies and secondly to the demand for internal auditing. In order to reach the first objective the following contributing factors such as the profiles of CAEs of participating companies' IAFs as well as their audit committees, the structures, services and status of IAFs of participating companies, and awareness of The IIA(SA) were considered. These factors are based on information provided and

perceptions expressed by stakeholder respondents. The second objective is achieved by obtaining the perceptions of the stakeholder respondents on the current and anticipated future services performed by participating companies' IAFs, and the composition of and demand for staff in the IAFs.

The research report has specific delimitations since it was limited to 30 large listed participating South African companies. The small sample size may have influenced the results, and its openness to generalisation may therefore be questionable.

The research builds on the current body of knowledge of the standing of and the demand for internal auditing. The findings are important from a theoretical perspective because internal auditing in the South African context is a relatively unexplored area about which limited literature exists. The research could benefit The IIA by providing information on the standing of and the demand for IAFs in large listed companies in the private sector, information that The IIA could use in developing its standards and providing guidance to its members. The findings of the research could be considered when education and training requirements for internal auditors are reviewed or developed, to ensure that these are sufficient to maintain or even enhance the standing of internal auditors and that their expertise will remain in demand.

In addition, the research could be useful to companies when comparing the standing and demand of their own IAFs to the findings reported on in this research report. This comparison may provide insights about their own IAFs and trigger initiatives for improvements where such standing is found to be lacking. Prospective internal auditors can compare a position in internal auditing to other career opportunities in terms of the qualifications required, salaries offered, work experience and expectations, status and demand.

1.3 LITERATURE REVIEW

The literature review focuses on issues identified through previous research that would mostly influence or determine the standing of and demand for internal auditing within an organisation. These issues are being discussed with regard to issues affecting the standing, issues affecting both the standing and demand, and issues affecting the demand for internal auditing.

1.3.1 The standing of the IAF within an organisation

The standing of the IAF within an organisation depends on it effectively fulfilling a variety of requirements, some admittedly more important than others. Furthermore, the greater the extent to which internal and external stakeholders recognise the value of the IAF the more the IAF will be utilised. This will in turn influence the investment that management and the board is prepared to make in

the function, further influencing the quality of the function. This section interrogates current literature on four of the issues that most strongly influence the standing of the IAF within larger businesses namely, the profile of the CAE and the audit committee, organisational awareness of The IIA's activities, compliance with The IIA *Standards*, the structure and reporting lines of the IAF, and the value added by the IAF to the organisation.

□ **Profiles of the CAE and the audit committee**

Profile of the CAE

The global and South African internal audit profession has seen an enormous growth in both membership and certification over the past years (Erasmus 2009; Ttappous 2009; IIA n.d. (a); Johnson 2009). Although The IIA is the governing body of the profession, not all individuals practicing as internal auditors are registered with The IIA (IIA n.d.(b)). However, the only recognised internal audit certification is the Certified Internal Auditor (CIA) designation, owned and managed by The IIA, and this remains the only standard by which individuals unambiguously demonstrate their competency and professionalism in the internal audit field (IIA n.d.(c)). The question arises whether the CAE, as the head of the IAF, supports IIA membership and the CIA qualification. By reporting that 75% or more of internal audit staff members of IAFs that add the most value to their organisations are certified, Roth (2003) proves that this requirement is well founded.

Apart from the above, Sarens (2009:4) lists further attributes expected from a CAE, namely educational background, previous work experience, training and development programmes, behavioural skills, technical skills and competencies. Other studies highlighted the impact of different attributes of the CAE's profile on internal audit quality. Arena and Azzone (2009:45) report a positive relationship between the CAE's membership of the Italian IIA and internal audit effectiveness. Van Peurseem (2004 and 2005) reports that line managers often believe that internal auditors do not have enough knowledge to provide useful help, and consequently do not consider internal auditors' recommendations. This reflects directly on the CAE as all reports are authorised by the head of the IAF. The third King Report on Corporate Governance (IOD 2009:97-98) makes several references to the need for a quality internal audit team that has the appropriate technical and business skills, also referring to the CAE.

Profile of the audit committee

Two aspects that should have an effect on the profile of the audit committee within the organisation are the composition of the audit committee and the scope of its duties (reflected in the number of meetings per annum).

The third King report requires an audit committee to consist of at least three members, all of whom should be independent non-executive directors (IOD 2009:57). The second King Report suggested that the majority of the members should be independent non-executive directors and financially literate (IOD 2002:12). The third report requires that the audit committee members collectively should have a good understanding of integrated reporting (financial reporting and sustainability issues), internal financial controls, internal and external audit processes, corporate law and risk management and governance processes within the organisation (IOD 2009:58). It recommends the audit committee to conclude and report annually to the stakeholders of the organisation and the board of directors on the effectiveness of internal financial controls (IOD 2009:65).

The role of the audit committee is to serve as an extension of the non-executive director function since, by implication, both possesses the quality of independence (Vinten & Lee 1993:11). Beasley, Carcello, Hermanson and Neal (2009:80), as well as Rezaee (2005:284 & 291) perceive an audit committee as part of a organisation's monitoring mechanism, overseeing the integrity and quality of its financial reporting process and the effectiveness of both internal and external audit functions as the guardians of shareowners' interests. The interaction between the IAF and the audit committee is discussed below.

□ Awareness of The IIA

The IIA, being the governing body for internal auditors world-wide, regards its *Standards* as the authoritative source for the practice of internal auditing. The IIA's Code of Ethics requires that all who perform internal audit activities comply with these *Standards* (IIA 2009). Abdolmohammadi (2009:29) states in this regard, "... one would expect that CAEs who are also members of The IIA would fully use, and fully comply with the *Standards*. Failure to do so would indicate a challenge to the strength of the *Standards* as a unified set of rules for the practice of internal auditing worldwide". In South Africa, effective corporate governance (IOD 2009:93) requires that IAFs adhere to the IIA *Standards*. However, in the CBOK study (IIARF 2007:108), 81.9% of the respondents indicated that their organisations adhere to the *Standards* in whole or in part.

- **The structure of the IAF with specific reference to an in-house function versus outsource decisions as well as reporting lines**

In-house versus outsourced IAFs

The structure of a typical IAF consists of an in-house function (all engagement activities performed by internal auditors employed by the organisation), an outsourced function, or co-sourcing (a combination of the two previously mentioned forms). Co-sourcing, a partnership between an organisation and its external provider, allows the in-house IAF to retain responsibility for the internal audit process, while relying on the external provider for specialised technical skills and personnel (Thomas & Parish 1999:85). It enables an organisation to be cost-effective and derive external expertise, while retaining the advantage of direct control over internal auditing (Subramaniam, Ng & Carey 2004:87). In a study performed in Australia (Subramaniam *et al.* 2004:91), it was concluded that organisations that co-sourced internal auditing used the external providers to supplement areas in which the in-house IAF lacked technical expertise, while those that made use of full outsourcing ascribed it to the improved quality of service provided by external providers.

Outsourcing is a management strategy by which an organisation delegates functions or activities formerly performed inside the organisation to specialised and efficient service providers (Elmuti & Kathawala 2000:112). The outsourcing of the IAF only became popular during the 1980s (Moeller 2004:42) although this practice is well established in the accounting environment for a while, for example by using service organisations to maintain an organisation's derivative records (Billing 2002:26), perform inventory management and distribution (Gavin & Matherly 1997:118), managing information technology functions (Selim & Yiannakas 2000:214) and complying with accounting and tax requirements (Gavin & Matherly 1997:118; Selim & Yiannakas 2000:214; Frost 2000:34).

Outsourcing as a means of reducing organisational costs, providing flexibility and 'capturing' innovation (Naidu, Reed & Heywood 2005:235) has often been suggested. Due to the close scrutiny of internal audit costs (Spira & Page 2003:653; Sawyer, Dittenhofer & Scheiner 2003:1305; Moeller 2004:42) and the increased demands placed on the skills and competencies of internal auditors (Specklé, Van Elten & Kruis 2007:103) during the 1980s, the practice of outsourcing internal auditing (Caplan & Kirschenheiter 2000:392) to especially public accounting firms (Carey, Subramaniam & Ching, 2006:27) has gained momentum.

Most of the above reasoning could be applicable when deciding whether the internal audit function or part thereof should be outsourced or co-sourced. Although internal auditing is a prominent element of sound corporate governance principles, it may happen that, together with other services

such as security, it is sometimes regarded as being a non-core activity in countries where corporate governance is not optimally addressed (Figg 2000:50; Van Peurseem & Jiang 2008:220). Management may argue that when outsourcing the function, more resources could be spent on core activities (Figg 2000:50; Van Peurseem & Jiang 2008:221). However, effective outsourcing should not be less expensive than in-house activities, and thus should have no effect on resources.

The only South African study that addresses internal audit outsourcing practices found that management considered internal auditing to be a non-core function (Mjoli 1997:67), thus justifiable for outsourcing. This narrow viewpoint has thereafter been replaced by the notion that the distinction between core and non-core services for outsourcing purposes has become irrelevant, because such practices are increasingly applied for all services and are driven by other rationales (Burnes & Anastasiadis 2003:356).

Reporting lines

Internal auditing will always operate within the dynamic contradiction of, on the one hand being a part of the organisation, and on the other hand trying to remain independent and objective (KPMG 2003:2-3; Crowe Chizek 2006:3). The independence of the IAF and the objectivity of the internal auditor can be enhanced by various factors, the most important being the reporting lines. According to The IIA (IIA 2009:47) and reports issued by other major role players (IOD 2002:186; KPMG 2005:26-32; ECIIA 2005:28; Crowe Chizek 2006:2; Marx 2008:291; IOD 2009:96), operationally or functionally the CAE should report to the audit committee, while administrative reporting should be to the CEO. Legislation and other guidance (Companies Act 2008:S94; IOD 2009:56) highlight the independence of the audit committee, making this line of reporting the ideal route to follow for internal auditing. According to the third King Report on Governance (IOD 2009:97), internal auditing must be strategically positioned to accomplish their objectives:

Companies should have an **effective** IAF that is independent and objective. Internal audit should **report functionally to the audit committee** to assure this and should have **the respect and cooperation** of both the board and management.

The statistics available on the reporting structures in the private sector are contradictory. In an Australian study conducted amongst CAEs (Christopher, Sarens & Leung 2009:211), only 38.24% of the respondents report functionally to the audit committee, and only 32.35% report administratively to the CEO, the reporting channels that currently define independence. A further concerning result is that 26.47% report functionally to the chief financial officer (CFO). Reporting lines that result in poor

independence of IAFs are commonplace, as supported by a study conducted by Green and Gregory (2005:59) amongst USA organisations.

Although displaying a clear trend that CAEs are increasingly reporting to audit committees, many CAEs still report directly and exclusively to their CFOs. Other studies indicate a higher incidence of appropriate reporting lines. According to studies performed by PWC (2007 and 2008a) on the latest trends in internal auditing, 81% (2007:42) and 89% (2008a:7) of the respondents indicated that the IAF does report functionally to the audit committee, and 88% reported that the function reports administratively to the CEO. The IIA's CBOOK study (IIARF 2007:185), while not as optimistic as PWC's 2007 research, is more positive than the Australian situation (Christopher et al. 2009), where 54% of the respondents report to the CEO and 51% to the audit committee.

In South Africa, a study performed by Marx (2008:433) on audit committees in larger private sector companies concluded that "audit committees review the findings of the IAFs", a statement that probably refers to functional reporting lines. On the other hand, only 94% of the respondents indicated that the internal auditors have unrestricted access to the CAC, and although it is a significant number, being the top companies in South Africa, unrestricted access was expected to be 100%.

The IAF should be structured as an independent function within the organisation. This can be achieved by allowing the IAF to report functionally directly to the highest level of management, namely the board via the audit committee, and administratively to the CEO, representing senior management. This reporting line may be deemed indicative of the high standing of the IAF within the organisation, while more vulnerable reporting lines would suggest a lower respect for and standing of the IAF in the organisation.

Enhanced IAF status through value added services

The concept of adding value has been extensively researched, including in relation to the practice of internal auditing (Bou-Raad 2000:183; Nagy & Cenker 2002:133-134; Roth 2003:37; Bota-Avram 2008:137). The IIA states, as part of the definition of internal auditing, that an IAF is designed to render a value-added service to an organisation. The International Professional Practices Framework (IPPF) states that an IAF will add value when it provides important opportunities to achieve organisational objectives, identifies operational improvement and contributes to reducing risk exposure (IIA 2009:40). This implies that the IAF should provide important opportunities to achieve organisational objectives, including its strategic objectives. A study conducted by Melville (2003:210) found that the IAF plays an active role in strategic management within organisations

by evaluating and supporting the strategic management decisions made. Ray (2009:5) argues that the IAF should be viewed as a support function creating value within the organisation and assisting in the achievement of organisational objectives. .

Mihret and Yismaw (2007:472) believe that internal audit findings and recommendations will not serve much purpose unless management is committed to implementing them. Gramling and Hermanson (2009:37) identify the reliability and usefulness of the work products or deliverables of an IAF as indicators of internal audit quality. According to Rupšys and Boguslauskas (2007:13) the status of an IAF as viewed by senior management significantly correlates with the percentage of their recommendations which are implemented. Sarens (2009:4) agrees, but maintains that the frequency of consideration of the recommendations made by the IAF also serves as an indicator of IAF quality.

According to the *Standards*, the IAF must evaluate and contribute to the improvement of, specifically, governance, risk management and control processes, systems and operations (IIA 2009:40). Each of these attributes is discussed in detail in the next section of this paper.

1.3.2 Aspects that address both the standing of and demand for internal auditing

Certain issues affect both the standing of and the demand for internal auditing within companies. These include the services performed and audit approach followed by the IAF, the role of the IAF with regard to risk, and the role of the IAF with regard to corporate governance and fraud.

□ The services performed by IAFs and the audit approach followed

During recent years internal auditing has evolved from an accountancy-based profession to a management-oriented profession, striving to assist senior management of the organisation in accomplishing their strategic and operational objectives (Anderson 1996; Enyue 1997; Nordin van Gansberghe 2005:69). In addition, major global events such as corporate scandals also had a significant influence and impact on the direction of the types of activity IAFs provides globally (IOD 2009:9). With the evolvement of the internal audit profession, an expectation gap emerged between how users of internal audi services perceive the potential of the IAF and what services (activities) they actually can provide (Weingardt 2001). The IIA realised that in order to address the gap, organisations and The IIA should take a renewed look at the potential value of internal auditing. *Standard* 1000.A1 (assurance services) and 1000.C1 (consulting services) state that the nature of the assurance and consulting services that the IAF performs must be defined in the internal audit charter (IIA 2009:15). As the *Standards* require that the internal audit charter must be approved by the board (IIA

2009:45), it could be accepted that senior management gives its full support to the activities of the IAF that are included in the annual audit plan.

The IAF, through the conduct of assurance internal audit engagements, has become one of the mechanisms readily available to management of organisations to provide the share owners or investors, boards of directors, senior management and other stakeholders in organisations with reasonable assurance that their respective interests or investments in the organisation are protected (Enyue 1997:205). These services are meant to strengthen the governance and control processes of the organisation. In addition to assurance provided, senior management relies on the IAF for guidance and assistance through consulting services with regard to sound corporate governance, risk management and internal control systems (Coetzee & du Bruyn 2001:63).

In the performance of assurance and/or consulting activities, the audit universe (Spencer Pickett 2006:114-115; IIA 2009:93) is a list of all possible auditable engagements that could be performed within an organisation 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 2009:25-26) and Practice Advisory 2010-1 (IIA 2009a:93-94), the 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 performed by management, 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 & 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 & 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 & D'Onza 2003:197; McCuaig 2006:4; Arena, Arnaboldi & Azzone 2006:287; Sarens & De Beelde 2006a:76) indicate that organisations do not use this valuable source of information. A possible result linked to this is that CAEs world-wide (Ernst & 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 & Young 2007:10).

□ **The role of the IAF with regard to risk**

According to corporate governance guidance (COSO 2004:83; AS/NZS 2004:27; Spencer Pickett 2005:8-9; Atkinson 2008:42-45; IOD 2009:73-74), the responsibility for risk management lies with the board and senior management. Many organisations implement a board risk committee to assist with this task (PWC 2006:34-35; PRMIA 2008; IIA 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, Clune & Hermanson 2005:529; De la Rosa 2007; PRMIA 2008:13; Hettlinger 2009:49). This leaves the IAF independent to provide the board with assurance on the risk management framework and process.

According to Standard 2120 (IIA 2009:28-29) the IAF must evaluate the effectiveness of the risk management process. According to Practice Advisory 2120-1 (IIA 2009:107-110) 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 to verify whether management has planned and designed the process in such a manner that it provides reasonable assurance that the organisation'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 organisation. Internal auditing's involvement may vary from no role, to auditing the risk management process, to actively and on a continuous basis being involved, or to manage and coordinate the process. No mention is made of the overall risk management framework (COSO 2004:83; AS/NZS 2004:27; Spencer Pickett 2005:8-9; Atkinson 2008:42-45; IOD 2009:73-74).

Studies exploring the role of internal auditing with regard to risk management (McNamee & Selim 1998:13; Spira & Page 2003:656-657; Allegrini & D'Onza 2003:198-199; Baker 2004:17; Beasley et al. 2005; Sarens & De Beelde 2006b:73-75; Gramling & Myers 2006:52-58; Roffia 2007:9; Fraser & Henry 2007:403; Deloitte & IIA (UK and Ireland) 2008:8;

PWC 2008a:9; Ernst & Young 2008:5-6; IIA 2009a:9) all indicate the growth of the implementation of risk management by organisations. 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 2009a:9-10) includes the overall effectiveness of risk management within the organisation's risk environment, referring to both the risk management framework and the risk management process. This risk management framework supports the role of the IAF with regard to corporate governance.

□ **The role of the IAF with regard to corporate governance and fraud**

Corporate governance

The past decade has witnessed a proliferation of corporate governance guidelines and codes. South Africa's corporate governance practices were formalised for the first time in 1994, when the King Report on Corporate Governance (King I) was released (IOD 1994); a second (IOD 2002) and third (IOD 2009) updated version followed.

King III regards the board of directors as the focal point for and custodian of corporate governance (IOD 2009:29), and therefore the board of directors is vested with the full responsibility for the direction and management of the organisation (Vinten & Lee 1993:14). Research on the relationship between the IAF and the board of directors is limited (Gramling, Maletta, Schneider & Church 2004:233). Sarens (2007) views the IAF as the partner of top management in monitoring the organisation. Fadzil, Haron and Jantan (2005:846) expand on the latter notion by stating that senior management (represented by executive directors on the board of directors) normally expects that the IAF performs sufficient audit work and gathers sufficient evidence to form a judgement on the adequacy and effectiveness of the control processes. In their study on the relationship between senior management and the IAF, Sarens and De Beelde (2006b:238) found that senior management expects an IAF to compensate for the loss of control they experience as a result of increased organisational complexity and to fulfil a supporting role in the monitoring and improvement of risk management and internal control.

As discussed previously, the IAF should report functionally to the audit committee. Allegrini, D'Onza, Paape, Melville and Sarens (2006:849) found that IAFs perceive their relationship with audit committees in a positive light. Evidence is available that the more independent an audit committee is from executive management, the more active its approach to internal auditing is (Turley & Zaman, 2004:317). Raghunandan, Read and Rama (2001:116, 117) found a positive association between independence among audit committee members, the review of internal audit results and the frequency of meetings with the CAE. Goodwin (2003:274) reached a similar conclusion, and reported that the independence of the audit committee and the level of accounting experience among its members have a complementary impact on the audit committee's relation with the IAF. Myers and Ziegenfuss (2006:51 & 61) examined communication between the IAF and audit committees and found that effective audit committees communicate more with CAEs. Sarens, De Beelde and Everaert (2009:91) investigated the reason why audit committees look for support from the IAF, and found that audit committees seek comfort with respect to the control environment and internal controls, and that the IAF can provide such comfort.

In South Africa, the three King Reports on corporate governance (IOD 1994, 2002, 2009) acknowledge the role of an effective IAF as a mechanism in a good corporate governance structure. These reports state that the audit committee should be responsible for overseeing the IAF and that the latter should be strategically positioned to achieve its objectives. Research supports the principles in the King Reports that value should be placed on internal auditing as a monitoring function as the IAF contributes to an improved control environment (James 2003:323). Rezaee (2005:294) views the IAF as the first-line defence against fraud because of internal audit staff's knowledge and understanding of the organisation's business environment and internal control structure. This viewpoint is supported by Coram, Ferguson and Moroney (2008:557) who found that organisations with an IAF are more likely to detect and self-report fraud through misappropriation of assets than those that do not. The Carcello, Hermanson and Raghunandan (2005:70) study proved that organisations facing higher risk will increase their organisational monitoring through internal auditing.

Fraud

The role of internal auditors in detecting and preventing fraud is emphasised in the *Standards*. According to Standard 1220 (IIA 2009:20) – Due Professional Care, internal auditors should be alert to the possibility of significant errors and fraud. It indicates that internal auditors can be viewed as a first line of defense against fraud, as a result of their knowledge and understanding of the organisation's control structure and business environment. Moyes and Hasan (1996:41-46) emphasise that the experienced auditor is more likely to detect fraud than inexperienced

auditors. According to an empirical analysis by Moyes and Hasan (1996:46) internal auditors who are CIAs are more likely to detect fraud.

Rezaee (2002:208) states that internal auditors are well positioned to prevent and detect all types of frauds including employee fraud, embezzlement and financial statement fraud. Grazioli, Jamal and Johnson (2006:65) state that internal auditors detect fraud by looking at red flags. Ziegenfuss (2001:319) lists the most frequent type of red flags that may be detected by internal audit review, employee notification and specific investigation by management, including issues such as internal controls being ignored; changes in employees' lifestyle or behaviour; reports ignorance; internal audit ignorance; and ignoring employee comments.

Alleyn and Howard (2005: 297-298) in their study of audit responsibility for fraud detection, emphasise that an organisation with strong internal controls, internal auditors and audit committees is better equipped to prevent and detect fraud of any form. Consequently, fraud prevention remains the responsibility of management, since management has a responsibility to implement appropriate internal control systems to prevent fraud in their organisations.

1.3.3 The demand for internal audit staff

Attempts to meet the demand for competent internal auditors are compounded by the need to consider both the knowledge and the skills required in internal auditing as well as the ability to apply internal audit knowledge and skills in various industries; thus internal auditors need to possess a greater range of skills, attributes and competencies (Ramamoorti 2003). According to Harrington (2004:66), contemporary internal auditors should have a comprehensive set of skills and competencies that enable them to cope with the extensive changes and complexities that characterise both private and public sector operations. Oxner and Oxner (2006:6-10) agree with this assessment by stating that internal auditors should demonstrate expertise in many areas, including control evaluations, operational reviews and system analyses. A recent study by Ernst & Young (2008:10) found that the continuously expanding role of the internal auditor still lead to a skills gap and highlighted that there still is a need for more skilled internal auditors. In South Africa, the Sector Education and Training Authority (SETA) for the sector Finance, Accounting, Management Consulting and Other Financial Services (Fasset 2008:13-14) supports this tendency, with internal auditing being recognised as a scarce skill for the sector.

Studies performed world-wide identify two main problem areas linked to the scarcity of internal auditors (Goodwin 2004:644; Ernst & Young 2007:6-7; Singer 2008:7). Firstly, organisations struggle to attract the right mix of talent to be able to meet the needs of all the stakeholders and to add value to the organisation. Secondly, they do not succeed in retaining internal auditors in the internal audit

function long enough for them to be able to make a significant contribution to the organisation as a whole. The fact that many organisations use internal auditing as a stepping stone to prepare individuals for managerial positions (Oxner & Oxner 2006:56; Christopher *et al.* 2009:209), place a further burden on the remaining staff.

1.4 RESEARCH METHODOLOGY

This investigation employed a quantitative research design that used three different questionnaires as the data collection instruments. The questionnaires were developed and finalised after extensive literature reviews had been undertaken, discussions with stakeholders had been held and pilot testing had been done in South Africa. The questionnaires were completed using a combination of face-to-face interviews, conducted by members of the iKUTU research team, emails or faxes to collect the data for the CACs and CEOs/CFOs/COOs questionnaires. The CAE questionnaire was a self-administrated personal and web-based questionnaire in addition to the email and fax versions.

Sample and scope

The initial focus was to target the top 40 listed companies in South Africa, based on their market capitalisation. Such a list was not representative of companies across all the main sectors for listed companies in the South African economy. This initial list was therefore adjusted to incorporate at least one company from each main sector. The main sectors included in this study are:

- Basic materials: forestry and paper, metals and mining
- Financials: banks, general, life insurance and non life insurance
- Industrials: goods and services and support services
- Technology
- Telecommunications

Not all targeted companies were prepared to participate in the study. Some companies refused to participate because of a policy of non participation, while for others some of their targeted respondents refrained from responding due to work commitments. As the study sought the views of various stakeholders within one company; a member of the executive management, the chair person of the audit committee and the chief audit executive, only those companies where all these stakeholders responded are regarded as participants or responding companies. In an attempt to obtain at least 30 responding companies, a non participating company (thus where all the stakeholders did not respond) was, where possible, replaced with an alternative large listed South African company

operating in the same sector. Welman, Kruger and Mitchell (2005:71) consider it as a general rule that a sample should not be less than 15 units of analysis but preferably consist of more than 25 units of analysis, thus the 30 responding companies in this study was deemed sufficient for the descriptive analysis of the results. Given the limited number of responding companies the choice of sample size could have influenced the results and the generalisability of the results may therefore be limited.

In total, 30 CAEs, CACs and CEOs/CFOs/COOs of large listed companies were included in the sample of the iKUTU investigations that were undertaken in 2007 and 2008. For the purposes of this report and in order to enable a comparative analysis to be made, the CACs, CEOs/CFOs/COOs and CAEs of thirty large listed companies participated. These responses were collated and analysed. In the light of the size and market impact of the participating companies, the research findings can be used as a gauge of the current standing and demand of internal auditing in listed South African companies. The research results are presented by means of detailed graphic and brief descriptive representations in the findings chapter.

The sample of the study limited the possibility of comparison with other similar studies, such as the CBOK study. The scope of the 2006 CBOK study in respect of South African respondents was not limited to the large listed companies. All organisations were included in the scope of the 2006 CBOK study (IIA 2009).

CHAPTER 2: FINDINGS

2.1 PROFILES

This section presents the profiles of the CAE respondents and of the listed companies' audit committees.

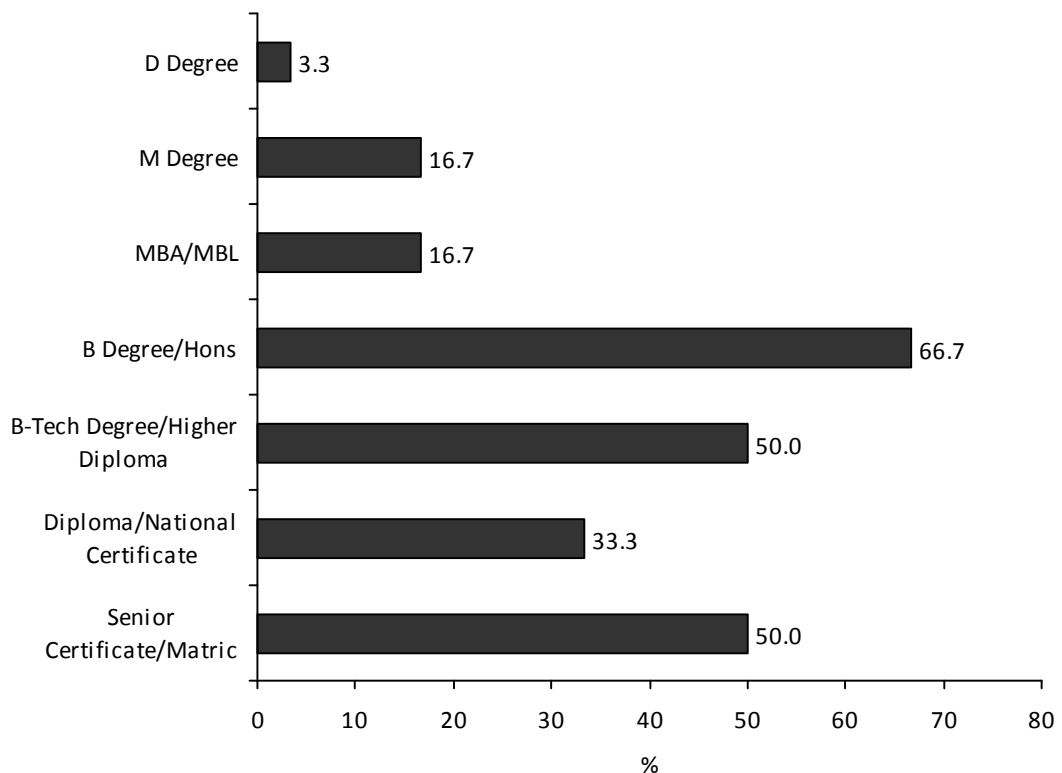
2.1.1 CAEs' profiles

Section 2.1.1 provides an overview of the CAE respondents who participated in this investigation in respect to their formal qualifications, fields of specialisation, professional qualifications, remuneration, experience, employment records, and membership of The IIA.

□ CAEs' formal qualifications

CAE respondents were requested to indicate all their formal qualifications. Two-thirds of them hold either a bachelor's degree or an honours degree (figure 1).

Figure 1: CAE – Formal qualifications

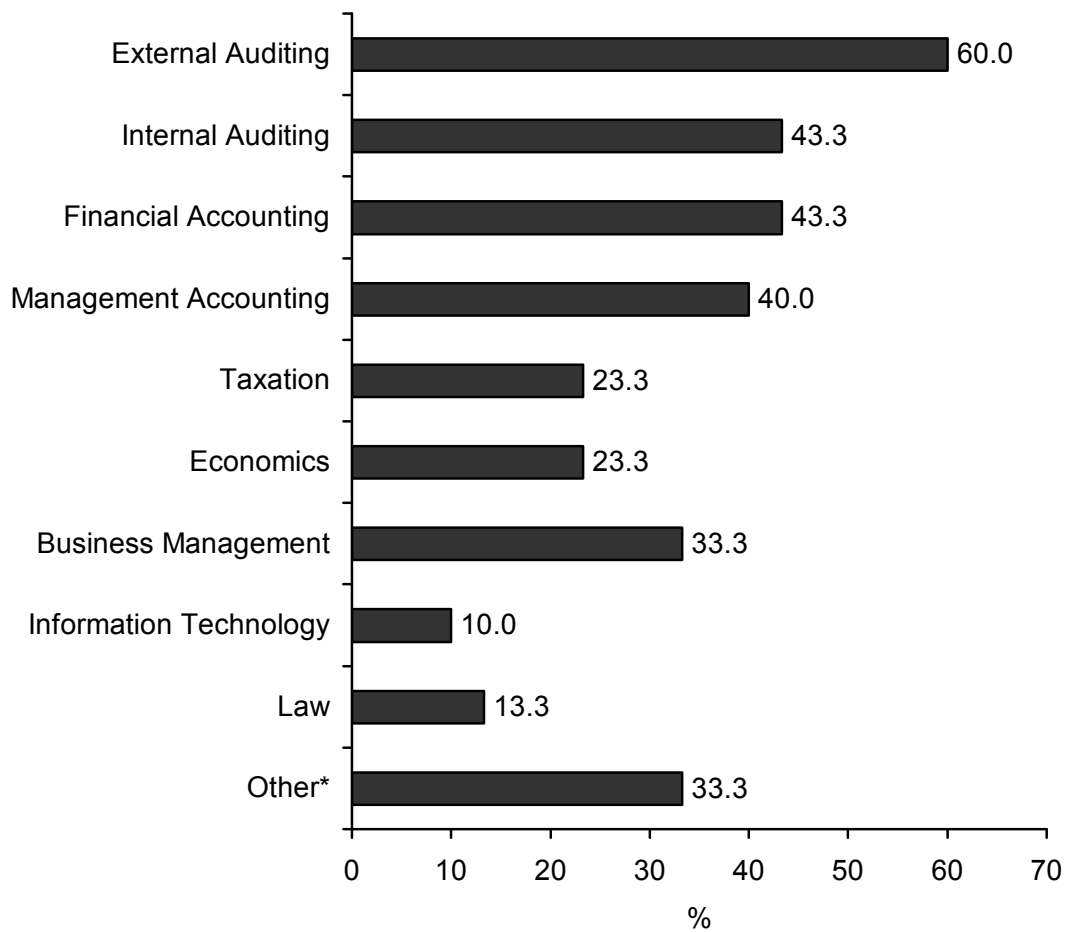


Note: Respondents could indicate more than one qualification. Thus, the presentation of information in the corresponding figures will not add up to 100%.

