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AN EVALUATION OF THE COSTS AND BENEFITS OF AN INTERNAL AUDIT DEPERTMENT: A CASE STUDY OF LIFEL INVESTMENTS

BY

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DEDICATION

To my mum, whose fascinating anecdotes lured me into this profession; to my dad, by whose example I became accustomed to and enjoyed hard work and a scholarly approach to life; to my supervisor, by whose example i developed an insatiable desire to figure out better ways to achieve better practices for my research project.

ABSTRACT

The main research objective underlying this study was to evaluate the costs and benefits of establishing an internal audit department within an organisation and to explore whether it is more beneficial and cost effective to outsource the audit function or to have a permanent internal audit from within the organisation. To enable a comprehensive data collection on the topic the study took a case study approach. The research was conducted on the internal audit function of Lifel Investments using a sample size of twenty five respondents drawn from four different departments namely the finance and administration department, the internal auditing department, the risk management department and the accounting department. Information was gathered through administration of structured questionnaires and interviews. Results reflected that though the internal audit department is viewed as a major cost component within an organisation and the initial cost of establishing the department and documenting the system of internal control is a significant cost that requires time to be recovered, an effective internal audit department results in substantial benefits that outweigh the costs, though not necessarily quantitatively. Some respondents interviewed highlighted that they have internal audit departments as a statutory requirement. On the other hand, respondents regarded internal controls as critical to the organizations' ongoing success hence the need for a robust internal audit department**.** The author recommended for a more proactive approach to tackling fraud and reducing misstatements by efficiently utilizing the forensic accounting expertise at its disposal and also vulnerability analysis involving all departments across various functions of the organization in order to identify areas that are more prone to loopholes and fraud eminences.

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TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

LIST OF APPENDICES

CHAPTER I

INTRODUCTION

1.1 Introduction

This chapter outlines a general introduction to the study. It defines the parameters of this research and provides a conceptual analysis of the problem in a bid to evaluate the costs and benefits of the internal audit department within an organization. It introduces the guidelines for the research, the problem statement, aims and objectives of the study, assumptions of the study, research questions, limitations and delimitations to the study.

1.2 Background to the Study

The role of the internal audit department has shifted over the past decades (Anderson 2003). The internal audit function has become more globally important and prevalent. Today's business has become complex in both structure and operation, coupled by various financial squabbles that have threatened survival of firms. Of late, the media coverage has heavily debated the ineffectiveness of the internal audit function and the audit committee in overseeing the auditing function and the resultant difficulties faced by organisations thereof (Rezaee et al., 2003). It is thus of paramount importance that organisations implement effective control mechanisms that will ensure the survival of the organization. Internal audits often serve as the first line of defence against disclosure errors, exposing unintentional errors caused by weaknesses in a company's internal controls and intentional errors due to fraud (Mercer, 2004). Today's business also has become a long way since the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) went into effect, both in terms of assisting management in complying with requirements for evaluating and testing financial controls over financial reporting and improving internal audit's ability to perform more traditional internal audits. Financial reporting improprieties and business failures in companies involving Enron, WorldCom and Adelphia have cost organizations and tax authorities billions of dollars between years dating 1996 and 2000 owing to the failure of the internal audit function to detect and maintain effective internal controls. Such global corporate accounting scandals have brought the role of internal audit and audit committees under increased scrutiny (Strategic Direction 2003). The Zimbabwe Stock Exchange has called for a mandatory requirement of an internal audit function for companies listed on the stock exchange market. The Reserve Bank of Zimbabwe has also raised this requirement for all banks to have an internal audit department in response to the 2004 banking crisis. This step has alarmed other organizations and various sectors in the economy to appreciate the significance of the internal audit function in guarding against theft, misappropriation of funds, fraud and financial misstatements. The King 3 Report 2009 advises companies to have an effective internal audit function that has the respect and co-operation of the board and management so as to deter the high possibilities of risk and business failure. It is with this background that this research topic has been chosen the aim been to come up with ideas on how internal audit departments can maximize its benefits by improving organizational internal controls at minimized costs.

1.3 Statement of the Problem

Generally, internal audit departments are viewed as a major cost component to an organization. Most organizations establish the internal audit department in order to conform with statutory requirements without taking into cognisance the immense contribution such a department brings to the success of an organization.

1.4 Research Objectives

- To explore the possible benefits and costs of an Internal Audit Function within an organization.
- To explore the role of the internal audit department.
- To evaluate the effectiveness of an Internal Audit Department in reducing financial misstatements and corporate frauds.
- To investigate whether the benefits of an internal audit department outweigh the costs.
- To investigate the attributes of a competent internal audit function from a best practice perspective.

1.5 Research Questions

- What are the costs and benefits of the internal audit department
- What role is played by the audit department in minimizing costs?
- How effective is the internal audit function in reducing financial misstatements and fraud?
- Do the benefits of an internal audit department outweigh the costs?
- What are the attributes of a competent internal auditing function from a best practice perspective?

1.6 Significance of the study

a) To the student

- The research project will be in partial fulfilment of the requirement of Bachelor of Commerce Honours in Financial Intelligence Degree.
- The researcher will gain practical experience and skills in communication in business, customer care and public relations as result of interacting with both clients and other individuals in the business arena.

- The researcher will have an appreciation of the usefulness of research in problem identification and solving
- The research will equip the student with research skills and useful knowledge confined to the area of study

b) To Bindura University of Science Education

The study will act as literature review for other researchers who may in future embark in this area of study.

c) To Lifel Investments

Findings from this study are meant to improve the significance of the audit department to the proper operation of a business. Findings are also expected to result in improved business performance, reduction in audit costs and business risk.

1.7 Assumptions of the Study

- Respondents will supply the appropriate and accurate data.
- Respondents will respond within a reasonable time period.
- All respondents will fully respond and participate where appropriate.

1.8 Delimitation of Study

Lifel is a diverse safety wear manufacturing firm. The research project will be confined to the audit function of Lifel Investments, from which information and data will be gathered, and restricted only to the period dating from January 2011 to December 2012.

1.9 Limitations and Counter Limitations to the Study

Although the researcher will try to gather as much information as possible in coming up with a solid research there are inherent limitations which are as follows;

- Incorrect data may be supplied by respondents to the researcher. The researcher had to supplement the questionnaire with interviews so as to increase reliability of the findings
- Respondents to questionnaires may take longer than expected due to busy work schedules. The researcher had to make prior arrangements with respondents so as to improve the response rate.
- Due to confidentiality concerns associated with the audit function, respondents may not be willing to release some of the questions posed to them. The researcher had to formally distribute an introductory letter that served to introduce the research to the respondents. In addition the research gave assurance to the respondents that the research was purely for academic use.

1.10 Definition of Key Terms

Defined below are some of the key terms to be used in the research though there are some terms not defined below that may be used in the research.

Auditing: An audit is an examination by a competent independent person of the financial statements of an enterprise, in conjunction with relevant and reliable supporting evidence in order to express an opinion whether or not the statements give a true and fair view. (Introduction to Auditing-A survival Guide-Ernst & Young 2004)

Internal Auditing: An independent, objective assurance and consulting activity designed to add value and improve an organization's operatives. It helps an organization accomplish objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance process. (Institute of Internal Auditors 2002)

Accounting System: is a series of tasks and records by which transactions are processed as a means of maintaining financial records. Such systems identify, analyse, calculate, classify, record and summarize transactions and other events.

Audit Committee: An audit committee is composed of members or neither board of directors who are normally neither officers nor employees of the organization. Audit committees are independent from management and usually maintain a direct line of communication between the board of directors and the entity's internal auditors.

Financial statements: formal record of the financial activities of a business or other entity. They include the statement of financial position, statement comprehensive income, statement of changes in equity, statement of cash flow and notes to the financial statements.

Misrepresentation: includes manipulation, falsification or alteration of records or the suppression of the effects of transactions from records or documents.

Corporate Governance: According to Smith (2005:5), corporate governance is the system or power by which companies are selected and controlled. Directors of the board are responsible for the governance of the companies. The shareholder's role in governance is to appoint the directors and the external auditors.

1.11 Chapter Summary

Internal auditors play a pivotal role in evaluating the effectiveness of control systems and contribute to on-going effectiveness of business operations. Due to its authority and position in an entity, an internal audit department also plays a significant monitoring role. Internal auditors are expected to provide high quality audits at lower costs. Internal auditors need to understand that there are other services other than providing observations to management that they can provide.

CHAPTER II

LITERATURE REVIEW

2.1 Introduction

This chapter is a review of literature that has been written by numerous other researchers on the subject. The chapter provides facts for the purpose of the research project. It concentrates on the underlying principles of a competent internal audit department and the costs and benefits that result from the establishment of an audit department, elaborating the cornerstones on which an effective internal audit department should be.

2.1.1 Theoretical and Conceptual Framework

2.1.2 The Significance of the Internal Audit Department

The Canadian Comprehensive Audit Foundation (1991) defines an audit as an independent, objective assessment of the fairness of management's representations on business performance. Denmark CIS Auditing Study Pack 2003, page 30, describe internal audit as an appraisal activity established by management for the review of accounting and internal control systems as a service to the entity. It reviews, monitors and makes recommendations for the improvement of systems.

2.1.3 Scope of Internal Audit

The Institute of Internal Auditors (1999) explain internal auditing as an independent, objective assurance and consulting activity designed to add value and improve an organisations' operations. It helps an organisation accomplish its objective by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes. The KPMG Internal Control Review Practical Guide (2006) give the following key elements of an effective audit:

- It must create credible processes for feedback for risk management processes are adequate to identify and monitor significance risks
- It should provide assurance that the management processes are adequate to identify and monitor significance risks
- It must be objective and ensure that the board receives the right quality of assurance and information from management and that the information is reliable.
- The internal audit function should coordinate with other internal and external providers of assurance to ensure proper coverage of financial, operational and compliance controls and to minimise duplication of efforts (Kings Report 2002).
- It must confirm the effective operation of the established internal control systems.

