

Internal Audit (ACCT 337)

Chapter 5 Business Processes and Risks

Definition of Business Process

Business Process: The set of connected activities linked with each other for the purpose of achieving a business objective.

Example:

- Objective: Getting to 8:30 am class tomorrow on time.
- What do you need to do to achieve this objective.

Types of Business Processes

1. Operating Processes:

- Core processes through which the organization achieves its primary objectives
- Examples: design product / market and sell/ produce the product / deliver the product / invoice and collect

2. Management and Support Processes:

- To oversee and support the organization operating processes
- Examples: HR/ finance/IT/external relationships

3. Projects:

- To structure nonroutine activities to create assets for the organization use
- Example: selection and implementation of new accounting software

Levels of Process Depiction

High Level Perspective?

Detailed (Low) Level Perspective?

Business Process - IAs

A1: Understanding Business Processes

- Understand the organization Business Model (objectives and business processes)
- 2 approaches that help in understanding business processes:
 1. Top Down Approach
 - Organization level with the organization objectives
 - Identify **key processes** critical to the success of these objectives
 2. Bottom Up Approach
 - Looking at all processes at the activity levels (people responsible for actual activities)
 - Identified processes are then aggregated
 - Works well for smaller organization with limited number of processes

Business Process - IAs

A1: Understanding Business Processes

- Once the process is identified (Top Down/Bottom Up), determine the key objectives of the process.
 - Process Owner
 - Existing policy and procedure documentation for the process
- IA should understand the following 4 areas of the business process:
 1. Inputs to the process
 2. Process activities
 3. Process outputs
 4. KPIs: a metric or a measurement to determine if the process is performing as intended.

Business Process - IAs

A2: Documenting Business Processes

- Process owner:
 - Orienting new employees.
 - Defining areas of responsibility
 - Evaluating the efficiency of the process
 - Identifying key risks and controls
 - Not to lose or distort the process
- Internal auditors:
 - Must documents their understanding of the process?

