CONCEPTUALISING BALANCED RELIANCE ON INTERNAL AUDIT WORK BY EXTERNAL AUDITORS

by

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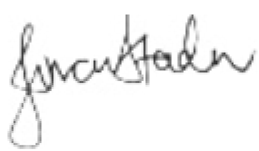

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ABSTRACT

Reliance refers to the incorporation of internal audit work into audit evidence during statutory external audits. Inappropriate reliance undermines audit effectiveness and quality while fair reliance enhances audit efficiency. Reliance is complex, implementation problems are common and academic knowledge gaps prevail. Consequently, the research question of this study is formulated as follows:

> *How can reliance on internal audit work by external auditors be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors?*

Responding to the research question, the major contribution of this study is the substantive theory of balanced reliance, explaining how management, the audit committee and internal and external auditors overcome disconnect between their reciprocal influences on reliance to *achieve mutual agreement that reliance is appropriate and fair, balanced, whatever the reliance decision*.

The study is based on the classic grounded theory methodology of Glaser and Strauss (1967) and was implemented in three phases:

Phase 1: Theoretical sampling included 32 interviews. Five key data sets (22 initial and three follow-up interviews) represented five diverse South African listed companies. Each data set comprised data from the key audit stakeholder groups of the company, namely, the chief financial officer, audit committee chair, chief audit executive and external audit engagement partner. A further data set of seven interviews involved other knowledgeable audit professionals.

Joint data collection, open coding and analysis identified the main concern – the *disconnect* between the stakeholder groups' reciprocal influences on reliance – and the core category (*achieving mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

Phase 2: Joint theoretical sampling, selective and theoretical coding and analysis saturated the substantive categories' properties and relationships.

Phase 3: Theoretical sorting and writing delimited the substantive categories into theoretical constructs, explaining the substantive theory. Comparisons indicated how the substantive theory broadened and transcended extant knowledge.

The substantive theory of balanced reliance developed in this study explains how the stakeholder groups' willing *reciprocal synchronisation* resolves disconnect between the stakeholder groups' roles, interpretations, interests and practices influencing reliance. This, in turn, renders viable their *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. With *reciprocal synchronisation* as a foundation, a voluntarily formed *team mindset* is the predominant mediator of *habitual integration* and *fair alignment* of internal and external audit work. These co-variant conditions change stakeholder groups' *mutual agreement* from being viable to practicable, as the disconnect between internal and external audits is resolved. Stakeholder groups' participation in *facilitative communication* and a strong audit committee's *balancing oversight* create the context for sustaining stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced)*, *whatever the reliance decision*.

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CHAPTER 1

INTRODUCING THE STUDY

CHAPTER 1

INTRODUCING THE STUDY

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1.1 INTRODUCTION

This classic grounded theory study investigates reliance by external auditors on internal audit work during statutory external audits (referred to as “reliance”). It conceptualises interview data collected from the chief financial officers, chairs of audit committees, external audit engagement partners and chief audit executives of five diverse listed South African companies, as well as other knowledgeable senior internal and external audit professionals. In line with this formalised research methodology, inductive data collection and analysis by constant comparison in three phases generated the participant groups’ main concern about reliance and the core category, explaining how they overcome it in practice. This study contributes the substantive theory of balanced reliance as a response to disconnect between the reciprocal influences of management, the audit committee, internal and external auditors (the stakeholder groups) on reliance. The theory explains how the stakeholder groups overcome disconnect between their reciprocal influences on reliance to achieve mutual agreement that reliance is appropriate and fair, balanced, whatever the reliance decision.

This introductory chapter starts off by providing a background on reliance and highlighting the importance of such research, considering complexity, real-world problems and prevailing knowledge gaps. Using insights from a review of literature, the central research problem is inferred and the related research aim, question and expected outcomes are stated. A brief description of the research design, methodology and delimitations provide an indication of how the study answered the research question. The contributions of the study are then highlighted. Since this South African study addresses a global auditing problem, the wider relevance of the study is emphasised. The chapter closes with an outline of the remaining chapters of the study and lists of abbreviations, key terms and annexures.

1.2 BACKGROUND

For almost 40 years now, external and internal auditing professional standards have acknowledged reliance on internal audit work during statutory external audits (IAASB, 2018: ISA 610 (Revised 2013); IIA, 2016: Standard 2050; Brown, 1983:444-445). In the current study, the terms “reliance”, “practising reliance” and “reliance practised” imply using internal audit work ‘to modify the nature or timing, or reduce the extent, of procedures to be performed directly by the external auditor’ on a statutory audit (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13), by incorporating internal audit work into external audit evidence. The term “reliance work” refers to two types of reliance work, (i) work performed in the normal course of an internal audit, and (ii) “direct assistance work” performed by internal auditors under the direction, supervision and review of the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13). External auditors also use “peripheral support by internal auditors”, also known as ‘indirect reliance on tangential IAF [internal audit function] work’ (Bame-Aldred, Brandon, Messier Jr., Rittenberg & Stefaniak, 2013:255). Such support work does not produce external audit evidence.