Having outlined the significance of the internal audit function to a business it is apparent that an internal audit is essential to a business since it creates necessary checks and balances for businesses.

2.1.4 The development of internal audit profession

There are various factors that have contributed to the rapid growth in the internal audit profession. Many companies have resorted to relying much on internal audits as a result of the high costs that the external audit demands. Increase in size of companies due to mergers and takeovers has led to management difficulties in ensuring that effective controls have been implemented hence the need for internal audits (Lynch 2004 ACCA, Study Text page 285)

According to Elliot and Korpi (2004), by comparison reports give that the internal audit contribution results in the reduction of audit fees. These results provide support for an inverse relation between the internal audit contribution and the external audit fees. There samples consist only of manufacturing companies and financial institutions from a single external audit fees. With respect to the current relevance of the findings, a number of significant changes have occurred in the audit environment the latest being the internal audit contribution to financial statements which have received increased emphasis, (Tread way Commission 2007).

The development of the profession has also been as a result of the rapid growth and ever dynamic complex IT systems coupled by intense competition thereof and lower margins requiring tighter control over all aspects of business and also the need to comply with legislation and regulation (Lynch 2004 ACCA, Study pack Text page 285)

The American Institute of Certified Public Accountants (AICPA) concurs that internal auditors are there to ensure that the company achieves its mission, among other objectives, promoting efficiency and reducing the risk of asset losses. Besides ensuring reliability of accounts, internal auditors should assist management with ideas on how to deal with rapidly changing economic environments especially in Zimbabwe where the economics of Zimbabwe is highly volatile.

2.1.5 Key Elements of an Effective Audit Function

The KPMG Internal Control Review Practical Guide (2002) concurs that an effective audit function strengthens governance by materially increasing shareholder ability to hold their firm accountable. Internal auditors perform an important function in those aspects of business that are crucial in the private sector for promoting credibility. Equity and appropriate behaviour of company officials while reducing the risk of fraud and corruption. Therefore, it is crucial that the internal audit function is configured and have a broad mandate to achieve these objectives. The audit function must be empowered to work within integrity and produce reliable services, although the specific means by which auditors achieve these goals vary. The KPMG Internal Control Review Practical Guide (2002) gave the following key elements of an effective audit:

- A legal mandate. The audit function's powers and duties should be established by the government's constitution, charter or other basic legal document. Among other topics, this document would address procedures and requirements of reporting the obligation of the audited entity to collaborate with the auditor.

- Organizational Independence. The audit function should be independent from those it is required to audit. (i.e., the chief audit executive must report to someone outside the line of authority of the audited entity). Organizational independence allows the audit function to conduct work without interference by the entity under audit. Consequently, users can rely on the objectivity and a accuracy of the auditors' results and report.

- Unrestricted Access. Audits should be conducted with complete and unrestricted access to employees, property and records

- Stakeholder Support. The legitimacy of the audit function and its mission should be understood and supported by a broad range of elected and appointed and government officials, as well as the media and involved citizens.
- Competent Leadership. The head of the audit function must be able to effectively recruit, retain and manage highly skilled staff. Moreover the chief audit executive should be an articulate public spokesperson for the audit function.

- Sufficient Funding. The audit function must have sufficient funds relative to the size of its audit responsibilities. This important element should not be left under the control of the organization under audit because the budget impacts the audit function's capacity to carry out its duties.

- Competent Staff. The audit function needs professional staff equipped with collectively necessary qualifications and competence to conduct the full range of audits required by its mandate. Auditors must comply with the minimum continuing education requirements established by the relevant auditing standards.

2.1.6 Benefits of an Internal Audit Department

The Institute of Chartered Accountancy of Zimbabwe (2006) stresses that an internal audit function can play a crucial role in ensuring an effective accounting system, internal controls and the reporting of information that is relevant, meaningful and of significance to stakeholders.

The Price Waterhouse Coopers Guide (2006) emphasizes that a sound internal audit department identifies the skills and resources that management need to achieve its organisational objectives. Internal auditing continuously measures the level of staff proficiency as well as development progress. Lynch (2009) elaborates that the establishment of the internal audit department assist members of the executive and senior management in the effective discharge of their duties and responsibilities, furnishing management with analysis, appraisals and recommendations on the weakness of internal controls.

The essence of auditing has been further reinforced by the Institute of Internal Auditors (2006) as including reviews of the reliability and integrity of financial and operating information, the systems of internal control, the means of safeguarding assets, the efficient management of the firm's resources and the conduct of its operations. The American Institute of Certified Public Accountants (AICPA) Journal (2010) outlines that an internal audit department is beneficial to organizations as it improves the accountability, internal controls and safeguarding of companies assets and property.

The purpose of an internal audit department is to assist the management and board of directors to deliver its responsibility for the conduct of business operations and stewardship of funds under its control (Caplan 2008). The internal audit department seek to provide assurance to the board and audit committee that internal controls are in place and the business is operating according to the rules and regulations and that assets are safeguarded against theft, pilferage or wastage.

Another advantage of an audit can be drawn from Ernst and Young Guide, (2006:123) which outlines that an internal audit serves as a mechanism for the detection of fraud and errors. The guide also elaborated that an internal audit acts as a deterrent to both employee and management fraud although there is little evidence to confirm this, but it is likely true that knowledge of an impending auditing exercise acts as a moral check on the employees who may otherwise be tempted to engage in embezzlement.

In contrast, there is no full proof method of detecting errors and fraud. An internal audit may be thorough but accounting and internal control systems may present problems as they have inherent limitations. The existence of an effective accounting and internal control system reduces risk of fraud and errors but may still be ineffective against fraud because of collusion by staff members and senior partners. Risk that material misstatements would remain undiscovered is much higher in cases of fraud compared to errors because it often entails action to disguise fraud. An example of such a scandal (February 2006) involved internal auditors of Dore and Legion of Singapore. The case held that there was alleged collision between the internal auditors and the management where the auditors did not exercise the professional duty to report to the audit committee as a result the losses of billions of dollars.

2.2 Empirical Literature

2.2.1 The usefulness of an Internal Audit Report by Holt and Dezoort (2009)

Holt and Dezoort carried out a study on the importance of the Internal Audit Report in an experiment administered by 180 MBA students acting as proxies for non-professional investors at Weather head School of Management. Findings were carried out by manipulating company fraud risk and the presence of a descriptive Internal Audit Report detailing the composition, responsibilities and activities of an effective internal audit function. The study asserted 89% of investors viewing the disclosure of an Internal Audit Report to be positively related to investor confidence oversight effectiveness and financial reporting reliability. Furthermore their results indicate that confidence in oversight effectiveness and financial reporting reliability mediates the relation between the disclosure of an Internal Audit Report and the likelihood of the investor to purchase the company's stock.

2.2.2 The effectiveness of the Internal Audit Function in Detecting Financial Misstatements Brown and Pinello (2007)

Brown and Pinello (2007) carried out a study focused on the effectiveness of the internal audit department in detecting financial misstatements. The study was carried out using a sample of 205 companies listed on Canada's Stock Exchange Listings. Findings gave that of the 188 companies out of the 205 companies that actively participated in the research reported an overall percentage of 66 % of the reliability of an internal audit department in detecting financial misstatements.

2.2.3 Internal Auditing Outsourcing and Its Relation to Size

The study investigated the determinants of internal auditing outsourcing using survey data on 99 companies listed on the Australian Stock Exchange, where 55% percent fully rely on in-house facility and 46% outsource some or all of their internal audit function. Results suggested that internal audit outsourcing is associated with perceived cost savings and the technical competence of the external audit provider. Findings also suggested that for a subsample of firms that have previously undertaken internal audit activities before outsourcing, contrary to expectations, the larger the organization the greater the propensity to outsource

2.2.4 The Importance of an Internal Audit Department by Sarens and De Beelde (2006)

Sarens and De Beelde (2006) carried out a study that focused on management perception of the role of internal auditors. Sarens and De Beelde (2006) carried out a survey of 10 companies listed on the Wall Street and Belgian Stock Exchange in the USA and Belgium. Sarens and De Beelde (2006) asserted that the internal audit can be of value but on the other hand can turn to be a sore when the costs of the internal audit exceed the benefits derived.

Findings from the study by Sarens and De Beelde (2006) provided that financial costs of internal audit vary based on the size of the organization and goal of the internal audit function. Additionally the internal costs of the audit department were based upon the resources used to perform the work. The most significant non-financial cost was found to be a negative reputation of the internal audit role throughout the organisation.

2.2.5 Cooperation between the Internal and External Auditors

KPMG, Reliance on Internal Auditors Guide, 2005, Publication B, carried out a study on the cooperation between the internal and external auditors. The study utilized the survey research design and data generated from questionnaires distributed to internal and external audit staff and staff of other departments in KPMG Australian Boards reflect that the cooperation between external and internal auditors in sharing experience in the public practice is of advisory capacity in the operation of an internal audit department. On the other hand findings elaborated that auditors knowledge of the entity will be of assistance to the external auditors when there are carrying out their audit and this reduces the level of duplication efforts and improves efficiency in provision of auditing and advisory services.

2.2.6 Contribution of Auditing to the Integrity of Financial Reporting by Salem and McNamee(2009)

Salem and McNamee (2009) carried out a study based on five companies listed on the Indian Stock exchange. The study revealed that the Internal Audit department improves the reliability and integrity of financial reporting information and ensures compliance to plans, policies and laid down procedures. Salem and McNamee used interviews to obtain their data. It was found out that eighty percent of professional expects including internal and external auditors argued that the benefits of establishing an internal audit department within the organisation outweighs the costs while twenty percent argued that the department is an unnecessary cost because internal audit independence is compromised and recommendations from audits are not.

