CHAPTER 1

Background to the Study

1.0 Introduction

This chapter gives the background information to the problem. Auditing and internal auditing are defined and discussed. The differences between external and internal auditing are also given. The history of the internal auditing profession is discussed, from the very early stages up to the present era, when the Institute of Internal Auditors is the globally recognised standard-setting and certification body for the internal auditing profession. The concepts of independence and objectivity of internal auditors are also discussed at length. Both organisational independence and individual objectivity are discussed. The scandals that occurred in the United Kingdom and the United States of America are briefly touched, as these gave rise to demands for good governance to prevent recurrence of such scandals. Incidentally this also led to an increase in the demand of internal audit services.

A brief history of the parastatals in Zimbabwe is then given. Highlighted in the discussion are governance problems that have resulted in loss of public funds due to scandals. This has led to the current thrust towards commercialisation and privatisation. These developments have also meant that the services of internal auditors may be required to prepare these parastatals for privatisation, since investors are interested in viable entities. The next items discussed are: the statement of the problem, the purpose of the study, research questions, research objectives and significance of the study. The delimitation and limitations of the study are then discussed. Ethical considerations to be observed in the study are then discussed, and the chapter ends with a description of the methodology that was used in the study.
In the modern organisation there is separation of duties, in that the shareholders, who are the owners and contribute the capital, are not involved in the day-to-day running of the organisation (Berle and Means 1932; Hindley 1970; Chapelle 2005; He and Sommer 2006; Hilt 2008; Clark and de la Rama 2006). This important duty is left to managers who are appointed by directors. This situation results in managers having more information than the shareholders (Jensen and Meckling 1976). There is a danger that the managers could use this information to enrich themselves at the expense of the shareholders (Scapens 1985). To provide assurance that managers will not act to the detriment of the owners of the organisation, the shareholders appoint external auditors. External auditors check on the work of the managers, to ensure adequacy of the internal control system and compliance by management to it. They also check that the operating results of the business and its financial position are properly reported by management (Millichamp 2002). However external auditors do not carry out detailed checks but rather perform more of reasonableness checks on the aggregated accounting information with the aim of expressing an opinion on whether the annual financial statements show a true and fair view of the operations of the business and its financial position (Arens & Loebbecke 2005; Millichamp 2002). The board therefore appoints internal auditors who carry out more detailed examinations, and because of their intimate knowledge of the business, as insiders, they are able to advise management from an informed position (Sawyer, Dittenhofer and Schelner 2003). The responsibility of designing and maintaining an internal control system as well as risk management lies with management (IIA 2008; COSO 2013; King III 2010). The internal auditors check for adequacy and compliance to the systems and report and advise management accordingly. Due to the nature of their duties, internal auditors need to be free from influence from any officials within or outside the organisation, so that they can examine systems and issue unbiased reports on the activities examined. Independence of the internal auditors is therefore of great importance.
1.1 External audit professional bodies

External Auditors have organised themselves into professional bodies in order to self-regulate, issue standards and codes of ethics to be followed by all their members, and ensure observance thereof. Examples of these professional bodies are, the Institute of Chartered Accountants of England and Wales (ICAEW) in the United Kingdom, which is a recognised supervisory body for auditors in terms of the Companies Act of 2006 and the American Institute of Certified Public Accountants (AICPA) in the United States of America, as provided by the US Public Company Accounting and Oversight board (PCAOB). These bodies are responsible for specifying the technical qualifications, setting the examinations, and determining the practical training required for admission into the profession. They maintain a register of members and practitioners, and have the power to bar members from public practice if they breach the professional standards and/or ethics. Most countries have these professional accounting bodies with similar duties and responsibilities. In South Africa, there is the South African Institute of Chartered Accountants, which falls under the purview of the Auditing Profession Act of 2005, and in Zimbabwe we have the Institute of Chartered Accountants which is regulated by the Public Accountants and Auditors Act No. 13 of 1995. All these bodies are affiliated to the International Federation of Accountants which is the global body of the profession.

1.2. Differences between external audit and internal audit

Differences between internal and external auditors are not always understood, and most people confuse the two (IIA Australia 2009). As shown in the Table 1.1, external auditors conduct their audits in accordance with specific statutory requirements or specific contracts, and report to the shareholders of the company. On the other hand, internal auditors focus on
improving the operations of the entity and their coverage is company-wide, reporting to management through the audit committee.

Table 1.1

Differences between external and internal audit

<table>
<thead>
<tr>
<th>ASPECT</th>
<th>EXTERNAL AUDIT</th>
<th>INTERNAL AUDIT</th>
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<tbody>
<tr>
<td>Mandate</td>
<td>Statutory opinion to shareholders on the accuracy of the company’s annual report and financial statements</td>
<td>Broad based assurance program set with the Board and Senior Management. This usually includes the adequacy of the company’s risk management framework, operational performance of business units, integrity of management reporting and other areas as requested by the Board and Senior Management.</td>
</tr>
<tr>
<td>Reporting</td>
<td>Primary responsibility to shareholders via the audit committee and Chief Financial Officer. Also available for questions by shareholders at the AGM</td>
<td>Primary responsibility to the Board via the Audit Committee. Works closely with management, with the aim of providing independent insight to the Senior Management, the CEO and the Board Audit Committee.</td>
</tr>
<tr>
<td>relationships</td>
<td>Finance and accounting</td>
<td>Organisation wide – all areas, all departments, all functions.</td>
</tr>
<tr>
<td>Areas of focus</td>
<td>Governed by Australian Auditing Standards and relevant accounting standards.</td>
<td>Follows the IIA’s Professional Practices Framework – a broad based program which ensures objectivity, professionalism and ethics.</td>
</tr>
<tr>
<td>Standards</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Approach</td>
<td>Sufficient work completed to form an opinion on the financial statements.</td>
<td>Sufficient work undertaken to provide insight and give an informed independent view to the Board and Senior Management.</td>
</tr>
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<td>-------------------</td>
<td>---------------------------------------------------------------------------</td>
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</tr>
<tr>
<td>Independence</td>
<td>Is external to the organisation.</td>
<td>Part of the organisation but independent of management – independence is achieved by reporting to the Board (via the Board Audit Committee.)</td>
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<tr>
<td>Risk and control</td>
<td>Identifies risks and assesses controls over financial reporting and places reliance on controls to the extent practicable. Emphasis is on gaining sufficient audit evidence to conclude that the financial statements present a true and fair view.</td>
<td>Provides an independent view on the organisation’s risk management, risk assessment and governance processes. Reviews the adequacy of control design to ensure that risks are effectively managed, and then tests operation of key controls to ensure they are operating as intended and therefore are effective in managing the company’s risk.</td>
</tr>
<tr>
<td>Driving results</td>
<td>Makes recommendations to improve the internal control environment</td>
<td>Makes recommendations to improve the internal control environment and to improve the performance of the organisation. Also required by the IIA’S standards to ensure that a follow up process is put in place to drive results and make sure that agreed recommendations are actioned.</td>
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</tbody>
</table>
Typical career path

University qualifications in accounting followed by a move into professional services firm, then followed by a move into the finance department of a large organisation or progression towards partnership.

Broad intake including engineers, accountants and other specialists often with experience outside the audit profession. Will join a company or service provider initially before fast-tracking into management or senior finance position within a sizeable organisation.

Source: THE Institute of Internal Auditors Australia

Having clarified the differences between internal and external auditors, it is opportune to briefly look at the history of internal auditing and the Institute of Internal Auditors.

1.3 A brief history of internal auditing and the Institute of Internal Auditors (IIA)

The origins of internal auditing are intuitively described by historian Richard Brown (1905) quoted by Ramamoorti (2003:2) as follows:

The origin of auditing goes back to times scarcely less remote than that of accounting... Whenever the advance of civilization brought about the necessity of one man being entrusted to some extent with the property of another, the advisability of some kind of check upon the fidelity of the former would become apparent.

Record keeping systems were first instituted by organised businesses and governments in the Near East as far back as 4000 BC, to correctly record receipts and payments and for collection of taxes. Public systems in Babylonia, Greece, the Roman Empire developed systems of checks and balances to prevent and detect errors and fraud. The emergence of double entry bookkeeping in around 1494 AD enhanced the need for exercising stewardship and control. In the early part of the 20th century, as businesses grew in size, scope and complexity, employing thousands of employees in different locations, a critical need for
verification of information used for decision making emerged (Ramamoorti 2003). Fraud and error were the major problems and the volume of transactions resulted in prohibitive bills for those companies which wanted to maintain the traditional audit by the external auditor. As a result most big organisations had some form of internal audit function. Initially the emphasis was on protection against payroll fraud, loss of cash and other assets and internal auditors concentrated their efforts on examination of financial records and verification of those assets that were most vulnerable to misappropriation. Auditing served as a psychological deterrent against would-be wrong doers (National Industrial Conference Board Report 1963). The necessity of internal auditing can best be described by visionary remarks by Arthur E Hald, (quoted by Flesher 1996:1) one of the charter members of the Institute of Internal Auditors in 1944

Necessity created internal auditing and is making it an integral part of modern business. No large business can escape it. If they haven’t it now, they will have it sooner or later, and, if events keep developing as they do at present, they will have to have it sooner.

Prior to 1941, internal auditing was essentially a clerical function within an organisation with no set standards of conduct. The turning point came in 1941, as a result of two events. In that year, the first book on internal auditing, written by Victor Z Brinks was published. In the same year, a group of 24 individuals came together to form the Institute of Internal Auditors. On November 1941, the Institute of Internal Auditors’ Certificate of Incorporation was filed (IIA 2012). It identified the Institute as a membership corporation and stated the specific purposes of the institute which were to:

- To cultivate, promote and disseminate knowledge and information concerning internal auditing and subjects related thereto;
- To establish and maintain high standards of integrity, honour and character among internal auditors;
• To furnish information regarding internal auditing and the practice and methods thereof to its members and other persons interested therein and to the general public;
• To cause the publication of articles relating to internal auditing and practices and methods thereof;
• To establish and maintain a library and reading rooms and social rooms for the use of members;
• To promote social intercourse among its members; and
• To do any and all things which shall be lawful and appropriate in furtherance of any of the purposes herein before expressed (Ramamoorti 2003)

The statement of responsibilities issued by the IIA in 1947 (IIA 2012) stated that internal audit primarily dealt with accounting and financial matters, but may also deal with matters of an operational nature. However the 1957 version stated that the auditor should be concerned with any phase of the business activity and includes the following duties for the internal auditor:

• Reviewing and appraising the soundness, adequacy and application of accounting, financial and operating controls
• Ascertaining the extent of compliance with established policies, plans, and procedures
• Ascertaining the extent to which organisational assets are accounted for, and safeguarded from losses of all kinds
• Ascertaining the reliability of accounting and other data developed within the organisation
• Appraising the quality of performance in carrying out assigned responsibilities (Ramamoorti 2003)
There was therefore a shift from purely financial and accounting audits to emphasis on operational audits, aimed at ensuring that the organisation achieved its objectives. The statement of responsibilities was further revised in 1976, 1981, and 1990 to reflect the rapidly changing responsibilities of internal auditors, necessitated by developments and advances in the business world (IIA 2012). These changes are summarised in Table 1.2:

**Table 1.2: IIA Statements of responsibility**

<table>
<thead>
<tr>
<th>Issue</th>
<th>Statement of Internal Auditing</th>
<th>Changes</th>
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</table>
| 1947  | Internal audit is an independent appraisal activity within an organisation for the review of the accounting, financial, and other operations as a basis for protective and constructive service to management. It deals primarily with accounting and financial matters but it may also properly deal with matters of an operating nature. | Establishing internal audit:  
  - As an independent activity within an organisation  
  - To deal with accounting, financial and accounting matters |
<p>| 1957  | Internal audit is an independent appraisal activity within an organisation for the review of the accounting, financial, and other operations as a basis for service to management. It is a managerial control, which functions by measuring and evaluating the effectiveness of other controls. | As a managerial control function that is a manager control. The statement referred to operations focus by auditors. |
| 1971  | Internal audit is an independent appraisal activity within an organisation for the review of operations as a service to management. It is a managerial control, which functions by measuring and evaluating the effectiveness of other controls. | Scope expansion from narrow focus for audit attention with no automatic right for audit attention with no automatic right to audit accounting operations (hence accounting operations (hence 1997:25; Blackburn, 2003) |</p>
<table>
<thead>
<tr>
<th>Year</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>1976</td>
<td>Female members of the IIA recognised as professional equals and suggested that the IIA publications should not be gender biased.</td>
</tr>
<tr>
<td>1978</td>
<td><strong>Definition of Internal Auditing:</strong> Internal auditing is an independent appraisal function established within an organisation to examine and evaluate its activities as a service to the organisation. The objective of internal auditing is to assist members of the organisation in the effective discharge of their responsibilities. To this end, internal auditing furnishes them with analyses, appraisals, recommendations, counsel and information concerning the activities reviewed. The first definition of Internal auditing has several changes to the original statement - a service to the organisation broadened to management but also positioned it to external bodies. There is also explicit reinforcing the move away from serving internal audit departments and the unavoidable functions.</td>
</tr>
<tr>
<td>1981</td>
<td>Internal audit responsibilities - additional objective and scope - &quot;economy, efficiency as well as program evaluation audits&quot;. Scope of internal audit expanded to include review of program results - the equivalent within public sector auditing.</td>
</tr>
<tr>
<td>1990</td>
<td>&quot;Internal auditing is an independent appraisal function established within an organisation to examine and evaluate its activities as a service to the organisation.&quot; Internal audit's primary client changed to the broader client base of &quot;service to reflect and align with the definition of the Professional Standards of Internal Audit&quot;.</td>
</tr>
</tbody>
</table>
| 1999 | Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. Definition was radically updated to reflect the role of internal audit departments and the unavoidable functions. Definition is criticized for people (Blackburn, 2003). 'Objective' is word 'assurance' replaces 'appraisal'. Definition is criticized for people (Blackburn, 2003). 'Objective' is 'consulting', adding value and improving.
A professional journal, entitled The Internal Auditor, was introduced in September 1944. The first Certified Internal Auditor examinations sponsored by the Institute of Internal Auditors were held in 1974. (IIA 2012)

According to Ramamoorti (2003) and Anderson and Dahle (2009), in 1978 the Institute of Internal Auditors formally approved the standards for the professional practice of internal auditing which had the following purposes:

- Assist in communicating to others the role, scope, performance and objectives of internal auditing;
- Unify internal auditing throughout the world;
- Encourage improved internal auditing;
- Establish the basis for consistent measurement of internal auditing operations; and
- Provide a vehicle by which internal auditing can be fully recognised as a profession.

Another development that affected the profession was the Treadway Commission Report of 1987 (Ramamoorti 2003). The Treadway Commission was organised by 5 accounting organisations, namely, the Institute of Internal Auditors (IIA), the American Institute of Certified and Public Accountants (AICPA), the American Accounting Association (AAA), the Institute of Management Accountants (IMA) and the Financial Executives International (FEI), known as the Committee of Sponsoring Organisations (COSO). Its mandate was to study the cause of fraudulent financial reporting. It concluded that:

- An internal audit function should exist in every corporation;
There should be a corporate audit committee composed of non-management directors of the corporation (COSO 1987).

These recommendations further elevated the status of the internal audit profession (Ridley 2008). Additionally, in 1997, the Institute of Internal Auditors appointed a Guidance Task Force (IIA2012) to study the gap between the evolving internal auditing practices and auditing standards, to determine how existing standard setting processes could be improved (Anderson and Dahle 2009). Its key recommendations included revising the definition of internal auditing and the creation of a new professional practices framework, The International Professional Practices Framework (IPPF). In 1999, a new definition embracing risk management, control and governance processes, with emphasis on value addition was approved by the Institute of Internal Auditors, and in December 2000, new standards were issued (IIA2012). The following is the wording of the new definition according to IIA (2004: xxvii)

An independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Chapman and Anderson (2002) argue that by including assurance and consulting, the new definition reflects a focussed approach and by stressing value addition, it broadens the mandate of internal auditing and underscores the significant contribution it makes to an organisation. As independence and objectivity are key elements in the definition of internal auditing, this study sought to determine how much independence the internal auditors in parastatals enjoyed, and how this affected their activities.

As the global professional body for internal auditing, the IIA is responsible for prescribing technical training, setting the examinations for, and admitting new member into the profession. It issues internal auditing standards in the form of the International Professional
Framework for Internal Auditing (IPPF), which comprises the Ethics and Standards, Practice Advisories, and Development and Practice Aids, which are discussed below:

- Standards and Ethics are mandatory guidance;
- Advisories are strongly recommended, and
- Development and Practice Aids are helpful reference materials developed and endorsed by the Institute of Internal Auditors.

These resources are important in the proper execution of internal auditing duties, and this study inquired the extent to which they are available to and used by the internal auditors.

The purpose of the IPPF is “to organise the full range of internal audit guidance in a manner that is readily accessible on a timely basis … by encompassing current internal audit practice as well as allowing for future expansion.” (Institute of Internal Auditors 2004:ii). The institute has a research foundation whose mission is “to expand knowledge and understanding of internal auditing by providing relevant research and educational products to advance the profession globally.” (www.theiia.org/rf-news/about-the-foundation-1/). The foundation carries out periodic surveys to determine the state of internal auditing globally. The Ethics and Standards are mandatory guidelines, which have been submitted for review by the profession through the exposure draft process. This process involves sending the draft standards to members and practitioners, inviting their comments, and reviewing all the comments, before a standard is finally issued (IIA 2012). Observation by all practising internal auditors, be they members of the IIA or not is mandatory. The Practice Advisories are interpretations of the standards and are considered the best ways of implementing the standards. They are issued after review by the IIA’s Professional Issues Committee. Development and Practice Aids are materials developed and/or endorsed by the IIA, for example, research studies, books, and seminars, and provide auditors with views of various
experts on internal auditing techniques and practices. (IIA 2012). These resources and seminars are necessary to ensure an improvement in the professional practice of the internal auditors and this study examined the extent to which the internal auditors had access to them (the resources).

These developments show that the internal auditing had now truly attained professional status, and this is further evidenced by the principles contained in the Code of Ethics, (IIA 2004) which are briefly stated below:

- **Integrity** – The integrity of internal auditors establishes trust and thus provides the basis for reliance on their judgement.

- **Objectivity** – Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the activity or process being examined. Internal auditors make balanced assessments of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgements.

- **Confidentiality** – Internal auditors respect the value and ownership of the information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.

- **Competency** – Internal auditors apply the knowledge, skills and experience needed in the performance of internal auditing services.

This study looked at the extent to which these ethical principles were observed, with emphasis on objectivity.

In Zimbabwe there is an active chapter of the IIA which was formed in 1988 (https://theiia.org/chapters/index.cfm/home.page/cid/222). It is also pertinent to mention that, unlike external audit professions, which have statutory backing to bar a defaulting member
from public practice, the IIA does not have the power to bar members from practice because of breach of ethics or standards. This was cited by Christopher, Leung and Sarens (2007) as one of the reasons hampering consistency in the implementation of best practices.

The International Professional Practices Framework continues to be reviewed and updated through the exposure draft process, to keep the profession abreast of rapidly changing economic and social conditions. In this respect this study enquired whether the internal audit functions had the latest copies of the IPPF.

1.4 Importance of Internal Audit

Internal audit is one of the four pillars of good corporate governance (IIA Canada 2007) together with the board (board audit committee), management and external auditors. These four elements work together to achieve the objectives of the organisation. The role of internal audit is important in that it is involved in monitoring operations of the organisation more closely and from within, advising management on risk management, providing consultancy service to the organisation as and when required. The internal auditor has a more intimate knowledge of the organisation and with his or her technical training he/she is able to advise management and the board in steering the organisation in the right direction (Moeller 2005). This study looked at the relationships between the internal audit function and the board and management, and how these relationships affected the effectiveness and independence of the internal audit function.

The importance of internal audit is also illustrated by the Three Lines of Defence model (ECIIA 2011; IIA 2013). It is an organisational model to manage risks and compliance obligations and specifically defines the related roles and responsibilities of the particular organs involved in the organisation. It has been increasingly applied in recent years and is a
useful tool to explain and demonstrate the different roles of organisational organs in internal governance and the interplay between them (ECIIA 2011). The model is shown on Fig. 1.1

**Fig. 1.1: The three lines of defence model.**

![The Three Lines of Defence Diagram](image)

**Source: ECIIA (2011)**

The first line of defence is the organisation’s operational management, which has ownership, responsibility and accountability for assessing, controlling and mitigating risks (ECIIA 2011; IIA 2013). The activities of this line of defence are examined by internal auditors, who then give advice on improvement of operations. It is therefore necessary that the internal auditors are not influenced by anybody in their examination of activities, as well as when they report on the activities of operational management. This research examined the extent to which internal auditors had independence to examine all/any activities of operational management, and to what extent their reports were accepted and acted upon.
The second line of defence is the risk management function and other supporting functions which facilitate and monitor the implementation of effective risk management practices by operational management and assist the risk owners in reporting adequate risk related information up and down the organisation (ECIIA 2011; IIA 2013).

The third line is the internal audit function. It will, through a risk based approach, provide assurance to the organisation’s board and senior management on how effective the organisation assesses and manages its risk, including the manner in which the first and second lines of defence operate. The assurance task covers all elements of an organisation’s risk management framework, from risk identification, risk assessment and response to communicating of risk related information (ECIIA 2011). This clearly demonstrates the huge responsibility placed on the shoulders of internal audit in relation to the critical task of enterprise risk management. In order to effectively carry out this responsibility, the internal auditors should be independent and objective in planning their activities, performing the audits and reporting their findings. This study sought to find out to what extent the internal auditors were independent and objective in planning and performing audits as well as reporting their findings.

A number of writers and scholars (Wood 2004; Gramling, Malletta, Schneider and Church 2004; ISA 610 2008; and Office of the Auditor General, Canada 1992) have acknowledged the importance of internal auditing in improving the operations of organisations. In a survey of 480 organisations in Australia and New Zealand, Coram, Ferguson and Moroney (2008) found that organisations with an internal audit function were better placed and more likely to detect fraud within the organisations than those without such a function. They also found that those organisations that relied on in-house internal audit services were more likely to detect fraud than those which relied solely on outsourced internal audit services. They concluded
that the internal audit function adds value through improving the control and monitoring environment, and that the function was a crucial part of an entity’s corporate governance.

In another study, Wallace and Kreutzfeldt (1991) found that the number and magnitude of errors requiring adjustment by the external auditor were substantially less in entities with an internal audit function than those that did not have one. Nestor (2004) also noted that internal audit is an important governance tool to protect corporations from internal criminal behaviour. Similarly, Luehfeng, Daily, Phillips and Smith (2003) and Belloli (2006) argued that internal audit is a vital tool in fraud detection involving misappropriation of assets by employees or outsiders. These assertions support the statement by the IIA (IIA 1999) that the objectives of internal auditing are to improve effectiveness of risk management, control and governance. However, for this improvement to take place, internal auditors should be independent and objective when performing their duties. This study sought to find out how much the internal auditors in parastatals were independent and objective.

1.5 Definition of internal auditing and internal auditors

The IIA (2004: xxvii) defines internal auditing as:

> An independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Internal auditors are defined as “institute members, recipients of or candidates for IIA certifications, and those who provide internal auditing services within the definition of internal auditing.” (IIA 2004: xxix – xxx) This definition is wide enough to include all those who practise internal auditing be they members of the IIA or not. The expectation therefore is that all practitioners of internal auditing will be guided by the IIA standards and the code of ethics. In conducting this study therefore the assumption is that all internal auditors are
guided by the standards. Most scholars and authors, including Sawyer, Dittenhofer and Scheiner (2003), Moeller (2005) and Pickett (2010) support this view. Consequently, in this research, it is assumed that internal auditors in parastatals are guided by IIA standards.

The definition of internal auditing clearly states the need for independence and objectivity in the performance of audits. The glossary to the IIA standards (Institute IIA 2004: 25-30) defines these two concepts as follows:

**Independence**: The freedom from conditions that threaten objectivity or the appearance of objectivity. Such threats must be managed at the individual auditor, engagement, functional and organisational levels.

**Objectivity**: An unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they have an honest belief in their work product and that no significant quality compromises are made. Objectivity requires internal auditors not to subordinate their judgement on audit matters to that of others.

Independence and objectivity lie at the heart of auditing. They are imperative for the effective discharge of duties by internal auditors, because of the need to give impartial and unbiased assessments and reports. Various auditing bodies including the Institute of Chartered Accountants in England and Wales (ICAEW) and the American Institute of Certified Public Accountants (AICPA) emphasize the importance of these attributes in their standards and codes of ethics. In fact, in terms of ET Section 101: Independence, the AICPA prohibits firms from issuing an opinion unless the auditor is independent. This study therefore examined the extent to which internal auditors in parastatals enjoyed independence and objectivity when performing their duties.

**1.6 Inherent conflicts of interest,**

There are however inherent conflicts of interest with the potential of impairing objectivity and independence of the internal auditor. The internal auditor is an employee of the organisation and is expected to audit those who are responsible for payment of his salary, his promotion and his career advancement (Paape 2007). This creates a situation where the
internal auditor may feel that following the standards and maintaining an independent stance on certain issues could jeopardise his or her chances of progressing to higher positions within the organisation. The fact that the internal auditor may be called upon to perform operational duties or act in an advisory capacity creates the danger that the auditor might later audit his or her own work. There are also instances where the requirement of the internal auditing standards may be at variance with the objectives of the organisation, and the internal auditor will be forced to choose between the two. These threats to independence have to be properly managed, and this study examines how they are managed in the three organisations under review, using the internal auditing standards as a yardstick, since they are regarded by audit practitioners as the best practices within the internal auditing profession.

1.7 Components of independence

Mautz and Sharaf (1961), cited by Mutchler (2003) suggest that independence comprises programming independence (the auditor has control over the nature of the audit program), investigative independence (the auditor is free to collect and evaluate all the evidence deemed necessary without interference) and reporting independence (the auditor is free to report the results of the audit without interference). They suggest that these concepts will help a practitioner to achieve honest disinterestedness (to promote unbiased judgements and consideration of facts as determinants of a final opinion). These three concepts cover the three steps in the audit process, from determining the scope of the audit to issuing of the final report, and this study endeavours to determine the amount of independence the auditors enjoy in each of the three aspects.
1.7.1 Independence in appearance and in fact

The two types of independence frequently cited are independence in fact (when the auditor actually maintains an unbiased attitude throughout the audit), and independence in appearance (the result of others’ perceptions of this independence) (Arens and Loebbecke 1999). Independence in appearance is enhanced by the standards and code of ethics, and is necessary to retain the confidence of audit clients in the profession. However, independence in fact is most the important, as it involves the personal commitment of audit practitioners to independence and objectivity. Some writers argue that perceptions of users of audited financial statements (independence in appearance) are important as this might lead them to believe that they cannot rely on the audited financial statements (Lowe, Geiger and Pany 2001; Olazabal and Almer 2001). However, other writers (McGrath, Siegel, Dunfee, Glazer and Jaenecke 2001) have argued that if an auditor can make independent decisions, despite perceptions of lack of independence or when exposed to a potentially compromising situation, he is considered independent in fact.

1.7.2 Organisational independence and individual objectivity

The IIA standards distinguish between organisational independence - freedom from influences/interference from within the organisation through its various organs (Standard 1110) and individual objectivity - personal commitment of the auditor to independence and objectivity (Standard 1120).

Organisational independence means independence from interference by the other three elements of corporate governance, namely, management [including the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO)], the external auditor, and the board (through the audit committee). (IIA 2004; Moeller 2005; Sawyer 2002)
the relationships between the internal audit and these organs to determine the degree of independence afforded the internal auditors and what effect this has on their effectiveness.

Individual objectivity relates to the internal auditor’s personal commitment to independence. The auditor may be faced with many situations of conflict of interests during the course of his/her duties. The seven main threats to Individual objectivity are: self-review (when the auditor reviews his own work); social pressure (when auditor is under pressure from the auditee or other members of the audit team); economic interests (dealing with someone who can influence the financial status of the auditor, e.g. incentives or salary); personal relations (where the auditee is a personal friend or relative), familiarity (resulting from a long relationship with the auditee); cultural bias (resulting from lack of understanding of some culture or customs); and cognitive bias (resulting from some pre-conceived biases) (IIA 2001). The standards make it very clear that situations of conflict of interests should be avoided, and should be fully disclosed before commencement of an audit whenever they exist. Furthermore any situations of potential impairment of objectivity should be properly managed (IIA 2004). Despite all these guidelines, financial irregularities of huge proportions, involving the top brass of organisations continue to happen. This study inquired into threats and impairments faced by internal auditors in parastatals and how these were managed.

1.8 Some Financial Scandals that Occurred in Some Developed Countries

Concerns about independence and objectivity of auditors came to the fore in the 1980 - 90s following financial scandals and the fall of big companies like Maxwell, BCCI, and Lloyds of London in the UK. In the USA, the Enron high profile accounting scandal in 2001 shattered investors’ confidence in auditors. Enron was the seventh largest company in the United States of America. It collapsed after it was discovered that profits had been inflated by $ 600 million since 1997 (Schwartz, Dunfee and Kilne 2005). Many people asked: Where were the
auditors when all this was happening? (Moeller 2005) These collapses came at a time when external auditors were offering non audit services, including internal auditing to their audit clients. The provisions of non audit services proved to be lucrative business for external auditors, and soon spread rapidly throughout the profession. This practice started in the late 1980s. External audit firms offered internal audit services to their audit clients, promising them lower costs. Because the majority of senior management and audit committee members did not understand the difference between internal and external auditing, this practice soon spread to many large organisations in the United States of America (Moeller 2005). Though the IIA initially fought against their practice, it continued to grow in the 1990s (Moeller 2005). An IIA sponsored survey in the USA and Canada revealed that twenty-five percent of the surveyed organisations outsourced their internal audit functions, with public accounting firms doing the bulk of the work. Reasons for outsourcing were given as cost savings, adding specialised audit skills and to clean the house of incompetent people with a perceived lack of value (Moeller 2005).

The Enron case shows how far some of the accounting firms had gone in the provision of non audit services. Arthur Anderson, the external auditor for Enron managed the internal audit of Enron. The internal and external audit functions shared offices and resources and there was a seamless relationship between the two. A number of senior manages in Enron also came from Anderson. These arrangements created serious conflicts of interest and impaired the independence and objectivity of both the internal and external audit functions. The external auditors of the company, Anderson, had been auditing the company for more than two decades, and their independence was impaired due to familiarity. (Moeller 2005) The collapse of World Com, Health South, Tyco, Parmalat and others further highlighted concerns about auditor independence. These incidents resulted in huge losses to investors and shook investor confidence in the accounting and auditing profession. The US responded by
enacting the Sarbanes Oxley Act (SOX) of 2002, which tried to enhance auditor independence, by banning nine types of non-audit services, and introducing compulsory rotation of partners in audit engagements every 5 years, among other provisions.

A summary of some of the provisions of the Sarbanes Oxley Act which affect auditing is given in table 1.3

**TABLE 1.3**
*Sarbanes-Oxley Act Key Provisions Summary*
The following are the major sections of SOA of interest to internal auditors

<table>
<thead>
<tr>
<th>Section</th>
<th>Subject</th>
<th>Rule or Requirement</th>
</tr>
</thead>
<tbody>
<tr>
<td>101</td>
<td>Establishment of PCAOB</td>
<td>Overall rule for the establishment of PCAOB, including membership requirements</td>
</tr>
<tr>
<td>104</td>
<td>Accounting Firm Inspections</td>
<td>Schedule for registered firm inspections.</td>
</tr>
<tr>
<td>108</td>
<td>Auditing Standards</td>
<td>The PCAOB will accept current standards, but will issue new ones.</td>
</tr>
<tr>
<td>201</td>
<td>Out of Scope Practices</td>
<td>Outlines prohibited practices such as those related to internal audit outsourcing, bookkeeping, and financial systems design</td>
</tr>
<tr>
<td>203</td>
<td>Audit Partner Rotations</td>
<td>The audit partner and the reviewing partner must rotate off an assignment every five years.</td>
</tr>
<tr>
<td>301</td>
<td>Audit Committee Independence</td>
<td>All audit committee members must be independent directors.</td>
</tr>
<tr>
<td>302</td>
<td>Corp. Responsibility for Financial Reports</td>
<td>The CEO and CFO must certify the periodic financial reports.</td>
</tr>
<tr>
<td>305</td>
<td>Officer and Director</td>
<td>Bars&lt;br&gt;If funds are received as part of fraudulent/illegal accounting, the officer or director is required to personally reimburse funds received.</td>
</tr>
<tr>
<td>404</td>
<td>Internal Control Reports</td>
<td>Management is responsible for an annual assessment of internal controls.</td>
</tr>
<tr>
<td>407</td>
<td>Financial Expert</td>
<td>One audit committee director must be a designated financial expert.</td>
</tr>
<tr>
<td>409</td>
<td>Real Time Disclosure</td>
<td>Financial reports must be distributed in a rapid and current manner.</td>
</tr>
</tbody>
</table>
The SEC may prohibit an officer or director from serving in another public company if guilty of a violation.

Source: Moeller (2005): Brink’s internal auditing

In the UK, the “Ethical standards for auditors in the UK” was issued by the Auditing Practices Board in 2004. These included the rotation of audit partners every 5 years and key personnel every 7 years on audit engagements, and the compulsory withdrawal when non-audit services are incompatible with audit objectives.

In Australia, at the time of the high profile collapses, lack of independence was rife, due to major accounting firms establishing multi disciplinary practices (with consulting, legal and tax practices) in an attempt to offer a one stop advisory service to clients and maximise fees. (du Plessis, Hargovan and Bargaric 2011). The response was the Common Law Economic Reform Program (CLERP 9) of 2002. Reforms were instituted to enhance auditor oversight and independence, and these include:

- A general requirement for auditors to be independent under the Act.
- Enhancing disclosure requirements for non audit services given to clients in terms of type of service and the amounts involved.
- Prohibiting audit partners directly involved in an audit from becoming directors of the audited client within a cooling off period of two years after resigning from the firm.
- Establishing of an auditor independence supervisory board
- Prohibition of services where there is a conflict of interests or where the auditor’s independence is impaired.

These regulations were intended to prevent recurrence of the scandals by among other things enhancing auditor independence. In addition, several corporate governance codes were
issued. This study examined the extent to which the IIA and corporate guidelines were observed by internal auditors.

1.9 A Brief History of Parastatals in Zimbabwe

In the colonial era, economic policies were characterised by unprecedented investment in physical and social infrastructure for whites. The state used parastatals to effect controls in all sectors of the economy. Ensuring control over strategic economic activities, and investing in areas deemed unattractive to the private sector, like the Cold Storage Commission and the Rhodesia Iron and Steel Company. (Zhou and Masunungure 2006). The majority of the parastatals were wholly owned state monopolies and the state controlled the prices of goods and services provided by the parastatals. The prices were pegged at low levels, making it difficult for the parastatals to recover their operational costs. As a result, they received heavy subsidies. (Zhou and Masunungure 2006)

This is the situation that was inherited by the new black government at independence. The government adopted the policy of Growth with Equity in 1981, in order to address the inequities between blacks and whites, and in line with its redistributive policies, more parastatals were established, e.g. Small Enterprises Development Corporation (SEDCO), National Social Security Agency (NASSA), National Oil Company of Zimbabwe (NOCZIM), and existing ones were expanded. From 1980 to 1990, the number of parastatals had risen from 20 to 40, with the majority being wholly owned monopolies. (Zhou and Masunungure 2006). The role of the parastatal sector as outlined in the Zimbabwe government publication entitled Zimbabwe: First Decade 1980 -1990 was to provide the state with a means and agency through which the state could intervene in economic and social sectors. Parastatals were established under different legal forms, some through a special act of parliament, some through the companies act, and others as joint ventures with private
companies, with the state having a majority ownership (51% and above). The parastatals Commission was put in charge of all parastatals from 1988 to 1990, and after its dissolution, each parastatal was managed by a board whose members were appointed by the responsible minister. (Zhou and Masunungure 2006)

1.9.1 Financing and management of parastatals

Parastatals continued to receive subsidies, with no improvement in their financial performance(Zhou and Masunungure 2006). Table 1.4 shows subsidies to major parastatals during the period 1986 to 1990.

Table 1.4: Government subsidies to Public enterprises (PE’s): 1986 to 1990. (Z$ million)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GRAIN MARKETING BOARD</td>
<td>48.1</td>
<td>123.9</td>
<td>80.0</td>
<td>48.9</td>
</tr>
<tr>
<td>DAIRY MARKETING BOARD</td>
<td>65.0</td>
<td>43.3</td>
<td>40.0</td>
<td>56.1</td>
</tr>
<tr>
<td>COLD STORAGE COMMISSION</td>
<td>49.5</td>
<td>31.2</td>
<td>11.0</td>
<td>37.5</td>
</tr>
<tr>
<td>COTTON MARKETING BOARD</td>
<td>-</td>
<td>11.7</td>
<td>25.0</td>
<td>17.7</td>
</tr>
<tr>
<td>AGRICULTURAL MARKETING AUTHORITY</td>
<td>3.4</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>NATIONAL RAILWAYS OF ZIMBABWE</td>
<td>80.0</td>
<td>100.0</td>
<td>120.0</td>
<td>100.0</td>
</tr>
<tr>
<td>AIR ZIMBABWE</td>
<td>45.0</td>
<td>39.9</td>
<td>10.0</td>
<td>15.0</td>
</tr>
<tr>
<td>AFFRETAIR</td>
<td>15.0</td>
<td>3.0</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>ZIMBABWE IRON AND STEEL COMPANY</td>
<td>82.0</td>
<td>100.0</td>
<td>167.0</td>
<td>100.0</td>
</tr>
<tr>
<td>AGRICULTURAL FINANCE CORPORATION</td>
<td>18.4</td>
<td>4.5</td>
<td>15.0</td>
<td>12.5</td>
</tr>
<tr>
<td>Total</td>
<td>406.4</td>
<td>457.5</td>
<td>468.0</td>
<td>387.7</td>
</tr>
</tbody>
</table>
Table 1.5 shows the financial performance of these parastatals during the same period, i.e. 1986 to 1990.

### Table 1.5

**Trends in profits and losses of major parastatals 1986 to 1990 (Z$ million)**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GRAIN MARKETING BOARD</td>
<td>(82.9)</td>
<td>(86.6)</td>
<td>(71.7)</td>
<td>(71.8)</td>
</tr>
<tr>
<td>DAIRY MARKETING BOARD</td>
<td>(55.6)</td>
<td>(49.3)</td>
<td>(51.3)</td>
<td>(52.2)</td>
</tr>
<tr>
<td>COLD STORAGE COMMISSION</td>
<td>(33.4)</td>
<td>(28.9)</td>
<td>(36.7)</td>
<td>(18.0)</td>
</tr>
<tr>
<td>COTTON MARKETING BOARD</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>AGRICULTURAL MARKETING AUTHORITY</td>
<td>(91.7)</td>
<td>126.8</td>
<td>(116.7)</td>
<td>(117.6)</td>
</tr>
<tr>
<td>NATIONAL RAILWAYS OF ZIMBABWE</td>
<td>(25.1)</td>
<td>(23.2)</td>
<td>(27.1)</td>
<td>(10.1)</td>
</tr>
<tr>
<td>AIR ZIMBABWE</td>
<td>(3.3)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>AFFRETAIR</td>
<td>(57.9)</td>
<td>(89.4)</td>
<td>87.2</td>
<td>(77.6)</td>
</tr>
<tr>
<td>ZIMBABWE IRON AND STEEL COMPANY</td>
<td>(14.6)</td>
<td>(17.9)</td>
<td>(16.0)</td>
<td>-</td>
</tr>
<tr>
<td>AGRICULTURAL FINANCE CORPORATION</td>
<td>(13.4)</td>
<td>119.9</td>
<td>112.2</td>
<td>5.9</td>
</tr>
<tr>
<td>NATIONAL OIL COMPANY OF ZIMBABWE</td>
<td>(11.1)</td>
<td>(50.0)</td>
<td>(33.4)</td>
<td>(21.0)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>(389.0)</strong></td>
<td><strong>(353.1)</strong></td>
<td><strong>(327.9)</strong></td>
<td><strong>(362.4)</strong></td>
</tr>
</tbody>
</table>

Key: Figures in parenthesis reflect losses.

**Source:** Adapted from Government of Zimbabwe (1991): A Framework for Economic Reform.

This subsidy dependence syndrome became a heavy burden on the fiscus. Zhou *et al* (2006) also point out that besides handouts from the treasury, parastatals also enjoyed hidden
subsidies in the form of tax exemptions, cheap government-guaranteed credit facilities and below market price purchases from the government. The state continued to set prices for parastatal goods and services, and inordinate delays were experienced in approving price increases. Zhou (2001) cites instances where the government took twenty-six months to approve a request for a tariff increase by the National Railways of Zimbabwe, and Air Zimbabwe had to wait three months before it could increase its fares. This led to huge deficits by parastatals. Losses were also incurred as a result of social mandates of some parastatals, which were not economically viable but beneficial to society as a whole.

1.9.2 The Economic Structural Adjustment Program (1991 -1995)

When the Economic Structural Adjustment Program (ESAP) was adopted in 1991, one of its major components was Public Enterprise reforms, aimed at making parastatals more efficient, and thus reducing the fiscal burden of paying subsidies. The government stated that it would “de-emphasize its expenditure on social services and emphasize investment in material production sectors” (Government of Zimbabwe 1990:6). The July 1990 policy statement specified targets, which included reduction of the budget deficit by 1994/95 from 10 to 5 percent of the gross domestic product (GDP). This would be achieved, *inter alia*, through phasing out of subsidies to parastatals and the introduction of cost recovery measures. The Framework for Economic Reform 1991-95 document, which is a more detailed version of the program specified a 94% reduction in subsidies to parastatals from Z$629 million in 1990/91 to only $40 million in 1994/95. In 1994, the Inter Ministerial Committee on Privatisation and Commercialisation produced a paper entitled “Privatisation and Commercialisation Policy and Strategy Paper.” It divided parastatals into 3 broad categories, namely, category 1 to be retained because of their social or promotional roles, category 2 to be retained because of strategic reasons, and category 3 for commercialisation and ultimate privatisation.
1.9.3 The post ESAP era

Zhou et al (2006) note that not much was achieved during the ESAP era, in the nature of commercialisation, privatisation or reduction of parastatal deficits. They argue that restructuring and rationalisation of parastatals proved very difficult, and they continued to incur huge losses, posing a drain on the budget. This, they opine, was largely due to the fact that parastatals continued to operate under their traditional enabling acts, with the government exercising direct controls on pricing, investment, hiring and firing.

Because some of the ESAP targets were not met, a successor program, the Zimbabwe Program for Economic and Social Transformation (ZIMPREST) (1996 – 2000) was introduced. However, it was officially launched in 1998. One of the objectives was to complete public enterprise reforms through commercialisation and privatisation of public enterprises. In 1999, the Privatisation Agency of Zimbabwe was launched, with the mandate to spearhead and manage the privatisation program.

1.9.4 Successful privatisations

Dairy Marketing Board became the first parastatal to be privatised and the major events in the road to privatisation are highlighted below (www.dairibord.com/index):

- 1992- Break even achieved and thereafter operated as a viable enterprise;
- 1995 – Preparations for privatisation undertaken;
- 23-10-1996 – Government announced plans to privatise state enterprises;
- June 1997 – Privatisation completed, with the government divesting seventy –five percent to private investors;
- September 1997 – Dairibord Zimbabwe Limited listed on the Zimbabwe stock exchange;
• 1998 – Dairibord Zimbabwe Limited acquired sixty percent in Dairibord Malawi;
• 1988 – Government sold the remaining twenty-five percent equity to private investors.

Other successful privatisations which followed were:

The Cotton Company of Zimbabwe (Cottco) and Commercial Bank of Zimbabwe (CBZ) in 1997, Rainbow Tourism Group (RTG) and the Zimbabwe Reinsurance Company (ZimRe) in 1999. (Kateera 2001; RBZ 2007)

Privatisation is defined in the government produced PAZ documents as the transfer of what are currently state owned assets to the private sector, while commercialisation means restructuring of parastatals and transforming them into profitable entities.

1.9.5 Recent developments in the parastatal sector in Zimbabwe

Recent developments show that the government of Zimbabwe is committed to commercialisation and privatisation of parastatals. The government has since produced a code of corporate governance for parastatals (Daily News, 2 March 2013) as well as a restructuring manual to guide state owned enterprises in management and restructuring processes (The Herald, 23 November 2013). It is also interesting to note the following remarks by the Minster of State Enterprises and Parastatals. He is quoted in the Herald of 7 May 2012 as saying that most parastatals were run by incompetent managers, as evidenced by their failure to come up with meaningful restructuring proposals. The same newspaper on 10 March 2012 also highlights the fact that about seven parastatals had been operating for more than two years without boards. Given this state of affairs, it appears independent internal audit presence in the respective parastatals would assist in improving the situation.
It is clear that the government has chosen the commercialisation and privatisation path for all parastatals. This means that parastatals will either be privatised or commercialised. It is therefore my opinion that an empowered, independent and objective internal audit would greatly assist the parastatals earmarked for commercialisation and privatisation to achieve break-even and even profitability, thereby making them attractive to investors.

1.10 Scandals and financial mismanagement in Zimbabwe

Zimbabwe has not been spared of financial scandals and instances of financial mismanagement. In his 2011 budget speech, the Minister of Finance bemoaned the huge perennial losses being incurred by parastatals and state enterprises. He highlighted the following losses during the six-month period from January to June 2010:

- Agribank: $2,820,239
- Air Zimbabwe: $14,609,463
- Cold storage commission: $3,036,248
- Grain Marketing Board: $4,505,205
- Noczim: $11,942,685
- National Railways of Zimbabwe: $9,621,069

Furthermore, a number of financial scandals involving high ranking officials have occurred, and these include the Cold Storage Commission (CSC) (Daily Gazette 6 January 1993 and 26 May 1993), Zimbabwe United Passenger Company (ZUPCO) (The Financial Gazette, 13 July 2006 and 17 April 2008), the Grain Marketing Board (GMB) (The Herald, 26 August 2006). More recently scandals involving senior executives awarding themselves ridiculously high
salaries and perks have been unearthed at the ZBC, (Daily news, 13 December 2013) and PSMAS (Newsday, 31 January 2014).

These incidents resulted in unnecessary loss of public funds, which could have been used elsewhere to better the welfare of some members of the community.

When instances of financial irregularities occur and continue to rear their ugly head, despite the presence of internal auditors whose responsibility is to “evaluate and improve the effectiveness of risk management and governance processes”, (IIA 2004:xxvii) members of the public may begin to question whether the internal auditors have adequate independence and objectivity to be effective. This study therefore examines and evaluates the amount of independence and objectivity internal auditors in parastatals enjoy. It is pertinent to note that a review of related literature revealed a few previous research studies in Zimbabwe on this important aspect of internal auditing. It was the aim of this study to fill this gap in literature.

1.11 Statement of the problem

The post-independence era in Zimbabwe has been characterised by perennial losses in state enterprises. Furthermore, a number of high profile scandals have occurred, resulting in unwarranted losses of public funds. This has occurred despite the presence of internal auditors in the organisations concerned. In view of the continued occurrence of losses and financial scandals in the parastatals, and despite the presence of internal auditors, the question begging for attention is, Do internal auditors have adequate independence to enable them to effectively perform their duties?

1.12 Purpose of the study.

The purpose of this study therefore is to examine whether internal auditors in fact have this independence and objectivity and how this affects their effectiveness.
1.13 Objectives of the Study

The following were the objectives of the study:

- To determine if reporting structures permit independence and objectivity of internal auditors in the performance of their duties;
- To determine the extent to which the relationships between internal audit and other corporate governance arms enhance independence and objectivity;
- To explore the threats to independence and objectivity of the internal audit function;
- To determine if there are adequate procedures to deal with threats to independence and objectivity within the internal audit function;
- To make appropriate recommendations to enhance internal audit independent and objectivity.

1.14 Research questions

The study was guided by the following questions:

- To what extent do the reporting structures ensure broad audit coverage and freedom from interference in audit work?
- How much do relationships between Internal Audit (IA) and other corporate governance arms (the board, management, and external audit) enhance effectiveness and good governance?
- What are the threats to independence and objectivity in the IA function?
- What are the current procedures for dealing with threats to independence and objectivity within the internal audit function?
1.15 Significance of the study

The revelations of this study, if availed to concerned parties, will assist the organisations examined to gain insight into this important aspect of corporate governance and enable their managements and boards to make decisions from an informed position. The standard setters (the IIA) will also be apprised of the state of affairs in the Zimbabwean setting and this will enable them to plan their activities from an enlightened position. The government, as the major shareholder in the organisations examined will have a clear picture of what is obtaining in the organisations, from an independent source and this will enable it to take any corrective action where necessary. Government, in its capacity as legislator, it will also assess the need for any statutory enactments resulting from this study. It is also hoped that organisations not specifically covered by the study will learn lessons from it and use the knowledge to enhance good corporate governance.

The researcher feels that this study came at the right time. The country was emerging from a very difficult economic era, which was characterised by unprecedented hyperinflation, serious commodity shortages and chronic liquidity problems. In those circumstances, organisations were preoccupied with survival, and often, ethics and corporate integrity were sacrificed in the name of survival. It was hoped that the research findings will act as a timely reminder of the need to return to good governance and corporate integrity.