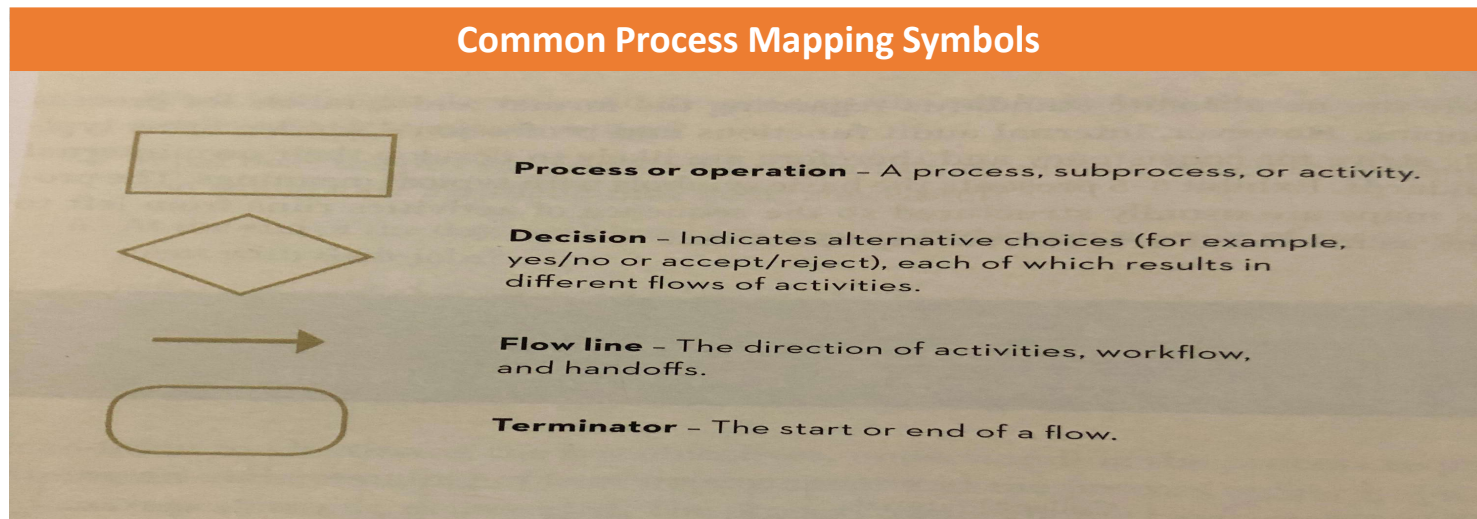
Business Process - IAs

A2: Documenting Business Processes

- 2 methods for documenting business processes:
 1. Process Maps:
 - Pictorial representation of the process using standard symbols (see next slides)
 2. Process Narratives