2.2.7 The Role of Internal Auditing at Harley Davidson by Goodwin and Yeo, (2001)

Goodwin and Yeo (2001) carried out a study at Harley Davidson Research Institute in Canada. The study focused on the contribution of the internal audit department in the wake of increasing demands to apply accepted governance principles in order to adhere to sound risk management. In order to ascertain the role of the internal audit function, Goodwin Yeo (2001) carried out a survey of directors and top management at Harley Davidson. The major findings were that internal audits are essential since they create the necessary corporate governance ensuring that risk management and internal control processes are followed and are successful within an organisation.

2.2.8 Senior Management Expectation Gap on the role of Internal Auditing by Spira and Page (2003)

Spira and Page (2003) conducted a study on the expectation gap that arises when audit customers do not recognise the value of the Internal Audit function. Spira and Page carried out a survey using a sample of blue chip companies in Atlanta trading on the New York Stock Exchange. The study revealed that an internal audit department that fulfils this definition is uniquely positioned to support the board and management as an essential component of their governance mechanisms. Moreover Spira and Page found that effective oversight and sound internal controls and the value given to internal audit by management has increased.

Spira and Page suggested that in order to effectively close the expectations gap, the internal audit function and customers of audit services should possess a similar understanding of what make internal auditing a value-adding activity. Failure to reach this understanding could result in the perception that internal audits are simply a hindrance to achieving organisational goals thus leading in underutilised audit services.

2.2.9 The Value of Internal Auditing in Fraud Detection

KPMG (2004) carried out a study focused on the internal audit department and fraud detection. The study was a biennial survey of fraud cases within Australia and New Zealand. 164 research instruments were sent to Australia and New Zealand's largest organizations and of these 45 % had experienced fraud. Results also gathered that of the 45% organizations that experienced fraud cases, 68 % reported internal audit works surfacing the fraud cases.

2.3 Knowledge Gap

The above research findings are based on large companies that are listed on the stock exchange and have wide coverage. However, the researcher is focusing on a relatively small growing company (Lifel) which is not listed on the stock exchange. The researcher also made his findings using mainly (Lifel) which differs from the previous above findings where various different large organizations were utilised to obtain results of a research topic.

2.4 Chapter Summary

This chapter aimed to identify and review evidence for specific costs and mainly benefits associated with the internal audit function found out by numerous other researchers and writers. The conclusions of the literature review provide a basis for ongoing empirical research

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter explains methods used to collect and analyse data from various sources, the rationale for using the methods, the merits and challenges of the research instruments used in the study. It will specifically dwell on the research design to be adopted, the population sample, sources and types of data, participants, research instruments and data collection and presentation procedure.

3.2 Research Design

Seutiz et al (1982:31) defined a design as, "a deliberately planned arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with the economy of procedure." Research design is a systematic and orderly approach which reflects how data was gathered in the most economical and feasible manner and includes measures adopted to safeguard the validity of the findings. According to Creswell 2012 a research design encompasses the methodology and procedure employed to conduct scientific research. The researcher relied on both primary and secondary data. Secondary data, largely obtained through literature review, was essential in establishing the background to the current problem and to perceive the current investigation in a wider content. A questionnaire and in depth interviews were primarily used for primary data collection. The researcher adopted a descriptive case study in order to establish the nature of existing condition in which this research sought to do and to come up with an accurate description of the costs and benefits of the audit department at Lifel Investments.

Justification of using the Descriptive Research Design

A descriptive research design enabled the researcher to collect comprehensive data and provide an accurate description of the situation from respondents using a variety of data collection methods. A descriptive research approach also enabled the researcher to conduct an in-depth study of the costs and benefits of the audit department at Lifel Investments. Due to the intensive nature of descriptive research, the researcher can collect valid and reliable data which is relevant to the topic understudy.

Disadvantages of Descriptive Research

The researcher found it difficult to cover many respondents. This posed as threats to the external validity to the research findings. Contrary, it was not enough to invalidate the findings because an appropriate sample was taken to represent the whole population.

3.3 Sources of Data

The researcher applied primary and secondary sources of data to conduct the study.

3.3.1 Primary Sources of Data

This refers to the original and raw data collected by the researcher of a project currently undertaken. Primary data is information gathered to address a specific issue or problem at hand (Leedy, 1997). This data is captured at point of origin for specific use. The primary data was used to complement secondary data already available. These sources provide direct description of the study by the individuals who actually carried out the research or observations. The following were employed to collect information from primary sources:

- Questionnaires
- Interviews

3.3.2 Secondary Data

Secondary data is information that already exists which had been collected for another purpose. They can be obtained from the internal records of the company and external sources such as government publications, newspapers, trade journals, store audits and annual reports. The researcher has used secondary sources of data from annual reports of Lifel Investments, monetary policy review statements, newsletters, business journals and internal articles.

Advantages of Secondary Data

Access time was short and less time was spent in collecting data as data was readily available. Information from such documents was already simplified and easily understood by the researcher. Data was generally cheaper to acquire and the data was collected from reputable sources which can easily be verified.

Disadvantages of Secondary Data

Some of the data was difficult to interpret due to technical jargon. Due to environmental changes some data was outdated and not specific to the problem at hand.

3.4 Target Population

Sullivan et al (1995:114) defined population as, “the total set of units in which the investigation is interested. The target population of this study was fifty (50) which members were randomly drawn from four major functional departments that are directly related to the auditing function namely; the audit department, the risk management department, the accountancy department and the finance and administration department at Lifel Investments.

3.5 Sampling Scope and Size

Green (2006) defined a sample as a number of individual cases selected from a large population. Cooper and Schindler (2003) describe sampling as the procedure by which some elements of a given population are selected as representative of the entire population. In statistics and survey methodology sampling is concerned with the selection of a subset of individuals from within a statistical population to estimate characteristics of the whole population. The sample size for this study was twenty-five (25) respondents drawn from four departments of Lifel Investments namely; Accounting, Finance and Administration, Risk and Auditing departments. Members to form part of the survey were randomly drawn from a total group of the target population using random selection of names that were contained in the departmental databases.

3.6 Sampling Technique

Hektner (2007) describes a sampling technique as the identification of a specific process by which entities of the samples have been selected. The researcher used a simple random sampling technique to select sampling elements within the accounting department, the audit department, the risk management department and finance and administration department at Lifel Investments. Simple random sampling was selected owing to its simplicity. The sampling technique enabled the researcher to make a generalisation about the entire population. Purposive sampling was used to select a representative sample for the structured interview.

3.7 Research Instruments

Research instruments are measurement guides designed to obtain data on a topic of interest from research. Tools used to gather information relevant to the research problem included questionnaires and interviews.

3.7.1 Questionnaire

Leedy (1993) regarded a questionnaire as the most widely used technique for collecting primary data. The researcher employed both closed and open-ended questions in the questionnaires. A standard questionnaire was designed to address the research objectives. One standard structured questionnaire was drafted for all the targeted respondents to ensure comparability of results. For closed questions the respondents were requested to tick the answer they thought was most appropriate. Suggested answers were provided to enable systematic analysis of data. However, open-ended questions were also used to seek details, which the researcher had little knowledge.

Advantages of a questionnaire

- Questionnaires facilitated contact with inaccessible respondents, incentives were used to increase response rate and allow the respondent's time to think about the questions.

- The use of questionnaires enabled easy analysis and evaluation of data or responses given as information is collected in a standardised way and straightforward to analyse.

- Rapid data collection was enhanced as structured questions made it simple and quick for respondents to complete.

- Questionnaires were more cost effective, less interviewer bias and respondents were more willing to answer sensitive issues which users may feel uncomfortable speaking to an interviewer about.

Disadvantages of using questionnaires

- There was no room for probing, since respondents were only addressing given questions.
- There was absence of non- verbal analysis, such as facial expressions.
- There was absence of verbal analysis such as changes in voice over time.

In order to overcome the drawbacks, the researcher made use of in depth interviews, to probe the respondents for lucid responses, to assess the facial expressions and also to analyze changes in voice overtime.

3.7.2 Quantitative Research Method

In this study quantitative research methods were used as a formal and systematic process in which numerical data was utilised to obtain information that involve counting and measuring events. Quantitative research method enabled the research to embrace a broad scope that enabled the collection of large amounts of data within a short space of time. Due to the high objectivity levels posed by quantitative research methods an independent researcher can replicate results. In this study the structured questionnaire was used as a major quantitative research method.

On the other hand, Best and Khan (1989) argue that quantitative research methods are based on the values of the researcher who designs the questionnaires. The use of structured questionnaires required respondents to choose from a specific selection of answers and do not allow for the respondents to qualify their answer or elaborate. Another shortcoming posed by the quantitative research method is that on some instances data did not reflect the true explanation of human behaviour within this natural context. The researcher resolved this anomaly through triangulating qualitative research methods as to get an in-depth understanding of issues underlying the costs and benefits of the internal audit department.

3.7.3 Qualitative Research Method

Qualitative research provided the researcher with an accurate description of a phenomenon since it uncovered emotions, perceptions and expectations of the topic of the costs and benefits of the internal audit department.

However, due to the subjective nature of qualitative research some responses given by the respondents were beyond the scope of his study. In order to guide the respondents from straying from the research objectives, the researcher took a clue from quantitative responses. Qualitative research also posed a challenge in that the researcher could not collate and measure responses from all respondents as such a selected group of respondents were used in order to collect qualitative data.

3.7.4 Interviews

These involve the collection of data through face-to-face question and answer sessions where the interviewer completes questions based on what the respondents say. Interviews were conducted to complement information gathered by the questionnaire. A set of questions was compelled and sent to the interviewee in advance after setting the interview date.