□ **CAEs' fields of specialisation**

CAE respondents were requested to indicate their main fields of specialisation in their highest post-matric qualifications. The field of specialisation of the majority of the CAE respondents was external auditing followed by internal auditing and/or financial accounting and/or management accounting (figure 2).

Figure 2: CAE – Main fields of specialisation



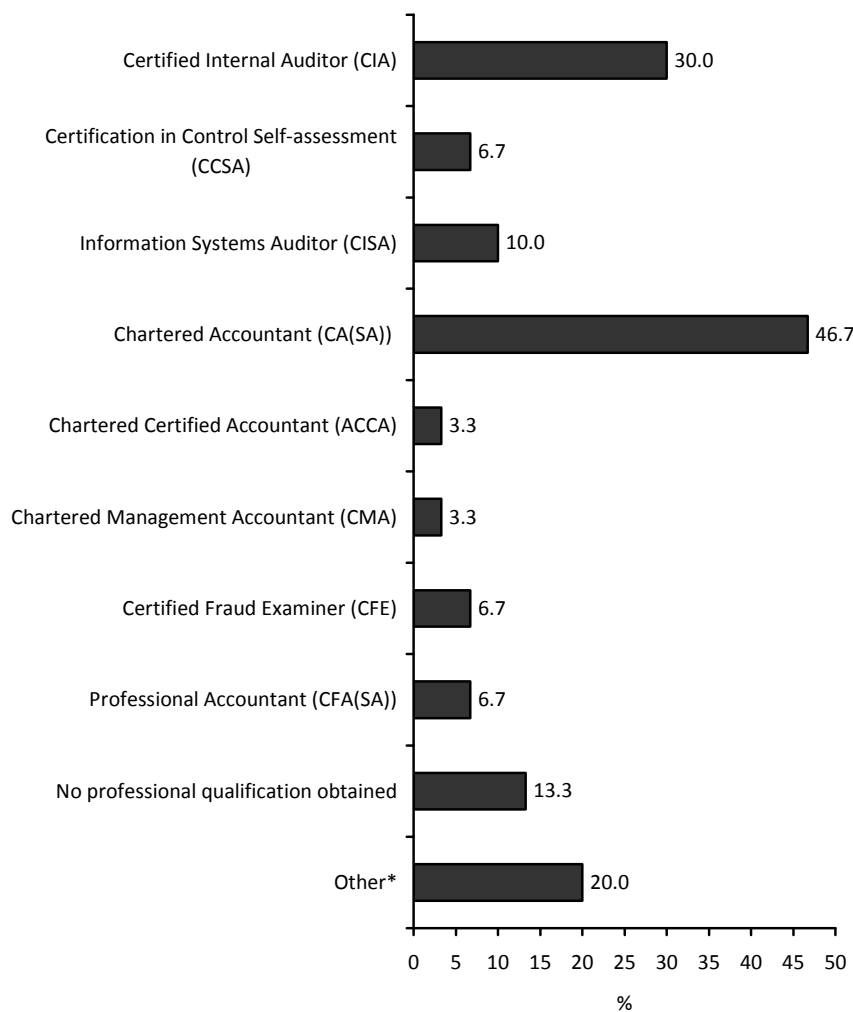
* The category "Other" includes Costing, Banking, Forensics and Risk Management

Note: Respondents could indicate more than one specialisation. Thus, the Presentation of information in the corresponding figures will not add up to 100%.

□ CAEs' professional qualifications

CAE respondents were requested to indicate all their professional qualifications. Almost half of the CAE respondents (46.7%) are qualified chartered accountants (CAs (SA)). As external auditing represents the main field of specialisation of 60% of the CAE respondents (figure 2, above), the high percentage of chartered accountants is not surprising. Only 30% of the CAE respondents are certified internal auditors (CIAs) (figure 3). The reasons for this phenomenon should be investigated in order that The IIA (SA) can take the required action to ensure that the CIA become the qualification of choice for the position of CAE.

Figure 3: CAE – Professional qualifications



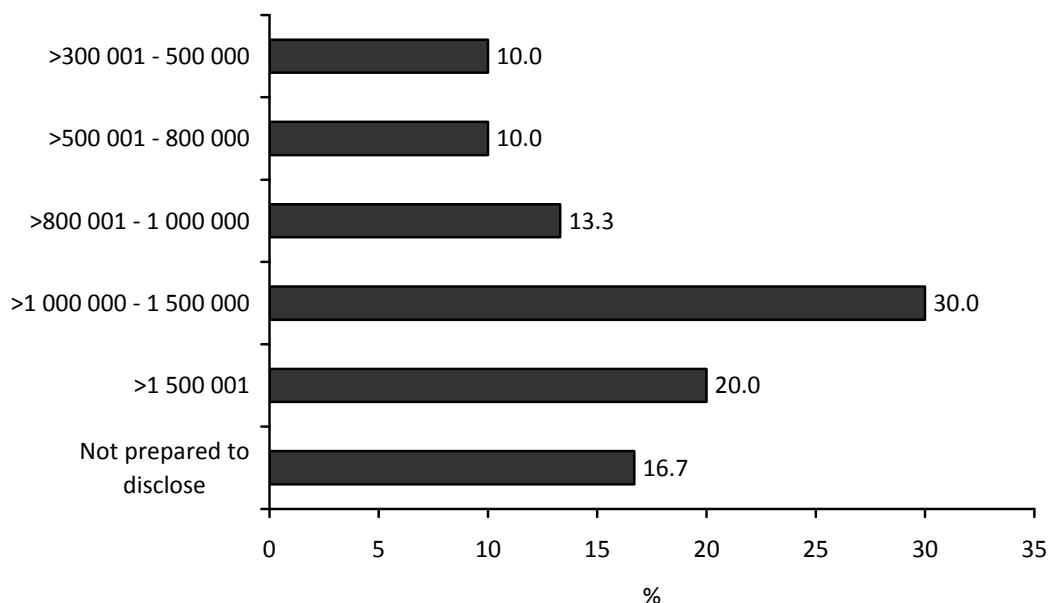
* The category "Other" includes Associate General Accountant (AGA), Fellow of the Chartered Management Institute (FCMI) & Certified Ethics Officer, Fellow of the Institute of Risk management and Certified Financial Service Auditor

Note: Respondents could indicate more than one professional qualification. Thus, the Presentation of information in the corresponding figures will not add up to 100%.

□ **CAEs' remuneration**

CAE respondents were requested to indicate the band within which their remuneration packages fall. Approximately half of the CAE respondents who answered this question earn more than R1 million per year (figure 4). A total of 16.6% of these respondents refrained from disclosing their remuneration package.

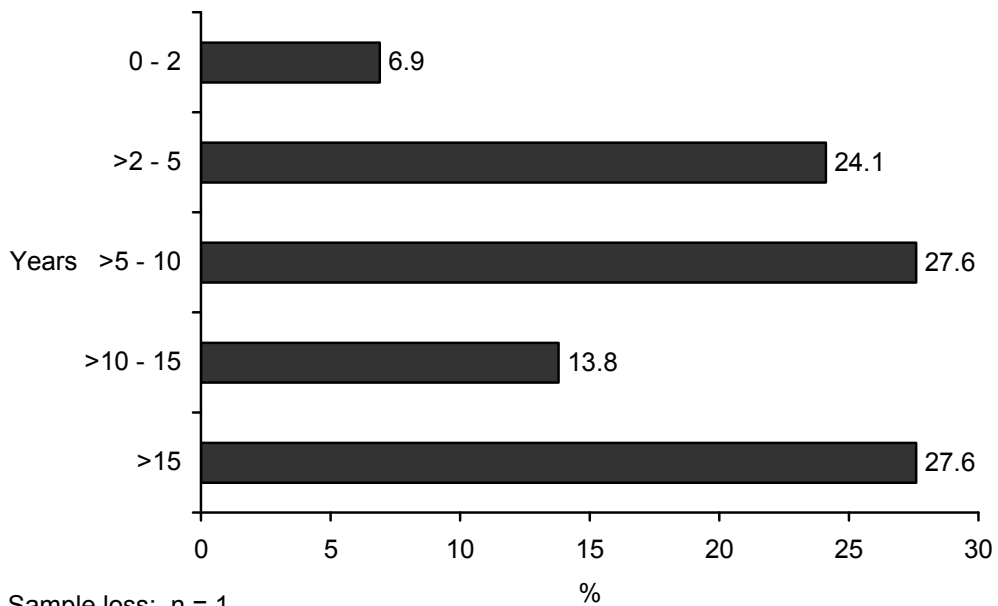
Figure 4: CAE – Annual remuneration package



□ **CAEs' experience in internal auditing**

CAE respondents were requested to indicate their years of experience in the internal auditing field. Approximately two-thirds (69%) of them have more than five years of experience in the internal auditing field, while 41.4% have more than 10 years of experience in the field. Only 6.9% of the CAE respondents have less than two years of experience in the field of internal auditing (figure 5).

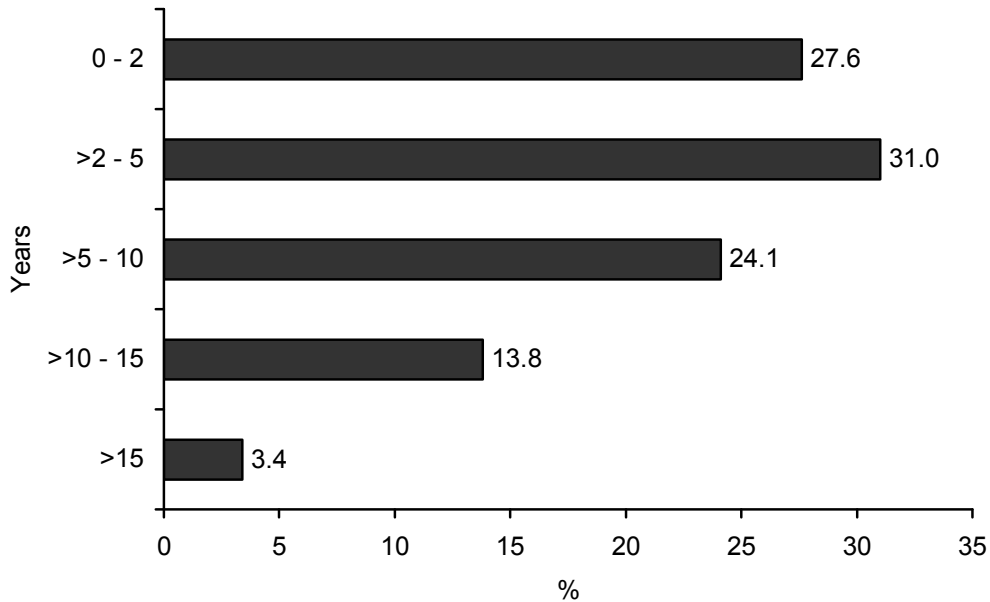
Figure 5: CAE – IAF experience



□ CAEs' years of internal audit experience

Figure 6 indicates that whilst more than two thirds (69%) of CAE respondents have more than five years of experience in the field of internal auditing (figure 5, above), only 41.3% of CAE respondents have held the position of CAE for that period. A total of 27.6% of the respondents have been in the position of CAE for the past two years only.

Figure 6: CAE – Employment record

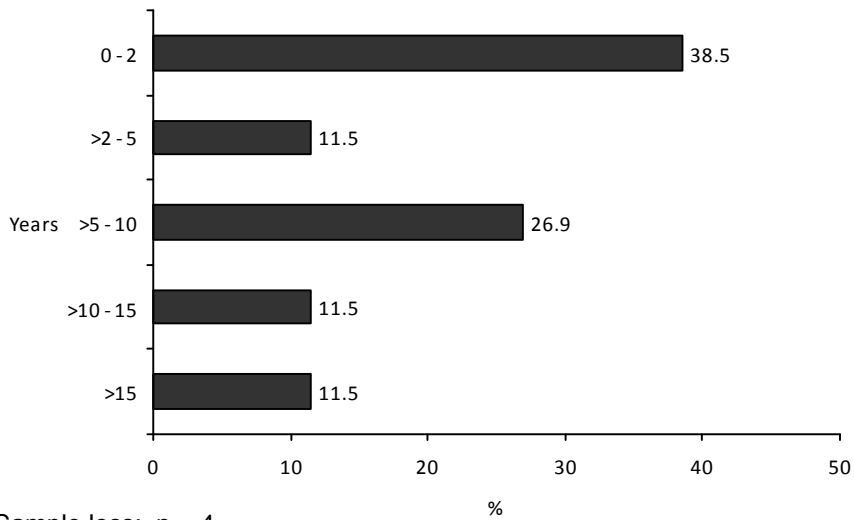


* Sample loss: n = 1

□ CAEs' period of service with current employers

Figure 7 indicates that a relatively high percentage (38.5%) of CAE respondents joined their current employer in the course of the past two years, while 11.5% have been employed by their current employer for the past two to five years. About one-quarter (23%) of CAE respondents have been employed by their current employer for at least the past decade. A measure of flexibility in internal auditing is demonstrated by the fact that half (50%) of the CAE respondents indicated that they have changed employers in the past five years, while the remaining half of the respondents have not made such a change, during that time.

Figure 7: CAE – Period of service with the current employer

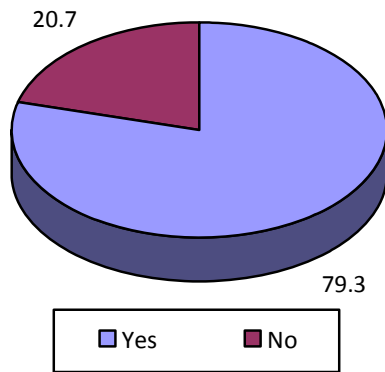


* Sample loss: n = 4

□ CAEs: IIA membership

Figure 8 illustrates that, although only 30% of the CAE respondents hold the CIA qualification (figure 3, above), nearly 80% (79.3%) are members of The IIA (SA).

Figure 8: CAE – IIA Membership



* Sample loss: n = 1

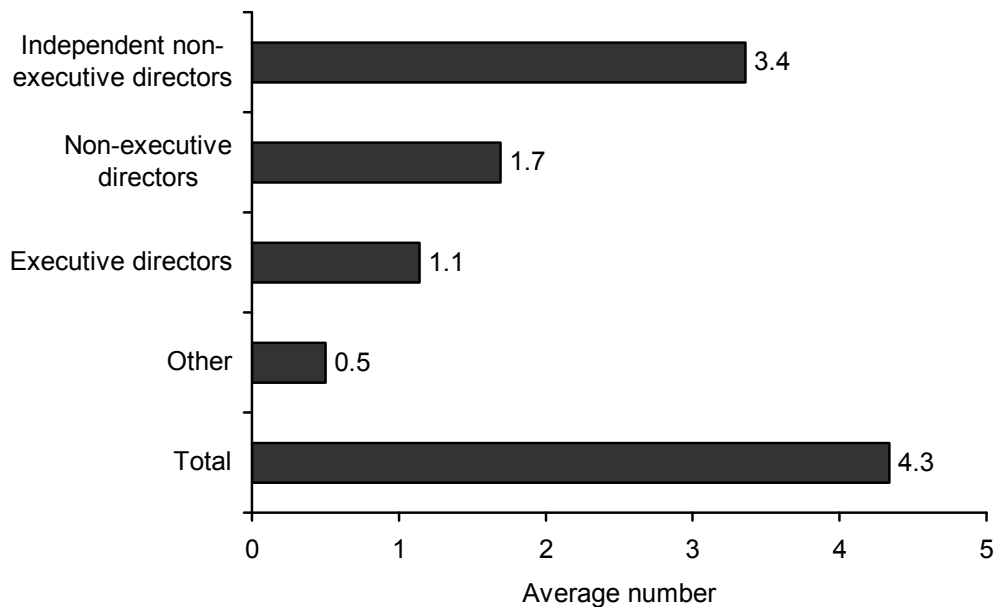
2.1.2 Profile of audit committees

This section provides an overview of on the composition of the audit committees and frequency of audit committee meetings of the responding South African listed companies.

□ Composition of audit committees

Based on the information provided by the CAC respondents, it appears that a typical audit committee within the 30 large listed South African companies is comprised of four members of whom at least three are independent non-executive directors (figure 9).

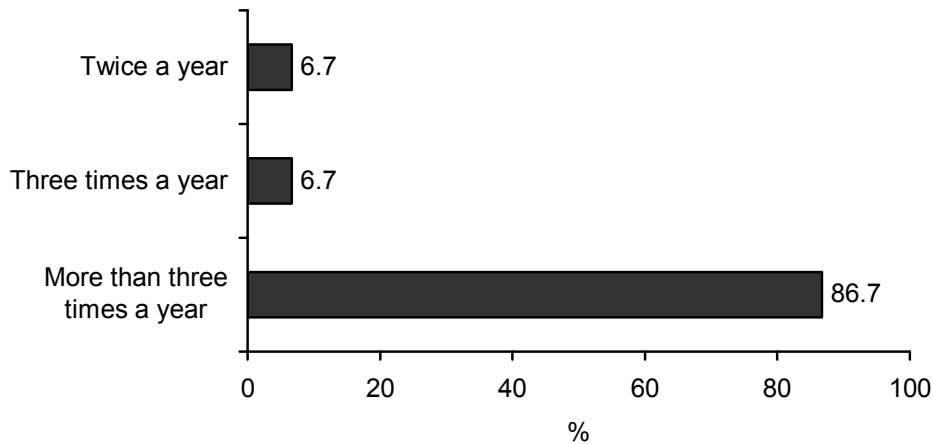
Figure 9: CAC – Composition of audit committees (average number of members per category of members)



□ Frequency of audit committee meetings

CAC respondents indicated that the overwhelming majority (86.7%) of their audit committees meet more than three times a year. Only 6.7% of those audit committees meet twice a year (figure 10).

Figure 10: CAC – Frequency of audit committee meetings



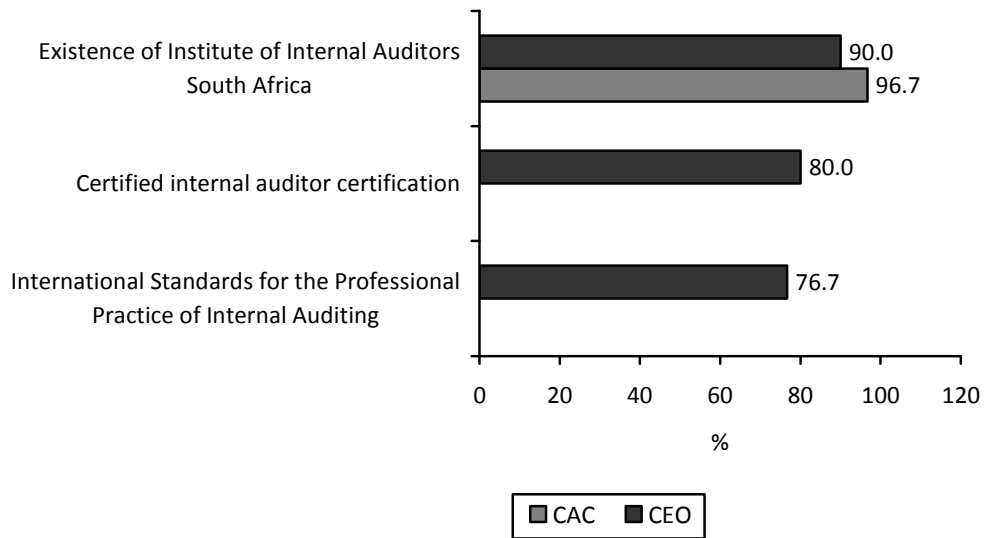
2.2 USERS' AWARENESS OF THE IIA (SA) AND STANDARDS

This section focuses on user awareness of The IIA (SA), the CIA qualification, and internal auditing standards. The responses presented in this section should be considered in the context that only 30% of the CAE respondents are certified internal auditors (CIAs) (figure 3).

2.2.1 Awareness of The IIA (SA)

A very large majority of the responding CACs (96.7%) and CEOs/CFOs/COOs (90%) are well acquainted with the existence of The IIA (SA) (figure 11). Eighty percent of the latter group of respondents is also aware of the qualification of certified internal auditor and 76.7% are aware of the *Standards*. From the above findings, it appears that the existence of The IIA (SA), its professional qualification, and the *Standards* have been sufficiently promoted among the CAC and CEO/CFO/CCO respondents in order to create a high level of awareness of these matters. The reasons for the differences in the perceptions of the CAE and the CEO/CFO/COO are an area for future research.

Figure 11: Level of awareness of IIA (SA)



2.2.2 Perceived compliance with the Standards

Figure 12 demonstrates that the majority of the CAC (90.0%) and CEO/CFO/CCO (76.7%) respondents indicated that their IAFs comply with the *Standards*, while figure 13 illustrates the views of CAE respondents on their IAFs compliance with certain aspects of the *Standards*. Based on responses from CAE respondents, the majority of IAFs comply with these *Standards* to a lesser or greater extent. The reasons for the differences in the perceptions of the CAE and the CEO/CFO/COO with regard to the application of the *Standards* are an area for future research.

Figure 12: CAC and CEO/CFO/COO – Perceived compliance of IAFs with International Standards for the Professional Practice of Internal Auditing

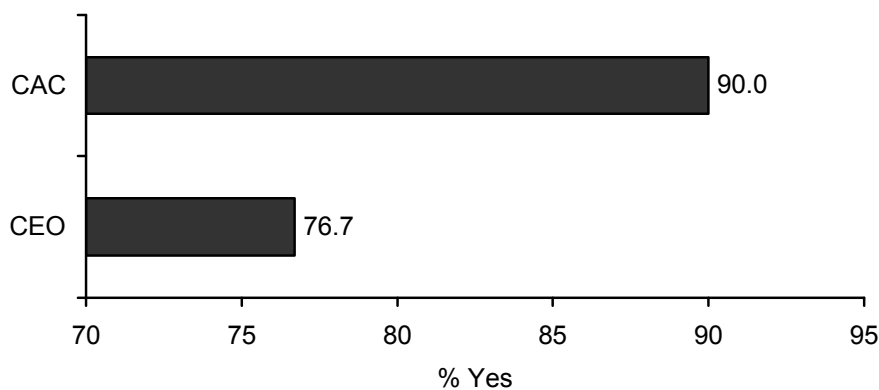
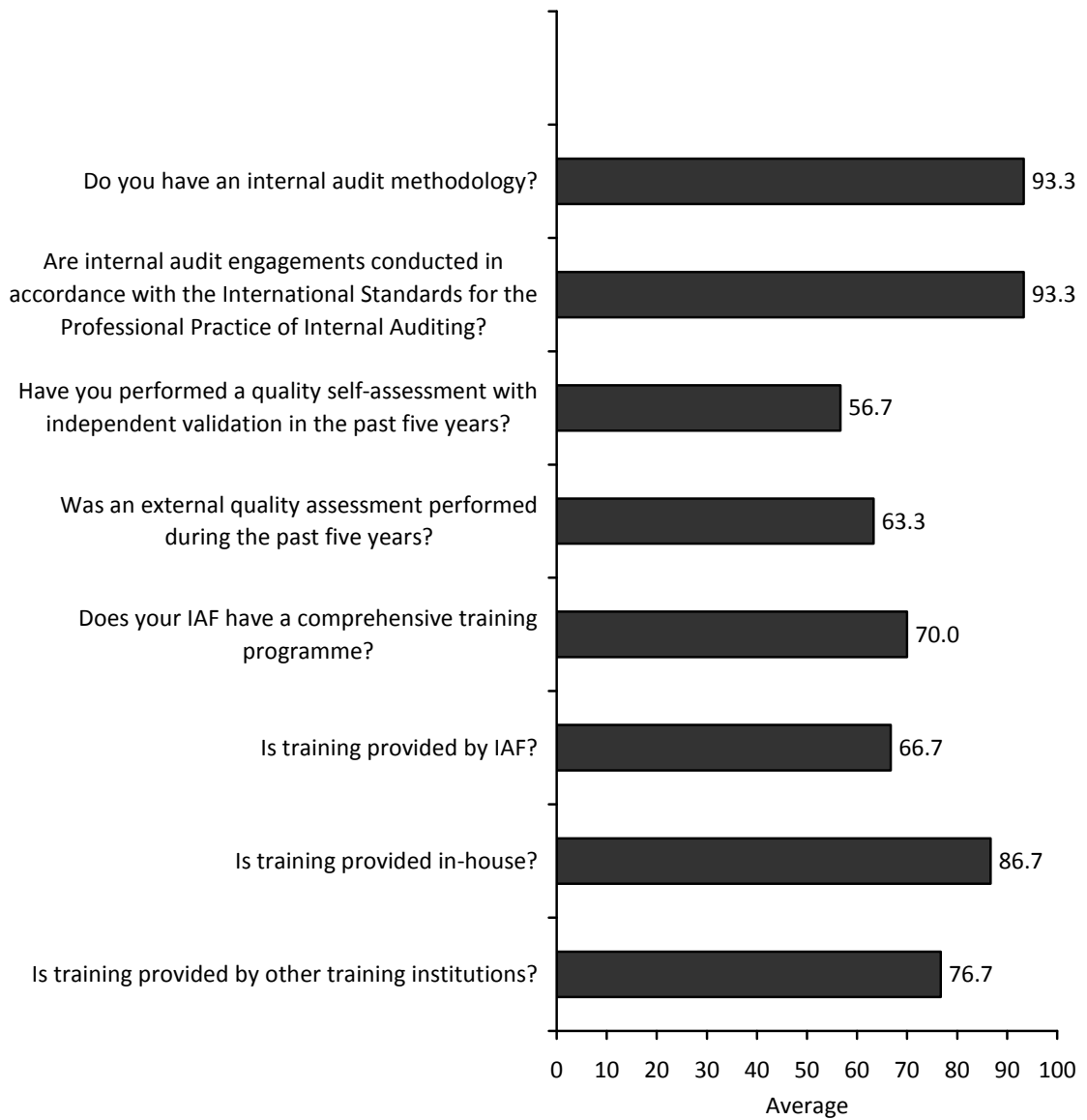


Figure 13: CAE – Compliance with specific Standards



2.3 STRUCTURE OF THE IAFs

Section 2.3 presents an overview of the structure and reporting responsibilities of the participating companies' IAF's, as well as the reasons for the choice of the selected structure. These results are presented from the perspective of the CAC, the CEO/CFO/COO, and the CAE respondents.

2.3.1 IAF structure – CAC and CEO/CFO/COO

Section 2.3.1 presents information on the structure of the IAFs from the perspective of the CAC respondents. The following information is presented:

- The level of in-house, outsourced and co-sourced IAFs;
 - The reporting lines of CAE's;
 - Reasons for the outsourcing of IAFs; and
 - Reasons for using in-house IAFs.
- **CAC and CEO/CFO/COO – levels of in-house, outsourced and co-sourced IAFs**

Figure 14 illustrates that, according to CAC respondents, the majority of internal audit services are performed by an in-house team of internal auditors (53.3%) while 40.0% of the CAC respondents indicated that their in-house IAFs are supported by outsourced IAFs.

Figure 15 should be read in conjunction with figure 14. Figure 15 reflects that, according to CEO/CFO/COO respondents, the majority of internal audit services are executed in-house (53.3%). Figure 14 similarly reflects that, according to CAC respondents, the majority of internal audit services are executed in-house (53.3%). A total of 40.0% of the CAC respondents indicated that their IAFs use an in-house IAF that is supported by an outsourced IAF while 33.3% of the CEO/CFO/COOs indicated the same arrangement. According to CEO/CFO/COO respondents, 13.4% (compared to the 6.7% indicated by the CAC respondents) of IAFs are wholly outsourced.

