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THE ROLE OF INTERNAL AUDIT IN REDUCING OPERATIONAL RISK AT THE IMAM KHOMEINI RELIEF COMMITTEE OF KOHGILUYEH AND BOYER-AHMAD PROVINCE

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ABSTRACT

The objective of this research is to study the role of internal audit to reduce operational risk at the Imam Khomeini Relief Committee in province Kohgiluyeh and Boyer-Ahmad Province. The purpose of this research is based on the application and the type of research is cross-correlation and in terms of method it is field – survey. Internal audit and its measures are considered as independent variables and operational risk reduction as dependent variable, therefore, the internal audit based on the model of Hess *et al.*, (2006), was defined in two dimensions in order to examine the relationship of each of these dimensions to reduce operational risk in the Relief Committee of Imam Khomeini in Kohgiluyeh and Boyer-Ahmad Province. In this study, a questionnaire with Likert scale was used for data collection and data analysis was performed using SPSS software. The study population of the research consists of 98 people of all managers involved in the mission, goals and operational activities associated with the experience of experts in the field of monitoring (inspection, audit, and investigation of complaints) and financial and administrative areas of both working and retired employees of Kohgiluyeh and Boyer-Ahmad Relief Committee. The results of test hypothesis indicate the existence of significant, positive and strong relationship between the internal audit and operational risk activity reduction. Based on the findings of the research, internal of Imam Khomeini Relief Committee has effect in terms of ensuring internal audit services and counseling to reduce the risk of operational activities and strategic.

Keywords: *Internal Audit, Advisory Role of Internal Audit and Reassurance Role of Internal Audit*

INTRODUCTION

Internal auditors should be able to design and implement tests in order to prevent and detect interior irregularities, detailed understanding of operations, processes and procedures of the organization and to determine the processes and procedures specified in the schedule (Clark *et al.*, 1980).

Providing information about the efficiency of the system of internal controls and the quality of the business unit to business unit managers and the Board of Directors and Chief Executive Officer, are of responsibilities of internal auditors. Companies that have the best internal audit guidelines, those that employ leading procedures and the expectations and strategic objectives that have been established by management and the board of directors generally have better control. The importance of strong corporate governance risk management today has increasingly been confirmed. Organizations in order to identify all the risks that they face in their business, social, ethical, environmental, financial, operational, and to explain how they managed to an acceptable level, they are strongly under pressure. In the meantime, using the framework of risk management in the organization has been expanded with knowledge of its advantages over less coordinated approaches (Hirth, 2008).

Risk Management in an organization is a structured, consistent and continuous process throughout the organization to identify, assess, and decide on responses to and reporting on opportunities and threats that affect the achievement of objectives, macro management or Board of Directors has overall responsibility for ensuring risk management. In practice, the managers delegate the operation of the risk management framework to the management team who are responsible for the following activities. It may also be defined in a separate function that undertakes the coordination and management of the activities and

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benefits the skills and knowledge. Everyone in the organization plays a role in ensuring the successful implementation of risk management in the organization but the primary responsibility for identifying risks and managing them lies with management (Pakravan, 2007).

Internal audit, as well as providing assurance, helps advisory services to various forms of risk management. Internal audit may provide advisory services that improve leading the company, risk management, and control processes. With the expansion of organizations and reduction of their sources and reduction of the possibility of personal management control, internal audit has felt sufficient incentive to extend the maturity of its effectiveness and efficiency of use of scarce resources (Dittenhofer, 2001).

Accordingly they extended the domain of operations farther than only financial audit. In this kind of audit, the concentration of investigations is on key activities of the organization. Performance assessment criteria are also activity oriented and the financial and nonfinancial criteria are used to assess performance. As a result, this assessment is an internal assessment following identifying weak points of operational activities and providing suggestions for performance improvement. Therefore, present study, at the meantime of investigating and studying internal audit is looking for its effects on operational activities risk reduction of Imam Khomeini relief committee that necessary evidences are provided to answer following question.

Does internal audit have influence on operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province?