It is hoped that the results of the study will also shed insight into auditor independence. This information will be of benefit to the standard setters (the IIA), the policy makers (government), the affected organisations and hopefully, other organisations in commerce and industry. If the findings are acted upon by the relevant bodies, it is hoped that the independence of internal auditors will be enhanced and this would contribute in reducing financial scandals in parastatals."""
1.16 Delimitation of the study

The study is restricted to the examination of independence and objectivity of internal auditors in state controlled organisations. It is a case study covering three organisations. The findings therefore primarily relate to these three organisations and care should be exercised when generalising to other organisations. The study also examines in-house internal auditors only and does not cover outsourced services. The period covered by the study is 2010 to 2014. The study is guided by the best practices in the profession as pronounced by the global internal auditing professional body, the IIA.

1.17 Limitations of the study

This is a case study of three organisations, and the findings relate specifically to those organisations.

This is a very sensitive topic, but one that has to be tackled now. As a result a number of challenges were met along the way. When permission to conduct the research was being sought from the respective CEOs, there was a general reluctance to grant it. They wanted to know why the research was being carried out, who had ordered it, and how the information was going to be used and by whom. In one instance, the CEO requested copies of questionnaires and interview guides that would be used in the research, before he could grant permission, and these were provided. I informed the CEOs that the research was purely an academic exercise and the information collected would be treated in the strictest confidence and would not be disclosed or divulged to third parties. After these assurances, permission was granted. However, in one case, the CAE declined to give permission, citing the fact that the institution was in the process of a major re-organisation. He stated that staff were not in the mood to entertain outsiders, as they were anxiously awaiting the outcome of the
reorganisation. They were preoccupied with retaining their positions in the organisation. Consequently, another organisation was approached and permission was obtained.

Some participants were not comfortable with the use of a voice recorder during interviews and group discussions. The researcher explained that this was necessary so that the researcher would be able to properly analyse the data obtained from the participants. Some participants who were knowledgeable about qualitative research as a result of current or previous studies confirmed this to their colleagues and this put the participants at ease. However in one instance, a principal auditor declined the use of a voice recorder stating, “I don’t know where that voice will end up.” This highlights the culture of fear that has hit this society. He was given a questionnaire with open ended questions, which he completed and provided some useful information.

Another challenge that was encountered was the question of availability of participants for interviews and group discussions. Where it was not possible to find times that were convenient to the participants, they were given questionnaires with open ended questions. These were completed and returned to me.

In view of the sensitivity of the topic, the question of honesty or lack of it, regarding information given by the participants had to be tackled. Triangulation was used to check the accuracy or veracity of the information. The CAEs tended to give a picture where there were very few problems. As an example, the CAEs stated that they had fully adopted the IIA standards and code of ethics. However, during group discussions with the auditors and interviews with audit supervisors, it became clear that this was not the case. Most auditors, including the audit supervisors did not even know the meaning of IPPF (International Professional Practice Framework).
1.18 Review of Related Literature

This involved the review and critique of previous research and writings as well as current issues on the topic. This was done in order to establish the current state of knowledge and avoid replication of studies done in the past (Thomas 2004). The review also provided insights into methodological as well as substantive issues, and the researcher was able to learn from past studies (Gill and Johnson (2002). The review also enabled the researcher to identify a gap in existing knowledge, which was filled by the present research. The literature reviewed is discussed in more detail in Chapter 2 of this study.

1.19 Research Methodology

The qualitative approach was adopted for this study. This method was chosen because of its ability to expose the situation under review as it exists and the reasons why it so exists. It was also possible to capture the feelings, perceptions and opinions of the participants.(Denzin and Lincoln 1994; Merriam 1998; Patton 2002). The research is a multiple case study of three parastatals. Being a case study, the topic was studied in its real-life context.(Yin 1984; Denscombe 2007). Focus group discussions, interviews, and questionnaires with open ended questionnaires were used to collect data from participants. The data were then analysed to extract meaning from it. A detailed discussion of the methodology employed in the study is contained in Chapter 3 of this report.

1.20 Definition of Terms

The definitions appearing first under each of the terms were taken from the IIA glossary (Institute of Internal Auditors 2004). In this study, the words and terms assume the same definitions as those given by the IIA. Relevant definitions taken from other sources are also
included in order to give a more complete picture regarding how other authorities and scholars interpret the terms.

**Add value** – The internal audit activity adds value to the organization and its stakeholders when it provides objective and relevant assurance, and contributes to the effectiveness and efficiency of governance, risk management, and control processes. (IIA 2004)

**Assurance services**

An objective examination of evidence for the purpose of providing an independent assessment of risk management, control or governance processes for the organisation. Examples may include financial, performance, compliance, system security and due diligence engagements. (IIA 2004)

AICPA definition - Services which improve the quality of information, or its context, for decision-makers

**Board**

A board is an organization’s governing body, such as a board of directors, supervisory board, head of an agency or legislative body, board of governors or trustees of a non-profit organization, or any other designated body of the organization, including the audit committee to whom the chief audit executive may functionally report. (IIA 2004)

**Charter** – The charter of the internal audit function is a formal written document that defines the activity’s purpose, authority and responsibility. The charter should (a) establish the internal auditor’s position within the organisation (b) authorise access to records, personnel and physical properties relevant to the performance of the engagement and (c) define the scope of internal audit activities. (IIA 2004)
**Conflict of Interests** – Any relationship that is or appears not to be in the best interests of the organisation. A conflict of interests would prejudice an individual’s ability to perform his or her duties and responsibilities objectively.

Pickett (2003) – A situation in which an internal auditor, who is in a position of trust, has competing professional or personal interests.

MacDonald, McDonald and Norman (2002) – A situation in which a person has a private or personal interest sufficient to appear to influence the objective exercise of his or her official duties as, say, a public official, an employee or a professional.

**Consulting Services**

Advisory and related client service activities, the nature and scope of which are agreed with the client and which are intended to add value and improve an organisation’s governance, risk management and control processes without the internal auditor assuming management responsibility. Examples include counsel, advice, facilitation and training.

AICPA definition - Consulting Services provided by CPA firms in addition to the traditional audit, accounting, and tax services (e.g. systems work, production planning). The AICPA CS Team provides educational and technical guidance to firms and private sector employees who offer consulting services to clients.

**Governance**

Any combination of processes and structures implemented by the board in order to inform, direct, manage and monitor the activities of the organisation toward the achievement of its objectives.
Financial Reporting Council (2010) - The purpose of corporate governance is to facilitate effective, entrepreneurial and prudent management that can deliver the long-term success of the company. Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders’ role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board’s actions are subject to laws, regulations and the shareholders in general meeting

Impairments

Impairments to individual objectivity and organisational independence may include personal conflicts of interest, scope limitation, restrictions on access to records, personnel, properties and resource limitations (funding).

Objectivity

An unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgement on audit matters to others.

Risk

The possibility of an event occurring that will have an impact on the achievement of objectives. Risk is measured in terms of impact and likelihood.

Risk management
A process to identify, assess, manage and control potential events or situations to provide reasonable assurance regarding the achievement of the organisation’s objectives.

AICPA definition - Risk Advisory Services - Services designed to identify, assess and manage risks of an entity and measure and monitor the risk management strategies implemented by that entity.

COSO (2004) - Enterprise risk management is a process, effected by an entity’s board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives

Standard

A professional pronouncement promulgated by the Internal Auditing Standards Board that delineates the requirements for performing a broad range of internal audit activities, and for evaluating internal audit performance.

ICAEW - Auditing Standards - Auditing standards (SASs) are the basic principles and essential procedures with which auditors are required to comply with in the conduct of any audit of financial statements.

1.21 Ethical considerations

The principles espoused in the Belmont report (1979), Zimmerman (1997) and the British Psychological Society’s Code of Human Research Ethics (2010) will be observed during the conduct of the research, and these are: informed consent, confidentiality, respect for persons, beneficence, justice, and respect for communities, and these are discussed below.
1.21.1 Respect for persons.

This principle includes two ethical convictions. The first one is that persons should treated as autonomous individuals capable of making their own decisions. Respect is shown when individual opinions and choices are encouraged and accepted. Lack of respect is shown when individuals are denied the opportunity to make informed decisions. The second ethical conviction is that persons with diminished autonomy are entitled to protection. It acknowledges that not all people have the capacity for self determination. Capacity may be lost due to illness or mental disability, and in such cases, sufficient protection should be provided, so that they are not exploited.

Informed consent

Application of the principle of respect for persons requires that the participants give informed consent. The process of informed consent involves three elements, namely, information, comprehension and voluntariness. The information element requires that participants be given full information about the research, their involvement, any risks or benefits and the fact that they can withdraw from the research at any time, and ask that all their data be destroyed. The comprehension element requires that information be provided to participants in a language and at a level that they can understand. Voluntariness requires that the informed consent process be free from coercion (threat or intention to harm a person), undue influence (e.g. an offer of an excessive or unwarranted reward in order to gain compliance), and unjustifiable pressures. (e.g. when a person in authority urges a certain course of action)
1.21.2 Beneficence

This requires a commitment to ensuring the well being of participants. It is an obligation and is based on two rules, i.e. (1) do no harm and (2) maximise possible benefits and minimise possible harms.

Assessment of risks and benefits

The application of this principle requires the assessment of risks and benefits associated with the research. Risk is the possibility that harm may occur, and benefit is something of positive value related to the well being. The research should be justifiable on the basis of a favourable risk/benefit assessment.

1.21.3 Justice

This revolves on who should receive benefits and bear the burdens, and requires that the formulations on which benefits and burdens are distributed should be fair.

Selection of participants.

Application of this principle requires that fairness should be exercised in the selection of participants. The procedures and outcomes in the selection of participants should be transparent, and no individuals or groups should be favoured.

1.21.4 Respect for the community

This involves the obligation to respect the values and interests of the community in which the research is carried out and whenever possible to protect the community from harm.
The above principles were observed, and the objectives of the research, the methods used to obtain information and how this information will be used were explained to the participants. The researcher gave the participant his contact details, i.e. telephone and cell phone numbers, as well as the office where he could be contacted if the participants had any questions, and committed himself to answer any of these questions within a day at most. He made it clear that participants were free to withdraw from the research at any time without any repercussions. The researcher also explained that confidential information obtained from the participants would be held in the strictest confidence and would not be passed on to third parties, and information supplied by the participants would be anonymised so that it cannot be traced back to source.

The observation of ethics throughout the research is illustrated in Figure 1.2:
Fig 1.2 Ethical issues at different stages of the research


1.22 Organisation of the Thesis

The thesis is divided into the following chapters:

Chapter 1: Background to the study. This chapter provides the background information, which led the researcher to identify the problem under investigation. The statement of the problem, purpose of the study, research questions, research objectives, significance of the
problem, assumptions of the study, delimitations of the study, limitations of the study are discussed and definitions of key terms given.

**Chapter 2: Review of related literature.** This chapter covers the literature which was reviewed, which is discussed under the following headings: Organisational independence, Approval of internal audit budget, Inputs into internal audit annual work plans, Hiring and firing of the Chief Audit Executive (CAE), Reporting lines for the CAE, The use of internal audit as a training ground for future managers, Conflict of roles between consulting and assurance, as well as risk management and assurance, Relations with the audit committee, Skills, experience and training of audit committee members, Relations with external auditors, and Individual objectivity.

**Chapter 3: Research methodology.** The chapter starts by explaining the differences between qualitative and quantitative research methods, before identifying the research philosophy (interpretivism), which informed the study as well as the research method (qualitative) selected. The research design, namely, the case study is discussed. This is followed by discussion of the population, the sample and the sampling method. Purposive sampling is discussed. Data collection, research instruments, i.e. questionnaires, interviews and focus group discussions follow.

**Chapter 4: Data analysis, presentation and discussion.** The research findings are presented and discussed in this chapter

**Chapter 5: Summary conclusion and recommendations.** The findings of the study are summarised, conclusions drawn and appropriate recommendations made.
1.23 Summary

This chapter provided background information to the study. It started with a brief discussion of the governance structures of the modern corporation, and the checks and balances normally employed to ensure transparency and good governance. The meaning, purpose and importance of internal auditing, as well as the differences between internal and external audit were explained. The terms internal auditing, independence and objectivity were also explained. A brief history of parastatals was then given, highlighting the move towards commercialisation and privatisation of the majority of these entities, which processes could be assisted by independent internal audit functions. This was followed by the statement of the problem, the purpose of the study, research questions, research objectives, significance of the study, limitations of the study and delimitation of the study. Ethical considerations were discussed next, and this was followed by the proposed organisation of the thesis, the last item on the chapter. The next chapter looks at the related literature that was reviewed in order to determine the state of knowledge, learn from previous studies and identify the gap in knowledge to be filled by this study.
CHAPTER 2

Review of Related Literature

2.0 Introduction

This chapter deals with the review and critique of literature to determine work done by previous researchers and writers as well as current topical issues on the question of internal auditor independence and objectivity. The review of related literature provides a solid foundation for the research, establishes current state of knowledge and facilitates avoidance of unintentional replication of previous studies (Thomas 2004). It also provides an insight into both substantive and methodological issues on the topic, and thus gives an advance appreciation of the problems and possibilities that are likely to arise during the study (Gill and Johnson 2002). The review also helps to determine the gap in knowledge to be filled by the study and as Gill and Johnson (2002:25) put it, “will help to refine the focus and enable a researcher to set conceptual boundaries on what is relevant.” The review of related literature continued throughout the duration of the study, to enable the researcher to keep abreast of developments in the area of interest.

Important outcomes of a well conducted review of literature are succinctly summarised by Gill and Johnson (2002:25) as follows:

- It helps describe a topic of interest and refine either research questions or directions in which to look;
- It presents a clear description and evaluation of the theories and concepts that have informed the research into the topic of interest;
• It clarifies the relationship to previous research and highlights where new research may contribute by identifying research possibilities which have been overlooked so far in the literature;
• It provides insights into the topic of interest that are both methodological and substantive;
• It demonstrates powers of critical analysis, for instance, exposing taken for granted assumptions underpinning previous research and identifying the possibilities of replacing them with alternative assumptions, and
• It justifies any new research through a coherent critique of what has gone before and demonstrates why new research is both timely and important.

The review of literature in the current study was informed by the guidance stated in the previous paragraphs. Because of the nature of the study, extensive reference will be made to the IIA standards, ethics, and practice guidelines, as the IIA is the global professional body for the internal auditing profession. The study was informed by the agency theory, which is discussed in the next paragraph.

2.1 Theoretical Framework

The study was informed by the agency theory and used the IIA Standards and Ethics and Practice Advisories (the best practices in the profession) as benchmarks against which prevailing conditions were compared.

The agency theory states that a firm consists of a nexus of contracts between the owners of resources, who are the principals and the managers who are the agents, charged with the responsibility of using and controlling the resources (Jansen and Meckling, 1976). Such a situation subsists in modern corporations, where shareholders (owners) provide the capital, but are not involved in the day-to-day running of the corporation. This is left to managers
Agents will therefore have more information than principals. The agency theory describes the difficulties that arise from this situation of incomplete and asymmetric information and measures taken by the principals to ensure that their interests are being served (Eisenhardt 1989). The theory assumes that principals and agents act rationally, and will use the contracting process to maximise their utility, interests or wealth. Agents have more information than the principals, and this information asymmetry adversely affects the principal’s ability to monitor if his interests are being properly served. Because agents have self-seeking motives, they are likely to engage in opportunistic behaviour and act against the interests of the principals, thereby enriching themselves at the expense of the principal, by, for example partaking in high levels of perquisite consumption (Adams 1994). Scapens (1985) refers to this as a moral hazard. Moral hazard, also known as hidden action is central to the agency theory. (Hendrikse 2003). Additionally, the principal does not have access to all available information when a decision is made by the manager, and is unable to ascertain if the manager’s decision is in the best interests of the firm. This is termed adverse selection.

To manage the information asymmetry and the moral hazard, and align the agents’ behaviour with their interests, the principals put mechanisms to ensure that the agent acts in the best interests of the firm. They will incur monitoring costs, and examples of these are the board of directors, audit committees, internal and external audit, as well as the annual financial reports.

Agents on their part also incur bonding costs to signal to principals that they are acting in their best interests of the firm. Wallace (1980) suggests that examples of bonding costs are expenditure on audit committees, non-executive directors and internal auditors. Sherer and Kent (1983) consider internal audit to be a bonding cost, and a feedback mechanism which enables management to remedy any weaknesses before they have a significant effect on the overall internal control system and financial position of the organisation. As shown above
different scholars classify internal audit differently (i.e. whether it is a monitoring or bonding cost) but it is clear that it is a cost that is incurred to ensure that managers act in the interests of the firm, and is therefore typically a monitoring cost.

Adams (1994) and Paape (2007) used the agency theory to show the internal audit as an important function which assists management in the evaluation of information asymmetry between principal and agent. The theory can also be used to explain the need for internal audit in organisations, its characteristics, size and scope of activities. (Adams 1994). Having discussed the theoretical framework, some of the major previous studies on the topic under review are given below.

2.2 A Summary Of Major Previous Studies

Internal audit in general and independence and objectivity in particular have attracted a number of researchers. These include J Mutchler (2003) and J Steward and N Sabramaniam (2010) who carried out reviews of literature on internal audit independence and objectivity, and identified areas of further research. Sarens and de Beelde (2006) explored the relationship between management and internal audit and concluded that when internal audit primarily support management, it is perceived to lack objectivity and its relationship with the audit committee is weak.

Studies on role conflict as a result of providing both assurance and consulting services include: De Zoort, Houston and Reisch (2000), in the USA; Ahlawat and Lowe (2004) in the USA; Van Peursem (2005) in New Zealand and Selim, Woodward and Allegrini (2009) in the United Kingdom (UK) and Ireland.

The present study made an in-depth examination of the independence and objectivity of internal auditors in Zimbabwe, using a multiple case study strategy. It examined, not only the state of affairs, but also explore the reasons behind this state of affairs and elicit the views and perceptions of the internal auditors and other interested parties on this very important issue. The study will add to the existing body of knowledge on this issue, and will break new ground, as the researcher did not come across any previous studies of this topic, covering the state of affairs in Zimbabwe.

It is also pertinent to note that the IIA commissioned the Common Body of Knowledge (CBOK) in 2006 to determine the state of the art of internal auditing in view of the emerging changes in the business environment. Questionnaires were sent to members of the IIA throughout the world. This resulted in reports by Cooper, Leung and Wong (2006) on the Asia Pacific region; Hass, Abdolhammadi and Burnaby (2006) on the Americas; and Allegrini, D’Onza, Paape and Sarens (2006) on Europe. The global summary compiled by Burnaby and Hass (2007) indicated that most members were using the standards and believed that they were adequate. On the code of ethics, all those who responded confirmed compliance, and indicated that breaches were dealt with by various bodies, like the ethics committee, or disciplinary committees. Audit charters were in existence in the majority of cases, and most Audit Executives confirmed oversight by audit committees, as well as adequate and regular meetings with the audit committee. It is interesting to note that at that time the Zimbabwe chapter of the IIA had 557 members and only three usable responses were received from Zimbabwe by the research team. Previous surveys had been made in the
years 1972, 1985, 1991, and 1999. This literature will be discussed below under the broad headings of Organisational independence and Individual objectivity.

The majority of these studies were conducted in the developed countries. It is therefore necessary to find out what is happening in the developing world in general and Zimbabwe in particular. In this respect the study will break new ground. In the next section, independence and objectivity are discussed.

2.3 Independence and objectivity

The definition of the terms independence and objectivity, as given by the IIA were given in the paragraph 1.20 above. The International Organisation of Supreme Audit Institutions (INTOSAI) page 3 gives the following definition:

Independence can be generally defined as freedom from dependence on or influence or control by, another person, organization, or state. Internal auditors work for and primarily report to, the audited entity. For internal auditors, independence is the freedom from conditions that threaten the ability of the internal audit activity or the chief audit executive (CAE) to carry out internal audit responsibilities in an unbiased manner. Independence permits internal auditors to render the impartial and unbiased judgements essential to the proper conduct of engagements.

INTOSAI emphasizes that independence and objectivity are vital in ensuring that stakeholders view the audit work performed and the results as credible, factual and unbiased, therefore, there should be no interference or pressures from the organisation or the area being audited. This ties in very well with the IIA definition, showing that independence is important in both the private and the public sectors.

As independence and objectivity are pervasive and critical to the whole of the auditing profession, be it internal or external, it is interesting to look how these concepts have been dealt with in the major public accounting bodies. Bearing in mind that these bodies have been in existence much longer than the internal auditing bodies, valuable lessons can be learnt...
regarding independence and objectivity, and the related identification of threats and impairments, as well as the safeguards to eliminate or reduce such impairments and threats to acceptable levels. The provisions of the International Federation of Accountants (IFAC) which is the global body for the accounting profession are examined first.

2.3.1 The International Federation of Accountants (IFAC)

The International Ethics Standards Board for Accountants of the International Federation of Accountants has issued a code, entitled, ‘Handbook of the Code of Ethics for Professionals Accountants’, in which issues of independence and objectivity are dealt with in detail (IESBA 2012).

Objectivity and independence

Section 120, which deals with objectivity states that the principle of objectivity imposes an obligation on all professional accountants not to compromise their professional judgement because of bias, conflict of interests or the undue influence of others. It goes on to state that a professional accountant shall not perform a professional service if a circumstance or relationship biases or unduly influences the accountant’s professional judgement with respect to that service. The public accountant shall determine whether there are threats to compliance with fundamental principles of objectivity resulting from having interests in or relationships with, a client or its directors, officers or employees. (IESBA 2012).

A professional accountant in public practice is also required to be independent of the client. Independence of mind and in appearance is necessary to enable the accountant to express a conclusion and be seen to express a conclusion, without bias, conflict of interest or undue influence of others. The professional accountant in public practice is required to evaluate the
significance of any threats and apply safeguards to eliminate them or reduce them to an acceptable level. Examples of such safeguards are given as follows:

- Withdrawing from the engagement;
- Supervisory procedures;
- Termination of the financial of business relationships giving rise to the threat;
- Discussing the issue with high levels of the management within the firm; and
- Discussing the issue with those charged with governance of the client.

If safeguards cannot eliminate or reduce the threat to an acceptable level, the profession accountant is required to decline or terminate the engagement. (IESBA 2012).

The framework defines independence as follows:

Independence comprises:

a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgement, thereby allowing an individual to act with integrity, and exercise objectivity and professional scepticism. (IESBA 2012)

b) Independence in appearance – the avoidance of facts and circumstances that are so significant a reasonable and informed third party, would be likely to conclude, weighing all the specific facts and circumstances, that a firm’s or a member of the audit team’s integrity, objectivity or professional skepticism has been compromised. (IESBA 2012)

A conceptual framework approach to independence, which is described in detail in the code of ethics, is used in achieving and maintaining independence. The framework is applied by accountant to:
• Identify threats to independence;
• Evaluate the significance of threats identified; and
• Apply safeguards, when necessary, to eliminate the threats or reduce them to an acceptable level. (IESBA 2012)

The framework encourages regular communication between the firm and those charged with the governance of the client to enable them to:

• Consider the firm’s judgement in identifying and evaluating threats to independence;
• Consider appropriateness of the safeguards applied to eliminate or reduce them; and
• Take appropriate action. (IESBA 2012)

The framework further goes on to describe some specific circumstances and relationships that create or may create threats to independence. These include:

• Having a financial interest in an audit client;
• A loan, or guarantee of a loan, to a member of the audit team, or a member of that individual’s immediate family or the firm from an audit client that is a bank or similar institution;
• A close business relationship between a firm or a member of the audit team or a member of that individual’s family, and the audit client or its management;
• Family and personal relationships between a member of the audit team and a director or officer or certain employees of the audit client may create self-interest, familiarity or intimidation threats;
• Employment with an audit client, e.g. in preparation of the client’s accounting records may create familiarity and intimidation threats;
• Lending of staff by a firm to an audit client may create a self-review threat;
Self interest, self review and familiarity threats may be created if a member of the audit team has recently served as a director, officer or employee of the audit client;

The provision of non audit services to a client may create self review, self interest and advocacy threats;

Accepting gifts or hospitality from an audit client may create self interest and familiarity threat; and

Actual or threatened litigation between the firm or a member of the audit team and the client, create self interest and intimidation threats. (IESBA 2012)

Threats are divided into the following categories: self interest, self review, advocacy, familiarity, and intimidation, and these are briefly described below.

**Self interest threat** – The threat that a financial or other interest will inappropriately influence the professional accountant’s judgement or behaviour. Examples are:

- A firm having undue dependence on total fees from one client;
- A member of the audit team entering into employment negotiation with the audit client;
- A member of the assurance team having a direct financial interest in the assurance client; and
- A member of the audit team having a close business relationship with an audit client. (IESBA 2012)

**Self review threat** – the threat that a professional accountant will not appropriately evaluate the results of a previous judgement made or service performed by the professional accountant, or by another individual within the professional accountants’ employing firm or organisation,
on which the accountant will rely when forming a judgement as part of providing a current service. Examples are:

- A firm issuing an assurance report on the effectiveness of the operation of financial systems after designing and implementing the systems;
- A member of the assurance team being or having recently been a director or officer of the client; and
- A firm having prepared the original data used to generate records that are the subject matter of the assurance engagement. (IESBA 2012)

**Advocacy threat** – the threat that the professional accountant will promote a client’s or employer’s position to the point that the professional accountants objectivity is compromised. Examples are:

- A firm promoting shares in an audit client; and
- A professional accountant acting as an advocate on behalf of an audit client in litigation or disputes with third parties. (IESBA 2012)

**Familiarity threat** – the threat that due to a long or close relationship with a client, or employer, a professional accountant will be too sympathetic to their interest or too accepting of their work. Examples are:

- A member of the engagement team having a close or immediate family member who is a director or officer of a client;
- A member of an engagement team having a close or immediate family member who is an employee of the client who is in a position to exert significant influence over the subject matter of the engagement; and
• A professional accountant accepting gifts or preferential treatment from a client unless the value is trivial or inconsequential. (IESBA 2012)

**Intimidation threat** – the threat that a professional accountant will be deterred from acting objectively because of actual or perceived pressures including attempts to exercise undue influence over the professional accountant. Examples are:

• A firm being threatened with dismissal from a client engagement;
• A firm being threatened with litigation by a client; and
• A professional accountant being pressured to agree with the judgement of a client employee because the employee has more expertise on the matter in question. (IESBA 2012)

Safeguards that may eliminate or reduce threats to an acceptable level fall into two categories:

• Safeguards created by the profession, legislation or regulation; and
• Safeguards in the work environment. (IESBA 2012)

The conceptual framework is principle-based, and gives a comprehensive guide to professional accountants on issues of independence and objectivity. The next section deals with the standards of the largest body of public accountants in the United States of America (USA), the American Institute of Certified Public Accountants (AICPA).

**2.3.2 The American Institute Of Certified Public Accountants (AICPA) Independence Standards**

The independence standards of the American Institute of Certified Public Accountants are dealt with under the a conceptual framework and detailed rules.
The Conceptual Framework for AICPA Independence Standards

The AICPA uses a conceptual framework to develop standards of independence for its members (AICPA 2013). Detailed rules regarding independence and impairments and threats to independence are contained in the Code of Professional Conduct. The conceptual framework describes the risk-based approach to analyzing independence matters that is used by the Professional Ethics Executive Committee (PEEC) of the AICPA when it develops independence standards. Under that approach, a member’s relationship with a client is evaluated to determine whether it poses an unacceptable risk to the member’s independence. Risk is unacceptable if the relationship would compromise (or would be perceived as compromising by an informed third party having knowledge of all relevant information) the member’s professional judgment when rendering an attest service to the client. Key to that evaluation is identifying and assessing the extent to which a threat to the member’s independence exists and, if it does, whether it would be reasonable to expect that the threat would compromise the member’s professional judgment and, if so, whether it can be effectively mitigated or eliminated. Under the risk-based approach, steps are taken to prevent circumstances that threaten independence from compromising the professional judgments required in the performance of an attest engagement. (AICPA 2013)

The conceptual framework is used by members when making decisions on independence matters that are not explicitly addressed by the Code of Professional Conduct. It is provided that under no circumstances, however, may the framework be used to overcome prohibitions or requirements contained in the independence interpretations and rulings. (AICPA 2013)

The risk-based approach entails evaluating the risk that the member would not be independent or would be perceived by a reasonable and informed third party having knowledge of all relevant information as not being independent. That risk must be reduced to an acceptable level to conclude that a member is independent under the concepts in the
framework. Risk is at an acceptable level when threats are at an acceptable level, either because of the types of threats and their potential effect, or because safeguards have sufficiently mitigated or eliminated the threats. Threats are at an acceptable level when it is not reasonable to expect that the threat would compromise professional judgment.

The risk-based approach involves the following steps. (AICPA 2013)

- Identifying and evaluating threats to independence—Identify and evaluate threats, both individually and in the aggregate, because threats can have a cumulative effect on a member’s independence. Where threats are identified but, due to the types of threats and their potential effects, such threats are considered to be at an acceptable level (that is, it is not reasonable to expect that the threats would compromise professional judgment), the consideration of safeguards is not required. If identified threats are not considered to be at an acceptable level, other safeguards should be considered.

- Determining whether safeguards already eliminate or sufficiently mitigate identified threats and whether threats that have not yet been mitigated can be eliminated or sufficiently mitigated by safeguards—Different safeguards can mitigate or eliminate different types of threats, and one safeguard can mitigate or eliminate several types of threats simultaneously. When threats are sufficiently mitigated by safeguards, the threats’ potential to compromise professional judgment is reduced to an acceptable level. A threat has been sufficiently mitigated by safeguards if, after application of the safeguards, it is not reasonable to expect that the threat would compromise professional judgment.

- If no safeguards are available to eliminate an unacceptable threat or reduce it to an acceptable level, independence would be considered impaired.
The framework gives the following definitions:

**Independence** is defined as:

- **Independence of mind**—The state of mind that permits the performance of an attest service without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism. (AICPA 2013)

- **Independence in appearance**—The avoidance of circumstances that would cause a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, to reasonably conclude that the integrity, objectivity, or professional skepticism of a firm or a member of the attest engagement team had been compromised. (AICPA 2013)

This definition is used as part of the risk-based approach to analyze independence. It reflects the longstanding professional requirement that members who provide services to entities for which independence is required be independent both in fact and in appearance. The state of mind of a member who is independent “in fact” assists the member in performing an attest engagement in an objective manner. Accordingly, independence of mind reflects the longstanding requirement that members be independent in fact. (AICPA 2013)

**Impair**—For purposes of this framework, impair means to effectively extinguish (independence). When a member’s independence is impaired, the member is not independent. (AICPA 2013)

**Threats**—Threats to independence are circumstances that could impair independence. Whether independence is impaired depends on the nature of the threat, whether it would be reasonable to expect that the threat would compromise the member’s professional judgment
and, if so, the specific safeguards applied to reduce or eliminate the threat, and the
effectiveness of those safeguards. (AICPA 2013)

Many different circumstances (or combinations of circumstances) can create threats to
independence. It is impossible to identify every situation that creates a threat. However, seven
broad categories of threats should always be evaluated when threats to independence are
being identified and assessed. They are self-review, advocacy, adverse interest, familiarity,
undue influence, financial self-interest, and management participation threats. The following
paragraphs define and provide examples, which are not all-inclusive, of each of these threat
categories. Some of these examples are the subject of independence interpretations and
rulings contained in the Code of Professional Conduct.

*Self-review threat*—Members reviewing as part of an attest engagement evidence that results
from their own, or their firm’s, nonattest work such as, preparing source documents used to
generate the client’s financial statements (AICPA 2013)

*Advocacy threat*—Actions promoting an attest client’s interests or position. e.g.

- Promoting the client’s securities as part of an initial public offering and
- Representing a client in a U.S. tax court (AICPA 2013)

*Adverse interest threat*—Actions or interests between the member and the client that are in
opposition, such as, commencing, or the expressed intention to commence litigation by either
the client or the member against the other. (AICPA 2013)

*Familiarity threat*—Members having a close or longstanding relationship with an attest client
or knowing individuals or entities (including by reputation) who performed nonattest services
for the client. The following are examples:
- A member of the attest engagement team whose spouse is in a key position at the client, such as the client’s chief executive officer;

- A partner of the firm who has provided the client with attest services for a prolonged period;

- A member who performs insufficient audit procedures when reviewing the results of a nonattest service because the service was performed by the member’s firm;

- A member of the firm having recently been a director or officer of the client; and

- A member of the attest engagement team whose close friend is in a key position at the client. (AICPA 2013)

**Undue influence threat**—Attempts by an attest client’s management or other interested parties to coerce the member or exercise excessive influence over the member. Examples are:

- A threat to replace the member or the member’s firm over a disagreement with client management on the application of an accounting principle;

- Pressure from the client to reduce necessary audit procedures for the purpose of reducing audit fees; and

- A gift from the client to the member that is other than clearly insignificant to the member. (AICPA 2013)

**Financial self-interest threat**—Potential benefit to a member from a financial interest in, or from some other financial relationship with an attest client. The following are examples:

- Having a direct financial interest or material indirect financial interest in the client
• Having a loan from the client, from an officer or director of the client, or from an individual who owns ten percent or more of the client’s outstanding equity securities

• Excessive reliance on revenue from a single attest client

• Having a material joint venture or other material joint business arrangement with the client (AICPA 2013)

Management participation threat—Taking on the role of client management or otherwise performing management functions on behalf of an attest client. Here are some examples:

• Serving as an officer or director of the client;

• Establishing and maintaining internal controls for the client; and

• Hiring, supervising, or terminating the client’s employees. (AICPA 2013)

Safeguards are defined as - Controls that eliminate or reduce threats to independence. Safeguards range from partial to complete prohibitions of the threatening circumstance to procedures that counteract the potential influence of a threat. The nature and extent of the safeguards to be applied depend on many factors, including the size of the firm and whether the client is a public interest entity. To be effective, safeguards should eliminate the threat or reduce to an acceptable level the threat’s potential to impair independence.

The framework states that the effectiveness of a safeguard depends on many factors, including those listed here:

• The facts and circumstances specific to a particular situation;

• The proper identification of threats;

• Whether the safeguard is suitably designed to meet its objectives ;

• The party or parties that will be subject to the safeguard;
- How the safeguard is applied;
- The consistency with which the safeguard is applied;
- Who applies the safeguard. (AICPA 2013)

Safeguards are divided into three broad categories, and the relative importance of a safeguard depends on its appropriateness in light of the facts and circumstances.

- Safeguards created by the profession, legislation, or regulation;
- Safeguards implemented by the attest client;
- Safeguards implemented by the firm, including policies and procedures to implement professional and regulatory requirements. (AICPA 2013)

Examples of various safeguards within each category are presented in the following paragraphs:

**Examples of safeguards created by the profession, legislation, or regulation**

- Education and training requirements on independence and ethics rules for new professionals;
- Continuing education requirements on independence and ethics;
- Professional standards and monitoring and disciplinary processes;
- External review of a firm’s quality control system;
- Legislation governing the independence requirements of the firm;
- Competency and experience requirements for professional licensure. (AICPA 2013)

**Examples of safeguards implemented by the attest client that would operate in combination with other safeguards**
• The attest client has personnel with suitable skills, knowledge, and/or experience who make managerial decisions with respect to the delivery of nonattest services by the member to the attest client.

• A tone at the top that emphasizes the attest client’s commitment to fair financial reporting.

• Policies and procedures that are designed to achieve fair financial reporting.

• A governance structure, such as an active audit committee, that is designed to ensure appropriate decision making, oversight, and communications regarding a firm’s services.

• Policies that dictate the types of services that the entity can hire the audit firm to provide without causing the firm’s independence to be considered impaired. (AICPA 2013)

Examples of safeguards implemented by the firm

• Firm leadership that stresses the importance of independence and the expectation that members of attest engagement teams will act in the public interest.

• Policies and procedures that are designed to implement and monitor quality control in attest engagements.

• Documented independence policies regarding the identification of threats to independence, the evaluation of the significance of those threats, and the identification and application of safeguards that can eliminate the threats or reduce them to an acceptable level.

• Internal policies and procedures that are designed to monitor compliance with the firm’s independence policies and procedures.
• Policies and procedures that are designed to identify interests or relationships between the firm or its partners and professional staff and attest clients.

• The use of different partners and engagement teams that have separate reporting lines in the delivery of permitted nonattest services to an attest client, particularly when the separation between reporting lines is significant.

• Training on and timely communication of a firm’s policies and procedures, and any changes to them, for all partners and professional staff.

• Policies and procedures that are designed to monitor the firm or partner’s reliance on revenue from a single client and, if necessary, cause action to be taken to address excessive reliance.

• Designating someone from senior management as the person who is responsible for overseeing the adequate functioning of the firm’s quality control system.

• A means of informing partners and professional staff of attest clients and related entities from which they must be independent.

• A disciplinary mechanism that is designed to promote compliance with policies and procedures.

• Policies and procedures that are designed to empower staff to communicate to senior members of the firm any engagement issues that concern them without fear of retribution.

• Policies and procedures relating to independence communications with audit committees or others charged with client governance.

• Discussing independence issues with the audit committee or others responsible for the client’s governance.
• Disclosures to the audit committee (or others responsible for the client’s governance) regarding the nature of the services that are or will be provided and the extent of the fees charged or to be charged.

• The involvement of another professional accountant who (1) reviews the work that is done for an attest client or (2) otherwise advises the attest engagement team (This individual could be someone from outside the firm or someone from within the firm who is not otherwise associated with the attest engagement.).

• Consultation on engagement issues with an interested third party, such as a committee of independent directors, a professional regulatory body, or another professional accountant.

• Rotation of senior personnel who are part of the attest engagement team.

• Policies and procedures that are designed to ensure that members of the attest engagement team do not make or assume responsibility for management decisions for the attest client.

• The involvement of another firm to perform part of the attest engagement

• The involvement of another firm to reperform a nonattest service to the extent necessary to enable it to take responsibility for that service

• The removal of an individual from an attest engagement team when that individual’s financial interests or relationships pose a threat to independence.

• A consultation function that is staffed with experts in accounting, auditing, independence, and reporting matters who can help attest engagement teams (1) assess issues when guidance is unclear, or when the issues are highly technical or require a great deal of judgment and (2) resist undue pressure from a client when the engagement team disagrees with the client about such issues.
• Client acceptance and continuation policies that are designed to prevent association with clients that pose an unacceptable threat to the member’s independence.

• Policies that preclude audit partners from being directly compensated for selling nonattest services to the audit client (AICPA 2013)

Rules

The following is a summary of some of the rules and interpretations of the rules, contained in the standards, pertaining to independence of public accountants and auditors:

Rule 101 – independence (AICPA 2013)

A member in public practice shall be independent in the performance of professional services as required by standards promulgated by bodies designated by Council.

The interpretation of this rule is given as follows:

Interpretations under Rule 101

Independence

In performing an attest engagement, a member should consult the rules of his or her state board of accountancy, his or her state CPA society, the Public Company Accounting Oversight Board and the U.S. Securities and Exchange Commission (SEC) if the member's report will be filed with the SEC, the U.S. Department of Labour (DOL) if the member's report will be filed with the DOL, the Government Accountability Office (GAO) if law, regulation, agreement, policy or contract requires the member's report to be filed under GAO regulations, and any organization that issues or enforces standards of independence that would apply to the member's engagement. Such organizations may have independence
requirements or rulings that differ from (e.g., may be more restrictive than) those of the AICPA. (AICPA 2013)

The interpretation goes on to state that independence is impaired if:

During the period of an engagement, the member

- has committed to acquire any director or material indirect financial interest in the client;
- had any loan to or from the client, any officer or director of the client or any individual owning ten percent or more of the client’s outstanding equity securities or other ownership interests;
- The partner, or his or her immediate family or any group of such persons held more than five percent of the entity’s outstanding equity securities;
- the partner of professional employee of the firm was simultaneously associated with the client as a (1) director officer or employee in any capacity equivalent to that of a member of management (2) promoter, underwriter or voting trustee (3) trustee for an pension or profit-sharing trust of the client. (AICPA 2013)

**Rule 102 Integrity and objectivity states that:**

In the performance of any professional service, a member shall maintain objectivity and integrity, shall be free of conflicts of interest, and shall not knowingly misrepresent facts or subordinate his or her judgment to others. A member misrepresents in the preparation of financial statements if: (AICPA 2013)

- he makes or permits or directs another to make false and misleading entries in an entity’s financial statements or records or
- fails to correct an entity’s financial statements or records that are materially false and misleading when he or she has the authority to record an entry or
• signs or permits or directs another to sign a document containing materially false and misleading information (AICPA 2013)

Rule 102-2 – Conflicts of interests

Conflicts of interests may occur if a member performs a professional service for a client or employer and the member or his or her firm has a relationship with another person, entity, product or service that could, in the member’s professional judgement, be viewed by the client, employee, or other appropriate parties as impairing the member’s objectivity. (AICPA 2013)

If the member believes the professional service can be performed with objectivity and the relationship is disclosed and consent obtained from such client, employer or other appropriate parties, prohibition of performance of the service shall not apply. The following examples are given:

• in relation to a personal financial planning engagement, a member plans to suggest that the client invests in a business in which he or she has a financial interest;
• A member serves on a city’s board of the tax appeals, which considers matters involving several of the member’s tax clients;
• A member has been approached to provide services in connection with the purchase of real estate from a client of the member’s firm. (AICPA 2013)

Rule 102-4 – Subordination of judgement by a member

Prohibits a member from knowingly misrepresenting facts or subordinating his or her professional judgement when performing professional services. If a member and his supervisor have a disagreement relating to the preparation of financial statements, or recording of transactions, the member should (1) research and seek advice to determine if what the supervisor suggests is an acceptable alternative and if not (2) present his concerns to
an appropriate higher level within the organisation. If, after this, he or she concludes that appropriate action was not taken, he or she should consider his or her continued relationship with the employer, and any obligations to report the irregularity to third parties, for example, regulatory authorities. (AICPA 2013)

A comparison of the pronouncements to the two bodies on independence reveals striking similarities. In their definitions of independence both recognise the two aspects of independence, namely, independence in fact (real or actual independence) and independence in appearance (perceived independence). There is a slight difference in the categorisation of threats, in that whereas the IFAC has five, the AICPA has seven. The AICPA categorisation is more elaborate, but this does not mean that the IFAC categorisation is deficient. The threat identified by AICPA as financial self interest is included in self interest in the IFAC list. Similarly, the threat identified as management participation by AICPA fits into the self review category of IFAC. The management of threats is basically the same in the two frameworks, namely, identify the threat, evaluate it, and apply safeguards. The categorisation of safeguards appears to be different, as IFAC gives two, as opposed to three given by AICPA. However, this is caused by AICPA dividing the work environment into two namely the client and the firm.

The only major difference is that AICPA has detailed rules for the application of the independence standards, whereas the IFAC is mainly principles based. This perhaps explains the fact that the AICPA provisions are more elaborate and detailed than the IFAC provisions.

A comparison with other professional and regulatory bodies reveals more of similarities than significant differences, as depicted on the following table:

**Table 2.1: Definitions and comments about independence from regulatory frameworks**

<table>
<thead>
<tr>
<th>Framework</th>
<th>Comments on independence</th>
<th>Distinction between independence of mind and independence in appearance</th>
</tr>
</thead>
</table>

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| IFAC, Australia | The use of the word ‘independence’ on its own may create misunderstandings. Standing alone the word may lead observers to suppose that a person exercising professional judgment may be free from all economic financial and other relationships. This is impossible as every member of society has relationships with others (IFAC, 8.9, Australia, principle 12). |
| UK (ICAEW ethical guide) | Threats to objectivity can be general in nature or relate to the specific circumstances of an engagement or appointment. The easiest way of avoiding such threats would be for members to decline to act in any circumstances where the slightest threat to objectivity might exist. This could deny to clients and employers proper access to a member’s breadth of expertise and knowledge of the …business, and in deciding whether to include such a prohibition, the Institute always bears in mind the need to maintain a balance that respects the interests of clients | Independence of mind |
| | The state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism (IFAC, 8.8, Australia, principle 14). |
| Independence in appearance |
| The avoidance of facts and circumstances that are so significant a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm’s or a member of the assurance team’s integrity, objectivity or professional skepticism had been compromised (IFAC, 8.8, Australia, principle 14). |
| Independence in appearance |
| Members should therefore take into consideration the public interest and reasonable and informed public perception in deciding whether to accept or continue with an engagement or appointment, bearing in mind that the level of public interest will be greater in larger entities and entities that are in the public eye (1.200.2.5) The term ‘public interest’ relates to matters of |
**US SEC Rules**

In determining whether an accountant is independent, the Commission will consider all relevant circumstances, including all relationships between the accountant and the audit client and not just those relating to reports filed with the Commission (SEC, part 210.2-01(b)).

**Independence of mind**

Objectivity is a state of mind and except in unusual circumstances a state of mind is not subject to direct proof. Usually it is demonstrated by reference to circumstantial evidence (Discussion of Final Rules. C. The General Standard for Auditor Independence).

**Combined Statement on independence of mind and in appearance**

The Commission will not recognise an accountant as independent, with respect to an audit client, if the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant’s engagement (Part 210.2.01(b)).

**Ontario ICAO Rules**

Chartered Accountants (CAs) cannot practice their profession or participate in the affairs of their community without being exposed to circumstances that may place pressure upon their objectivity and integrity, and it would be impossible to impose detailed proscriptions intended to cover all conceivable situations. To do so on a rigid basis would be to inhibit the rendering of useful services when the likelihood of impairment of the CA’s objectivity is relatively remote. It may be difficult for a CA always to appear completely free of any disabling influence, interest or relationship in respect of his or her client’s affairs (Rules of Professional Conduct, Foreword).

**Combined statement on independence of mind and independence in appearance**

A member who engages or participates in an engagement (a) to issue a written communication under the terms of any assurance engagement or (b) to issue a report on the results of applying specified auditing procedures, shall be and remain free of any influence, interest or relationship which in respect of the engagement impairs the member’s professional judgment or objectivity or which, in the view of a reasonable observer, would impair the member’s professional judgment or objectivity (rule 204.1).

**Independence in appearance**

The public must be assured of the chartered accountant’s freedom from any conflict of interest. The profession tests the existence of this freedom against the criterion of whether a reasonable observer would conclude that a specified relationship between a chartered accountant and a client posed an unacceptable threat to the chartered accountant’s independence of judgment. Only thus can public confidence in the objectivity and integrity of the chartered accountant be sustained…The reasonable observer should be regarded as a hypothetical individual who has knowledge of the facts which the chartered accountant knew or ought to have known, and applies judgment objectively with integrity and due care (Foreword, principles governing conduct)
What clearly comes out of the literature is that there is general consensus that the two elements of independence are important to the profession. Independence of the mind is in fact the more important of the two because it involves the state of mind of the practitioner when performing his or her professional duties. However, independence of the mind is something that is internal to an individual and cannot normally be observed or verified. It is a choice that the individual makes and involves acting with integrity and objectivity in the performance of professional duties. It ensures that the opinion issued by the practitioner is not tainted by external influences, but is his or her honest opinion.

Independence in appearance on the other hand is judged by what a reasonable, informed third party would construe as independence, in view of the surrounding circumstances. In other words it is observable and verifiable in that certain acts and relationships can be construed by the public to provide evidence of independence and objectivity of the practitioner or lack of it. Professional and regulatory bodies are therefore able to give guidelines on which actions or relationships are considered to impair the independence and objectivity of the practitioner. Independence is necessary to maintain the credibility of the profession, and the confidence that the public has in the profession.

Having looked at the treatment of independence and objectivity in the external audit realm, it is now time to turn to the internal audit area. The independence and objectivity of the internal auditor is a more complicated issue, as the auditor is expected to audit management who are his or her employer, and who are responsible for such things as his or her continued employment, promotion and salary increases. The Institute of Internal Auditors gives
guidelines on the subject of independence and objectivity through auditing standards and practice advisories.

2.3.3 The Institute of Internal Auditors (IIA)

The institute of internal auditors, as the global standard setting board for the internal auditing profession has issued guidelines to practitioners in the form of the International Professional Practices Framework (IPPF). These comprise the code of ethics, standards, and practice advisories. Compliance with the code of ethics and standards is mandatory, whereas the practice advisories are strongly recommended. The provisions of these guidelines as they apply to the internal auditing profession are discussed in the ensuing section.

2.3.3.1 IIA Code of Ethics on objectivity

It is pertinent to mention here that all internal auditors, be they members of the IIA or not, are required to observe the IIA code of ethics, whose purpose is “to promote an ethical culture in the profession of internal auditing… founded as it is in the trust placed on its objective assurance about risk management, control and governance” (IIA 2004:xxii). One of the principles of the code that internal auditors are expected to uphold and follow is objectivity. In this regard, internal auditors are required to exhibit the highest level of professional objectivity in the gathering, evaluating and communicating of information about the activity or process being examined. They are also required to make a balanced assessment of all relevant circumstances and not be unduly influenced by their own interests or by others in forming judgements. (IIA 2004) The rules of conduct regarding objectivity prohibit internal auditors from participating in any activity that may impair or be presumed to impair their unbiased assessment, including those activities or relationships that may be in conflict with interests of the organisation. Acceptance of anything that may impair or be presumed to
impair their professional judgement is also prohibited. Full disclosure of all facts, which, if not disclosed could distort reporting activities under review is required. (IIA 2004)

2.3.3.2 Organisational Independence and individual objectivity

In a publication entitled ‘How does internal audit maintain its independence’, The IIA states that the audit charter should establish independence for the internal audit activity. This is done by a dual reporting relationship to management and the organisation’s most senior oversight group. It goes on to say that the chief audit executive should report to the executive management for assistance in establishing direction, support and administrative interface and to the audit committee for strategic direction, reinforcement and accountability. Auditors should have access to all records and personnel as necessary and carry out investigations without impediments. To maintain objectivity, the publication states that internal auditors should have no personal or professional involvement with or allegiance to the area being audited, and should maintain an unbiased and impartial mindset.