Figure 14: CAC – Structure of an IAF

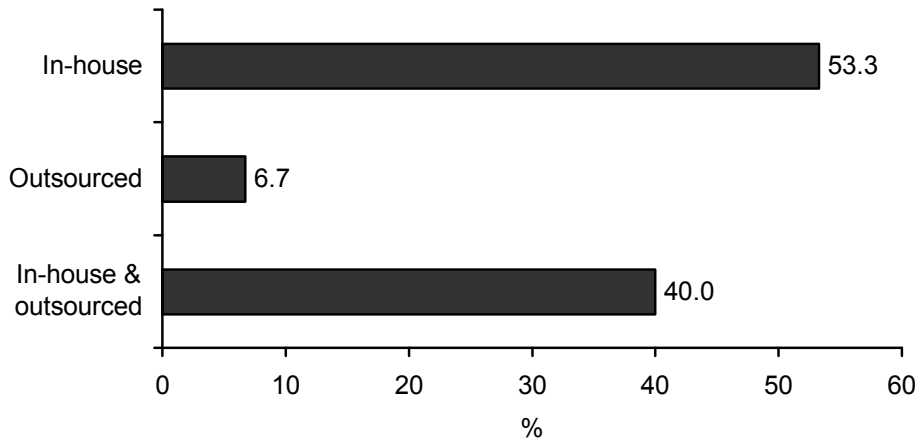
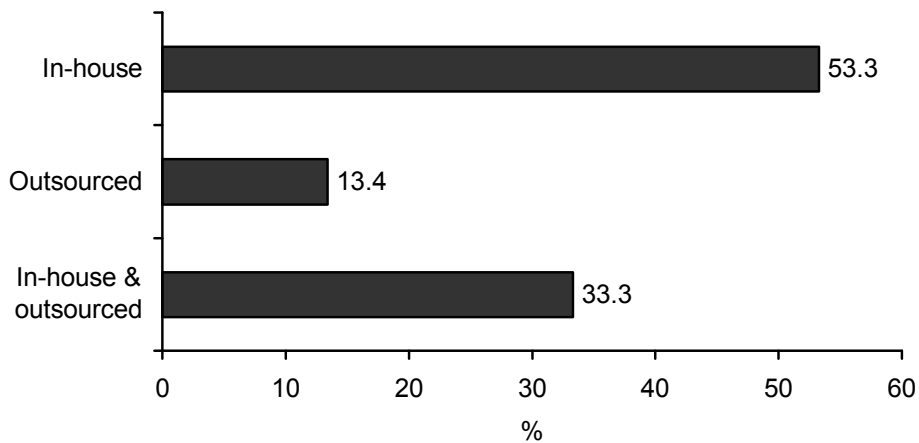


Figure 15: CEO/CFO/COO – Structure of the IAFs



□ CAC and CEO/CFO/COO – reporting lines

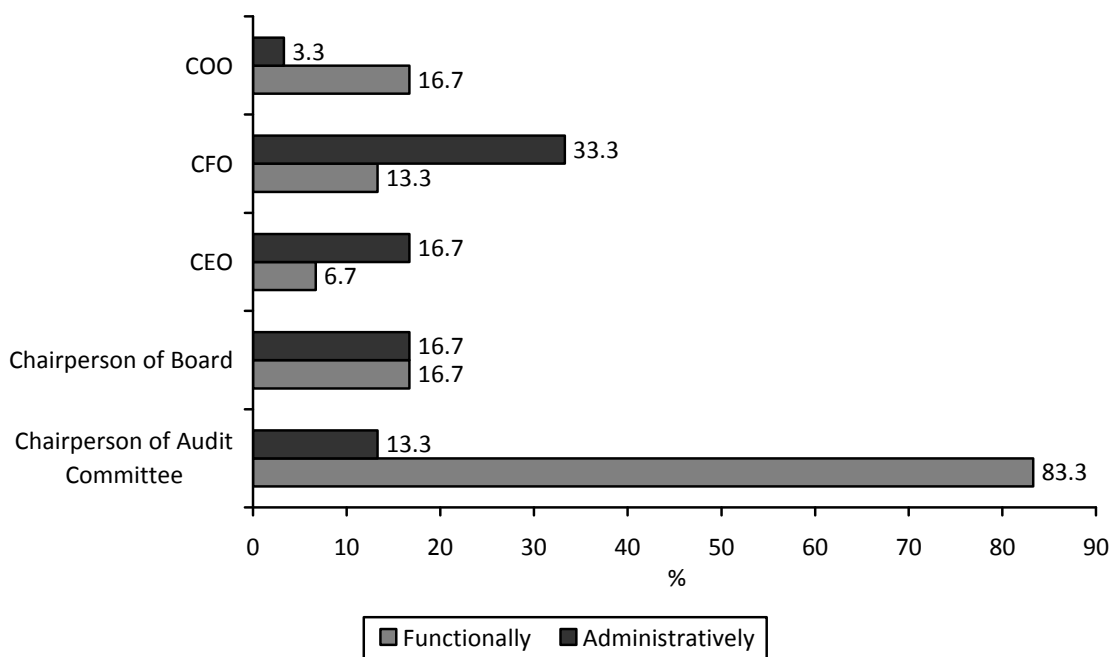
Figure 16 reflects the responses of the CAC respondents on their companies' reporting lines of the CAEs. The respondents could choose from several alternatives and had to distinguish between the CAE's functional and administrative reporting lines. According to 83.3% of their CAC respondents, the CAE reports all functional matters to the individual who acts as the chairperson of the audit committee. A third of the CAC respondents indicated that the CAE reports administratively to the CFO, while 16.7% indicated that the reporting is done to either the CFO or the CEO.

Figure 17 should be read in conjunction with figure 16. Figure 17 reflects the responses of CEO/CFO/COO respondents, while figure 16 reflects the responses of the CAC respondents on the reporting lines of CAEs. The CEO/CFO/COO respondents had to choose from several alternatives and had to distinguish between CAE's functional and operational reporting lines. The majority of the CEO/CFO/COO respondents (56.7%) indicated that the CAE reports to the chairperson of the audit committee on all functional matters (CAC 83.3%). Twenty percent of the CEO/CFO/COO respondents indicated that the CAE reports to the CFO on functional matters.

A total of 43.3% of the CEO/CFO/COO respondents indicated that, for administrative purposes, their CAE reports to the CFO, while 26.7% indicated that their CAE reports to the CAC for administrative purposes. Of these respondents, 16.7% indicated that their CAE reports operationally to their CEO.

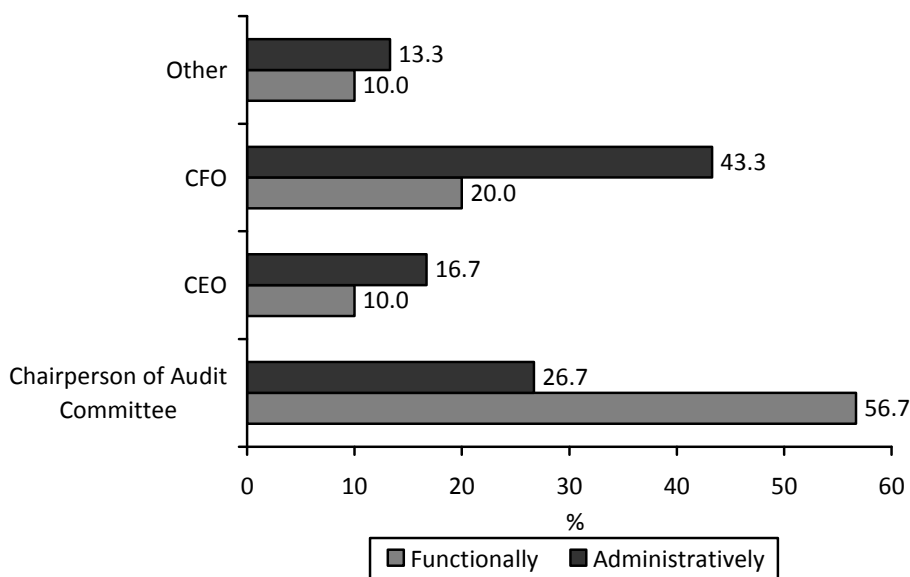
It is clear from these results that there is a difference between the information provided by the CEO/CFO/COO respondents and the CAC respondents. Further research is needed to identify the reason for this difference.

Figure 16: CAC – Reporting lines of the CAE



Note: In some instances multiple reporting lines were indicated by the participants, therefore the corresponding figures will not add up to 100%.

Figure 17: CEO/CFO/COO – Reporting line of the CAE



* The category “Other” primarily includes Risk Officer or Risk Executive

Note: In some instances multiple reporting lines were indicated by the participants, therefore the corresponding figures will not add up to 100%.

□ CAC and CEO/CFO/COO – reasons for co-sourcing/outsourcing IAFs

The importance of the reasons that were provided for outsourcing some or all IAFs was measured on a five-point scale that ranges from 1 (not important) to 5 (extremely important). A response of 3 is taken to indicate an importance that is higher than 2 and lower than 4, rather than being an indication of central tendency bias.

The need for specialised technical expertise (mean = 3.7) is perceived by CAC respondents to be very important in deciding whether to outsourced IAFs. All the other reasons listed in figure 18 are perceived by the CAC respondents to be important (2.00 ≤ mean < 3.00). None of the identified reasons were perceived by the CAC respondents to be of only reasonable importance or not to be important at all.

The results reflected in figure 18 should be read in conjunction with those in figure 19. CEO/CFO/COO respondents considered the need for specialised technical expertise to be an extremely important reason (mean = 4.1) for the outsourcing of some or all IAFs, while CAC respondents considered that reason to be very important (mean = 3.7). CEO/CFO/COO respondents considered the shortage of competent internal auditors to be a very important reason (mean = 3.7) for the decision to outsource IAFs. CAC

respondents also considered the shortage of competent internal auditors to be an important reason (mean = 2.9) for outsourcing IAFs.

The importance of reasons given for outsourcing some or all the IAFs were measured on a five-point scale that ranges from 1 (not important) to 5 (extremely important). A response of 3 is taken to indicate an importance that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

All the other reasons that were listed in figure 19 were considered to be important by both CEO/CFO/COO and CAC respondents ($2.00 \leq \text{mean} < 3.00$). CAC and CEO/CFO/COO respondents did not consider any of the given reasons to be of only reasonable importance or not to be important at all.

The importance of the various reasons for outsourcing/co-sourcing IAFs were measured on a scale that ranged from 1 (not important) to 35 (extremely important). A response of '15' was taken to indicate an importance that was higher than '10' and lower than '20' rather than being an indication of central tendency bias.

Figure 18: CAC – Reasons for decision to outsource IAFs

(Scale anchors: 1 = not important, 5 = extremely important)
 Extremely important (mean ≥ 4.00); Very important ($3.00 \leq \text{mean} < 4.00$); Important ($2.00 \leq \text{mean} < 3.00$); Reasonably important ($1.00 \leq \text{mean} < 2.00$); Not important (mean < 1.00)

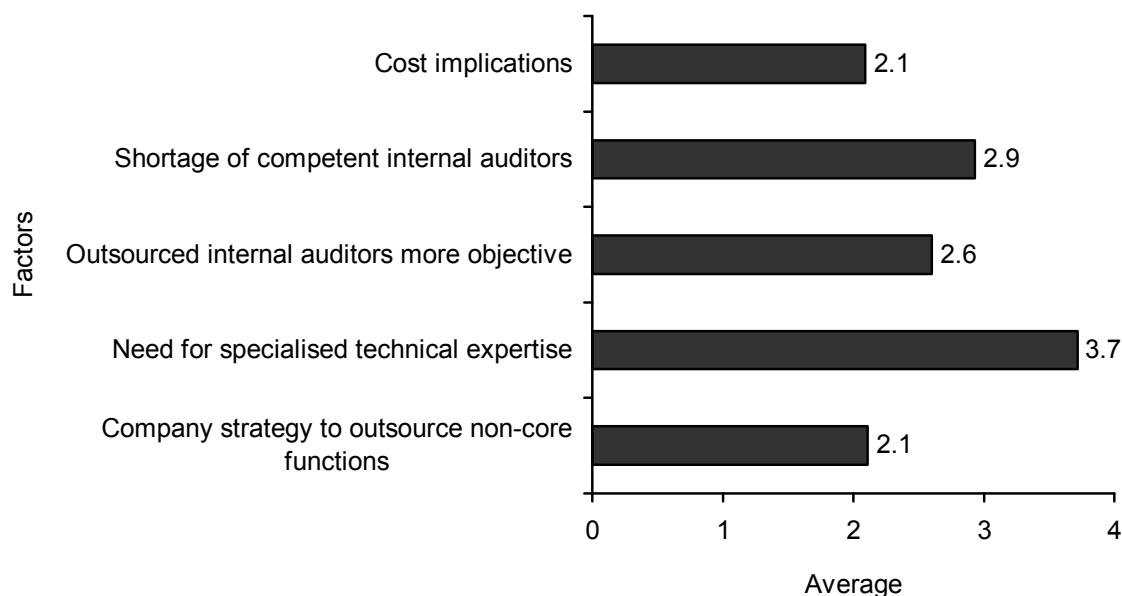
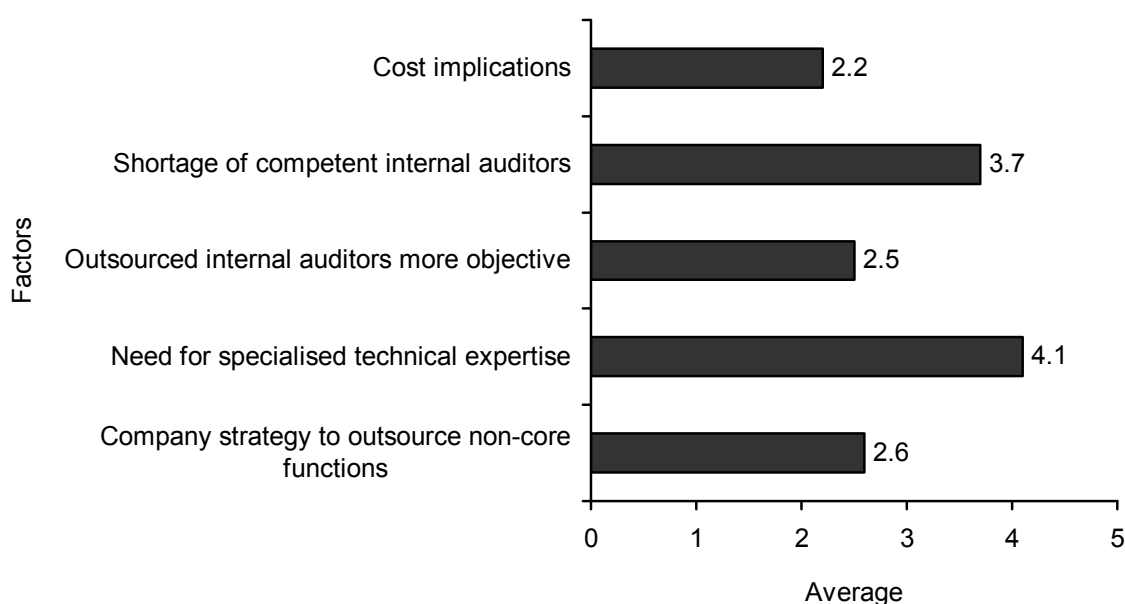


Figure 18 reflects that better access to specialised technical expertise was the only reason that CAC respondents considered to be very important in deciding to outsource internal audit services, while they perceived a similar reason (namely the shortage of competent internal auditors) to be important. CEO/CFO/COO respondents considered the need for specialised technical expertise to be an extremely important reason for outsourcing internal audit services and they furthermore perceived the shortage of competent internal auditors to be a very important reason for that decision (figure 19). These responses emphasise the shortage of high-level skills in the internal audit environment.

Figure 19: CEO/CFO/COO – Reasons for the decision to outsource IAFs

(Scale anchors: 1 = not important, 5 = extremely important)
 Extremely important (mean ≥ 4.00); Very important ($3.00 \leq \text{mean} < 4.00$); Important ($2.00 \leq \text{mean} < 3.00$); Reasonably important ($1.00 \leq \text{mean} < 2.00$); Not important (mean < 1.00)



□ **CAC and CEO/CFO/COO – reasons for using in-house IAFs**

The importance of the reasons given for using in-house internal audit services for some or all internal audit services was measured on a five-point scale that ranges from 1 (not important) to 5 (extremely important). A response of 3 is taken to indicate an importance that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

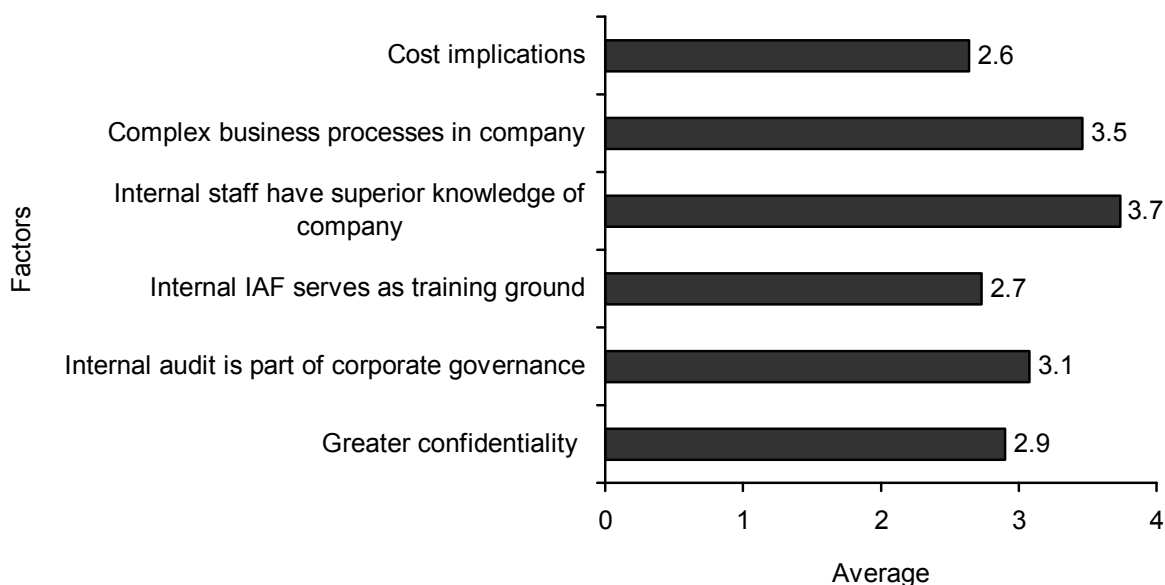
The three reasons that the CAC respondents consider to be very important in the decision to have certain or all internal audit services performed in-house (figure 20) are complex business processes in the company (mean =

3.5), the superior knowledge of the staff of the company (mean = 3.7) and the fact that the internal audit was perceived to be part of corporate governance (mean = 3.1). The CAC respondents consider all the other reasons listed in figure 21 to be important ($2.00 \leq \text{mean} < 3.00$).

The results reflected in figure 21 should be read in conjunction with those in figure 20. The three reasons perceived by CEO/CFO/COO respondents to be extremely important in deciding to use in-house IAFs for some or all of the internal audit services were the complexity of business processes in the company (mean = 4.2), the superior knowledge that internal staff have of the company (mean = 4.2) and the fact that internal auditing was perceived to be part of corporate governance (mean = 4.2). These three reasons were the only ones that are perceived to be very important by the CAC respondents ($3.00 \leq \text{mean} < 4.00$) in making the decision to use in-house IAFs.

Figure 20: CAC – Reasons for the decision to have some or all internal audit services performed in-house

(Scale anchors: 1 = not important, 5 = extremely important)
 Extremely important (mean ≥ 4.00); Very important ($3.00 \leq \text{mean} < 4.00$); Important ($2.00 \leq \text{mean} < 3.00$); Reasonably important ($1.00 \leq \text{mean} < 2.00$); Not important (mean < 1.00)

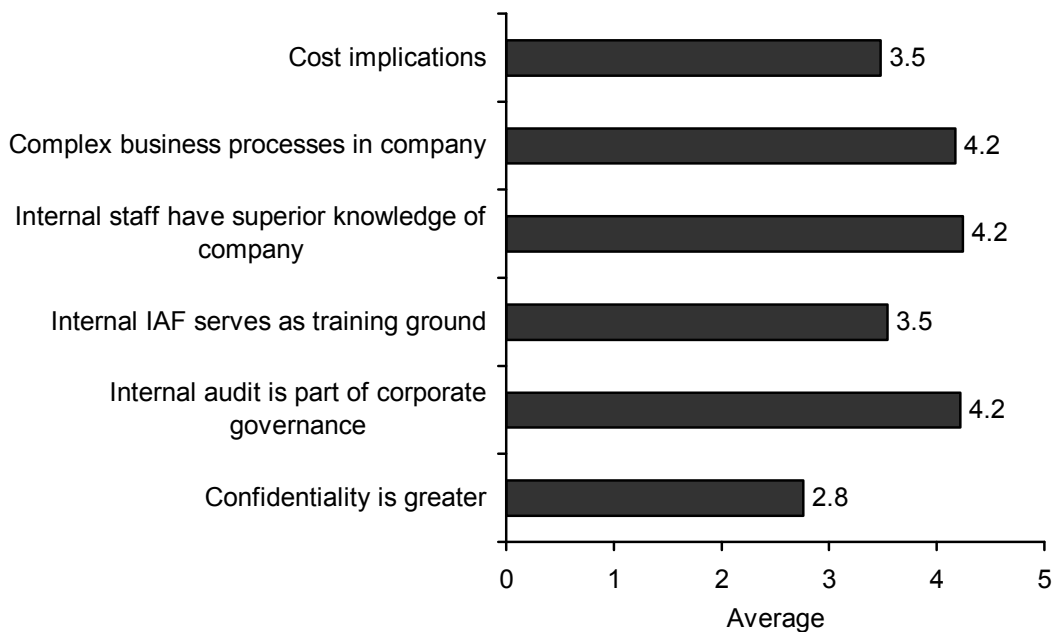


The CEO/CFO/COO respondents consider cost implications (mean = 3.5) and the fact that the internal audit function serves as the training ground for management (mean = 3.5) to be very important, while these respondents consider the remaining reason, namely that confidentiality is improved when an in-house IAF is used, only to be important (mean = 2.8). The CAC

respondents perceive all of the reasons that are discussed in this paragraph to be important ($2.00 \leq \text{mean} < 3.00$). The CEO/CFO/COO respondents as well as the CAC respondents do not identify any of the reasons to be of only reasonable importance or not to be important at all.

Figure 21: CEO/CFO/COO – Reasons for the decision to have some or all internal audit services performed in-house

(Scale anchors: 1 = not important, 5 = extremely important)



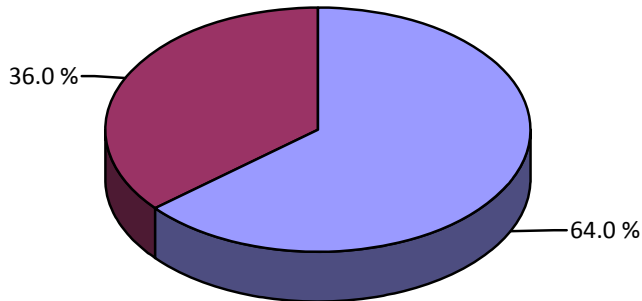
2.3.2 CAE – IAF structure

Section 2.3.2 provides the unique perspective of CAE respondents on the IAFs' structure.

□ CAE – levels of inhouse and co-sourced/outsourced internal audit services

CAE respondents indicated that 64.0% of IAFs are outsourced or co-sourced (figure 22). CAE respondents therefore indicated that a higher percentage of IAFs were performed by non-employees than the other respondents in the investigation did.

Figure 22: CAE – Percentage of the internal audit services that is outsourced/co-sourced



* Sample loss: n = 5

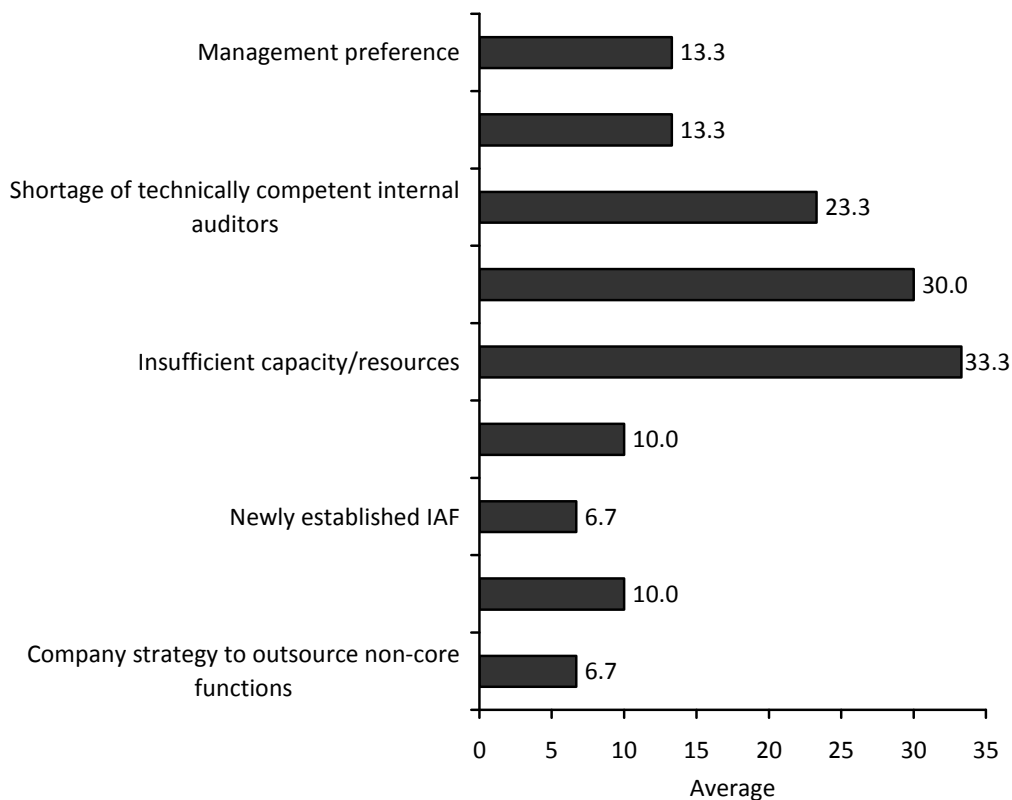


□ CAE – Reasons for outsourcing internal audit services

CAE respondents considered two reasons for the decision to outsource/co-source internal audit services to be extremely important, namely insufficient capacity/resources within their own companies (mean = 33.3) and the fact that outsourcing provides better access to specialised technical expertise (mean = 30.0) figure 23).

Figure 23: CAE – Reasons for outsourcing/co-sourcing internal audit services

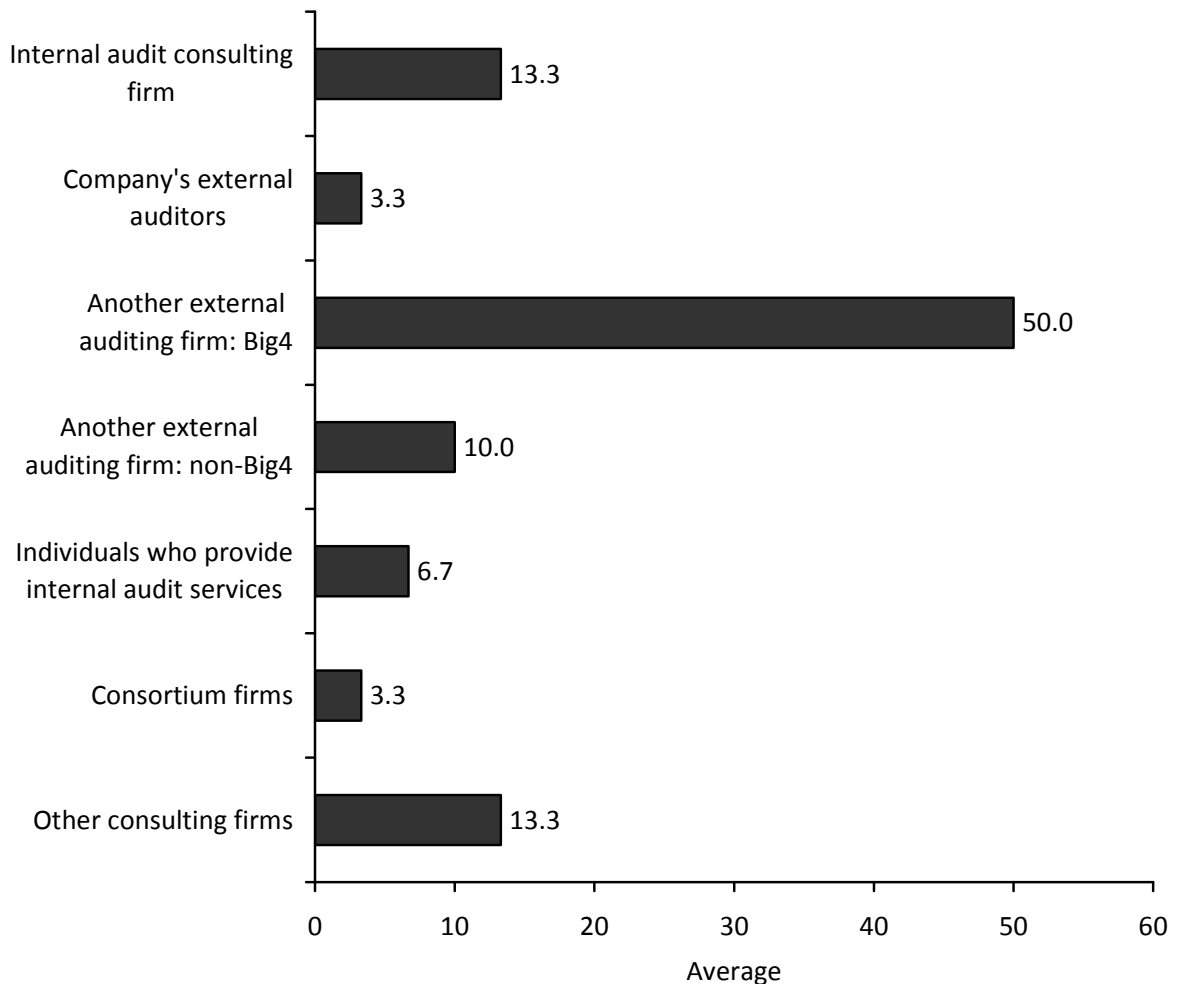
Extremely important (mean ≥ 30.00); Very important ($20.00 \leq \text{mean} < 30.00$); Important ($10.00 \leq \text{mean} < 20.00$); Reasonably important ($5.00 \leq \text{mean} < 10.00$); Not important (mean < 5.00)



□ CAE – parties to whom internal audit services are outsourced

As in the case of the CEO/CFO/COO respondents (figure 25), CAE respondents also indicated that the Big 4 external auditing firms, excluding the company’s own external auditors, are the major sources to which IAFs are outsourced (figure 24). The other parties to whom IAFs are outsourced are other consulting firms, internal audit consulting firms and other external non Big 4 auditing firms. However, CEO/CFO/COO respondents indicated a lower extent of usage of the latter firms, than the extent indicated by CAE respondents.

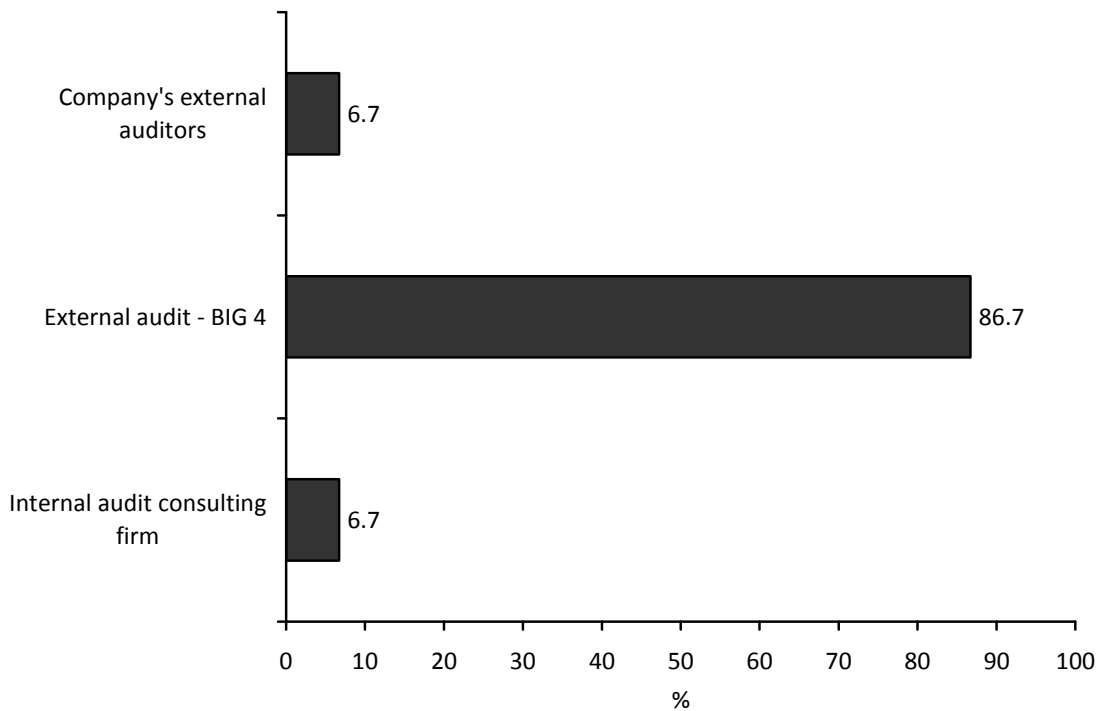
Figure 24: CAE – Parties to whom internal audit services are outsourced



□ CEO/CFO/COO – parties to whom internal audit services are outsourced

Figure 25 reflects the CEO/CFO/COO respondents' responses regarding the parties to whom the internal audit services are outsourced. These activities are mainly outsourced to one of the Big 4 external auditing firms. Internal auditing consulting firms and their company's own external auditors are the parties that are used to a limited extent. The usage of the latter may cause some concern because the external auditors' independence could be influenced. The data contained in figures 14 and 15 reflect that both CAC and CEO/CFO/COO respondents indicated that 46.7% of internal audit services were outsourced.