Review of Literature

Internal Audit

Internal audit consists of vast area of items: internal control system, risk management, accounting information system and etc. Thus, internal audit works as an independent assessment on internal control and much farther than other forms of external organizational control (such as independent audit) or monitoring, but simultaneously it is a part of internal control of each company. In addition to this, it is believed that internal auditor plays the role of an advisor. A study published by the Basel Committee shows that this should be a secondary activity of internal auditor and special care must be taken to accomplish the activities of the internal auditors and not endanger consulting. Therefore, the exceptional service of internal audit unit is derived from all groups specific audit work (Arjmandinejad, 2006).

Internal audit functions as independently assessment which is created by management to evaluate the internal control system. Internal audit reports and evaluates adequacy of internal control systems from aspect of effective and efficient use of resources test (Arbabsoleimani, 2004). "Internal audit is an independent, targeted and counseling activity that is designed to add value and improve business operations; this activity helps organizations achieve their objectives by providing a systematic approach to evaluate and improve the effectiveness of risk management, control and governance processes (Hassasyegane, 2006).

The Objective of Internal Audit

Following items can be referred to for settlement of a strong internal control system:

- Applying policies of the organization
- Identification and recognition of the principles and values of the organization
- Compliance with laws and regulations
- Accurate and reliable financial statements and other information that are released
- Efficient and effective management of human resources and other resources
- Compliance with social issues, including the environment

The objective of internal auditing is helping management to ensure that all of the above mentioned items are performed or observed as they should be (Auditing Standard No. 200, revised 2002).

However, the main objective of internal audit is evaluation of the tasks assigned to different units of the Institute. Internal audit staff members are under the supervision of the CEO or other senior officials. This top position in the organizational structure of the institution ensures that the internal auditors have access to the majority of institutions. It is necessary that independent internal auditors be of the heads and managers who audit their work (KarimiShahraki, 2004).

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Tasks of Internal Audit

Internal audit has a fundamental and key role in compiling all of internal control methods – no matter financial or nonfinancial – settlement of internal control system in its general sense, evaluation and assessment of internal control system in its general sense, offering constructive suggestions for improving the system and assessing the effectiveness and efficiency of enterprise resources (Saffar, 2004).

Most of the organizations have determined major function of internal audit to assess the adequacy of internal controls and the reliability of financial information. But now, the scope of internal audit activities is much more expanded. They evaluate the efficiency of operations, reliability of information, effectiveness and efficiency of business transactions within and outside the country, helping to improve the processes and operations of the Company and monitor their customers' satisfaction. This new task occurs in addition to the traditional function of the search and discovery of the fraud perpetrated. In other words, the scope of their activities has gone far beyond the environment traditional financial control and stewardship role. Since then, internal auditors understand the situation and decide to go beyond supporting role and have more dynamic and more fundamental role in the management structure, and offer a variety of services. Management also showed a good response of the services provided by them and more important role in improving the operation of the internal auditors (Pakravan, 2007).

Risk

The term risk is widely used. But the audience has often rather different interpretations of it. For example, methods of risk associated with the opportunity depend on how to consider the risk. Sometimes, one situation may provide both opportunities for profit and potential loss. But in other cases, there is no opportunity for profit only potential loss.

This risk can be further sub divided into two types:

1. Speculative risk;
2. Dangerous risk;

Speculative Risk

In the speculative risk, you can have a realized profit or improvements in routine conditions of existing state of mind and simultaneously, have the potential to experience a loss or deterioration of the status quo. Gambling is an example of a speculative risk. You bet, you should assess the possibility to obtain more money from the expected loss of betting condition. Increase in your wealth and your willingness to invest in risk, in order to provide a profitable opportunity.

Dangerous Risk

In contrast, dangerous risk has only a potential risk of serious harm associated with the procedure does not provide any opportunity for improvement. For example pay attention how to consider security as a dangerous risk. Suppose you are concerned about the protection of valuable objects which are kept in the house. Your main goal in this example is to ensure that the misappropriation of objects in your home will not happen without your knowledge or consent. After the evaluation of the safety of objects, it is possible that you have decided to install a security system in your home to prevent thieves steal your things. Note that the purpose of this example is only focus on the potential risk of loss. In the most favorable conditions, you only protect what you already own it and there is no potential for profitability.