Advantages of using Personal Interviews

- Personal interviews facilitated easier communication by allowing flexibility in language.
- Interviews enabled the researcher to rephrase questions which appeared vague or where necessary.
- Interviews facilitated the use of follow up questions, probe for answers and the obtaining of more elaborate responses.

Disadvantages of using Personal Interviews

- It took longer periods of time to gather data from interviews as the interviewer had to interview a single respondent at a time and allowing probing of questions and clarifications.
- Not all respondents were present during the research period. Three respondents from the risk management department were not available at the time of interviewing.

3.8 Reliability and Validity

In this study the use of questionnaire method enabled respondent's time to interpret the questionnaires hence giving quality and accurate data. Campbell, (1979) define validity as the extent to which data collection method accurately measure what they were intend to measure. Personal interviews helped in avoiding distortion of data while an optimal number of questions were crafted into the questionnaires to cross validate data obtained. The researcher endeavoured to ensure reliability of research results through the use of structured questions in the questionnaire method which comprised of open and closed ended questions. The use of structured questions enabled an independent researcher to come up with similar results.. Bell (2003) define reliability as the degree to which data collection methods will yield consistent findings, similar observations would be made or conclusions reached by other researchers or there is transparency in how sense was made out of the raw data.

3.9 Research ethics

The researcher managed to demonstrate ethical considerations by the use of an informed consent and describing objectives of the study as well as stressing anonymity and confidentiality to the respondents upon distribution of the questionnaire and conducting of the interviews. The researcher ensured voluntary participation, she made sure that no responded was coerced into participation. The researcher also ensured honesty, objectivity and respect for intellectual property throughout the research process.

3.10 Data Collection Procedure

Data collection procedure refers to a plan that clearly lay down rules and procedures which enable the researcher to do the study and come up with the desired results (Oppenheim, (1992).

The approach to information gathering was two tired; involving a self-administered questionnaire survey targeted at Lifel five different departments. The researcher personally administered the questionnaires to the respondents. The justification for physically distributing questionnaires was to enable the researcher to have directed contact with respondents and able to give explanations to the questions were necessary An appointment date and time was set for the collection of the questionnaires in order to lessen the burden on the respondents of getting hold of the researcher upon completion of the filling in of the questionnaires. This also ensured that the questionnaire falls into the hands of the intended respondents. The researcher gave the respondents a fortnight to complete the questionnaires. Completed questionnaires were physically collected by the researcher from the respondents. In addition the research consortium conducted interviews with the members of the organisation who took part in the questionnaire. Disparities were then sought and presented, alongside examples of general evidence gathered from empirical findings. The reports of interviews were used to supplement the information obtained from the questionnaire, particularly on the contributions and benefits associated with the internal audit function and to provide further detailed breakdown of specific cost and benefit areas.

3.11 Pilot Study

A pilot questionnaire was disbursed prior to the final questionnaire. A pilot study is a small scale preliminary study contacted before the main research in order to check the feasibility or to improve the design of the research. The researcher had to distribute nine (9) sample questionnaires to three different individuals from each of the Public Relations, Marketing and Sales Departments of Lifel Investments in order to ascertain the validity of the research. Out of the nine (9) individuals who were asked to assist in the attempting of the pilot questionnaire, six (6) respondents attempted and returned the questionnaire thus giving the researcher a reliable basis to ascertain how effective the questionnaire was for the purpose of the research. None of the respondents advocated for clarification on any of the questions and all questions were respondent to in a satisfactory attempt hence giving the researcher assurance that the research instrument was well designed and feasible.

3.12 Data Presentation and Analysis

Data was presented using the various findings from the questionnaires, interviews and secondary sources of data. Presentations were in the form of graphs, frequencies, percentages and pie charts. The findings were recorded in quantitative form necessitated by the capturing of figures. Data analysis is the reduction of accumulated data to a manageable size by developing summaries, looking for patterns and applying statistical techniques. The researcher employed both qualitative and quantitative methods to analyse the data. It is through data analysis that some conclusions were drawn.

3.13 Chapter Summary

This chapter outlined the research methods employed in the research, the target population, the research techniques used and the merits and drawbacks of these research methods. The analysis and interpretation of the various data collected will be done in next chapter.

CHAPTER FOUR

DATA PRESENTATION, INTERPRETATION AND ANALYSIS

4.1 Introduction

This chapter provides the presentation, evaluation and interpretation of data findings in relation to the theory underlying the study. Findings obtained through self-administered questionnaires and interviews are used in the evaluation of data, linking them to those of literature review and research objectives. The researcher made use of the interview and circulated self-administered questionnaires (see appendix 1 for questionnaire and 2 for interview guide) as the source of data referred to in this chapter.

4.2 Questionnaire Response Rate

The survey comprised of twenty five respondents which were drawn from four departments of Lifel Investments. Twenty-three responses were returned making a response rate of 88%. Such a high response rate indicated that the respondents contributed much to the gathering of information by the researcher.

Table 4.1: Survey Response Rate

Detail	**Number of Responses**	**Percentage of Responses**
Number of questionnaires dispatched	25	100
Replies Received	22	88
Usable Replies	22	88
Final Response Rate	22	88

Table 4.2: Departmental Response Rate Table

Department	**Response Rate**
Internal Auditing	100
Finance and Administration	100
Accounting	100
Risk Management	88
Overall Response	88

Out of the 25 respondents, 22 respondents attempted the questionnaire and were also present for interviewing. Three of the respondents from the risk management department, reasons unknown to the researcher, did not return the questionnaire nor were they present for the interviews.

4.2.1 Effective Sample Rate

Population (N)

Effective Sample (n)

Effective Sample Rate = (n/N %)

= 22/50

= 44%

Out of the 50 employees of Lifel Investments, only 25 employees, from four different departments, were selected for the research purpose. Among the 25 to whom questionnaires were distributed, 22 attempted the questions and returned the responses hence resulting in an effective sample rate of 44 %.

4.3 Benefits of the Internal Audit Department

Respondents were asked to identify benefits of an internal audit department. The results are highlighted in figure 4.3 below. Chief among them was improvement in internal controls. Fifty two percent 52% of the respondents agreed that the department results in an improvement in internal controls, twenty-four percent 24% agreed that they would be a reduction in the risk of misstatements (fraud and errors), fifteen percent 15% agreed that such a department will lead to a reduction in external audit fees and only six percent 6% of the respondents agreed the presents of an internal audit department could lead to an improvement in investor confidence whilst five percent 5% believed in a reduction in the cost of capital. Findings from the study carried out by Holt and Dezoort (2009) which indicate that the disclosure of an Internal Audit Report increase investor confidence and likelihood of the investor to purchase the company's stock.

Table 4.3: Benefits of an Internal Audit Department

Benefit	% of Approving Respondents
A. Improvement in internal controls	52
B. Reduced risk of financial misstatements	24
C. Reduction in external audit fees	15
D. Reduction in cost of capital	5
E. Reduction in investor confidence	6

Raw Data

The above results are illustrated diagrammatically below (Figure 4.1)

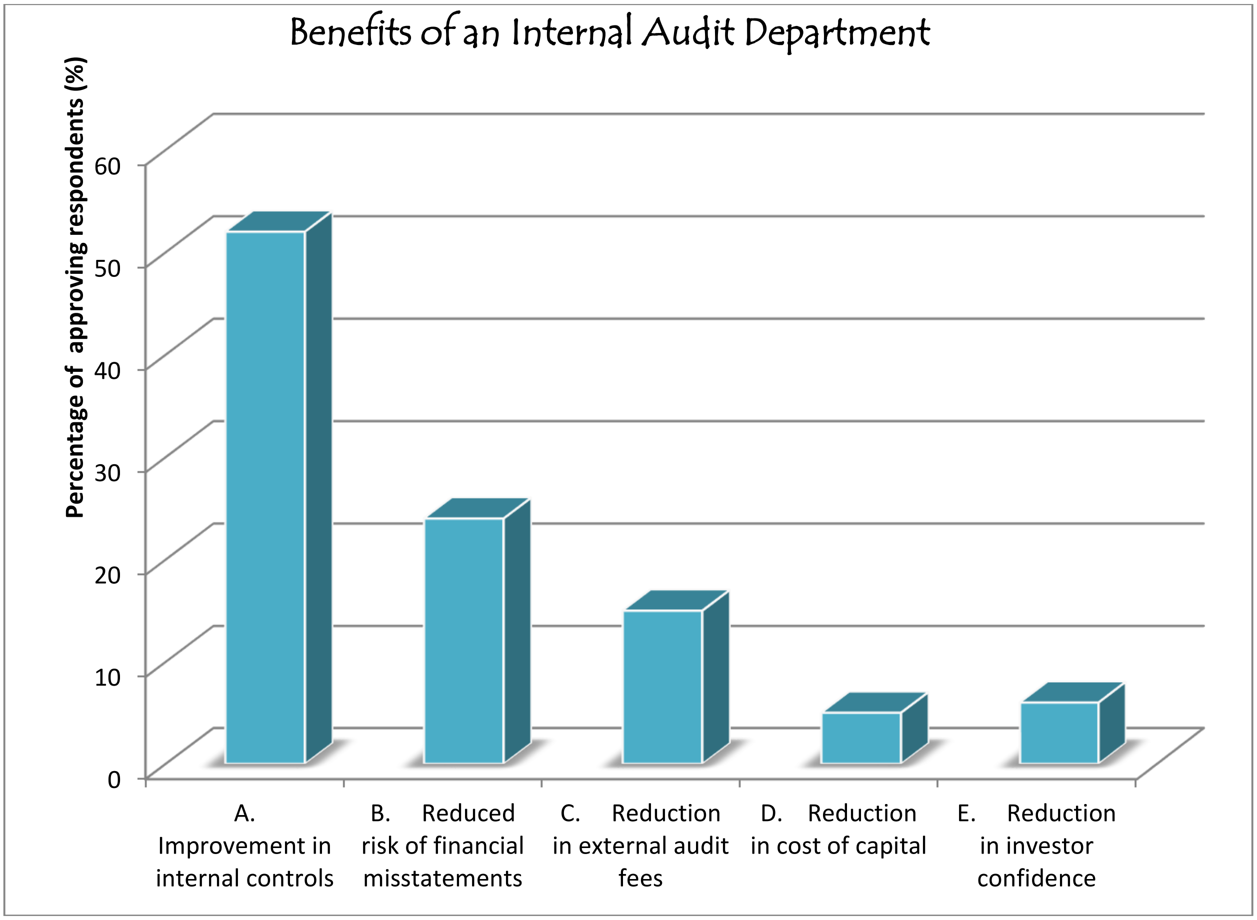

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Figure 4.1: Benefits of an Internal Audit Department