Figure 25: CEO/CFO/COO – Parties to whom internal audit services are outsourced



2.3.3 Areas of significant use of in-house and co-sourced/outsourced internal audit services

Section 2.3.3 is based on responses to two open-ended questions put to CACs and CEOs/CFOs/COOs. Both these categories of respondents were invited to list any areas in which, in their opinion, their companies would make significant use of their IAFs in future. The areas identified by the respondents are listed in tables 1 and 2 below.

Table 1: CAC and CEO/CFO/COO – Areas in which future significant use could be made of in-house internal audit services

CAC	CEO/CFO/COO
Assurance	Review of audit committee plan
Assessment of employee excellence	Cash management
Regulatory compliance and monitoring	Consulting: Design of controls and processes
Due diligence	Ethical code of conduct
Internal investigations	Forensic investigations
Problem solving	Hedging
Environmental issues	Perform Sarbanes Oxley audit/testing
Forensic auditing	Project management
Financial control reviews	Monitoring of vision, strategies and business plans
Inventory audits	Due diligence review inputs
Training and development	Training, supervision and staff performance
Monitoring of management	Assurance
Monitoring of compliance with Sarbanes Oxley requirements	Portfolio management
Portfolio management	High-risk IT reviews
IT systems/developments	
Payroll	
Tenders	
Deterring and identifying fraud	
Identification of risks	
Incentive bonus reviews	
Special projects/investigations	

Table 2: CAC and CEO – Areas in which significant future use could be made of outsourced IAFs

CAC	CEO
Audit risk management system	Review of audit committee plan
Resources management	Risk consulting, control and management
Risk-revenue assurance	Technical assurance
Incentive bonuses	Assurance on IT technology
Whistle blowing	Tenders/contracts
IT audits	Treasury internal audit
Treasury audits	
Valuation of bonds	
Operational risks	
Forensic investigations	
Offshore operations	
Skills shortages	
Sarbanes Oxley requirements	

2.4 SERVICES OF IAFs AND AUDIT APPROACHES FOLLOWED

Section 2.4 presents an overview of the services rendered by IAFs. It is based on the information provided by CAE respondents and presents the following information:

- Services currently rendered/to be rendered in future by IAFs;
- Average time allocated to services currently rendered by in-house IAFs, other internal departments and external parties;
- Average time expected to be spent on services in future by in-house IAFs and external parties;
- Approaches followed by IAFs;
- Perceived importance of services rendered by IAFs; and
- Compliance with *Standards*.

2.4.1 CAE – services currently rendered/to be rendered in future by IAFs

Figures 26, 27, 28, 29, 30 and 31 are based on 13 identified services that are rendered by IAFs.

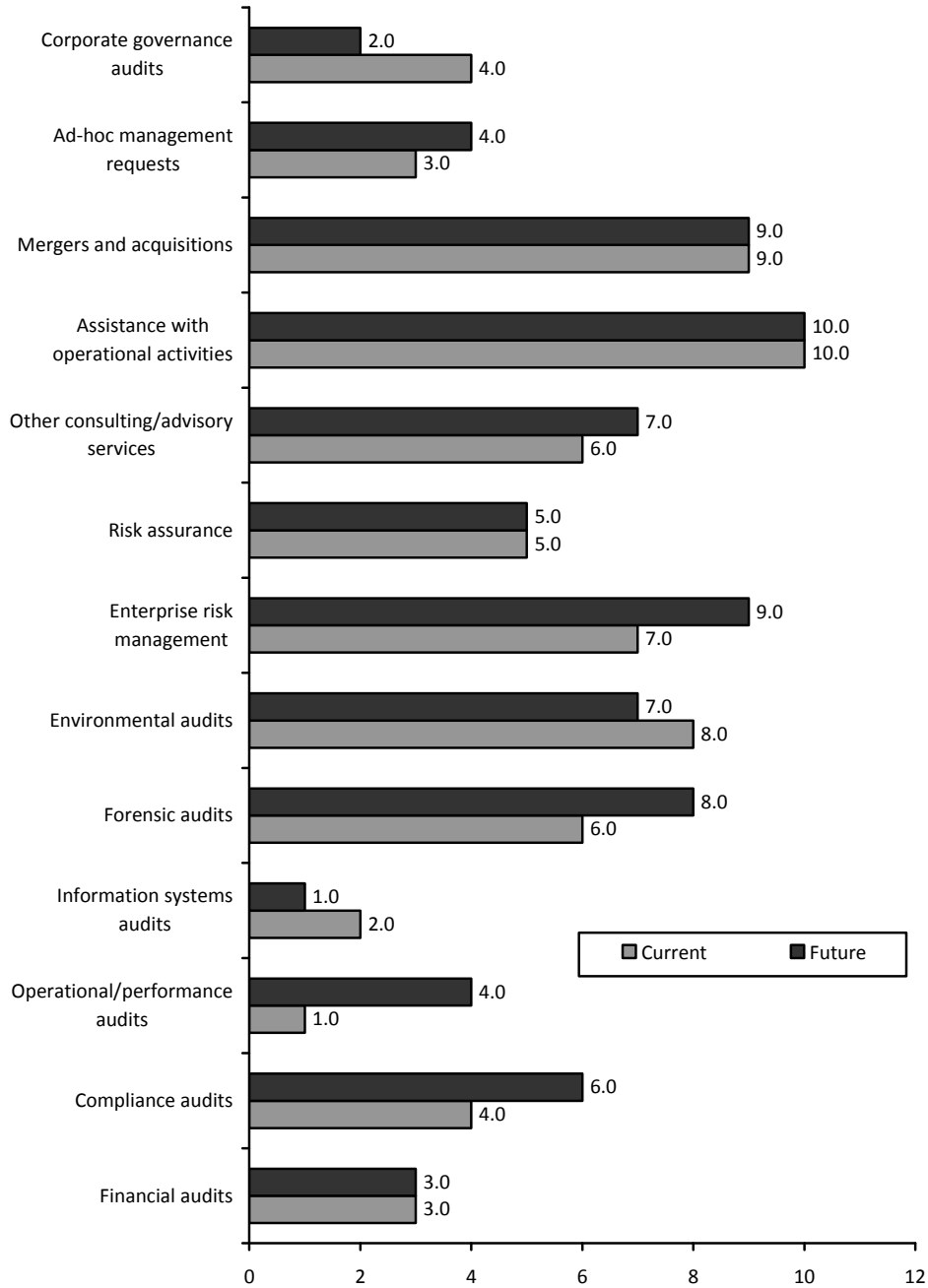
Figure 26 reflects the views of CAE respondents regarding the current services that their IAFs render and the services that they anticipate their IAF will render in future. These views are presented in a ranking order where 1 indicates the service most performed by a company's IAF and 9 the service least performed. A score of 10 represents services not performed by the IAF.

The majority of CAE respondents (figure 26) indicated that their IAF's services currently focus on operational/performance audits (1), information systems audits (2), financial audits (3) and the execution of *ad hoc* management requests (3). There is a slightly lower level of consensus on the part of CAE respondents regarding their IAFs' current rendering of compliance audits and corporate governance audits. Other services currently rendered by IAFs, include forensic audits, risk-assurance and other consulting or advisory services, mergers and acquisitions, enterprise risk management and environmental audits. CAE respondents indicated that their IAFs do not currently render assistance with operational activities.

In respect of services rendered by IAFs, figure 27 reflects that the actual time spent by IAFs of different CAE respondents, corresponded with the above-mentioned on the types of services currently rendered by their IAFs. By far the most hours are currently spent on operational/performance audits, information system audits and financial audits.

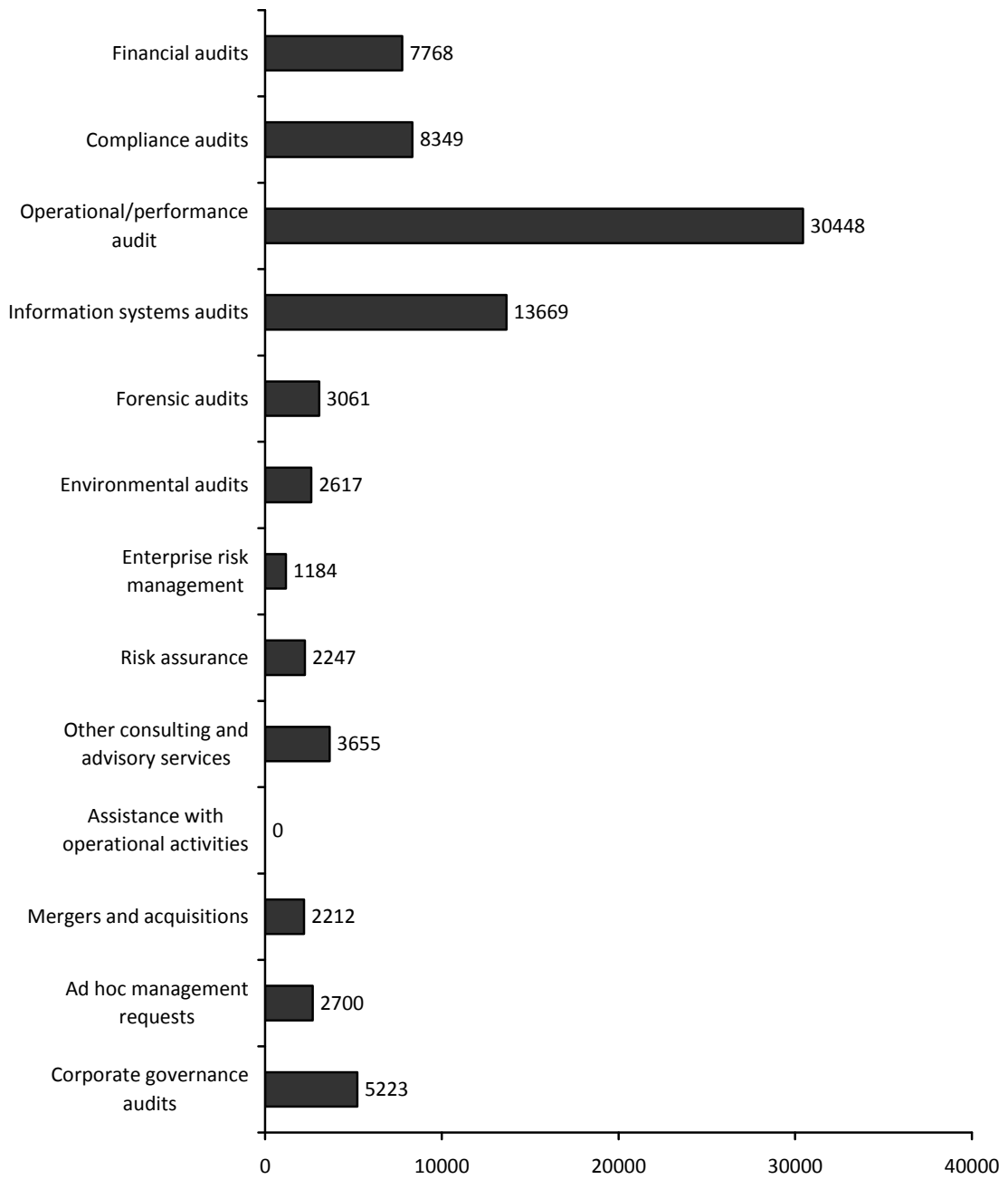
Although CAE respondents perceive corporate governance audits to be an important service that is currently rendered by their IAFs, the actual time spent (figure 27) and estimated time that will be spent (figure 28) on those audits in future does not reflect that importance. This discrepancy could be ascribed to the fact that a corporate governance audit is a high-level audit and is therefore less time consuming.

Figure 26: CAE – Internal audit services currently rendered/to be rendered in future



Rating: 1 = most performed service; 9 = least performed service
10 = service not performed

Figure 27: CAE – Total average annual time (in hours) allocated to various current internal audit services rendered by IAFs



The data in figure 28 reflects the estimated time that will be spent on internal audit services by IAFs in future, as perceived by CAE respondents. It clearly reflects that the emphasis of IAFs will remain compliance audits, operational/performance audits and information systems audits, followed by financial audits. CAE respondents expect that the time that IAFs spend on compliance audits will increase tenfold in future. This expectation indicates a strongly increased future demand for internal audit staff.

Figure 29 reflects the number of hours spent per annum on internal audit services rendered by another department in CAE respondents' own companies. According to CAE respondents, such other departments are not solely responsible for any internal audit services but assist to a limited extent with information systems audits and corporate governance audits.

Figure 28: CAE – Average annual time (in hours) expected to be spent in future on various internal audit services rendered by IAFs

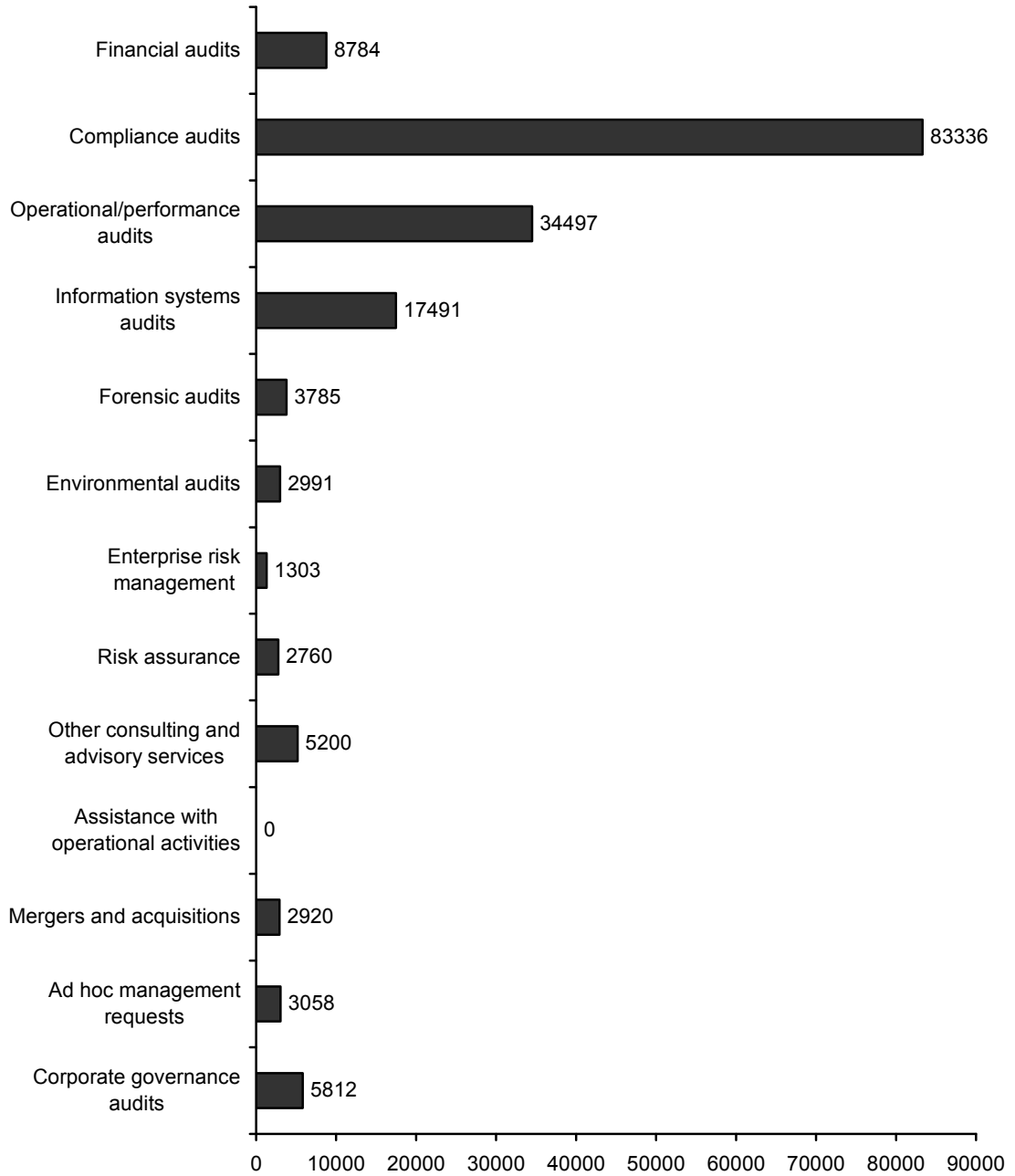
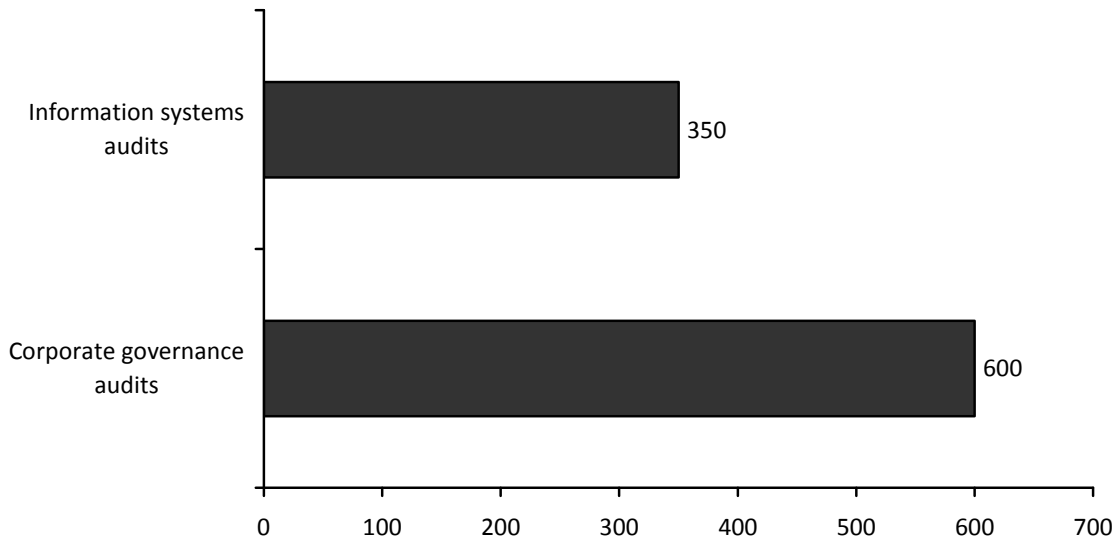


Figure 29: CAE – Average annual time (in hours) allocated to various current internal audit services* rendered by another internal department



* Services not listed or not measurable separately = 0

Figure 30 reflects the number of hours spent by an external party on outsourced internal audit services. CAE respondents indicated that external parties are not solely responsible for any internal audit services but assist to a limited extent with operational/performance audits and financial audits. They also assist to a very limited extent with information systems audits and environmental audits while they also provide some input on forensic audits. These respondents also indicated that no internal auditing activities with regard to mergers and acquisitions or other consulting and advisory services are outsourced. The fact that outsourced internal audit services comprise mainly of limited assistance with operational/performance audits and financial audits supports the earlier indications by CAC and CEO/CFO/COO respondents that outsourcing is a result of their companies' need for specialised technical expertise (figure 18 and 19).

Figure 30: CAE – Average annual time (in hours) allocated to various current internal audit services rendered by an external party

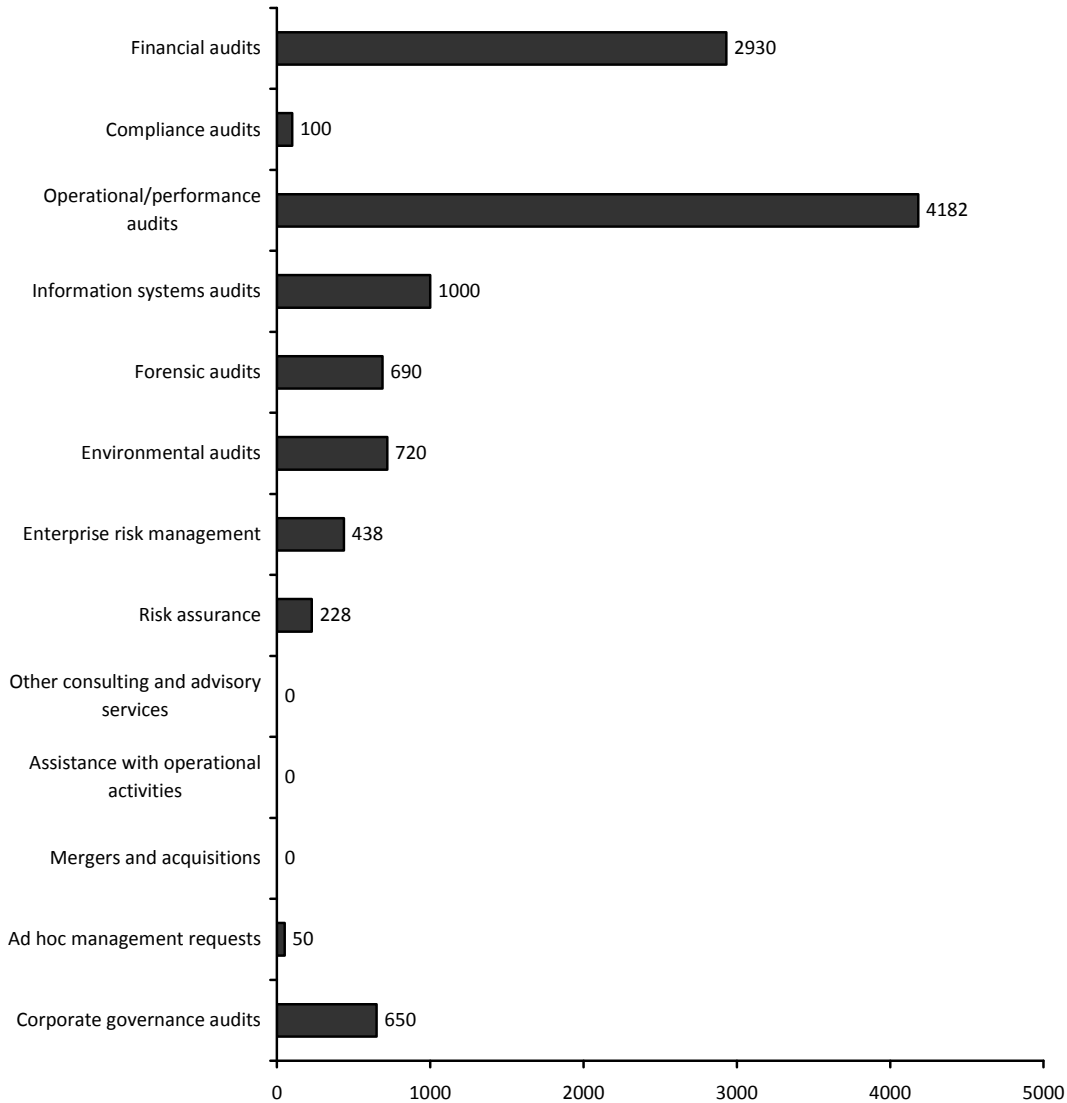
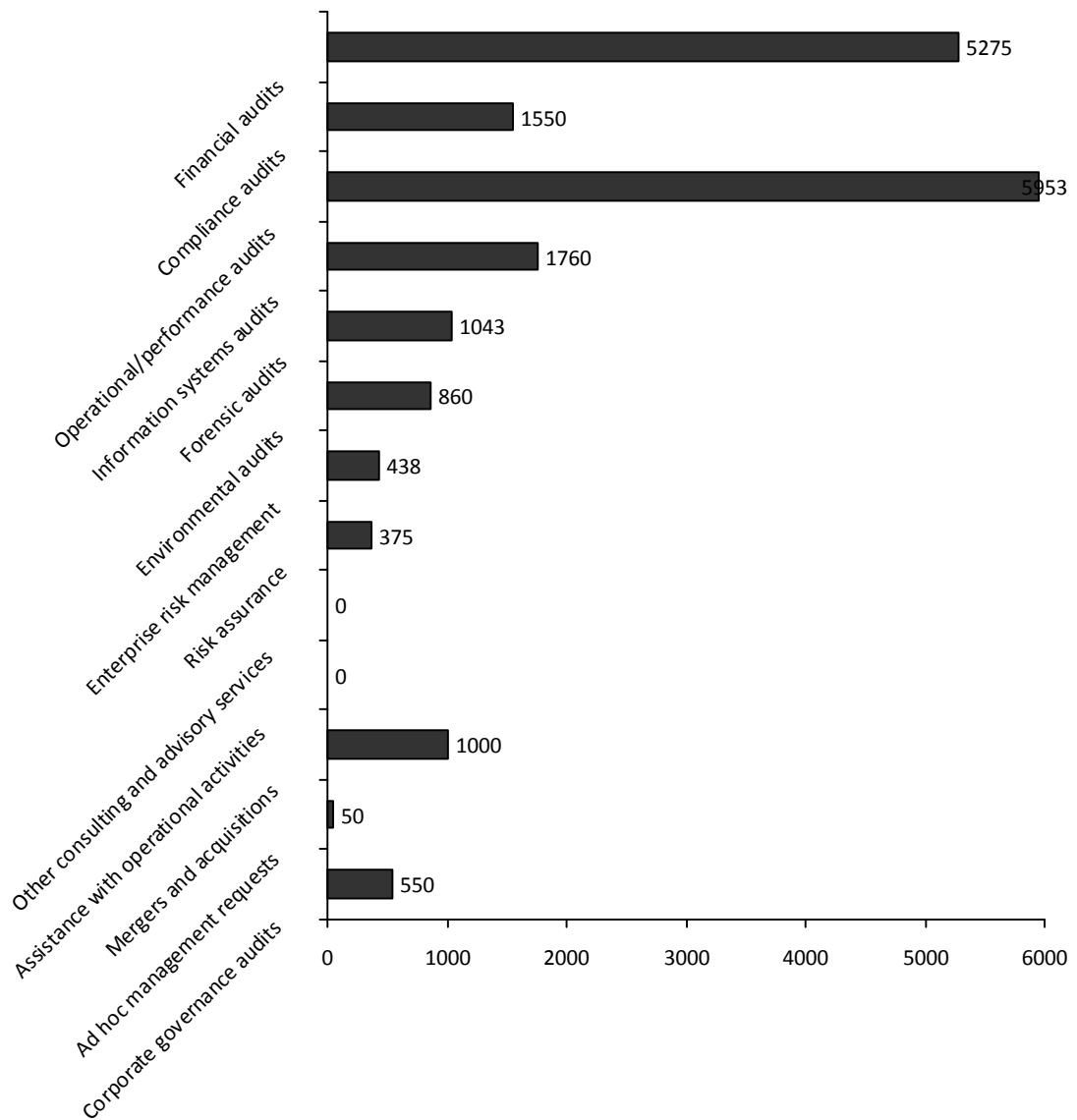


Figure 31 reflects the estimated time that external parties will spend on internal audit services in future, as perceived by CAE respondents. They expect that the future involvement of external parties will primarily be in respect of operational/performance audits and financial audits. This expectation corresponds with the *status quo* (figure 30). They also expect that external parties will in future be involved to a lesser extent in information systems audits, forensic audits and compliance audits.

Figure 31: CAE – Average annual time (in hours) expected to be spent on future internal audit services rendered by external parties



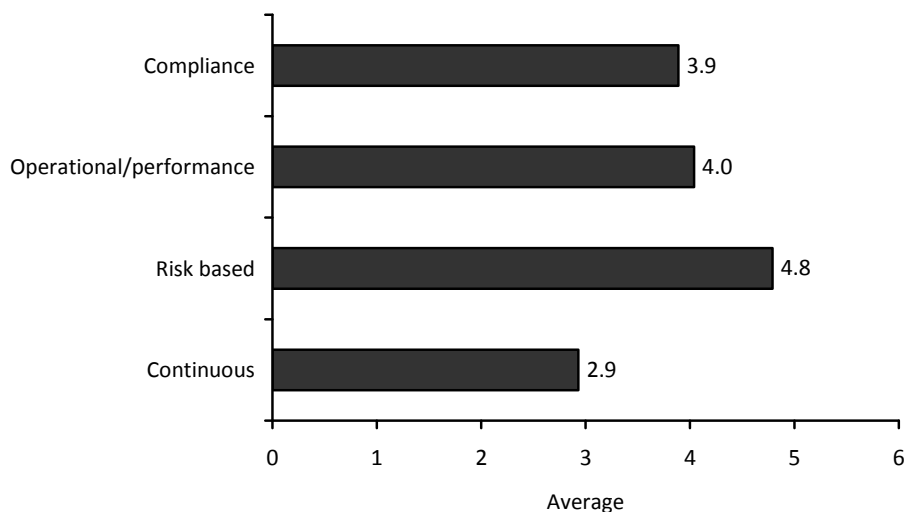
2.4.2 CAE – audit approaches followed by IAFs

The emphasis placed on various audit approaches by IAFs was measured by means of a five-point scale that ranges from 1 (not important) to 5 (extremely important). A response of 3 is taken to indicate an importance that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

Figure 32 reflects CAE respondents' perceptions of the emphasis placed on each of four different approaches by IAFs.

Figure 32: CAE – Emphasis placed on audit approaches by IAFs

(Agreement scale anchors: 1 = strongly disagree, 5 = strongly agree)
Extremely important (mean ≥ 4.00); Very important ($3.00 \leq \text{mean} < 4.00$); Important ($2.00 \leq \text{mean} < 3.00$); Reasonably important ($1.00 \leq \text{mean} < 2.00$); Not important (mean < 1.00)



CAE respondents perceive the risk-based audit approach (mean = 4.8) and the operational/performance audit approach (mean = 4.0) to be extremely important. They perceive a compliance approach (mean = 3.9) to be very important, while they are of the opinion that a continuous approach receives the least emphasis from IAFs.