In this example, you tend to gain peace of mind by avoiding the unpleasant consequences of entering your home.

Your goal as a sense of security determines the condition that is called risk. After analyzing the situation, you may decide to install a security system in your home to create obstacles for thieves. You may argue that the increase in security is likely to bring you more security and cause peace of mind that you are looking for. In this example; you are willing to invest money in a security system to provide an opportunity to feel more secure. Security risks in this example, is speculative, because in this case the tolerance for risk (eg the amount of money you wish to invest in a security system) with the opportunity to realize your interests (eg for peace of mind) is in the balance. Thus, it is quite clear that risk cannot be classified as dangerous and speculative according to their type but it is classified based on the circumstances in which it is perceived.

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Strategic Risk

Strategic risk is the risk that an organization accepts to achieve its business objectives. The content of this definition, the potential profit and loss both exist, which makes strategic risk naturally speculative. Notice how the four elements of risk are applied to strategic risk. For example, assume a condition that senior management in a financial institution is reviewing about entering a new market like online banking services. Since this is implemented due to the decision making process, the management must investigate the potential opportunities and threats in the market. Content in this particular example is the market for online banking services. All actions, conditions and consequences must be considered within the specific context. Activities in this example are measured in a range of strategic selections. Management has a number of options that can be followed, including the following four in progress:

- Deciding to enter market as quickly as possible
- Precautionary actions through some experimental services
- Not practically done at the present but reserving the rights of future actions
- Deciding on not to enter market

The conditions in this example includes current processes and lack of assurance toward online banking service such as potential customers, what competitors may do, and main sustainability of organization in the present. Combination of each strategic activity with current processes and lack of assurance produces a range of outcomes or a set of profitability and loss for the organization. Management investigates the relative degree of opportunities and risks associated with each of the strategic. They select the best choice based on the risk tolerance of the tendency to obtain benefits from its opportunities. Therefore, four main elements of risk provide a useful tool for analyzing and understanding a strategic business risk. These elements are also useful in determining a dangerous risk, as operational risk (Bagherzadeh, 2002).

Operational Risk

Managers in all organizations are dealing with risk. Management focus on high levels of organization most of the time is on speculative nature of risk. Investment risk management adjusts organizational assets against potential return of the investment and manages risk in activities of the organization and funding by strategic considerations. However, at the operational levels of the organization, management and staff as usual focus on some kind of dangerous risk called operational risk. As the staff and management run work affairs, operational risk begin to arise. Shortcomings inherent in the process can lead to inefficiencies and problems during operation, which could adversely affect the organization's success (Nikkhahazad *et al.*, 1997).

Unfortunately, there is no universal definition of the term operational risk. Basel Banking Supervision Committee has published a perfect framework known as "Basel two" and includes a definition of operational risk, which is widely used by the financial community. Operational risk based on framework of Basel II, is defined as the risk of loss resulting from inadequacy or failure of internal processes, people and systems or from external events. Another definition of operational risk is also available. Operational risk means the potential failure to achieve the objectives of the mission. This definition includes losses (failure to achieve the objectives of the mission) and uncertainty (probability of occurrence or non-occurrence of failure). Simultaneously, this definition is suitable for use in many different contexts (Anderson, 2004).

In summary, although various forms of risk exist (including commercial risk, operational, project and security), but all of them have the same notion. However, there can be significant differences between the various types of risk based on the content and visual perception. For example, a speculative risk as a business risk has unique features that distinguish it from a dangerous risk such as operational risk. Speculative nature of business risk may follow profit and loss. The operational risk does not provide any opportunity for profit. As already mentioned, the definition of operational risk used in this text is: the operational risk is potential possibility of failure to achieve the objectives of the mission (Windram and song, 2004).