4.3.1 Internal Auditing in Improving Internal Control System

Research carried out gave that the major benefit in internal auditing is the improvement in internal controls which in turn result in improved investor confidence, reduction in misstatements and reduction in external audit fees. These broader social benefits are inherently difficult to quantify. A majority of the respondents revealed that the internal control system was now strong since the adoption of an internal audit department at Lifel. This is also elaborated by the Institute of Internal Auditors (2006) which reflects that the internal auditing has a significant impact on internal control system, the efficient management of firm's resources and the means of safeguarding assets.

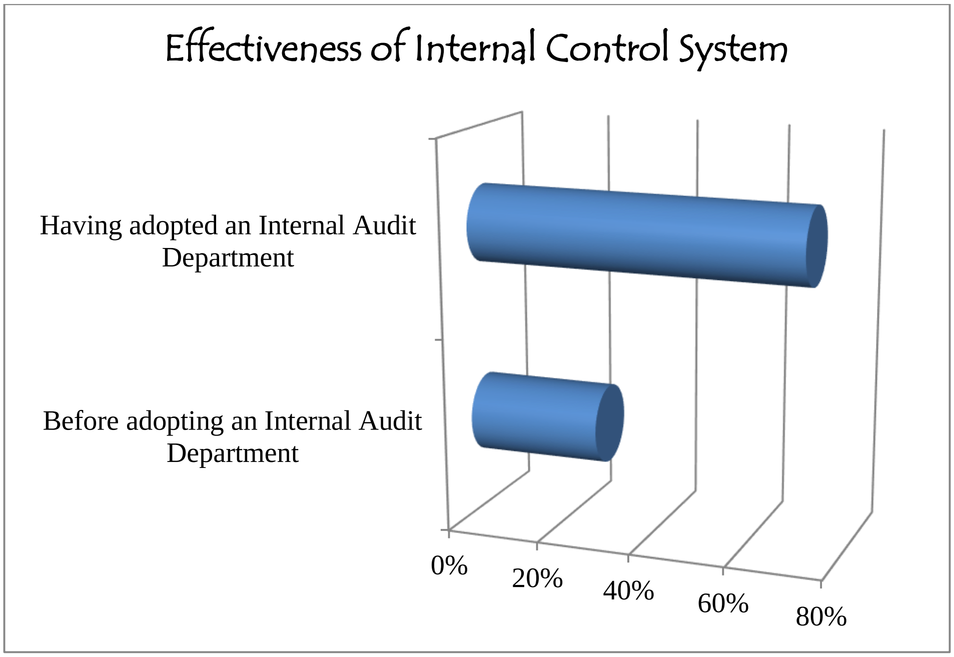

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Figure 4.2: Internal Auditing and Internal Control Effectiveness

A critical examination of the responses given clearly shows that in the absence of the internal audit department internal controls are weak. It may be inferred that the internal audit department improved the internal control system at Lifel Investments. Professionals in accounting argued that a company with a good reputation for widespread accounting irregularities would necessitate a higher cost of capital when they are seeking equity financing. Reducing the perceived probability of such irregularities should tend to reduce the cost of capital. Quantification of benefits constitutes provision of quality information for managerial decisions in achieving organizational objectives. Based on the interviews it has also been proven that prudent managerial decisions are as a result of better internal controls.

However, internal controls can provide only a reasonable and not an absolute assurance that the objectives of an organization will be met. Additionally, the concept of reasonable assurance only implies a high degree of assurance constrained by the costs and benefits of establishment increment costs.

4.3.2 Internal Audit and Risk

The diagram below is an illustration of the effectiveness of an internal audit department in minimising risks. (Fig 4.2)

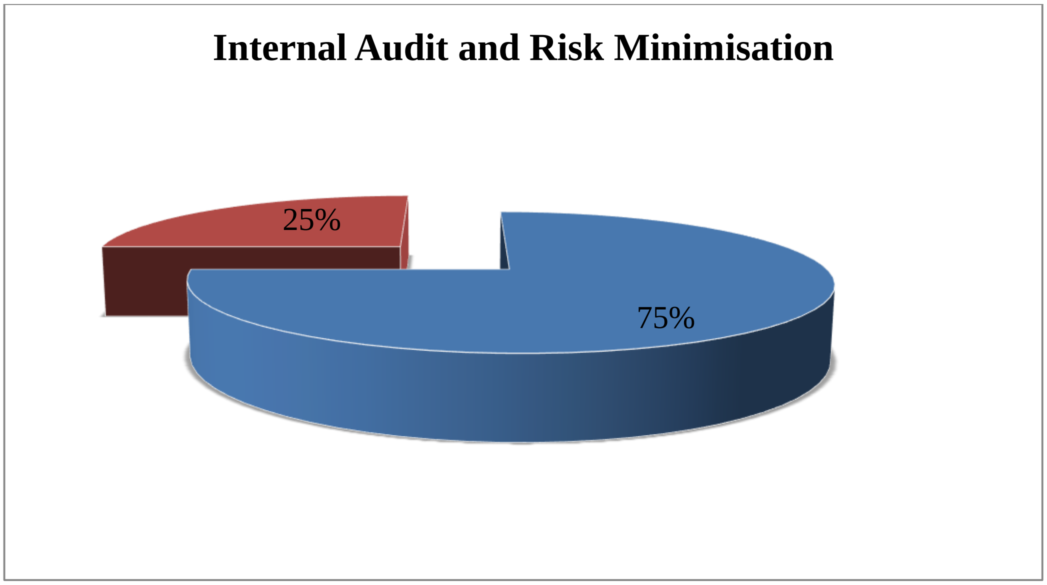

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Figure 4.3: Internal Audit and Risk Minimisation

75 percent of the respondents were of the view that an effective internal audit department reduces information risks due to reliable and credible information for management decision making which form part of good governance principles. Respondents agreed that internal audits ensure systems and processes that support the identification, capture and exchange of information in a form and time frame that enable organizational arms to effectively carry out their responsibilities. Also the relevant identification of risks enables the organization to counter plan on how to manage the risks thereby sustaining the organization. The assertion agrees with the findings carried out at Harley Davidson by Goodwin and Yeo (2001) which gave that internal audits play a role in creating necessary corporate governance principles which ensure that risk management and internal control processes are followed and applied effectively in an organization.

However, identification of risk does not necessarily guarantee the success of an organization. There is need for rich and applicable counter solutions to guarantee success. Unavailability of funds, human capital knowhow for effective decisions and also other external or even internal factors beyond the organizations' control can limit the deterrence of the risk brought out.

4.3.3 Reduction in Costs of External Auditing

The pie chart below shows respondents views on the cost reduction as a result of setting up an internal audit department. (Fig 4.3)

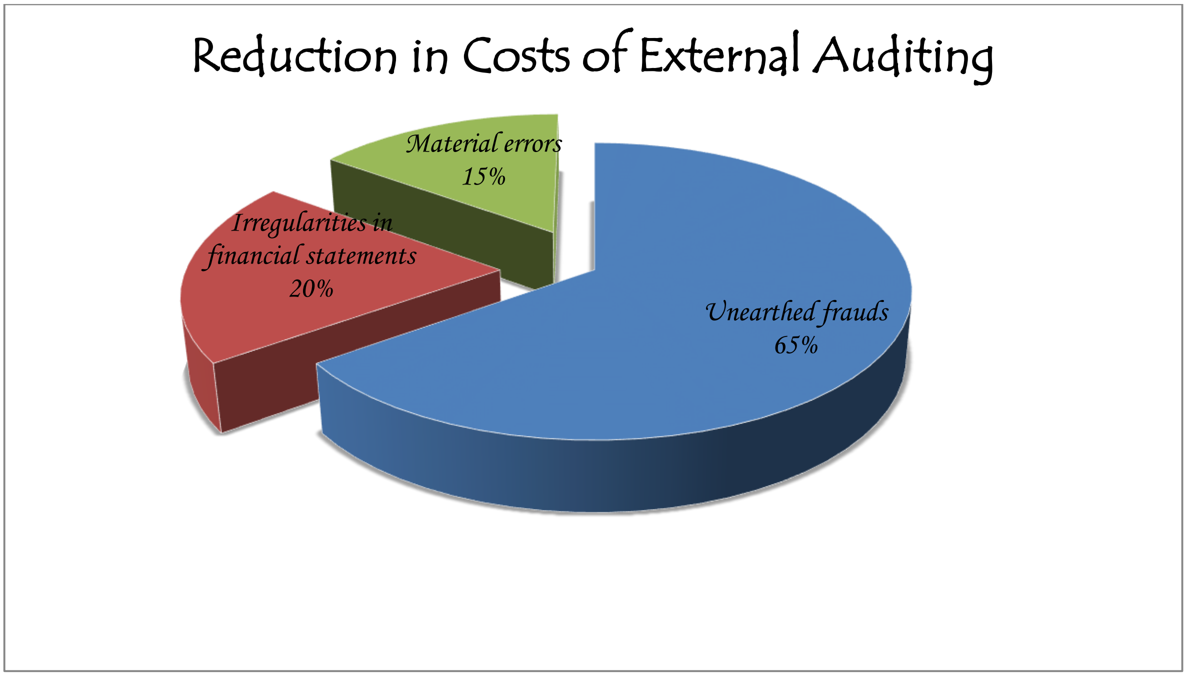

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Figure 4.2: Reduction in Costs of External Auditing

Respondents highlighted that their costs of external audit fees have been reduced owing to the effective work by the internal audits which led to external auditors relying on the work of the internal auditors. The results go hand in hand with findings from the research carried out by KPMG (2005) which elaborated that the cooperation between external and internal auditors acts as advisory capacity in the operation of an internal audit department and also the internal auditors knowledge of the entity will be of assistance to the external auditors work thus reducing the level of duplication efforts and hence a reduction in external audit fee.