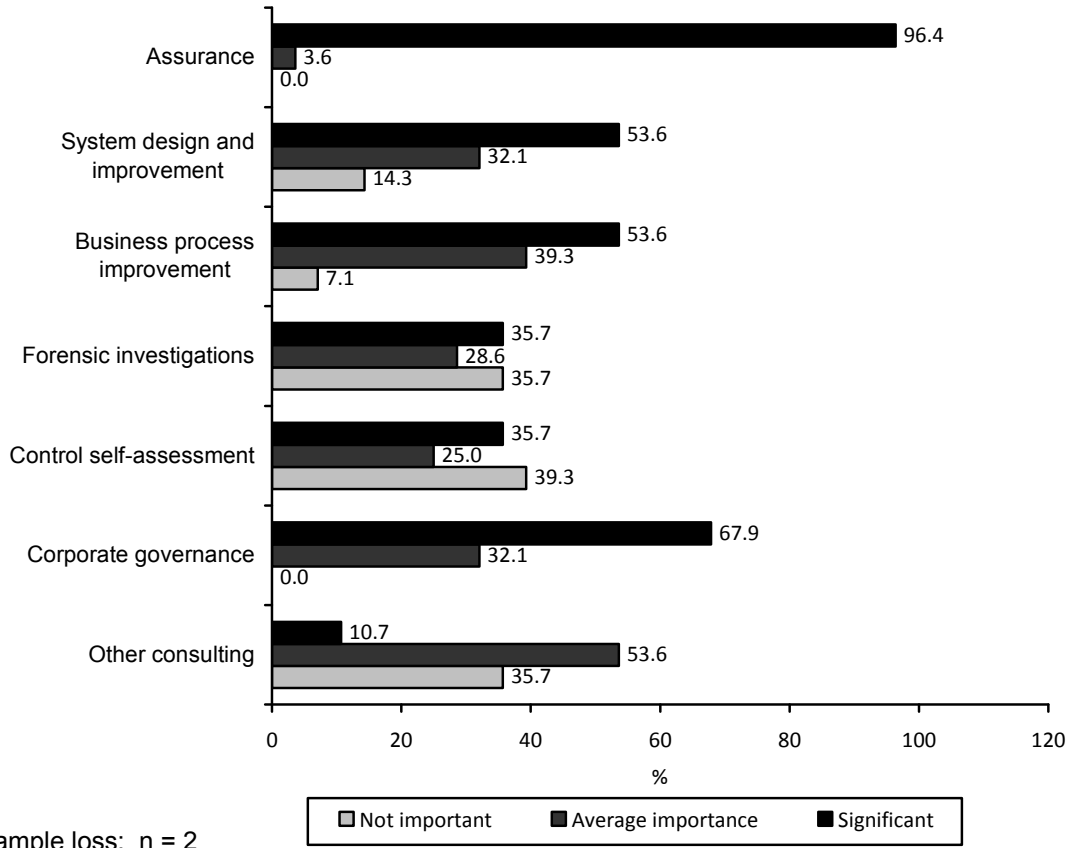
□ **CAE – Perceived importance of services rendered by IAFs**

CAE respondents' perceptions of the relative importance of seven IAF services are reflected in figure 33. CAE respondents were requested to rate services as being not important, of average importance or of significant importance. Assurance was rated of significant importance by 96.4% of CAE respondents. Corporate governance audits were rated of significant importance by 67.9% of CAE respondents, while the remaining 32.1% of these respondents rated it of average importance.

The majority of CAE respondents (53.6%) rated system design and improvement as well as business process improvement of significant importance, while approximately a third (32.1% and 39.3% respectively) rated these of average importance. CAE respondents were not in agreement on the importance of forensic investigations and control self-assessments. Approximately one-third (35.7% in both instances) rated these two services to be of significant importance, while the remaining respondents either rated them of average importance or not important at all.

The majority of CAE respondents (53.6%) rated other consulting and advisory services of average importance, while 35.7% rated these services as not important. Only 10.7% of these respondents rated the latter service as of significant importance.

Figure 33: CAE – Rating of the importance of IAF services



2.5 STATUS OF IAFs

In section 2.5, the responses from CACs and CEOs/CFOs/COOs related to the status of IAFs are presented and discussed. The following matters are addressed:

- Level of satisfaction with various IAF attributes;
- Current value added by IAFs and the value to add in future;
- Extent of implementation of IAF recommendations;
- Reliance on the work of IAFs by external auditors and co-ordination between IAFs and external auditors; and
- CAE's perceptions of the status of their IAFs.

2.5.1 Status of IAFs

Section 2.5.1 is based on the perceptions of CAC and CEOs/CFOs/COOs respondents to the factors that affect the status of their IAFs.

□ **CAC and CEO/CFO/COO – levels of satisfaction with various attributes of IAFs**

The level of satisfaction with various attributes of IAFs was measured by means of a five-point scale that ranges from 1 (not satisfied) to 5 (extremely satisfied). A response of 3 is taken to indicate satisfaction that is greater than 2 and lesser than 4 rather than being an indication of central tendency bias.

CAC respondents were extremely satisfied (mean ≥ 4) that their in-house IAFs demonstrate compliance with each of the six attributes that are listed (figure 34) as well as with the competency of their outsourced IAFs. Further they were very satisfied with the commitment, effectiveness of services rendered, flexibility and value added by their outsourced IAFs ($3.00 \leq \text{mean} < 4.00$). They were also very satisfied with the extent to which their outsourced IAFs fulfilled their expectations.

The perceptions of CEO/CFO/COO respondents reveal that they were extremely satisfied (mean ≥ 4) with the extent to which their in-house IAF demonstrates compliance with each of the six attributes that were listed (figure 35), as well as with the competency (mean = 4.0), commitment (mean = 4.1) and flexibility (mean = 4.2) of their outsourced IAFs. The CEO/CFO/COO respondents appeared to be very satisfied ($3.00 \leq \text{mean} < 4.00$) with the effectiveness of the services rendered and value added by their outsourced IAFs. Their satisfaction also extended to their outsourced IAF's fulfillment of their expectations.

Similar perceptions were reported by CAC respondents (figure 34). These respondents reported that they were extremely satisfied with the extent to which their in-house IAFs complied with each of the six attributes listed. They were equally satisfied with the competency displayed by their outsourced IAFs. With regard to the other attributes of their outsourced IAFs, CAC respondents reported that they were very satisfied.

Figure 34: CAC – Levels of satisfaction with various attributes of in-house/outsourced IAFs

Extremely satisfied (mean ≥ 4.00); Very satisfied ($3.00 \leq \text{mean} < 4.00$); Satisfied ($2.00 \leq \text{mean} < 3.00$); Reasonably satisfied ($1.00 \leq \text{mean} < 2.00$); Not satisfied (mean < 1.00)

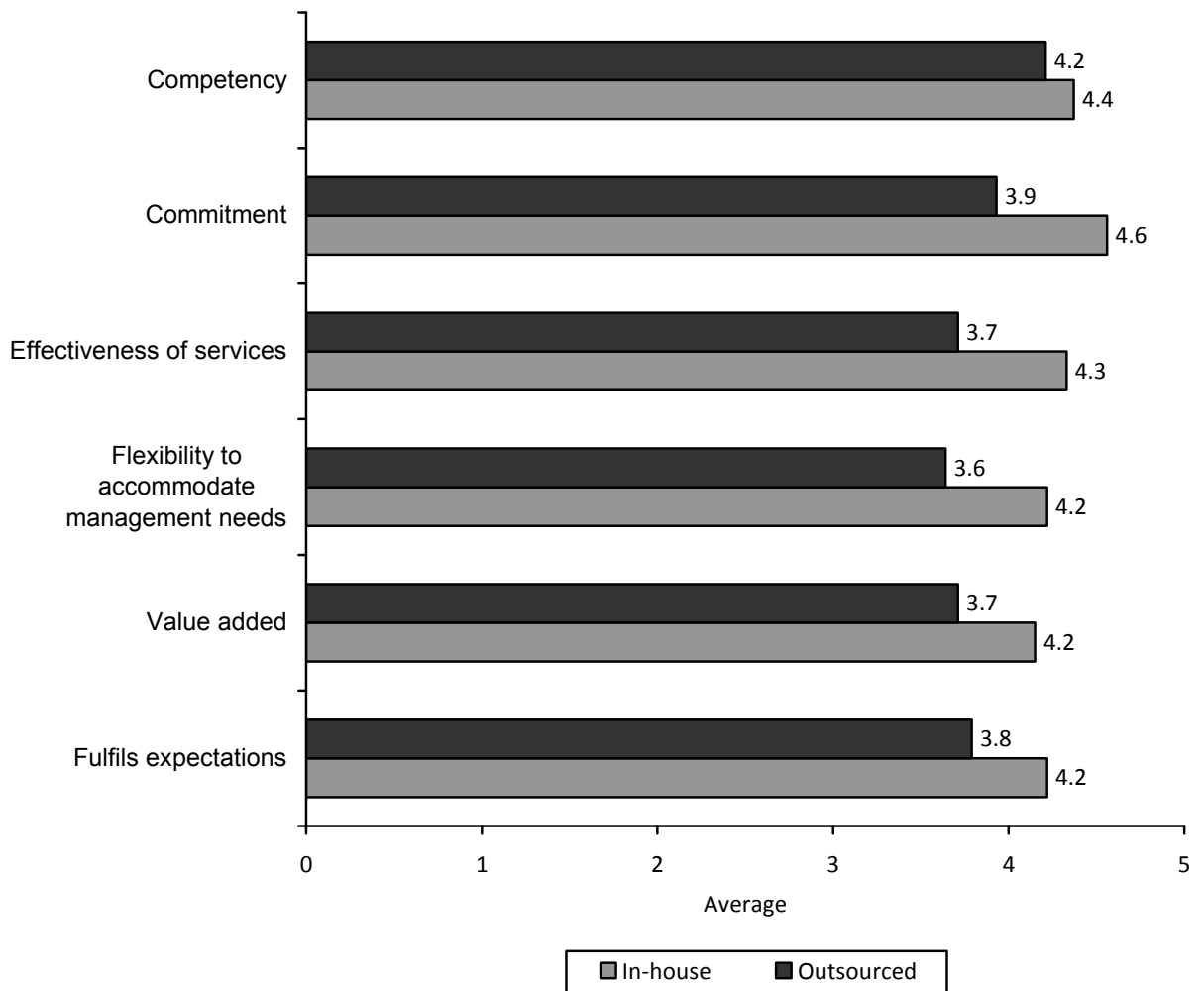
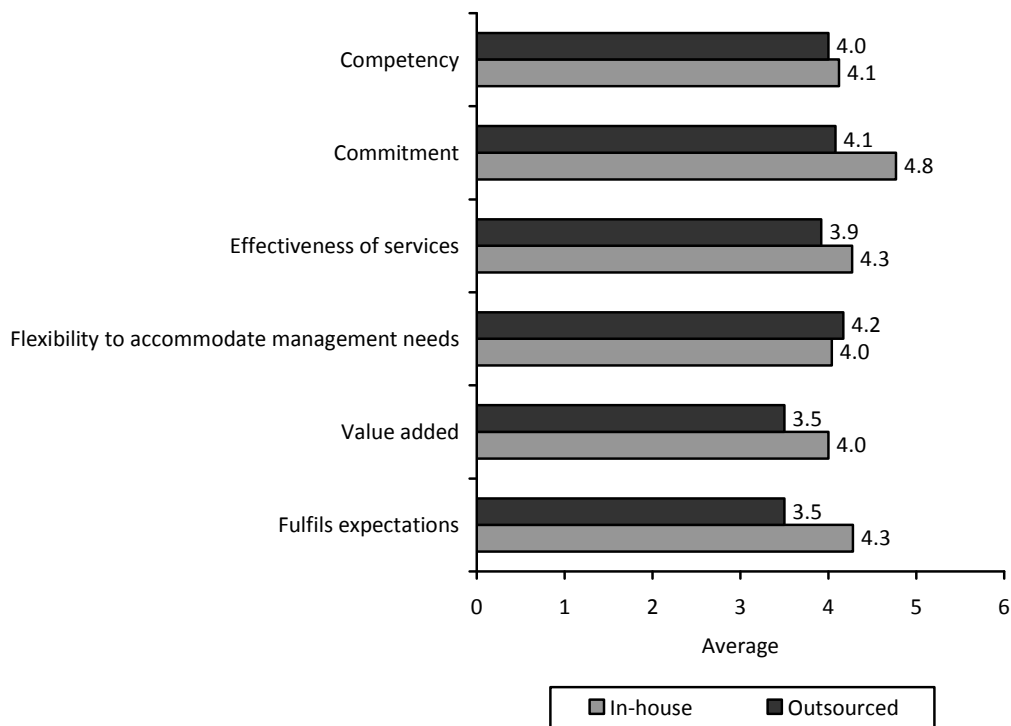


Figure 35: CEO/CFO/COO – Levels of satisfaction with various attributes of IAFs (in-house and outsourced)

Extremely satisfied (mean ≥ 4.00); Very satisfied ($3.00 \leq \text{mean} < 4.00$); Satisfied ($2.00 \leq \text{mean} < 3.00$); Reasonably satisfied ($1.00 \leq \text{mean} < 2.00$); Not satisfied (mean < 1.00)



□ **CAC and CO/CFO/COO – Current value added by IAFs**

The perceived current value added by IAFs by means of services that they render were measured by means of a five-point scale that ranges from 1 (significant value added) to 5 (no value added). A response of 3 is taken to indicate a degree of value added that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

CAC respondents perceived that in-house IAFs add much value ($1.00 \leq \text{mean} < 2.00$) through seven of the eight listed activities that they perform (figure 36). In-house IAFs are perceived to add only average value with regard to assistance provided in respect of mergers and acquisitions. Only outsourced IAFs are perceived to add reasonable value in forensic investigations (mean = 3.1) and services they render in respect of mergers and acquisitions (mean = 3.2). CAC respondents considered outsourced IAFs to add average value in respect of all the other activities listed in figure 36.

CEO/CFO/COO respondents perceived in-house IAFs to currently add much value ($1.00 \leq \text{mean} < 2.00$) in respect of all the listed services, except for services that relate to mergers and acquisitions (figure 37). The perceptions correspond with those of CAC respondents.

Figure 36: CAC – Current value added by IAFs (in-house and outsourced)

(Scale anchors: 1 = significant value, 5 = no value)
 No value added ($\text{mean} \geq 4.00$); Reasonable value added ($3.00 \leq \text{mean} < 4.00$); Average value added ($2.00 \leq \text{mean} < 3.00$); Much value added ($1.00 \leq \text{mean} < 2.00$); Significant value added ($\text{mean} < 1.00$)

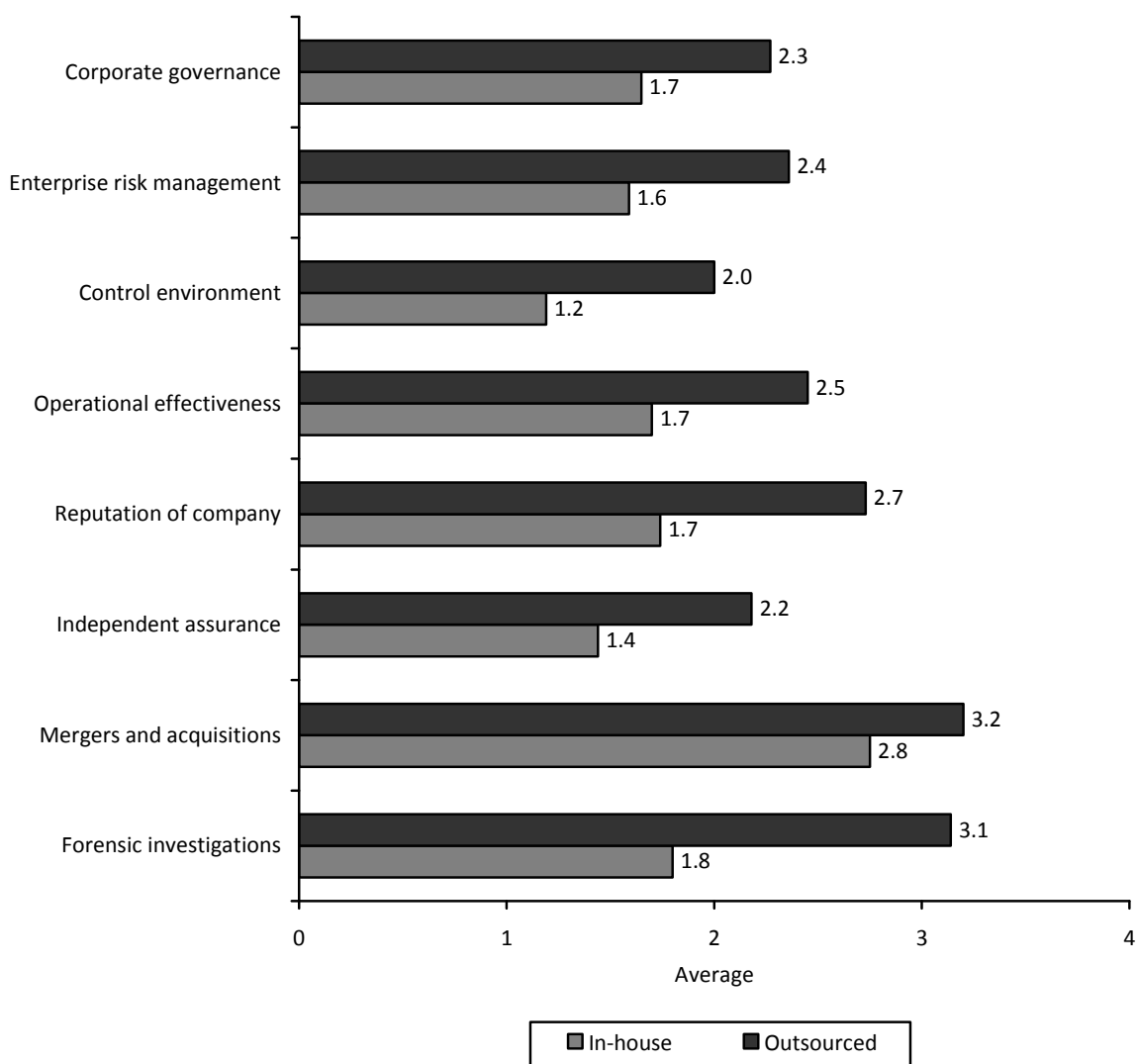
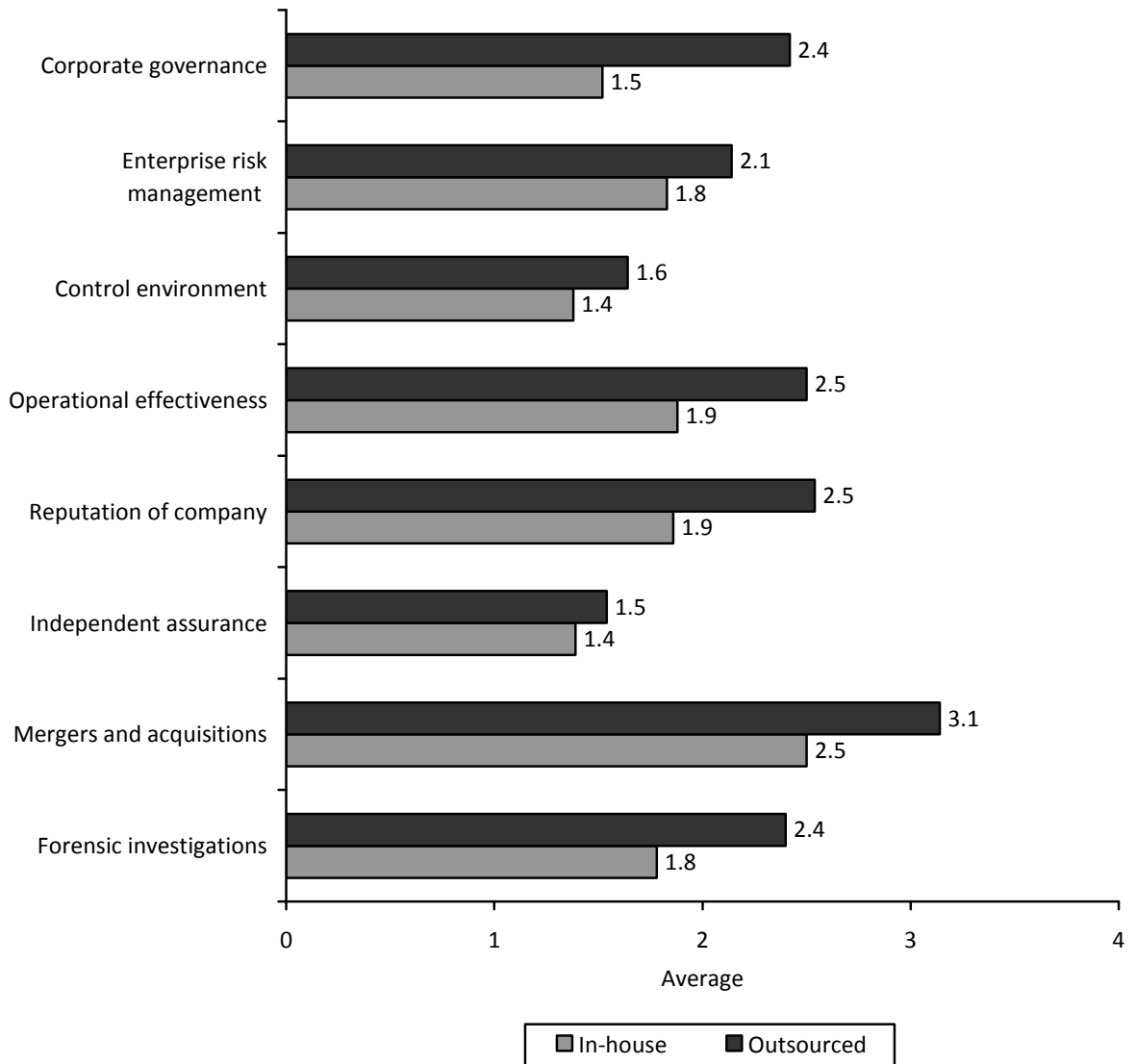


Figure 37: CEO/CFO/COO – Value currently added by IAFs (in-house and outsourced)

(Scale anchor: 1 = significant value, 4 = no value)

No value added (mean ≥ 4.00); Reasonable value added ($3.00 \leq \text{mean} < 4.00$); Average value added ($2.00 \leq \text{mean} < 3.00$); Much value added ($1.00 \leq \text{mean} < 2.00$); Significant value added (mean < 1.00)



CEO/CFO/COO respondents perceived outsourced IAFs to currently add reasonable value by means of their services in respect of mergers and acquisitions (mean = 3.1) while CAC respondents had a similar view on forensic investigations (mean = 3.1) and services in respect of mergers and

acquisitions (mean = 3.2) (figure 36) rendered by their outsourced IAFs. CEO/CFO/COO respondents considered their outsourced IAFs to currently add average value by means of all the other listed services that they rendered. They did, however, consider their outsourced IAFs to add much value in respect of providing independent assurance and their activities with regard to their companies' control environments. CAC respondents perceived their outsourced IAFs to currently add value to an average extent by means of all the other activities that they rendered (figure 36).

□ **CAC and CEO/CFO/COO – Value envisaged to be added by IAFs in future**

The contributions that IAFs are envisaged to make in future by means of various services that they render were measured by means of a five-point scale that ranges from 1 (significant value added) to 5 (no value added). A response of 3 is taken to indicate a degree of value to be added that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

CAC respondents indicated that they envisaged that in-house IAFs will in future probably add much value (mean ≤ 2) in respect of seven of the eight services listed in figure 38. They expected that in-house IAFs will in future add value to an average extent in respect of mergers and acquisitions activities (mean = 2.4).

In the case of outsourced IAFs, CAC respondents anticipated that value will be added to an average extent by future forensic investigations (mean = 2.0), mergers and acquisitions (mean = 2.3), services relating to the reputation of the company (mean = 2.4) and reviews to determine operational effectiveness (mean 2.1). They envisaged that outsourced IAFs will in future add much value in respect of the remainder of the listed services ($1.00 \leq \text{mean} < 2.00$) (figure 38).

Perceptions on current value added that are presented in figure 36 were compared to perceptions on future value that will be added that are presented in figure 38. It is apparent that CAC respondents envisaged that for six of the eight services listed the value that will be added by outsourced IAFs will increase in future. CAC respondents' perceptions regarding the value that will be added by in-house IAFs in future appear to remain at the significant level.

Figure 38: CAC – Value envisaged to be added by IAFs (in-house and outsourced) in future

(Scale anchors: 1 = significant value, 5 = no value)

No value added (mean ≥ 4.00); Reasonable value added ($3.00 \leq \text{mean} < 4.00$); Average value added ($2.00 \leq \text{mean} < 3.00$); Much value added ($1.00 \leq \text{mean} < 2.00$); Significant value added (mean < 1.00)

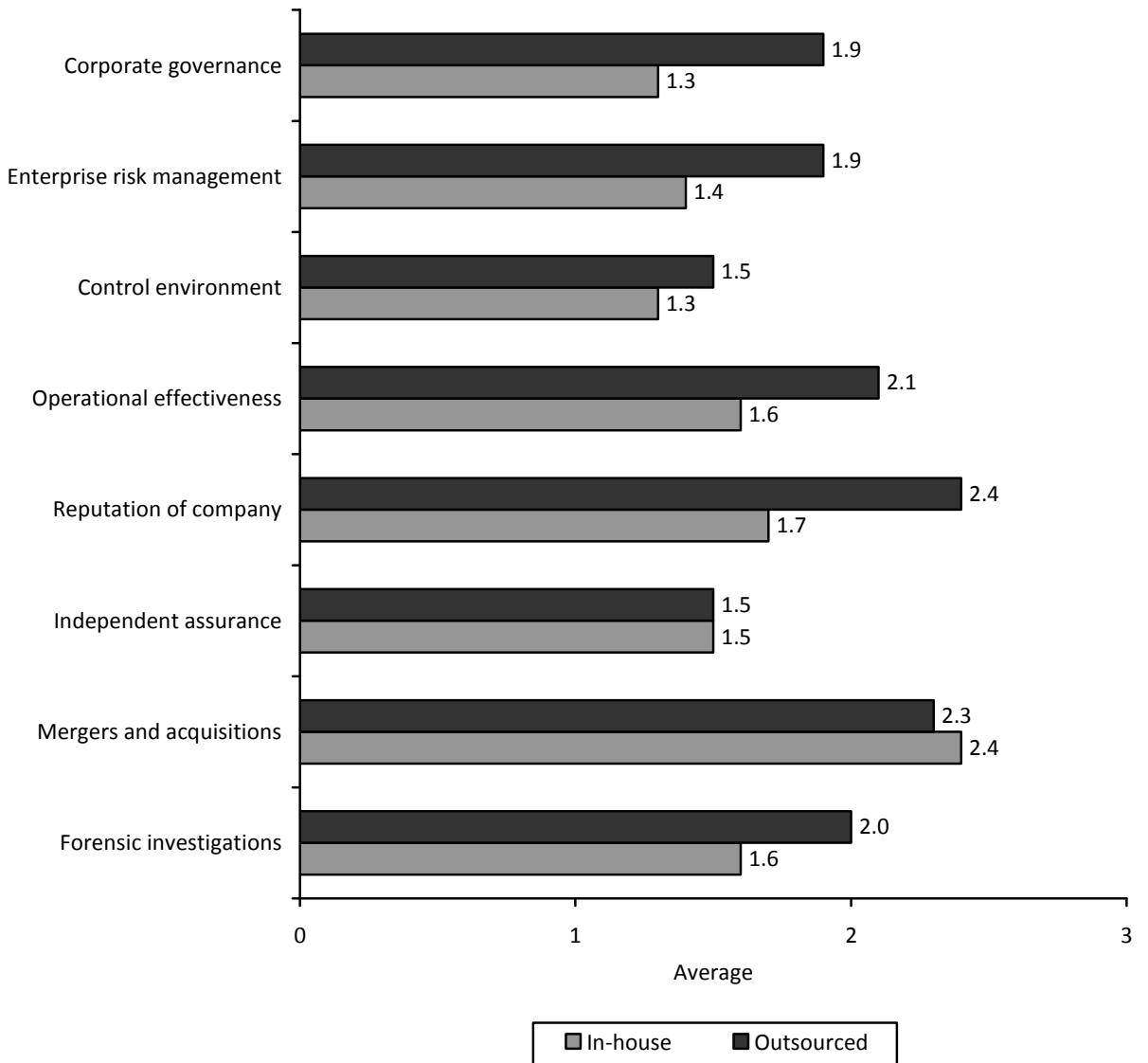
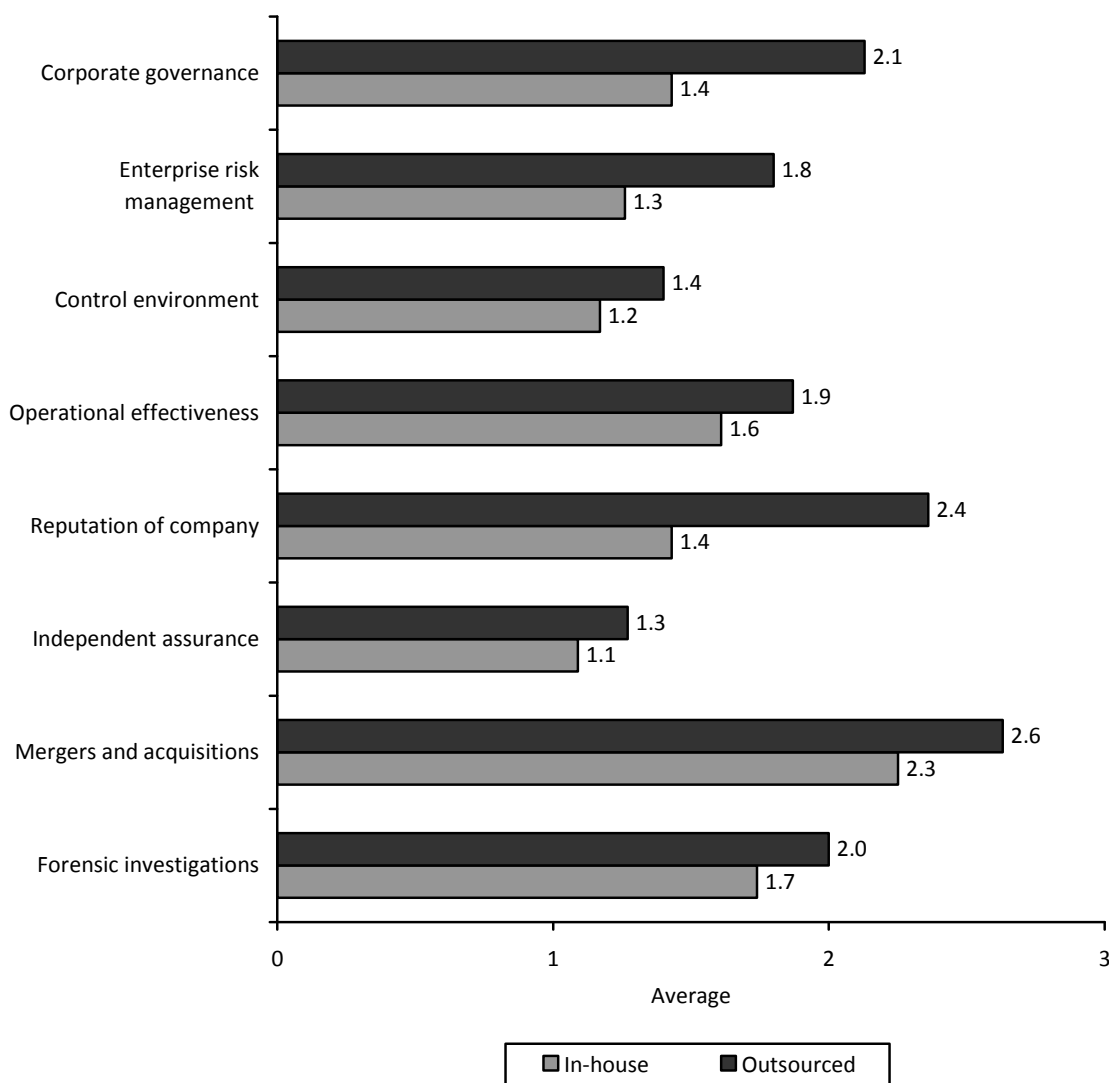


Figure 39: CEO/CFO/COO – Future expectations of the value to be added by IAFs (in-house and outsourced)

(Scale anchor: 1 = significant value, 4 = no value)
 No value added (mean ≥ 4.00); Reasonable value added ($3.00 \leq \text{mean} < 4.00$); Average value added ($2.00 \leq \text{mean} < 3.00$); Much value added ($1.00 \leq \text{mean} < 2.00$); Significant value added (mean < 1.00)



CEO/CFO/COO respondents indicated that they envisage that their in-house IAFs will in future probably add much value (mean ≤ 2) to seven of the eight services listed (see figure 39). They also envisaged that in-house IAFs will in future add average value to their companies' mergers and acquisitions (mean = 2.3). The perceptions correspond with the reported perceptions of the CAC respondents (figure 38).