Based on the purposes of this study, as well as the theoretical framework of the research model, to develop a conceptual model and a description and evaluation of the measured variables of interest:

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Figure 1: conceptual model of research

Hypotheses

Main Hypothesis

There is a significant relationship between the role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

First Subordinate Hypothesis

There is a significant relationship between the advisory role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

Second Subordinate Hypothesis

There is a significant relationship between the assurance role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

MATERIALS AND METHODS

The purpose of this research is based on the application and the type of research is cross-correlation and in terms of method it is field – survey. The study population of this research consists of operational managers or influential people in the planning and operational decision-making activities of Imam Khomeini Relief Committee in Kohgiluyeh and Boyer-Ahmad and other experts are considered as another part of society who are directly in relation with financial and accounting activities. Because of the limited size of the target population, therefore, the sampling is not done in this study. Therefore, the census or enumeration is used in the data collection of the sample size in this study the statistical population is 98 people.

To summarize the relationship between the main hypothesis of major and minor questions or elements used in the questionnaire with questions related to them are as follows:

Table 1: Correlation between variables in the questionnaire

Components	Main elements
The Educational role of internal audit	The advisory role of internal audit
The Facilitation role of internal audit	
The synchronization role of internal audit	
the adjusting targets role of internal audit	
The Variety of services role of internal audit	
The Evaluation of performance role of internal audit	The assurance role of internal audit
The Control activities role of internal audit	
The Cognitive event role of internal audit	
The information and communication role of internal audit	

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In the present study, according to the analysis and interpretation of the data that was performed using the SPSS software, in order to assess the reliability of the method "Cronbach alpha" was used. Cronbach's alpha value of 886% was obtained by questionnaire. Inferential analysis of data and test research hypotheses was done using the Friedman test and the correlation coefficient.

Data Analysis

To test the normality of the dependent and independent variables in the questionnaire study of goodness of fit test Kolmogorov - Smirnov test was used.

H₀: Data is not normally distributed;

H₁: Data is normally distributed

Table 2: Output of Kolmogorov - Smirnov test

Internal audit system		
Assurance role	Advisory role	
98	98	Sample size
3.9173	4.0439	Normal average
0.48248	0.60121	Standard deviation
0.071	0.175	The maximum absolute
0.058	0.138	Positive difference
0.071	0.175	Negative difference
0.805	1.730	Kolmogorov - Smirnov test
0.537	0.501	Significant relationship

According to table (2) if significance level of Kolmogorov - Smirnov test is lower than %5 we reject H₁ hypothesis. As can be seen since sig is more than 0.05 thus a normal distribution assumption is established for all variables.

First Subordinate Hypothesis

H₀: there is no significant relationship between the advisory role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

H₁: there is a significant relationship between the advisory role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

Table 3: Pearson testing results of first hypothesis

Reduce the risk of operational activities		
0.607	Pearson correlation	
0.000	Sig	Advisory role
98	N	

As the table (3), implies, the significance level of 0.000 and less than 0.05 and with respect to the Pearson correlation coefficient of 0.607, therefore H₀ is rejected and H₁ is accepted. Based on this, there is a significant, positive and strong relationship between the advisory role of internal audit and operational activities risk reduction; and it can be said when the advisory role of internal audit is most used, reducing the risk of operational activities will reach its maximum and vice versa.

Second Subordinate Hypothesis

H₀: there is no significant relationship between the assurance role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

H₁: there is a significant relationship between the assurance role of internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

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Table 4: Pearson testing results of second hypothesis

Reduce the risk of operational activities		
0.487	Pearson correlation	
0.000	Sig	Assurance role
98	N	

The findings of table (4), implies, the significance level of less than 0.05 the error is considered and obtained 0.000, therefore the H1 hypothesis that there is a relationship between two variables is confirmed. Pearson correlation intensity has been 0.487, which means there is asignificant, strong and positive relationship between the role of assurance and operational activities risk reduction; thus when the assurance role is the most used in internal audit, reducing the risk of operational activities will reach its maximum and vice versa.

Main Hypothesis

H₀: there is no significant relationship between the internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

H₁: there is a significant relationship between the internal audit and operational activities risk reduction in Imam Khomeini relief committee in Kohgiluyeh and Boyer-Ahmad Province.

Table 5: Pearson testing results of main hypothesis

Reduce the risk of operational activities		
0.498	Pearson correlation	
0.000	Sig	Internal audit
98	N	

Due to the significance level in table (5) which is less than 0.05 and Pearson correlation coefficient has been 0/498 there is asignificant, strong and positive relationship between the internal audit and operational activities risk reduction; thus the H₁ hypothesis is confirmed, when the internal audit is most used, consequently reducing the risk of operational activities will reach its maximum and vice versa.