However, the establishment of an internal audit department does not necessarily result in reduction in audit fees. External auditors may choose to place limited reliance on the work of the internal auditors. More so, if the external auditors perceive the internal audit department as not competent enough they will not rely on the work of the internal auditors hence the audit work carried out will still be the same thus no reduction will result in the external audit fee.

4.3.4 Can benefits outweigh the Costs

The majority of the respondents (81%) believed that the benefits derived from an internal audit department outweigh costs. A total of 19% of the respondents however were of the view that the costs outweigh benefits (Figure 4.4)

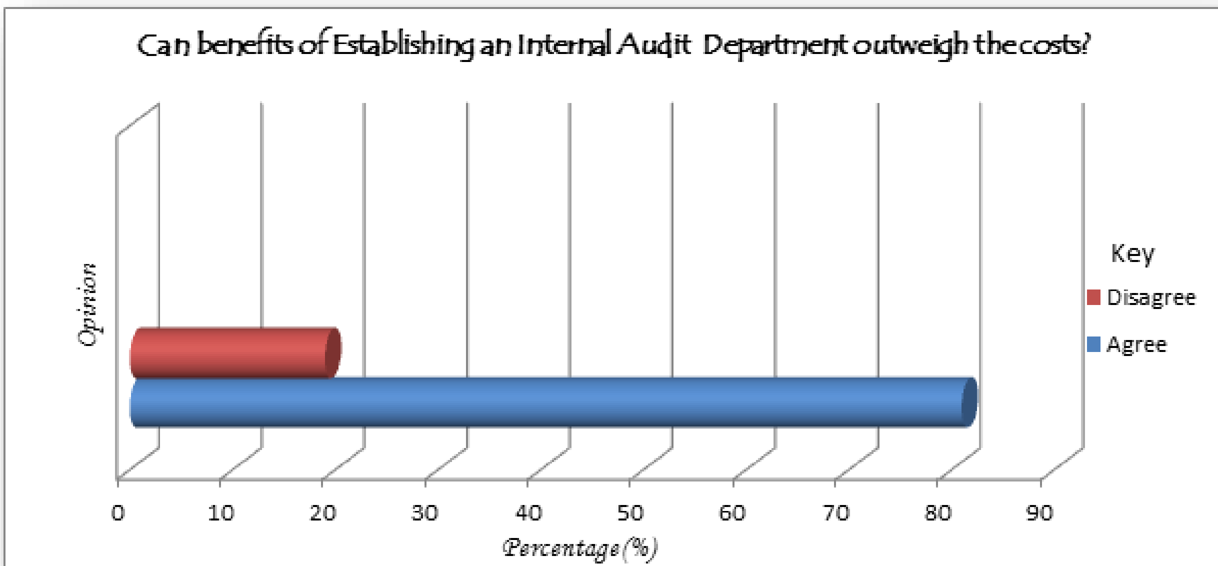

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Figure 4.3: Can benefits of an Internal Audit Department outweigh its costs?

Findings obtained from the majority of the professional expects interviewed in the study carried by Salem and McNamee (2009), based on five companies listed on the stock exchange gave that the benefits of establishing an internal audit department within the organization outweighs the costs.

4.3.5 Reduction in Misstatement

Respondents concurred that the internal audit department has uncovered some irregularities in financial statements and material errors in the organisation. During the years between 2009 and 2010 a thousands of dollars were saved owing to the unearthing of fraud and errors by the internal audit department.

Sixty five percent (65%) of the respondents generally agreed with the notion that an internal audit department will result in reduced incidences of misstatements in organizations financial reports, improvement in the quality of financial disclosure resulting in better corporate governance. Thirty five percent (35%) however viewed that the reduction of misstatements in financial information lies within the company policies and management attitude towards the maintenance of internal controls. The diagram below shows the views of respondents on the reduction of misstatements as a result of setting up an internal audit department.(Fig 4.5)

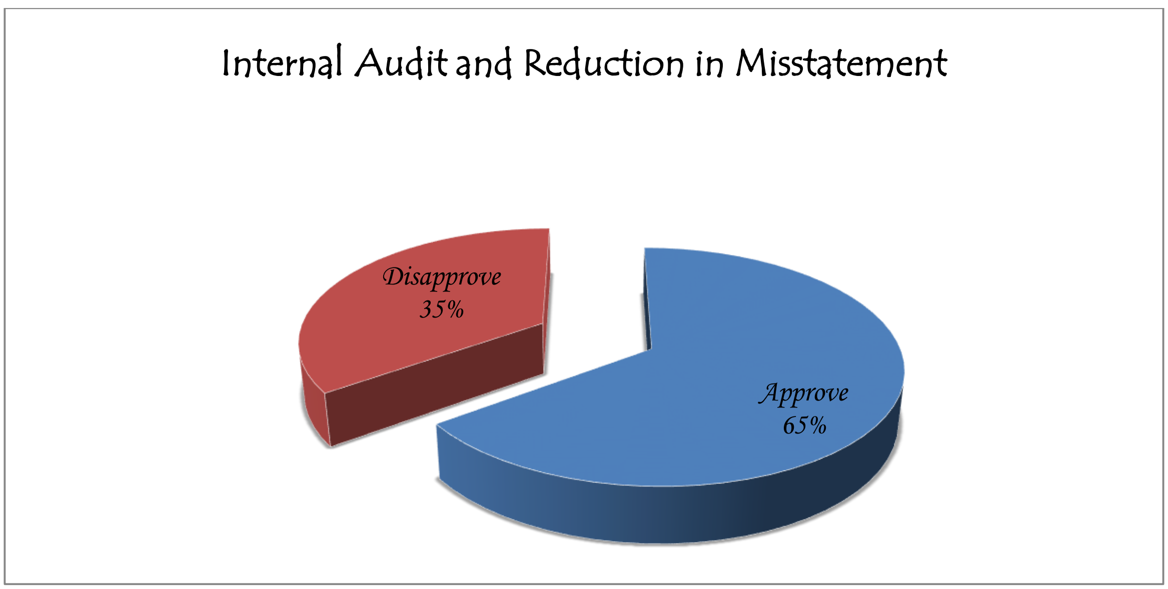

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Figure 4.4: Internal Audit and Reduction in Misstatements

Most Respondents viewed the internal audit department as an objective independent examination of financial statements that increase the value and credibility of financial statements produced by management thus increasing user confidence, reduced investors risk and consequently reduces the cost of capital of the financial statements preparer. Findings from the research support the study carried out by Brown and Pinello (2007) on companies listed on Canada' Stock Exchange which gave evidence of 66 % of the participating companies reflecting the reliability of the internal auditing department in detecting financial misstatements.

However, the audit opinion, after verification of the financial statements by the internal audit department, is intended to provide only a reasonable assurance that the financial statements are presented fairly in all material aspects.

4.3.6 Corporate Fraud

45 percent of respondents said the lack of effective and efficient internal audit is a cause of corporate scandals. 35 percent were of the view that the internal audit department cannot be blamed for failing to curb corporate scandals. In most cases, corporate scandals are carefully planned by management and are a result of collusion between employees hence difficult to unearth. 20 percent of the respondents were indifferent and not sure whether internal auditors can be blamed for failing to unearth corporate scandals.

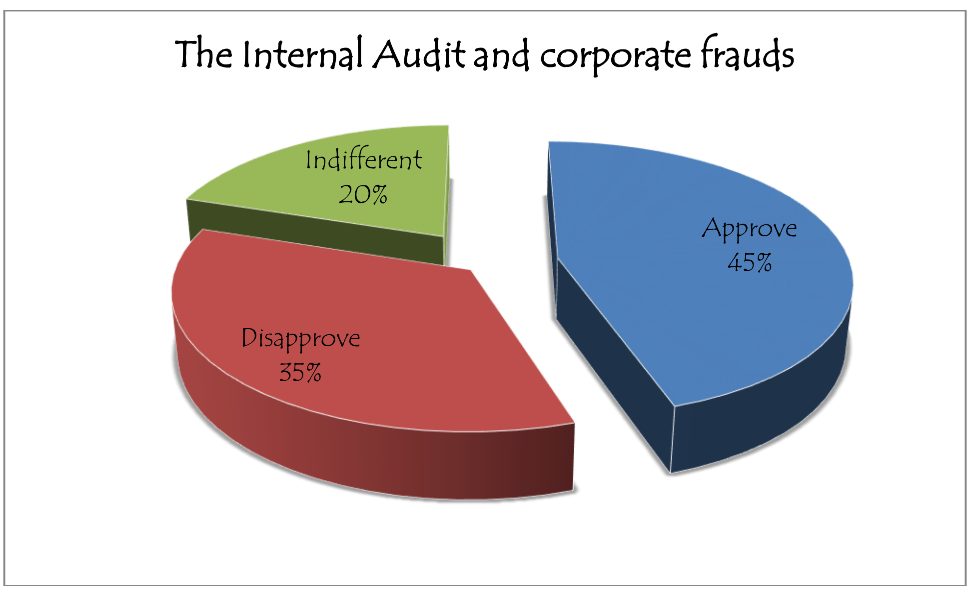

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Figure 4.5: The Internal Audit and Corporate Frauds

Most respondents however approved that the internal audit department plays a pivotal role in detection and curbing of corporate frauds. Findings from the KPMG (2004) study on the value of the internal audit function in fraud detection also reported 67.5% of fraud cases detected in Australia and New Zealand large firms owing to internal audit works.