Outsourced IAFs were anticipated by CEO/CFO/COO respondents to add value in future to an average extent by means of forensic investigations (mean = 2.0), contributions to mergers and acquisitions (mean = 2.6), services relating to the reputation of their companies (mean = 2.4) and corporate governance audits (mean = 2.1) (figure 39). CAC respondents anticipated that outsourced IAFs will add value in future to an average extent by means of the rendering of the latter services (except for corporate governance audits) and that those IAFs will add value in future to an average extent by means of reviews to determine operational effectiveness (figure 38).

In respect of the remainder of the services of IAFs, both CEO/CFO/COO and CAC respondents perceived that outsourced IAFs will probably add much value in future ($1.00 \leq \text{mean} < 2.00$).

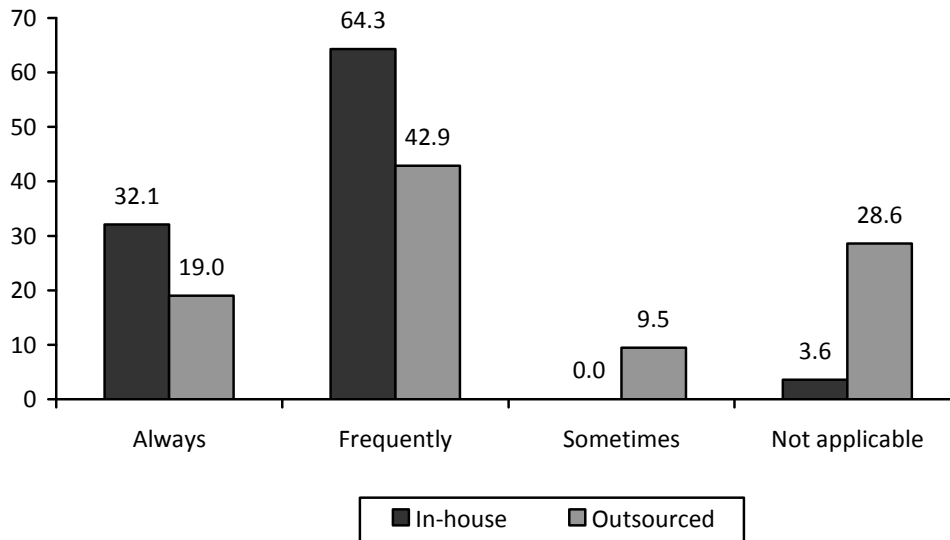
Perceptions reflected in figures 38 and 39 were compared to determine whether a relationship exists between the perceptions of CEO/CFO/COO respondents on the current value added by IAFs and the future value that they are expected to add. These respondents perceived that the value added by outsourced IAFs in respect of ERM services and reviews of operational effectiveness will probably increase from the current position. Although CAC respondents (figure 38) expected an increase in the value to be added in future in respect of six of the eight listed services and CEO/CFO/COO respondents held a similar view in respect of only the two activities mentioned above, these two groups of respondents had similar expectations regarding the value that will be added by outsourced IAFs in future. The difference between the perceptions of the two groups of respondents is in respect of the current value added by outsourced IAFs (figures 38 and 39).

□ **CAC – Implementation of IAF recommendations**

Figure 40 reflects the perceived extent to which the responding companies implement the recommendations that were made by their in-house and/or outsourced IAFs.

In the opinion of CAC respondents, the recommendations made by their in-house IAFs were always implemented by approximately a third (32.1%) of the surveyed companies and frequently implemented by 64.3% of those companies. In respect of outsourced IAFs, the perceptions of CAC respondents were that a much lower percentage of companies implemented the recommendations that were submitted by such outsourced IAFs (19.0% and 42.9% respectively).

Figure 40: CAC – Extent to which the recommendations of IAFs are implemented by companies (in-house* and outsourced)**



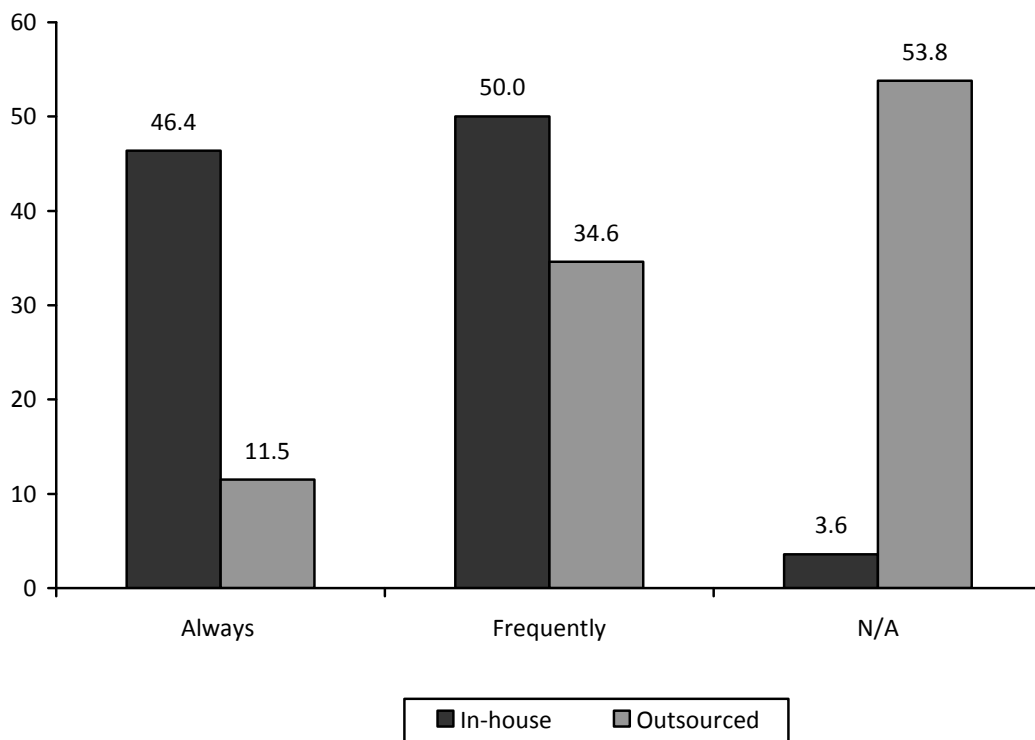
* Sample loss: n = 2 ** Sample loss: n = 9

Figure 41 should be read in conjunction with figure 40. Figure 41 reflects the extent to which the surveyed companies implement the recommendations that were made by their in-house and outsourced IAFs.

Less than half (46.4%) of CEO/CFO/COO respondents reported that recommendations made by their in-house IAFs were always implemented while half of these respondents reported that such recommendations were frequently implemented. A total of 96.4% (46.4% + 50%) of these respondents therefore reported that the recommendations made by their in-house IAFs were implemented frequently or more often. The percentage of CAC respondents who had this perception also totals 96.4% (32.1% + 64.3%) (figure 40).

The majority of CEO/CFO/COO respondents perceived the recommendations made by their outsourced IAFs not to be applicable. This perception is a reason for concern, especially since those respondents indicated that a high percentage of internal audit services were outsourced or co-sourced (46.7% - figure 15).

Figure 41: CEO/CFO/COO – Extent to which IAFs’ recommendations are implemented by their companies (in-house* and outsourced)**



* Sample loss: n = 2

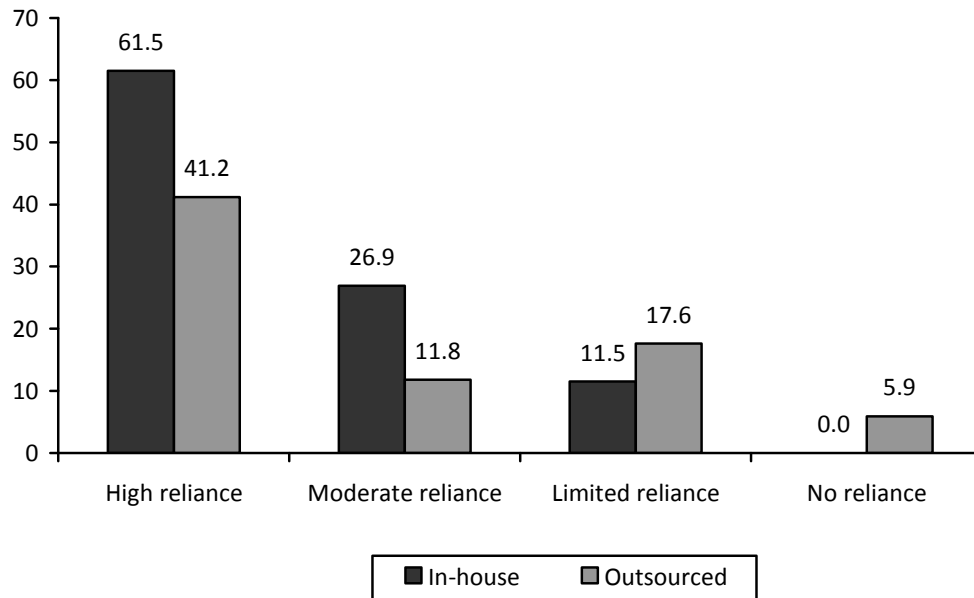
** Sample loss: n = 4

□ CAC – Reliance that external auditors place on IAFs

Figure 42 reflects the perceived reliance that the surveyed companies’ external auditors placed on the work done by their in-house and/or outsourced IAFs as reported by CAC respondents.

A total of 61.5% of CAC respondents perceived that the external auditors of their companies were heavily reliant on the work of their in-house IAFs. In the case of outsourced IAFs, only 41.2% of CAC respondents perceived that their companies’ external auditors were heavily reliant on the work of such IAFs. Only 11.5% of CAC respondents perceived that the external auditors of their companies placed limited reliance on the work of their in-house IAFs. The latter percentage increases to 17.6% in respect of outsourced IAFs. These reported perceptions suggest that a higher percentage of CAC respondents perceived that external auditors placed a high or moderate reliance on the work of their in-house IAFs, which is more than the reliance that such external auditors were perceived to place on the work of outsourced IAFs.

Figure 42: CAC – Ratings of reliance placed by external auditors on the work of IAFs (in-house* and outsourced)**



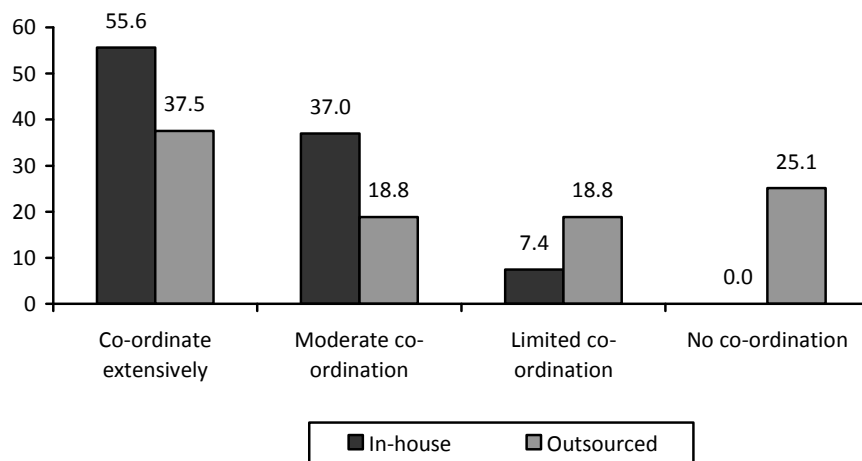
* Sample loss: n = 4 ** Sample loss: n = 13

CAC – Co-ordination between external auditors and an IAF

Figure 43 reflects the level of co-ordination that was perceived to exist between surveyed companies' external auditors and their in-house as well as outsourced IAFs as reported by CAC respondents.

A total of 55.6% of CAC respondents perceived that there was extensive co-ordination between their companies' external auditors and in-house IAFs. While their level of this perception in respect of outsourced IAFs was only 37.5%. Only 7.4% of CAC respondents perceived that there was limited co-ordination between the external auditors and their in-house IAFs. The latter percentage was 18.8% in respect of outsourced IAFs. According to 25.1% of CAC respondents, no co-ordination existed between their companies' external auditors and their outsourced IAFs.

Figure 43: CAC – Ratings of perceived co-ordination between external auditors and an IAF (in-house* and outsourced)**



* Sample loss: n = 3

** Sample loss: n = 14

2.5.2 CAE – Status of IAFs

Section 2.5.2 is based on perceptions reported by CAE respondents in respect of various statements that could impact on their status.

Figure 44 reflects the opinions of CAE respondents on the status of their IAFs. The level of agreement was measured by means of a five-point scale that range from 5 (strongly agree) to 1 (do not agree). A response of 3 is taken to indicate a level of agreement that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

The CAE respondents strongly agree (mean ≥ 4) with the following fourteen statements:

- 1 Their IAFs effectively understand all the key operations of the entire company.
- 2 Recommendations made by their IAFs are implemented by management.
- 3 Internal audits are performed with the emphasis on risk.
- 4 Their IAFs are able to influence key decisions that are taken on matters within their field of expertise.
- 5 Their IAFs are aids to management.
- 6 Their IAFs are held by the board and top management to have a significant role in the enhancement of corporate governance.
- 7 The auditees recognise the value of their IAFs' services.
- 8 Their IAFs are provided with adequate resources to operate effectively.

- 9 Their IAFs should acquire additional skills to meet future requirements.
- 10 The current position of their IAFs is conducive to the long-term interest of their companies.
- 11 When a function/responsibility of an IAF is outsourced/co-sourced, the performance of the contractor is monitored by the CAE.
- 12 Their IAFs are not used to accommodate the non-performing members of staff of other functions.
- 13 Their IAFs are permitted to audit corporate governance.
- 14 The CAE is consulted regularly or the CAE is able to meet with the CAC.

Figure 32 reflects the emphasis that the CAE respondents reportedly place on a risk-based audit approach. The extensive support expressed by these respondents for statement 3 above serves as corroborative evidence of the emphasis that they place on risk-based auditing.

The perceptions reflected in figures 40 and 41, of CAC and CEO/CFO/COO respondents regarding the extent to which the recommendations of their in-house IAFs were implemented differ from CAEs' perceptions in this regard reflected in statement 2 above. Less than half (46.4%) of CEO/CFO/COO respondents were of the opinion that the recommendations made by their in-house IAFs were always implemented and half of those respondents were of the opinion that these recommendations were frequently implemented (figure 41). In the case of CAC respondents, the corresponding percentages were 32.1% and 64.3% respectively (figure 40).

The results reflected in figures 26, 27, 28, 29, 30 and 31 indicate the prevalence of corporate governance audits that are conducted by in-house IAFs. These are corroborated by statement 6 above.

According to CAE respondents, there is a shortage of high-level internal auditing skills, as evident from their extensive support expressed for *statement 9*. This perception is supported by the results reflected in section 2.8.

CAE respondents agreed to a large extent that their IAFs could be regarded as a training ground for operational managers and that their IAFs provided advice to other departments in their companies. These respondents also agreed to a large extent that their IAFs are included in management meetings.

CAE respondents furthermore agreed that their IAFs are regarded as the appropriate department in which to develop inexperienced staff and that they are sources to other departments. Based on these assertions, it could be assumed that a relatively high staff turnover rate could prevail in IAFs (table 10 and figure 60).

The CAE respondents also agree with the statement that their internal audit activities are performed with a view to reducing external audit fees and that they are included as part of the board meetings.

Figure 44: CAE – Status of IAFs

Strongly agree (mean ≥ 4.00); Agree to a large extent ($3.00 \leq \text{mean} < 4.00$); Agree ($2.00 \leq \text{mean} < 3.00$); Agree to a lesser extent ($1.00 \leq \text{mean} < 2.00$); Do not agree (mean < 1.00)

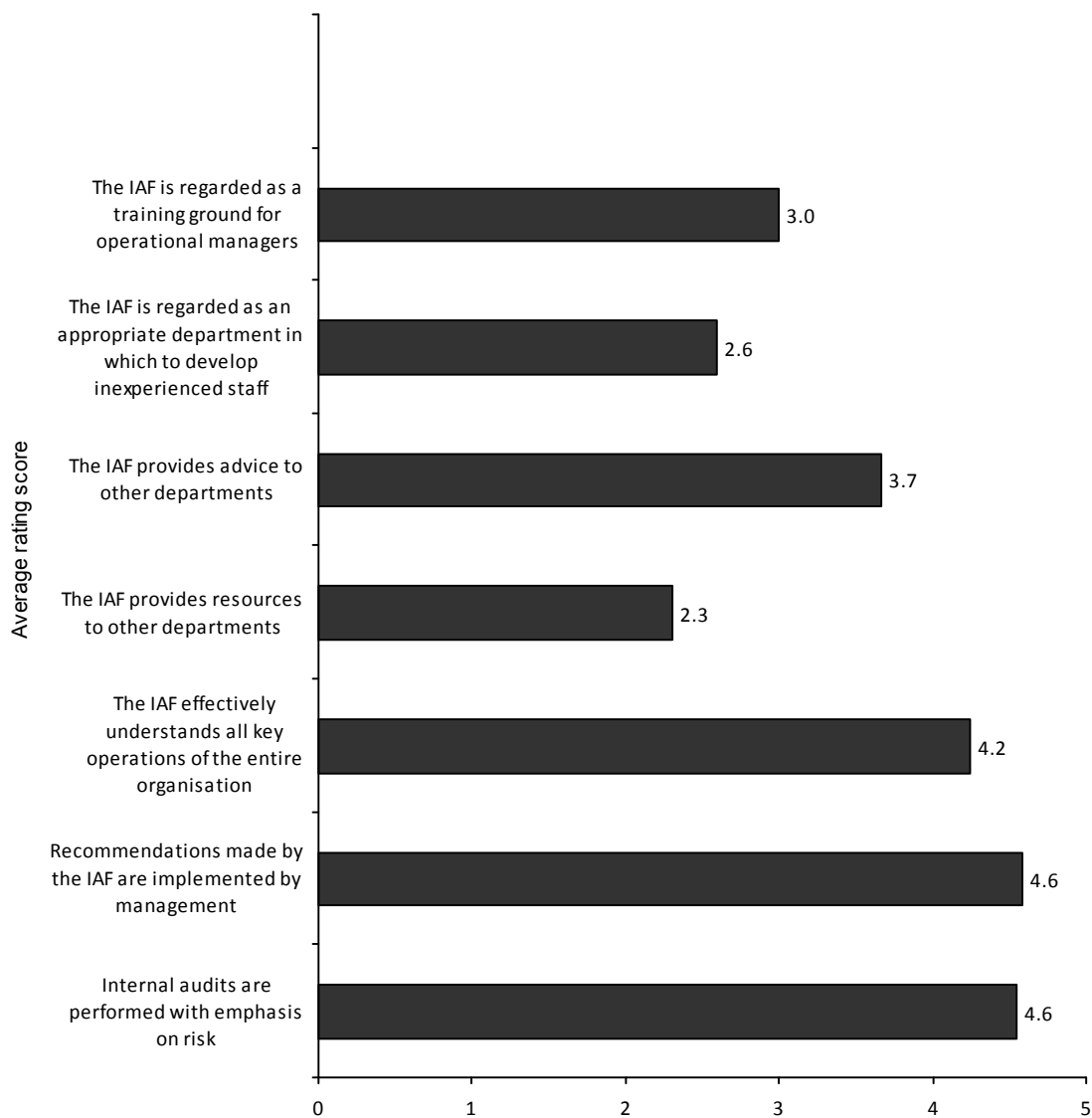
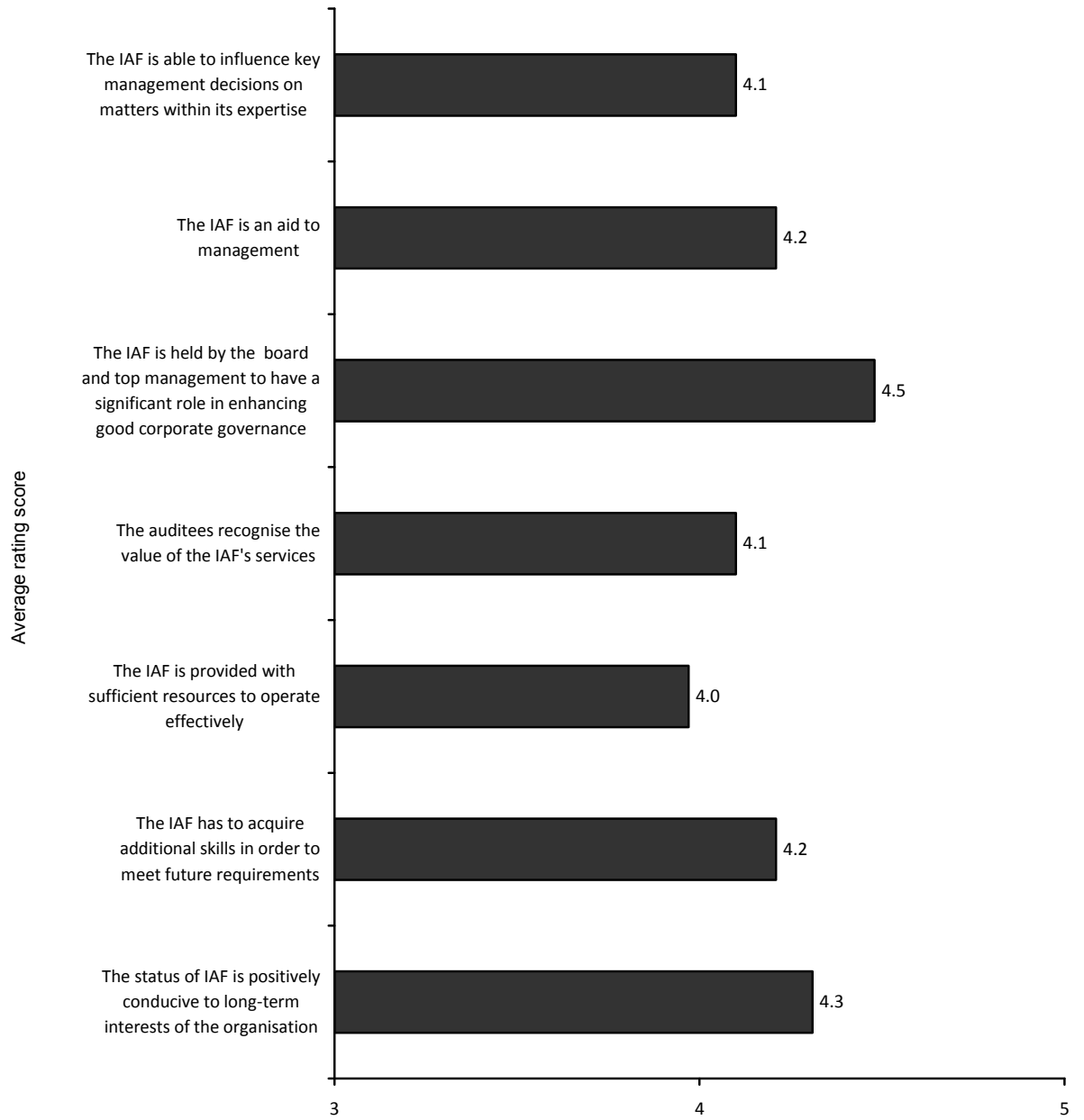


Figure 44 (continued)



2.6 RISK AND RISK MANAGEMENT

Section 2.6 reflects perceptions of CACs, CEO/CFO/COOs and CAEs on risks and risk management. The following risk related responses are reflected:

- Contributions of in-house and outsourced IAFs to the management of the five most important risks that are faced by the participating companies;
- The contributions of various parties to risk assessment, management and communication;
- The effect of a risk management division on the importance of IAFs in risk management;
- Involvement of and assurance provided by IAFs in risk management; and
- The use of separate board risk committees and their independence from IAFs.

2.6.1 Risk and risk management

Section 2.6.1 compares the perceptions of CAC respondents with that of the CEO/CFO/COO respondents on their companies' risks and risk management.

CAC – Existence of a separate board risk committee

According to 63.3% of responding CACs, their companies have established separate board risk committees.

Figure 45: CAC – Existence of a separate board risk committee



□ **CAC – Risk assessment, management and communication**

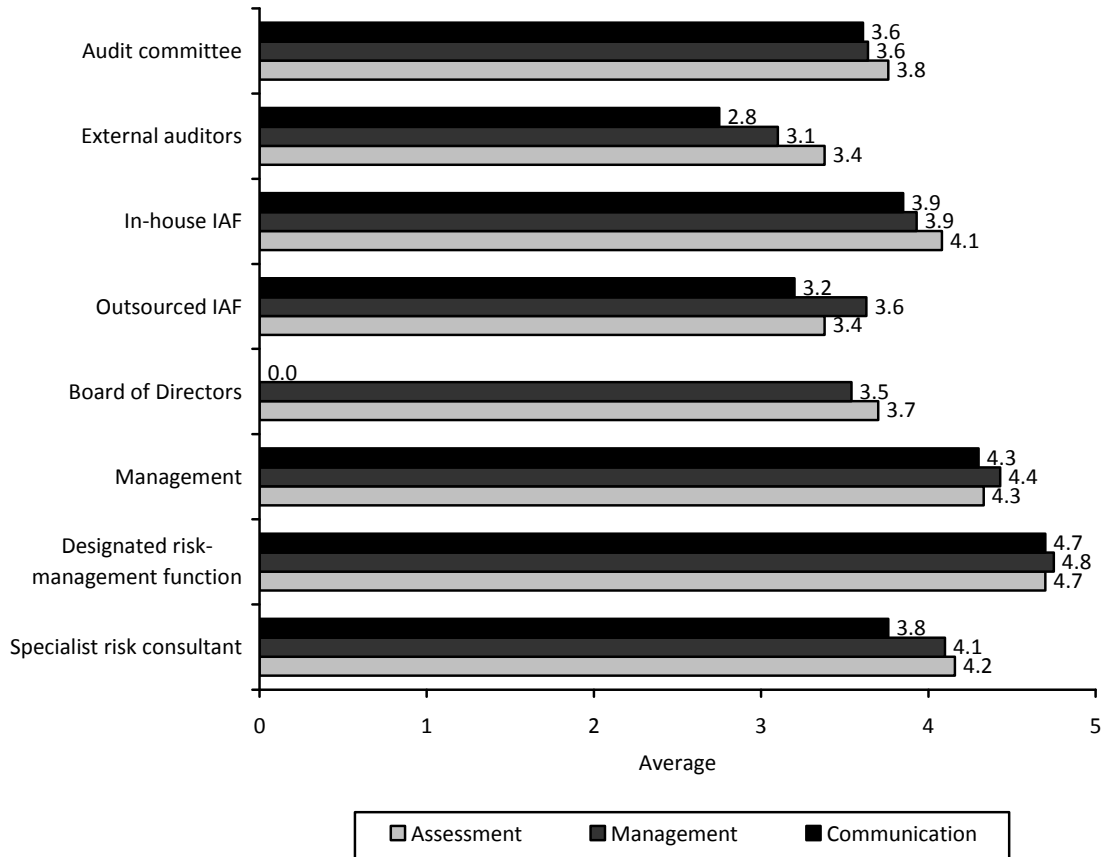
Figure 46 reflects the extent of the contributions made by various parties to risk assessment, risk management and risk communication, as perceived by CAC respondents.

These respondents are of the opinion that all the parties listed below make very important contributions or even significant contributions to risk assessment, risk management and risk communication (mean > 3) except for their companies' boards of directors who are perceived to make no contribution to risk assessment (mean = 0) and their companies' external auditors whose roles in risk assessment are perceived to be only important (mean = 2.8). CAC respondents perceive a designated risk-management function and management, to make the bigger contribution to risk assessment, management and communication as their contributions are perceived to be significant (mean = ≥ 4). They perceive specialist risk consultants to make significant contributions to risk management and risk communication (mean = ≥ 4), while they perceive these parties' contributions to risk assessment to be very important (mean = 3.8).

CAC respondents perceive the contributions that are made by outsourced IAFs to these three aspects of risk to be very important ($3.00 \leq \text{mean} < 4.00$), while in-house IAFs are perceived to make a very important contribution to risk assessment (mean = 3.9) and risk management (mean = 3.9) and a significant contribution to risk communication (mean = 4.1).

Figure 46: CAC – Extent of the contribution made by various parties to risk assessment, management and communication

(Scale anchors: 1 = no contribution, 5 = significant contribution)
 Significant contribution (mean ≥ 4.00); Very important contribution ($3.00 \leq \text{mean} < 4.00$);
 Important contribution ($2.00 \leq \text{mean} < 3.00$); Reasonably important contribution ($1.00 \leq \text{mean} < 2.00$);
 No contribution (mean < 1.00)



□ **IAFS' contribution to the management of their companies' five most important risks**

Respondents were requested to list the five most important risks to their respective companies and rank the potential effect (contribution) of each risk according to a 5-point scale (1 – no contribution, to 5 – significant contribution). The CEO/CFO/COO and CAC respondents listed a total of 203 risks. The 203 risks were categorised into the following seven risk areas:

- finance;
- fraud;
- information technology (IT) related;
- operations;
- people;
- strategic; and
- other.

The number of responses per risk category, as indicated in table 3 below, indicates the number of times a specific risk category was chosen under each of the ratings. The risk category that was mentioned most by the CEO/CFO/COO and CAC respondents was 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 3: CEO/CFO/COO versus CAC – Number of responses per risk category

Risk Category	Number of responses										Mean	
	None		Limited		Average		Significant		Total			
	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO*	CAC	CEO/CFO/COO	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 4 illustrates the relative importance of the risks within a specific category. The CEOs/CFOs/COOs 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).

Table 4: CEO/CFO/COO versus CAC – Importance of risk categories

Risk Category	Not Mentioned		5 th (least)		4 th		3rd		2nd		1 st (most)		Total		Mean	
	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO*	CAC	CEO/CFO/COO	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

Tables 5 and 6 illustrate the responses of the CEO/CFO/COO 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 CEO/CFO/COO 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 CEO/CFO/COO 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 outsourced IAFs make the most valuable contribution to risk management in respect of fraud-related risks (mean 2.33). The perceptions of the CEO/CFO/COO and CAC respondents of the in-house IAFs (table 3) reveal similar views, whereas this is not the case with their perceptions on the outsourced IAFs (table 5). For example, for the risk category finance, the mean perceptions are respectively 2.24 and 2.79 for the in-house IAFs, but differ substantially for the outsourced IAFs with respective means of 3.8 and 1.47.

Table 5: CEO/CFO/COO 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			
	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	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

Table 6: CEO/CFO/COO 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			
	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	CAC	CEO/CFO/COO	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

Tables 3 to 6 above indicate that according to the perceptions of the CEO/CFO/COOs and CACs, the IAF is not in the ideal position to assist with the mitigation of the perceived 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.