Ranking of Research Variables

Table 6: Descriptive results of Friedman test

Maximum	Minimum	Std. Deviation	Average	N	
8.30	2.30	0.60121	4.0439	98	Advisory role
4.80	2.10	0.48248	3.9173	98	Assurance role

Table 7: Ranking the components of internal audit

Audit components	Average rating
Advisory role	1.62
Assurance role	1.38

Table 8: the results of Friedman statistical test

N	98
Chi-Square	5.944
df	1
Asymp. Sig.	0.015

As the data of table (7) and (8) implies, the significance level obtained in Friedman test is equal to 0.015 which considered that the amount of the error is less than 0.05, thus the zero hypothesis is rejected and this represents that the average rank of none of the internal audit components are same. In this regard, the

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significance relationship of advisory role of internal audit system ranked first or most relevant in reducing the risk of operational activities of the organization are studied and the connection is direct. The next priority is the assurance role variable associated with a reduced risk of operational activities of the organization's data.

RESULTS AND DISCUSSION

According to the findings of internal audit research in Imam Relief Committee two forms of advisory and assurance services has impact on risk reduction of operational and strategic activities. Panahian (2006), has studied on the impact of internal audit on reinforcement of internal control in Iran's national oil company, the conclusion drawn by his research represents that internal audit of Iran's national oil company has had impact on providing advisory and assurance services regarding the reinforcement of internal controls. Therefore it is consistent with the present study. Zwaan *et al.*, (2011), in a research done in Australia investigated the impact of involvement of internal audit in enterprise risk management on their enthusiasm for the reporting of failures in risk management practices, whether robust internal audit by the Audit Committee, has effect on this enthusiasm or not.

In this study, the use of enterprise risk management and internal auditing's role in enterprise risk management are also examined. The results of the researcher indicated that involvement of internal audit in enterprise risk management has impact on their enthusiasm for reporting the failure of risk management procedures to the Audit Committee. Internal auditors committee (2005) has done a world-wide research on the involvement of internal audit in enterprise risk management through internet. The results showed that 36 percent of surveyed participants were internal auditors responsible for enterprise risk management. Also in some cases, internal auditors have been involved in activities that are wrong or not recommended by the committee of auditors. Both results were consistent with the present study.

Thus, the finding of present study based on applying internal audit consisting role of advisory and role of assurance components in order to reduce the risk of operational risks in organization been studied confirms the results of Zarate (2001), Gramling and Mayers (2006), and Castanira *et al.*, (2009) researches and shows the statements of internal auditors committee- Britain and Irland (2003) and a complete consistency.

Castanira *et al.*, (2009) have done a research with the purpose of identifying the factors related with applying internal audit based on risk and discovering the role of internal audit in enterprise risk management. They concluded that annual auditing plans, applying the approach based on risk in international companies and Portugal Stock Exchange member firms are statistically significant. They also concluded that there is a strong correlation (but not too much) the annual audit plan based on risk and private entities, financial and large industry and in planning the audit, risk-based approach positively with the size of the unit is connected.

MousaviShiriet *al.*, (2013), have reviewed the participation of internal auditors in the risk management firm, the main objective of this study was to investigate the role of internal audit in enterprise risk Management Company listed in Tehran Stock Exchange. The results indicate that internal auditors have had low participation in enterprise risk management, but they are also involved in activities that could jeopardize their neutrality (MousaviShiriet *et al.*, 2014).

Suggestions

- According to senior executives and operational managers believe that internal audit has had impact on risk reduction activities, therefore, it is suggested that the overall management of the Imam Khomeini Relief Committee must strengthen the organizational status of the internal audit.
- In order to establish or maintain the independence of internal auditing at different levels of organization in terms of access to management, access to documents, autonomy and independence to vote on the report, it is suggested that the necessary measures in the case of other organizations, institutions and companies should be taken.
- The programs and activities of the internal audit guidelines recommended by the Forums Code of professional standards and regulation should be used.

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