The two concepts (i.e. organisational independence and individual objectivity) are discussed under the broad headings of organisational independence (attribute standard 1110), individual objectivity (attribute 1120) and impairments to independence and objectivity (attribute 1130). (IIA 2004) The standards, which are considered the best practices in the profession are stated and discussed first. This is followed by the review and critiquing of current literature and the identification of the gap to be filled by the present study.

2.3.3.2.1 Organisational independence

Organisational independence requires that the internal audit be free from interference from other organs of corporate governance in the performance of their duties. Attribute Standard 1000 - Purpose, authority and responsibility, (Institute of internal auditors 2004:33) states that
“the purpose authority and responsibility of internal audit activity should be formally defined in a charter, consistent with the standards and approved by the board”. Moeller (2005:182) is in agreement and states that the internal audit charter “is a broad, but general document that defines the responsibilities of internal audit within the organisation, describes standards to be followed, and defines the relationships between the audit committee and internal audit.” The Kings report (2005) also provides that if the board decides that there is a need for an internal audit function, it must approve an internal audit charter, which, inter alia, formally defines the purpose, authority and responsibility of the internal audit activity.

Practice advisory 100 –1 (Institute of Internal Auditors 2004) requires that the charter be in writing, and that the chief audit executive should seek approval of senior management and acceptance of the board. Such approval and acceptance should be minuted. The charter should establish the internal audit’s position within the organisation, authorize access to records, personnel, and physical properties relevant to the performance of engagements, and define the scope of internal audit activities. The practice advisory goes on to state that such a written document provides formal communication for review and approval by management and acceptance by the board. It also provides that the charter be subject to periodical assessment for adequacy in the face of changing circumstances and be amended as necessary.

It is important that this document be circulated and explained to all levels of management so that they are aware of the duties responsibilities of internal audit, which in turn will facilitate their cooperation. Management should also ensure that the contents of this charter are disseminated to all staff levels of the organisation, as internal auditors interact with all levels of staff during the course of their duties. This is a very important document, as the
effectiveness on the internal audit function partly depends on the cooperation they receive from management and operational staff.

This study will sought to establish the existence of the charter in the organisations under review, who approved it, the contents, and dissemination thereof, and whether it is understood and respected by management and staff.

2.3.3.2.1.1 Approval of the internal audit budget

Aligned to the issue of reporting lines is the question of approval of the internal audit budget. It will be appreciated that the budget is a very powerful tool, as the amount of resources put at the disposal of the internal audit function determines the extent of its audit coverage. The ideal position, and that recommended by the standards is for the board (audit committee) to approve this budget. It should be borne in mind that both the CEO and the CFO are clients of the internal audit function. If they are allowed to approve the internal audit budget, this would constitute an impairment of independence and objectivity, as they could deliberately limit the scope of the internal audit function by not availing adequate funds. There is a paucity of empirical evidence on who approves the internal audit budget. Christopher et al (2009) in a survey of 34 Australian CAEs found that in only about a quarter of the companies surveyed the internal audit budget was approved solely by the audit committee. In the rest of the cases it was either the CEO, the CFO, or the Audit Committee in conjunction with other senior officials. It appears that this is an area which still requires a lot of attention.

This study enquired into the current practice in relation to this very important aspect, in order to determine if audit independence could be affected by such practices.
2.3.3.2.1.2 Inputs into the internal audit annual work plan

Closely related to the budget is the right to determine what should go into the annual work plan of the internal audit function. In order to maintain independence and objectivity, there should not be any undue influence from management regarding the scope or coverage of internal audit. The internal audit function should independently determine its annual work plan, based on, among other things its own assessment of risk, as well as the state of internal controls in various parts of the organisation. It is therefore necessary that management (including the CEO and CFO) should not dictate what should and should not go into the work plan (although they can suggest areas to be included for the consideration of the internal audit), as they are auditees and cannot be allowed to determine which part of their work should be subjected to audit scrutiny and which should not. To allow this would result in gross impairment of internal audit independence and objectivity. However, it is good practice for the Chief Audit Executive to seek inputs for possible inclusion from management. Christopher et al (2009), in the survey referred to in paragraph 2.3.3.2.1.2 above, found that a substantial proportion of both the CEOs and CFOs had inputs in the internal audit planning. The researchers argue that although this does not indicate a direct influence, it might put pressure on internal audit to cooperate with management instead of checking on them.

I did not come across any studies of this aspect on the Zimbabwean situation. This research sought to know how the internal audit annual work plans are put together and what influence if any, senior management have, as well as its impact on internal audit independence.

2.3.3.2.1.3 Hiring and firing of the Chief Audit Executive (CAE)

In order to maintain objectivity, the hiring and firing of the Chief Audit Executive should be the preserve of the audit committee. (IIA 2004) The Chief Executive Officer and the Chief Financial Officer are all clients of internal audit and allowing them to be involved in the
hiring and firing of the Chief Audit Executive would amount to impairment of independence and objectivity of the CAE. This position is supported by the corporate governance guidelines (BRC 1999, Smith guidance 2005). McHugh and Raghunandan (1994) and Bariff (2003) concur with this position. Goodwin and Yeo (2001) found that audit committees were involved in the dismissal of the CAE the majority of cases (seventy-two percent) in Singapore, and in Australia and New Zealand Goodwin (2003) found that fifty-two percent were similarly involved. This shows that there is movement towards compliance with the guidelines.

This study sought to find out what the position in Zimbabwe is and the reason thereof.

2.3.3.2.1.4 Reporting lines for the chief audit executive

Traditionally the Chief Audit Executive (CAE) has reported to either the Chief Executive Officer (CEO) or the Chief Financial Officer (CFO) (Bariff 2003). However this arrangement is flawed in that those to whom he or she reports are also audit clients. The independence and objectivity of the auditor in such an arrangement would be impaired, as he or she would find it difficult to issue an adverse report on his or her boss. The advantages and disadvantages of reporting to different levels of senior management are shown in the table below.

<table>
<thead>
<tr>
<th>Reporting to</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>CEO</td>
<td>Establishes audit status</td>
<td>CEO may have too many direct reports</td>
</tr>
<tr>
<td>CFO</td>
<td>Reinforces financial control. CFO often understands the role of internal audit and can provide advice</td>
<td>Potential conflict of interest:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• If audit findings reflect badly on CFO</td>
</tr>
<tr>
<td></td>
<td>If resources are diverted to lower priorities</td>
<td></td>
</tr>
<tr>
<td>--------------------------</td>
<td>-----------------------------------------------</td>
<td></td>
</tr>
<tr>
<td>Other senior executive</td>
<td>Good for audit independence if the executive has no or few direct operational responsibilities subject to significant internal audit scrutiny</td>
<td>Executive may lack knowledge of operations and internal controls or may not have a motivation for internal audit to be effective</td>
</tr>
<tr>
<td>Chair of Audit Committee</td>
<td>Good for audit independence</td>
<td>Internal audit is no longer seen as supporting and partnering with management. Chief Audit Executive may lose status and acceptance as a member of the management team.</td>
</tr>
</tbody>
</table>

**Source:** Fraser and Lindsay (2004) 20 questions directors should ask about internal audit.

The ideal reporting structure is one in which the CAE reports to the Chair of the Audit Committee. Let us now turn to guidance given by the Institute of Internal Auditors.

Attribute standard 1110 – organisational independence (Institute of internal auditors 2004:7) requires that the chief audit executive report “to a level within the organisation that allows the internal audit activity to fulfil its responsibilities.” Practice advisory 1110-1 organisational independence, (IIA 2004) states that auditors should have the support of senior management and the board to gain the cooperation of auditees and perform their work without interference. As a result, the chief audit executive should report to an individual with sufficient authority to ensure broad coverage and appropriate action on audit recommendations. (IIA 2004) It further advocates that the CAE should ideally report to the audit committee functionally and to the CEO administratively. Functional reporting covers such areas as the approval of the audit charter, the hiring and firing of the CAE, approval of the audit plan and budgets. Administrative reporting on the other hand covers human resources administration and other policies and procedures. (IIA 2004)
Practice advisory 1110-1 (IIA 2004) also recommends that the chief audit executive should have direct communication with the board, by regular attendance and participation in board meetings to keep each other informed on matters of mutual interest.

Practice advisory 1110-2 (IIA 2004) emphasizes that appropriate reporting lines are critical to the achievement of independence and objectivity, and organisational stature necessary to achieve its objectives. In order to achieve the necessary independence, the chief audit executive should report functionally to the audit committee or its equivalent, and for administrative purposes, in most instances he should report directly to the chief executive officer of the organisation.

2.3.3.2.1.4.1 Functional reporting

This is described by the practice advisory (IIA 2004) as the ultimate source of the internal audit function’s independence and authority, hence the need to report to the highest possible level within the organisation, such as the audit committee, the board of directors or other appropriate governing authority. The practice advisory explains that functional reporting means that the governing authority would:

- Approve the charter of the internal audit function
- Receive reports of results of audit activities and have private meetings with the chief audit executive without the presence of management.
- Be responsible for hiring and firing the chief audit executive as well as determine the annual salary and adjustment.
- Ensure that there are no scope or budgetary limitations that impede proper execution of the internal audit activity’s responsibilities
- Have final authority to review the annual internal audit plan and any changes thereto
• Review performance of the chief audit executive at least once a year.
• Facilitate open and direct access to the chair and members of the audit committee and the board (IIA 2004)

2.3.3.2.1.4.2 Administrative reporting

This is described by the practice advisory (IIA 2004) as the reporting relationship that facilitates day-to-day operations of the internal audit function and includes the following:

• Budgeting and management accounting
• Human resource administration, internal communications, and administration of the organisation’s policies and procedures. (IIA 2004)

The practice advisory emphasizes the importance of reporting to an individual with sufficient authority, stature, and appropriate control and governance mindset, interest to actively support the CAE on audit issues and ensure effectiveness of the function. The administrative authority should facilitate open and direct communications with all levels of executive and line management including the chief executive officer and ensure that budgetary controls it imposes do not impede on the internal audit’s ability to discharge its responsibilities. (IIA 2004)

It is pertinent to note that the standard and practice advisories acknowledge that it would be fallacious to prescribe a “one size fits all” recommendation, due to differences in, among other things, the size, nature, complexity of each organisation as well as common practices in each country. The reporting structures espoused in the standards are the ideal ones. Whatever structures are adopted, the internal auditor should use professional judgement in determining the extent to which guidance provided by the standards should be applied.
It is very important that the CAE reports to the highest level possible for him to be taken seriously by management and for the internal audit activity to be effective. However in some cases, the size of the company may not make this arrangement possible. Where this is the case, it would be necessary to put in place other safeguards to ensure that the independence of the internal auditor is not compromised. (IIA 2004)

The dual reporting structure is supported by the Kings Report (2002) and the Blue Ribbon Committee report(1999). However, Bariff (2003) argues that traditionally, the CAE reports to the Chief Financial Officer and that this practice still exists.

Leung et al (2004) used an online survey of 85 CAEs and in-depth interviews of 16 CAEs and 7 senior business representatives in Australia, to explore the role of internal auditors in corporate governance and management. They reported that although most CAEs reported to the audit committee, more than 22 percent reported either to the CEO or the CFO.

Paape, Scheffe and Snoep (2003) conducted survey of 105 CAEs from European companies to examine the relationship between internal audit and corporate governance. They found that less than half of the respondents reported to the audit committee and that the audit committee was not always involved in the hiring and firing of the CAE. Christopher et al (2009) found that slightly over a third of the CAEs in their study reported to the audit committee, with the rest having multiple reporting lines.

Empirical evidence from the USA appears to support the reporting lines recommended by the IIA and the corporate governance codes. James (2003) conducted a survey of 63 United States bank loan officers. The aim was to find out whether internal audit reporting structures affected the perceptions of financial statement users on the ability of the internal audit function to prevent financial statement fraud. His findings were that in-house internal auditors who reported to senior management were perceived to be less able to prevent
financial statement fraud than those reporting to the audit committee. Financial statement fraud is usually committed by, or with the consent of senior management, so it would be difficult for an internal auditor to stop his boss from committing the fraud. Their independence would therefore be impaired.

In another study, Van Peursem (2005) carried out a multiple case study of six New Zealand organisations to examine how internal audit could cooperate with management while remaining independent enough to report on the performance of management. He found that close relationships between internal audit and management could threaten the independence of internal auditors.

In a multiple case study of five Belgian companies by Sarens and de Beelde (2006), aimed at understanding mutual expectations and perceptions of internal audit and senior management, it was found that when internal audit operates for the sole purpose of supporting management, the internal audit function was perceived to lack objectivity. Further, the relationship between internal audit and the audit committee was found to be weak.

I was unable to find studies on CAE reporting lines, that were conducted on Zimbabwean organisations. However empirical evidence from Europe, and New Zealand seems to indicate that there is movement towards the adoption of structures where the CAE reports to the audit committee, as this enhances his/her independence and that of the internal audit function.

It appears that the position that the internal audit function should report to a body higher than senior management has wide support, as this enhances the independence of internal auditors. The degree of compliance with these reporting requirements, advocated by the IIA and corporate governance codes, and where impracticable, the nature and extent of safeguards were examined in this study.
This study also explored the reporting lines for the chief audit executive, and mechanisms put in place to ensure that his or her independence was not impaired.

2.3.3.2.1.5 The use of internal audit as a training ground for future managers.

Because of its strategic positioning within the organisation, the use of internal audit as a training ground is widespread (Arena, Arnaboldi and Azzone 2006, De Beelde and Sarens 2006, Selim, Sadarsanam and Lavine 2003). This practice usually takes two forms: graduates are hired as internal auditors and transferred to management position after a few years. Alternatively, current employees are seconded to internal audit for some time before being promoted to management positions (Goodwin and Yeo 2001). Christopher, Leung and Sarens (2009) found that this practice was quite prevalent, and argue that this affected the long term commitment of the internal auditors, who would be reluctant to raise a report against a potential future boss. It appears that the main reason for maintaining this practice is that the internal audit function provides the prospective managers with an opportunity to have an overview of the organisation’s systems and functional areas and how they operate and complement each other in achieving the objectives of the organisation. A survey in the USA by Oxner and Kusel (2002) showed that almost forty-five percent of the directors stated that management used the internal audit function as a training ground. However, the study did not explain reasons for this practice. Prawitt (2003) argues that this practice gives employees a unique opportunity to see the resources and processes of the entire organisation. He goes on to state that in some companies it is used to fast-track high potential employees into management position. In this way, staff with highly sought after technological skills can be attracted and retained. This would then enable the internal audit function to reduce the number of outside personnel the function relies on. Barrier (2001) states that the exposure given to the management trainees helps them to understand the business as a whole. This is
supported by the Office of the Auditor General, Canada (1992) which states that the management trainees have a bird’s eye view of the organisation’s activities, which allows them to know the organisation’s business by its conduct guidelines, its control standards and its code of ethics, and provides an opportunity to see different leadership styles in action. More recently, Abbot, Parker and Peters (2010) reported that in a survey of 134 internal auditors from the fortune 1000 firms, sixty-five percent said they used the internal audit function as a management training ground.

However, this practice has its downside, as the high staff turnover in the internal audit function that results leads to lack of continuity, which might adversely affect audit quality. (Prawitt 2003). This is because the trainees know that they will only be in the internal audit function for a short period, before moving on to the management positions for which they are earmarked. There could also be more emphasis on soft skills, such as leadership and communication skills (Prawitt 2003) at the expense of core internal auditing activities. This practice results in a few career internal auditors in the organisations that emphasise internal audit as a management training ground.

Messier, Reynolds, Simon and Wood (2011) found that the use of the internal audit function as a management training ground affected both the external audit fees and the external auditor’s perception of the internal audit function. The external auditor’s perception was used as external auditors are required by their standards to evaluate the objectivity, competence and due care of internal auditors, before they can use the work of internal auditors. (AICPA 1990; IFAC2009; PCAOB 2007). Increased reliability on, and use of the work of internal auditors translated to less audit fees. In their study, Messiers et al found the practice prevalent, as more than half of the companies with an internal audit function specifically hired personnel with the purpose of promoting them to managerial positions or
cycled current employees into the internal audit function for a short stint, before promoting them to managerial positions. The study also found that external auditors charge higher fees to companies that use the internal audit function as a training ground for management. The external auditors also perceived internal auditors employed by an internal audit function used as a training ground for management to be less objective, though not less competent than those employed in an internal audit function not used as a management training ground. They suggest that the reason for the higher fees could be the concerns of the external auditors with the objectivity of internal auditors in companies using the internal audit function as a management training ground. Christ, Adi, Nathan and Wood (2012) also concluded that using the internal audit function as a management training ground can compromise internal auditors’ monitoring effectiveness. They advise firms to consider the potential costs of using the internal audit function as a training ground from which to promote managers when designing their internal audit functions.

What appears to come out from the majority of the studies is that there is a real potential of the internal auditors’ independence and objectivity being compromised, and that the quality of the work of the internal audit function might be adversely affected by the practice as a result of the lack of continuity or commitment. It is interesting to note that the study by Goodwin and Yeo (2001) found that internal audit was viewed as a stepping stone to managerial positions in forty-three percent of the companies surveyed. The internal auditor may not want to give an adverse report on a potential future boss for fear of jeopardising his career progression. There is also the possibility of self review, where the internal auditor could audit the work he performed before moving to the internal audit department. Another threat is that of familiarity, as the auditor might have to audit the work of his previous colleagues or workmates. Clearly, there are a lot of threats associated with the use of internal audit as a training ground for management, and this calls for strong safeguards to ensure the
independence of internal auditors and quality of work produced by the internal audit function.

No studies of this practice in Zimbabwe were found. This study therefore endeavoured to establish how widespread the use of internal audit as a training ground for management was, and its impact on the independence and objectivity of the internal auditor, and any safeguards put in place to ensure independence and objectivity are not compromised.

2.3.3.2.2 Individual objectivity

A commitment to objectivity by the individual auditor who performs audit work is imperative, in order to maintain the integrity and credibility of the profession and the truthfulness of the work produced by the internal auditor. Standard 1120 (Institute of internal auditors 2004:7) on individual objectivity states that ‘internal auditors should have an impartial, unbiased attitude and should avoid conflicts of interest”. Individual objectivity is the equivalent of what is referred to as independence of the mind, or real independence. It concerns the state of the mind of the internal auditor and personal choices that he or she makes in the performance of his or her duties. It is difficult to determine if the internal auditor is really objective, since it is impossible to observe or measure a person’s mental attitude or personal integrity. Practice advisory 1120-1 (IIA 2004) states that objectivity is a mental attitude to be maintained by internal auditors when performing engagements and adds that internal auditors should not subordinate their judgement on audit matters to that of others. To ensure objectivity, the practice advisory recommends reviewal of all audit work for objectivity, declaration of all instances of potential conflict of interest by auditors before an engagement and rotation of staff on assignments. (IIA 2004) The acceptance of material or substantial gifts, fees or entertainment from an auditee are considered unethical as they create an appearance of impairment of objectivity and any such offers should be reported to the
internal audit supervisor immediately. Because of the importance of objectivity, the internal audit should have a policy for the disclosure and management of conflicts of interest. (IIA 2004)

2.3.3.2.2.1 Impairments to independence and objectivity

Impairments are defined in the glossary as “Impairments to individual objectivity and organisational independence may include personal conflicts of interest, scope limitations, restrictions on access to records, personnel, and properties and resource limitations (funding)” (IIA 2004:28). The AICPA’s definition is short and to the point. To impair is defined as to effectively extinguish independence, and when a member’s independence is impaired, it means that he or she is not independent.(AICPA 2012).

Standard 1130 on Impairment to Independence and Objectivity (IIA 2004) - states that if independence or objectivity is impaired in fact or appearance, the details of the impairment should be disclosed to appropriate parties. The nature of the disclosure will depend upon the impairment. Practice advisory 1130-1 (IIA 2004) provides that internal auditors should report situations of conflicts of interest or bias to the chief audit executive, who should then reassign staff as necessary. The practice advisory requires that scope limitations be reported to the board. Scope limitations may restrict the scope defined in the internal audit charter, access to records, personnel and properties relevant to the audit, performance of procedures or staffing plan and financial budget, thereby precluding achievement of audit objectives and plans. Practice advisory 1130-A1(IIA 2004) prohibits internal auditors from assessing operations for which they were previously responsible within the previous year (self-review). Practice advisory 1130-A1-1 further explains that internal auditors should not assume operating responsibilities, but when required to do so by management, it should be made clear that they are not functioning as internal auditors, in addition, when staff are transferred to or
temporarily engaged by internal audit from operation, care should be taken to ensure that they
do not audit activities for which they were previously responsible, until expiry of a
reasonable time (at least one year). Attribute standards 1130.A1, 1130A2, 1130.C1, and
1130.C2 (IIA 2004) prohibit assessing operations on which the internal auditor was
responsible within one year, and provide that functions for which the Chief Audit Executive
has responsibility should be overseen by a party outside the internal audit activity. They also
allow internal auditors to carry out consulting services for operations for which they were
previously responsible. The standards also require internal auditors to disclose potential
impairments before acceptance on an engagement. The relevant practice advisory (Institute of
Internal Auditors 2004:63) states that internal auditors “should not subordinate their
judgement on audit maters to that of others.” It advises, among other things that acceptance
of gifts and entertainment from auditees is unethical and that assignment to audits should be
made to avoid conflict of interests. Reviewal of work before issue of reports is also
recommended in order to ensure objectivity. The advisory also provides that where there is a
scope limitation that prevents internal audit from achieving its objectives and plans, this
should be communicated to the board in writing. It warns internal auditors against
performing non-audit activities that are subject to periodic internal audit assessment, in order
to avoid self-review. (IIA 2004) If such assignments cannot be avoided, then the appropriate
parties should be advised of the impairment threat and the fact that when performing such
activities, the internal auditor would not be acting in their auditing capacity.

The crucial issue here is that the individual auditor should have a full commitment to
independence and objectivity. He or she should disclose all instances of potential conflict of
interests before commencement of the audit. This would enable the Chief Audit Executive to
redeploy staff in such a way that there is no impairment of objectivity. The Chef Audit
Executive has to ensure that situations of conflict of interests that arise or are brought to his
or her attention are properly managed. It is therefore necessary for the internal audit function to have properly thought out and documented procedures for the management of conflict of interests. These procedures must be reviewed periodically to ensure that they adequately cover all situations of potential conflict of interests. It is of paramount importance that all internal auditors are aware of these procedures.

This research sought to find out how situations of conflict of interests and impairment to objectivity were handled in the organisations under review.

2.3.3.2.2 Threats to independence and objectivity

The IIA guidance entitled Independence and objectivity: A Framework for Internal Auditors (IIA 2001) identifies several threats among them, the seven briefly described below

**Self review**

This occurs when the internal auditor reviews his or her own work, e.g. when the auditor is required to audit activities he was responsible for before moving to the internal audit function.

**Social pressure**

This relates to exposure to pressure from social groups, e.g. where a team member is reluctant to oppose views generally held by the team (groupthink)

**Economic interests**

This occurs when the auditor has financial interests which could be adversely affected by negative audit findings

**Personal relationships**
The auditor may not want to pass adverse comments when the auditee is a close relative or friend.

**Familiarity**

Threats may arise due to a long term relationship with the auditee. This may make the auditor to be lenient or assume problems previously unearthed do not still exist.

**Cultural, racial or gender bias**

The auditor may be biased against certain cultural, racial/gender groups or a particular gender due to a lack of understanding of the different practices and customs.

**Cognitive biases**

This may arise from unintentional psychological bias in interpretation of information or having some preconceived ideas before the audit (IIA 2001).

However there are circumstances where a combination of these threats are present at the same time. In assessing the impact of these threats, the auditor should also consider mitigating factors.

This list compares very well with that given by the American Institute of Certified Public Accountants (AICPA)(1999) in its Practice alert 99-1, which identifies the following risks:

- Self interest risk – a threat that arises from an auditor acting in his or her own interest
- Self review risk – a threat that arises from an auditor reviewing his own work or the work done by others in the auditor’s firm
- Advocacy risk – a threat that arises from an auditor acting as an advocate for or against an auditee’s position or opinion rather than as an unbiased attester.
• Familiarity or trust risk – a threat that arise from an auditor being influenced by a close relationship with an auditee.

• Intimidation risk – a threat that arises from an auditor being influenced inappropriately or pressured by an auditee or by another interested party. (AICPA 1999)

2.3.3.2.3 Mitigating factors

Mitigating factors reduce the significance of identified potential threat. The following are some of these factors: (IIA 2001)

Organisational position and policies

These may discourage auditees from trying to influence or intimidate auditors

Environment- strong organisational governance system

A supportive environment that encourages continuous improvement as well as a strong audit committee is necessary to ensure audit objectivity

Incentives (rewards, discipline)

A system-wide policy that rewards objective thinking and penalises bias can encourage objectivity in the organisation.

Use of teams

This can diffuse threats due to familiarity, self review, and cognitive bias, but are vulnerable to groupthink.

Supervision and/or peer review
These can mitigate individual biases, and the awareness of supervisory or peer review will encourage the auditor to avoid biases.

**Internal consultations**

In cases of doubt, the auditor can seek advice and guidance from a respected professional colleague or superior. The audit unit can develop formal procedures to determine when an auditor should seek consultation.

**Rotation/reassignment**

This can reduce threats due to familiarity and self-review.

**Outsourcing**

Outsourcing to an external provider can be used in the absence of effective internal tools. However, this will be an additional cost to the organisation (IIA 2001).

### 2.3.3.2.2.4 Management of threats to independence and objectivity

The Institute of Internal Auditors gives guidance in the management of threats to independence and objectivity in a publication entitled “Independence and Objectivity: A Framework for Internal Auditors” (IIA 2001). The framework recognises that objectivity is a state of mind, and therefore relies heavily on the professionalism of individual internal auditors and their supervisors to identify, assess, mitigate or manage the identified threats to objectivity.

The figure below summarises steps recommended in the management of threats to objectivity within the internal audit function.
Fig. 2.1 Managed Objectivity Framework for Individuals

The various steps of the management of threats to independence and objectivity are briefly explained below: (IIA 2001)

**Identify threat**

Any situation that may raise questions regarding the auditor’s ability to act without bias are identified and regarded as threats

**Assess significance of threat**

Those performing the audit consider if identified threats might compromise their objectivity

**Identify mitigating factors**

The auditor considers relevant mitigating factors and how best to mitigate the risk of compromised objectivity.

**Assess residual threat**

**Source:** IIA (2003) Research Opportunities in Internal Auditing 

The various steps of the management of threats to independence and objectivity are briefly explained below: (IIA 2001)
Assess any threat remaining after considering mitigating factors and if in doubt seek reviewal by the chief audit executive, senior management or the audit committee.

**Proactively manage residual threat**

Tools to manage residual threat include third party reviews and separation of audit duties

**Assess the presence of unresolved threats to objectivity**

During the course of the engagement, be alert for threats not previously identified or not adequately resolved. If there are any unresolved threats it is necessary to inform the users before commencement and to carefully consider reporting implications. (IIA 2001)

**Consider the reporting and documentation implications**

Identified mitigating factors and steps taken to manage threats should be documented. If work is undertaken despite the presence of material, unresolved threats, these should be reported on a continuous basis to the appropriate level, e.g. senior management, the audit committee or the board. This will prevent users from unknowingly deriving unwarranted assurance from work performed under such conditions. (IIA 2001)

**Ex post review and monitoring**

This process starts with self-review of the individual auditor, is enhanced by a review of the team as a whole, to determine if judgements were made in the most objective manner. The overall review is made by the chief audit executive, and other bodies like the audit committee can be part of this process. Peer review can also be included. (IIA 2001)

The guidance also suggests a framework for managing threats to objectivity at all levels of auditor involvement in the organisation as depicted on the figure below.
Framework for managing threats to objectivity at all levels in the organisation

Managed Objectivity Framework

I. Individual Level Issues:
- Management of auditor objectivity
- Management of professionalism

II. Engagement Level Issues:
- Review auditor objectivity
- Review auditor professionalism and the audit process

III. Internal Audit Department Level Issues:
- Rotation of employees on jobs
- Ensure objectivity is managed (incl. third-party outsourcing)
- Reporting responsibilities

IV. Company Level Issues:
- Management interest in objectivity
- Human resources policies (hiring, firing, promotion)
- Level of audit committee involvement

V. Profession Level Issues:
- Standards setting, education, and Enforcement
- Active promotion of objectivity management
- Monitoring of profession-level results
- Certification

Source: IIA (2003) Research Opportunities in Internal Auditing

Level I depicts the individual auditor level where threats are identified and proactively managed.

Level II is the engagement level and involves the review of auditor objectivity and related threats, as well as the standard review of audit procedures, practices and judgements.

Level III depicts the internal audit department level, where the chief audit executive takes steps to enhance objectivity, reports any unmitigated threats and considers outsourcing if objectivity cannot be appropriately managed.

Level IV is the organisational level. The chief audit executive should be actively involved with the audit committee to ensure the audit department is given freedom to appropriately manage threats to objectivity, without fear of repercussions.
Level V depicts the professional level. Professional bodies should ensure standards and guidance are promulgated to enhance the auditor’s ability to effectively manage objectivity and offer certification opportunities to enhance professionalism. Educational programs aimed at assisting auditors to identify and understand threats, and the objective judgement and management thereof can be devised. (IIA 2003)

This study critically examined the identification, analysis and management of threats to objectivity in the entities under review, to ascertain the adequacy of procedures to ensure internal auditor objectivity

2.3.4 Conflict of roles

The new definition of internal auditing (IIA2004) has expanded the internal auditor’s responsibilities, to include consulting. Concerns have been raised about this dual role of consulting and assurance and how it will impact on the need for the auditor to remain independent and objective. (Brody and Lowe 2000; McCall 2003). In the external audit realm, similar concerns were raised especial after the collapse of large companies like Enron. In the United States of America, the Sarbanes Oxley Act of 2002 prohibited the provision of the following services by external auditors to their audit clients:

- Bookkeeping or other services related to the accounting records or financial statements of the client;
- Financial information systems design and implementation;
- Appraisal or valuation services, fairness opinions, or contribution-in-kind reports;
- Actuarial services;
- Internal audit outsourcing services;
- Management functions or human resources;
- Broker or dealer, investment adviser, or investment banking services;
• Legal services and expert services unrelated to the audit; and
• Any other service that the Board determines by regulation, is impermissible.

Debate on the issue has been very vigorous, with opinions varying from advocacy for outright prohibition of provision of non-audit services to appeals for provision of adequate safeguards. A brief look at some of the reasons for and against the retention of non audit services will illuminate some of the problems on this issue. A brief analysis of the problem by the ICAEW (ICAEW 2012), which summarises the main problems and suggested solutions is given below.

2.3.4.1 ICAEW view on provision of non audit services to audit clients

In is publication, entitled “Provision of non audit services to audit clients’ the ICAEW states that non audit services fall into three categories: (ICAEW 2012)

1. Services required by legislation or contract to be done or undertaken by auditors of the business;
2. Services that it is most efficient for the auditors to provide because of their existing knowledge of the business, or because the information required is a by-product of the audit process, for example, tax compliance; and
3. Services that could be provided by a number of firms. In this case, the fact that the firm is the auditor is incidental and it would generally only be chosen because, for example, it had won a tender process. Examples are: management consultancy or human resources consultancy. (ICAEW 2012)

Argument for general prohibition.

The ICAEW states that when companies fail, auditors are accused of having allowed inappropriate accounting treatments, because their independence was compromised either
because they had become too close to the auditee company (the familiarity threat) or because their objectivity was challenged by overreliance on income from a single source. (ICAEW 2012)

Present safeguards

The following are presented as the existing arrangements to provide safeguards (ICAEW 2012)

- The Institute’s ethical code forbids the provision of non audit services to clients if that would present a threat to independence for which no adequate safeguards are available. The auditor must refuse to supply non audit services or resign.
- Under the Combined code of corporate governance, the audit committee oversees the relationship with auditors and keeps the nature of non audit services under review. In the United Kingdom, for listed companies, audit partners must: (1) disclose in writing relationships likely to have a bearing on the firm’s independence and the objectivity of the engagement partner and staff, including the safeguards that are in place and (2) confirm that the firm is independent and objectivity of the engagement partners and staff is not impaired
- The ethical code specifies that an audit appointment should be declined if the client provides an unduly large proportion of the firm’s gross income.
- Shareholders can assess the extent of non audit services as the companies act requires disclosure of the total amount paid for non audit services. (ICAEW 2012)

Arguments against general prohibition

The ICAEW feels that prohibition would have unintended adverse effects on the quality of audits through restrictions of knowledge and skills, as detailed below: (ICAEW 2012)
Knowledge

This would lead to poorer understanding of the business and a lower likelihood of key issues being identified and could result in likelihood of undetected misstatements.

Skills

Auditors need to draw on the knowledge and experience of colleagues who are experts or specialists in key risk areas like taxation, information systems, fraud, actuarial assessment and other business processes. Inhibiting such exchanges in a firm would be likely to lead to a deterioration in audit quality.

Quality of recruits

Specialists would gradually move out of audit firms to set up separate entities. The remaining firms would find it very difficult to attract the brightest graduates, because of the restriction to an audit-only career. This would adversely affect areas like fraud where the brightest brains are required.

Dependence on clients

Prohibition of non audit services would make firms smaller and this would translate into bigger clients becoming an intimidation threat, as they would form a larger part of the firm’s income.

Quality of business systems

The quality of information technology and accounting systems would suffer, as, often, the auditors are best positioned to advise clients on systems

Speed of reporting
There would be delays in provision of reliable financial information, as external advisers would have to be consulted by the auditors

Cost

Auditors have the advantage of cumulative knowledge and can provide non audit services at a far less cost to the client. Non audit services prohibition would therefore increase the costs to the client. (ICAEW 2012)

The ICAEW concludes by stating that wholesale prohibitions would harm both clients and the auditing profession, and advocate the provision of adequate safeguards, or declining to provide non audit services where adequate safeguards cannot be provided. (ICAEW 2012)

Internationally, various regulating bodies have moved in with various provisions as shown on the table below:

**Table 2.3 Recommended treatment of non audit services in regulatory frameworks**

<table>
<thead>
<tr>
<th>Type of non audit service referred to in the framework</th>
<th>Regulatory framework</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>IFAC</td>
</tr>
<tr>
<td>Exercise management authority</td>
<td>No</td>
</tr>
<tr>
<td>Determine client implementation of auditor’s own recommendations</td>
<td>No</td>
</tr>
<tr>
<td>Report in a management role to client governance body</td>
<td>No</td>
</tr>
<tr>
<td>Custody of client assets</td>
<td>No</td>
</tr>
<tr>
<td>Supervise client employees in normal activity</td>
<td>Normally</td>
</tr>
<tr>
<td>Prepare accounting</td>
<td>Normally</td>
</tr>
<tr>
<td>Service Description</td>
<td>No if material</td>
</tr>
<tr>
<td>------------------------------------------------------------------------------------</td>
<td>----------------</td>
</tr>
<tr>
<td>Records and financial statements for public interest entities</td>
<td>No</td>
</tr>
<tr>
<td>Valuation services and other expert services</td>
<td>No if material</td>
</tr>
<tr>
<td>Taxation services</td>
<td>Yes</td>
</tr>
<tr>
<td>Internal audit services</td>
<td>Caution</td>
</tr>
<tr>
<td>IT services &amp; financial information technology systems</td>
<td>Caution</td>
</tr>
<tr>
<td>Temporary staff assignments</td>
<td>Caution</td>
</tr>
<tr>
<td>Litigation support services</td>
<td>Caution</td>
</tr>
<tr>
<td>Legal services</td>
<td>No</td>
</tr>
<tr>
<td>Recruiting senior management &amp; HR</td>
<td>Caution</td>
</tr>
<tr>
<td>Corporate finance and similar</td>
<td>Caution</td>
</tr>
<tr>
<td>Actuarial services</td>
<td>No specific guidance</td>
</tr>
<tr>
<td>Broker/dealer</td>
<td>No specific guidance</td>
</tr>
</tbody>
</table>

Key:
No = prohibited;
 Normally no = prohibited except in very limited or exceptional circumstances;
 No if material = only permitted if the figures involved are not material to the financial statements;
 Caution = threats and safeguards of each case should be considered before proceeding;
 Yes = permitted;
 No specific guidance = not referred to as NAS in the framework, therefore no specific guidance provided.
Table 2.3 shows that certain services are prohibited by all regulating authorities, because of their potential adverse effect on audit independence. Examples are, the exercise of management authority, and the preparation of records and financial statements. This would create a self review threat. It appears that all regulating authorities are alive to the potential adverse consequences of non audit services to audit independence, and are active in ensuring that either appropriate safeguards can be applied, or the service is prohibited if such safeguards cannot be provided. I also feel that despite the strong evidence given by the ICAEW in trying to defend their consulting activities, the professional bodies should confine themselves to Auditing and Accounting related areas like income tax, and should not venture into other areas like human resources, because their training does not include a comprehensive coverage of such areas, to enable them to be consultants.

Having looked at the external audit realm to gain insight into how the provision of non-audit services have affected audit independence in the external audit sphere, it is now opportune to look at the internal audit arena. The nature, importance, and benefits of consulting as well as safeguards necessary to ensure that the internal auditor maintains independence and objectivity while performing consulting activities are discussed in the ensuing paragraphs.

2.3.4.2 Consulting and Assurance for internal auditors

Besides the assurance role, the internal auditor is also required to carry out consulting activities, usually on an ad hoc basis. Consulting and assurance are not mutually exclusive and many audit services include both an assurance and a consulting role (IIA2004). Consulting was included in the definition of internal auditing for the first time in the 1999 definition. However, internal auditors had been doing consulting work in organisations long before this inclusion (Gray and Gray 1994). Nagy and Cenker (2002) confirm this when they
state that the change in definition simply reflected an existing practice, as auditors had been doing consulting and other value-adding activities for a long time. A survey of the internal audit function in top companies in the European Union revealed that about two thirds of the respondents include providing advice on risk assessment, risk management as well as consulting services in their activities (Paape, Scheffe and Snoep 2003). While acting in this role, the internal auditor is required to work together and cooperate with management, that is, being a partner of management, in identifying problems, analysing them, and prescribing solutions. In this role the internal auditor will be assuming duties normally carried out by management, and when they cooperate and work together with management, there is a possibility that management may come to regard internal auditors as partners and lose sight of the real role of internal audit (there is also the threat of self review, when the auditor later comes to audit the activities originally covered by consulting services carried out by him) (Christopher, Leung and Sarens 2007).

Consulting is defined in the glossary as follows (IIA 2004:26)

Advisory and related client service activities, the nature and scope of which are agreed with the client and which are intended to add value and improve an organisation’s governance, risk management, and control processes, without the internal auditor assuming management responsibility. Examples include counsel, advice, facilitation and training

The internal audit activity is ideally positioned to perform consultancy services because of its adherence to the highest standards of objectivity and its breadth and depth of knowledge about the organisation’s processes, risks and strategies (IIA 2004). HM Treasury (2010) argues that internal auditors are trained and skilled in understanding risk and the development of appropriate controls, and can help the organisation to achieve its objectives in an economic, efficient and effective manner, thereby adding value to the organisation. Possible areas in which internal audit can play this role are given as: (HM Treasury 2010)
• Facilitation of management activities – for example as a facilitator at workshops;

• Educational roles – for example, imparting risk and control skills at any level in the organisation; and

• Advice on particular risk and control issues (HM Treasury (2010)).

This view is supported by Selim, Woodward and Allegrini (2009) who state that there are positive benefits with regard to staffing, morale, the general standing of internal audit and the ability to add value, though at the cost of increasing workloads. However, they also point out the need for provision of safeguards for objectivity as proposed in the IIA professional standards.

Anderson (2003) presents these two services as a continuum of six basic types of audits: financial auditing, performance auditing, quick response auditing, assessment services, facilitation services and remediation services. (Figure 2.3 below). The extreme left depicts the traditional financial attestation services and as one moves to the right, one moves away from the traditional services to consulting services.
Assurance engagements include financial, performance, compliance, system security and due diligence audits. Assurance engagements have three distinctive elements that separate them from consulting activities. First, they involve a systematic process of objectively obtaining evidence and evaluating it. Secondly, they need the existence of established criteria against which the evidence is compared. Thirdly, they involve communication of the results to interested users or parties who are neither the provider of the service nor involved in the process or area under review. These parties are usually not present or involved in the establishment of the engagement contract. (Anderson 2003)

In contrast, consulting involves only two parties, the auditor or service provider and the activity management (client), who is the customer, who determines the value added by the consulting engagement. These two positions are depicted by Fig.2.4 and Fig.2.5 below.
Fig 2.4 Parties to an assurance engagement

Source: Anderson (2003) Assurance and Consulting Services
Other differences are that while assurance engagements result in an opinion being expressed, regarding compliance with established criteria, consulting engagements produce recommendation for improvements.

Anderson (2003) explains the stages in the continuum as follows:

*Financial auditing* includes engagements that follow the traditional attestation model, for example, compliance attestations.

*Performance auditing* or operational auditing involves a risk based approach with the objective of minimising risk with constrained resources.

*Quick response* auditing includes special requests by upper management, seeking assurance on specific areas.

*Assessment services* are engagements in which the internal auditor examines or evaluates a past, present or future aspect of operations and renders information to assist management in making decisions, for example, assessment of controls in a system design.
Facilitation services are engagements in which the internal auditor assists management in examining organisational performance for the purpose of promoting change, for example, assisting in developing performance measurement, or estimating the savings from an outsourcing process.

Remediation services present the most extreme and threatening type of activity in terms of incompatibility with providing assurance, in that they involve responsibilities of management. They are necessary in order to prevent or remediate known or suspected problems, for example, the drafting of policies for cash handling. The auditor should make recommendations, which can be adopted or rejected by management, so that independence is not impaired. (Anderson 2003)

When performing consultancy services, internal auditors are usually required to work closely with management as partners, and there is the danger that internal auditors could inadvertently end up performing duties of management, thereby impairing their objectivity. Clear guidance on this is given in Practice Advisory PA 1000.C1 (IIA 2004) which states that internal audit is not a management decision-making function, and decisions to adopt or implement recommendations made as a result of an internal audit advisory service should be made by management. Therefore internal audit objectivity should not be impaired by decisions made by management.

Further guidance on how to deal with conflicts of interest, or possible impairments of independence and objectivity arising from performance of consulting services are given in PA 1000C1-1 and PA 1000C1-2. (IIA2004) These advisories acknowledge that internal auditors have been performing consulting work in organisations for a long time. They also acknowledge that internal auditors are perhaps better placed to perform consulting services, as they have an intimate knowledge of the organisation and strictly adhere to the highest
standards of objectivity. Consulting also enhances the auditor’s understanding of business processes or issues related to the engagement. It is also pointed out that consulting and assurance are not mutually exclusive, as some of engagements may include both roles. In order to maintain independence and objectivity, the PAs make the following recommendations: (IIA 2004)

- There must be ground rules for performance of consulting services and these should be codified in the audit charter and disseminated to all members of the organisation so that they are understood by all.
- Any conflicts arising should be resolved consistent with the code of ethics and the standards.
- If impairments to independence and objectivity exist or subsequently develop during the engagement, they should be immediately reported to management for resolution.
- Care should be taken to ensure auditors do not inappropriately or unintentionally assume management responsibilities. Auditors make recommendations and management make decisions to accept/implement or otherwise.
- Independence and objectivity may be impaired if assurance services are provided within one year after a formal consulting engagement. Different auditors should be assigned to such engagements.
- Internal auditors should avoid acceptance of responsibility for non audit functions that are subject to periodic internal audit assessments.
- Care should be taken in consulting services of a continuous nature, to ensure that internal auditors do not inappropriately or unintentionally assume management responsibilities.
- If senior management directs internal auditors to perform non audit work, it should be made clear that they are not functioning as internal auditors.
- Persons transferred to or temporarily engaged by internal audit should not be assigned to audit activities they previously performed, until a reasonable period, namely, one year has elapsed. (IIA 2004)

It appears that these guidelines are very clear and if followed, instances of conflict of interests or impairment of independence and objectivity may be controlled.

Most of the studies on assurance vs. consultancy examined the degree of involvement of internal auditors in consulting activities. Paape et al 2003 surveyed fifteen CAEs of European companies and sixty four percent of the respondents reported that they engaged in consulting activities. Sixty-one of those surveyed did not agree that internal audit should decline consulting engagements to protect independence.

Arena et al (2006) conducted a multiple case study of six Italian companies and found that in only one company the internal auditors had been involved in consulting services. Allegrini et al in their literature review of European internal auditing state that consulting forms a very small part of the auditing activities. An example is Belgium where an average of only twelve percent of the internal audit time was spent on consulting activities.

In a study by Selim et al, (2009) ninety-four UK/Ireland and two hundred and ninety-eight Italian internal auditors were surveyed. The aim was to find out the nature and extent of the change in internal audit consulting activities. They found that there was a significant increase in both countries. Regarding the effect of consulting on objectivity, there were mixed feelings. In the UK/Ireland, sixty-four percent felt there was an increase in the risk of conflict of interest and thirty-eight percent felt that it reduced the independence and objectivity of internal auditors. In Italy, on the other hand, fifty-one percent felt that consulting had no effect, while thirty-eight percent said involvement in consulting increased internal auditors’ ability to be independent and objective. The researchers attributed the differences between
the two countries to the fact that there are more family owned businesses in Italy, hence the low perception of the importance of independence in that country.

The present study sought to find out if there are sufficient safeguards to ensure that independence and objectivity of internal auditors are not impaired as a result of performance of consulting services.

The review of literature shows that although consulting forms a small part of internal audit activities, there is acceptance that this is necessary, and it appears that internal audit involvement in this sphere will continue to grow. There is also realisation that this practice could lead to conflict of interests and threaten the independence and objectivity of internal auditors, as indicated by the study by Selim et al (2009). Empirical evidence is in agreement with the IIA guidelines and the new definition of internal auditing which includes consulting as part of the internal audit responsibilities.

A review of literature did not reveal any studies in Zimbabwe relating to assurance and consulting for internal auditors, and this study examined the involvement of internal auditors in consulting in Zimbabwe and the effect this had on their independence and objectivity.

Another new dimension introduced in the 1999 definition of internal auditing is the involvement of the internal audit function in risk management, and this is discussed below.

2.3.4.3 Risk management and Assurance

Internal audit has evolved from the traditional independent appraisal function (Gay and Simnet 2010) to an assurance and consulting service which extends to all areas of the organisation (Leung, Coram and Cooper 2007). Internal auditors can add value by providing assurance that risks facing the organisation are identified and are properly managed and
recommending improvements, where there are weaknesses (Leithhead 1999; Walker, Shenkir and Barton 2003 Lindow and Race 2002).

Risk management is a very important aspect of the management of any organisation. By assessing and evaluating risks facing an organisation, management is able to take appropriate action to minimise the adverse impacts of risk. The extent to which internal audit can be involved in the risk management process without impairing its independence and objectivity is an interesting point of discussion. There are dangers of self review, when the internal auditor examines risk management processes in which he or she was involved in setting up. There is also the danger of familiarity due to the close relationship between the internal auditor and the risk management function, when the two work together in the establishment of a risk management system. It is therefore necessary to look at the risk management process to determine to what extent the internal auditor can be involved in it without having his or her independence and objectivity impaired.