However, control processes manage the risk of fraud up to an acceptable level. The risk that senior management override important financial controls to manipulate financial reports is a key drawback to fraud deterrence and fraud risk management.

4.3.7 The level of Liaison

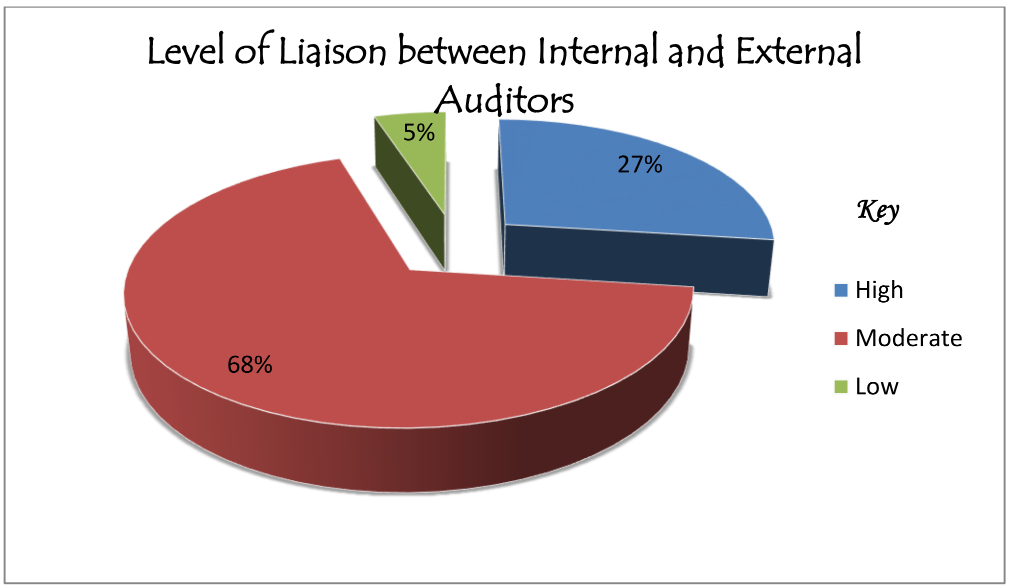

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Figure 4.6: The Level of Liaison between Internal and External Auditors

When asked to comment on the level of liaison between internal and external auditors, 68 percent said that the internal and external auditors liaise moderately. 27 percent indicated that the level of liaison is high whilst the other 5 percent gave to it that the level of liaison is very low. The above findings indicate that there is no much liaison between the internal and the external auditors. This increases the risk of not identifying potential significant operational risks affecting the entities' and increase external audit fees. Research carried out by KPMG (2005) elaborated that the cooperation between the internal and external auditors is of advisory capacity in the operation of an internal audit department as well as a tool to avoid duplication of effort as external auditors carry out their work.

A good relationship between the internal and external auditors will ensure that appropriate work has been carried out in each area of the audit thus minimising audit risk. The external auditor should not rely entirely on the internal auditors work. Basically the external auditor should check the internal auditors work by performing test checks. If the external auditor tests show similar results to those of the internal auditors' then the external auditor can check fewer items, thus resulting in a saving in external audit work and time and hence reduced external audit fee.

4.4 Benefits and costs in relation to size

Respondents were of the views that as the organization expand its operations; benefits of establishing an internal audit department will increase up to a point when there will no longer be any additional benefits no matter how further the organization will continue to expand. At the same time, if the organization continues to expand, the average cost of establishing an internal audit department in relation to the size of the organization is more likely to decrease. The organization will be said to be at equilibrium size (where benefits are equal to costs) and thus it will be of an indifferent opinion on whether to outsource or to establish an internal audit department from within the organization; at this point benefits are equal to costs, any size greater than the equilibrium size benefits will outweigh costs. Refer Figure 4.8 below

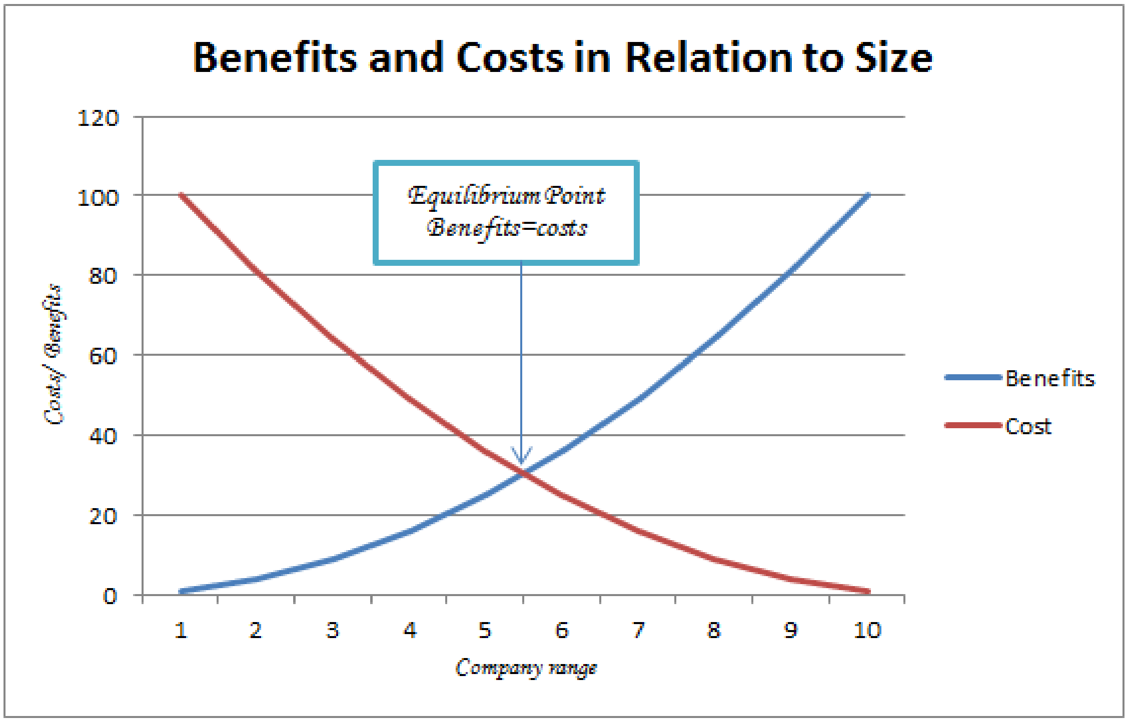

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Figure 4.7: Benefits and Size in Relation to Size

According to the diagram above, organizations falling in the range of 1-5 are relatively small firms and do not enjoy benefits from establishing an Internal Audit Department-the costs are more likely to outweigh the benefits. The equilibrium size is at 5.5 where costs are equal to benefits. Any size above 5.5 the company would benefit from establishing the department as costs will be lower than benefits. The assertion concur with Sarens and De Beelde (2006) which provided that financial costs of internal audit vary based on the size of the organization and the goal of the internal audit department and internal costs based upon the resources used to perform the work. The size of an organization can be measured in terms of assets or turnover; however the researcher was not able to come up with figures on what size can be said to the small, equilibrium or large.

4.4.1 Benefits of Outsourcing or Co-sourcing in relation to size

Respondents were of the view that benefits of setting up an internal audit department or outsourcing depends on the size of the firm. 70 percent of the respondents were of the opinion that the cost of establishing the internal audit department for a relatively small organization outweighs the benefits but as the organization expands in operations and increase its market share the benefits would outweigh the costs as a result of economies of scale. 30 percent of the respondents were of the view that the benefits of the internal audit department are enjoyed when the firm is still small as it will be manageable more efficiently than a large organization. The results concur with the research carried out using 99 companies listed on the Australian Stock Exchange which gave that the larger the organisation, the greater the propensity to outsource. Results also suggested that internal audit outsourcing is associated with perceived cost savings and the technical competence of the external audit provider.

4.4.2 Cost of Implementation

70 percent of the respondents said most of internal audit recommendations are not implemented. They said most of the recommendations are discussed with management and documented but are never implemented and whenever internal auditors carry follow ups and write reports to the top management about the non-compliance of their recommendations nothing is done to implement them, resulting in the increase in operational costs and pilferage of materials and assets. Respondents highlighted that given such a scenario, the establishment of an audit department is an unnecessary cost that should be avoided. 30 percent said their recommendations do get implemented. Refer to figure 4.9 below

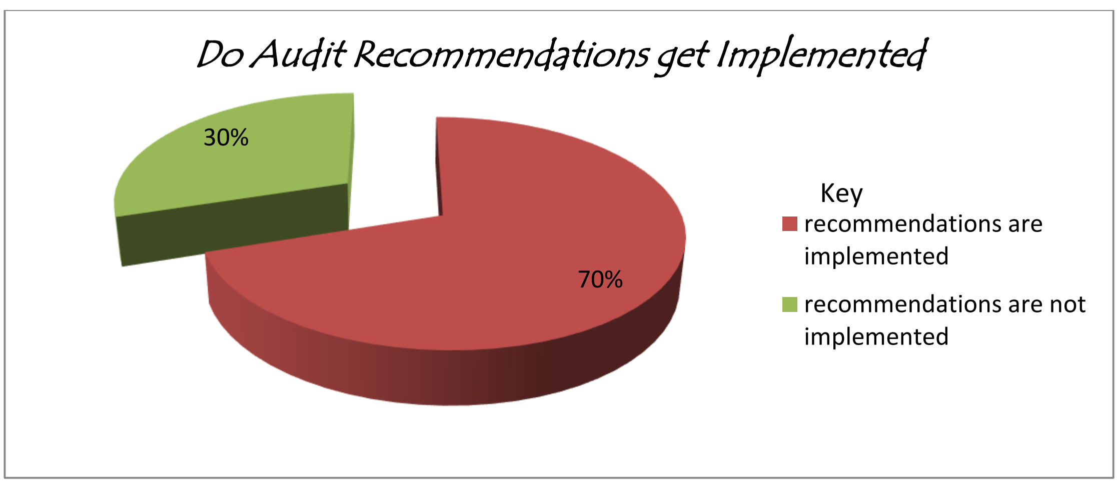

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Figure 4.8: Implementation of Audit Recommendations

The study carried out by Spira and Page (2003) on blue chip companies' management teams trading on the New York Stock Exchange, however, gave that the value given to internal audit by management has increased hence an improved possibility that the audit recommendations will get implemented.