A concern is however that the latter two risk categories (fraud and IT-related risks) are perceived to be the most significant two. Further research could investigate why IAFs are not perceived to make a more significant contribution to the more significant risk categories. Furthermore, the perception was that the in-house IAF can contribute more to the mitigation of the top risks than the outsourced IAF, most likely due to the fact that the in-house team are part of the company structure and thus understand the operations and risks better. It is also clear from tables 3 to 6 that the roles fulfilled by IAFs in the management of their companies' most pertinent risks vary from one company to the next. On the whole, CAC respondents perceived in-house IAFs to make a more meaningful contribution to the management of these risks than outsourced IAFs.

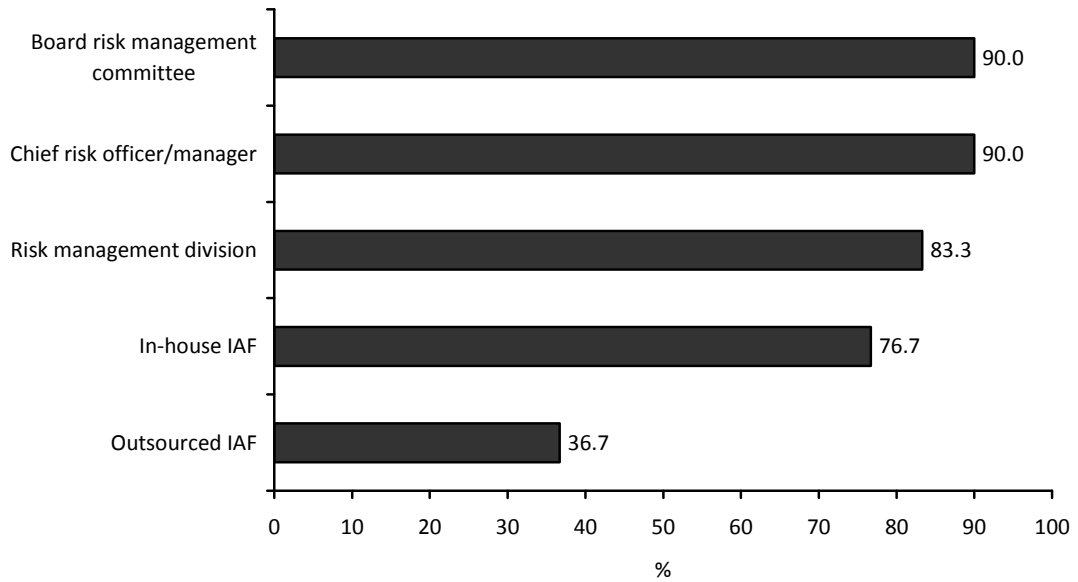
2.6.2 CEO/CFO/COO – Risk and risk management

Section 2.6.2 reflects the perceptions of CEO/CFO/COO respondents of their companies' risks and risk management.

□ CEO/CFO/COO – parties involved in enterprise risk management (ERM)

A total of 90% of CEO/CFO/COO respondents perceived the board risk management committee and the chief risk officer/manager to be an integral part of their companies' enterprise risk management function, while 83.3% of these respondents hold a similar view of the risk management division (figure 47). Further 76.7% of these respondents, perceived that their in-house IAFs form part of their companies' enterprise risk management function, while only 36.7% perceived their outsourced IAFs to fulfill this role.

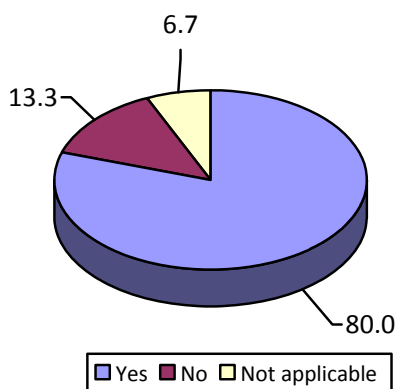
Figure 47: CEO/CFO/COO – Parties involved in enterprise risk management (ERM)



□ CEO/CFO/COO – ERM division’s independence from IAF

Figure 48 reflects that 80% of CEO/CFO/COO respondents were of the opinion that their enterprise risk management divisions are independent from their in-house and/or outsourced IAFs. Only 13.3% of these respondents were of the opposite view.

Figure 48: CEO/CFO/COO – ERM division’s independence from IAF



□ **CEO/CFO/COO – Risk assessment, management and communication**

The contributions of various parties to risk assessment, management and communication were measured by means of a five-point scale that ranges from 1 (no contribution) to 5 (significant contribution). A response of 3 is taken to indicate a greater contribution than 2 and a lower contribution than 4 rather than being an indication of central tendency bias.

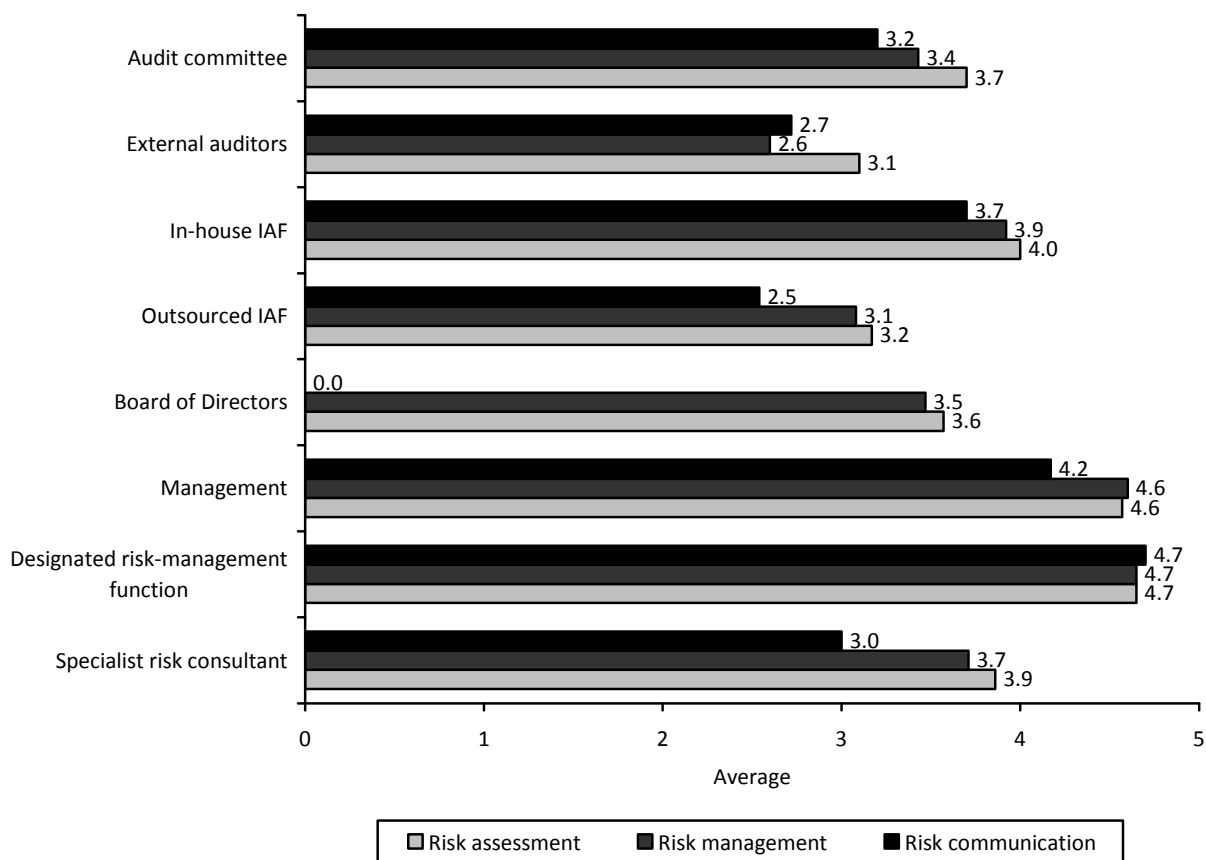
Figure 49 should be read in conjunction with figure 46 in order to compare responses of CACs with those of CEOs/CFOs/COOs. Both figures reflect the extent of the contributions that are made by the various parties to risk assessment, risk management and risk communication.

Based on the perceptions of CEO/CFO/COO respondents, most of the parties listed in figure 49 make very important contributions, or even significant contributions, to risk assessment, risk management and risk communication. The exceptions to the general perceptions are that the boards of directors make no contribution to risk assessment (mean = 0); external auditors whose role in risk assessment (mean = 2.7) and risk management (mean = 2.6) are perceived to be important only; and the contributions of outsourced IAFs which are also perceived to be important only (mean = 2.5). The major role players in this regard are perceived to be designated risk management functions and management, because CEO/CFO/COO respondents perceived the contributions of these parties to risk assessment, risk management and risk communication to be significant (mean \geq 4). The CAC respondents had similar perceptions (figure 46).

CEOs/CFOs/COOs perceive specialist risk consultants to make a very important contribution to risk assessment (mean = 3.0), risk management (mean = 3.7) and risk communication (mean = 3.9). CAC respondents perceived specialist risk consultants to make a significant contribution to risk management and risk communication, while their contribution to risk assessment was perceived to be very important.

Figure 49: CEO/CFO/COO – Extent of the contributions of various parties to risk assessment, management and communication

(Scale anchors: 1 = no contribution, 5 = significant contribution)
 Significant contribution (mean \geq 4.00); Very important contribution ($3.00 \leq$ mean $<$ 4.00); Important contribution ($2.00 \leq$ mean $<$ 3.00); Reasonably important contribution ($1.00 \leq$ mean $<$ 2.00); No contribution (mean $<$ 1.00)



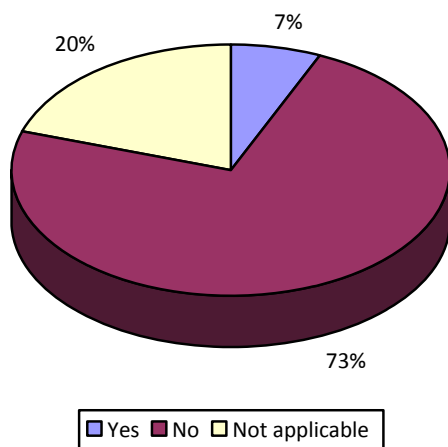
CEO/CFO/COO respondents perceived that the contribution made by outsourced IAFs to risk management (mean = 3.1) and risk communication as very important (mean = 3.2), while outsourced IAFs' contribution to risk assessment were perceived to be important (mean = 2.5). CEO/CFO/COO respondents perceived in-house IAFs to make significant contributions to risk communication and very important contributions to risk assessment and risk management.

The data above reflects that CAC and CEO/CFO/COO respondents were in agreement on the contributions that are made by in-house IAFs to risk assessment, risk management and risk communication. These respondents perceived the contributions made by in-house IAFs to be of greater importance than those made by outsourced IAFs.

□ **CEO/CFO/COO – The effect of a risk management division on the importance of an IAF in risk management**

Figure 50 reflects that only 6.7% of CEO/CFO/COO respondents were of the opinion that the existence of a risk management division has decreased the importance of the role that an in-house and/or an outsourced IAF fulfill in risk management.

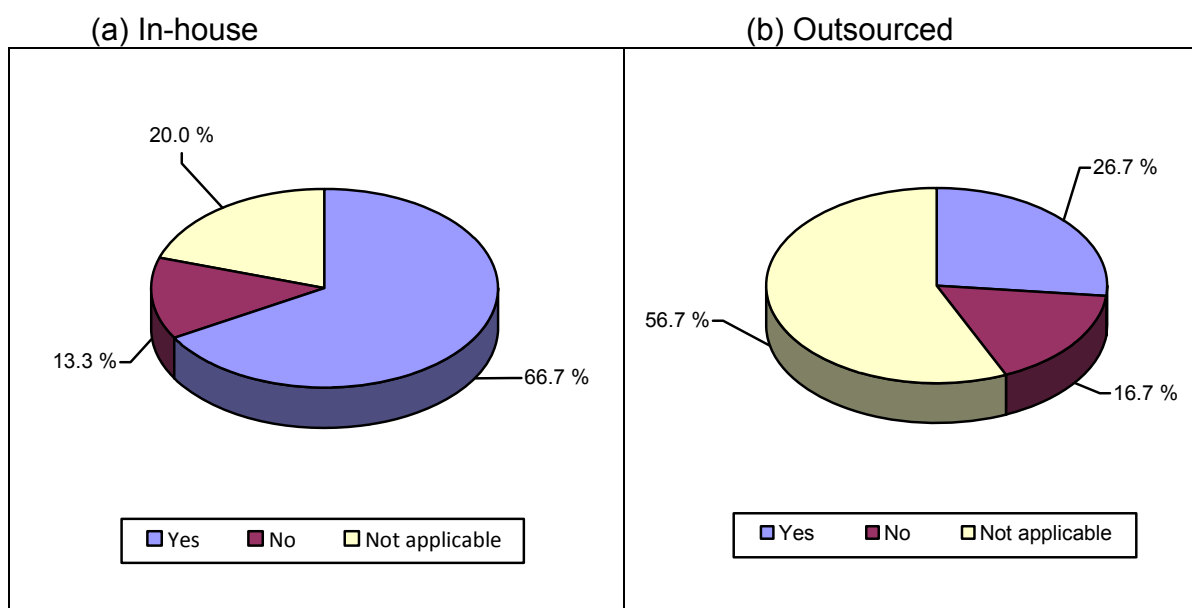
Figure 50: CEO/CFO/COO – Agreement with the statement that a risk management division has decreased the importance of an in-house/outsourced IAF in respect of risk management



□ **CEO/CFO/COO – Assurance provided by IAFs in the risk management process**

Figure 51 reflects that 66.7% of CEO/CFO/COO respondents perceived that their in-house IAFs provide assurance concerning the enterprise risk management process, while only 26.7% of these respondents held that view in respect of outsourced IAFs.

Figure 51: CEO/CFO/COO – Assurance provided by an IAF in respect of the risk management process



2.6.3 CAE – IAF risks

Section 2.6.3 reflects the perceptions of CAE respondents of the involvement of their companies' IAFs in identifying, assessing and communicating risks.

□ **CAE – IAF involvement in risks**

The contributions of IAFs to specified risk related activities were measured on a five-point scale that ranges from 1 (no involvement) to 5 (significant involvement). A response of 3 is taken to indicate a greater involvement than 2 and a lower involvement than 4 rather than being an indication of central tendency bias.

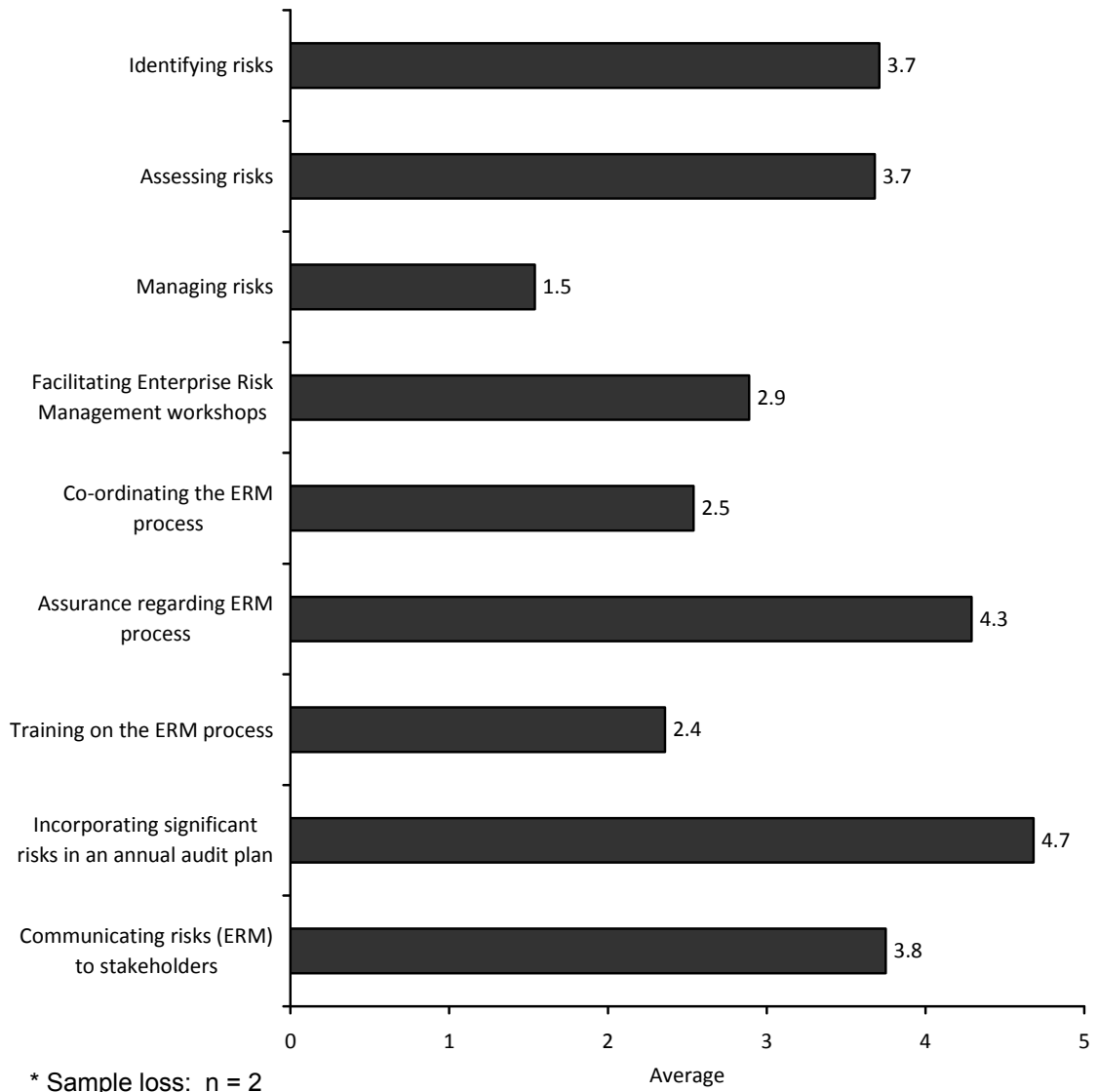
Figure 52 reflects the contribution of IAFs in respect of risks as perceived by CAE respondents.

According to CAE respondents, their IAFs incorporated risks to a significant extent in their annual audit plans (mean = 4.7) and provided assurance regarding their companies' enterprise risk management processes (mean = 4.3). CAEs perceived their IAFs to be very involved in the identification, assessment and communication of risks ($3.00 \leq \text{mean} < 4.00$). Similar perceptions were held by CEO/CFO/COO respondents. Both CAC and CEO/CFO/COO respondents perceived in-house IAFs to make a significant contribution to risk assessment and a very important contribution to risk communication and risk management (figures 46 and 49).

CAE respondents perceived IAFs to have an important involvement in the ERM processes (mean = 4.3), the facilitation of workshops (mean = 2.9), coordination of ERM processes (mean = 2.5) and provision of assistance with training (mean = 2.4) on such processes.

Figure 52: CAE – IAF involvement in risks

(Scale anchors: 1 = no involvement, 5 = significant involvement)
Significant involvement (mean ≥ 4.00); Very important involvement ($3.00 \leq \text{mean} < 4.00$);
Important involvement ($2.00 \leq \text{mean} < 3.00$); Reasonably important involvement ($1.00 \leq \text{mean} < 2.00$); No involvement (mean < 1.00)



2.7 CORPORATE GOVERNANCE AND FRAUD

Section 2.7 reflects responses related to corporate governance and fraud and the impact of IAFs on those. The following aspects are addressed:

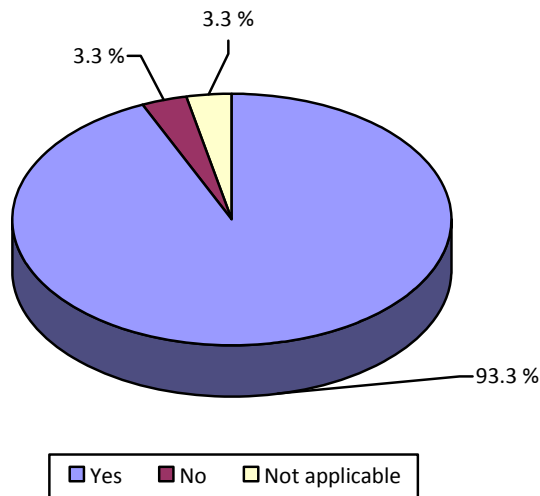
- Reporting done by IAFs to audit committees;
- Contributions of various parties to corporate governance; and
- The role of IAFs in respect of incidents of fraud.

The findings in section 2.7 are based on the perceptions reported by both the CAC respondents and in some instances also CEO/CFO/COO respondents.

2.7.1 CAC – Reporting lines of CAEs to audit committees

Figure 45 reflects that 93.3% of CAC respondents were of the opinion that CAEs report to their audit committees.

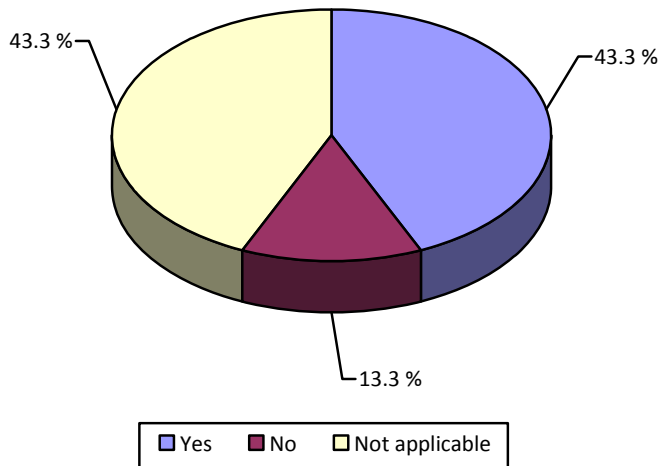
Figure 53: CAC – CAEs report to their audit committees



2.7.2 CAC – Reporting lines of the persons in charge of outsourced IAFs

Figure 54 reflects that 43.3% of CAC respondents were of the opinion that the persons in charge of their outsourced IAFs report to their audit committees. The same percentage of respondents considered such reporting as not applicable.

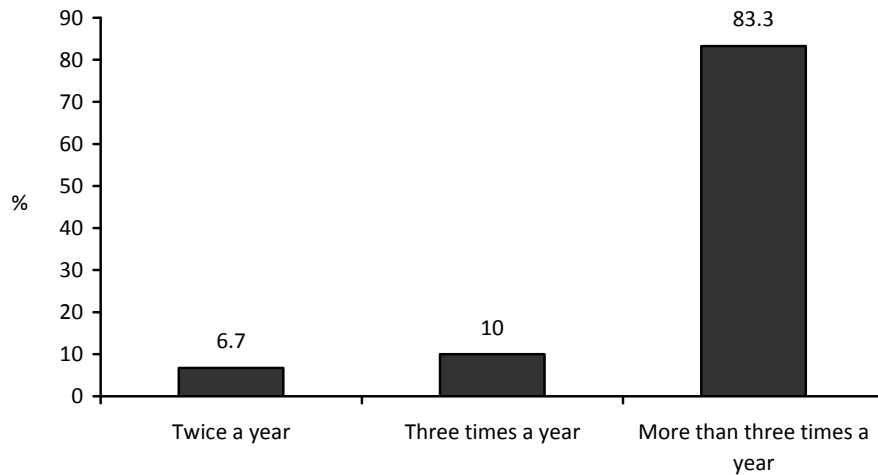
Figure 54: CAC – Do the persons in charge of outsourced IAFs report to their audit committees?



2.7.3 CAC – Frequency with which CAEs report to audit committees

Figure 55 reflects that 83.3% of the CAC respondents were of the opinion that CAEs report to their audit committees at regular intervals, i.e. more than three times a year. A mere 6.7% of these respondents perceived that such reporting was limited to twice a year.

Figure 55: CAC – Frequency with which CAEs report to their audit committees



2.7.4 CAC and CEO/CFO/COO – Contributions made by various parties to corporate governance of their companies

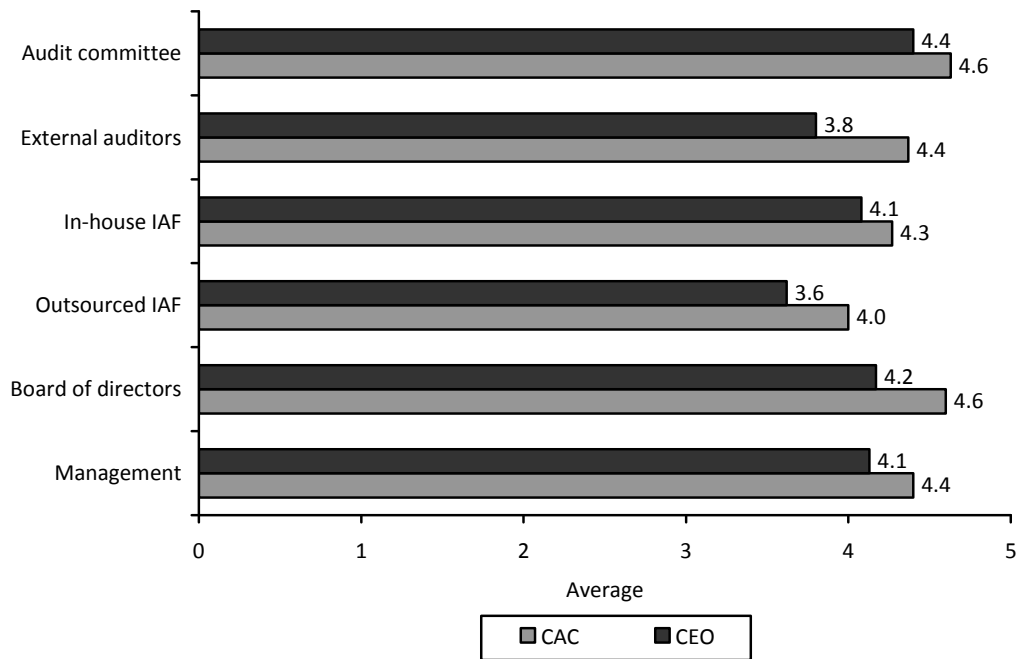
Respondents' level of satisfaction with the contributions that listed parties made to the corporate governance of their companies were measured by means of a five-point scale that ranges from 5 (extremely satisfied) to 1 (extremely dissatisfied). A response of 3 is taken to indicate a level of satisfaction that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

Figure 56 reflects the levels to which CAC and CEO/CFO/COO respondents were satisfied with the contributions that listed parties made to the corporate governance of their companies.

CAC respondents were extremely satisfied (mean ≥ 4) with the contributions made by all the listed parties to the corporate governance of their companies. CEO/CFO/COO respondents were extremely satisfied with the contributions made by audit committees, in-house IAFs, boards of directors and management, while they were very satisfied with the contributions of their external auditors and outsourced IAFs.

Figure 56: CAC and CEO/CFO/COO – Levels of satisfaction with contributions made by listed parties to corporate governance

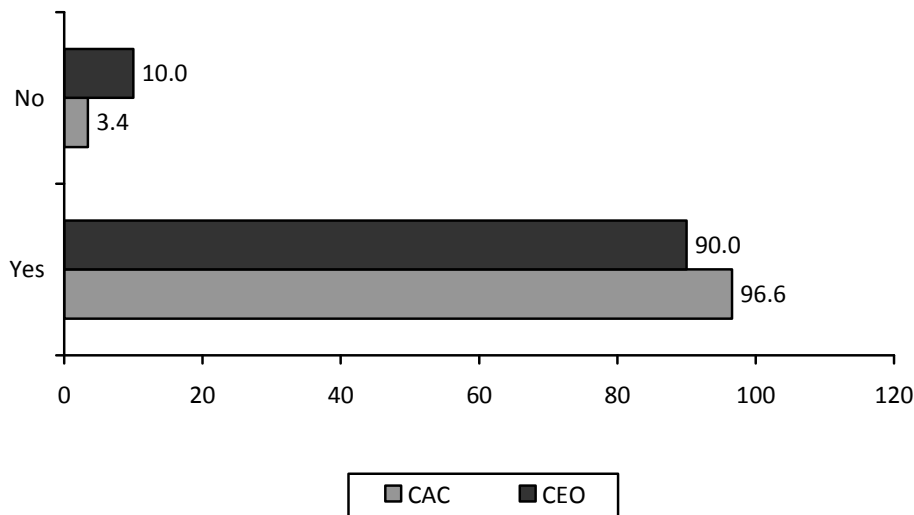
(Scale anchor: 1 = extremely dissatisfied, 5 = extremely satisfied)
 Extremely satisfied (mean ≥ 4.00); Very satisfied ($3.00 \leq \text{mean} < 4.00$); Satisfied ($2.00 \leq \text{mean} < 3.00$); Rather dissatisfied ($1.00 \leq \text{mean} < 2.00$); Extremely dissatisfied (mean < 1.00)



2.7.5 CAC and CEO/CFO/COO – Occurrence of incidents of fraud

Figure 57 reflects that a very high percentage of both categories of respondents (96.6% of CAC respondents and 90.0% of CEO/CFO/COO respondents) were of the opinion that their companies had been a victim of fraud during the past five years.

Figure 57: CAC and CEO/CFO/COO – Was their company a victim of fraud in the past 5 years?



* Sample loss: n = 1

2.7.6 CAC AND CEO/CFO/COO – Degree of comfort provided by various parties

The degrees of comfort provided by listed parties in respect of the prevention and detection of fraud was measured by means of a five-point scale that ranges from 5 (significant comfort) to 1 (no comfort). A response of 3 is taken to indicate a degree of comfort that is higher than 2 and lower than 4 rather than being an indication of central tendency bias.

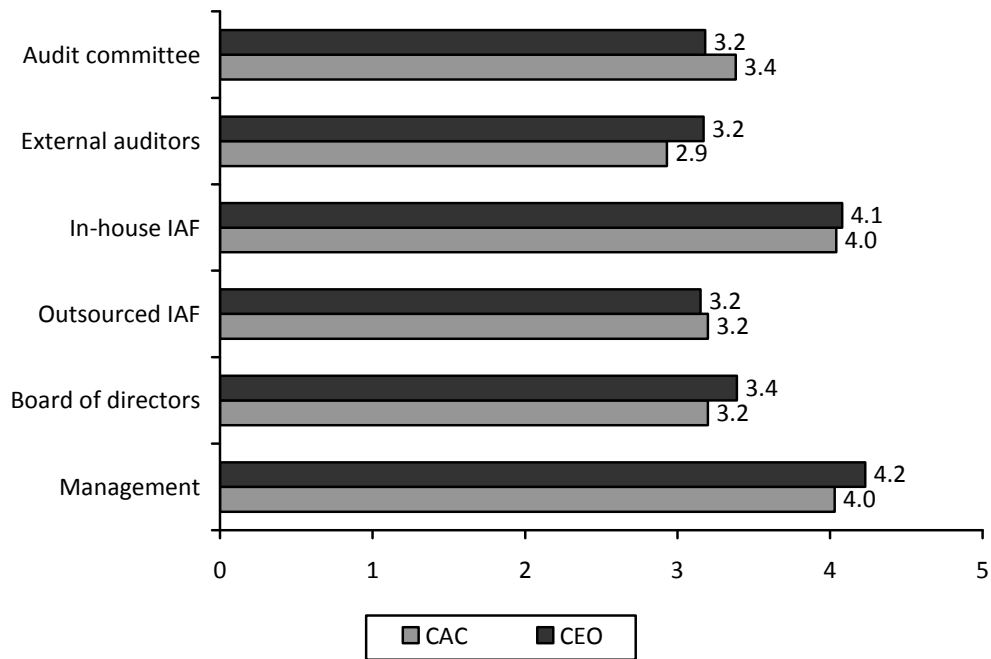
Figure 58 reflects the degrees to which both CAC and CEO/CFO/COO respondents derived comfort from the activities of listed parties regarding the prevention and detection of fraud in their companies.