2.3.4.3.1 Risk management

Risk management has assumed phenomenal importance, spurred by the global crisis of 2008, which demonstrated the importance of risk management, and stakeholders have become more and more concerned about how risk is managed in organisations. Risk is an unavoidable element of business and can impact an organisation in the short, medium and long term, affecting the strategic, operational, tactical and financial aspects of an organisation. The table below shows the evolution of enterprise risk management
Table 2.4 Evolution of risk management thinking

<table>
<thead>
<tr>
<th>Old Thinking</th>
<th>New Thinking</th>
</tr>
</thead>
<tbody>
<tr>
<td>Little risk management strategy</td>
<td>Risk strategy linked to business strategy</td>
</tr>
<tr>
<td>Risk management limited to certain areas.</td>
<td>Risk culture created throughout the enterprise</td>
</tr>
<tr>
<td>Risk analysis typically in silos</td>
<td>Risk management is a continuous, systematic process integrated within the enterprise’s culture</td>
</tr>
<tr>
<td>Risk not owned</td>
<td>Risk management responsibilities clearly defined</td>
</tr>
<tr>
<td>Inspect, detect, react</td>
<td>Risk is quantified, aggregated and studied for interrelationships</td>
</tr>
<tr>
<td>Correlation among risks not understood</td>
<td>Risk is a key consideration for decision making.</td>
</tr>
</tbody>
</table>

**Source:** P Brady (2006) Roles of Internal Audit in Enterprise Risk Management. Presentation at the 2006 European Conference

The abundance of interest in enterprise risk management has resulted in a number of guidelines or standards to inform the process. These include the ISO 31000 issued by the Internal Organisation for Standardisation (ISO), the Committee of Sponsoring Organisations (COSO) guide entitled “Enterprise Risk Management – An Integrated Framework”, and a risk management standard issued by the three organisations, namely the Institute of risk management (IRM), the Association of Insurance and Risk management (AIRMIC) and the National Forum for Risk management in the Public Sector (ALARM). The COSO and ISO guidelines are more widely accepted than the other guides. In order to appreciate the role of internal audit in enterprise risk management, it is necessary to understand what this concept involves. In the ensuing paragraphs, a brief account of what enterprise risk management entails is given.
2.3.4.3.2 The risk management process

Risk is defined by the ISO guide 73 as the effect of uncertainty on objectives. (ISO 2009) This means that risk is related to objectives. Risk management is defined as the process whereby organisations address risks attached to their activities. In other words it involves the assessment of significant risks and the implementation of suitable risk responses. The risk management process is presented as a list of representing the 7 Rs and 4 Ts of risk management: (IRM, AIRMIC and ALARM 2002)

- Recognition /identification of risks
- Ranking or evaluation of risks
- Responding to significant risks
  - Tolerate
  - Treat
  - Transfer
  - Terminate.
- reviewing the risk management framework.
- Reporting and monitoring

This process is depicted by the following figure (Fig 2.6):
The risk management process


The various stages are explained below:

**Risk assessment**

This is defined by ISO IEC guide 73 as the overall risk analysis and risk evaluation.

Risk analysis involves risk identification which requires intimate knowledge of the organisation, its environment and its strategic and operational objectives and the relevant risks and opportunities and threats.

**Risk description**
This is done to identify risk in a structured manner, and includes the nature, scope, quantification, tolerance, treatment and control mechanisms and identification of functions responsible for developing the risk strategy.

**Risk estimation**

This can be in quantitative or qualitative terms, in terms of the probability and consequences, and includes both threats (down side) risk and opportunities (up side).

**Risk evaluation**

Risk evaluation is used to make decisions about whether each specific risk should be accepted or treated.

**Risk reporting**

This can be internal, and reports are used to inform insiders, i.e. the board, the audit committee, business units and individuals on a regular basis. External reports can also be made to interested stakeholders.

**Risk treatment**

Risk treatment involves the section and implementation of measures to control/mitigate risk, and includes risk avoidance, risk transfer and risk financing.

**Monitoring and review of the risk management process**

The review and monitoring of the risk management process is done to provide assurance of the understanding of and compliance with procedures. It should also identify changes in the system. This is an ongoing exercise, aimed at providing assurance of the understanding of
and compliance with procedures. It should also identify changes in the environment and effect appropriate changes (IRM, AIRMIC and ALARM 2002).

2.3.4.3.3 The COSO framework

The COSO framework bears a strong resemblance to the one described above, but is presented in the format of a cube, as shown on Figure 2.7. (COSO 2004)

**Fig. 2.7 COSO Enterprise Risk Management Framework**


It is an expansion of the COSO Internal Control Framework, which has five elements, namely: (COSO 2004)

- The control environment
- Risk assessment
The COSO Risk management framework was constructed on the basis of this internal control framework, and consists of the following interrelated components: (COSO 2004)

- Internal environment (the organisation’s risk culture) – management sets the risk philosophy, establishes the entity’s risk culture and risk appetite.
- Objective setting (the organisation’s objectives) – management considers risk appetite in the setting of objectives.
- Event identification (events that might affect objectives) – management identifies internal and external events that present risk or opportunity. Opportunities are channelled back to the strategy and objective setting process.
- Risk assessment (how risks are assessed) – the likelihood and impact of risks are assessed in quantitative and qualitative terms.
- Risk responses (how risks are managed) – management makes decisions whether risks should be avoided, accepted, reduced or shared and develops actions to align risks with the organisation’s risk tolerance.
- Control activities - policies and procedures are established to ensure management’s risk responses are carried out effectively.
- Information and communication (how risk is communicated) –timely communication takes place to ensure roles and responsibilities are performed effectively in the whole enterprise risk management process.
• Monitoring (how enterprise risk management as a whole is performing and whether it needs improvement.) – ongoing enterprise risk management monitoring occurs and modifications are made as necessary. (COSO 2004)

The depiction of a cube emphasizes that enterprise risk management cuts through all levels and units of the organisation and relates to strategic, operational, financial and compliance objectives of the entity. (COSO 2004)

As can be seen there is not much difference between the two frameworks, as the crucial stages, in the risk management process, namely, identification and assessment of risk, response to significant risk, reviewing and monitoring as well as reporting are present in both of these frameworks.

2.3.4.3.4 Benefits of enterprise risk management

In a position paper entitled “The role of internal auditing in enterprise-wide risk management” (IIA UK and Ireland 2003) the IIA state that the benefits include the following:

• Greater likelihood of achieving objectives.
• Consolidated reporting of disparate risks at board level.
• Improved understanding of the key risks and their wider implications
• Identification and sharing of cross business risks.
• Greater management focus on the issues that really matter
• Fewer surprises or crises.
• More focus internally on doing the right things in the right way. (IIA UK and Ireland 2003)
The paper also suggests that the internal auditor can perform the following activities without impairing their independence and objectivity: (IIA UK and Ireland 2003)

- Reviewing the adequacy and effectiveness of the entity-wide enterprise risk management processes and providing recommendations for improvement
- Reviewing critical control systems and risk management processes and responses for adequacy and effectiveness
- Providing advice in the design and improvement of control systems and risk mitigation strategies
- Implementing a risk-based approach to planning and executing the internal audit process
- Ensuring that internal audit resources are directed at those areas most important to the organisation
- Challenging the basis of the management’s risk assessment and evaluating the adequacy and effectiveness of risk-treatment strategies and the reliability of management’s assurances.
- Providing assurances on completeness of the management’s classification and reporting of risks
- Facilitating enterprise risk management workshops (IIA UK and Ireland 2003)

Having discussed the enterprise risk management process, it is now opportune to look at the professional guidance given concerning the role of internal audit in enterprise risk management.
2.3.4.3.4 The role of internal audit in enterprise risk management

The Institute of Internal Auditors advocates risk based internal auditing. PA 2010 .A1 (IIA 2004) states that internal audit’s activities should be based on risk assessment undertaken at least once annually. Concerning the enterprise risk management process itself, PA 2010 (IIA 2004) states that the internal audit activity should assist the organisation by identifying and evaluating significant exposure to risk and contribute to the improvement of risk management and control systems. It is clear that in this capacity, the internal audit activity will be acting in an advisory capacity, because they will be assisting management, and not assuming operational duties.

Practice advisory 2100 – 3 (IIA 2004) clearly delineates the responsibilities of management as opposed to those of internal audit. It states that risk management is a key responsibility of management who should ensure the risk management processes are in place and functioning properly. It further states that internal auditors assist management and the audit committee by examining, evaluating, reporting and recommending improvements on the adequacy and effectiveness of management’s risk processes. It also states that management and the board’s expectations of internal audit should be codified in the charters of the internal audit and the audit committee.(IIA 2004)

Standard 2110 (Institute of Internal Auditors 2004:14) states that “The internal audit activity should assist the organisation by identifying and evaluating significant exposures to risk and contributing to the improvement of risk management and control systems.”. It must be made very clear that management has the responsibility of identifying, analysing, measuring risk as well as designing, operating and maintaining a risk management system. The response to significant risks identified is usually incorporated in the internal control system which is also subject to internal audit scrutiny. This position is clarified in paragraph 2110.1A, (Institute of
Internal Auditors 2004:15) which states that “The internal audit activity should monitor and evaluate the effectiveness of the organisation’s risk management system.” No conflict of interests should therefore exist, as the internal auditor’s responsibility is to assess or evaluate and make recommendations to management. The auditor should therefore not be involved in implementing the design of the risk management system. As such, no conflicts will arise as long as the auditor sticks to his role.

Recent guidance on this issue has come in the form of an executive report issued by the Institute of Internal Auditors (IIA) and compiled in conjunction with the Risk and Insurance Management Society Inc. (RIMS) (IIA 2012). In this report, they advocate collaboration between the internal audit and risk management, in order to develop stronger risk management practices and meet stakeholders’ expectations. They emphasise that adequate safeguards should be put in place to ensure that the independence and objectivity of the internal auditor are not threatened. They also strongly recommend the adoption of the position paper produced by the IIA UK and Ireland (IIA UK and Ireland 2003), entitled “The role of internal auditing in enterprise risk management”. At the core of this paper is an 18 element “fan” graphic (Fig 2.8) depicting core roles of internal audit in enterprise risk management. (IIA UK and Ireland 2003).
On the left third of the fan are assurance activities, which fulfil the objective of giving assurance on risk management. On the centre are those roles which are adopted by internal audit in a consultative or advisory capacity. In this segment, it is necessary to ensure that sufficient safeguards are in place so that the independence and objectivity of internal auditors are not impaired. The further the internal auditor moves to the right in this segment, the greater are the safeguards required to ensure that independence and objectivity are not impaired. The IIA position paper (IIA 2009) suggests the following safeguards:
• It should be clear that management remains responsible for risk management.
• The nature of internal auditor’s responsibilities should be documented in the internal audit charter and approved by the audit committee.
• Internal auditing should provide advice, challenge and support to management’s decision making, as opposed to taking risk management decisions themselves.
• Internal auditing cannot also give objective assurance on any part of the enterprise risk management framework for which it is responsible. Such assurance should be provided by other suitably qualified parties.
• Any work beyond the assurance activities should be recognised as consulting engagement and the implementation standards related to such engagements should be followed. (IIA 2009)

The last third (on the right) consists of those responsibilities which should not be undertaken by internal audit, as they are the preserve of management. The risk maturity of an organisation determines which roles are assumed by internal auditors, generally moving from left to right. This model succinctly summarises the role of internal audit in risk management. (IIA 2009)

On the whole, professional guidance is very clear that internal audit should only act in an advisory or consultative role and not take management responsibilities in enterprise risk management.

There have been a number of studies on the involvement of internal audit in ERM, and the effect of this involvement on the independence and objectivity of internal auditors. In a comparative study, Sarens and de Beelde (2006b) interviewed CAEs of six Belgian and 4 USA companies, to determine how they perceived their role in ERM. In both countries, participants said internal auditor involvement in ERM was necessary to enhance risk
assessment and internal control practices. Burnaby et al (2007) in the CBOK also found that sixty-seven percent of the respondents were involved in ERM and a further twenty-five percent expected to be similarly involved within the next three years. This appears to indicate that involvement of internal auditors in ERM is gaining ground.

Gramling and Myers (2006) surveyed 361 global internal auditors to examine their adherence to roles recommended by the IIA. They found instances of involvement in inappropriate activities.

Fraser and Henry (2007) used interviews with finance directors, directors of risk management, audit committee chairs, and CAEs of five UK companies to examine mechanisms for identification and management of critical risks, and what roles internal audit and the audit committee could play. They found major involvement of internal audit in ERM as well as instances of internal audit having responsibility for ERM practices (in violation of IIA recommendations). They gave an example where the internal auditor was responsible for setting up the ERM system, which is normally a management responsibility. They recommended a separate function to be responsible for ERM, as well as a board committee to be responsible for ERM. These measures would enhance independence and accountability.

De Zwaan et al (2009) conducted a survey of 117 Australian Certified Internal Auditors (CIA) to examine if the involvement of internal auditors in ERM and their relationship with the audit committee had any impact on perceived independence. They found that internal audit involvement in ERM could negatively impact on their objectivity and result in reluctance to report weaknesses in ERM procedures. This finding is to be expected as the internal auditors would be auditing their own work (self review), and would be less willing to criticise their own work.
I could not find any previous research on the involvement of Zimbabwean internal auditors in ERM. This research set out to find out the role played by internal audit in risk management and how this affected their independence and objectivity.

2.3.5 Relations with the audit committee

The IIA standards (IIA 2004) recommend that the CAE should report to the Audit Committee of the board of directors, in order to maintain independence and objectivity. The audit committee comprises members of the board of directors. A properly constituted audit committee plays a very important role in ensuring that the internal audit activity receives adequate authority and resources to fulfil its responsibilities and in safeguarding the independence of the function. It can also assist by enabling the internal audit function to gain respect, recognition and cooperation from management. The internal audit function on the other hand assists the audit committee by providing an assurance service on the control, risk, and governance processes, over which the audit committee has oversight. The internal audit function also provides an educational service to the audit committee, and normally also checks information submitted to the audit committee by management or the external auditor for accuracy. This mutual interdependence and reciprocal strengthening is illustrated in the figure (fig 2.9) below: (Sarens and De Beelde 2005)
Consequently, there must be a close working relationship between the two bodies. It is therefore important for the audit committee to thoroughly understand the role of the internal audit function in an organisation in order for it to properly perform its oversight role. Because of this empowering role the audit committee has on Internal Audit, it is important to thoroughly understand its duties and responsibilities as well as the expectations of the various stakeholders. The Risk Management and Governance Board of the Canadian

**Source:** Sarens and De Beelde (2005) Interaction between internal audit and different organisational parties: an analysis of expectations and perceptions
Institute of Chartered Accountants issued a publication entitled “20 questions directors should ask about internal audit” to help board members, boards and audit committees who have or are contemplating having an internal audit function (Fraser and Lindsay 2007). Because of the importance of the relationship between these two bodies, these questions and the respective discussions are given below:

1. **Should we have an internal audit function?** (Fraser and Lindsay 2007).

Organisations that do not have internal audit are encouraged to seriously consider establishing one if the size, type of business, source of capital and risk factors warrant it. The decision to establish it should involve the CEO, CFO, and the Audit Committee. Criteria to consider includes the following: (Fraser and Lindsay 2007)

- The audit committee wants to get independent and objective assurance on the adequacy of internal controls from someone other than the CEO or CFO
- The CEO wants to get independent and objective assurance on the adequacy of internal controls from someone other than the CFO
- The CFO wants to get independent and objective assurance on the adequacy of internal controls from someone other than the line managers (Fraser and Lindsay 2007).

It is recommended that managements of organisations without internal audit functions review the need for this function periodically.

2. **What should our internal audit function do?** (Fraser and Lindsay 2007).

Each organisation must identify its own audit needs and use them to define the role of its internal audit function. Reference may also be made to the definition of internal auditing given by the IIA, and other textbooks on internal auditing. It is recommended that the Chief
Audit Executive in consultation with senior management and the Audit Committee establishes the scope of activities of the internal audit function and reduce this to writing in an audit charter, which should be periodically reviewed (Fraser and Lindsay 2007).

3. What should be the mandate of the internal audit function? (Fraser and Lindsay 2007).

Internal auditors need a mandate that provides the authority they need within a structure that supports their independence and objectivity. This is best done through a written audit charter, which is compatible with best current practices and approved by the board audit committee. Internal audit should not have operational accountability or perform any functions that would be subject to subsequent internal audit review (Fraser and Lindsay 2007).

4. What is the relationship between internal audit and the audit committee? (Fraser and Lindsay 2007).

The internal audit function is a major source of information and assurance to the Audit Committee on internal financial controls and other risk management activities and should have a functional reporting relationship with the audit committee. The Chief Audit Executive should have direct access to the Chair of the Audit Committee and attend Audit Committee meetings to present the audit plan for approval and to report audit findings. The Audit Committee charter to include provisions for: (Fraser and Lindsay 2007)

- The audit committee to review and endorse the appointment or replacement of the Chief Audit Executive.
- The internal audit charter to be compatible with that of the Audit Committee. The internal audit charter to be approved by the Audit Committee periodically.
- Internal audit to provide the Audit Committee members and senior management with independent, objective views on risk and internal controls within the organisation.
• The Chief Audit Executive to attend Audit Committee meetings.
• The Chief Audit Executive to meet privately with the Chair of the Audit Committee to discuss sensitive issues.
• The Chief Audit Executive to report the results of major activities and key findings and issues to the Audit Committee.
• The Chief Audit Executive to meet with the Audit Committee periodically without management present.
• The Chief Audit Executive to have unrestricted access to the chair of the audit committee (Fraser and Lindsay 2007).

5. To whom does internal audit report administratively? (Fraser and Lindsay 2007).

The CAE reports functionally to the Audit Committee, but must report to someone administratively for the purpose of pay, performance, space and equipment and related matters. This person should be selected on the basis of his or her ability to respect and give effect to the independence of internal audit rather than for the position he or she holds. It is recommended that the Chief Audit Executive reports administratively to the Chief Executive Officer and that the Audit Committee reviews this administrative relationship annually (Fraser and Lindsay 2007).

6. How is the internal audit functions staffed? (Fraser and Lindsay 2007).

The organisation has three alternatives: (Fraser and Lindsay 2007)

• In-house resources – assign responsibilities to a corporate internal audit department or
• A fully outsourced internal audit function reporting to a designated executive – hiring an external firm.
• A combination of the above.
The Chief Audit Executive in consultation with senior management and the Audit Committee determines the most cost effective mix of in-house and outsourced resources based on the skills required for the approved audit plan. The size is benchmarked against similar organisations. (Fraser and Lindsay 2007).

7. **How does internal audit get and maintain the expertise it needs to conduct its assignments?** (Fraser and Lindsay 2007).

Internal auditing calls for a diverse set of knowledge, skills and experience, to provide the necessary control assurance and related advice to the Audit Committee. Qualifications for internal auditors include: (Fraser and Lindsay 2007)

Professional accounting designations like Chartered Accountants (CA), Association of Certified Chartered Accountants (ACCA), and Certified Public Accountants (CPA)

Internal audit qualifications like Certified Internal Auditor (CIA) and Certified Information Systems Auditor (CISA)

Qualifications in specialised areas such as Certified Environment Auditors (CEA)

Other disciplines like engineers, economists etc. (Fraser and Lindsay 2007).

It is recommended that internal audit recruits only people with appropriate qualifications, experience and industry knowledge and promotes and budgets for continuing professional development. Internal audit should report to the Audit Committee on staff capabilities and adequacy. (Fraser and Lindsay 2007).

8. **Are the activates of internal audit appropriately coordinated with those of the external auditors?** (Fraser and Lindsay 2007).
External auditors rely on the work of internal auditors if they are satisfied with the scope, audit approach, standards and results of the internal audit function, as well as the objectivity of the internal auditors. The internal and external auditors should work in collaboration to achieve the best possible value in audit coverage. The Audit Committee should ask both internal and external audit if they are satisfied with the extent of the cooperation and compare answers. It is recommended that the audit committee reviews the plans of both the internal and the external audit and questions any situations of duplication or inadequate coverage. Internal audit staff should be used by the external auditors only if it benefits the organisation, and not at the expense of other valuable work. (Fraser and Lindsay 2007).

9. How is the internal audit plan developed? (Fraser and Lindsay 2007).

The internal audit plan is key to matching the work of internal audit to the needs of and expectations of the audit committee, external audit and senior management, and provides a basis for evaluating internal audit performance. The Chief Audit Executive prepares a risk based annual plan, which includes staff resources, after seeking management and external auditors’ inputs. The Audit Committee reviews and approves the internal audit plan after ensuring that it covers all significant risks. The Chief Audit Executive informs the Audit Committee of any major changes in the audit plan during the year. (Fraser and Lindsay 2007).

10 What does the internal audit plan not cover? (Fraser and Lindsay 2007).

Ideally, the Chief Audit Executive, senior management and the board should ensure that all significant risks are covered, and agree on those areas of risk that will not be audited and the reasons thereof. The audit committee should be alert to the danger of underfunding the internal audit function (Fraser and Lindsay 2007).
11. How are internal audit findings reported? (Fraser and Lindsay 2007).

Audit reports should be action-oriented, balanced, in writing and include the scope and objectives of the audit, the findings as well as recommendations for improvement. Where the volume is high the Chief Audit Executive prepares an executive summary for senior management and the Audit Committee. Periodically, the Audit Committee requests for detailed reports to understand the methodology and quality of reporting. (Fraser and Lindsay 2007).

12. How are corporate managers required to respond to internal audit findings and recommendations? (Fraser and Lindsay 2007).

The Audit Committee and senior management should play their important role of monitoring and enforcing commitment to take corrective action recommended by internal audit. Open support and monitoring of internal audit activities by the Chief Executive Officer and Audit Committee can help ensure that all managers cooperate with internal audit. Support in accordance with the internal audit charter should be provided by: (Fraser and Lindsay 2007)

- Maintaining the independence of internal audit.
- Ensuring line management’s cooperation in the performance of audits.
- Requiring prompt responses and action from management on audit reports.
- Recognising and promoting internal audit as a value added activity.
- Refraining from using internal audit resources for non audit purposes that cut unto audit time or create a conflict of interest and
- Keeping internal audit informed of key plans and changes to the risk and control profile of the organisation’s policies and procedures. (Fraser and Lindsay 2007).
It is recommended that management provide plans and dates for implementation before or soon after the audit report is issued, and accepts responsibility for monitoring corrective action on weaknesses reported by internal audit. The Chief Executive Officer should establish and maintain a formal follow up process for monitoring and ensuring that management actions have been effectively implemented. The Audit Committee should receive periodic reports on high risk recommendations which have not been implemented. (Fraser and Lindsay 2007).

13. **What services does internal audit provide in connection with fraud?** (Fraser and Lindsay 2007).

While prevention and deterrence of fraud is the responsibility of management, internal audit should develop programs and procedures to evaluate the internal controls that have been established by management to manage risk of fraud. It is recommended that internal audit includes fraud as a risk to be evaluated and included in the audit plan. (Fraser and Lindsay 2007).

14. **How do you assess the effectiveness of your internal audit function?** (Fraser and Lindsay 2007).

The internal audit function should use the results of their self assessment processes, together with feedback from the external auditors and other stakeholders, to monitor trends over time and achieve continuous improvement in the practices and procedures. It is recommended that the Chief Audit Executive develops performance measures for the internal audit function and agrees them with the audit committee, and that there is an external quality review of the internal audit function at least once in every five years. The results of these evaluations should be reported to the audit committee. The internal audit function should also benchmark its operations and effectiveness with those of other organisations. (Fraser and Lindsay 2007).
15. Does internal audit have sufficient resources? (Fraser and Lindsay 2007).

This is an important and sensitive question to be answered by the Chief Audit Executive. Where the answer is no, the Chief Audit Executive should provide the audit committee with a comprehensive analysis of the situation and steps taken to resolve the problems with management. Resources may be insufficient because: (Fraser and Lindsay 2007)

- Management does not respect the role and contribution of internal audit.
- Management include internal audit in general under funding to meet short-term forecasts.
- Management diverts internal audit resources to manage short term goals, operational crises and special projects. (Fraser and Lindsay 2007).

The internal audit function needs to attract and retain skilled staff, and the audit committee should be aware of any excessive turnover which may be an indication of poor management or lack of respect for the function in the organisation. Insufficient staff turnover may also be due to staff not progressing in their careers and becoming stale or too close to management. The audit committee should ask the Chief Executive Officer about audit resources and get his or her perspective and recommendations, as well as seek management’s explanations for any resource shortages. (Fraser and Lindsay 2007).

16. Does the internal audit function get appropriate support from the Chief Executive Officer and senior management team? (Fraser and Lindsay 2007).

There should be a good working relationship and mutual respect between internal audit on the one hand and the Chief Executive Officer and the management team on the other, and this includes: (Fraser and Lindsay 2007)

- Support for audit findings – by addressing them in a timely manner.
• Inclusion of the Chief Audit Executive in communications and forums of the senior management to keep him or her informed of the strategies and business plans of the organisation.

If the Chief Audit Executive answers “no” to this question, the audit committee should consider all the evidence and assess whether further action is needed (Fraser and Lindsay 2007).

17. Are you satisfied that this organisation has adequate internal controls over its major risks? (Fraser and Lindsay 2007).

When preparing a report to the board on the soundness of the design, implementation and effectiveness of the system of internal control, the audit committee seeks information and opinions from a wide range of sources including, the CEO, Chief Risk Officer, the external auditors and the Chief Audit Executive. The Chief Audit Executive’s response to this question may involve integrating and summarising the results of audit work and related activities such as risk and control self assessments, internal control surveys, consulting projects and involvement in major projects and new systems. (Fraser and Lindsay 2007).

18. Are there any other matters that you wish to bring to the audit committee’s attention? (Fraser and Lindsay 2007).

If there are any issues relating to controls, the integrity of management or the quality of financial reporting that are not addressed in the internal audit reports, the audit committee expects the Chief Audit Executive to raise them and explain why these matters were not formally raised in the internal audit reports. The audit committee should reach out and build a level of trust with the Chief Audit Executive which will permit honest and appropriate
communication of sensitive issues and opinions related to risk and control. (Fraser and Lindsay 2007).

19. Are there other ways in which internal audit and the audit committee could support each other? (Fraser and Lindsay 2007).

This question provides an opportunity for the Chief Audit Executive and the audit committee to discuss such matters as improving audit reporting to the committee and using internal audit to provide training on risk and control aspects of the business either for new members to the audit committee or the committee as a whole. (Fraser and Lindsay 2007).

20. Are we (the audit committee) satisfied with our internal audit function? (Fraser and Lindsay 2007).

Further questions that the audit committee could ask itself or use in discussions after meetings with the Chief Executive Officer, Chief Audit Executive, and external auditors are: (Fraser and Lindsay 2007)

- How well does the Chief Audit Executive respond to probing by the Audit Committee?
- How well respected is the Chief Audit Executive by senior management and how healthy is the tension between them?
- How well respected is the Chief Audit Executive by the external auditors and how healthy is the tension between them?
- How often do we get surprises where something that the internal audit has audited subsequently reveals control problems that were not identified by their reports?
- Does the Chief Audit Executive provide adequate assurance in areas requested by the audit committee?
• Does internal audit Chief Audit Executive bring forward significant issues to the audit committee that might not otherwise be disclosed to the committee? Ideally these should have been raised first by management and their identification attributed to the internal audit function

• Is the Chief Audit Executive respected within the auditing profession? (e.g. frequent speaker, writing articles) (Fraser and Lindsay 2007).

The authors concede that while these questions do not represent an exhaustive checklist, but assist directors with a basis for critically assessing answers they get and digging deeper as necessary, they summarise current thinking on the issues and practices of leading organisations. (Fraser and Lindsay 2007). I believe that any audit committee member worth his or her salt should be able to ask all the questions and get appropriate answers. By virtue of their responsibilities, audit committee members should have a thorough and current knowledge of the entity’s operations as well as risks facing the entity and how they are managed. The audit committee must influence the tone at the top and ensure organisation-wide independence, respect and support for the internal audit function. It is necessary to ask tough questions and get answers.

It is necessary to examine the composition and responsibilities of the audit committee, as well as its relationship with the internal audit function, in order to determine its role in safeguarding the independence of the internal auditors.

The audit committee is perhaps the most important board committee as is tasked with the oversight of the financial reporting, risk management, internal control, compliance, ethics, management, internal and external auditors. (Smith guidance 2005).
In order to appreciate the importance of this committee one has to look at its responsibilities. The following list of some of the responsibilities is taken from a sample audit charter provided by the Institute of Internal Auditors (IIA 2009):

Financial statements

- Reviewing significant accounting and reporting issues and understanding their impact on the financial statements. These issues include:
  - Complex or unusual transactions and highly judgemental areas;
  - Major issues regarding accounting principles and financial statement presentations, including any significant changes in the company’s selection or application of accounting principles;
  - The effect of regulatory and accounting initiatives, as well as off-balance sheet structures, on the financial statements of the company;
- Review analyses prepared by management and/or the independent auditor setting forth significant financial reporting issues and judgements made in connection with the preparation of the financial statements, including analyses of the effects of alternative GAAP methods on the financial statements;
- Review with management and the external auditors the results of the audit, including any difficulties encountered. This review will include any restriction on the scope of the independent auditor’s activities or on access to required information and any significant disagreements with management.
- Discuss the annual audited financial statements and quarterly financial statements with management and the external auditors. (IIA 2009)

Internal controls
• Consider the effectiveness of the company’s internal control system, including information technology security and control;

• Understand the scope of internal and external auditors’ review of internal control over financial reporting, and obtain reports on significant findings and recommendations together with management’s responses. (IIA 2009)

Internal auditing

• Review with management and the chief audit executive the charter, plans, activities, staffing and organisational structure of the internal audit function;

• Ensure there are no unjustified restrictions or limitations and review and concur in the appointment, replacement or dismissal of the chief audit executive;

• Review the effectiveness of the internal audit function including compliance with the IIA’s International Professional Practice of Internal Auditing (IPPF);

• On a regular basis, meet separately with the chief audit executive to discuss any matters that the committee or internal audit believes should be discussed privately. (IIA 2009)

External auditing

• Review the external auditor’s proposed audit scope and approach, including coordination of audit effort with internal auditing.

• Review the performance of the external auditors, and exercise final approval on the appointment or discharge of the auditors. In performing this review, the committee will:

  ➢ At least annually, obtain and review a report by the independent auditor describing the firm’s internal quality control procedures; any material issues raised by the most recent internal quality control review or peer review, of the firm, or by any inquiry or investigation by governmental or professional authorities, within the preceding five
years, respecting one or more independent audits carried out by the firm, and any steps taken to deal with any such issues; and (to assess the auditor’s independence) all relationships between the independent auditor and the company;

- Take into account the opinions of management and internal auditing;
- Review and evaluate the lead partner of the independent auditor;
- Present its conclusions with respect to the external auditor to the board. (IIA 2009)

- Ensure the rotation of the lead audit partner every five years and other audit partners every seven years, and consider whether there should be regular rotation of the audit firm itself;
- Present its conclusions with respect to the independent auditor to the full board;
- Set clear hiring policies for employees or former employees of the independent auditors;
- On a regular basis, meet separately with the external auditors to discuss any matters that the committee or auditors believe should be discussed privately. (IIA 2009)

Compliance

- Review the effectiveness of the system for monitoring compliance with laws and regulations and results of management’s investigation and follow up (including disciplinary action) of any instances of noncompliance;
- Review the findings of any examinations by regulatory agencies and any auditor observations;
- Review the process for communicating the code of conduct to company personnel, and for monitoring compliance therewith;
- Obtain regular updates from management and company legal counsel regarding compliance matters. (IIA 2009)
Reporting responsibilities

- Regularly report to the board of directors about committee activities and issues that arise with respect to the quality or integrity of the company’s financial statements, the company’s compliance with legal or regulatory requirements, the performance and independence of the company’s independent auditors, and the performance of the internal audit function;
- Provide an open avenue of communication between internal audit and the external auditors, and the board of directors;
- Report annually to the shareholders, describing the committee’s composition, responsibilities and how they were discharged and any other information required by rule, including approval of non-audit services. (IIA 2009)

Other responsibilities

- Discuss with management the company’s major policies with respect to risk assessment and risk management;
- Perform other activities related to the charter as requested by the board of directors;
- Institute and oversee special investigations as needed;
- Review and assess the adequacy of the committee charter annually requesting board approval for proposed changes, and ensure appropriate disclosure as may be required by law or regulation;
- Confirm annually that all responsibilities outlined in the charter have been carried out;
- Evaluate the committee’s and individual members’ performance at least annually.
Having looked at the responsibilities of the audit committee, it is necessary to look at the skills and other attributes that the audit members should possess in order to carry out their duties efficiently and effectively. (IIA 2009)

2.3.5.1 Skills, experience and training of audit committee members

The Blue Ribbon Committee Report (1999) emphasizes the importance of board membership, by noting that it should not just be a reward for making it in the corporate world, but requires appropriate attitudes, capabilities and demands time and attention. Personal characteristics required include integrity, a sense of accountability, a history of achievement, and the ability to ask tough questions. Core competences include financial literacy, experience with organisations, leadership and strategic thinking.

Because of the nature of the responsibilities of the audit committee discussed above, its members should have the proper background and knowledge base. There is a need for members to be independent, as well as possess relevant current business experience and financial expertise. Several scholars and corporate governance guidelines (BRC 1999, De Zoort 1998, GAO 1991, Kalbers and Forgarty 1993, Lee and Stone 1997, NACD 2000, Treadway Commission 1987) have questioned the ability of audit committee members to carry out their responsibilities effectively without these attributes. It is pertinent to note that these requirements have now been included into the codes of corporate governance bodies (Blue Ribbon Commission 1999; The Smith Guidance 2005; Cadbury 1992) these codes recommend that members of the audit committee should be independent non-executive directors, have business experience and financial literacy, and at least one member should have recent financial expertise.

Financial literacy means the ability to read and understand fundamental financial statements, including the statement of financial position, the income statement or statement of
comprehensive income, and the statement of cash flows (BRC1999). This can be achieved through company sponsored training programs, within a reasonable period after appointment. Financial expertise is taken to mean membership of one of the professional accounting bodies or experience in corporate financial matters as a Chief Executive Officer or Chief Financial Officer. The corporate governance guidelines also emphasize the induction and training of members of the audit committee on an ongoing basis to keep them abreast of current developments in finance, accounting and corporate governance. The main impediment to standard implementation of these guidelines is the lack of legislative backing. As a result each organisation implements them as it sees fit (Christopher et al 2009).

A number of scholars have examined various aspects of the audit committees. Goodwin and Yeo (2001) conducted a survey of 65 Singaporean internal auditors, to find out how the relationship between internal audit and the audit committee affected the independence of internal auditors. They found out that interaction between internal audit and the audit committee was greater when the audit committee comprised independent directors. This seemed to enhance the independence of internal auditors. This finding buttresses the requirement that the audit committee should comprise of independent directors.

Ranghundanan, Read and Raman (2001) conducted a survey of 114 internal auditors in the United States of America to examine the association between the composition of the audit committee and its interaction with internal audit. They found that in audit committees where at least one of the members had financial expertise, the CAE was provided private access, meetings with the CAE were longer and there was review of the internal audit program, results and interaction with management. This finding reinforces the requirement that there should be at least one financial expert in the audit committee.
Goodwin (2003) conducted a survey of 120 internal auditors in Australia and New Zealand, to explore the impact of audit committee and financial expertise on the audit committee’s relationship with internal audit. He found that independence of the committee was associated with process issues such as hiring and firing of the CAE, and financial expertise was associated with review of internal audit work. These findings illuminate the importance of independence of the audit committee, which in turn can enhance the independence of the internal audit function.

Attribute standard 2060 (IIA 2004) deals with reporting to the board and senior management. It states that the chief audit executive should report periodically to the board and senior management on the internal audit activity’s purpose, authority, responsibility, and performance relative to its plan. Reporting should also include significant risk exposures and control issues, corporate governance issues, and other matters needed or requested by the board and senior management.

Practice advisory 2060-1 (IIA 2004) requires periodic reports by the chief audit executive throughout the year, highlighting significant observations and recommendations and any deviation from approved work schedules, staffing plans and financial budgets and reasons thereof. Significant observations are those that could adversely affect the organisation and include irregularities, illegal acts, errors, inefficiencies, waste, conflict of interests and control weaknesses. The board should also be advised of senior management’s decisions on all significant observations.

Practice advisory 2060-2 (IIA 2004) deals with the relationship with the audit committee, and is a summary of what the Institute of Internal Auditors considers to be important aspects and attributes of an appropriate relationship between the audit committee and internal audit. It adds that the chief audit executive can ensure an effective relationship by:
• Assisting the audit committee to ensure that its charter, activities and processes are appropriate to fulfil its responsibilities;

• Ensuring that the charter, role, and activities of internal audit are clearly understood and responsive to the needs of the audit committee and the board

• Maintaining open and effective communication with the audit committee and the chairperson. (IIA 2004)

With regard to effective communication, the advisory considers that the chief audit executive is the key, trusted advisor to the audit committee. In this core role, the chief audit executive should assist the audit committee to gain a complete understanding of the organisation’s operations. (IIA 2004) This will entail, among other things:

• Meeting privately with the audit committee to discuss sensitive issues;

• Providing periodic reports and an annual summary of results of audit activities;

• Keeping the audit committee informed on emerging trends in internal auditing and;

• Reviewing information submitted to the audit committee for completeness and accuracy. (IIA 2004)

The Smith Guidance (2005) specifies the following responsibilities of the audit committee: monitoring and reviewing the effectiveness of the internal audit function; approval of the internal audit annual work plan and budget; approval of the appointment and dismissal of the chief audit executive. The review of internal audit also includes: ensuring the chief audit executive has direct access to the board chair and audit committee chair, and is accessible to the audit committee; reviewal and assessment of internal audit annual work plans; receiving reports from internal audit periodically and monitoring management’s responses to audit findings and recommendations; meeting the head of internal audit in the absence of management at least once a year. (Smith Guidance 2005). Another important duty is to
approve the internal audit budget and ensure that the function has adequate resources to effectively discharge its responsibilities. In this respect, a good relationship between the CAE and the audit committee enhances the performance of both (Gramling et al 2004). This view is also supported by Goodwin and Yeo (2001), Turley and Zaman (2004) and Bariotta (1999).

Practice advisory 2060-2 (Institute of Internal Auditors 2004) mentions 3 key areas to effective relations with internal audit: (1) Internal audit should assist the audit committee to ensure that its charter, activities and processes are appropriate; (2) The audit committee to ensure the internal audit charter, role and activities are clearly understood and responsive to the needs of the audit committee. (3) The audit committee to monitor open an effective communication. In respect to communication, the practice advisory recommends: regular private meetings between the audit committee and the chief audit executive to discuss sensitive issues, that the chief audit executive should issue periodic activity reports, as well as an annual summary of activities, and that the audit committee discuss fulfilment of the audit committee’s information requirements together with external auditors. These requirements tally with those of the corporate governance bodies.

This study sought to determine the degree of compliance with these standards and corporate governance guidelines in Zimbabwe in a bid to see how this impacts on independence and objectivity of the internal auditor.

2.3.6 Relations with external auditors

This is an issue that has not attracted the attention of many scholars (Brown 1983; Schneider 1984; Edge and Farley 1991; Krishnamoorthy 2002). Traditionally, internal and external auditors have always worked closely together, especially in the planning stages of the audit process, in order to ensure adequate audit coverage. As a result, external auditors usually consider the work performed by internal auditors in determining the nature, timing, and
extent of their procedures (Schneider 1985). This interaction between internal and external auditors has been considered by a number of researchers. (Felix, Gramling and Maletta 2001; Carey, Creswell and Simnet 2000; Lempe and Sutton 1994; Stein, Simunic and O’Keefe 1994; Brody, Golen and Reckers 1998). Effective communication between the two parties is of vital importance in order to ensure audit quality and to realise benefits of this collaboration. (Lempe and Sutton 1994; Haron, Chambers, Ramsi, and Ishak 2004; Brody, Galen and Reckers 1998; Felix, Gramling and Maletta 2001). Financial benefits in the form of a reduction of audit fees can also be realised if the external auditor relies on the work of internal audit. Felix, Gramling and Maletta (2005) appear to have confirmed this when they found that audit fees were reduced by approximately eighteen percent when external audit coordinated their work with internal audit. However, external auditors should not be allowed to dictate what should go into the annual work plan of the internal auditor as this would impair internal audit independence. It is common practice for external auditors to use the work of internal auditors when they are carrying out their audits. (Moeller 2005)

2.3.6.1 Using the work of internal auditors

IFAC provisions

ISA 610 Using the work of internal auditors (IFAC 2009) - deals with factors to be considered when the external auditor wants to use the work of internal auditors. It states that while the objectives of the internal audit function and the external auditor are different, some of the ways in which the two achieve their goals may be similar. In determining whether and to what extent to use the work of internal auditors, the external auditor shall determine:

- Whether the work of internal auditors is likely to be adequate for audit purposes;
• If so, the effect of the use of the work of the internal auditor on the nature, timing or extent of the external auditor’s procedures. (IFAC 2009)

In determining whether the work of internal auditors is likely to be adequate for purposes of the audit, the external auditor shall evaluate:

• the technical competence of the internal audit function;
• the technical competence of the internal auditors;
• whether the work of the internal auditors is likely to be carried out with due professional care; and
• whether there is likely to be effective communication between the internal auditors and the external auditor. (IFAC 2009)

With regard to objectivity, the external auditor will consider the following factors:

• the status of the internal audit function within the entity and the effect that status has on the ability of internal auditors to be objective;
• whether the internal audit function reports to those charged with governance or an officer with appropriate authority and whether internal auditors have direct access to those charged with governance;
• whether the internal auditors are free from any conflicting responsibilities;
• whether those charged with governance oversee employment decisions relating to the internal audit function;
• whether there are any constraints or restrictions placed on the internal audit function by management or those charged with governance;
• whether and to what extent management acts on recommendations of the internal audit function and how such action is evidenced (IFAC 2009)
2.3.6.1.2 AICPA provisions

Statement on Auditing Standard No. 65 (SAS No.65) “The auditors consideration of the internal audit function in an audit of financial statements” (AICPA 1990) contains the AICPA’s pronouncements regarding the coordination of external audit and the internal audit function. The standard discusses procedures to be followed when coordinating with internal auditors. These procedures are depicted on and involve obtaining an understanding of the internal audit function, assessing its competence and objectivity, coordinating work, and evaluating the effectiveness of this work. This process is shown on figure 2.10.
Fig. 2.10 Internal audit decision flowchart

Source: Moeller (2005) Brink’s internal auditing
Other suggested ways of coordination include, holding periodic meetings, providing access to working papers, and discussing possible accounting and auditing problems.

These procedures are briefly explained below.

**Obtain an understanding of the internal audit function**

The external auditor determines whether internal audit reports to proper levels in the organisation, if audits are properly planned and supervised and that the provisions of the IIA are observed in the performance of audits. (AICPA 1990)

**Assess competence and objectivity of internal audit**

The external auditor assesses the competence of individual internal auditors and the quality of their work. This entails consideration of their educational qualification, professional certifications and internal audit experience as well as the programs for continuing professional development. The quality of working papers as well as the degree of supervision of audit work are also assessed. (AICPA 1990)

**Consider the effects of internal audit on the external auditor’s plan**

The external auditor considers how internal audit can contribute to the overall audit objectives.

**Plan and coordinate work with internal audit**

When the external auditor is satisfied that the internal audit function meets the external auditor’s quality standards, then audit work can be planned and coordinated (AICPA 1990)

**Evaluate and test the effectiveness of internal audit work**

The external auditor will evaluate the work of the internal auditors working with them.
Both professional bodies encourage coordination of the work of internal and external auditors. Some of the advantages of this practice are the avoidance of duplication and excessive demands on organisational personnel (Moeller 2005), effective audit coverage and reduced external audit fees. The procedures for evaluating the internal audit function are very similar to those of the IFAC. It can be seen that external auditors play a very important role of evaluating the independence, objectivity and effectiveness of the internal audit function, because they are required to assess these aspects before they can use the work of internal auditors. The external auditors are therefore a very important source for determining the independence and objectivity of internal auditors.

This study tried to find out to what extent external auditors use the work of internal audit, and this would give an indication of how the external auditors rate the independence of the internal audit function.

2.4 Summary

This chapter dealt with the review of related literature. The theoretical framework informing the study was explained, and a summary of major researches on the topic under review was given. This was followed by a discussion of independence and objectivity, which was divided into two broad categories, namely Organisational independence and Individual objectivity. On organisational independence, the discussion centred on the reporting lines for the chief audit executive (CAE), hiring and firing of the CAE, inputs into, and approval of the internal audit budget and annual work plan, as well as the use of internal audit as a training ground. Relations with the audit committee and the external auditors were also discussed. The discussions entailed seeking authoritative guidance from the profession of internal auditing, contained in the IPPF and other authoritative pronouncements. This was compared
with practice on the ground as revealed by previous research and observations by practitioners and scholars.

On individual objectivity, guidance of the IPPF was discussed, the threats to individual objectivity were stated and the methods of mitigating the threats were discussed. Relations of internal auditors with the audit committee and with external auditors were the last to be discussed.

Standards, regulations and codes of ethics of professional accounting and auditing bodies, including AICPA, IFAC, INTOSAI were reviewed, to learn lessons about how they view audit independence, threats to independence of auditors and how these threats were managed by the respective bodies. In respect of external auditors, literature relating to management of conflict of interests of auditors as a result of performance of non-audit services to their audit clients was studied. The aim was to learn lessons from their experiences, as internal auditors faced a similar situation in respect of their involvement in risk management and consulting assignments. Relevant previous studies and comments by scholars and writers were included in the examination.

Corporate governance codes (Cadbury, Smith guidance) were also studied to determine the duties, responsibilities and authority they prescribe for internal auditors as well as their requirements for independence of internal auditors. Of particular importance was the issue of audit committees, who are the guarantors of internal auditors’ independence. The composition of the audit committee, as well as qualifications and attributes of their members and the independence of the body were explored. Relevant literature by writers and scholars on this issue was also examined.
Enterprise risk management frameworks (COSO, ISO, etc.) were referred to, including relevant comments from scholars, to determine to what extent internal auditors can be involved in such activities without compromising their independence.

The next chapter deals with the research methodology employed in this study.
CHAPTER 3

Research Methodology

Introduction

This chapter covers the research methodology employed in this study. It is necessary to choose a suitable approach, in order to achieve the objectives of the study. There are two main approaches to research, namely, the quantitative and the qualitative approaches, with a third hybrid one, combining the two approaches, which is generally known as the Mixed methods (Guba and Lincoln 1994; Myers 2009; Denzin and Lincoln 2005). The underlying philosophy for this study, interpretivism, is discussed first. This is followed by discussion of the qualitative method, which is the chosen one for this study. This is followed by descriptions of the population the sample, and discussion of the sampling method that was used in this study. Research instruments, that is, questerviews, interview guides and focus group discussion guides are discussed next. The chapter ends with data analysis.

3.1. The research philosophy

The underlying philosophy for this study is interpretivism. Myers (1997) states that interpretive studies attempt to understand phenomena through meanings that people assign to them. The study examined the independence of internal auditors in parastatals. This could best be done by enquiring into how the internal auditors understood this independence, what their experiences and expectations were and interpreting these to determine the meaning they ascribe to their independence as internal auditors. It was felt that such an inquiry would be best conducted under the chosen philosophy. Interpretivism was chosen, because under this philosophy, the researcher was able to interact and have dialogue with the participants. This was necessary, in order for the researcher to have a clear and in-depth knowledge of the
participants’ views, feelings, expectations, and suggestions on any areas considered deficient relating to the independents of internal auditors. The philosophy allowed the researcher to understand the worldview of the participants, and be able to accurately describe it. This study investigated things like independence, relationships between internal auditors and auditees/CEOs/Audit Committees, which cannot be accurately measured and given a numerical value. In such instances, interpretivism is the most suitable philosophy as it is concerned with understanding meanings given to phenomena by the participants.

3.2 The qualitative method

In this study, the qualitative method was adopted. According to Berg (2001) quality refers to the what, how, when, where of a thing. Qualitative research therefore refers to the meanings, concepts, definitions, characteristics, symbols and holistic in-depth descriptions of things (Veal 2005). It is conducted in the natural settings of the problem. The researcher is concerned with representing the richness, texture and feeling of raw data, and the inductive approach is used to develop insights within the data collected (Neuman 2003; Gall, Borg and Gall 1996; Umaru 2009).

Denzin and Lincoln (1994) opine that qualitative research focuses on interpretation of phenomena in their natural surroundings to make sense in terms of the meanings people attribute to these settings. They go on to state that this involves collecting information about personal experience, introspection, life story, interviews, observations, historical, interactions and visual text which are significant moments and meaningful in people’s lives.

Merriam (1998) states that qualitative research is characterised by an understanding of the meaning people have constructed in which the researcher is the primary instrument of data collection and analysis and usually involves fieldwork and primarily employing an inductive
strategy focusing on process, meaning and understanding resulting in a richly descriptive product. Creswell (1998:52) states that “…researchers look for essentials, invariant structure (or essence) or the central underlying meaning of the experience and emphasise the intentionality of consciousness where experiences contain both outward appearance and inward consciousness based on memory, image and meaning” Patton (2002) on the other hand regards qualitative research as attempting to understand the unique interaction in a particular situation, with the purpose of not necessarily being able to predict what might occur, but rather, to understand in-depth the characteristics of a situation and meaning brought by participants and what is happening to them at the moment, the aim being to truthfully present findings to others who are interested in the subject of the research. Pope and Mays (1995) state that qualitative researchers study things in their natural surroundings in an effort to discover the meanings seen by those who are being researched or participants rather than that of the researcher. This is referred to as the emic perspective by Gall, Borg and Gall (1996).

3.2.1. Strengths of the qualitative method

From the above definitions, it is clear that qualitative research is an interactive process shaped by both the researcher’s and the participants’ experience and perceptions among other things, and is interpretive in that it seeks to find and explain meanings attributed to phenomena surrounding the participants, by the participants themselves. It is also based on context, and is tied to a particular setting or population. Because it produces contextually rich information and focuses on a particular situation, qualitative research is useful in seeking solutions to problems in many sectors of the economy. This being the case, the qualitative research was the regarded as more appropriate for the present research. (Creswell 2008; Denzin and Lincoln 2005).
This approach was chosen because of its ability to facilitate the exposure of both the situation as it exists, and the reasons for that situation. It was also necessary to capture the perceptions, feelings and opinions of the participants in this study, and the qualitative approach was well placed to capture these aspects. This study involves concepts that cannot be easily measured and be given a numerical value. Such things as the independence, relationships between internal auditors and other corporate governance arms, and experiences of internal auditors cannot be accurately measured, but can be studied and described using the qualitative method. The qualitative method was also chosen because it allowed the researcher to interact with the participants and get all the information he required direct from the participants, which would ensure the accuracy of data obtained.

