

# **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

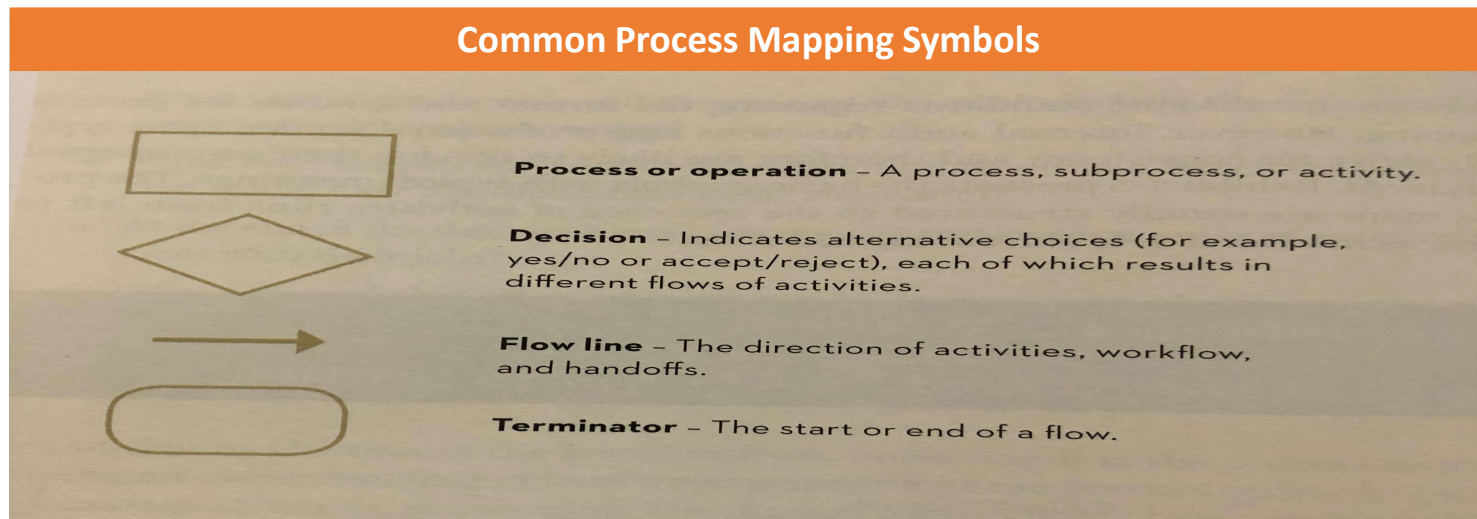
## A2: Documenting Business Processes

- 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

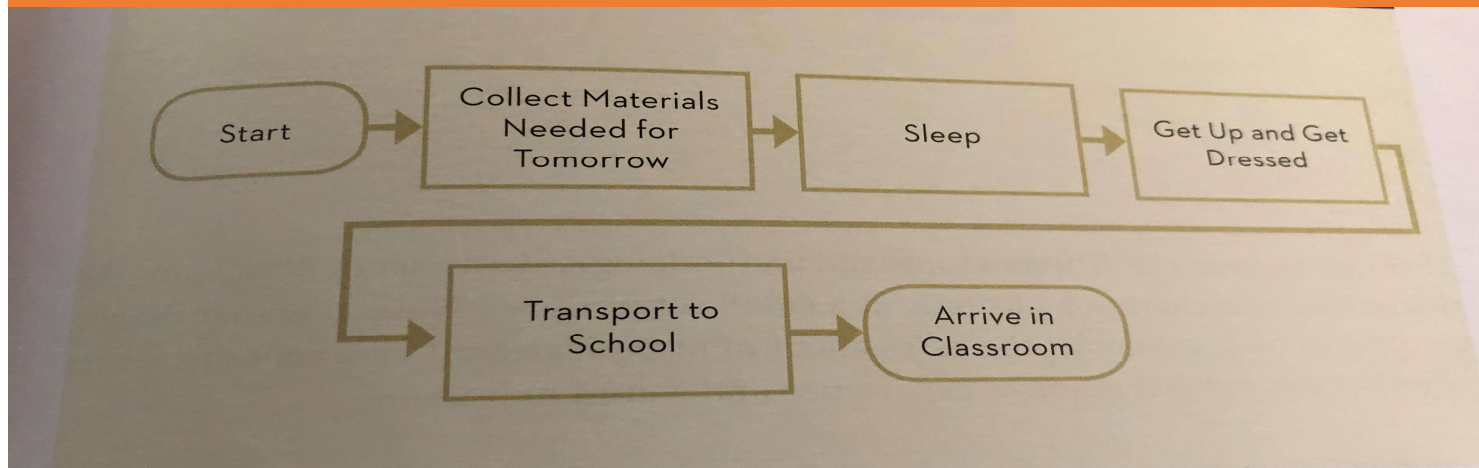
## A2: Documenting Business Processes



# Business Process - IAs

## A2: Documenting Business Processes

High Level Process Map  
(Getting to class on time)



# 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%)
<b>1 – 6 Low Risks</b>						
<b>7 – 15 Moderate Risks</b>						
<b>16 – 19 High Risks</b>						
<b>20 – 25 Critical Risks</b>						

# Business Process - IAs

## A3: Identifying and Assessing Business Risks

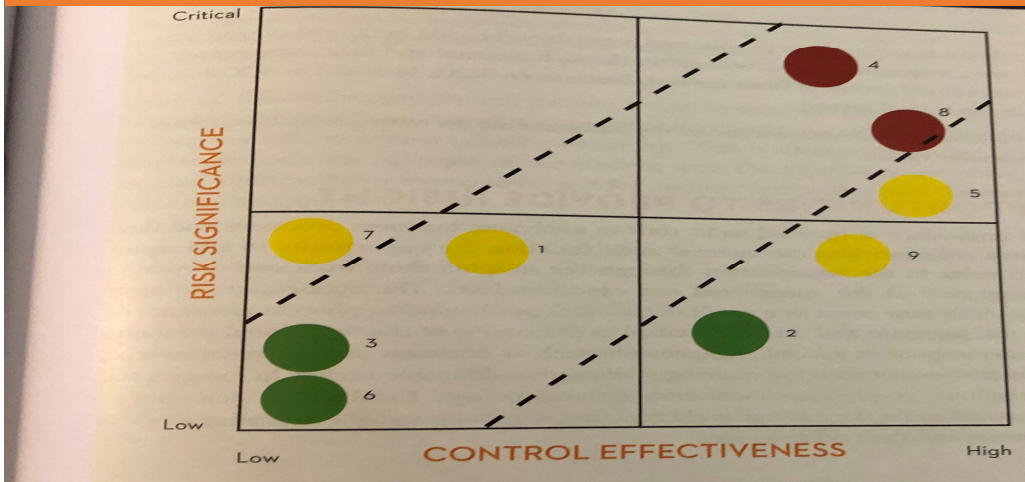
Four types of risk responses:

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