CAC respondents were of the opinion that their in-house IAFs and management provide significant comfort (mean ≥ 4), while their audit committees (mean = 3.4), outsourced IAFs (mean = 3.2) and boards of directors (mean = 3.2) provided much comfort and their external auditors provided an average degree of comfort (mean = 2.9) in this regard.

CEO/CFO/COO respondents were of the opinion that their in-house IAFs and management provided significant comfort in respect of the prevention and detection of fraud, while they were of the opinion that all the other listed parties provided much comfort in this regard.

Figure 58: CAC and CEO/CFO/COO – Degree of comfort provided by listed parties in respect of the prevention and detection of fraud

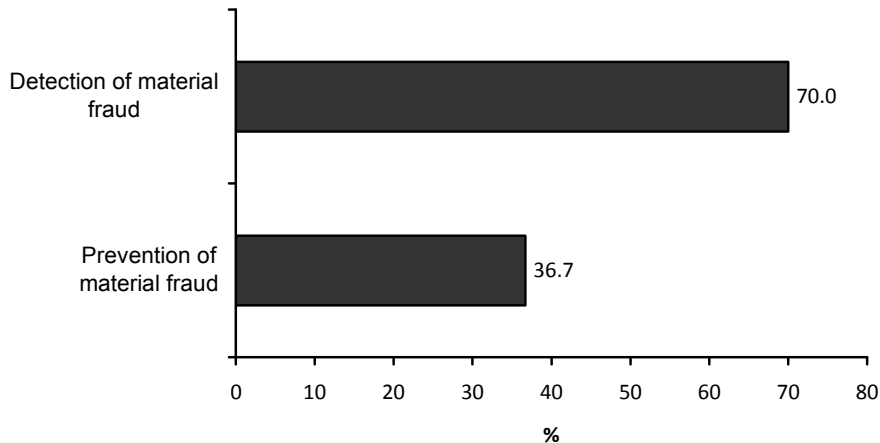
(Scale anchor: 1 = no comfort, 5 = significant comfort)
 Significant comfort (mean ≥ 4.00); Much comfort ($3.00 \leq \text{mean} < 4.00$); Average comfort ($2.00 \leq \text{mean} < 3.00$); Limited comfort ($1.00 \leq \text{mean} < 2.00$); No comfort (mean < 1.00)



2.7.7 CAC – IAFs responsibilities in respect of fraud

Figure 59 reflects that 70% of CAC respondents were of the opinion that their IAFs had a responsibility to detect material fraud, while 36.7% of these respondents also perceived that their IAFs had a responsibility to prevent fraud.

Figure 59: CAC – IAF responsibilities/functions regarding fraud



2.8 CURRENT STAFF COMPLEMENTS OF IAFs AND CURRENT DEMAND FOR IAF STAFF

Section 2.8 reflects details of IAFs in respect of the current staff complements and the future expected staff demand with emphasis on the following aspects:

- Average number of staff currently employed in an IAF (ranked in the order of the highest academic qualification obtained);
- Average number of staff in an IAF (ranked in the order of experience);
- Distribution of current staff over the different IAF positions;
- Average staff turnover in IAFs during the past 12 months;
- Average number of years of experience of staff in different IAF positions;
- Current average annual remuneration of staff in different positions in an average IAF;
- Current vacancies in different fields of expertise in an average IAF; and
- Recruitment sources used to employ IAF staff.

Section 2.8 is based on an analysis of the perceptions reported by CAE respondents. Based on the results reflected in table 7, the following are evident:

- The average IAF of 30 large South African listed company comprised of approximately 45 permanent employees and two temporary or contract employees. It therefore had an average total of 47 employees;

- The majority of these employees had lower-level academic qualifications;
- Approximately 19% (9/47) of these employees were graduates; and
- A low percentage of these employees held professional qualifications.

Table 7: CAE – Current average number of full-time and part-time staff in IAFs and the highest academic qualification and professional designation held by such staff

	Average number
Full/part-time	
Permanent	45.2
Temporary/contract	2.4
Academic qualification level (all qualifications indicated)	
Lower than senior certificate	12.0
Senior certificate	11.9
National diploma	10.7
National higher diploma	4.8
Degree	8.8
Degree with articles (external audit)	7.5
Degree with articles (internal audit)	3.1
Honours degree	9.7
Master's degree/doctorate	1.8
MBA/MBL	2.6
Professional designation (all designations indicated)	
CIA	4.9
CA(SA)/RA	3.5
CISA	9.4
CFE	2.4
ACCA	1.5
CCSA	3.4
CGAP	1.0
CMA	1.2
Professional Accountant (SA)	2.3

Based on the results reflected in table 8, the following are evident:

- On average, 44.9% of current IAF employees (21.4/47.7) had more than five years of IAF experience, while the remaining 55.14% had less than five years of IAF experience;
- On average, more than a third of current IAF employees (38.0% = 18.1/47.7) had experience in external auditing; and
- On average, 44.9% of current IAF employees (21.4/47.7) had experience in fields other than internal and external auditing.

Table 8: CAE – Number of auditors in an average IAF by years of experience

Experience	In an IAF	External auditing	Other fields
Less than 1 year	6.9	2.3	2.7
1-3 years	10.9	6.4	5.3
>3-5 years	8.5	4.9	4.9
>5-10 years	11.4	3.0	4.7
More than 10 years	10.0	1.5	3.8
TOTAL	47.7	18.1	21.4

Based on the results reflected in table 9 (which reflects the averages of information provided by all participating CAE's for a twelve-month period) the following are evident:

- Only 18.3% of current IAF employees (7.2/39.3) held a position at the audit manager level;
- Almost half (46.8%) of current IAF employees (18.4/39.3) hold a position at the audit senior level;
- Approximately one-quarter (28.8%) (11.3/39.3) of current IAF employees held a position at the auditor/assistant level;
- Only 6.1% of current IAF employees (2.4/39.3) were trainees;
- The gender distribution of current IAF employees were 43.4% (27.9/64.3) female and 56.6% (36.4/64.3) male; and
- Although the majority of the current IAF employees were African/Indian/Coloured, the distribution is not representative of the composition of the South African population. The gender/race distribution was as follows:
 - African/Indian/Coloured females = 23.7% (15.3/64.3)
 - African/Indian/Coloured males = 28.1% (18.1/64.3)
 - Total African/Indian/Coloured employees = 51.9%% (33.4/64.3)
 - White females = 19.6% (12.6/64.3)
 - White males = 28.5% (18.3/64.3)
 - Total Whites = 48.1% (30.4/64.3)

Table 9: CAE – Current distribution of employees of an average IAF in terms of position held and race/gender group during the past 12 months (averages)

Position	Total number of positions filled	Number of African/ Indian/ Coloured females	Number of White females	Number of African/ Indian/ Coloured males	Number of White males
Audit managers	7.2	1.6	2.4	2.8	4.4
Senior auditors	18.4	6.6	5.0	8.8	7.9
Auditors/assistants	11.3	5.3	5.2	4.9	5.0
Trainees	2.4	1.8	0.0	1.6	1.0
TOTAL	39.3	15.3	12.6	18.1	18.3

The above is based on year averages which explain all disparities

Based on the results reflected in table 10 (which reflects the average for a twelve-month period), the following are evident:

- A decline was experienced at the audit manager and senior auditor levels, because more employees resigned than were appointed in that period;
- Employees at the CAE level who resigned were replaced within a period of 12 months. This fact indicates that such a strategic position should be filled at all times; and
- It appears that transformation initiatives were accorded a high priority, because nearly three times more African/Indian/Coloured females were appointed by an average IAF and approximately one and a half times more African/Indian/Coloured males were appointed by an average IAF than the number of resignations that occurred in an average IAF in these designated groups.

The decline that was experienced at the senior staff level may be indicative of the shortage of individuals who have high-level internal auditing skills.

Table 10: CAE – Staff turnover in an average IAF during the past 12 months

Position	Total number of staff		Number of African/ Indian/ Coloured females		Number of White females		Number of African/Indian/ Coloured males		Number of White males	
	New appointments	Resignations	New appointments	Resignations	New appointments	Resignations	New appointments	Resignations	New appointments	Resignations
CAE	1.0	1.0	1.0	0.0	0.0	0.0	1.0	0.0	1.0	1.0
Audit manager	1.8	2.5	1.0	0.0	1.0	1.5	1.2	1.3	1.0	1.3
Senior auditor	2.9	4.7	2.4	1.5	1.3	1.1	2.8	1.9	1.5	2.0
Auditor/assistant	4.6	2.2	3.0	1.6	1.5	1.3	2.9	2.0	3.0	1.5
Trainee	2.4	1.0	1.6	0.0	0.0	0.0	1.5	1.0	1.0	0.0
TOTAL	12.7	11.4	9.0	3.1	3.8	3.9	9.4	6.2	7.5	6.3

The above is based on year averages, which explain the disparities

Table 11 indicates that the seniority of the positions held by IAF employees and the average number of years of experience in those positions they have in those positions are loosely related.

Table 11: CAE – Number of years of experience in different positions of an average IAF

Position	Average years
CAE	9.8
Audit manager	6.1
Senior auditor	4.1
Auditor/assistant	2.6
Trainee	0.8

Table 12 reflects that there was a direct correlation between the seniority of the position held by an IAF employee and the remuneration package linked to the position held.

Table 12: CAE – Annual remuneration package offered by an average IAF for different employment positions

Position	Rand
CAE	857 692
Audit manager	507 823
Senior auditor	368 062
Auditor/assistant	229 642
Trainee	132 727

Table 13 reflects the number of vacancies per field of specialisation in an average IAF over a 12 month period and indicates that:

- The largest number of vacancies existed at the audit manager level, followed by the senior auditor level. These vacancies may once again be indicative of the shortage of individuals who have high-level internal audit skills;
- Overall the largest number of vacancies was for persons who would be used for operational/performance audits, followed by financial audits.;
- An average IAF had sufficient staff to perform corporate governance audits and to respond to other management requests;
- Had all reported vacancies been filled, the number of employees in an IAF would have been up to 78 (47 + 31); and
- Based on the above, the current vacancy rate of an average IAF is estimated to be 39.7% (31/78).

The above analysis clearly shows that there is currently a demand for internal auditors, especially high-level, skilled, internal auditors.

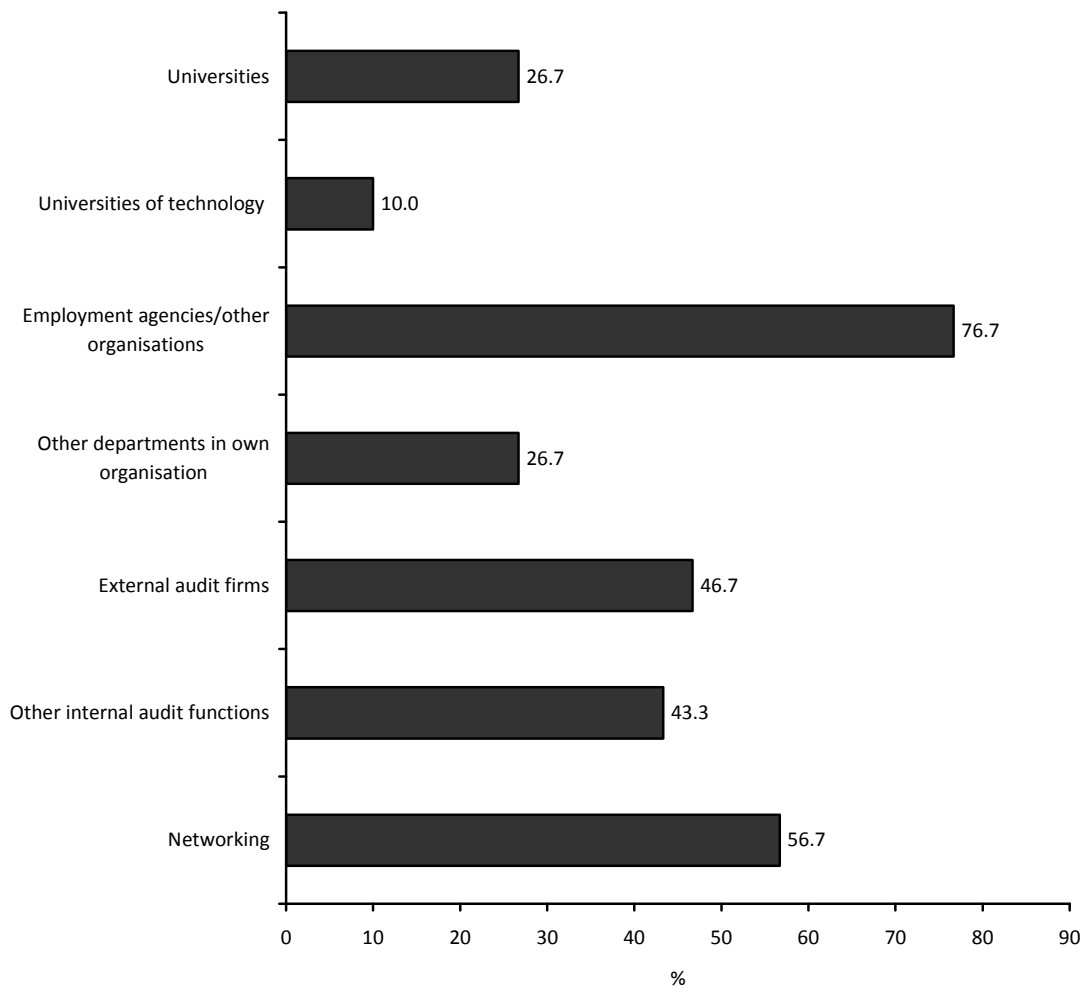
Table 13: CAE – Number of vacancies per field of specialisation in an average IAF over a 12 month period

Field of expertise	Audit manager	Senior auditor	Auditor/ Assistant	Trainee	TOTAL
Financial audit	1.5	1.9	2.3	1.0	6.7
Compliance audit	1.0	1.3	1.0	0.0	3.3
Operational/ performance audit	6.0	1.4	3.3	2.0	12.7
Information systems audit	1.5	1.7	0.0	0.0	3.2
Enterprise risk management	1.0	1.0	1.0	0.0	3.0
Corporate governance	0.0	0.0	0.0	0.0	0.0
Forensic audit	1.0	1.0	0.0	0.0	2.0
Other	0.0	0.0	0.0	0.0	0.0
TOTAL	12.0	8.3	7.6	3.0	30.9

The above figures are based on year averages, which explain the disparities

Figure 60 illustrates the main sources of recruitment used by IAFs as perceived by CAE respondents. A total of 76.7% of CAE respondents indicate that the main source of recruitment for employees by their IAFs was employment agencies or other companies. The majority of these respondents are also in favour of recruiting through networking. Two other recruiting options that obtained reasonable support from CAE respondents were recruiting from external audit firms and other internal audit functions.

Figure 60: CAE – Main sources of recruitment used by IAFs



2.8.1 Expected future staff complements and demand for IAF staff

Section 2.8.1 reflects the expected future staff complements of an average IAF and the demand for IAF staff. Section 2.8.1 is based on the perceptions of CAE respondents.

Based on tables 14 and 15, the following are evident:

- CAEs perceived the largest demand for IAF staff in the future would be at the audit manager level (19.0 positions) and at the senior auditor level (19.1 positions). These perception emphasise the demand that exists for high-level, skilled, internal auditors;
- CAEs expected that the future demand for female internal auditors (at all levels, except for trainees) would exceed that for male internal auditors;
- CAEs envisaged that the future demand for Black/Indian/Coloured internal auditors (at all levels) would exceed that for White internal auditors; and
- CAEs expected that the largest future demand would be for internal auditors who have the skills to perform assurance assignments, forensic investigations and control self-assessment.

Table 14: CAE – Expected future demand of an average IAF for auditors at the audit manger and senior auditor levels

Field of expertise	Audit managers				Senior auditors				TOTAL
	F/O	F/W	M/O	M/W	F/O	F/W	M/O	M/W	
Assurance	2.0	1.0	1.0	1.0	1.8	1.0	1.7	1.3	10.8
System design/improvement	1.0	0.0	1.0	0.0	1.0	2.0	1.0	0.0	6.0
Process improvement	0.0	0.0	0.0	0.0	0.0	1.0	1.0	0.0	2.0
Forensic investigations	1.0	1.0	1.0	1.0	1.3	1.0	1.0	1.0	8.3
Control self-assessment	1.0	0.0	1.0	1.0	1.0	0.0	1.0	0.0	5.0
Other consulting	1.0	2.0	1.0	1.0	0.0	0.0	0.0	1.0	6.0
TOTAL	6.0	4.0	5.0	4.0	5.1	5.0	5.7	3.3	38.1
GENDER TOTAL	10.0		9.0		10.1		9.0		
CULTURAL GROUP TOTAL	11.0		8.0		10.8		8.3		
GRAND TOTAL	19.0				19.1				

KEY: F = Female; M = Male; O = Other: Black/Indian/Coloured; W = White

Table 15: CAE – Expected future demand of an average IAF for auditors at the auditor/assistant and trainee levels

Field of expertise	Auditor/assistant				Trainee				TOTAL
	F/O	F/W	M/O	M/W	F/O	F/W	M/O	M/W	
Assurance	1.7	1.0	1.0	1.0	1.0	1.0	1.3	1.0	9.0
System design/ improvement	1.0	0.0	0.0	1.0	0.0	0.0	0.0	0.0	2.0
Process improvement	1.0	1.0	0.0	0.0	0.0	0.0	1.0	1.0	4.0
Forensic investigations	1.0	1.0	1.0	0.0	1.0	0.0	1.0	1.0	6.0
Control self- assessment	0.0	1.0	1.0	1.0	1.0	0.0	0.0	1.5	5.5
Other consulting	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL	4.7	4.0	3.0	3.0	3.0	1.0	3.3	4.5	26.5
GENDER TOTAL	8.7		6.0		4.0		7.8		
CULTURAL GROUP TOTAL	7.7		7.0		6.3		5.5		
GRAND TOTAL	14.7				11.8				26.5

KEY: F = Female; M = Male; O = Other: Black/Indian/Coloured; W = White

It is clear from the data presented that there is a demand for internal auditors, especially for high-level, skilled, female, internal auditors. Future demand will be the greatest for individuals from previously disadvantaged groups.

CHAPTER 3: CONCLUSIONS AND DIRECTIONS FOR FUTURE RESEARCH

The objective of this research report is twofold, namely firstly to determine the standing of internal auditing within 30 large listed South African companies and secondly to determine the demand therefor. The overall findings of the research are presented accordingly:

3.1 THE STANDING OF THE IAF WITHIN THE COMPANY

3.1.1 Profiles of the CAEs and the audit committees

The research found that the average CAE of a larger South African listed company holds a postgraduate academic qualification, obtained professional certification in either external or internal auditing or both, is a member of The IIA, has five years of internal auditing experience, has been a CAE for five years, has worked for the current employer for approximately five years and receives an annual remuneration in excess of one million rand. It was also determined that the profile of the average CAE is closely related to the minimum profile requirements for prospective CAEs, except that prospective CAEs are required to have more years of experience in internal auditing and can expect to receive a lower annual remuneration. Further, auditees prefer certification as an external auditor above certification as a CIA.

The research found that a typical audit committee of a large listed South African company meets at least three times per year and comprised of four members of which at least three members were independent non-executive directors.

3.1.2 Awareness of The IIA

It appears as if the existence of The IIA, its professional qualification and standards had been significantly promoted under the CAC and CEO/CFO/COO respondents to create a high level of awareness.

3.1.3 Practices followed by IAFs

Nearly all CAE respondents indicated that they followed an internal audit methodology and that their engagements were conducted in accordance with the *Standards*. These respondents indicated that they had a comprehensive training programme for their internal audit personnel. Performance of quality self-assessments with independent validation and external quality assessment on the participating companies' IAFs appear to be a followed practice.

In the opinion of CAE respondents, a risk-based audit approach and a compliance/operational audit approach were the most important approaches followed by their IAFs. The provision of assurance was regarded to be the most significant function of IAFs.

3.1.4 The structure and reporting lines of the IAF

The research found that the participating companies mainly used in-house and co-sourced IAFs, but complete outsourcing was also present. The research found that certain or all services of participating companies' IAFs were mostly outsourced to one of the Big 4 public accounting firms. This finding concurs with past research such as the Van Peurse and Jiang (2008:233) study in New Zealand and the UK study of Selim and Yiannakas (2000:220). Factors contributing to the Big 4 public accounting firms being preferred outsourced parties represent an area for further exploration. In particular the finding of Caplan and Kirschenheiter (2000:411) that public accountants provide the same or higher levels of testing than in-house internal auditors which may result in a higher fee warrants further investigation.

The findings showed that both CAC and CEO/CFO/COO respondents perceived the need for specialised technical expertise as being the most important rationale for outsourcing all or certain services of IAFs. CEO/CFO/COO respondents perceived the shortage of competent internal auditors in South Africa as a very important rationale. These findings align with the Australian Subramaniam et al. (2004:93) study and the UK respondents' views in the Selim and Yiannakas (2000:223) study who viewed their inability to retain and recruit people with necessary skills as the main reason for outsourcing internal audit services. More than a decade ago the Mjoli study (1997:68) also identified the scarcity of skills as a key driver for outsourcing internal auditing in South Africa and since then Fasset (2008:13 & 14) has identified internal audit as a scarce skill in South Africa. It affords an opportunity for further research investigating the competencies (knowledge, skills and attitudes) required of internal auditors at specific levels and to determine the current and expected shortfall in the supply of competent internal audit managers, seniors, assistants and trainees.

The research furthermore revealed that both CAC and CEO/CFO/COO respondents perceived the complex business processes of their companies and the superior knowledge of internal staff as being the two most important rationales for using an in-house IAF to perform certain or all internal audit services.

With regard to the reporting lines of the IAF, the findings indicate two concerns. The first is the inconsistency between the responses of the CACs and CEO/CFO/COOs with regards to the reporting lines of the CAE. Although CACs and CEO/CFO/COOs of the same companies were targeted, in a number of cases they did not share the same view. This is a concern as these respondents

hold senior positions and should have a better understanding of the reporting lines of their IAFs. The second concern is that, although in the minority, a significant number of CEO/CFO/COOs and CACs indicated that the CAEs' functional reporting lines pointed to office bearers other than the CAC. Furthermore, the CEO/CFO/COOs and CACs indicated that the CAE reported administratively, in the most cases, to the CFO. In order for the IAF to remain independent the King Report on Governance (IOD 2009:97) is adamant that the CAE should report operationally or functionally to the CAC. Further research could therefore determine the causes of the inconsistency between the responses of the CACs and CEO/CFO/COOs. It could further explore the impact on the IAF and the company if its operational reporting line is not to the CAC.

3.1.5 The services performed by IAFs

It can be inferred from the responses of CAE respondents that the majority of IAF functions focused on the execution of operational/performance audits, information systems audits, financial audits and responding to ad hoc management requests. These respondents perceived that more hours were spent on these functions (with the exclusion of ad hoc management requests) than on other functions and this pattern is likely to continue in future. They envisaged that IAFs will in future be involved to a greater extent than at present in corporate governance audits. Corporate governance audits therefore represent a potential area into which the IAF functions could be extended.

The findings indicated that outsourced parties spent a greater proportion of their time on specialised audits (forensic audits and environmental audits) than their in-house counterparts did. In view of the fact that specialised audits could require high-level skills, the aforementioned difference in time spent on specialised audits could be ascribed to the shortage of specialised skills in the current internal auditing environment.

IAFs are regularly tasked with *ad hoc* management requests. The respondents indicated a high level of involvement in these activities which could be a hampering factor as it requires the IAF to deviate from its annual audit plan and thus prevents the achievement of the internal audit objectives as set out in the annual audit plan. The ad hoc management requests are not provided for with regard to resources in the annual audit plan. A matter of concern, which requires further research, is the impact or effect of the high percentage of ad hoc management requests indicated by the CAE respondents on the annual internal audit plan which should be risk based (IIA 2009a:28-29).

It is perceived that the average number of annual hours spent on the various activities by both in-house and cosourced/outsourced will increase substantially in future when compared with the annual average hours currently spent on these activities. Although the respondents had to indicate their perceptions of current and expected future annual hours on the same list of activities used where they

had to indicate which activities they currently perform, their responses to the two questions do not correspond. On the question to indicate the internal audit activities they currently perform or to be performed in future, the respondents indicated a slight decrease (ranging from 6% to 13.4%) in respect of compliance, operational/performance and information systems audits. Their perceptions in respect of the current and future hours spent on these activities, however, show increases ranging from 13% to 898% (compliance audits).

3.1.6 Value adding to the company

The respondents perceived the value added by their in-house IAFs to be more than the value added by their outsourced IAFs. Various attributes that affect the status of IAFs were investigated. These attributes include their competency, commitment, service, performance, flexibility and the value that they add. To determine the perceived status of both in-house and outsourced IAFs, the importance of these attributes were determined, the value added by IAFs in various activities was investigated and the frequency at which IAFs' recommendations were implemented by the participating companies was determined. The results revealed that CEO/CFO/COO respondents were extremely satisfied that their in-house IAFs demonstrated compliance with each of the identified six attributes, as well as being extremely satisfied with the competence, commitment and flexibility displayed by their outsourced IAFs. CAC respondents' perceptions of their in-house IAFs were similar to the perceptions of the CEO/CFO/COO respondents, but for their outsourced IAFs they only perceived extreme satisfaction with regard to the competence attribute. The CEO/CFO/COO respondents expressed satisfaction with the flexibility and commitment of their outsourced IAFs.

Both CAC and CEO/CFO/COO respondents reported that their in-house IAFs add more value than their outsourced IAFs, except in respect of independent assurance and activities that concern the control environments. In respect of the latter, CEO/CFO/COO respondents were of the opinion that both their in-house and outsourced IAFs add similar value. CAE respondents strongly supported the view that auditees recognised the value added by their IAFs' services. Both CAC and CEO/CFO/COO respondent groups were of the opinion that outsourced IAFs will probably add more value in future and that the significant value already added by in-house IAFs will be maintained.

One of the perceptions that were used to assess IAF status was to determine the extent to which its recommendations were implemented by the companies. CAE respondents strongly supported the view that the recommendations made by their IAFs were implemented by management, because they consider their IAFs to be aids to management who were able to influence key decisions that were taken on matters within their expertise.

CAE respondents agreed strongly with the statement that recommendations made by their IAFs were implemented by management. Nearly all the CAC respondents (93.3%) and all (100%) of the CEO/CFO/COO respondents perceived that the managements of their companies always or frequently implemented the recommendations made by their IAFs. The findings of the research furthermore revealed that recommendations made by in-house IAFs are implemented more frequently than those of the IAFs to whom certain or all internal audit services were outsourced. CEO/CFO/COO respondents perceived more value to be added by their outsourced IAFs than the CAC respondents did.

The results of the research also showed that the majority of CEO/CFO/COO respondents perceived recommendations from their outsourced IAF as not applicable. This finding represents an area which should be further explored, because it contradicts these respondents' perceived satisfaction with the attributes of their outsourced IAFs and the value added by them. An investigation should be conducted to determine whether recommendations from outsourced IAFs are considered relevant and possible causes of this contradiction.

Almost two-thirds of CAC respondents were of the opinion that their external auditors placed a high reliance on the work done by in-house IAFs, while less than half (41.2%) of these respondents shared a similar view with regard to their outsourced IAFs. A higher percentage of CAC respondents were of the opinion that there is extensive or moderate co-ordination between their external auditors and their in-house IAFs, which exceeded the co-operation perceived to have existed between their external auditors and their outsourced IAFs.

The above findings indicate that IAFs have acceptable status within their companies. Respondents expressed much satisfaction with the contributions made by their IAFs. In many instances the contributions that were made by in-house IAFs were considered to be slightly greater than that made by outsourced IAFs.

3.1.7 The role of the IAF with regard to risk

Respondents perceived a designated risk-management function and the management of their companies as the major participants in risk assessment, risk management and risk communication. Respondents furthermore perceived that the contribution of their in-house IAFs to risk assessment, risk management and risk communication were of greater importance than the contribution made by their outsourced IAFs. CEO/CFO/COO respondents held a similar view in regard to the assurance provided by their IAFs in respect of the Enterprise risk management (ERM) process. Two-thirds of the latter respondents believe that in-house IAFs provide assurance in respect of the ERM process, while only 26.7% held a similar view in regard to their outsourced IAFs.

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 CEO/CFO/COO 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 CEO/CFO/COO and CAC respondents when compared with contributions to the risk management process and risk management framework. 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 and represents an area that should be explored in future.

With regard to the current and expected value that IAFs can add in respect of risk, the perceptions of the CEO/CFO/COO and CAC respondents are that the IAFs' future contributions should increase. This is an indication that the CEO/CFO/COOs and CACs expect greater utilisation of the IAF in respect of risk, 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.

The results of the research 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.

Respondents indicated that neither their in-house nor their outsourced IAFs made a significant or above-average contribution to the management of their companies' five most important (top five) risks. It was apparent, however, that both CAC and CEO/CFO/COO respondents perceived the contribution of their in-house IAFs to be greater than that of their outsourced IAFs. The areas that were identified by CAC and CEO/CFO/COO respondents as being areas in respect of which their in-house and outsourced IAFs could be used to a significant extent in future also concern risk assessments and risk management. The aforementioned findings clearly indicate that IAFs already play a relatively important role in risk assessment, risk management and risk communication, but that their role could be extended in future.

3.1.8 The role of the IAF with regard to corporate governance and fraud

All the respondents in the project perceived the role of their in-house IAFs to be significant in respect of enhancing corporate governance. CEO/CFO/COO respondents also shared this view with regard to the role of their outsourced IAFs in the enhancement of corporate governance, while CAC respondents were not extremely satisfied, but only very satisfied, with the role of the outsourced IAFs in this regard.

Almost all CAC and CEO/CFO/COO respondents indicated that their companies had been the victims of fraud over the past five years. These respondents perceived that their in-house IAFs provided significant comfort in respect of the prevention of such fraud, while the contributions of their outsourced IAFs in this regard were perceived to be at a lower level, namely that the latter provided much comfort in regard to the prevention of fraud.

3.1.9 The demand for the IAF within the company

The findings indicate that the average in-house IAF comprised of 47 employees. The greater majority of these employees held relatively low academic qualifications and very few were in possession of professional qualifications. A fair number of these employees were experienced in the field of internal auditing or external auditing. The majority (76.7%) of CAC respondents stated that these employees were appointed with the assistance of employment agencies or were recruited from other companies.

It was reported that a typical IAF was structured as follows:

- 20% of its employees held a position at the managerial level;
- 50% were at the audit senior level;
- a further 20% were at the auditor/assistant level; and
- the rest at the trainee level.

The gender distribution indicated a preponderance of males (60:40 ratio). The various race groups employed in an average IAF was not representative of the composition of the South African population.

Based on the information provided by the CAE respondents, there was a decrease in the number of IAF employees at the audit senior level. This trend could be indicative of the shortage of high-level internal auditing skills. Furthermore, it is apparent that transformation initiatives were impacting on the employment of IAF staff. Based on the vacancies reported by CAE respondents, it is clear that the future demand for internal auditors will be predominantly for high-level, skilled, female, internal auditors from previously disadvantaged groups.

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