3.2.2. Challenges of the qualitative method

The fact that the researcher is the main instrument in both data collection and data analysis is usually considered a weakness in that the quality of the research heavily depends on the qualities of the researcher (bias, intellect skills, etc). Massive amounts of data are also produced in the qualitative method (Veal 2005) and the main challenge is to reduce the volume, by identifying the significant patterns and reporting the essence of what the data reveals (Silverman 1993: Miles and Huberman 1994). The researcher was aware of the challenges and measures taken to address them are detailed in paragraph 3.2.3 below.

3.2.3. Measures taken to address the challenges of the qualitative method

To address the weaknesses associated with the researcher being the main instrument in both data collection and data analysis, clear research objectives as set out in paragraph 1.13 and clear research questions as set out in paragraph 1.14, observance of high standards of ethics described in paragraphs 1.21 – 1.21.4 as well as well thought out data collection and data analysis procedures explained in paragraphs 3.7 - 3.8.2.8 were employed in this study. To
respond to the challenge in respect of massive amounts of data, clear research objectives were formulated, and there was a proper focus in data collection, as well as a disciplined approach to data analysis. The use of multiple sources facilitated triangulation (Stake 1995), which ensured accuracy of findings, by comparing data obtained from different sources.

3.3 Research Design

The case study design was used in this study. Yin (1984:23) defines a case study as “…an inquiry that investigates contemporary phenomenon within its real-life context; when the boundaries between phenomenon and context are not clearly evident; and in which multiple sources of evidence are used.” Denscombe (2007) agrees and opines that the case study focuses on just one or just a few instances of a particular phenomenon with a view to providing an in-depth account of events, relationships, experiences or processes occurring in that particular instance. He goes on to state that the spotlight is therefore focused on the individual instances rather than a wide spectrum, although the insights gained can have wider implications, which could not have been unearthed through another strategy, e.g. a survey.

Perhaps Denscombe (2007) aptly describes the characteristics of the case study when he states that it emphasises:

- Depth of the study rather than breadth;
- The particular rather than the general;
- Relationships rather than outcomes and end products;
- Holistic view rather than isolated cases;
- Natural settings rather than artificial situations; and
- Multiple sources rather than one research method.
It was also necessary to bind the case study, in order to avoid the pitfall of having too many objectives for one study, thereby ensuring that its scope remains reasonable (Yin 2003; and Stake 1995). Suggestions for doing this include: by time and place (Cresswell 2003), by time and activity (Stake 1995), and by definition and context (Miles and Huberman 1994). In this study, the research is bound by time (2010 to 2014), by activity (internal auditing), by the sector (parastatals), specific entities in that sector (the three parastatals) and by specific concepts (independence and objectivity).

3.3.1 Advantages of the case study design

This design was selected as it facilitated an in-depth study of the situation in the three organisations, in that the researcher was able to capture not only the situation that exists, but also the feelings and perceptions of the participants. Only information-rich participants were selected, so the sample was representative. Participants who did not have relevant information were automatically eliminated as being unsuitable for the study. Yin (2003) argues that the case study method ensures that the topic is well explored and the essence of the phenomenon are revealed.

3.3.2. Disadvantages of the case study

The main criticisms of this design centre around generalisability, because of the small number of cases examined and perceived researcher subjectivity.

Denscombe (2007) offers three arguments to counter this criticism:

- Although each case is in some respects unique, it is also a single example of a broader class of things;
- The extent to which findings from the case study can be generalised to other examples in the class depends on how far the case study example is similar to others of its type;
• Reports based on the case study include sufficient detail about how a case compares with others for the reader to make an informed judgement about how far the findings have relevance to other instances. (Denscombe 2007)

In line with these observations, in this study, decision to generalise or not to generalise which parts of the findings is left to the reader, after considering the similarities with other cases not covered by the case study. It is also important to note that this case study can form the basis from which a wider survey can be made, in search of replications which would make generalisation possible. (Denscombe 2007)

3.3.3. Measures taken to address weaknesses of the case study design.

Yin (1994) also suggests using multiple sources of evidence, and having the draft case study report reviewed by key informants. He also suggests that one method of achieving reliability is development of the case study protocol, and goes on to say that the case study protocol should have the following sections:

- An overview of the case study project (objectives, issues, topics being investigated)
- Field procedures (credential and access to sites, sources of information)
- Case study questions (specific questions the researcher must keep in mind during data collection)
- A guide for case study report (outline format for the report.)

It is also interesting to note that a number of researchers have used the case study design successfully, and these include Robert E Stakes, Helen Simons and Robert K Yin. The following six steps which bear a strong resemblance to Yin’s case study protocol can be drawn from their work:
• Determine and define the research questions;
• Select the case and determine data gathering and analysis techniques;
• Prepare to collect data;
• Collect data in the field;
• Evaluate and analyse data; and
• Prepare the report.

These steps were followed in the course of this study. Furthermore, triangulation of sources of data as well as verification of transcribed data by participants were used as a way of checking the validity of data obtained from participants.

3.4. Population of the study

The population of the study consisted of chief audit executives, chief financial officers, principal internal auditors, internal auditors, and managers employed in Zimbabwe’s 66 (www.mosep.gov.zw/list-of-parastals) parastatals.

3.5 Sample of the study

Only information-rich participants were included in the sample and table 3.1 shows the numbers included.
Table 3.1

Sample of the study

<table>
<thead>
<tr>
<th>Participant</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chief Audit Executives</td>
<td>3</td>
</tr>
<tr>
<td>Chief Financial Officers</td>
<td>3</td>
</tr>
<tr>
<td>Principal Auditors</td>
<td>5</td>
</tr>
<tr>
<td>Internal Auditors</td>
<td>13</td>
</tr>
<tr>
<td>Managers</td>
<td>9</td>
</tr>
<tr>
<td>Total</td>
<td>33</td>
</tr>
</tbody>
</table>

The sampling method used in the study is discussed next.

3.6 Sampling method

Sampling techniques can be divided into two broad categories. Probability sampling, is based on the probability theory which can predict the statistical likelihood of the occurrence of a random event. This sampling method is associated with quantitative research and sampling techniques such as random sampling. Non-probability sampling on the other hand does not use the probability theory, but is based on some other criteria such as the researcher’s judgement. (Gall, Borg and Gall 1996) It is associated with qualitative research, and such sampling methods as purposive, and convenience. (Gall, Borg and Gall 1996)

The choice of a sampling method depends on the aims of the researcher. When the aim is to ensure that the sample is representative of the population, in that certain characteristics are similar, probability sampling techniques are employed. Where the researcher is interested in some specific theoretical criteria, a non-probability technique like purposive sampling is
used. If the researcher wants the research to be easy and less costly, the non-probability technique of convenience sampling would most likely be ideal.

3.6.1 Purposive sampling

The sampling method used in this study is purposive sampling. Patton (1990:169) describes it as “…selecting information-rich cases for study in depth” As the name implies, purposive sampling is sampling with a purpose in mind. It starts with a purpose and then the sample is selected to include only information-rich participants for in-depth analysis of the central issues under study (Maree, 2007). This is a type of non-probabilistic sampling that requires the researcher to use his subjective judgement drawing on theory (i.e. academic literature) and practice (the experience of the researcher) and the evolutionary nature of the research process (Maree, 2007). This method was selected because it facilitated a thorough examination of the independence of internal auditors, as well as their feelings and perceptions on the issue. The use of probability sampling techniques would not have captured the soft aspects of the study. The sample selected for this study had an abundance of information on the independence of internal auditors, and participants were able to make meaningful and workable suggestions to address areas they considered to be deficient. Samples of the respective interviews and group discussions are attached as appendix 4.

3.6.1.1. Advantages of purposive sampling

The main advantages attributed to this sampling method are that it eliminates subjects who do not fit the requirements of the enquiry, and therefore produces an accurate or near accurate sample (Bogdan and Biklen 1992, Umaru 2009). This being the case, the results of the study are expected to portray an accurate situation. Selection of respondents was less time-consuming, and the method involved lesser costs than other probability sampling methods. In this study, it was easy to select the sample because the criteria used included educational
qualifications, relevant internal auditing experience and positions held within the organisations. This selection criteria proved to be suitable for the study, as the participants were well informed about the issues involved, understood the questions posed and their implications, and provided very useful information and suggestions for improvement of areas where they indicated there were deficiencies.

3.6.1.2. Disadvantages of purposive sampling

The main criticism levelled against the method is subjectivity in the choice of the respondents which some writers say inevitably reflects the bias of the researcher and affects the findings (Patton 1990). Selection of participants is based on the judgement of the researcher, and if such judgement is not based on a clear criteria, this becomes a serious disadvantage. Strategies to address this weakness are discussed in the next paragraph.

3.6.1.3. Measures taken to address disadvantages of purposive sampling

In order to counteract this perceived weakness, selection of participants was based on their knowledge and experience regarding internal auditing and the independence and objectivity of internal auditors. Among other things, the respondents’ academic and professional qualifications, auditing experience, and positions held in the organisations were used in selecting the respondents, because participants with these attributes would be in a better position to inform the study. Triangulation of sources was also employed. Data collected from different sources (internal auditors, principal internal auditors, and CAES) on the same issue were compared for accuracy. For example, data were collected from CAEs and internal auditors on the same issue. The data were then compared. If the data from these two sources were the same, this was taken to be an indication of the accuracy of the data. If they were not the same, then further probing was undertaken, in order to discover the true position. Triangulation of data generating instruments was also employed in that data obtained using
interview guides and focus group discussion guides and questionnaires (appendices 1-3) were similarly compared. The merits and demerits of these methods as well as measures taken to counteract the demerits are discussed in paragraphs 3.7.2.1 to 3.7.2.3.

3.7 Data collection

Certain preliminary considerations were taken into account in the planning stage of data collection. It was necessary to determine if the required data were already available from an existing source. Consideration was also given to the most appropriate method of collection, as well as when, where, and by whom the data would be collected as well as the data collection instruments to be used. These considerations were applied to each of the research questions. Issues relating to the coding and analysis of data and the piloting of research instruments were also considered at this stage. Having done the preliminary planning the next thing was to design the research instruments. The researcher was also aware that unlike in quantitative research, the line dividing data collection and data analysis procedures is not so distinct in qualitative research, but is rather blurred, and these two procedures take place simultaneously (Strauss 1987). As the researcher collected data, he was critically thinking about that data, what it meant and how it fits in with the data already collected. This information guided him on what, how and when to collect the next data. There was always this movement back and forth throughout the research. I also made notes of the thoughts, impressions and observations made during fieldwork, as these assisted in the analysis of data. I also wrote memos detailing the impressions he got from the data collected at any stage, and those memos assisted him in making decisions on the next data to be collected, the analysis of data and the compilation of the final report. Figure 3.1 below illustrates this movement back and forth.
Figure 3.1

Data collection and analysis

![Data collection and analysis diagram](image)


**Explanation of figure 3.1**

After collecting data the researcher partially analysed the data to find out if any new ideas emerged from the data collected. If there were such new ideas, the he added them on to the questions to be asked in the next interview or group discussion. During data collection the researcher was always thinking about the data collected, and wrote down in the form of memos, any observations, insights or reflections that came to him, and these were also included into the next interviews or group discussions. This explains the movement back and forth as indicated by the arrows.

**3.7.1 Data generation instruments**

Data collection instruments are the tools which are used in the generation of data. The most common research instruments are questionnaires, interview guides, and focus group
discussion guides. In qualitative research, the researcher is an important instrument. In this study, questionnaires with open ended questions, interview guides, focus group discussion guides were used. Each of these instruments is discussed below.

3.7.1.1 Interview guides

Gall, Borg and Gall (1996) state that interview guides specify questions, the sequence in which they are to be asked and guidelines concerning what the interviewer will say at the start and end of the interview. This is an important instrument when conducting interviews, as it ensures that all the important aspects of issues being investigated are covered. In this research, interview guides were prepared on the basis of the research questions, and the researcher further probed during the interviews, depending on the responses of the participants. Refer to appendix 2 for interview guides used.

3.7.1.2 Focus group discussion guides

The guide contains a set of questions that were discussed by the group. (Gall et al., 1996). The guide helped the researcher ensure that all topics to be discussed by the group were included. As with the interview guide, it was also based on the research questions. This instrument was used in the conduct of focus group discussions. Refer to appendix 3 for focus group discussion guides.

3.7.1.3 The researcher as an instrument

In qualitative research, the researcher is the primary instrument for gathering and analysing data and must maintain an impartial attitude and be aware of how his personal biases may prejudice the interpretation of data (Veal 2005). The skills required of qualitative researchers were identified by a number of writers, among them Merriam (1998). These skills guided the researcher throughout the study and are listed below:
Tolerance for ambiguity. This entails the ability to tolerate and accept inconsistencies and uncertainties. The researcher must be prepared to face unforeseen events and even change direction;

The researcher must be sensitive. This refers to data collection. The researcher must be sensitive to information collected in terms of what it reveals and how it reflects what is happening and have a keen sense of timing, e.g. when to probe, allow silence or change direction when interviewing.

He must be able to detect personal biases. The researcher as a human being has his own values, and he should not allow these values to creep into interviews and observations made. Infiltration of his or her own perceptions or interpretations should be minimised.

He should be a good communicator. “a good communicator empathises with respondents, establishes rapport, asks good questions and listens intently.” (Merriam 1998:23). He should also have good listening and oral skills.

Throughout the study, the researcher was cognisant of his role and was guided by these very important requirements.

3.7.2 Data generation procedures

In this research, interviews and focus group discussions and questionnaires with open ended questions (questerviews) were used in the collection of data, and the procedures followed are discussed below.

3.7.2.1 Interviews

In this research interviews were conducted with the following respondents: one Chief audit executive, and two principal auditors. The other CAEs and principal auditors were given
The use of interviews is appropriate when it is necessary to gain insight into people’s feelings, opinions, emotions and expectations (Myers and Newman 2007; Rubin and Rubin 1995). McNamara (1999) argues that interviews are particularly useful for getting the story behind a participant’s experiences, and goes on to say that they can also be used as a follow up, to verify the participant’s responses in the questionnaire. He further states that they are also useful in getting information of sensitive nature, as participants can be encouraged to open up, and discuss the issues in an honest manner. The use of interviews made it possible to gain direct access to interviewees at affordable costs in terms of time and travel.

In this research the semi structured interview was used. The researcher introduced a theme or topic and let the interviewee develop ideas and follow his train of thought, thereby allowing the interviewee to speak their mind. This is a way of discovering things about complex issues. This type was selected because it allowed the interviewee to freely answer questions and speak their minds while at the same time the researcher did not lose sight of the objectives of the interview. The fact that the interviewer was more flexible meant that the interview vacillated between the semi-structured and unstructured versions of the interview.

### 3.7.2.1.2 Advantages of interviews

The use of interviews made it possible for me to get detailed information on issues relating to the independence and objectivity of internal auditors in parastatals. I was able to clarify any questions which were not clearly understood by the participants. It was also possible to probe further, where the participant gave incomplete or vague responses. The only equipment required was a voice recorder and the response rate was one hundred percent as the
interviews were pre-arranged. It is pertinent to note that these advantages have been noted by a number of writers, among them Bryman (2001); Creswell (2008) and Colin (2011).

3.7.2.1.3 Disadvantages of interviews

I found that a lot of time was needed to transcribe the data, as the recorded data had to be typed verbatim. Data analysis also posed a challenge as the responses were non-standard. I also noted that some participants were a bit uncomfortable with the use of a voice recorder, but this quickly waned off after assurances that the recordings would be kept confidential and destroyed soon after transcription and member checking.

3.7.2.1.4 Strategies to minimise effects of the disadvantages

In order to counteract these disadvantages, sufficient time was set aside for the preparation, transcribing, coding and analysis of data. Proper interviewing techniques were also employed, in order to avoid bias and to ensure that the interviewee was at ease as early into the interview as possible. The result was that the participants supplied a lot of relevant information for this study.

3.7.2.1.5 Preparation for the interview

Preparations for the interview entailed choosing a suitable venue, where there were no distractions, explaining the purpose of the interview, and assuring the interviewee that the highest degree of confidentiality would be maintained on the information provided during the interview. I also indicated approximately how long the interview would take, provided my contact details and allowed the interviewee to seek any clarification about the interview. A Dictaphone machine was also secured to record the interview.
3.7.2.1.6 Measures to ensure trustworthiness of interview data

The biggest challenge of qualitative research is how to ensure quality and trustworthiness of the research (Gable 1994; Lee 1991). Janesick (2000:390) complains about “an almost constant obsession with the trinity of validity, reliability and generalisability,” and has christened this obsession as methodolatry. These three requirements apply to the quantitative method.

In this study, the following strategies suggested by Willig (2001), Gall, Borg and Gall (1996), Finaly (2000), Lincoln and Guba (1985), Ballinger 2006), and Altheide and Johnson (1994) were employed to enhance trustworthiness of the data collected.

*Triangulation*

This involved the generation of data using more than one method and comparing the results. Data collected using different instruments (interview guides, focus group discussion guides and questerviews) were compared, and data collected from different groups (CAEs, principal auditors and internal auditors) were also compared. If the data was corroborated, this enhanced the trustworthiness of the data. Where this was not the case, I re-examined the data and made further enquiries in order to establish the cause of the differences.

*Member checking*

After transcribing the data, I went back to the research participants, who supplied the data, to get confirmation that what I had recorded was in fact what they actually said. The participants read the transcribed data, and any corrections were made to their satisfaction. During the interviews, I also summarised what the participant had said, and sought the participant’s confirmation as a way of ensuring that I had properly understood what the participant had said.
Peer review

The methodology employed, findings, interpretations and conclusions I made were discussed with peers at the Bulawayo region of the Zimbabwe Open University, who were not involved in the research, in order to get their opinions regarding the extent to which these were appropriate and supported by the data collected.

Low inference descriptors

I also employed the use of low inference descriptors. These are words or phrases that are as close to what the participant said as possible. For example, the phrase “scope limitation” was used to describe instances where the auditee “refused to be audited by somebody junior to him” or “refused to be audited saying the information was confidential”. These are instances where the scope of the auditor is limited, thus the use of the phrase “scope limitation.”

Audit trail

I maintained detailed and accurate records of all my activities and data generated, in an organised manner for easy retrieval, as evidence of data generated. The records maintained and stored include: interview guides, focus group discussion guides, completed questerviews, transcribed data, master code list, recordings of interviews and focus group discussions and summaries of findings.

Reflexivity

In order to minimise the likelihood of my values creeping into the interpretation of data I critically examined myself to detect any potential bias or inclination that may influence conclusions about the data. Throughout the data collection and processing, right up to the
report writing stage, I was on the lookout to ensure that bias did not influence any of these stages of the study.

Johnson (1997), Newman and Benz (1998) Krefting (1991) are among some of the authors who have also identified these strategies for enhancing internal validity

3.7.2.2 Focus group discussions

Focus group discussions were held with internal auditors from two of the three organisations. Krueger and Casey (2000) define focus group discussion as a method of generating data, in a safe environment, from more than one individual at a time, regarding a specific area of interrogation. Denscombe (2007) states that focus groups consist of small groups of people who are brought together by a “moderator” (researcher) to explore attitudes, perceptions, feelings and ideas about a specific topic. They rely on group dynamics (interaction within the group) to elicit information with the role of the moderator being facilitation of group interaction. It was therefore necessary to ensure full participation by all members of the groups. The value of focus group discussions is highlighted by Morgan (2006:121) who observes that group members:

share their experiences and thoughts, while also comparing their own contributions to what others have said. This process of sharing and comparing is especially useful for hearing and understanding a range of responses on a research topic. The best focus groups thus not only provide data on what the participants think but also why they think the way they do.

The discussions were recorded using a Dictaphone and I made relevant notes during the course of the discussions. Arrangements were made for a venue where there were no distractions. I tried to establish rapport as early as possible. I initiated the discussion and allowed free discussion among the participants without interference, but guided the discussion towards the goals to be achieved. I avoided contaminating the discussion with my own ideas and bias, and allowed the group members to discuss among themselves. Whether
there was consensus or disagreement among participants, I gained insight into why
participants held the views they had.

After the first focus group discussion, I transcribed the proceedings and partially analysed
them in order to find out if there were any new themes that had emerged from the group
discussion. Such new themes were then included in the focus group discussion guide in
preparation for the next focus group discussion.

3.7.2.3. Questionnaires with open ended questions (Questerviews)

Where it was not possible to set mutually convenient times for interviews and focus group
discussions, questionnaires with open ended questions were used to collect data. Open ended
questions were chosen because they do not impose limitations on responses, and participants
were free to answer questions on their own terms, thereby revealing more insights into the
issues under scrutiny. The use of questionnaires also eliminated the personal bias of the
researcher, as there was no direct interaction between the researcher and the participant when
the questionnaire is being completed. (Gall, Borg and Gall 1996)

In compiling the questionnaire, I ensured that only those questions that were relevant to the
study were included. This was achieved by making reference to the research objectives and
research questions, and including only those questions that were absolutely necessary for the
research. The use of unnecessary jargon, embarrassing, insensitive or offensive language was
avoided. The inclusion of leading questions was also avoided. Clear and unambiguous
instructions on how to complete the questionnaires were also given.

The questionnaires were subjected to a pilot study, and feedback from this was used to refine
them before administration.
In order to counteract a possible low response rate, I personally distributed the questionnaires and retrieved the completed questionnaires and as a result the response rate was one hundred percent. The following participants completed these questionnaires: 2 CAEs, 3 CFOs, 3 Principal auditors, 6 internal auditors and 9 managers

3.8 Data analysis: an overview

There are several traditional approaches to qualitative data analysis, and these include the grounded theory approach (Strauss and Corbin 1990), phenomenology (Van Manen 1990), discourse analysis (Potter and Wetherall (1994) and Narrative analysis (Leiblich 1998), each of which has its own assumptions, procedures and jargon.

Leech and Onwuegbuzie (2008) give quite a comprehensive list of qualitative data analysis techniques as depicted on figure 3.2.

Figure 3.2

Qualitative data analysis techniques
Source: Leech and Onwuegbuzie (2008)

The following are brief descriptions of each of the techniques:
<table>
<thead>
<tr>
<th>Type of analysis</th>
<th>Short description of analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant comparison analysis</td>
<td>Systematically reducing data to codes then developing themes from the codes</td>
</tr>
<tr>
<td>Classical content analysis</td>
<td>Counting number of codes</td>
</tr>
<tr>
<td>Keywords-in-context</td>
<td>Identifying keywords and utilizing the surrounding words to understand the underlying meaning of the keyword</td>
</tr>
<tr>
<td>Domain analysis</td>
<td>Utilising the relationships between symbols and referents to identify domains</td>
</tr>
<tr>
<td>Taxonomic analysis</td>
<td>Creating a system of classification that inventories the domains into a flowchart or diagram to help the researcher understand the relationships among domains</td>
</tr>
<tr>
<td>Componential analysis</td>
<td>Using matrices and/or tables to discover the differences among the subcomponents of domains</td>
</tr>
<tr>
<td>Conversation analysis</td>
<td>Utilising the behaviour of speakers to describe people’s methods for producing orderly social interaction</td>
</tr>
<tr>
<td>Discourse analysis</td>
<td>Selecting representative or unique segment of language use, such as several lines of an interview transcript, and then examining the selected lines in detail for rhetorical organisation, variability, accountability and positioning.</td>
</tr>
<tr>
<td>Secondary data analysis</td>
<td>Analysing non-naturalistic data or artefacts that were derived from previous studies</td>
</tr>
<tr>
<td>Membership categorisation analysis</td>
<td>Utilising the role that interpretations play in making descriptions and the consequences of selecting a particular category (e.g. baby, sister, brother, mother, father = family)</td>
</tr>
<tr>
<td>Semiotics</td>
<td>Using talk and text as systems of signs under the assumption that no meaning can be attached to a single term.</td>
</tr>
<tr>
<td>Manifest content analysis</td>
<td>Describing observed (i.e., manifest) aspects of communication via objective, systematic and empirical means (Berlson, 1952).</td>
</tr>
<tr>
<td>Latent content analysis</td>
<td>Uncovering underlying meaning of test</td>
</tr>
<tr>
<td>Qualitative comparative analysis</td>
<td>Systematically analysing similarities and differences across cases, typically being used as a theory-building approach, allowing the analyst to make connections among previously built categories, as well as to test and to develop the categories further.</td>
</tr>
<tr>
<td>Narrative analysis</td>
<td>Considering the potential of stories to give meaning to individual’s lives, and treating data as stories, enabling researchers to take account of research participants’ own evaluations</td>
</tr>
<tr>
<td>Text mining</td>
<td>Analysing naturally occurring text in order to discover and capture semantic information</td>
</tr>
<tr>
<td>Micro-interlocutor analysis</td>
<td>Analysing information stemming from one or more focus groups about which participant(s) responds to each question, the order that each participant responds, the characteristics of the response, the nonverbal communication used, and the like.</td>
</tr>
</tbody>
</table>
In order to avoid the restrictions imposed by following one type of analysis, the general inductive approach was adopted for this study (Bryman and Burgess 1994; Dey 1993). Thomas (2003:2) describes this as “a systematic procedure for analysing qualitative data where the analysis is guided by specific objectives.” In this study, the research objectives which are clearly stated in paragraph 1.13, guided the data analysis.

The purpose of the general inductive approach is to condense extensive raw data into brief summary format and to establish clear links between research objectives and the summary findings derived from raw data.

The following are some of the assumptions of the general inductive approach (Thomas 2003):

- Data analysis is determined by both research objectives and multiple reading of the raw data. The findings are derived from both the research objectives outlined in the research and findings arising from the analysis of the raw data.
- The primary mode of analysis is the development of categories from raw data that capture key themes and processes.
- The research findings result from multiple interpretations made from the raw data by the researcher who codes the data.
- Trustworthiness of the findings can be assessed using various techniques which include triangulation and feedback from the research participants. (Thomas 2003).

The procedures employed in this research are discussed in the next paragraphs.
3.8.1 Procedures for data analysis

Before commencing data analysis, I obtained a thorough knowledge of the data collected by reading and re-reading transcripts and listening to the audio recordings several times. This enabled me to discern themes and concepts that recur in the data. I was guided by the research objective (refer paragraph 1.13) and my initial focus was to relate the collected data to the research questions (refer to paragraph 1.14), the purpose of the study (refer to paragraph 1.12) and how the results of the study would be used.

3.8.2 Detailed procedures

The following paragraphs briefly describe the stages in the data analysis process.

3.8.2.1 Transcription of data

I typed the text from field notes, memos, interviews and focus group discussions into word processing documents in preparation for data analysis.

3.8.2.2 Member checking.

After transcription of the interviews, the transcribed data were printed and given to the respective participants, for them to read and confirm that what was recorded was in fact what they had actually said. In this way, they were given an opportunity to confirm the accuracy of the transcript and correct any errors.

3.8.2.3 Segmentation and coding of data

After verification of the transcribed data, I read through the data several times in order to discern general ideas coming from the data, with reference to the research questions, in preparation of data analysis. I then carefully read the data line by line and divided them into
meaningful units or segments, with each segment containing similar data. The segments were then coded, i.e. each segment was given an identifying label or descriptive name, the code. (Rossman and Rallis 1998). These were descriptive codes, depicting the nature of the data contained in the segment. At the same time, a master list of all the codes developed and used in the research was maintained.

3.8.2.4 Enumeration

In this process I quantified the number of times a word or phrase appeared in a document. This assisted in clarifying the use of such words as “some”, “few”, “almost all” in the final report. However this quantification was not taken to have any statistical implications.

3.8.2.5 Establishing relationships among categories

I examined categories for similarities and combined those codes which related to the same idea, under a new code. I went on to look for relationships between categories which could assist in shedding more light into the data. For example cause and effect relationships. Spradley (1979) gives a list of some of the relationships to be looked for in the data, as shown on the table 3.3.
### Table 3.3

**Spradley’s universal semantic relationships**

<table>
<thead>
<tr>
<th>Title</th>
<th>Form of relationship</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Strict inclusion</td>
<td>X is a kind of Y</td>
</tr>
<tr>
<td>2 Spatial</td>
<td>X is a place in Y; X is part of Y</td>
</tr>
<tr>
<td>3 Cause and effect</td>
<td>X is a result of Y; X is a cause of Y</td>
</tr>
<tr>
<td>4 Rationale</td>
<td>X is the reason for doing Y</td>
</tr>
<tr>
<td>5 Location for action</td>
<td>X is a place for doing Y</td>
</tr>
<tr>
<td>6 Function</td>
<td>X is used for Y</td>
</tr>
<tr>
<td>7 Means-ends</td>
<td>X is a way to do Y</td>
</tr>
<tr>
<td>8 Sequence</td>
<td>X is a step (stage) in Y</td>
</tr>
<tr>
<td>9 Attribution</td>
<td>X is an attribute (characteristic) of Y</td>
</tr>
</tbody>
</table>

**Source:** Spradley (1979)

The researcher was guided by this list when looking for relationships among categories.

### 3.8.2.6 Identifying patterns and connections within and between categories

The categories were used to generate information on the findings of the research. I examined each category to determine the key ideas expressed, as well as differences and similarities in the responses, and wrote a summary for each category. I also decided the relative importance of each them by counting the number of times it comes up. However this was just a rough estimate of the importance of the theme, but did not have *prima facie* statistical relevance. Data was also scanned for themes that always occurred together in the data, which could help *answer* the question “Why”. Examples which ran counter to the prevailing themes were also examined to determine whether they were important to the interpretations or
understanding of the researcher. I also looked for verbatim quotations and other evidence in the data to support the information extracted from the data.

3.8.2.7 Interpretation

Interpretation is the process of attaching meaning and significance to the analysis. The themes, categories and category summaries as well as relationships established between categories were used in the process of interpreting the results. I listed findings resulting from the categorising and further examination of the data. I then reflected on what major lessons were learnt from the study and how these would be of use to the end users, as well as whether the findings could apply to other settings in the internal auditing field. This process included a comparison of the findings with literature reviewed, internal auditing standards, practice advisories and practices and ethics, as well as existing theories on the independence of internal auditors. After these considerations, I developed an outline for presenting the results, which I used as a basis for writing up the final report. I also made note of important quotes or descriptive examples to illustrate points and bring life to the data.

3.8.2.8 Cross-case analysis

I also examined the data across the three cases to identify similarities and differences in order to determine which findings could be generalised among the three organisations and why there were differences if any.

3.9. Ethical considerations

Participants were given full information regarding the research. They were advised that it was being undertaken to fulfil the requirements of the D Phil programme on which I had embarked. They were advised to use their free will in deciding whether to participate in the study or not. No undue influence or coercion was used to get them to participate. They were
encouraged to ask any questions they might have in connection with the research, and I gave them my contact details, that is, the telephone number, the cell phone number, the email address, and my office number. They were also advised that they were free to withdraw from the study at any time, without any consequences, and that the information they supplied would be treated in the strictest of confidence and not divulged to third parties, and would be anonymised so that no one could identify the supplier of the information.

In the design of the research instruments, care was taken to ensure that no questions that would be offending to the participants or their communities would be included. During data collection, I maintained objectivity and ensured that my own biases would not influence the process. The same stance was also maintained during the analysis of data, up to report writing stage. Data collected were treated in the strictest confidence, and were not divulged to third parties. Recordings of interviews and focus group discussions were anonymised soon after transcription and verification.

3.11 Summary

This chapter covered the research methodology employed in this study, starting with the underlying research philosophy for the study. The two main approaches to research, namely, qualitative and quantitative methods were briefly explained and compared. The research philosophy of the study, namely interpretivism was explained and justified. Reasons why the qualitative approach was chosen for the study were given. The case study design, which was chosen for the research was explained, together with the reasons why it was chosen. The population of the study, sample selected and sampling method used were also described. Data collection instruments, namely the researcher, interview guides, focus group discussion guides and the questerviews, as well data generation procedures were described. The following is a summary of methods used to collect data:
Table 3.4

How data were collected

<table>
<thead>
<tr>
<th>Participant</th>
<th>Number per collection method</th>
<th>Questerviews</th>
<th>Interviews</th>
<th>Focus group discussions</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CAE</td>
<td></td>
<td>2</td>
<td>1</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>CFO</td>
<td></td>
<td>3</td>
<td>-</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>Principal auditor</td>
<td></td>
<td>3</td>
<td>2</td>
<td>-</td>
<td>5</td>
</tr>
<tr>
<td>Internal auditor</td>
<td></td>
<td>6</td>
<td>-</td>
<td>7</td>
<td>13</td>
</tr>
<tr>
<td>Managers</td>
<td></td>
<td>9</td>
<td>-</td>
<td>-</td>
<td>9</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>23</td>
<td>3</td>
<td>7</td>
<td>33</td>
</tr>
</tbody>
</table>

This was followed by an explanation of how the data collected was analysed and measures taken to ensure the trustworthiness of data. The next chapter deals with data presentation and discussion.
Chapter 4

Presentation and Discussion of Research Finding

4.0 Introduction

In this chapter, research findings are presented and discussed. The chapter starts with the presentation of the bio data of the participants. Adoption and observance of IIA standards and ethics by the 3 parastatals is then discussed. This is followed by an examination of the introduction, review and dissemination of the audit charter in the three parastatals. After this, the research findings are presented and discussed under the respective research questions, namely, (a) reporting structures, (b) relations with other corporate governance arms, (c) threats to independence and (d) procedures for dealing with threats to independence. In order to facilitate comparison between cases, regardless of the designations given to the various posts in the three parastatals, in this study, the designation Chief Audit Executive (CAE) is used for the head of the internal audit function, the term principal auditor is used for the audit supervisor, who reports to the CAE and supervises internal auditors and the term internal auditors is used for the rest of the internal auditors. In the discussions, the three parastatals are designated Case1, Case 2 and Case 3, depicting parastatals 1 – 3 respectively.

4.1 Bio data of the participants

The bio data of the participants are presented on a case by case basis

4.1.1 Bio data for case 1

4.1.1.1 Age of participants

The following table shows the age groups of the participants.
Table 4.1

Ages of participants - Case 1

<table>
<thead>
<tr>
<th></th>
<th>Age of participants in years</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Up to 29</td>
</tr>
<tr>
<td>Chief audit executive (CAE)</td>
<td></td>
</tr>
<tr>
<td>Chief financial officer (CFO)</td>
<td></td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
</tr>
<tr>
<td>Internal auditors</td>
<td>3</td>
</tr>
<tr>
<td>Managers</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>3</td>
</tr>
</tbody>
</table>

It can be seen that the majority of the participants (nine) were in the above 45 years age group, with only 3 in the 30-45 age group. All the participants were therefore mature individuals. Meaningful, well considered responses were obtained from them.

4.1.1.2 Qualifications of participants – Case 1

The following table shows the highest qualifications of the participants.

Table 4.2

Qualifications of participants

<table>
<thead>
<tr>
<th></th>
<th>Highest qualification</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Diploma</td>
</tr>
<tr>
<td>Chief audit executive (CAE)</td>
<td></td>
</tr>
<tr>
<td>Chief financial officer (CFO)</td>
<td></td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
</tr>
<tr>
<td>Internal auditors</td>
<td></td>
</tr>
<tr>
<td>Managers</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
</tr>
</tbody>
</table>

The CAE was highly qualified. He had an MBA, a first degree in accounting and a CPA (Certified Public Accountant) professional qualification. The auditors also had relevant commercial qualifications. Four had first degrees in the commercial field and one had an accounting diploma. This indicates that the department was staffed with qualified personnel.
Because of the theoretical knowledge they possessed, the participants were able to understand all the questions I posed, as well as their implications, and give comprehensive responses. Their full cooperation was also given, as some of them indicated that they had also gone through the process of undertaking research in the course of obtaining their qualifications.

4.1.1.3 Auditing experience of participants – Case 1

The following table shows the audit experience of the participants.

Table 4.3

<table>
<thead>
<tr>
<th>Auditing experience of participants</th>
<th>Auditing experience in years</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Up to 5</td>
</tr>
<tr>
<td>Chief audit executive (CAE)</td>
<td></td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
</tr>
<tr>
<td>Internal auditors</td>
<td>1</td>
</tr>
<tr>
<td>Total</td>
<td>1</td>
</tr>
</tbody>
</table>

Only one participant had less than five years working experience. The rest of the auditors had experience which ranged from seven years to over 15 years. It was clear that the level of experience among the internal auditors (including the CAE and principals auditors) was very high. Because of their vast experience in internal auditing, the participants were able to share valuable experiences, and this resulted in the accumulation of high quality data for the study.

4.1.2 Bio data for Case 2

4.1.2.1 Age of participants – Case 2

The following table shows the ages of the participants
Table 4.4

Ages of participants – Case 2

<table>
<thead>
<tr>
<th>Age in years</th>
<th>Up to 29</th>
<th>30 to 45</th>
<th>Over 45</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chief audit executive (CAE)</td>
<td></td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Chief financial officer (CFO)</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Internal auditors</td>
<td>2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Managers</td>
<td></td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>2</td>
<td>6</td>
<td></td>
</tr>
</tbody>
</table>

The majority of the participants were mature adults, who were able to make well considered responses to questions posed. Even the 2 relatively young participants made very good contributions, because they were highly qualified.

4.1.2 Qualifications of participants – Case 2

The following table shows the highest qualifications obtained by each participant.

Table 4.5

Highest qualification obtained by participants – Case 2

<table>
<thead>
<tr>
<th>Highest qualification</th>
<th>Diploma</th>
<th>First degree</th>
<th>Masters</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chief audit executive (CAE)</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Chief financial officer (CFO)</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Internal auditors</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Managers</td>
<td>1</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>3</td>
<td>3</td>
<td>2</td>
</tr>
</tbody>
</table>

All the participants had either a diploma, a first degree or a masters degree. The internal auditors had appropriate qualifications, with one having a bachelor of commerce honours degree in accounting and a masters in strategic management and corporate governance., while the other had a bachelor of commerce degree in accounting. The CAE was also qualified for
the job, as he had a bachelor of accounting degree and an MBA. The participants gave their full cooperation, because most of them knew the importance of research in the development of knowledge, and some had gone through the same process of conducting a research in the course of attaining their qualifications.

4.1.2.3 Auditing experience of participants – case 2

The following table shows the auditing experience of the participants

Table 4.6

<table>
<thead>
<tr>
<th>Auditing experience of participants – case 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Auditing experience in years</td>
</tr>
<tr>
<td>Up to 5</td>
</tr>
<tr>
<td>Chief audit executive (CAE)</td>
</tr>
<tr>
<td>Principal auditors</td>
</tr>
<tr>
<td>Internal auditors</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

The CAE and the principal auditor were highly experienced, with auditing experience of 29 and 25 years respectively. The internal auditors on the other hand were relatively less experienced. This came about because the function was reduced to skeleton staff in the years prior to 2009 due to staff wastages as a result of the worsening economic conditions in the country. The CAE stated that most of the experienced staff left the organisation in search of greener pastures elsewhere, and no effort was made to replace them. After 2009, the organisation started resuscitating the function again, as economic conditions were slowly improving. However, the internal auditors had high qualifications and were fully capable of performing their duties in a professional and effective way. Their responses showed a deep understanding of both theoretical and practical aspects of internal auditing.
4.1.3 Bio data for case 3

4.1.3.1 Ages of participants - case 3

The following table shows the ages of the participants

Table 4.7

Ages of participants – case 3

<table>
<thead>
<tr>
<th>Age of participants in years</th>
<th>Up to 29</th>
<th>30 - 45</th>
<th>Above 45</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chief audit executive (CAE)</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Chief financial officer (CFO)</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Internal auditors</td>
<td></td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Managers</td>
<td></td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>3</td>
<td>8</td>
</tr>
</tbody>
</table>

All participants were mature adults, and their responses were well considered and comprehensive, reflecting the knowledge they had acquired during their working lives.

4.1.3.2 Qualifications of participants – Case 3

The highest qualifications of participants are shown below.

Table 4.8

Qualifications of participants – case 3

<table>
<thead>
<tr>
<th>Highest qualification</th>
<th>Diploma</th>
<th>First degree</th>
<th>Masters</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chief audit executive (CAE)</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chief financial officer (CFO)</td>
<td></td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Principal auditors</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Internal auditors</td>
<td>2</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Managers</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Total</td>
<td>3</td>
<td>5</td>
<td>3</td>
</tr>
</tbody>
</table>
There was a clear indication that the internal audit function was staffed with qualified personnel. This was reflected in the quality of the responses obtained from the participants.

4.1.3.3 Auditing experience of participants – Case 3

The following table shows the auditing experience of internal auditors

**Table 4.9**

<table>
<thead>
<tr>
<th>Auditing experience of participants – Case 3</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td>Auditing experience in years</td>
</tr>
<tr>
<td>Chief audit executive (CAE)</td>
</tr>
<tr>
<td>Principal auditors</td>
</tr>
<tr>
<td>Internal auditors</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

It was apparent that there was abundant auditing experience in the internal audit function. As a result, the participants gave responses that showed deep understanding of both theoretical and practical issues in internal auditing.

4.2 Membership of the Institute of Internal Auditors

In two of the three cases, it was found that only the CAEs were members of the IIA. In the third case, the CAE and one of the principal auditors were members of the IIA. Internal auditors cited the high cost of membership contribution and fees as factors preventing them from becoming members and attaining the Certified Internal Auditor (CIA) qualification. In their view, they were lagging behind others in the profession as they were not privy to the latest internal auditing techniques, and did not have the opportunity to interact with other professionals who were members of the IIA. In all three cases, internal auditors and principal auditors felt that their organisations should assist them become members of the IIA and get certification, by subsidising the payment of fees and contributions. I concur with the
sentiments expressed by the internal auditors and principal auditors, as it is necessary to ensure that all internal audit personnel keep abreast of the latest trends and developments in the profession. Such a move would also raise greater awareness of the necessity of independence by internal auditors, as well as strategies for dealing with threats to that independence.

4.2.1 Adoption of IIA standards and ethics

Although all the three CAEs stated that the IIA standards and ethics had been fully adopted in their organisations, the situation obtaining on the ground was completely different. It was found that none of the auditors or principal auditors had either a hard or electronic copy of the IPPF, which contains all the standards and ethics of the internal auditing profession. A case by case account of the experiences of each of the three audit functions is given below.

4.2.1.1 Case 1: Adoption of IIA standards and ethics.

For a long time during the 1980-90s, Coopers and Lybrand were the external auditors for this parastatal. As a result, they introduced their approach to auditing, known as the Coopers and Lybrand approach. They provided manuals and conducted workshops and seminars to ensure all the internal auditors were conversant and proficient in the application of the audit techniques involved. These included flowcharting, internal control questionnaires (ICQ), and program and record of functional tests (PRT). This knowledge was passed on to new entrants. To this date, these techniques were being used in the branch at the time of carrying out the study. This situation was succinctly stated by one of the internal auditors who said,

Yes, I was going to go into that, because the aspect of IPPF only came into our environment when the current chief internal auditor took over office. Because we have been guided, virtually everything by Coopers and Lybrand. Even seminars were being done by Coopers and Lybrand.
With the change in external auditors during the period commencing 2000 as well as a change in the CAEs, attempts were made to introduce the IPPF. This is highlighted by one of the auditors who said “...but, now when this current chief internal auditor came into office, there was now a bias towards the Institute of Internal Auditors, because he wanted to make people more professional.”

However it appears that these efforts were disjointed and applied on a piecemeal basis. This is evidenced by the fact that in the whole branch, only the CAE is a member of the IIA, and that no IIA training has so far been provided to the internal auditors. It is necessary that internal auditors be members of the IIA, so that they keep abreast of new techniques and other developments in the profession. Risk based internal auditing was only introduced at the insistence of the external auditors in 2013, according to one of the audit officers, who said “…in fact external auditors suggested that we should use the risk based approach and the board took it up and ordered us to do that.”

However, this practice had been widely adopted for many years in the profession. This highlights the need for all auditors to be members of the IIA.

Perhaps one major step in the adoption of IIA standards was the introduction of the internal audit charter. This is a very important document as it defines the need for the existence of the internal audit function, its duties, responsibilities and powers.

4.2.1.2. Case 2: Adoption of IIA standards and ethics.

Although the CAE stated that IIA standards had been adopted, it was apparent that this was not the case. When I asked the auditors if they had copies of the IPPF, the response was “IPPF? What is that?” I then explained that the IIA standards and code of ethics were contained in the IPPF. The auditors then explained that none of them were members of the
IIA, and lamented that because of this, they could not keep abreast of developments in the profession. One of the internal auditors had this to say,

> We came here as internal auditors, but unfortunately we are not affiliated to the institute of internal auditors. We know the body exists, but because of the resources we were talking about, you find we are not even affiliated to them. So we cannot share ideas, we cannot get information from our peers we cannot interact with them at any level because we are not affiliated. For us to be affiliated we have to pay subscriptions, we have to go through some courses they offer there. So you find sometimes the nature of our work is compromised. Perhaps there are more new ways of doing things in the world out there, but because we are not affiliated to such a body, we find we are left behind. We really left out at the end of the day.

In carrying out their audits, they are guided by the audit manual which is quite comprehensive as it covers all areas to be subjected to internal audit scrutiny. However, as highlighted by the auditor quoted above, it is necessary for internal auditors to be members of the IIA so that they can interact with others within the profession and keep abreast of developments regarding new audit techniques. Additionally, they would also become aware of the ethics of the profession.

4.2.1.3 Case 3: Adoption of IIA standards and ethics.

IIA standards had not been adopted. The question, “What standards or guidelines do you follow in the performance of your duties?” drew responses like “International financial reporting standards”, “International accounting standards,” and “International auditing standards”. None of the participants mentioned the IPPF. In one instance, an internal auditor responded, “The organisation has no audit charter in place, hence audit duties are basically general,” further indicating that IIA standards and ethics had not been adopted. Auditors in this parastatal are guided by the audit manual in the conduct of their duties.

The adoption of the IIA standards is necessary for any internal audit function that desires to perform its duties in a professional manner. The IPPF contains ethics of the profession, as
well as comprehensive definitions of audit independence and objectivity, and goes further to explain how to identify and manage threats to independence and objectivity. Therefore if internal auditors had access to and followed the provisions of the IPPF, they would have been in a better position to deal with any threats to independence and objectivity that they might encounter in the course of their duties.

4.3 The audit charter

The audit charter is a very important document, because it defines the purpose, authority and responsibility of the internal audit function. It defines the scope of internal audit activities and gives internal auditors power to access all records, documents, personnel, and properties necessary in the performance of their duties (IIA 2004). It makes provisions for internal auditors to perform their duties without interference. All members of the organisation have to know its contents in order to appreciate the role of the internal audit function and give maximum cooperation and support to the auditors. It should therefore be widely circulated within the organisation and its contents should be disseminated to all members of the organisation. This would facilitate the cooperation of all members of the organisation when internal auditors carry out their duties.

Although all the three CAEs stated that there were audit charters in their organisations, only the CAE for case 1 was able to produce a copy of the relevant charter. A follow up with the internal auditors and principal auditors for cases 2 and 3 revealed that none of them had seen the audit charters. The auditees of these two cases had also not seen the audit charters.

In case 2, one of the auditors had this to say, “Unfortunately, to my knowledge, I have never seen it. I don’t think it exists in the department, because if it was there we would have been furnished with copies. I don’t know if my colleague has seen it.”
This was corroborated by his colleague who said,

> Definitely, I think, normally looking at us, looking at the department being existing, definitely it might be there. But unfortunately we have not been provided with copies. I would like to think that it’s there but we have not been privileged to it. Maybe not knowing why we are not getting such an important document.

In case 3, although the CAE said copies of the audit charter had been distributed to all auditors, none of them could produce a copy. Their responses were, “I have not seen one”, “We do not have one” and “There is nothing.”

The fact that in cases 2 and 3 none of the internal auditors, principal auditors, or auditees could produce copies of the audit charters strongly suggests that no audit charters were in place. If the charters existed, then definitely the principal auditors and the internal auditors would have had copies and been aware of their contents. Even the respective CAEs could not produce copies of the audit charters. It can be safely concluded that the audit charters did not exist, and if by any chance, they were filed and forgotten somewhere in the offices of the CAEs, where they could not be located, then they did not serve any purpose.

Lack of an audit charter can have an adverse impact on the independence and operations of an internal audit function. Auditees could refuse to produce documents, refuse to be audited by staff who are junior to them in rank, or choose not to cooperate with the internal auditors. A lot of time would be wasted trying to get the cooperation of auditees, whereas if an audit charter were in place, all these problems would not exist, or would be easy to resolve without wasting too much time. This was confirmed in this study, as some auditees refused to be audited by junior staff, and others refused to give internal auditors information on the basis that it was confidential.
4.3.1 Case 1: Audit charter

As stated above, only case 1 had an audit charter. The audit charter was introduced in 2009. The CAE stated that it was based on a draft provided by the IIA, and this was confirmed by one of the principal auditors who said that it was drafted with assistance from the IIA. It appears there was a lot of resistance from the CEO. One of the principal auditors stated that there was a lot of resistance from the CEO, because he thought that the CAE would report to the directors, and he (the CEO) would be left to mark the register, without any control over the CAE. The other principal auditor confirmed this resistance. In answer to the question “When was the audit charter reviewed?”, he stated that

It has not been reviewed ever since, for the simple reason that a lot of things haven’t changed, but the other issue is possibly fear of it not being approved, because this one which we are currently using took more than a decade to be approved by the board and the general manager.