4.5 Chapter Summary

The primary goal of this evaluation was to determine whether the benefits of an internal audit department exceed costs. The researcher did not determine the exact value of any net benefits as costs or benefits are difficult to measure quantitatively. To reach an opinion regarding the effect of reduced misstatements based on the presence of an internal audit may prove to be a difficult decision department because the benefits derived are indirect and intangible while some costs incurred for the establishment and maintenance of such a department are also indirect. No interviewee was willing to estimate or provide quantitative information on benefits and costs although they generally agreed that benefits outweigh costs.

Regardless of the researcher failing to come up with quantifiable costs and benefits resulting from the establishment of an internal audit department the conclusion derived is that the benefit of having an audit function outweighs the costs. The research is mainly subjective rather than objective.

CHAPTER FIVE

SUMMARY, MAJOR FINDINGS AND RECOMMENDATIONS

5.1 Introduction

This chapter seeks to give a concluding summary, major findings and recommendations to the research study. The findings and recommendations were based on the information gathered

5.2 Summary of Findings

- The use or adoption of an internal audit department strengthens internal controls, reduces the risk of misstatements (fraud and errors), a reduction in external audit fees, an improvement in investor confidence as well as a reduction in the cost of capital.

- The presence of internal auditors will reduce control risk as audit tests will detect weaknesses in the accounting systems and implementation of recommendations will improve controls and result in reduced risk of fraud and error.

- Internal controls can be used to systematically improve business in terms of effectiveness and efficiency.

- Most of internal auditors' recommendations are not getting implemented as a result of top management failing to give the internal audit department much appreciation and consideration.

- Lack of an effective and efficient internal audit results in high occurrences of corporate scandals. The internal auditing at Lifel Investments is fulfilling its role of fraud prevention.

- The costs of establishing an internal audit department when a firm is still small outweighs the benefits but as the organization grows and expands in operation, size and market share, the benefits outweighs the costs as a result of economies of scale. It was deduced that as an organization continue to expand, benefits of establishing an internal audit department will increase up to an optimum point beyond which there are no additional benefits regardless the size of the organization.

- The internal audit department at Lifel has resulted in the uncovering of some material errors as well as irregularities in the organizations' financial statements.

- Establishment of an internal audit department does not necessarily result in audit fee reduction but will depend on whether the external auditors perceive the work of the internal audit department as competent.

- It was established from the study that the internal audit department will result in reduced occurrences of misstatements in organizations' financial reports and thus an improvement in the quality of financial disclosure resulting in better corporate governance.

5.3 Conclusions

Basing on the findings the research conclude that

- Generally, the benefits of establishing an internal audit department outweigh the costs

- The establishment of an internal audit department will result in improvement in internal controls.

- Implementation of internal auditor's recommendations will reduce operation costs and pilferage of material and assets.

- The costs of establishing an internal audit department when a firm is still small outweighs the benefits but as the organization expand in operation and size the benefits outweighs the costs as a result of economies of scale.

- The internal audit department minimise costs by improving internal controls, reducing the risk of misstatements, reducing the cost of capital and external audit fees and an improvement in investor confidence.

- Control provide only timely information or feedback on progress towards achievement of operational and strategic objectives but cannot guarantee achievement

- Whether an organisation achieve operational or strategic objectives may depend on factors outside the enterprise i.e. technology innovation and competition

- Lack of an effective internal audit department increases or result in no reduction in external audit fees

- An internal audit department will improve management performance in decision making due to reliable information.

- Not all audited financial statements reflect a true and fair view of a firm's operations but however the possibility of financial misstatements is greatly reduced.

- Internal auditing play a crucial role in preventing and detecting fraud and protecting the organization's resources.

5.4 Recommendations

- Due to strenuous budgets and limited funds, the internal audit department at Lifel Investments has to focus more on offering suggestions that include re evaluating underutilized existing systems within the organization which may increase business efficiency without necessarily leading to additional high costs because some recommendations are not implemented due to costs considerations which might not meet the financial status.

- Lifel Investments should carry out vulnerability analysis involving all departments across various functions of the organization. The internal audit should identify high risk areas that are more prone to loopholes and fraud eminences and put much concentration on them in order to detect and deter fraud. As a result, they are often in a position to identify deteriorating control situations before major loss to the organization occurs.

- Due to the complex nature of the manufacturing business, Lifel Investments should consider co-sourcing the internal audit department, which confers the advantages of outsourcing while keeping the effective parts of the in-house function. The in-house department is well versed with the processes involved in the operation of the business and thus can identify errors quickly and in time whilst the external providers will bring expertise and ideas that the in-house function might be missing or overriding

- For benefits of Lifel Investments audit function to outweigh the costs, it is recommended that the department should take a more proactive approach to tackling fraud and reducing financial misstatements by efficiently utilizing the forensic accounting expertise at its disposal. The internal audit department of Lifel Investments should place greater emphasis on the prevention procedures of fraud occurrences and financial misstatements rather than against detection, investigation and prosecution after a fraud has occurred.

- A whistle blowing policy must be put in place to enhance the efforts of the internal audit function. This can be achieved by putting up an independent fraud management committee which reports to the audit committee. More so, Lifel Investments should consider the use of an experienced outside agency managing the whistle-blower hotline to enhance the perception of confidentiality.

- Staff education on the role and significance of internal audit department must be done to both management and staff employees to enable them appreciate the significance of an internal audit department within the organization. Proper awareness on the risk of weak internal controls and fraud consequences among other sentiments need to be conducted to increase the acceptance of an internal audit department within the organization.

5.5 Implications for further studies

Future researches should be conducted on the effectiveness of forensic accounting in curbing financial statements fraud in Zimbabwe's local authorities in order to establish a model for Zimbabwe's local authorities.

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Appendix 1: Questionnaire

I am a student at Bindura University of Science Education, Registration number B1025605, studying a Bachelor of Commerce (Honours) Degree in Financial Intelligence. I am kindly requesting for your assistance and co-operation in answering the following questions for the purpose of my research study that seek to evaluate the Costs and benefits of an Internal Audit Department. I would like to assure you that opinions you are going to express will be handled in strict confidence and will solely be used for academic purpose. Please feel free to express your true and honest opinions on the issues raised.

1. Which of the following do you think is a benefit of the internal audit department? (Yes or No)

Benefit	Response
Reduced risk of misstatements and external audit fees	
Improvement in internal controls	
Reduction in the cost of capital	
Improved investor confidence	

P.S: Tick in the suggested box for questions (2-6)

2. Is the internal audit department proving to be of significance in improving internal controls?

(Tick in the suggested box)

Yes ☐ No ☐

3. Can the benefits of the internal audit department outweigh the costs?

Yes ☐ No ☐

4. Of late, where there any cases of fraud detected by the internal audit?

Yes ☐ No ☐

i. If yes, how many were they and briefly explain how there were detected

....

5. Has the existence of an internal audit department showed a decrease in external audit fees?

Yes ☐ No ☐

6. As the line of business expands what do you view best for Lifel Investments?

Set up an internal audit department ☐

Outsource the audit function ☐

7. What are your views on the costs and benefits of the internal audit function as an organisation grows?

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....
....
....

8. What are your views on the level of interaction between Internal and External Auditors?

High ☐ Moderate ☐ Low ☐

9. Outline the major costs of setting up an internal audit department.

a)

b)

c)

d)

10. Outline the major benefits of setting up an internal audit department

a)

b)

c)

d)

12. What is your opinion on the costs and benefits of the internal audit function as the organization expands in size and operation?

....

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13. Should an organization rely on its own permanent employees for audit services or should it consider outsourcing? Tick the suggested opinion

Rely on its own permanent employees ☐

Outsource ☐

Appendix 2: The Interview Guide

1. What are your views on the costs and benefits of an Internal Audit Department?
2. Given the volatile technological environment are the internal auditors coping up with the latest developments in the industry?
3. How do you determine the performance of internal auditors in your organization?
4. What can you say on the effectiveness of internal auditing on curbing fraud and misstatements?
5. Apart from detecting fraud and financial misstatements what other role has the internal audit played in the organization?
6. To what extent can be an unintentional error due to misstatement or weaknesses in a company's internal control system and an intentional error due to fraud be justifiable?
7. What measures have you put in place to safeguard financial information from unauthorized manipulation?
8. Can you comment on the relationship between on the relationship between the internal and the external auditor
9. To what extent is the issue of auditor independence relevant in internal auditing given that the audit team will be members from within the organisation?
10. How do you control your database?
11. Is it always that audited financial statements reflect a true and fair view of the firm's operations?