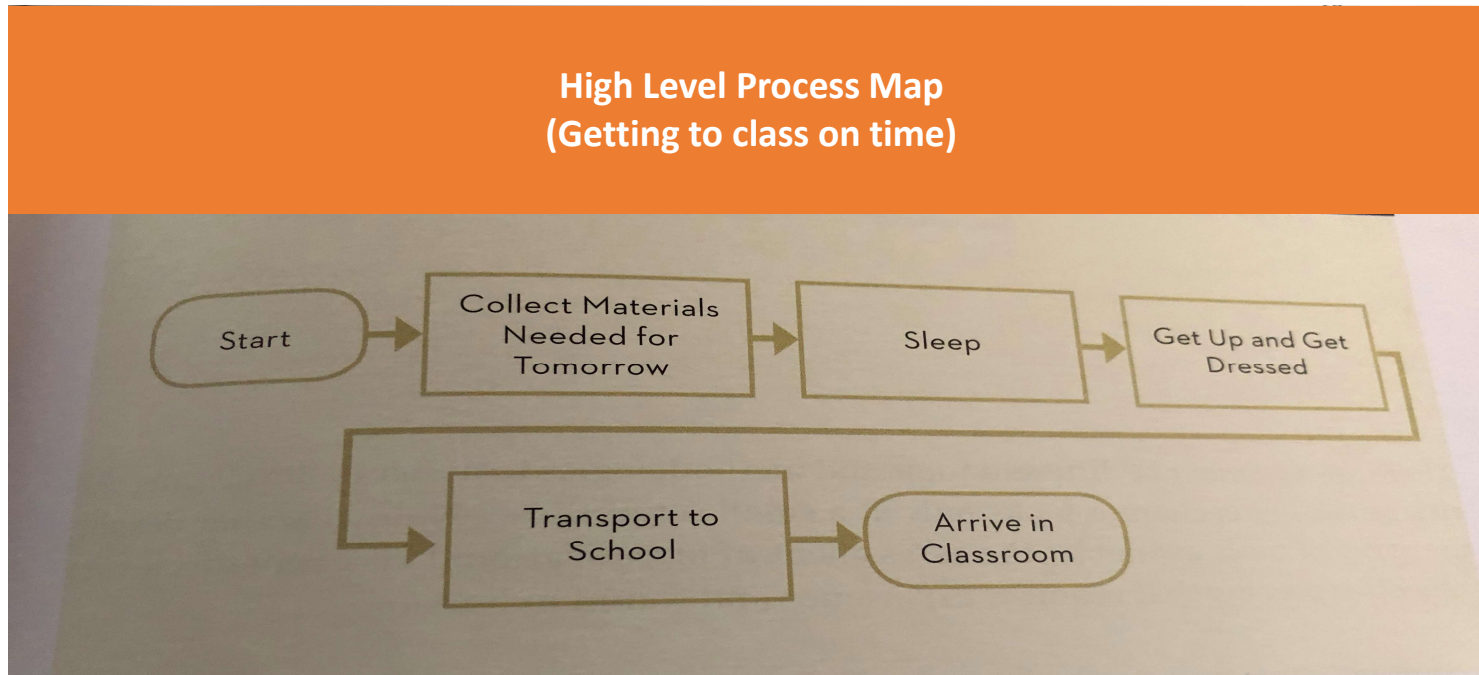
Business Process - IAs

A2: Documenting Business Processes



Business Process - IAs

A2: Documenting Business Processes



Business Process - IAs

A3: Identifying and Assessing Business Risks

- Identifying Risks
 - Risk Profile:
 - Developed by management
 - ERM
 - If such profile is not existing, the IAF will need to create the profile.
- Assessing risks: Impact and Likelihood
- 3 categories (H/M/L)
- 5 Categories:
 - Impact: Extreme/High/Medium/Low/Negligible
 - Likelihood: Certain/Probable/ Possible/ Unlikely/ Remote

Business Process - IAs

A3: Identifying and Assessing Business Risks

- 5 Categories:
 - Impact: Extreme/High/Medium/Low/Negligible
 - Likelihood: Certain/Probable/ Possible/ Unlikely/ Remote
- Risk Assessment Model

Business Process - IAs

A3: Identifying and Assessing Business Risks

Risk Assessment Model

IMPACT	Extreme	15	19	22	24	25
	High	10	14	18	21	23
	Medium	6	9	13	17	20
	Low	3	5	8	12	16
	Negligible	1	2	4	7	11
		Remote (0-25%)	Unlikely (25-50%)	Possible (50-75%)	Probable (75-90%)	Certain (90-100%)

1 – 6 Low Risks
7 – 15 Moderate Risks
16 – 19 High Risks
20 – 25 Critical Risks

Business Process - IAs

A3: Identifying and Assessing Business Risks

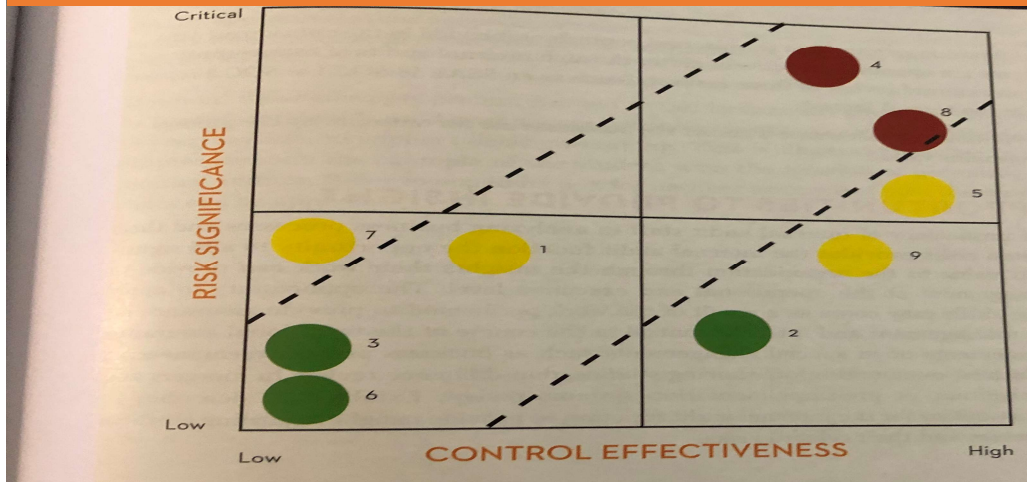
Four types of risk responses:

1. Acceptance
2. Avoidance
3. Reduction (ICs)
4. Sharing

Business Process - IAs

A4: Assessing Controls Effectiveness

Risk Control Map



Risk 7: Under controlled (no appropriate balance)

Risks 1, 3, 4, 6, and 8: Appropriately balanced

Risks 2, 5, and 9: Overcontrolled

Business Process Outsourcing

- The act of transferring some of an organization's business processes to outside provider:
 - Cost reduction
 - Operating effectiveness
 - Operating efficiency

End of Chapter