This resistance from the CEO is quite surprising. One would have thought that because of the strategic importance of the internal audit function in the achievement of organisational objectives, the CEO would have welcomed the introduction of the audit charter. The reason the CEO feared that the CAE would be reporting to the directors was used as an excuse, as the IIA draft clearly states the ideal reporting structure. i.e. that the CAE reports to the CEO administratively and to the audit committee functionally. It is apparent that the CEO feared that the CEO would become more powerful than him since he would be reporting to the Board Audit Committee, and this therefore, was a fight for turf. This is apparently confirmed by the fact that at one point, the CEO violated the provisions of this charter by refusing to produce a document required by an auditor during a routine audit, even after intervention of the CAE. The stance taken by the CEO put the internal audit function in an unenviable position, as full support of senior management is necessary for the function to operate effectively and efficiently. This was an impairment of internal audit independence.
4. 3.1.1 Dissemination of the provisions of the audit charter within the organisation

Internal auditors examine all aspects of an organisation. It is necessary that everybody within the organisation, from the CEO to the lowest graded employee within the organisation be aware of the provisions of the audit charter, because during the course of their duties they would interact with the internal auditors, and be requested to produce documents or be asked to answer questions. They should therefore be aware of the authority, duties and responsibilities of the internal auditors, so that they can willingly cooperate with the internal auditors.

Asked if the audit charter had been disseminated to everybody within the organisation, the CAE replied, “After it had been approved by the board, it was distributed to each of the officers who are the section heads and there was an instruction that they should also make sure that all staff are aware of it.”

However, on the ground, it appears the audit charter has not been fully disseminated or embraced by all members of staff. As one auditor put it,

The audit charter is excellent, but the implementation part of it is a challenge, especially when you have divisional heads here who do not understand what audit is. They view audit as somebody who is coming to look for errors. And automatically some documents will not be availed to you as and when you require them. Because the charter has not been fully embraced by the entire organisation. Whilst the audit committee has approved it and senior management has approved it, but the rest of the other managers, do they really appreciate what that document empowers the auditors to do?

The other auditors expressed the same sentiments, stating that on several instances auditees refused to produce documents required by auditors, stating that the information on those documents was confidential. The documents were only produced after the auditees were shown the audit charter.
From the views expressed by the auditors, it is apparent that the majority of staff were not aware of the provisions of the audit charter. Such a situation created unnecessary impediments to the smooth conduct of audits and was a threat to the independence of internal auditors. It was necessary to embark on an organisation-wide campaign to educate all staff on the provisions of the audit charter, soon after its introduction.

4.4 Reporting structures, audit coverage and independence of internal auditors

When determining the independence of the internal audit function it is important to look at the hierarchical positioning of the CAE in the organisation as well as the reporting structures applicable to him or her. The IIA recommends that the CAE reports to the audit committee functionally, and to any other senior official administratively (IIA 2004). The standard further explains that where the CAE reports to the CEO, there should be other mechanisms or arrangements to ensure that the CAE’s independence is not impaired.

Shown below are organisation charts for the 3 cases, showing the hierarchical positioning of the CAEs as well as their reporting lines. The organisation of all the three parastatals are shown first, thereafter discussions relating to the charts are given.

Figure 4.1

Case 1: Organisation chart
Figure 4.2

Case 2: organisation chart
4.4.1 Positioning of the CAE in the organisational hierarchy

As shown on the organisation chart for Case 2, (Figure 4.2), the CAE is positioned just below the CEO, at the same level as directors. This positioning signifies the importance attached to the internal audit function and engenders the cooperation of other senior executives and managers. It appears that at some point there was realisation of the importance
of the function, because, as one auditor put it, the CAE position used to be placed at middle management level. This is what he said:

I think on the original structure he was meant to be among the middle management, but since then, CSC has sort of gone through a transformation process over the years. He is now relatively very, very close to the highest senior official. Way back he used to be among the middle management. I think he has sort of ascended to an ex-officio position of even deputy chief executive officer

The situation was different for Cases 1 and 3 in that there was a layer of directors/general managers between the CAEs and the CEO. This layer of directors/general managers views the CAE as a junior in the organisational ranks, and because of this, they can resist being audited by their junior and his members of staff. Internal auditors in all three cases highlighted instances where senior managers resisted being audited, as a result of this perception. The situation in relation to Case 1 was worsened by the fact that, within the branch heads rank, in which the CAE was placed, there were three salary grades, and the CAE is at the bottom grade. As one of the internal auditors put it: “On the hierarchy of the organisation, he reports direct to the chief executive of course, but in terms of salaries and all that, he is down, even below the finance officer. His salary is also determined by the chief executive and not the audit committee.”

People usually associate the importance of a post or function by, among other things, the amount of remuneration it attracts. The fact that the CAE was at the bottom rung of the branch heads salary scales not only diminished his status in the organisation and the amount of respect he commanded among senior management, but also made it appear as if the internal audit branch was relatively less important than other branches. It is probably because of this that the internal auditors in Case 1 experienced a number of problems in the execution of their duties. These included demands by senior managers to be audited by internal auditors of grades equal to or higher than their grades, and refusal by some staff to produce documents required by internal auditors in the course of their duties.
4.4.2 Reporting lines for the CAEs

In order to maintain the independence of the internal audit function, IIA standards (IIA 2004) recommend that the CAE reports functionally to the audit committee and administratively to a senior ranking official who has the interests of the function at heart. What is involved in functional and administrative reporting is briefly outlined below, and thereafter the findings relevant to these aspects are then discussed.

4. 4.2.1. Functional reporting

In terms of the IIA practice advisory 1110-2 (IIA 2004), functional reporting is the ultimate source of the internal audit’s independence and authority and there is therefore need to report to the highest level in the organisation. The body to which the CAE functionally reports would:(IIA 2004)

- Approve the charter of the internal audit function;
- Receive reports of results of audit activities and have private meetings with the chief audit executive without the presence of management;
- Be responsible for hiring and firing the chief audit executive as well as determine the annual salary and adjustment;
- Ensure that there are no scope or budgetary limitations that impede proper execution of the internal audit activity’s responsibilities;
- Have final authority to review the annual internal audit plan and any changes thereto;
- Review performance of the chief audit executive at least once a year; and
- Facilitate open and direct access to the chair and members of the audit committee and the board.(IIA 2004)
4. 4.2.2 Administrative reporting

According to IIA practice advisory 1110-2 (IIA 2004), this is responsible for facilitating the day to day operations of the internal audit function and includes budgeting and management accounting, human resource administration, internal communications, and administration of the organisation’s policies and procedures. The practice advisory recommends that the person to whom the CAE should report to administratively, should have sufficient authority and a control and governance mindset, and an interest to support and ensure effectiveness of the audit function.

The dual reporting structure is supported by corporate governance guidelines (BRC 1999; Kings Report 2005). Empirical evidence indicated that there is movement towards adoption of this structure. Most of the studies carried out examined whether the CAE reported to the audit committee or to senior management. Goodwin and Yeo (2001) in their study, in Singapore found that the majority of CAEs (seventy-two percent) reported to the audit committee. In New Zealand, Goodwin (2003) found that fifty-two percent of the CAEs similarly reported to the audit committee. In Europe, Paape et al in their survey of 105 CAEs, found that slightly less than half of them reported to the audit committee. In Australia, Leung et al (2004) found that the majority of the CAEs reported to the audit committee. Turley and Zaman (2007) interviewed personnel of a large UK financial services company including the audit committee chair and the CAE. From these interviews, they argue that the audit committee is able to set the tone and strengthen independence of the internal audit function. Van Peursem (2005), in a multiple case study of senior internal auditors in New Zealand found that when there is a close relationship between internal audit and management, internal audit independence from management is threatened.
James (2003) examined the perceptions of bank lending officials in the UK regarding the impact of reporting structures on the ability of internal auditors to prevent fraud. He found that internal auditors who reported to management were perceived to be less able to prevent reporting fraud compared to those reporting to the audit committee.

It would appear that the practice of having the CAE report to the audit committee in gaining world-wide acceptance. There is also evidence that internal audit functions who report to management are perceived to lack independence. This is most likely because of the realisation of the need to have an independent internal audit function, as advocated by corporate governance guidelines, which have assumed prominence in the post-Enron era. Having looked at the IIA guidance and the corporate governance guidelines, it is now opportune turn to the findings of the present study.

4.4.2.3 Reporting lines for Case 1

Case 1 had an audit charter which provided that the CAE should report to the audit committee functionally and to the CEO administratively. However, it was found that in practice, the CAE reported both functionally and administratively to the CEO. By his own admission, the CAE confirmed this when he said “...we have our meetings on day to day activities and I submit reports weekly and quarterly to him (the CEO)”

Reporting directly to the CEO, who is an auditee impairs the independence of the CAE, and defeats the purpose of the dual reporting arrangement which is advocated by the IIA standards, and enshrined in the audit charter of this organisation.

The following findings were made in relation to the other duties that were supposed to be performed by the audit committee in order to safeguard the independence of the CAE and the internal audit function:
4. 4.2.3.1 Hiring and firing of the CAE

The hiring and firing of the CAE is one of the responsibilities of the audit committee. Previous studies found that in Singapore, seventy-two percent of audit committees, (Goodwin and Yeo 2001) and in Australia and New Zealand, fifty-two percent of the audit committees (Goodwin 2003) were involved in the hiring and firing of the CAE. However, Christopher et al (2009) cite lack of audit committee involvement in the hiring and firing of the CAE as a threat to the independence of internal auditors. Paape et al (2003), in their study, also stated that the audit committee was not always involved in the hiring and firing of the CAE. These studies show that there is a realisation that the CAE should be independent of senior management so that he/she can operate effectively and be able to report objectively on the performance of senior management. The findings of this study on this aspect follow.

The incumbent CAE had been appointed to the position prior to the introduction of the present audit charter. He stated that the CEO appointed him to the position. He opined that with the changed circumstances, after the introduction of the audit charter, the audit committee would most likely hire and fire the CAE. However, the principal auditors and auditors were of the opinion that the CEO would still be responsible as the relevant employment regulations relating to senior managers had not been changed to accommodate the provisions of the audit charter. It would seem that the later argument appears more plausible, because the employment regulations take precedence over the audit charter in issues relating to hiring and firing of staff. So until such time as the employment regulations are amended, technically, the CEO can appoint and dismiss the CAE.

This situation impairs the independence of the CAE. It should be borne in mind that the CEO is one of the auditees of the CAE. In fact, he is the main auditee, as he is in charge of the whole organisation. If an auditee becomes responsible for hiring and firing the auditor, there
is gross impairment of the auditor’s independence. It would be difficult for the CAE to report any adverse audit findings in the organisation, especially those relating to the CEO’s office. Before reporting any serious irregularities in the organisation, the CAE would assess whether doing so would offend the CEO, and if this would affect his continued employment within the organisation. The CAEs independence and objectivity is therefore impaired in such a situation.

4.4.2.3.2 Appraisal of the CAE

The CAE stated that he had never been formally appraised by the audit committee. Asked if the CEO was now appraising him, he replied, “Yes, in the sense that we have our meetings on day to day activities and I submit reports weekly and quarterly to him, so it’s not a formal method of appraisal, but at least he has a feel of how things are going”.

Formal appraisals are important as they enable the audit committee to determine the extent to which the CAE performed his duties satisfactorily. They also present an opportunity for the CAE to inform the audit committee areas where he is experiencing challenges, so that appropriate action can be taken. The audit committee is failing to discharge its mandate by ignoring this important responsibility.

4.4.2.3.3 Remuneration of the CAE

The remuneration of the CAE should be determined by the audit committee, in terms of the IIA standards. In this organisation, however it is determined by the CEO together with those of other senior managers. This is a threat to the independence of the CAE, and the internal audit function, because the CAE will be under pressure not to issue any adverse reports for fear that this could result in the CEO refusing to grant him salary increases or other benefits.
4.4.2.3.4 Accessibility of the audit committee chairperson

The CAE stated that the audit chairperson stayed in Harare, and they only see him when he comes for board meetings. He however said that they communicated through e-mail and by cell phone. I feel that the chairperson of the audit committee should periodically walk the job, by visiting the internal audit section in between meetings, which are held quarterly, in order to get an appreciation of what is happening on the ground, and fully understand the environment in which the internal audit function works. This would enhance relations with internal audit and facilitate dialogue between the two, thereby enabling the internal auditors to report any threat to their independence.

4.4.2.3.5 Private meetings with the audit committee chairperson

Asked if he had any private meetings with the audit committee chairperson to discuss sensitive issues, the CAE replied, “Yes, only once when we were attending the annual conference of the Institute of Internal Auditors in Victoria Falls. He was also a participant. That was in September last year.”

It appears that this was just chance meeting and not pre-planned as envisaged by the IIA standards. Both parties happened to be at the same place at the same time and had some free time and decided to discuss a few business issues. It appears there was no effort by either party to have these meetings. I feel that these meetings are important, considering that the CEO is a member of the audit committee. The CAE would not be in a position to discuss sensitive issues in the presence of the CEO during the audit committee meetings. If such meetings are not held, there is a possibility that some matters which require the attention of the audit committee would not be addressed, as there would be no proper forum for the CAE to raise them.
Prior studies have found that when the audit committee is composed of independent directors, the CAE is has access to the audit committee chair and has private meetings with the audit committee chair. Goodwin and Yeo (2001) found that when all members of the audit committee are independent, the audit committee had more frequent meetings and more private meetings with the CAE. Raghunandan et al (2001) also found that audit committees with independent directors and at least one member with financial expertise held longer meetings and had private meetings with the CAE.

Private meetings give the CAE a chance to discuss sensitive issues with the audit committee chair. The fact that these were not held in this case is probably due to lack of interest by the audit committee chair, which is apparent in this study. Furthermore, fact that the CAE effectively reported to the CEO could have discouraged him from asking for such meetings for fear that the CEO would think that he was passing adverse reports to the audit committee chair. Such suspicions would strain relations between the two to the detriment of the CAE.

4.4.2.4 Reporting lines for case2

This case did not have an audit charter, but the CAE stated that he reported functionally to the audit committee and administratively to the CEO. However the principal auditor said that the CEO reported directly to the CEO both functionally and administratively. This view was also supported by the internal auditors who added that whereas the CEO was involved in the day to day activities of the audit function the audit committee was not at all involved. This was also given credence by the fact that the CAE is based in Bulawayo, and the audit committee chairperson is based in Harare. One of the internal auditors said,

I think the effect of such an arrangement whereby the CAE reports direct to the chief executive officer is whereby you, the ones who are on the ground and carrying out audit work, you will be sort of, how can I put it, you are weakened. You no longer have the independent mandate because your leader is part and parcel of the ones you are auditing. So at the end of the day you are weakened, so that definitely, your work is compromised.
When I visited the organisation during field work I also observed that, on a number of occasions, the CEO and the CAE were holding discussions in either the CAE’s or the CEO’s office. This seemed to confirm the involvement of the CEO in the day to day activities of the internal audit function.

Reporting functionally to the CEO erodes the independence of the CAE, for the simple reason that the CEO is an auditee. The auditors would be constrained from passing adverse reports on their boss, for fear of offending him/her and possibly losing their jobs. In such a situation, the audit function ceases to serve the organisation but serves the CEO, to the detriment of the organisation. Consequently the independence of the CAE, and the whole audit function was severely compromised as a result of this reporting arrangement.

4.4.2.5 Reporting lines for case 3

In this organisation, there was no board of directors and as a result, no audit committee. The CAE reported directly to the CEO who was also responsible for the hiring, evaluation and terminating the services of the CAE. In this situation the independence of the CAE was severely compromised. The CEO is an auditee, in fact the main auditee of the CAE. If the auditee becomes the boss to the auditor then obviously, the auditor would find it very difficult to report adversely on his or her boss, for fear of losing his or her job. The IIA standards state that where the CAE reports to the CEO, there should be other arrangements or mechanisms to ensure the independence of the CAE despite this reporting structure. In this case, no other mechanisms were in place to ensure the independence of the CAE. In fact, her independence was further affected by the fact that she is placed on the fourth tier, on the hierarchy of the organisation. People normally associate the importance of a function in the organisation to the position it occupies in the organisation structure. In this particular case, senior executives would tend to attach little importance to the audit function, and not
cooperate fully. Moreover the perception in the whole organisation might be that internal audit is not so important. All this tends to weaken the independence of the internal auditors and the respect they command in the organisation.

4.5 Relations with other corporate governance arms

4.5.1 Relations with the audit committee

The audit committee is the grantor and guarantor of the independence of the independence of the internal audit function. This committee should be independent and should comprise only of non-executive directors, to ensure that there is no influence from executive directors. This view is advocated by various corporate governance codes, including the Cadbury report (1992), the Blue Ribbon Commission (1999) and the Smith Guidance (2005). It should also have a financial expert, who would appreciate the need for independence of the internal audit function and the need to give the function full support, so that it executes its duties without interference from any quarters. A summary of the duties of the audit committee has already been given in paragraph 4.4.2.1.

Various scholars have examined different aspects of the relationship between the internal audit function and the audit committee. Turley and Zaman (2007) in a study involving interviews with staff of a large financial services company in the UK, concluded that the audit committee was able to set the tone and strengthen internal audit independence in an organisation. Mat Zain and Subramaniam (2007) in their study of 11 Malaysian organisations found that internal auditors trust the audit committee and rely on it to ask tough questions to management. The findings of Goodwin and Yeo (2001) and Raghundanan et al (2001) in respect of meetings between internal audit and the audit committee (refer paragraph 4.4.2.3.5 above) are also relevant here.
Previous studies support the IIA and corporate governance guidelines for the composition of the audit committee (that it should comprise of independent directors), that the audit committee should hold private meetings with the CAE, and that the audit committee should safeguard the independence of internal audit.

Contrary to the provisions of the corporate governance codes cited above there were executive members in the audit committee of Cases 1 and 2. In Case 1, the CAE, principal auditors and internal auditors all acknowledged the presence of the CEO in the audit committee. This situation is untenable. As he is one of the auditees it would not be possible to discuss issues impinging on the performance of the CEO, any other senior executives or any other sensitive issues in audit committee meetings during his presence. The CAE as someone reporting to the CEO would not be free to discuss deficiencies in performance of the CEO in his presence. These sentiments were expressed by one of the principal auditors, who said:

…the audit committee is comprised of three board members including the chief executive himself. So if there are any issues which one wants to report pertaining possibly to the chief executive or his subordinates, we might find it difficult to report. In short our reporting there is compromised although we have got the audit committee.

The auditors also expressed reservations over the issue, when one of them said,

…because unfortunately, our chef executive also sits in the audit committee. You get me right…..But as long as we have a chief executive who sits in the audit committee there is bad corporate governance. Because this is the only opportunity where the CAE can freely, freely discuss issues pertaining to the organisation with the audit committee members, representing the board of directors. But now, here is an auditee there, who happens to be also part and parcel of the audit committee. His office also comes under your purview. He is sitting there. Are you able to articulate issues pertaining to his particular office?

The CAE was also not happy with this set up and had this to say,

It comprises of three non executive directors, and the fourth one is the chief executive officer or general manager, which according to the institute of internal
auditors standards is a misnomer. He is not supposed to be sitting there except by invitation by the chairman if he is required.

If issues pertaining to top executives cannot be discussed by the body which is responsible for overseeing the financial matters of the organisation, then there is a real possibility of major financial scandals occurring right under the nose of the audit committee.

In relation to case 2, although the CAE stated that the audit committee comprised of non executive directors only, the principal auditor said that the CEO and the finance manager were also members. This situation impaired the independence of both the audit committee and the CAE

The audit committees of both cases 1 and 2 also failed to exercise their oversight duties, which were highlighted in paragraph 4.4.2.1, and this had an adverse effect on the independence of the internal audit functions of these organisations.

In response to the question, “In what way has the audit committee given you support?” the CAE said the audit committee demands action from management to implement audit recommendations. The principal auditor stated that they got audit reports, commented on them and made suggestions on how to improve audit work.

When it came to the internal auditors, however, they felt that the audit committee had had no impact whatsoever. One of them expressed this as follows, “... in terms of functionality, I think they have let us down. They are not serving their purpose. I would say it is window dressing...” They cited as an example the fact that although they are not members of the IIA, the audit committee had done nothing to ensure that they became members. They also pointed out that they had never seen or interacted with any member of the audit committee or received copies of any communication from the committee. They only saw their names on
letterheads. None of their problems had received the attention of the committee, and so to them the situation is as if there was no audit committee at all.

As the body charged with the responsibility of overseeing not only internal audit, but the entire financial and reporting aspects of the organisation, the audit committee is expected to take a keen interest in the activities of the internal audit function. This includes ensuring that it is well resourced, ensuring that the auditors have free access to all records personnel and properties necessary in the carrying out of their duties, and ensuring that auditors enjoy independence in the performance of their duties. One would expect the chairman of the audit committee to walk the job by visiting the offices where the auditors operate from, seeing whether they are adequately resourced, hearing their concerns, and setting up communication lines with them. The fact that this did not happen implies that the audit committee was not properly playing its role of ensuring that auditors were adequately resourced, and that there was no interference in their work. The sentiments expressed by the internal auditors seem to reflect the fact that is obtaining on the ground, i.e. that the committee was not properly executing its duties and responsibilities. The audit committee has a responsibility to safeguard the independence of internal auditors. If they neglect this responsibility, the internal auditors are exposed to various threats of their independence.

4.5.2 Relations with management

In all three cases, the CEOs had taken upon themselves to directly supervise the operations of the internal audit functions instead of leaving the functional reporting of the CAE to the audit committee, thereby seriously impairing the independence of the internal audit functions. Although the CAEs stated that they were satisfied with the cooperation they were getting from management, principal auditors and internal auditors stated that they were experiencing a number of problems with mangers, in the field, when performing audits.
The auditors pointed out that senior managers at times prevented them from examining certain areas. As one of them said,

Some threats also arise verbally whereby, at times, you go, you are carrying out your work as an auditor and you go to the auditee’s office and you are told, no, you are too junior to carry out this work, definitely you feel threatened. Or you are told, this is a no go area or you are just told, the chief executive officer's office is handling this and that’s that. But you see, during the audit process, that will be an area of emphasis, you will be seeing more risks in that area and then you are told, no it’s not your area. So at times it is a threat.”

The principal auditor seemed to confirm this when he stated that there was “indirect resistance from certain levels of the organisation.” Senior manager should actually welcome and cooperate with the internal auditors, because they (auditors) assist them make their units more efficient, thereby ensuring that targets and objectives are achieved. The question of whether the auditor is junior to the manager or not should not arise. Internal auditors are there to audit the system and not the person, so there is no need to determine the hierarchical position of the internal auditor before deciding to cooperate with him or not. The internal auditor and the manager have the same objective, that the organisation achieves its objectives in the most efficient and economic manner, and continues to survive, grow and improve its operations. As such there should not be any friction or animosity between them.

The lack of cooperation was also experienced at the highest levels in the organisations one of the internal auditors related his ordeal with the CEO

I will tell you my personal experience with the chief executive. I wanted a document from his office. He said to me get out!. Get out!. Get out!. I refused to get out, I just stood there for some time. Then he said, Come let me give you what you want. Then he produced document I wanted and then he blocked the upper part and the lower part of the document leaving one paragraph, and he said, what you want is just this paragraph.. and I said it will not make sense, I want the whole document. He said no, phone your boss. I phoned him from his (CAE’s) office, and he told the chief executive officer to give me what I wanted. But still he refused. He only photocopied just that one paragraph.. which did not make sense. And this is the chief executive who is supposed to know the role of internal audit.
Asked if this was due to the fact that the CEO was not aware of the need for auditees to produce all documents required by the internal auditor, another internal auditor stated that

I think that should be assumed knowledge. We will assume that as they get up there to chief executive, we cannot expect a chief executive who doesn’t know the role of internal audit. It’s assumed knowledge. He is supposed to know. We cannot have time to teach him the role of internal audit. He is supposed to know.

Such resistance at these high levels which should be encouraging cooperation with internal auditors is hard to understand, and make it hard for internal auditors to execute their duties smoothly.

4.5.3 Relations with external auditors

In all three organisations, the internal audit functions had cordial relations with the external auditors. There were no cases of the external auditors dictating to the internal audit function what to include in their work plans or how to conduct their audits. In this respect, all three internal audits departments were independent of the external auditors.

4.6 Threats to independence and objectivity

4.6.1 Audit of top management

In case 3, auditors indicated that top management was not covered by internal auditors, and that this was an area where auditors had to be very cautious, “…in order not to cross the path of the bosses.” One internal auditor said that “independence from interference is not guaranteed, hence the need to be very careful,” and went on to say “… you definitely need to be very careful, otherwise you step on slippery ground and end up on the receiving end.”

From these remarks and sentiments, it was apparent that top management was not subjected to any meaningful audit examination. As one of the auditors put it, “… senior management operate as they please or see fit and to their advantage and it is not safe for anyone to question.” This situation is unacceptable, considering that most of the serious financial
scandals are perpetrated at this level in organisations. Examples where top management were involved in financial mismanagement include the Enron scandal in the USA (Schwartz, Dunfee and Kilne 2005), Cold Storage Commission (CSC) (Daily Gazette 6 January 1993 and 26 May 1993), Zimbabwe United Passenger Company (ZUPCO) (The Financial Gazette, 13 July 2006 and 17 April 2008), and more recently the ZBC salary scandal (Daily news, 13 December 2013) and the PSMAS salary scandal (Newsday, 31 January 2014).

4.6.2 Audit of senior management payroll

Internal auditors in Cases 1 and 2 were prevented from auditing the pay and perks of senior management executives. In Case 1, the audit of salaries and perks for senior executives was not included in work plans for the section which is responsible for the audit of the organisation’s payroll. In terms of the CEO’s directives, this audit was to be done by the CAE, in the CEO’s office, and under the watchful eye of the CEO. Nothing was to be taken out of the office, and the resultant report was made to the CEO only. It was learnt that the reason given for this arrangement was that the remuneration packages of top executives was confidential information, and therefore a high degree of secrecy had to be maintained.

As alluded to in paragraph 1.7, audit independence comprises: programming independence (the auditor has control over the nature of the audit program), investigative independence (the auditor is free to collect and evaluate all the evidence deemed necessary without interference) and reporting independence (the auditor is free to report the results of the audit without interference) (Mutchler 2003). The situation prevailing in the audit of senior executives’ remuneration packages contravenes all three components of audit independence. The payroll section which has expertise in the organisation’s payroll procedures is prohibited from carrying out the audit of this area, and this is left to the CAE, who might not have an intimate knowledge of payroll matters. Additionally, restricting the CAE to the CEO’s office, and
prohibiting him/her from carrying anything out of that office is tantamount to interfering with the investigations. Directives as to whom the report should be made also contravenes reporting independence.

In case 2, the auditors stated that they were prevented from performing the audit of the senior management payroll, on the pretext that they were too junior to get that information. This is what one of the auditors had to say,

…the last time we carried out an audit of head office, we had problems with senior management furnishing us with information concerning the payroll of the senior management level. They didn’t want to avail that to us as internal auditors, who were carrying out that specific duty. Their argument was that you are too junior for us to show you that information, you are not privy to that, of which that rendered our independence compromised at the end of the day.

Asked if they eventually got the information they required, they replied

They never gave it to us…to some extent they would actually make concessions, like, say, they said, you can have your head of department, who is the chief internal audit manager come to do that work, of which, we felt, as people who were carrying out that work on the ground, we had the right to complete the process ourselves.”

The auditors now regard this as a no go area.

Parastatals are heavily subsidised by public funds through the fiscus. They should therefore be accountable to the public on how they use those funds. The stance that executive pay remuneration packages should be kept confidential or that certain auditors are too junior to conduct the relevant audit does not seem justifiable, in view of the fact that those who fund the organisation have a right to know how the money was used. There is a need for transparency and this requires that all aspects of the organisation should be subjected to an independent internal audit scrutiny.

It is also interesting to note that this is an area which is risky and prone to financial scandals. The recent revelations at the Zimbabwe Broadcasting Corporation (ZBC) where the CEO was
drawing a monthly salary and perks amounting to a shocking $40,000, while other employees had gone for seven months without being paid their monthly salaries, (Daily news, 13 December 2013) and at PSMAS where the CEO was getting $230,000 per month while the institution was struggling to clear outstanding creditors amounting to $40 million (Newsday, 31 January 2014) illuminate the need for an independent internal audit scrutiny of executive pay and perks.

4.6.3 Role conflict for the CAE

In case 2, the CAE admitted that he sometimes acted in the position of CEO. Such an arrangement was susceptible to the threat of self-review. When the CAE got back to his office after an acting stint, the decisions he made and work he performed as an acting CEO would be subjected to internal audit examination. As he was the head of the internal audit function, this would be a clear case of auditing one’s own work, or self-review. If that audit examination revealed anomalies in the work he performed as an acting CEO, there would be a strong temptation for him to water down the findings or not to report them at all.

The auditors also felt that the CAE had abandoned them and joined forces with the auditees and one of the internal auditors said “... because our senior internal auditor, who is supposed to be the chief internal audit manager has sort of become part and parcel of the executive management, so we are quashed or abandoned, because he has gone to the other side instead of being our leader.” This is a very strong statement and shows the degree of frustration that this arrangement is bringing to bear on the auditors.

It is apparent that these acting stints have impaired the CAE’s independence, both in appearance and in fact. It is advisable to stop these acting stints in order to retain the independence and effectiveness of both the CAE and the internal audit function.
4.6.4 Veiled threats by CEO – wanton dismissals of senior staff

In case 1, it was also stated that, during the period 2013 to 2014, a number of employees from the officer grades to director levels were forced to resign by the CEO for no apparent reason. One director, for example, was forced to retire three months before his retirement date. He was given the choice of retiring immediately or working in the CEO’s office, where he would no doubt be dismissed. He opted to go on immediate retirement. To the staff in general this was interpreted as a demonstration of absolute power to fire anybody within the organisation, without having to explain the reasons for such action to anybody in or out of the organisation. This is considered a threat to the whole organisation, and certainly to the independence of the internal auditors. In such a situation it becomes difficult to report anything that might offend the CEO for fear of his/her reaction. Intervention of the board is required to restore independence of the audit function and to remove the culture of fear in the organisation.

4.6.5 Restrictions on access to document and information

Instances of refusal to provide documents and information required for the audit were raised by the internal auditors. Departments mentioned include the manning section of the manpower branch, where information was said to be confidential, as it related to promotions. In other instances, auditors had problems with managers who stated that they could only deal with similarly graded internal audit staff. To overcome this resistance, internal auditors in Case 1 had to produce the audit charter. The managers cooperated after seeing that the audit charter was signed by the CEO and the chairperson of the board of directors. However, in some cases the internal auditors had to phone the CAE and ask him to speak to the errant managers, and only after he had spoken to them did they cooperate with the internal auditors.

It appears that refusal to cooperate stemmed from ignorance of the provisions of the audit charter in case 1. Therefore, an education campaign to ensure everybody is fully aware of the
provisions of the audit charter was necessary. The CAE, principal auditors and auditors all agreed that this campaign was long overdue.

4.6.6 Provision of resources by auditees

A number of auditee branches control and provide resources that are needed by internal auditors to carry out their duties. These resources include cash, fuel and guest houses. Internal auditors in all three cases complained that this put them at the mercy of auditees, who at times withheld the resources for no apparent reason, thereby frustrating their efforts and weakening their effectiveness. Planned audits had to be rescheduled at times, and at other times, resources were only released after recourse to the finance director, through the CAE.

This arrangement has several disadvantages that were mentioned by the auditors. Auditees in out stations were pre-warned of the auditors’ impending visit by the resource providers, and as a result the surprise element which is essential in certain types of audits like cash counts was killed. As one auditor put it, “If you want to do a cash count, you need not tell people that you are coming. The surprise element is no longer there (if they know you are coming) ... and you find that pilferages which happen are only discovered when it’s long overdue. So independence is not there.” Prior knowledge of the auditor’s impending visit gives the staff in charge of cash an opportunity to cover up any deficits.

The auditors also pointed out that if you were going to audit an area that fell under the provider of resources and he was aware that there were irregularities in that area, he or she would not give auditors the resources they needed. As one auditor put it

In terms of resources, we are supposed to be resourced somewhere else other than by the auditees, because we are dependents of the auditees instead. For us to articulate any task we have to first beg. Then the independence part of it is already compromised, because you have to say out what you are to do where you are to go.... and we are supposed to be given, or to have our resources availed in a different scenario which doesn’t involve our auditees. Because, for an example,
you want to go to Harare, you have to ask from the auditee if he can accommodate you, if he can feed you, if he can give you fuel, or back up service. Then the whole scenario is compromised. So, obviously we are not independent.

The sentiments expressed by the auditors were also expressed by the CAE, who said

…but we have a major challenge of resources, especially transport and accommodation and sometimes we have to go begging to the finance director to get money for relief expenses and to procure accommodation and when it is not available at a time when we want to do the audit, that means we end up having to postpone.

Internal auditors also pointed out that at times resources were used to hit back at the auditors after an adverse audit report. As an example, auditors stated that when they joined the organisation as internal auditors, they were initially getting their salaries on time. However, as time went on, after doing a number of audits, this ceased to be the case, and they were told that due to liquidity problems, they could not get their salaries on due dates. This trend had continued since then. As one internal auditor put it, “So you would like to wonder, is it because of your work or is it a genuine problem? So sometimes we feel threatened that we might be going were we should not be going”.

Some auditors also felt that resources were withheld in order to frustrate their efforts, and in this respect one of the internal auditors said “…I would like to think that at times the way they are not providing these resources, they are trying to make us weak so that they can push you around. It’s like they are dictating the pace, and at the end of the day, definitely our output will be affected.” The internal auditors pointed out that they were not provided with such basic office items as computers, and yet they were supposed to audit computerised systems. In comparison, their auditees had computers, had to bring their own laptops, to use for internal audit duties. Failure to provide computer resources has also meant that they cannot use modern computer assisted audit techniques (CAAT), which are more efficient and cost effective. The auditors were of the opinion that their requests for resources were given a
very low priority compared to requests from other departments. They said, “If you want to go on a trip, you will be told that there is no money. But if you look at it, you find that the money will not be available only when it is demanded by the audit department.” As a result of this practice, audit coverage was adversely affected. They pointed out that in some cases, only one audit was made when at least three had been planned. As one of the internal auditors pointed out, “...because of limited resources, the audit will not be able to execute as per plan, but, however, work with what is provided, hence audit work will be compromised”

Failure to provide internal auditors with resources as and when required weakens the effectiveness of audits and unnecessarily disrupts the proper execution of internal audit duties and completion of planned workloads. It is also pertinent to note that if the audit committee had a keen interest in the activities of the internal audit function, as they should, it would ensure that these resources are provided as and when required by the internal auditors. Lack of interest by the committee weakens the independence of the internal audit function.

**4.6.7 Threats of physical harm by auditees**

Of concern was the degree of militancy that had crept into case 1. This unfortunate development was highlighted by one of the auditors who said

We had quite a numerous number of threats to the extent that some of us acquired firearms at home in order to protect our property at home. Because auditors are not necessarily the best friends of most people in the organisation. When somebody is fired as a result of an audit, it is taken that it is the auditors who have got him fired. And we have had situations where, like workers’ union leaders would address their constituencies to say, auditor so and so is the one who is on us, making sure that our members are fired. Already that is a threat, and we feel very much threatened, and we were actually assisted by some members of the organisation to get firearms, because we were now afraid that the threat would now come outside the framework of the work environment. Those threats are there, but it has never stopped us from doing our work.
This was confirmed by one principal auditor who said, “We have had some instances where auditors were threatened. Some of the auditors were threatened. Some ended up arming themselves, buying rifles. So I take that one to be one of the threats”.

The CAE also confirmed this when he said “The unions have instructed their members not to cooperate especially if you are investigating fraud.” This stance by the unions was ill advised, as it amounted to condoning fraud in the mistaken belief that they would be protecting their members.

4.6.8 Lack of cooperation from trade unions

The CAE for case 1 stated that the trade unions had instructed their members not to cooperate with internal auditors, especially on fraud investigations. This was also confirmed by the auditors who cited several instances of lack of cooperation by staff, involving such issues as refusal to supply information/documents required during an audit. The CAE, principal auditors and auditors were also concerned by the degree of militancy that had crept into the organisation. Auditors were threatened with physical harm, through anonymous phone calls. This got to an extent where the threats could not be ignored, and some auditors were assisted to acquire firearms to protect themselves and their families. This organisation has a history of highly organised trade unions, which fight very hard for the improvement of the working conditions of their members. However, the instruction not to cooperate with internal auditors investigating fraud is regrettable as it unnecessarily disrupts internal audit activities, and might encourage criminal-minded employees to commit fraud. It amounts to interference with activities of internal audit work, which is a violation of audit independence. Perhaps it could be as a result of the fact that the trade union leaders did not understand the duties, authority, and responsibilities of the internal audit function, and had not had sight of the audit charter.
4.6.9 Processing of adverse reports on senior management

In all three cases, the auditors expressed concern and displeasure at the way adverse audit reports on senior staff were processed. They stated that these reports were submitted to the CAE, and after that they were told that the reports would be actioned by senior audit staff, that is, either the principal auditor or the CAE. However, the auditors had observed that in most cases, no action was taken thereafter. This is what one of them said when asked if they made follow ups to these reports, “Yes, we do, but sometimes we find if its involving senior staff, sometimes its only left in the hands of our superiors. We are told that it will be followed up by the senior guys. Sometimes it’s just left like that.”

A principal auditor also cited instances of watering down of audit reports from internal auditors by the CAE. These related to senior managers who were in good books with the CAE, and an employee who had done him some favours. Such actions frustrate the efforts of the internal auditors, and set bad precedents. They are also a violation of auditing ethics of independence and objectivity. There should be no “sacred cows”. Everybody should be treated equally. Those whose transgressions are condoned may think they are untouchable and commit more serious defalcations, to the detriment of the organisation.

I also feel that the auditors should be allowed to follow up and ensure that corrective action is taken or that audit recommendations are implemented, regardless of the status of the auditee. Giving special treatment to senior staff creates problems in that they could construe this as an indication that they can choose not to cooperate with the auditors if they so wish. This would lead to unnecessary disruptions in the smooth flow of audit work.

4.6.10 Familiarity threat

This threat arises from close or long term relationships with the auditee, which may influence the auditor to be lenient towards the auditee. All participants acknowledged the presence of
this threat, as auditors had close friends and relatives in other departments. Of concern however, was the fact that there were no guidelines in the form of a written procedure on what to do when the auditor was faced with this or other threats. The auditors stated that they would recuse themselves from audits where close friends or relatives were the auditees. The general view among all participants in the internal audit functions was that each auditor would use his or her professional judgement and avoid auditing their friends and relatives. However, one internal auditor seemed to contradict this sentiment when he said, “So, yes, I can safely say we do audit our friends at some point but we still try to maintain our independence in the course of duty,” indicating that he would not recuse himself, but continue with the audit and try to be impartial. The CAEs and principal auditors were also of the opinion that internal auditors would use their professional judgement in determining situation where their independence is compromised and recuse themselves from such assignments.

However, it came to light that not all internal auditors were recusing themselves from such situations, as highlighted by one principal auditor who said,

I have observed, in fact, I have come across a number of situations where an auditor would hide information, very critical information or some anomalies, simply because the auditee is a family member or a girl friend. This has happened in my section on several occasions. I can cite a number of cases or a number of examples.

This revelation indicated that not all auditors were using their professional judgement to avoid such situations. It was necessary to have a written procedure for dealing with threats to independence, for the guidance of internal auditors.
4.7 Summary

The research findings were presented and discussed in this chapter. It was noted that all three parastatals were staffed with adequately qualified and experienced internal auditors, with males widely outnumbering females. There were attempts in all three parastatals to adopt the IIA IPPF. However, none of the internal auditors were members of the professional body. Internal auditors cited lack of financial resources as the biggest obstacle to their joining the professional body and suggested that the employer should help finance the required fees and subscriptions.

In all three parastatals the CAEs effectively reported to the CEOs, although, in two cases, on paper, they were supposed to report to the audit committee functionally and to the CEO administratively. This reporting arrangement had greatly compromised the independence of the CAEs, as they were now reporting to an auditee. In the case of the third parastatal, the CAE reports to the CEO both functionally and administratively, without any other safety guards to guarantee her independence. The independence of the CAEs and the internal audit functions in general was also weakened by the inclusion of some senior executives in the audit committees. This also weakened the independence of the audit committee itself.

Independence of the internal audit functions in the 3 parastatals was also threatened by their reliance on auditees, mainly the finance departments for the provision of resources required to perform their duties. Cases of intentional withholding of resources were mentioned, and these led to unnecessary disruptions to planned workloads.

Interference in internal audit work was cited by internal auditors in that activities of senior management, mainly their payroll were not subjected to proper internal audit scrutiny. Some senior executives also resisted and resented being audited by junior staff. Additionally, it was
stated that all irregularities committed by senior staff were dealt with by the CAEs, and internal auditors never got to know how they were concluded.

Familiarity was also mentioned as a threat. Some internal auditors have audited close friends and relatives, when they should have declared a conflict of interests and recused themselves from the particular assignments. This occurred because there were no written guidelines on how to manage threats to independence and objectivity.

It was also noted that there were no written down procedures for dealing with threats to independence and objectivity of internal auditors. Such documented procedures would assist the internal auditors to identify, assess and manage any threats they come across during the course of their duties.

The next chapter deals with conclusions and recommendations of the study.
Chapter 5

Summary, Conclusions and Recommendations

5.0 Introduction

This chapter starts with a chapter by chapter summary of the whole study. This is followed by conclusions and recommendations of the study and finally recommendations for future research.

5.1 Summary of the study

A chapter by chapter summary of the study is given below.

5.1.1 Chapter 1: Background to the study

This chapter provided the background to the study. It was highlighted that financial scandals continued to occur despite the presence of internal auditors in the respective organisations, and this triggered the interest in the research. A review of literature did not reveal any previous studies on the independence and objectivity of internal auditors in Zimbabwe. Therefore, this study was undertaken to fill that gap in knowledge. The terms, internal auditing, independence and objectivity were defined. A brief history of parastatals was also given, and it was noted that the current thrust was towards commercialisation and ultimate privatisation of parastatals, an endeavour in which an independent internal audit function in each parastatal would play a significant role. The statement of the problem was given, the purpose of the study, its significance and objectives were also explained. The research questions were stated. Limitations and the delimitation of the study were also described. The last item was ethical considerations observed in the conduct of the study.
5.1.2 Chapter 2: Review of related literature

In this chapter, an account of the relevant literature reviewed was given. The theoretical framework informing the study was discussed. The meaning of independence and objectivity in internal auditing was explored. Reference was made to the standards and ethics of other professional accounting and auditing bodies, including AICPA, IFAC and INTOSAI. Extensive reference was made to the IPPF which contains the ethics, standards and practice advisories for the internal auditing profession. Previous studies on the independence and objectivity of both internal and external auditors were reviewed. Corporate governance codes, including the Cadbury report and the Smith guidance were studied. Enterprise risk management frameworks were also reviewed to determine to what extent internal auditors can involve themselves in these activities without impairing their independence and objectivity. Literature relating to the identification, assessment and management of threats to independence and objectivity of auditors was also examined, in order to learn lessons regarding how various accounting and auditing professional bodies deal with this important aspect of auditing.

5.1.3 Chapter 3: Research methodology

This chapter described the research methodology employed in this study. The underlying philosophy of the study, namely, interpretivism, the research method, i.e. the qualitative method and the research design, namely, a multiple case study were explained and justified. The population of the study, the sample selected and the sampling method were described. Data collection instruments used, namely, the researcher, interview guides, focus group discussion guides and questerviws (questionnaires with open-ended questions) were described. Data analysis procedures employed as well as strategies used to ensure
trustworthiness of data were explained. Finally, Ethical considerations observed in the study were explained.

5.1.4 Chapter 4: Presentation and discussion of research findings

In this chapter research findings were presented and discussed. The bio-data of the participants were given. In all the three parastatals, the IIA standards and ethics had not been fully adopted although the intention to do so was there. In all the three parastatals, CAEs reported both functionally and administratively to the CEOs resulting in their independence being severely curtailed. The inclusion of senior executives in audit committees of two of the parastatals further weakened the independence of both the internal audit functions and the audit committees. Reliance on auditee departments for resources to carry out audits (e.g. cash, fuel, accommodation) threatened the independence of internal auditors. There were also cases of intentional withholding of resources which led to disruptions to work plans. It was also noted that some senior managers resisted and/or resented being audited by junior staff.

In all the three cases, internal auditors were prevented from auditing the payroll of senior managers, an area which is considered risky. The familiarity threat was also present in all the parastatals, as some internal auditors audited their close relatives and friends instead of declaring a conflict of interests and recusing themselves. It was also noted that there were no laid down procedures for dealing with threats to independence and objectivity in all the three parastatals.

5.2 Conclusions

The conclusions are discussed under the respective research questions
5.2.1 Research question 1

To what extent do the reporting structures ensure broad audit coverage and freedom from interference in audit work?

5.2.1.1 Conclusions

5.2.1.1.1 CAE position in the hierarchy

IIA standards require that the CAE should be in a senior enough position in the organisational structure, to enable him to command the respect he or she needs in order to perform his or her duties effectively. Such a position would be within senior management and just below the CEO. In Case 2, the CAE was placed just below the CEO, and this conforms to the requirements of the standard. In Case 1 there was a layer of directors between the CAE and the CEO. Moreover, in terms of remuneration, the CAE earned less than other managers who are on the same level. This weakened the respect he commanded in the organisation, as the other senior managers tended to view the internal audit function as less important than the other functions. This created challenges in getting cooperation of the auditees, and was a threat to the independence of the internal audit function.

5.2.1.1.2 Reporting structures

On paper, the CAEs in Cases 1 and 2 reported to the audit committee functionally and to the CEO administratively. However, in practice, they effectively reported to the CEOs, as they reported regularly (daily/weekly) on the activities of their functions. The fact that the CAEs were based in Bulawayo while the CEOs were based in Harare seemed to have encouraged this practice. In Case 3, the CAE reported to the CEO. Reporting to the CEO adversely affects the independence of the internal audit function. In such an arrangement, the CAE was reporting to an auditee, and it would be difficult if not impossible to issue an adverse report.
on the official who was responsible for hiring, evaluating and terminating his or her employment with the organisation. Consequently, the CAE and the whole internal audit function did not have independence. In organisation 3, the CAE reported to the CEO, and there were no other arrangements to ensure that her independence was maintained. So she also did not have independence.

The lack of independence has affected audit coverage, as there were scope limitations regarding certain areas. In all Cases the remuneration of senior management could not be audited by internal auditors, and there were various restrictions. It can therefore be concluded that the reporting structures do not enhance audit coverage.

5.2.2 Research question 2

How much do relationships between Internal Audit (IA) and other corporate governance arms (the board, management, and external audit) enhance effectiveness and good governance?

5.2.2.1 Conclusions

5.2.2.1.1 The audit charter

This is an important document, as it alerts everybody within the organisation of the purpose, authority, duties and responsibilities of the internal audit function. Only Case1 had an audit charter. The only challenge was that it had not been distributed to all personnel within the organisation. This threatened the independence of internal auditors in that out of ignorance, some managers resisted being audited by junior staff or refused to provide auditors with information because they felt it was confidential. The other two parastatals did not have audit charters and their independence was similarly negatively affected.
5.2.2.1.2 Relations with the Board and the audit committee.

The internal audit function interacts with the board of directors through the audit committee. The independence of the audit committee in Case 1 was compromised by the inclusion of executive management, that is, the CEO for Case 1 and the CEO and finance manager for Case 2. This affected the independence of internal audit because the CAE would not be comfortable to bring to the committee and discuss freely issues pertaining to poor performance of the senior management. Case 3 did not have any board of directors and as a result it did not have an audit committee, therefore the independence of internal auditors in this parastatal was also adversely affected.

In all the three parastatals, the audit committees did not effectively perform their duties. This is evidenced by failure of the audit committee to ensure that risky areas like senior executives’ payroll were properly audited, and failure to ensure that internal audit functions had adequate resources to carry out their duties. As a result, internal auditors were prevented from auditing certain areas, which is a scope limitation, and amounts to impairment of audit independence. The result was that independence of internal auditors was threatened.

5.2.2.1.3 Relations with management

Internal auditors were facing a number of challenges when dealing with senior management. Lack of cooperation had manifested itself in instances where the senior managers refused to give information required by internal auditors. In some instances senior managers demanded that they be audited by more senior auditors. These managers were preoccupied with hierarchical positions instead of the objectives of the organisation or of their departmental units. All these are examples of interference in the activities and independence of internal auditors.
5.2.2.1.4 Relations with external audit

In all three parastatals, relations with external auditors were cordial. There was also good coordination of work plans to avoid duplication. The independence of internal auditors was not in any way compromised, as external auditors did not dictate what the auditors should do or how they should carry out their duties.

5.2.3 Research question 3

What are the threats to independence and objectivity in the IA function?

5.2.3.1 Conclusions

5.2.3.1.1 Status of the CAE

The status of the CAE was weakened by his position in the hierarchy in the case of two parastatals. In the case of Case 1, there is a layer of directors between the CEO and the CAE. His status was further weakened by the fact that in terms of remuneration, he got less than those on the same level in the organisational hierarchy. In the case of Case 3, the CAE was on the fourth tier on the organisation structure. When the CAE is placed in middle management, senior managers, tend to view the internal audit function as relatively unimportant, and this might lead them to be reluctant in giving full cooperation to the internal auditors. There was evidence of this tendency, as internal auditors encountered resistance in the form of refusal to provide information, as well as demands that the senior managers be audited by a more senior member of the internal audit function. Such behaviour by senior managers threatened the independence of internal auditors.
5.2.3.1.2. Approval of budgets and annual work plans

In all 3 Cases, budgets and annual work plans are independently prepared by the internal audit function. However, they are approved by the CEOs. The CEOs, as auditees, should not approve the budgets and annual work plans. This function should be done by the board which oversees the internal audit function, i.e. the audit committee. Approval of budgets and work plans by the CEOs was a threat to the independence of the internal audit functions.

5.2.3.1.3 Provision of resources by auditees

In all three parastatals the auditors get their resources (e.g. fuel, cash for subsistence expenses, accommodation etc.) from the auditees, mainly the finance department. There were instances of intentional withholding of resources by the auditees, when the auditors wanted to carry out their duties. This resulted in audits being postponed, or audit coverage being reduced, all of which diminishes the effectiveness of internal audit, to the detriment of the whole organisation. Such interference in the activities of the internal audit function was undesirable, as auditors were at the mercy of the auditees. Internal auditors were not happy with having to beg auditees for resources and this was a serious impairment of the independence of the internal audit function.

5.2.3.1.4 Irregularities by senior staff

There were indications that irregularities by senior staff were played down and the auditors who exposed the irregularities never get to know the final outcome of their report. Reports on such irregularities were handled by the CAEs, who in most cases sympathised with the senior staff, and in some cases watered down the reports. The auditors were disillusioned by the preferential treatment given to senior staff. Such preferential treatment eroded the objectivity of the internal audit function, and could embolden some criminally minded officials to
commit serious irregularities, which could lead to financial losses to the organisation. This practice was an impairment of internal audit independence.

5.2.3.1.5 Familiarity

Internal auditors were auditing their close friends and relatives when they should have declared a conflict of interests and recused themselves from taking part in such audits. Auditing their close relatives and friends affected their objectivity, as they were most likely to be lenient towards them, at the expense of quality of their work. CAEs and principal auditors assumed that auditors would use their professional judgement and advise the team leaders so that they could be redeployed to other assignments. However, this was not always happening. As a result principal auditors came across cases where internal auditors failed to exercise objectivity when auditing their friends and relatives. This situation was aggravated by the fact that there were no laid down procedures for identifying, assessing and managing situations of conflict of interests in the internal audit functions. Familiarity threatened the independence of internal auditors.

5.2.3.1.6 Self-review threat

One CAE acted in the position of CEO on several occasions. This gave rise to the threat that when he reverted to his substantive position, the work he performed while acting as CEO would be subjected to internal audit scrutiny. As the head of the internal audit function, the CAE would then review reports submitted by the internal auditors, before authorising them for submission to the auditee. This created a situation of conflict of interests, as the CAE could end up auditing his own work, and as such, his objectivity was impaired.
5.2.4 Research question 4

What are the current procedures for dealing with threats to independence and objectivity within the internal audit function?

5.2.4.1 Conclusion

In all the three parastatals there were no written procedures for dealing with threats to independence and objectivity. The CAEs indicated that they expected internal auditors to use their professional judgement when faced with situations threatening their independence and objectivity. However this did not happen, as a result threats to independence and objectivity were not always properly managed.

5.3 Recommendations

5.3.1 Research question 1

To what extent do the reporting structures ensure broad audit coverage and freedom from interference in audit work?

5.3.1.1 Recommendations

5.3.1.1.1 The audit charter

All parastatals should have audit charters, which are authorised by the board of directors. Where necessary assistance should be sought from the IIA when drafting such documents. In addition, the charter should be circulated or distributed to all members of the organisation so that they are aware of the duties, responsibilities, authority and purpose of the internal audit functions. This will encourage cooperation with internal auditors, and assist in the achievement of organisational objectives. The audit charters should also be regularly reviewed to ensure that they are in line with the current situation. The CAE, management
and the audit committee should ensure that the provisions of the audit charter are implemented and observed.

5.3.1.1.2 CAE position in the hierarchy

Parastatals should follow guidelines provided by the IIA and corporate governance codes in positioning the CAE on the organisation structure. It is necessary that the CAE be placed just below the CEO in order to reflect the importance of the audit function in the organisation. In such a position, the CAE would have the clout and command respect from senior management, which is necessary for the effective execution of internal audit duties, without any interference. His independence and that of the internal audit function would be enhanced, enabling the internal audit function to perform discharge its responsibilities effectively.

5.3.1.1.3 Reporting structures

Parastatals should adhere to the reporting lines for CAE advocated by the IIA, i.e. functionally to the audit committee and administratively to the CEO or other senior official with an interest in internal audit. The CEO should not be involved in the hiring, evaluation and firing of the CAE, and these duties must be performed by the audit committee. In addition to reporting functionally to the audit committee, the CAE should have access to the Auditor General as well as the responsible minister. Such an arrangement would ensure that all corporate governance arms are kept on their toes, and there is no one with absolute power and that any irregularities uncovered by internal audit are promptly attended to.

5.3.2 Research question 2

How much do relationships between Internal Audit (IA) and other corporate governance arms (the board, management, and external audit) enhance effectiveness and good governance?
5.3.2.1 Recommendations

5.3.2.1.1 Relations with the Board and the audit committee.

To ensure that the audit committee is independent, it should comprise only of independent non-executive directors. Members of senior management should only attend audit committee meetings at the invitation of the committee, when their presence is so required. It is also important that board members and indeed members of the audit committee are appointed on merit and not on any other criteria. The fact that executive management was allowed to take part in the activities of the audit committee is evidence of a lack of knowledge of corporate governance issues on the part of the boards. It is necessary to appoint people with proven business leadership to these boards. Members of boards should also be kept abreast of current governance issues and trends, by attending relevant workshops and courses hosted by the institute of directors.

5.3.2.1.2 Relations with management

The audit charter should be very clear that all persons in the organisation are subject to internal audit and that any auditor will audit any units or office regardless of the rank or position of the office bearer. Additionally there should be an education campaign, to enlighten the senior management about the benefits of an effective and independent internal audit function. The audit charter should be distributed to everyone within the organisation, and its contents should be explained, so that everybody will give maximum cooperation to the internal auditors.
5.3.2.1.3 Relations with external audit

The cordial relations should be maintained and coordination of work plans should be encouraged, so that unnecessary duplication is avoided and audit fees charged by external auditors is minimised.

5.3.3. Research question 3

What are the threats to independence and objectivity in the IA function?

5.3.3.1 Recommendation

5.3.3.1.1 Status of the CAE

In order to reflect the importance of the internal audit function in the organisation, the position of CAE should be just below the CEO. In this way, the CAE will command the respect he needs in order to carry out his responsibilities effectively. Senior managers will also cooperate with the internal auditors, when they realise the importance accorded this function.

5.3.3.1.2 Approval of budgets and annual work plans

The audit committee should take a keen interest in the activities of the internal audit function. The audit committee should discuss these budgets and work plans with the CAE and then approve them. After approval, the audit committee should monitor implementation of the work plans and ensure that budgeted funds are released at appropriate times to ensure completion of planned workloads.

5.3.3.1.3 Provision of resources by auditees

Auditors report to the board of directors through the audit committee. It is the duty of the audit committee to ensure that once the audit budgets and work plans are approved, the
function gets all the resources as and when they require them. The resource providers should be under strict instructions by the board that as long as budget provision still exists, internal auditors should be given the resources they require to carry out their duties. These instructions should be in writing and communicated to all affected personnel through the CEO. Where resources are denied for any reason, this should be brought to the attention of the audit committee chairperson, who should take up the matter with the CEO.

5.3.3.1.4 Irregularities by senior staff

No official should be made to feel that they can commit irregularities without any action being taken against them. All irregularities should be treated in the same manner, regardless of who has committed them. Furthermore, auditors should be allowed to make follow ups on their audits, until all matters raised in the reports are finalised. To ensure that no cases are played down or watered down, communication lines should be opened to enable auditors to anonymously report any such attempts direct to the chairperson of the audit committee, the board chair, and even the Auditor General. Opening such communication lines would greatly enhance the independence of the internal auditors, and help to prevent financial scandals.

5.3.3.1.5 Familiarity

There must be written guidelines on how internal auditors should deal with situations where their independence and/or objectivity is threatened. Under the current situation, some auditors may not know or claim not to know that it is necessary for them to declare the conflict of interests, and this could lead to compromises in the quality of work produced by the internal auditors.
5.3.3.1.6 Self review threat

The CAE should not act in the post of CEO, as this creates a situation where he would be required to audit his own work.

5.3.4 Research question 4

What are the current procedures for dealing with threats to independence and objectivity within the internal audit function?

5.3.4.1 Recommendation

Written guidelines or procedures on how to deal with threats to independence and objectivity should be issued and distributed to all internal auditors. In formulating these procedures, reference can be made to the IIA publication entitled “Independence and Objectivity: A Framework for Internal Auditors” (IIA 2001). When such procedures are in force, the auditors will be able to identify and manage threats effectively.

5.4 Recommendation for future research

In view of the ineffectiveness of audit committees revealed in this study, I would recommend future research on the appointment, training, induction and performance of audit committees in parastatals.

5.5 Summary

In this chapter, the first four chapters were summarised. Conclusions in respect of each research question are then given. Overall, it was concluded that internal auditors did not have adequate independence to effectively carry out their duties. Appropriate recommendations to address threats to independence were made in respect of each research question. The chapter ended with a recommendation for future research.
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APPENDIX 1 – QUESTERVIEWS

APPENDIX 1.1: QUESTERVIEW FOR CHIEF AUDIT EXECUTIVE (CAE).

Questionnaire- Open Ended Questions

CHIEF AUDIT EXECUTIVE

Bio data

Gender …………………….. Age …………………..

Qualifications

Membership of professional associations (e.g. IIA)

No. of years experience as an auditor …………………………………………………

No. of years in present position………………………………………………………………

Other work experience……………………………………………………………………

Length of service in present organisation……………………………………………………..

Questions

What standards or guidelines do you follow in the performance of your audit duties?

1. To what extent do organisational and reporting structures ensure broad audit coverage?

   i. Where is the office of the head of internal audit positioned in the organisation structure?

   ii. How does this affect audit coverage?
iii. To whom do you report?

iv. Does this reporting structure enhance independence of the unit?
   How?

v. Do you sometimes act in the position of the chief executive officer?

2. How is freedom from interference in internal audit work ensured?

i. What document defines the purpose, authority and responsibility of the internal audit unit?
   How was this document drafted and authorised?

ii. To whom and how has it been distributed?
   When was it last reviewed?

iii. Comment on its adequacy or otherwise.

Audit planning and performance
i. How are annual work plans prepared and who provides inputs? Who authorises the plans?

ii. Are there areas that are not covered by the plans and why?

iii. How are internal audit manpower and financial budgets prepared, and authorised?

iv. Comment on whether the budgeted amounts are always disbursed when required by the auditors.

v. How are irregularities involving senior staff dealt with?

vi. How are threats by staff to auditors dealt with?

Hiring and firing or the head of internal audit

i. Who is responsible for firing, terminating the services of, and evaluating the you?
ii. Comment on how this affects the independence and objectivity of the internal audit unit.

3. How do relations between internal audit and other corporate governance arms enhance good governance?

Audit committee

i. Who are the members, and are they all non executive directors?

ii. Is there a financial expert among the non executive members of the committee? Briefly give his professional qualifications/experience.

iii. Is the chairperson of the committee easily accessible and do you have private meetings with him in the absence of executive management?

iv. In what ways does the committee give you support?
External audit

i. Do external auditors use your work?
   How?........................................................................................................................................
   ........................................................................................................................................
   ........................................................................................................................................
   ........................................................................................................................................

ii. How do you interact with the external auditors?
    ........................................................................................................................................
    ........................................................................................................................................
    ........................................................................................................................................
    ........................................................................................................................................

Management and staff

i. Are management and staff aware of audit purpose, authority and responsibilities?
   How?
   ........................................................................................................................................
   ........................................................................................................................................
   ........................................................................................................................................
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   ........................................................................................................................................

4. What threats to independence and objectivity do internal auditors face?
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   i. Is the internal audit unit used as a training ground for potential managers?
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      ........................................................................................................................................
   
   ii. Do internal auditors sometimes audit their friends or relatives
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      ........................................................................................................................................

iii. What is the internal audit’s involvement in consulting and risk management?

5. What are the current procedures for dealing with threats to independence and objectivity (e.g. as a result of matters mentioned in 4 above)

Thank you
APPENDIX 1.2 QUESTERVIEW FOR PRINCIPAL AUDITOR

Questionnaire- Open Ended Questions

PRINCIPAL AUDITOR/ AUDIT OFFICER

Bio data
Gender ................................. Age .............................

Qualifications
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..............................................................................................................................
..............................................................................................................................
..............................................................................................................................

Membership of professional associations (e.g. IIA)
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..............................................................................................................................
..............................................................................................................................

No. of years experience as an auditor ............................... 

No. of years in present position .............................................

Other work experience ..............................................................
..............................................................................................................................

Length of service in present organisation ............................... 

Questions

What standards or guidelines do you follow in the performance of your audit duties?
..............................................................................................................................
..............................................................................................................................

1. To what extent do organisational and reporting structures ensure broad audit coverage?
   i. Where is the office of the head of internal audit positioned in the organisation structure?
      ..............................................................................................................................
      ..............................................................................................................................
      ..............................................................................................................................
      .................
   ii. How does this affect audit coverage?
      ..............................................................................................................................
iii. To whom does the head of internal audit report? .................................................................
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iv. Does this reporting structure enhance independence of the unit? How? ...........................................
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Audit planning and performance

i. How are annual work plans prepared and who provides inputs? Who authorises the plans?

ii. Are there areas that are not covered by the plans and why?

iii. How are internal audit manpower and financial budgets prepared, and authorised?

iv. Comment on whether the budgeted amounts are always disbursed when required by the auditors.

v. How are irregularities involving senior staff dealt with?

vi. How are threats by staff to auditors dealt with?
Hiring and firing or the head of internal audit

i. Who is responsible for firing, terminating the services of and evaluating the head of internal audit?

ii. Comment on how this affects the independence and objectivity of the internal audit unit.

3. How do relations between internal audit and other corporate governance arms enhance good governance?

Audit committee

i. Who are the members, and are they all non executive directors?

ii. Is there a financial expert among the non executive members of the committee? Briefly give his professional qualifications/experience.
iii. Is the chairperson of the committee easily accessible and do you have private meetings with him in the absence of executive management?

iv. In what ways does the committee give you support?

External audit

i. Do external auditors use your work? How?

ii. How do you interact with the external auditors?

Management and staff

i. Are management and staff aware of audit purpose, authority and responsibilities? How?
4. What threats to independence and objectivity do internal auditors face?

i. Is the internal audit unit used as a training ground for potential managers?

ii. Do internal auditors sometimes audit their friends or relatives?

iii. What is the internal audit’s involvement in consulting and risk management?

5. What are the current procedures for dealing with threats to independence and objectivity (e.g. as a result of matters mentioned in 4 above)?

Thank you
APPENDIX 1.3: QUESTERVIEW FOR INTERNAL AUDITORS

Questionnaire- Open Ended Questions

INTERNAL AUDITORS

Bio data

Gender ……………………… age …………………..

Qualifications

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……………………………………………………………………………………………………
……………………………………………………………………………………………………
……………………………………………………………………………………………………

Membership of professional associations (e.g. IIA)

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……………………………………………………………………………………………………
……………………………………………………………………………………………………

No. of years experience as an auditor .................................................................

No. of years in present position ...........................................................................

Other work experience ....................................................................................... 

Length of service in present organisation ..........................................................

Questions

What standards do you follow in the performance of your audit duties?

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1. To what extent do organisational and reporting structures ensure broad audit coverage?

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..........................................................................................................................................

i. At what level is the head of internal audit on the hierarchy of the organisation, and how does this affect audit coverage and independence of the internal audit unit?

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...........................................................................................................................................
ii. To whom does the head of internal audit report and how does this affect the independence and audit coverage of the internal audit unit?

iii. What problems / challenges are encountered by the internal audit unit because of the organisational structure or reporting relationships?

2. How is freedom from interference in audit work ensured?

Terms of reference

i. Is there a document that defines the purpose, authority and responsibility of the internal audit unit?

ii. How was it prepared (i.e. by whom, who provided inputs, who authorised it, when)?

iii. How and to whom was it disseminated?
iv. Comment on its adequacy.

Audit planning and performance

i. How are internal audit work plans prepared (e.g. who provides inputs, who approves it)?

ii. Which areas are not covered by these plans and why?

iii. How are budgets for internal audit prepared and approved (e.g. who provides inputs, what factors are considered)?

iv. Comment on the adequacy of the resources provided?

v. Comment on whether substantial changes are made in the process of reviewing reports from the auditors before they are submitted to the
vi. What procedures are there to deal with attempts to limit the scope of an audit, or impose restrictions on access to records, property or personnel during an audit?

3. How much do relations between internal audit and other corporate governance arms enhance good governance?

Audit committee
i. Who are the members and are they all non-executive directors?

ii. Is there a financial expert, and what are his qualifications/experience?

iii. In what ways has the committee supported the internal audit unit?
External auditors

i. How do you interact with external auditors (e.g. sharing resources, inputs into work plans, reporting etc.)?

ii. Are work plans co-ordinated, and are there any benefits from this?

Management

i. Comment on the cooperation and support you get from management and staff in general.

ii. How do you deal with irregularities by senior management?

4. What threats to independence and objectivity do you face?
i. Are there instances where you have felt threatened before, during or after an audit assignment?

ii. Is the internal audit unit used as a training ground for management?

iii. How do you feel about this practice?

5. What are the current procedures for dealing with threats to independence and objectivity of internal auditors, and are they in writing?

Thank you.
APPENDIX 1.4: QUESTERVIEW FOR CHEF FINANCIAL OFFICER

Questionnaire - Open Ended Questions

CHIEF FINANCIAL OFFICER

Bio data

Gender ..........................  Age  ......................

Qualifications
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...........................................................................................................
...........................................................................................................

Membership of professional associations (e.g. IIA)
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No. of years in present position .................................................................

Other work experience ............................................................................
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Length of service in present organisation ...................................................

Questions

Are you aware if the internal audit department has a charter?
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How did the charter come into being (who prepared it, who approved it)?
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What inputs if any, do you make into the internal audit annual work plans?
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What inputs if any do you make into the internal audit financial budget?
How are the work plans and financial budgets for internal audit approved?

Does the audit committee have a charter?

Comment on whether there is a financial expert on the audit committee

Comment on disbursement of funds when required to undertake audits.

How do you rate the contribution of the internal audit in the organisation?

Thank you.
APPENDIX 1.5 QUESTERVIEW FOR MANAGERS AND STAFF

Questionnaire - Open Ended Questions

MANAGERS AND STAFF

Bio data

Gender ……………………..  Age …………………..

Qualifications
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………………………………………………...
………………………………………………...
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Membership of professional associations (e.g. IIA)
………………………………………………...
………………………………………………...

Present position………………………………………………..

No. of years in present position……………………………………………….

Other work experience………………………………………………..

Length of service in present organisation………………………………………………..

Are you aware of a document that defines the duties and responsibilities of the internal audit department?

………………………………………………...

Comment on the frequency of audits by internal audit, and whether the same auditors perform the audits each time

………………………………………………...

How are audit findings communicated, and areas needing attention resolved?
Can you mention any areas that are not subject to internal audit scrutiny?

Comment on whether internal auditors conduct themselves professionally.

Comment on the involvement of internal auditors in risk management and consulting work.

Do you sometimes second staff in line for promotion to internal audit for training? How do you feel about the idea?

Which members of your staff usually get transferred or promoted to the internal audit branch?

Generally, how do you rate the contribution of the internal audit department in the organisation?
Thank you
APPENDIX 2: INTERVIEW GUIDES
APPENDIX 2.1: INTERVIEW GUIDE FOR CHIEF AUDIT EXECUTIVE (CAE)

Interview Guide –Chief Audit Executive

1 To what extent organisational and reporting structures ensure broad audit coverage?

Organisational independence

- Where is the position of the head of internal audit positioned in the organisation structure, in junior, middle or senior management?
- To whom does the head of internal audit report functionally and administratively?
- Are you happy with this reporting structure?

2 How is freedom from interference in audit work ensured?

The audit charter

- Do you have a document that defines you purpose, duties and responsibilities of the internal audit department?
- Who drafted it, and who provided inputs?
- Who authorised and approved the document?
- Has it been disseminated to other members of the organisation and how?
- How frequently has it been reviewed?
- Have there been any changes ever since it was introduced?
- Can I have a copy, or would you rather give me a brief outline of the document?
- Are you happy with it in its present state?

Audit planning and performance

- Are there any inputs by the following: CEO, CFO, Audit committee, External auditor in the preparation of annual work plans?
- How are the work plans authorised?
- Are work plans of internal and external audit coordinated to avoid duplication?
- Do your efforts as a department affect the audit fees charged by external auditors?
- Are there any areas that are not covered in the work plans?
- How is the internal audit financial budget prepared? Who provides inputs?
- Who authorises the budget?
- Do you get enough resources to carry out your work plans? Which standards guide you in your work? Do you have an internal audit manual to guide staff?
- Do the same auditors repeatedly audit the same areas?
- What measures are there to ensure that auditors do not audit their friends or relatives?
- Who gets copies of your reports?
- Are auditees cooperating?
- Have you dealt with any incidences of threats to auditors by auditees?
• How long does it normally take for auditees to respond to audit reports? To implement audit recommendations?
• What measures do you take if an auditee does not cooperate with you?
• How do you report irregularities involving senior staff?

**Hiring and firing of CAE**

• Who is responsible for hiring, terminating the services of the head of internal audit?
• Who is responsible for evaluating the performance of the head of internal audit?
• How frequently are the evaluations done?

**3. How do relations between internal audit and other corporate governance arms enhance good governance?**

**The audit committee**

• What is the membership of the audit committee?
• How many are independent, non executive directors?
• How are new members inducted?
• Are the members financially literate?
• Is there a financial expert among the members? Is he independent/non executive?
• How frequently do you meet with the audit committee?
• How accessible is the chairperson?
• Do you have private meetings with the chairperson, in the absence of executive management?
• Do you copy your reports to the audit committee?
• Do you provide any services to the audit committee?
• What requests do you get from the audit committee, and how frequently?
• How do you rate their performance?
• How supportive is the current committee/the previous one?
• What significant support has it given to the internal audit department recently?

**4. What threats to independence do internal auditors face?**

**Internal audit as a management training ground**

• Are there movements of staff in and out of the department to and from other departments?
• Is the department used as a training ground for potential managers?
• If so what mechanisms are there to prevent self review?
• What are you views about the use of the internal audit department as a training ground for prospective managers?
Consulting

- How much consulting work is done by the function in the organisation?
- Are procedures for conducting consulting assignments contained in the internal audit charter?

Risk management

- What is the department’s involvement in enterprise risk management?
- How is self review avoided?

5. What are the current procedures for dealing with threats to independence and objectivity?

Individual objectivity and independence

- What are the procedures for dealing with the impairments due to the following:
  - Attempts to limit the scope of the audit by the auditee of other parties
  - Restrictions of access to records, personnel and properties necessary for the conduct of the audit
  - Refusal to supply resources necessary for conducting the audit
- Are there any procedures for dealing with potential threats to objectivity of the auditors before commencement of the audit?
- Are auditors sometimes seconded to other departments and staff from other departments seconded to audit for certain periods?
- If so how is self review prevented?
APPENDIX 2.2: INTERVIEW GUIDE FOR PRINCIPAL AUDITOR

Interview Guide –Principal Auditor /Audit Officer

1 To what extent organisational and reporting structures ensure broad audit coverage?

**Organisational independence**

- Where is the position of the head of internal audit positioned in the organisation structure, in junior, middle or senior management?
- To whom does the head of internal audit report functionally and administratively?
- Are you happy with this reporting structure?

2 How is freedom from interference in audit work ensured?

**The audit charter**

- Do you have a document that defines your purpose, duties and responsibilities of the internal audit department?
- Who drafted it, and who provided inputs?
- Who authorised and approved the document?
- Has it been disseminated to other members of the organisation and how?
- How frequently has it been reviewed?
- Have there been any changes ever since it was introduced?
- Can I have a copy, or would you rather give me a brief outline of the document?
- Are you happy with it in its present state?

**Audit planning and performance**

- Are there any inputs by the following: CEO, CFO, Audit committee, External auditor in the preparation of annual work plans?
- How are the work plans authorised?
- Are work plans of internal and external audit coordinated to avoid duplication?
- Do your efforts as a department affect the audit fees charged by external auditors?
- Are there any areas that are not covered in the work plans?
- How is the internal audit financial budget prepared? Who provides inputs?
- Who authorises the budget?
- Do you get enough resources to carry out your work plans? Which standards guide you in your work? Do you have an internal audit manual to guide staff?

- Do the same auditors repeatedly audit the same areas?
- What measures are there to ensure that auditors do not audit their friends or relatives?
- Who gets copies of your reports?
- Are auditees cooperating?
- Have you dealt with any incidences of threats to auditors by auditees?
• How long does it normally take for auditees to respond to audit reports? To implement audit recommendations?
• What measures do you take if an auditee does not cooperate with you?
• How do you report irregularities involving senior staff?

Hiring and firing of CIA

• Who is responsible for hiring, terminating the services of the head of internal audit?
• Who is responsible for evaluating the performance of the head of internal audit?
• How frequently are the evaluations done?

3. How do relations between internal audit and other corporate governance arms enhance good governance?

The audit committee

• What is the membership of the audit committee?
• How many are independent, non executive directors?
• How are new members inducted?
• Are the members financially literate?
• Is there a financial expert among the members? Is he independent/ non executive?
• How frequently do you meet with the audit committee?
• How accessible is the chairperson?
• Do you have private meetings with the chairperson, in the absence of executive management?
• Do you copy your reports to the audit committee?
• Do you provide any services to the audit committee?
• What requests do you get from the audit committee, and how frequently?
• How do you rate their performance?
• How supportive is the current committee/ the previous one?
• What significant support has it given to the internal audit department recently?

4. What threats to independence do internal auditors face?

Internal audit as a management training ground

• Are there movements of staff in and out of the department to and from other departments?
• Is the department used as a training ground for potential managers?
• If so what mechanisms are there to prevent self review?
• What are your views about the use of the internal audit department as a training ground for prospective managers?
Consulting

- How much consulting work is done by the function in the organisation?
- Are procedures for conducting consulting assignments contained in the internal audit charter?

Risk management

- What is the department’s involvement in enterprise risk management?
- How is self review avoided?

5. What are the current procedures for dealing with threats to independence and objectivity?

Individual objectivity and independence

- What are the procedures for dealing with the impairments due to the following:
  - Attempts to limit the scope of the audit by the auditee of other parties
  - Restrictions of access to records, personnel and properties necessary for the conduct of the audit
  - Refusal to supply resources necessary for conducting the audit
- Are there any procedures for dealing with potential threats to objectivity of the auditors before commencement of the audit?
- Are auditors sometimes seconded to other departments and staff from other departments seconded to audit for certain periods?
- If so how is self review prevented?
APPENDIX 2.3: INTERVIEW GUIDE FOR INTERNAL AUDITORS

Interview Guide –Internal Auditors

Position of department in the organisation

- Where is the position of the head of internal audit on the organisation structure i.e. Junior management, middle management or senior management?
- How has this affected the department? Is there a better arrangement?
- To whom does the head of internal audit report? Is this an ideal arrangement?
- Do you encounter any problems while doing your duties because of this structure?

Audit charter

- Is there any document that defines your terms of reference as a department?
- Who prepared it? Did you make any inputs?
- Who approves it?
- When was it last reviewed?
- Is it adequate in its present state?
- If there are any inadequacies, have you brought to the attention of the authorities?
- Are auditees aware of this document? How were they made aware?

Audit committee

- Does the organisation have an audit committee?
- Do you know the members of the committee?
- Have you ever been asked to perform an assignment requested by the audit committee?

Internal audit as a training ground

- Are there movements of personnel from other branches to the audit department and vice-versa?
- Do some personnel do a stint in internal audit before being promoted? Do you think this is a good practice?
- Are there any measures to prevent such members from auditing their own work?

Consulting

- Does the department carry out special investigations or consulting jobs at the invitation of other departments?
- What measures are there to prevent members involved in these consulting jobs from auditing their own work?

Risk management
• Have you ever been involved in enterprise risk management? In what capacity?

Planning and performance of work

• Do you have adequate resources to carry out your duties?
• What guidelines or standards do you follow in the performance of your work? Is there an internal audit manual?
• Have there been budget cuts that have prevented you from doing some audits?
• How much cooperation do you get from auditees?
• How do you deal with the following:
  ▪ Attempts to limit the scope of the audit by the auditee or other parties
  ▪ Restrictions of access to records, personnel or properties necessary for the conduct of an audit
  ▪ Refusal to supply resources necessary for conducting the audit
• Are there any areas which are not subject to internal audit scrutiny?
• Do you sometimes audit your friends and relatives?
• Are there procedures to prevent this from happening?
• What challenges do you encounter in the course of performing your internal audit duties?
• What are the procedures for reporting your findings to the auditee?
• Do you always get cooperation, especially from the senior staff?
• How long does it take for auditees to respond to your reports?
• How long does it take for auditees to implement your recommendations?
• Where the auditee has taken too long to respond or implement your recommendations what do you do?

Relations with external auditors

• Do external auditors have inputs in your annual work plans?
• How do you relate with external auditors in terms of sharing resources/workloads?
• Are your reports copied to the external auditors? How do they use them?
• Do you sometimes work under the supervision of external auditors?
• Do external auditors use some of your work?
APPENDIX 2.4: INTERVIEW GUIDE FOR CHIEF FINANCIAL OFFICER

Interview Guide – Chief Financial Officer (CFO)

- Do you have a copy of the internal audit charter? who prepared it? who approved it? when was it last reviewed?
- To whom does the head of internal audit report, functionally and administratively?
- Do you make any inputs into the internal audit annual work plans? Who approves the work plans?
- Do you make any inputs into the internal audit budget? Who approves the budget?
- Are there any areas which are not subject to internal audit scrutiny? Which ones and why?
- What has been the greatest contribution of the internal audit department to the organisation?
- Is the internal audit department getting sufficient support from all levels in the organisation?

Audit committee

- How is the audit committee constituted?
- Does the audit committee have an audit charter?
- Is there a financial expert in the audit committee?
- How frequently do they meet?
- How do you evaluate the present committee? Previous committees?

External audit

- Are activities of external and internal audit coordinated? By whom? Any benefits of this coordination?
- How are external fees determined?
- Do internal auditors sometimes assist external auditors in their work?
- How frequently are external auditors changed?
APPENDIX 2.5: INTERVIEW GUIDE FOR MANAGERS AND STAFF

Interview Guide – Managers And Staff

- Are you aware of a document that defines the duties and responsibilities of the internal audit department?
- How frequently are you audited by internal auditors? Do you have the same auditors on every assignment?
- Do you discuss audit findings as well as how to correct any errors with the internal auditors at the end of every audit?
- Do you know of any areas that are not subject to internal audit scrutiny?
- How good are you relations with the internal auditors?
- Have you ever approached internal audit to assist in resolving problems within your department?
- Do you sometimes second staff in line for promotion to internal audit for training? How do you feel about the idea?
- Which members of you staff usually get transferred or promoted to the internal audit branch?
- Generally, how do you rate the contribution of the internal audit department in the organisation?
APPENDIX 3: FOCUS GROUP DISCUSSION GUIDE

FOCUS GROUP DISCUSSIONS WITH INTERNAL AUDITORS

INTRODUCTION

- How were you inducted into the internal audit function?
- Which standards or guidelines do you follow in the performance of your work?

Discussion questions

1. To what extent do reporting structures ensure broad coverage?
   - Where is the position of the head of internal audit on the organisation structure i.e. Junior management, middle management or senior management?
   - How has this affected the department? Is there a better arrangement?
   - To whom does the head of internal audit report? Is this an ideal arrangement?
   - Do you encounter any problems while doing your duties because of this structure?

2. How is freedom from interference in audit work ensured?

Audit charter

- Is there any document that defines your terms of reference as a department?
- Who prepared it? Did you make any inputs?
- Who approves it?
- When was it last reviewed?
- Is it adequate in its present state?
- If there are any inadequacies, have you brought to the attention of the authorities?
- Are auditees aware of this document? How were they made aware?

Audit planning/budgets

- Who provides inputs into the annual audit plans?
- How are the plans approved?
- Who provides inputs into the audit budget?
- How is the budget approved?

Performance of audits

- Comment on the adequacy of resources to enable you to make adequate coverage.
- Are there areas that are not subject to audit?
- Are reports modified before issue to the auditees?
- How do you deal with attempts to limit the scope of your audit, or restrictions to access to records required for the audit?
3 How much do relations between internal audit and other corporate governance bodies enhance good governance?

Audit committee

- Do you know the members
- Do you know if there is a financial expert in the committee?
- Have you ever done any work for the audit committee?

External auditors

- What are your relations with external auditors? (inputs into work plans, sharing resources, reporting, working as one team)
- Are your audit plans coordinated?
- Do you sometimes work together, and how does this affect the audit fees?

Management

- Do you receive adequate support and cooperation?

4 What threats to independence and objectivity do you face?

- Do you sometimes audit your friends and relatives?
- Are there instances when you are required to audit your own work, e.g. after having been involved in risk management or in a consultative capacity?
- Have you ever felt threatened before, during or after an audit assignment?
- Is the internal audit function used for training managers?
- What is the effect of this practice?

5 What are the current procedures for dealing with threats to independence of internal auditors?

- Are these documented?
APPENDIX 4: CODING OF INTERVIEW AND FOCUS GROUP DISCUSSION DATA (samples)
APPENDIX 4.1: CHEF AUDIT EXECUTIVE DATA

Interview With The Chief Audit Executive

The topic under discussion is the independence of internal auditors. I have broken this into 5 broad questions that will form the basis of our discussion, but before we go to those questions, I would like to know what standards or guidelines you use when carrying out audits.

In the NRZ we use the IPPF which are standards recommended by the Institute of Internal Auditors and they give you guidelines on how to conduct your assignment and how to structure your report and the follow-ups that you do after the report is submitted.

So you have a current copy of the IPPF?

Yes and we also have a soft copy that is available from the institute.

Let's now go on to the questions. The first question is, To what extent do organisational and reporting structures ensure independence and broad audit coverage? So we can start with the office of the chief internal auditor. Where is it positioned in the hierarchy of the organisation?

We report functionally to the audit committee of the board and administratively to the general manager who is the chief executive and this is in terms of the charter which was approved by the board in 2008.

Are you happy to report to the general manager, is the arrangement working?

Ordinarily, it should not cause any problems but in our case because the audit committee members are non executive directors, you find that most of the issues we resolve them with the general manager, who to some extent is also our auditee, but so far we have not had any major problems, he actually has been very supportive and facilitating our resources and any other things that are in his means to assist us in the discharge of our duties.

Let’s go on to the second question, that is How is freedom from interference in internal audit work ensured? We will start with the audit charter. How was it drafted and authorised?

The audit charter is based on a draft which is provided by the IIA which should basically have 3 parameters, the responsibility the reporting structure, the responsibility and the authority of internal auditors. And this one is also

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revised from time to time to ensure that it is relevant and captures all possible scenarios.

So when was it last reviewed?

Since 2008 it has not been reviewed since it is still very relevant.

Has it been disseminated to all members of staff and how has that been done?

After it had been approved by the board, it was distributed to each of the officers who are the section heads and there was an instruction that they should also make sure that all staff are aware of it.

So you are happy with it in its present state?

Yes but we will review it as and when necessary.

Let’s go on to audit planning and performance. Who provides inputs into your annual work plans?

We have shifted to risk based auditing, so the first port of call is to ensure that all the high risk areas are covered and we involve auditees by requiring them to submit risk registers, which is basically their risk profiles, and also that is based also on our experience in auditing over the years. We are able pick up the areas that we need to prioritise, but we also do other areas which are not necessarily high risk but which are desirable, like special requests from management or areas where we feel that for the comfort of our board or management we still need to do some audits.

Are there any inputs from the external auditors

Long back our program was actually linked to external audit and they would simply come and review our reports and ask us to extend our scope if they felt that we needed to, but at the moment the external auditors are concentrating on reporting centres and we ourselves we specialise in assessing controls and risk management.

The internal audit budget, how is it put together?

The staff budget, that is the Manning levels and the grades are slotted in and then they cost it out. Other things like our operational requirements, we submit through the finance manager. Thorough the relevant accountant and the costing cycle and so far we have had all our requirements approved. The only challenge we have is one on the actual disbursement because of cash flow problems.

So you are happy except that disbursements are not made when you require the resources?
Yes

When the auditors go into the field are there any chances that they can audit their friends and close relatives?

The chances are there.

Are there any measures to ensure that this is kept under control?

Normally we have teams and we assume that if among the team members there is anyone who is in a situation of conflict of interest he should advise the team leader so that he is given other assignments or duties that will not compromise his position.

Have you had any instances where auditors have been threatened by auditees or where auditees have refused access to documents or properties?

Not any direct threats but maybe indirect, but lack of cooperation, yes. The unions have instructed their members not to cooperate especially if you investigating fraud.

So what measures do you take if an auditee refuses to cooperate with the auditors?

Normally we proceed to finalise the audit on the basis of the evidence we have and then we refer the matter for discipline which will eventually force that person to cooperate with us, if he doesn’t want the outcome to be detrimental, but it’s a long process, otherwise we would have cleared it during the course of the audit.

And the sticky issue of irregularities by senior staff, how do you deal with that? if during the course of an audit the auditor discovers that there are some irregularities committed by senior staff how do you deal with it?

If it is a branch head and below we have not had any problem, we just treat it in the normal course. If it involves directors, we had only one such incidence. We have to upgrade it to the general manager and normally he exercises his discretion and allows us to proceed and have an interview with the director.

Let’s go on to the hiring and firing and evaluation of the chief internal auditor. Who is responsible for that?

When I joined in 1991 the hiring and firing and appraisal of the chief internal auditor was being done by the general manager. But under the new dispensation now, the hiring is still done through the normal procedures but the audit committee oversees the process which means they have the final say in all the appointment of the chief internal auditor as well as of his dismissal.
for any act of misconduct. As for appraisal, so far there has not been any formal appraisal done by the audit committee.

So the appraisal is now being done by the general manager?

Yes, in the sense that we have our meetings on day to day activities and submit reports weekly and quarterly, so it’s not a formal method of appraisal but at least he has a feel of how things are going.

Let’s go on to the third question. How do relations between internal audit and other corporate governance arms enhance good governance? We will start with the audit committee. What is the membership of the audit committee.

It comprises 3 non executive directors and the fourth one is the chief executive officer or general manager, which according to the institute of internal auditors standards is a misnomer. He is not supposed to be sitting there except by invitation by the chairman if he is required.

Would you know how the members were inducted into the committee?

Well it is just when the board is appointed, depending on their areas of speciality and experience, they are selected into those committees and then they went through the normal board induction including being exposed to courses and seminars by the institute of directors.

Do you know if there is a financial expert in the audit committee?

Yes the chairman is an accountant

How accessible is the chairperson to you?

He stays in Harare. We only see him when he comes to attend board meetings.

Do you have any private meetings to discuss any sensitive issues in the absence of executive management.

Yes, only once when we were attending the annual conference of the institute of internal auditors in Victoria falls. He was also a participant. That was in September last year.

How supportive generally is he?

He is very supportive, we communicate through e-mail and by cell phone.

Let’s also look at the external auditors. How do you interact with them? Things like sharing resources and any other ways in which you interact with them.
We rarely have any interaction with them. We see them when they come to do their final or interim audit and when they are doing their planning or during negotiations with the auditees. Otherwise in between we do not have any interaction.

Do they use your work when they are doing their annual or interim audits?

Yes especially when the accounting team does substantive tests, they require those reports so that they can also reduce their own scope and put some reliance on the figures on financial statements.

Does that in any way affect the audit fees that they charge?

According to them when the charge the fees they would have factored the fact that they would get assistance from internal auditors and the year end team for the finance branch.

And management, are they cooperating, and are they aware of your responsibilities? And authority? Do you have any problems with them in terms of cooperating with the auditors

Not with the current management. I don’t have that problem. They are actually very supportive and I am also invited to meetings of executive management to ensure that I am also kept current in and I can identify areas of risk where we need to audit.

Let’s move on to the fourth question What threats to independence and objectivity do internal auditors face? For example do you do any consulting work for the branches or are you involved in risk management?

Only in terms of assessing whether the process is being effective and whether the managers are aware of the risks that they have to manage in their branches or sections. We do not carry out any administrative duties. So we are totally detached from day to day operational administrative duties. This will ensure that when we carry out our work the situation does not arise where we can audit the work that we have performed.

Is the department sometimes used as a training ground for those who are earmarked for promotion or potential managers?

To the contrary, people that come to the audit branch seem to get stuck. It seems no one seems to get promoted, so I would not say it is used as a springboard to managerial posts.

The last question is What are the current procedures of for dealing with threats to independence and objectivity? We are looking at things like attempting to limit the scope of the audit by auditees or other parties or
restrictions on access to records or refusal to supply resources necessary to conduct the audit.

So far we have not had any major instances of anyone trying to limit our scope but we have major challenges of resources especially transport and accommodation and sometimes we have to go begging to the finance director to get money for relief expenses and to procure accommodation and when it is not available at a time when we want to do the audit, that means we end up having to postpone.

Do you have any written procedures for dealing with potential threats to independence and objectivity? We have already talked about familiarity when auditors audit their friends and self review when you audit what you previously performed. Are there any written procedures to prevent these?

No we don’t have any. We just rely on the professional judgement of the team leaders and section leaders.

We have gone through the 5 question I had but if you have anything to add we can discuss that as well.

Issues impinging on our independence?

Yes issues impinging on your independence and objectivity.

I can only think of one. There is an outstanding grievance by the auditors that we are not placed correctly in terms of the grading system. They have gone all the way up to labour court and it’s a pending case now. Our jobs are evaluated by a team of representing management and trade unions and the perceptions of the trade unions is that auditors are the ones who are responsible for the dismissal of their employees. So when it comes to using Patterson job evaluations, where they are supposed to use their discretion, they will not do so. We feel that has been prejudicial to us, compared to people in the finance branch where there are people with similar qualifications and experience.

Where all the channels within the organisation exhausted before going to court?

Yes there is an appeals committee which upheld the grades that were done by the evaluations committee, and after the appeals the only course was to the labour court.

Thank you very much for your time and the information you have given me

Any time you can call on me and I will be obliged to assist.

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APPENDIX 4.2: PRINCIPAL AUDITOR DATA

Appendix - Interview With The Principal Auditor

What I have done is that I have posed five broad questions under which we are going to discuss this, but before we get on to those questions, what I would like to know is what guidelines or standards do you follow when you are conducting your audits? The guidelines or standards you are following.

Like all other auditors we follow international standards on auditing and we make reference to international accounting standards.

How about the ones for the institute on internal auditors, do you also use those standards?

Yes we do, only that unfortunately there are no members. None of us is a member of the institute, although some of us have got their books. Once in a while we attend their courses. We use them also.

The railways as an organisation, has it made any efforts to get people trained by the institute of internal auditors, as far as you know, within the internal audit branch?

Once in a while, not necessarily the institute on internal auditors, but once in a while people are sent to attend these seminars. Some are conducted by the institute some are conducted by other institutions. We have got a number of people who run these courses, NUST is one of them, and then we have got others in Harare.

Let’s go to the questions now. The first question is To what extent do organisational and reporting structures ensure broad audit coverage. Let’s look at the structures especially at the top.

In the internal audit department?

In the whole organisation, on the railways as a whole, from the general manager to the directors, going on and on. Those structures, do they enhance broad audit coverage?

Yah
Otherwise we are looking at the place where is the office of the chief internal auditor positioned in the hierarchy. That is the question we are looking at, and how does it affect internal audit in general?

The chief internal auditor reports to the general manager, although, of course his grade is lower than that of directors and some of his colleagues, I mean the branch heads. His grade is lower, but he reports direct to the general manager.

How does that affect independence. That grading you have talked about, how does it affect his independence or his status in any way?

I wouldn’t say it affects independence, although he is lowly graded than his colleagues, the fact that he reports to the general manager, it gives him, there is a safeguard on his independence. And besides, the audit charter makes sure that everybody cooperates. It doesn’t matter whether he is a director, he is bound to cooperate. The fact that he is lowly graded, I wouldn’t say it affects independence.

So he reports to the general manager, the general manager, under normal circumstances is also an auditee, isn’t it?

Yes

Are you happy with that situation

Laughing    Ummm

Or would you rather have a better reporting structure?

If it was possible, the audit committee would be the best. But under the circumstances, the general manager is what we have got so he reports to the general manager. Also we now have a board, and they also get our reports.

So you talked about the audit charter, who drafted that charter?

It is signed by the general manager, the board, and the chef internal auditor didn’t sign, although he was supposed to sign. I don’t know why he didn’t sign. It was drafted by the chef internal auditor, then it was sent to the board for approval, they approved it and signed it, the general manager signed it.

Did you also provide inputs when the chief internal auditor was drafting it?

I am one of those who was asked to contribute. In fact it mainly came from or we sought the assistance from the institute.

Has it been disseminated to other branch heads and to all members of the organisation, all staff?

I am not sure.
But from your interaction with the other branches, what impression do you get?

Ahhhh…it’s difficult to say because we don’t normally have problems with them. I only know, I only heard of one incident where people had a problem with auditees, and showed them the charter, and then they cooperated.

When was it first issued?

Some time back.

Some years back?

Not far away back. A few years back, because there was resistance.

Who had been resisting?

The general manager was resisting, because he believed what the charter was saying is that the chief internal auditor must report to the directors and he would be required just to mark the register. It was really a matter of not understanding, I think.

How frequently has it been reviewed?

I am not aware, that’s the chief internal auditor's purview.

Lets come to your planning, when you are making you work plans, your annual work plans, who provides the inputs

Normally it’s from the senior internal auditors, they make those work plans, then they bring them. We sit down discuss and agree. When they make those work plans, they refer to the working papers, previous working papers, just to incorporate those problem areas. They input that with reference to working papers, and maybe discuss with the auditees. For instance, especially this current one where we moved from the systems based to the risk based approach. There was a lot of interaction with the auditees, because they provided the risk registers and for that reason the current ones were done by me instead of the senior internal auditors, because it was an initial thing to move to the risk based approach.

How about the external auditors and the audit committee do they also have inputs?

They didn’t except that it is the external auditors who instructed us that they wanted, no, in fact external auditors suggested that it should be, we should use the risk based approach and the board took it up and ordered us to do that.

Do you also work together with the external audit or share resources or just work together, and to what extent do you do that?
I wouldn’t say we work together.

Either your auditors work under their supervision or you have teams composed on internal and external auditors?

The only time we worked with them is like now when they are doing their work, they will come and ask for an internal auditor to be attached to them so that he can assist whenever they have problems.

Let’s look at the budget or the financial budget, How is it prepared?

Things like salaries, those we don’t involve ourselves. Then, say for my section, I will estimate the guys who will be going out for a certain period and then I calculate the approximate mileage they will cover, the fuel and their allowances. I will prepare for my section, then I will pass it on the accounting guy. He is the one who consolidates for the whole branch.

Then, final approval is made by whom?

From him it goes the chief internal auditor then to the accounting branch.

Who is responsible for approving it?

I am not sure who does the approving, whether it is the finance director.

When it come to disbursements, do you always get what you request?

In terms of?

In terms of amounts.

I wouldn’t say always.

Are there drastic or reasonable cuts?

No, ahh…When we make our budget it is based on the estimated number of trips they will make, the hotel accommodation and unfortunately with the revenue section there is nothing they can do. Because if they have to go to Masvingo they just have to go and stay in a hotel. So for that reason we normally, most of the time, we always get what we will have asked for. If we don’t it will only be postponed to a later date. We might say we want to go this time but for one reason or other we don’t, but we will eventually go.

Do the auditors repeatedly audit the same areas, Or the same personnel?

We visit sections only once a year. I am not sure if you say repeatedly if I have answered you question?
To an extent you have answered the question, but familiarity, how do you take care of that in terms of independence, people auditing their friends, their relatives and so on?

Unfortunately it cannot be avoided, because internal auditors are promoted from within the system, like somebody is a commercial clerk and is promoted to audit. He goes and audits the commercial clerks. Some of them are his friends, with whom he joined, trained and worked, so that cannot be avoided, but if you are too close to somebody, and say you are auditing something which you think it would affect you relationship you just phone and the we will ask somebody to go and replace you.

But is there a written procedure to cover that?

I wouldn’t say it’s there. It’s a known thing that you cannot go and audit your friends, because definitely, if you do and you don’t do a good job, you will be disciplined.

The second question is How is interference from internal audit work ensured?

Interference. I am trying to I think who would interfere with our work.

Any instances of interference, for example somebody refuses to give the auditors documents or somebody says no this should not be examined because its sensitive information, something like that.

Normally they cooperate, at one time we had that, it was last year. The marketing guys were refusing to give us some files. We simply phoned their director, and they were ordered to cooperate with us.

But why do you think they refused to give you the documents.

May be now to answer your first question, they may not be aware of the charter.

So you believe it has not been disseminated?

It could be that, because the guys were saying I don’t know if you are supposed to look at these files, until we had to speak to the director and the director ordered them to release everything we wanted.

At times you also come across irregularities by senior officials, those who are right at the top. How do you deal with such situations?

That one is a problem. Investigating the directors, it is a problem. The only one I came across, in fact it was not really fraud as such, but suspected. Some things were happening involving the director, so instead of rather sending an auditor, I thought it was best for me to carry out the audit, so I had to carry
out the audit, because it was a director involved. Well, obviously he wasn’t happy but he did cooperate.

Do you think it would be better to have something written regarding such instances?

Yeh it would be better. It would be better, because by then everybody would know that if something happens we expect at least this level to come and look into this problem, unlike now,. Here is the director there, I can decide to send a junior person. It’s not nice. Laughing. But then we cannot do anything. He just has to answer.

Let’s look at this one. Who is responsible for hiring, terminating the services of and evaluating the performance of the chef internal auditor? Are you aware?

The board is supposed to do that, it’s supposed to, but I am not sure if they do that, or maybe it’s the general manager. I am not sure.

Let’s move on to the third question. How do relations between internal audit and other corporate governance arms enhance good governance? Let’s start with the audit committee and then the other ones which are external audit and management.

The audit committee provides, let’s say a buffer between management and the auditors, and because of that I would say, yes, they promote good governance in that management may not cover some of the things. As long as the audit committee is aware, there is no way management can cover. They have to do the right thing or which the internal audit will have pointed. If they point out something then they will have to do it..

You are aware of the membership of the audit committee.

About 8.

The audit committee?

Oh, no, the audit committee, I am not sure.

Are you aware whether it includes the executive directors or its just composed of independent or non executive directors?

The general manager is supposed to go there on invitation, but I believe he goes there almost every time. But strictly speaking he is supposed to go there on invitation.

How do you feel about his attendance?
He is not supposed to, I feel he shouldn’t attend, because if he is there, depending on those board members, they might not discuss some of the things freely. Definitely, say the chief internal auditor is called to the meeting and they are supposed to discuss something which involves the general manager and directors, how does he freely express himself when the general manager is there? It’s not possible.

I was going to ask if among those members in the audit committee there is anybody who is financially literate. But since you don’t know the members, let’s skip that.

Your reports, who gets copies of the reports?

The external auditors get copies, the board members, once in a while they ask for copies. It’s not all the reports that get.

Have you received any requests to do any special audits from the audit committee?

I am not aware of it.

Generally how do you rate their support for the internal audit branch? Are they visible anywhere?

The problem is they deal with the chief internal auditor. If they want anything they speak to the chief internal auditor. The chief internal auditor speaks to us, so we wouldn’t know that it’s from to the board.

Let’s go on to the 4th question. What threats to independence do internal auditors face? Here we are looking at conflicts of interests, are there any instances where they face that problem? For example do you do any consulting work for the branches, or are you involved in risk management for the branches?

We were only involved this year, when we were starting on this risk based approach.

And how far did you go?

Since it had never been done and we wanted the risk registers done, we had to go to the branches explaining what it was, the purpose and how it should be done. We were heavily involved this year.

Up to what stage, up to implementation? Or did you just recommend?

I wouldn’t say, we had been directed to make sure that our work plans follow the risk based approach so we had to go to these different branches holding meetings with them, sort of educating them on what should be done. Then
they would come up with the risk registers, we would go through them with the branches until we got what we thought was good for us.

For your own use?

Yes, because we had to make our plans based on those risk registers.

When you go back to audit, how do you feel about it, since you have been part of that process?

The process was teaching them how to come up with risk registers it doesn’t affect the work. I wouldn’t say it has got any effect on our work. It’s not our work, what we did was to simply educate them on how it should be done and what should be contained, and they did the rest on their own then brought it to us. So it’s their work.

That is risk management, how about consulting, by this I mean have they asked you to investigate some problem areas and come up with recommendations? Do you get such sorts of requests from auditees or the branches?

Not really. Of late, now that they have got the inspectorate branch, I think that’s the branch that does most of this consulting. Ours is strictly auditing and of course if there is fraud we investigate.

Has the branch also been used as a training ground for people who are due for promotion or potential managers? They come in, have a stint and go back to their branches.

No. No that doesn’t happen.

How would you feel if that were to happen?

There are some organisations where you cannot be promoted unless if you have been in the internal audit branch, but not in the railways it doesn’t happen. It’s not like that.

Let’s go on to the last question. What are the current procedures for dealing with threats to independence and objectivity? We are talking about things like familiarity, we talked about self-review, and any other threats to independence and objectivity. There could be others, you have to educate me on what is on the ground.

Familiarity, there is nothing you can do, because we are like a family, like I said you start employment as a clerk with a group of others and train together, work together, the next day you are promoted as an auditor, you go back and audit there. That one may be your friend. Definitely that one cannot be
avoided. I don’t think there will be anything that will be done about it. As long as we are promoting within, that one will continue to be there.

Have you had instances where auditors have come to you and said I can’t audit this unit because my wife is there or something like that?

Fortunately, in my section, there is nothing like that, but there was a time when I was an auditor and my kid brother was involved in a fraud. So I had to excuse myself and send other guys.

How do you deal with impairments, like someone trying to limit the scope of your audit or restrict access to records, personnel or properties, or refuses to supply resources that are necessary for you to conduct the audit. How do you deal with such instances?

We go to his superior. Because everybody knows that they have got to cooperate. So if he refuses, we simply go to the superior and the superior will have to provide the resources.

I think we have covered what I had here. I would be very much interested to hear any more information that you think is relevant to the independence of internal auditors, because you experience these things on a daily basis. In some cases, when these things come out to the public it’s as if there is no internal audit in an organisation. You find them saying that the anti-corruption commission or external auditors or forensic auditors are investigating. This is what prompted me to come and investigate. Would the internal auditors not have come across those irregularities, or is there something else, or is there much more than meets the eye.

Internal auditors as employees, they are not very, very independent. The fact that they are employed, secondly, for instance in our case, talking about the revenue section, we deal with some transactions are in Botswana, Mozambique, South Africa. The business agreement can state that we can go there and audit things that pertain to NRZ. But I don’t decide that its now two years, we haven’t been there, let’s go there and audit. I have to get permission from the general manager. The general manager also has to get permission from the minister. So in that sense the independence is limited. Because if the general manager says we can’t go, we can’t go. Or if the minister says we can’t go, we can’t go. So in that sense our independence is limited.

Is there anything else, for example your reports, when the auditor submits his report, I think it goes through stages of review. How is that done and does that affect the end product which goes to the auditee?

The auditors carry out an audit, the report comes to me, from me it goes to the chief, its signed by the chief. Then it goes to the auditee. Depending on the issue, some of it will be copied to, if it’s a serious thing it will be copied to the
general manager. Unfortunately, there is no report that has been written involving the general manager so I wouldn’t know. Laughing

What I am getting at is, are there any instances where the report that finally comes out is very different from what came from the auditor, in substance, or major issues, how they are presented concerning seriousness and so on.

Not in my section. Not in my section. Yes I change what they would have written but not to reduce anything.

I don’t know if you have anything else pertaining to independence generally or the complaints you get from your auditors who say this thing is always a headache or whatever?

No, I don’t have anything to add. Independence is not, especially of internal auditors, is not really independence, like I said the fact that you are employed and the fact that you are dependent on somebody for the resources, you can’t make your own decisions, that also affects it.

Thank you very much for giving the vital information. Its valuable, and I can assure you that it will remain confidential. So thanks a lot.
Focus Group Discussion With Internal Auditors

Gentlemen, we are here to discuss the topic: An evaluation of the independence of internal auditors in parastatals in Zimbabwe. I have 5 broad questions under which we will discuss the topic, but, before we get to those questions there are two things we would like to discuss. The first one is how were you inducted into the internal audit branch, whether you came from outside or from other branches within the railways? What is involved in the induction process? Who would like to start? Laughing

Let me start. As for me I came from the branches, from accounting, into audit branch, into the accounting section. The induction which I received was such that I was taken first, shown the audit documents in terms of working papers and what they mean and what they constitute. The second step was the accounting cycle as it entails from an audit perspective rather than from an accounting perspective. That is to say, what I was doing in accounting, now you are looking at it from a reviewal point of view, from an audit perspective. So I was taken through that induction. From there, I was given a scenario, that is sort of a dummy scenario, to say, there is this situation, as an auditor how would you go through it in order to obtain… phone rings. Sorry about that. I had to go through that dummy situation. In the dummy situation you are given a scenario, to say, this is what happened as an auditor, what would you look at. What is it that you would want to obtain in order to come up with evidence that is 1. factual and 2. which can make you formulate an opinion of what your findings are 3. How are you going to compile the working paper which will actually show exactly what you have obtained from that. I went through that. Then the third point, I was given, now, a real situation where my boss, maybe, just said these are the requisitions, can you look at them vis-a-vis the working papers which I have shown you and the scenarios which I have shown you. And go through from a reviewal point of view, that’s from an audit point of view and see whether everything was according to procedure. So that’s how I went through my induction. Then from there I started, of course you learn as you go, some of the things. But the induction to me, I think was just superb

Did it cover any aspects of independence an objectivity?

Yes, from the independence point of view, because, you know when you come from accounting, and you don’t know the... Of course I had done a qualification, an accounting qualification, where I had done auditing I knew there was independence, but I didn’t know how, it was put in place from an audit point of view. I was inducted to say as an auditor you are free
to any railway document from any office, and with that if you have any hiccup you report back and say I can’t obtain that information, then maybe the boss would intervene. As far as independence was concerned, that is how it was put across to me. Then when it comes to objectivity, if I recall very well, it is five or six years ago, I was told, now, the approach in order to achieve objectivity. [When you get to the auditee, because auditees normally view auditors as bloodhounds, especially in these parastatals, they think when you get there you really want them out of the system, yet that is not the case.] [So you need to have a positive approach in order to yield positive results. Your objective is that you want to achieve what you have been assigned, so when you get there what you need to do, be polite. Put your request in a very polite way. That is to say, you should not be commanding, but you say excuse me sir, I am Mr so and so I am from audit, I would like to have this file, there is something I am working on. Normally the auditee will respond on that point, and your objectivity is, you have to be very careful, the auditee might find himself asking, what really do you want to do with that file. You would say unfortunately I also don’t know. I have just been assigned, can I have that file. Because you are not there to divulge, so that your objectivity is not blocked in the process. That’s what I can remember about objectivity.]

Do the others have anything to add on to that? Did you also go through the same process?

Yes

I think the processes which we all went through are all different.

But did they cover the aspect of independence and objectivity?

Like what was said, in most cases when you are inducted you find that you are introduced, like you have some protocols which need to be followed. You will be introduced, this is like you will be a new person to the department, they will take you around and say this in the office of the chief internal auditor, this is your boss, these are you other colleagues, this is the team you are going to work with and as a team you also need to have that team spirit. As auditors you should also coordinate and you should also….. ask where you are not so sure, from your team or boss. And you find that like somebody who is new you need to be familiar with the documents, especially the audit documents and all the procedures. So you find that you are introduced to the working papers. It may be your first time to see the working papers, and from there now you will go through all the procedures and all the circulars, and maybe accounting procedures which are done, and now to have an audit, maybe, a point of view when you are introduced to any document or any scenario.
Now, let’s look at the standards or guidelines that you follow when conducting your audits, be it an audit manual or anything else?

{When I came into the audit branch, we were fortunate enough to have Coopers and Lybrand as our external auditors. All these cupboards here, in the library, there was material in there, with manuals from Coopers and Lybrand. So when we came in, we were given those manuals. They would start telling you what auditing is all about. That’s where you got your first glimpse of what independence is all about and objectivity. We talked about, independence. That’s where we learnt that independence is the freedom from conditions that might interfere with what the auditors carrying out his work in an unbiased manner. That came from Coopers and Lybrand also. And those manuals would also detail work processes where does the process of auditing start. You have to understand the system. You have the pre-study, main study and all that, the entire sequence of flowcharting the system in order to understand the system and identifying the controls you can place reliance on and so on and things like that. You go to ICQs, how we came about with what we used to call PRTs, the program and record of functional tests that time we called them PRTs, program and record of functional tests. The terminology has changed. At that time we were talking about validation and functional tests, now we talk about substantive tests and compliance tests, that time it was functional tests. So we had Coopers and Lybrand who were familiar with our processes here.} {As far as the auditing part, the knowledge and experience you were expected to have when coming from payroll to audit you were expected to know the payroll procedures, and, nobody would assist you on that.} {But it was the understanding what audit was all about. How do you access records, but unfortunately at that particular time we did not have a charter. Unfortunately at that time we were more guided by the external auditors rather than by the standards.}

What is obtaining now?

{What is obtaining, at the moment is that we now have the current chief internal auditor, who came up with the audit charter in terms of the international standards professional practice of internal auditing. The very first standard, standard 1000, requires us to have an internal audit charter}

So in a nutshell we can say 1. there are Coopers and Lybrand procedures and 2 there is also the IPPF of the institute of internal auditors?

{Yes I was going to go into that, because the aspect of IPPF only came into our environment when the current chief internal auditor took over office. Because we have been guided, virtually everything by Coopers and Lybrand. Even seminars were being done by coopers and Lybrand, but, now
when this current chief internal auditor came into office, there was now a bias towards the Institute of Internal Auditors, because he wanted to make people more professional. He also wanted to say, look here you cannot be a professional if you don’t belong to a professional association. You have to belong to a professional association which follows some standards and gives you guidance on the practice of internal auditing and also the code of ethics. Things like that.

Do you have anything else to add to that? no.

So, now let’s tackle the actual questions. The first one I have got here is. To what extent do organisational and reporting structures ensure broad audit coverage? Otherwise we are first of all looking at where the head of internal audit is placed on the organisation chart. So, I don’t know, can we your contributions?

{It is very unfortunate, particularly on the railways. When you look at the chief internal auditor in terms of grade he is a d5, I don’t know whether he was upgraded, yes d5, which really, from a professional point of view, it creates some discord in the operations, because you can imagine, he has got the overall say in terms of audit, to all other branch heads, but he is at par with those same branch heads.}

When you say d5 what do you mean? Let’s look at the tiers. On what tier is he, starting with the general manager.

From the gm there are directors and then branch heads

{The general manager is grade f 3 then there are directors. e5 Then there are branch heads which are e2, e1 and then there is d5}

Meaning what? What is the meaning of this? Is he lower than e1?

{In terms of remuneration he falls in d5 which is lower. Which means, obviously, how do you appraise, because he is appraising all these guys and reporting to the general manager and he is at that level. This is what I am saying.} From a professional point of view, from that hierarchy, from the point you raised, I think the chief should be put at director level. Because he directs the whole railways in terms of audit, but he is put somewhere there. I don’t know how that happened but if you look at other organisations and if you read about other situations and other accounts which have been produced you find that the chief internal auditor is at that level and he reports to the chief executive. He is in line, just below the chief executive officer, but in our case you can see, even if you are doing something there, these guys are likely to challenge. although you report directly to the general manager. So your coverage is only in terms of the general manager, it’s not in terms of your authority in terms of your grade. So I think, that’s
where I personally felt there was something that your authority, in terms of your grade, you see what I mean. That’s where personally I felt there is some compromise in terms of corporate governance there. That’s what I think, but I might be wrong but I think this was something that needed to be addressed.

{You are very right, in terms of reporting to the general manager, he reports to the general manager administratively, and he is supposed to report to the audit committee functionally, of which, by virtue of ranking, he is supposed to be even higher than the directors, so that maybe he can articulate his duties freely, above the directors.}

{We all concur with you when you mention the word freely. We said independence in terms of conditions and conditions we are talking about, there are six conditions. Organisational structure is one of them, we are talking about organisational structure we are talking about access to records, we are talking about management philosophy and attitude and we are talking about policies and practices within the organisation, competence, conflict of interests. These are the conditions that might impinge the auditor from carrying out his work and things like that.}

Organisation structure in our situation, in the current structure which is obtaining, as long as the chief internal auditor is reporting to a senior official who is empowered enough to make a decision it will not cause any problem. {But in our situation, why probably my counterparts here are talking about the d5 aspect is that, there are too many other ranks above him to the extent that he cannot be said to be correctly positioned. He is supposed to be strategically positioned so that he can also operate at a strategic level. In other words you want to operate at a level where you can change things, where you can make decisions. Where the people you are talking to, like right now he sits in the management executive meetings. It means they realised the strategic nature of his portfolio. Because in manex that’s where decisions are made and so on.} {When it comes to the grading part, it’s something else, grading is done by Patterson grading system and unfortunately NRZ adopted this Patterson job grading system with the agreement of labour, and labour is heavily involved in the grading process. And that sort of interferes with our freedom. Because as internal auditors, we cannot be in a situation where our auditees are determining our fate, our future, our livelihood. Do you hear me?} This is where we are running into problems. {Ordinarly what should happen is the chief internal auditor, like we have right now, is reporting administratively to the general manager and functionally to the audit committee. In other words, we should be resourced, only the resourcing aspects of it, administratively, like going on leave and things like that, that should come from the general manager, we should report to the general manager, but when it comes to the other resources, like
even the conditions of service, they are supposed to be determined by the audit committee. They are supposed to hire and fire the chief internal auditor. They are supposed to be the ones who appraise us on our performance.

So if I get you right you are saying on paper the chief internal auditor reports to the audit committee functionally, but in practice he is actually reporting to the general manager. Do I get you right?

{You get me correct. On paper it’s written that functionally he reports to the audit committee. And also on paper it’s written that administratively he reports to the general manager. There are problems there. It is the ideal situation, the world best practice. Only if the audit committee is independent, because unfortunately our chief executive also sits in the audit committee. You get me right. I know you are recording things like that, this is not meant for their consumption. But as long as we have a chief executive who sits in the audit committee there is bad corporate governance. Because the only opportunity where the chief internal auditor can freely, freely discuss issues pertaining to the organisation is with the audit committee members, representing the board of directors. But now here is an auditee there, who happens to be also part and parcel of the audit committee. His office also comes under your purview. He is sitting in there. Are you able to articulate issues pertaining to his particular office.}

So do we all agree to that?.

{Yes we do agree but I may also add that it also depends on the structure or the people who have been appointed into that audit committee. An audit committee needs people who are relevant. I hope you understand when I say relevant, I mean one must have accounting knowledge, because you are dealing with the financial aspects and these should be non railway employees. Independent, so that when the chief internal auditor brings a problem or an issue they are able not to be biased. So his independence is not compromised, and similarly the independence of the organisation is not compromised. So the formulation of that audit committee needs to be put in place, such that it is well represented in terms of knowledge, qualifications and in terms of performance by the same audit committee. So, that will enhance the situation and in that audit committee charter there should be a clause in their operation to say, where issues which are sensitive and need to be discussed without the ex-officio, that is the chief executive officer, he should be excused. So that he knows that when the chief internal auditor needs to discuss sensitive issues, so that his independence is not compromised. Then he can be excused on that issue. And then people are there to make that decision, that’s what I think.}

Composition of the audit committee

Audit committee not independent
Let’s move on, so can you in brief tell us what you think would be the ideal situation as far as the where he should be placed on the organisational structure and the reporting part of it?

{We are not just looking at the office of the chief internal auditor. We are looking at the audit function. We are looking at organisational independence and we are saying as far as we are concerned we report to the audit committee, and as such our conditions of service, everything pertaining to the function of internal audit, should come under the purview of the audit committee. Its only on the administrative aspect, where possibly you need to be given a vehicle to go to Mutare or things like that, that, the other functions come in, we can now approach them.} {But it also has some problems as well. Because, the very same people whom I am supposed to kneel and ask for 10 litres of fuel are the same people that I am supposed to go and audit. It obviously I cannot be objective. My independence is already compromised because I need a full tank to go to Harare yet I am only given 20 litres of fuel. What would you expect me to do in order to obtain a full tank. You have to be a nice guy for him to give you what you want, to be able to do your assignment. That’s why we are insisting that everything of ours should be coming through the audit committee. We should not be going via any director or branch head. Our branch head should go to the audit committee on our behalf in order to get whatever we need in order to discharge our duties. Because the independence is seriously compromised, let’s say for arguments sake, we need something and we go through the chief executive officer, and he refers to be the human resource manager, who happens to be our auditee, and we are going to Harare to do an audit in the human resources office. You can see the audit function is seriously compromised in terms of independence, because there is a situation where by, like he puts it correctly, that you have to be a really nice guy in order to get what you want. But your objectivity is really seriously compromised and your independence is seriously compromised. But if you were independent from the audit committee, and if it was the audit committee saying, can you provide resources to the auditors who are going out, then, that way our independence would not be compromised.}

{I am also suggesting that the independence must start right at the top. The tone must be at the top. It must be the audit committee itself. It must be independent to the extent that it must be able to direct what is necessary. Currently the situation obtaining is that it is headed by a registered accountant, somebody who worked in the auditor general’s office. He knows what auditing is all about. But as far as independence of the committee is concerned we cannot vouch. What we can vouch at the moment is that we have an accountant who knows our job. But when it comes to issues pertaining to us, they are thrown back to the entire system,
we are just blanketed with the rest of the employees and as a result we cannot be effective.)

I think we have exhausted that one. Unless someone wants to add something new.

{I wanted to add to this scenario, you can see that, as an auditor you need to be independent in mind and in appearance. So from that scenario, on appearance there is no independence there. Seriously compromised.}

Are there any other issues? laughing

Fortunately you touched on a topic of much interest to auditors.

Maybe we will touch on it later on when we discuss relations with other arms of corporate governance.

{People feel aggrieved as far as the structure is concerned. The structure does not do us well. It does not do us any favour in as far as our ability to execute our duties as independently as possible.}

Ok may be let’s move on to the next question. How is freedom form interference in internal audit work ensured.

Maybe we can start this discussion under the audit charter to start with. Does it have any provisions to ensure that there is no interference in audit work.

Yes the audit charter has provisions, but in practice, that where the problem is. Because we are saying or talking of independence of the mind and independence in appearance. { In terms of resources, we are supposed to be resourced somewhere else other than by the auditees, because we are dependents of the auditees instead. For us to articulate any task we have to first beg. Then the independence part of it is already compromised, because you have to say out what you are to do where you are to go. How to articulate your duties. Then already the whole program is distorted. So, firstly, maybe I would first highlight on the housing part of it. As a matter of fact we are not supposed to be housed here where our auditees are. We are supposed to be somewhere else other than here. That’s for a fact. We are supposed to have our resources from a separate budget from the auditees, and we are supposed to be given, or to have our resources availed in a different scenario which doesn’t involve our auditees. Because, for an example, you want to go to Harare, you have to ask from the auditee if he can accommodate you, if he can feed you, If he can give you fuel, or back up service. Then the whole scenario is compromised. So, obviously we are not independent.}
The point he is bringing is, something has happened in a certain area. Ordinarily what should happen is that a team of auditors should go and investigate the irregularity. And everybody there will be very much aware that a team of auditors is coming. So the first thing is if the person who is responsible for allocating accommodation is somehow involved, they will definitely tell the auditor that there is no accommodation. Already he is interfering, or he can say I can only accommodate one when he knows that three guys are coming. Eventually what you have to do is to cancel the trip. Unlike possibly during the olden days when we used to stay in hotels and we were not housed here, but in town, independent from the rest. But because of the financial situation we found ourselves in the same buildings as auditees. When we used to go to hotels, we did not need the auditee to know whether we are coming or going. So we were very independent, but this current set up we have right now, we go into guest houses which are controlled by auditees, the provisions are controlled by auditees. He or she might tell you that you are coming here but there is no food for you, bring your own food. Already you are running into problems,. Then you go to the chief accountant here, he can tell you that I don’t have money to give you to go and buy food. So automatically you have no choice but to cancel. So what my colleague as suggesting is if we are going to be resourced from the chief executive officer's office. We know our budget is there under the chief executive officer’s office and we give him a copy of our plan. The same plan which goes to the audit committee. He knows this whole year I am going to have what teams of auditors going out, they will require so much in terms of accommodation and food provisions. It will not now involve the chief accountant, or the finance manager at all. And no begging will happen. If the chief executive’s budget does not allow him, it is only the chief executive and the auditors who would know. If the chief accountant knows that the budget does not allow it, so auditors will never go to Mutare. So he can do anything in the Mutare office, because the auditors have no capacity to go to Mutare. Because the auditors have no capacity to go to Mutare. You see. (Furthermore, just to add something to that, let’s say for arguments sake we rely on auditees and you are supposed to go to Harare, and already auditees are aware, what are you going to do. Even if there was something they have done. Do you think you are going to find any evidence?. There will be very little evidence if any.) So there is no independence there. So as a result, it means, as he rightly puts it there is interference, it means there is need such that, like spot checks. (If you want to do a cash count. You need not tell the people that you are coming. The surprise element is no longer there.) Even if I am going to surprise his office, but if this office is the one which is going to accommodate and feed me they already know that the auditors are coming and which section they are going to, definitely it’s not surprising. And you find that pilferages which happen are only discovered when it’s long overdue. So independence is not there}
On the aspect of freedom in our sections, our freedom is interfered with by the current set up within audit. The set up where you have auditors restricted to payroll, accounting, inventories and special investigation is, it does interfere, because that auditor is not competent enough to do the other work, if anything else happens, we are now restricted. Our staffing level is rather too high. I think we have one of the largest audit functions, because of that aspect. But if all people were versatile and could be changed around to any particular section you would find that we would not require as many auditors as we have.

Has anything been done to make auditors versatile so far?

What is being done now, gradually, its being appreciated, the fact that there is a drive to ensure that all auditors become professional, and it is hoped that when they are all professional then they will become members of the institute of internal auditors. It is hoped that at that point everybody will be able to do everything in auditing. Because auditing has nothing to do with experience. It’s got more to do with knowing the techniques. The techniques which are applied in accounting, payroll, and inventories are similar. The experience part of it only helps you as far as understanding systems. Of which you can understand systems, you can take internal auditors from Ernest and Young to audit our systems. He will come here and first understand our systems. but in our situation, we cannot do that. This is what we inherited.

Even if there are steps to try and professionalise the branch there are some limitations. It is a sacrifice that individuals are doing to finance their studies, if it was a staff development issue, to say people are given a chance to go on and further studies and they are given all the resources and maybe that way people would be well developed professionally, because very few if we talk of percentages, we talk about 3% of the staff trying to professionalise their studies, of which it is really a hiccup on that aspect again. I think it was supposed to be approached holistically to say people are resourced so that they can articulate that.

Are you happy with the audit charter as it is or are there any inadequacies?

The charter is excellent, but the implementation part of it is a challenge, especially when you have divisional heads here who do not understand what audit is. They view audit as somebody who is coming to look for errors. And automatically some documents will not be availed to you as and when you require them. Because the charter has not been fully embraced by the entire organisation. Whilst the audit committee has approved it and senior management has approved it, but the rest of the other managers, do they really appreciate what that document empowers the auditors to do.
Has it been disseminated to the whole organisation?

{Yes it has been disseminated, but the fact that you go into an office, for example you go to manning section, they will tell you that this file is very confidential because it deals with promotion. Already there is interference. And when the charter is quite specific and explicit that that particular aspect that we should have unlimited access to records. But you send your most seasoned auditor to collect a particular file from the manning section, they will tell you that this is a very confidential file, I cannot give it to you. Eventually the only way we get it is through the chief internal auditor’s office. It is a limitation. Already there is interference. And by the time you come to the chief internal auditor, some other documents are not there in the file. But if the auditor had picked the file at the particular time, all the documents would have been available. By the time it is sent thorough the chief internal auditor it’s nicely done. And the information you actually looking for, you will never be able to get it.}

That brings us to the question. How do you deal with irregularities by senior members of staff? You are out there, auditing and you discover an irregularity that involves a senior member of staff. What are the procedures? How do you proceed? Is there any procedure?

{On paper if it is fraud, our fraud policy empowers us to report it to the law enforcement agencies, without recourse to anybody else. On paper, but in practice what we would normally do is that when we see something like that we go through the office of the chief internal auditor. The chief internal auditor will normally want evidence. What we simply do is to produce our report, give him the evidence, and he will handle it at his level. But on paper it empowers the auditor, if they see anything amiss, even if it has been done by the most senior official, as long as it is theft or fraud, he should be able to say, report it straight to law enforcement agents.}

What has been your experience on that one? Is your report presented as it is or is it diluted, doctored or watered down? What has been the experience?

{Fortunately, I think with the current set up we have, I don’t think our reports are ever diluted. It’s probably the action that is taken out of that report. The report would go as it is. Its action which is taken when it comes to members of senior management. The entire NRZ is governed by a code of conduct. Whether you are a chief executive or things like that in terms of the labour act. We have a code of conduct. The code of conduct details the procedures to be followed when there is theft and things like that.}

{I think on that one normally, especially, maybe, let me say to all internal auditors, they audit maybe the entity which they report to, so on that scenario you find out mostly, like the set up, even in our situation the very
people which we audit are the very people which we report to. So you find out that on that scenario, let’s say, if I am auditing the finance manager, and I will also address the report again to him. Which means I am just auditing him like his member, it’s just the same as auditing him and report the same situation to him, and he is the one to make a decision. And sometimes, that’s why on independence, really on that issue it’s very, very difficult to say there is independence there. And you find out that most of your reports, they see them, we just report it as it is. And they take it as it is. You find that the responses to those reports, or implementation of recommendations on those reports may be slow, so, in other words we are saying that, really as auditors, internal auditors, our independence is compromised.

Let me add on that one. When it comes to, say and issue pertaining to the chief accountant and the finance manager, that audit report is not addressed to the finance manager it’s addressed to the chief executive or the director finance and administration, to his superior. If it has something to do with him or his particular office, where he has got interests. But unfortunately the system is such that its quite democratic it would allow the finance manager to also have access to that report and respond to the allegations via the office the of director finance or via the office of the chief executive to us.

Cooperation from the auditees, are you happy with the cooperation you are getting? For example implementation of recommendations and the time they take to respond to your audit reports. Generally what is the position? Are you happy or are there certain areas where you are not happy?

I don’t see any problem with cooperation. So far they have been cooperating. Most of our findings are discussed with senior managers of the respective sections. So where we recommend something they don’t agree with it, discussed with them such that it will not appear in the report if it’s not implementable. But when we put it in writing in our final report its implemented without any problems.

There is one issue here, I don’t know if we can get a response to that. You are aware of all the areas that should be covered by the auditors in the whole organisation. So are there any areas that are not subject to internal audit scrutiny?

{Our system is in such a way that we should have right in the middle of the centre circle internal controls, around it we are supposed to have risk management, and around that, the bigger circle which is corporate governance. We are restricted to internal controls which of course as far as I am are concerned we are doing nothing, because internal controls come as a result of risk management processes. And risk management processes are also a subset of corporate governance processes. Even if you look at the
definition of internal auditing, it talks about the effectiveness of risk management control and good corporate governance processes. But we are restricted to internal controls. As a result, like the question you have asked about issues pertaining to senior management, those issues hardly come up because we are restricted to the inner circle. If we move out of the circle to go to risk management and corporate governance it will now embrace everybody within the entity. But now it’s only to operatives, when you go to internal controls. It’s more to do with operatives. So we are not being effective. We are not actually improving or adding value to the organisation. We are simply saying, here is a control put across by management, is it being adhered to.}

Let’s go on to audit planning and budgets. What we want to find out here is who provides the inputs and who authorises the internal audit work plans and budgets.

{The work plans are approved by the general manager. They are initiated by us. We do the budgets, give them the audit plan and it goes, it is approved. But the actual resourcing part of it. The actual allocations, cost allocation, is done by the finance manager. This is where we run into problems, when there is a printout which comes out and says can you put what you requirements, on this particular cost code. You need say $2000 there, that amount may not be provided. It might scaled down. The plan itself would have been approved, but now to execute that plan, it needs some funding. That funding comes under the purview of the finance manager, and the finance manager, possibly looks on the finances available. If he does not prioritise internal audit and cuts on the internal audit. As we talk right now, we have problems of bond paper. We have problems of bond paper, you know, we do a lot of paperwork. Our systems are manual, and so there is a lot of paper work. For instance if we ask today, auditors to go on an audit, the first thing is they have to do is scrounge around for bond papers, in order to do some photocopying for their working papers. And it might not be possible. It might take too much time and effort in order to come up with that.}

I don’t know if there any other issues on interference with audit work? Any other areas where you feel that there is interference.

{One other thing I should mention is that among the hierarchy of the organisation, the managers and things like that there are some sections where you would actually find people who appreciate the role of internal audit, and there are some other areas who do not think that it is a necessary entity or function. That’s where we start having problems. When they look at us from a policeman perspective, instead of people who are here to add value and improve the organisation’s operations.}
But has there been some form of education to enlighten them on the duties and responsibilities of internal audit and how they add value to the organisation?

I don’t think that has been done. I think that’s where the problem emanated from.

{I think that should be assumed knowledge. We will assume that as they get up there to chief executive, we cannot expect a chief executive who doesn’t know the role of internal audit. Its assumed knowledge. He is supposed to know. We cannot have time to teach him the role of internal audit. He is supposed to know.}

Just to remind him, a refresher course perhaps?

{ I think it’s very pertinent to go that route, probably to conscientise them on what benefits they can derive from internal audit, because they will be more interested in the benefits. The reason why internal audit is there and the benefits they might derive from internal audit.}

Do they actually have a copy of the audit charter?

The audit charter was circulated to all branch heads. What we know is that it was circulated to all branch heads. What we don’t know is whether they managed to retain a copy or passed the same one back.

{I will tell you my personal experience with the chief executive. I wanted a document from his office. He said to me get out!. Get out!. Get out!. I refused to get out, I just stood there for some time. Then he said, Come let me give you what you want. Then he produced document I wanted and then he blocked the upper part and the lower part of the document leaving one paragraph, and he said, what you want is just this paragraph.. and I said it will not make sense, I want the whole document. He said no, phone your boss. I phoned him from his office, and he told the chief executive officer to give me what wanted. But still he refused. He only photocopied just that one paragraph.. which did not make sense. And this is the chief executive who is supposed to know the role of internal audit.}

{I think, the way I see it, the biggest problem with these chief executive is, he sees where he is at f3 and he sees my grade somewhere down the ladder, and he says I cannot talk to this one. I want somebody more senior. It takes us back to the issue of the organisational structure. Even at section level, when you go to Mutare and you want to talk to the workshop engineer, he says who are you. You introduce yourself. He knows that this one is a lower grade. And he says I can’t talk to you, I can’t give you this, bring your boss.
But my boss in Bulawayo. I can’t bring him here. Laughing. It’s ,maybe the same way some of us treat our messengers. You say I can’t give this to the messenger he will not appreciate it. Probably that’s the same way they also look at us.

So in some cases, there is not sufficient cooperation from the auditees?

{In isolated cases, but when it happens its really in bad taste, but it doesn’t happen often. The other thing is, we agree that probably their perception of audit is more driven by the aspect that they would be fully aware that some of these auditors were just clerks yesterday and automatically become auditors, and they may be saying, is this person going to be able to assist me. Probably it’s up to us to prove that we are necessary. We have to prove within the structure that we are important to this organisation, by recommending, suggesting things which will be able to save money, reduce costs, reduce wastage and things like that, improve operations and then we will have efficiency. If we assist or managers in that perspective they will start to respect the role of audit, and not to look at the role of audit as policemen, one who looks for faults and reports those faults}. {Unfortunately the system we inherited, the system based approach from Coopers and Lybrand was reporting by exception. which implies that you only report those items which are irregular.} {The modern day practice, we find ourselves, involved risk based approach. It is not appreciated if you just look at negatives. And they also look at you as a person who is a fault finder, which is not what we necessarily are. We are there to assist management to effectively discharge their duties.}

I think that one we have quite exhausted. Let’s go on to number 3. How much do relations between internal audit and other corporate governance arms enhance good governance. Starting with the audit committee. Are you getting cooperation and support in ensuring that you have sufficient independence?

{As far as the audit committee is concerned, what the fraternity of this particular audit family was expecting was, at one point we would want the audit committee to sit down with the auditors to listen to our concerns and on aspects pertaining to independence and objectivity. But that, I think 99.99% of the auditors, we don’t even know the members of the audit committee. If there was that opportunity to sit down with the auditors and listen to their concerns and what is hindering and what is interfering with the effective discharge of their duties it would have helped. Now the aspect of us just giving copies of our reports….a written documents is quality evidence, but at the same time it doesn’t give all the information, that’s why probably in this particular forum we will be talking, because you get much more when you are discussing rather than if you had given us pieces of

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paper to write. Because now we want to couch our words. We write what you want to hear. But in this discussion set up, this where we talk with our audit committee, so that they understand us, our concerns. They don’t know that we have grievances as far as our grading system. We have got a situation where people have gone to court. The case is coming on the 7 May involving internal auditors going to court trying to fight for a proper grade. That ordinarily should not be happening because its unprofessional. But it's happening because probably we have never had the opportunity to sit down with our bosses. Our real bosses are the audit committee. They are supposed to sit down with us and say look her guys if you have got any problems, this is how we want to go about it, and things like that, but what we expect out of you is this. We don’t know what they expect out of us. What we think they want out of us is what we read in the books. Which might not be what this particular committee wants.

Have they ever asked you to do any work for them? Special requests from the audit committee that can you look at such and such issues?

Actually it’s the converse, it’s the reverse actually. The reverse is when there is an issue which is raised by internal audit which they think requires further investigation, they would want to come back and say look at this again. But for a thing to emanate from the audit committee itself, we haven’t had that opportunity. Probably they take it up with the chief executive. We cannot say there are no issues. But it has never come to internal audit to say please can you go and investigate and give us a report on this particular issue.

Otherwise you are aware of the members of the audit committee, who constitute the audit committee

On paper, we know the names, but we haven’t met them.

And you also said there is a financial expert there?

(The chairman, Mr Mangemba, he is a former practising auditor, and accountant.)

Lets now look at external auditors. How do you interact with them? What are the relations, do they enhance good governance?

(They are currently here as we talk. We have a good rapport with them. Very much so apparently because of the manual nature of our systems, they have to rely more on our work. Otherwise they would not be able to effectively discharge their obligations. The NRZ as a complex organisation. They have to rely on internal audit work. But at the same time we do have some misgivings as far as that is concerned. Because our perception of the external auditor is we are supposed to benefit from the association with the
external auditors. When we attach a member of the internal audit to the external auditors we are supposed to benefit in terms of learning more about independence, about what is audit independence. But that, the current crop we get from our external auditors, they are not giving us that, We are not benefiting anything from them apart from we are just assisting them to effectively discharge their mandate.

Do they make any inputs into audit plans?

Not as such, no.

Or can I say are your programs or work plans are coordinated so that there is no duplication?

{We do our programs independently, and I want to believe that they also do theirs independently, but they have got access to our programs, of which I would like to think that they will look at our programs and see whether they will be helpful to their own programs.}

Do you sometimes work together or under the supervision of the external auditors?

{Not as such. We don’t really work together but we assist each other. Probably, I think because we have got different objectives, our objective is an internal one theirs is external one. But when it comes to the nitty gritties of and operations then we find our own focus.}

Your cooperation with external auditors, does it affect the audit fees they charge at the end of the day? Would you know?

{I would say that it does. Because if they are going to understand the system from the work of internal audit, it basically means that they would take less time trying to understand the system, if they are going to place reliance on our work. It also would reduce the man hours they are going to spend on their audit. It does assist.}

Let’s look at management. Are they cooperating? I think we have covered this. Most of them are cooperating but just a few.

I think there is a misconception when it comes to the concept of an auditor being a tool of management. They don’t really understand which management are we talking about, it seems all managers, maybe from the lowest level, they think we are tools of that management. That aspect must be explained, to say we are tools to audit committee management, and maybe the general manager, not to all Tom and Dick. That’s where the misconception is. The way they understand it is the other way round. Because really for them to place confidence on the auditor is really
something else. The cooperation part of it is not done in good faith, although to some extent we might point to individuals.

{I think Mr Matavire it stems from the aspect the that we are not here because the organisation requires internal audit. We are here because there is a statute which actually compels public entities to have a function called internal audit, and as a result as long as it is viewed from a legalistic point of view it’s just like we are just complying. Until such time when it is viewed from the aspect of adding value and improving operations, then you would start getting more cooperation from managers. As long as it is from the public finance act, that this organisation should have an internal audit because there are public moneys involved.}

So there is need for re-education of the managers?

Yes.

Let’s move on to the next question. What threats do you face concerning independence and objectivity. Here we are also looking at objectivity. Do you audit your friends and relatives and so non? Do you audit people with whom you have personal relationships and so on? Or sometimes are you required to audit your own work. For example after moving from other branches to internal audit.

I think on that issue, the auditor, if maybe, to say, I have got a relationship somewhere. Normally we recuse ourselves from auditing that. Maybe if it were my work, if previously I was in accounting and I was the one who was doing that work, normally we recuse ourselves from doing that. But now the threats which might be there on our independence, the issue like to say, the very people who fund our operations are the very people we are auditing. So you find out that, say, I am supposed to go to Mutare and I am supposed to audit the cooks, and the one who is cooking for me. there is also a threat there. The independence is threatened. So on that scenario, that relationship, where we’re saying as an auditor the same person you are auditing is the one who is providing you with some help. There is a threat to independence there.

This is more of personal one. Have you ever felt threatened before, during or after an audit? Have you had situations where you are saying going to audit that place again, if I had my way I would avoid it?

{We had quite a numerous number of threats to the extent that some of us acquired firearms at home in order to protect our property at home. Because auditors are not necessarily the best friends of most people in the organisation. When somebody is fired as a result of an audit, it is taken that it is the auditors who have got him fired. And we have had situations where,}
like RAU members would address their constituencies to say, auditor so and so is the one who is on us, making sure that our members are fired. Already that is a threat, and we feel very much threatened, and we were actually assisted by some members of the organisation to get firearms, because we were now afraid that the threat would now come outside the framework of the NRZ environment. Those threats are there, but it has never stopped us from doing our work. We will continue and the other aspect is, it comes back to the organisational arrangements, and to say this particular auditor here has got aspirations to move up the ladder, aspirations to become somebody within the organisation. That’s why he goes about and offers his services, and advises management on ways to improve, to be effective, to be efficient, to be economical. He has got aspirations. Now which basically means that auditor is also looking at the possibility of being moved to a higher post. But currently, those people are his auditees. Anything which is damning and negative, they will never forgive him. So when your application comes, they will never forget that this is the same auditor who wrote about this particular aspect. We do have classic examples where an auditor, probably, somebody seconded to us as an auditor, and eventually he wants to make an application within his own branch, but because he is alleged to have written a bad report about them, the man was never promoted, until we had to promote him into audit ourselves. That can happen. And moreover, also our line of movement upwards is not much. And because the steps are very few that’s why we were expecting ourselves to be at a certain level which would not encourage us wanting to move back into the auditees’ arenas. We should encourage auditors to stay in the audit field. But because there isn’t much in here in audit, because one once somebody gets to the level of c5 or even d2, that’s the end of you. And in most cases the chief internal auditors are normally recruited from outside. No matter what qualifications you have they will take somebody from outside. You can only be in an acting capacity. So people would want to go back to those functions. But remember at one time you were taking them to task on a particular issue. Especially on issues pertaining to corporate governance. That is the problem issues, governance issues. When it comes to issues of internal controls, they are very cooperative, when it comes to issues of risk management, they are so, so because it has a telling on his own job, the manager himself, that he is not doing his risk management. They are not very cooperative. But when it comes to internal controls we can say it is 120% cooperation.

Let's also look at this issue. Is the internal audit function also used as a training ground for those people who are being groomed for promotion into managerial posts and so on? Is that happening?
In the railways, at one point, the internal audit was being used as a dumping ground. Laughing. For those people who were not wanted, they are highly recommended to come to audit. But at the same time, we are glad to say that our skills have been appreciated by the same branches, that these people are not useless. They are useful. They can actually change things around. We have had quite a number who have moved back to the branches at a higher level and they are doing well.

We talked about the procedures for dealing with threats to independence. Are these documented? For example if you are about to go on an assignment and you discover that there is a close relative in that department, is there anything documented to guide you on what you should do?

{No, no, I don’t think it’s documented, what empowers us is only the audit charter. Then what we find on the ground itself, we look at it and we use our own judgement. If there is a situation where we cannot discharge our duties effectively, then we should use our judgement as an internal auditors that I cannot do this. And the other aspect is, we look at ourselves just as an appraisal function, and as such when you go out in the field, and you see something which is a matter of policy, and that policy might be detrimental, what we can only do is to recommend. What we can only do is to recommend, possibly review of that particular policy.}

Right, gentlemen. I think we have exhausted all the questions I had here. But is there anything else concerning independence and objectivity, which you might want to put forward, because you are the practitioners, you go into the field and you meet these situations, probably there could be something else that you feel should be discussed.

Maybe to sum up, the way we are structured as a branch needs to improve, because we are found to be, maybe trying to look for other greener pastures to other branches, which has a negative impact on our career development. Because there are some limitations within the branch, maybe about the hierarchy I must achieve for me to be say, to become somebody in the organisation. And also when we.. it will also enhance… to come professional… when I am satisfied with my confinements as an internal auditor, that and maybe also interaction within the sectional teams within audit, where we are supposed to harmonise the our roles or our professional expertise so that one becomes more versatile than to be limited to, or in our sections. I think that will help to groom the professional attributes within the function as a whole.

{Maybe I have something to add on the threats, though it’s not always, but at times you find out that as internal auditors, specifically we are there to appraise on internal controls, then to put some recommendations if there are
weaknesses in terms of improvements. But you find out sometimes, on some scenarios, the internal auditor, you find yourself involved in implementing maybe whatever you would have recommended. Which means on the other side you are saying that the one you are going to implement or that system you are going to set, you are also going to audit. So you find out that it’s very difficult, let’s say if you are a father, you have got a kid, it’s very difficult do say your kid is very ugly, or somehow misbehaving. So you find that, that one is also a threat to independence.

Are you involved in consultancy work, where branches ask you to come and examine a problem and come up with recommendations, or are you also involved in risk management processes, and to what extent? Do you get to a position where you implement, or do you just recommend?

Like what we said initially, that the other handicap we have had from time immemorial is the aspect of our own competence. We said one of the conditions which interfered without freedom to execute our jobs freely is competence and, as long as it is not seen, it cannot be seen that the auditors are competent enough to be able to engage in such services like consultancy, because the definition of internal audit is quite clear. And from the definition of internal audit, everybody should be competent. The definition is simple, it is an independent, objective assurance and consulting activity, designed to add value and improve organisation’s operations. It helps to achieve that objectively by bringing in a disciplined, systematic approach to evaluate and improve risk management, control and governance processes. That’s the institute definition. And now, from that perspective, as long as the NRZ does not take it upon themselves to say, all internal auditors should be member of the institute of internal auditors, so that we taught professionalism. So that we know what we are supposed to be doing. So that we are updated with the most current practices within the profession. We have got a problem. If they are expecting individual auditors to be members, and things like that, it will not bring the desired results. But if they were going to say for every auditor, they are paying for the subscriptions, everybody attends the courses and everything, they would expect something out of it. Because this is where these things are taught. But as we sit right now, I don’t think, apart from the chief internal auditor, he is the only member of the institute of internal auditors, because of the financial aspect, obviously because his is paid and ours is not paid. And the other aspect is, you talked about it that are we consulted, I wouldn’t say that we are not consulted. There is the chief internal auditor who is always consulted. He goes, probably, because he is a qualified man, they always consult him, and because probably the rest of the auditors might be lacking as far as competence is concerned they would rather end at that level.
But even at lower levels we are consulted. They consult us, at their level also, at corresponding level, horizontally they really consult.

I thought what he meant there was consultation as far as senior management and not divisional heads. He is referring to the consultation which will happen probably there is something to happen, and the audit committee says can we have your input, can we have your inputs, can we have your advice. Senior management, can we have your inputs. That hasn’t happened to us but it happens to the chief internal auditor. So we cannot say it doesn’t happen. It does happen. The fact that they allow him, they want him to sit in the manex meetings it basically means they want to consult him when it comes to policy issues.

But actually I would say it’s there at all levels, either directly or indirectly, that will add value to the same senior management, because from the lower level up the ladder, it constitutes the whole process to the manex level. So I think whatever level, I think its consultation.

But the question is how far do you go, do you just advise or do you go to the stage of implementing?

{Maybe you might be there as an observer, you might be there as an advisor and normally you don’t implement, because at the end of the day you come back and audit that aspect. So if you implement then it means you are auditing yourself.}

Ok gentlemen, I think we have exhausted the issue. I thank you very much for your participation.