Reliance implies incorporating internal audit work into external audit evidence supporting the external audit opinion (IAASB, 2018: ISA 610 (Revised 2013) paragraph 1). Therefore, reliance may lead to the modification of procedures directly performed by the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13, 14 (b)), including changes to the nature or timing, or reducing the extent of external audit procedures (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13). However, “inappropriate reliance” could decrease external audit quality (PCAOB, 2013:2, 35), for example, when the external auditor’s opinion relies on internal audit work providing unreliable, irrelevant or insufficient evidence (IAASB, 2018: ISA 500; PCAOB, 2013:2, 35).

External auditing professional standards contain a framework with requirements and guidance for practising appropriate reliance (IAASB, 2018: ISA 610 (Revised 2013)). Importantly, the external auditor remains solely responsible for the external audit opinion, irrespective of reliance (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). Internal auditing professional standards (IIA, 2016: Standard 2050) require the chief audit executive to share information and coordinate activities with the external auditor.

A logical foundational pre-requisite for practising reliance is the relevance of internal audit work for statutory audit purposes (IAASB, 2018: ISA 315 (Revised) paragraph 23, A115).

However, from professional pronouncements, distinct differences in the roles of internal and external audit are evident, implying that not all internal audit work may be relevant for external audit purposes (IIA, 2015a). More specifically, internal audit's role is wide, incorporating assurance and consulting on operational, governance, risk management and control matters (IIA, 2015a). In contrast, external auditing professional standards focus external audit's statutory role exclusively on expressing independent assurance on statutory financial reporting (IAASB, 2018: ISA 200 paragraph 11).

Despite these distinct roles of internal and external audit, some overlap in their work is possible. The extent of overlap depends on the scope and focus of internal audit's mandate and procedures (IAASB, 2018: ISA 315 (Revised) paragraph A115). The IIA (2017:3) highlights the potential for confusion among stakeholders, who may misunderstand the blurred boundaries between internal and external audit work and their potential effect on the overlap of internal and external audit work.

Many researchers have studied reliance (Bame-Aldred *et al.*, 2013 provide a summary of such studies). There is general consensus that reliance is complex, requiring simultaneous consideration of numerous interacting factors (Quick & Henrizi, 2018:26; Trotman & Duncan, 2018:254; Singh, Woodliff, Sultana & Newby, 2014:36; Bame-Aldred *et al.*, 2013:251-252, 282-283; Brody, 2012:11; Desai, Roberts & Srivastava, 2010:538; Krishnamoorthy, 2001:499; 513; Maletta, 1993:508; Edge & Farley, 1991:77).

Given this complexity and the potential audit quality implications as well as the potential confusion among stakeholder groups, there have been calls for more research on reliance (for example, Bame-Aldred *et al.*, 2013:251). At the audit practice level, specific areas requiring improved understanding include the decision-making processes of external auditors in the reliance process, for example how and to what extent the external auditor evaluates the quality of internal audit work, the litigation risk for external auditors when practising reliance, and how reliance influences external audit fees over time (Bame-Aldred *et al.*, 2013:253, 277,283). At the level of the auditing profession, Bame-Aldred *et al.* (2013:280) call on regulators to 'draft regulations and oversee the profession in such a way that reflects an understanding of the complex environment in which practitioners make reliance decisions'.

Complementary or similar work performed across professional roles is not unique to internal and external auditing. External auditors may also use evidence produced by other professionals, for example, management experts (IAASB, 2018: ISA 500 paragraph 8) and / or independent auditors' experts (IAASB, 2018: ISA 620) for statutory audit purposes. Outside the accounting field, research on interprofessional collaboration is especially prevalent in healthcare contexts (for example Vestergaard & Nørgaard, 2018; Xyrichis, Reeves & Zwarenstein, 2018; Mitchell, Parker, Giles & White, 2010; Baxter & Brumfitt, 2008; Pullon, 2008; D'Amour, Ferrada-Videla, Rodriquez & Beaulieu, 2005). Researchers highlight that interprofessional collaboration depends on role clarity, demonstrated professional competence, mutual respect and trust, communication skills and commitment to teamwork (Kebe, Chiocchio, Bamvita & Fleury, 2019:76; Suter, Arndt, Arthur, Parboosingh, Taylor & Deutschlander, 2009:41; Pullon, 2008:133).

1.3 IMPORTANCE OF THE STUDY

This study bridges an important gap, identified from evidence from the real world, about the challenges inherent in practising reliance. It also addresses shortcomings identified in the literature which, instead of resolving these challenges, contribute to their persistence. This section first provides examples of inappropriate reliance and allegations of unfair non-reliance in the real world. Then, after consulting the literature, the section reflects on the knowledge gaps inherent in real-world problems and considers why these shortcomings persist despite numerous academic studies on reliance. Specific knowledge gaps highlighted include "assurance effectiveness and efficiency" (include effectiveness (quality) and efficiency (effort and cost) of internal and / or external auditors' work), the interrelated yet distinct roles of internal and external audit determining the overlap in internal and external audit work, and methodological choices behind knowledge gaps. Understanding the real-world problems and related knowledge gaps lays the foundation for the research problem described in section 1.4.

1.3.1 Evidence from the real world

Regulators and oversight bodies of external auditors have expressed concerns over reliance. On the one hand, management exert ‘pressure’ on external auditors to increase reliance for ‘efficiency reasons’, expecting that reliance would reduce external audit fees (IAASB, 2012:4). On the other hand, regulatory inspections of the Public Company Audit Oversight Board (PCAOB) in the United States have identified instances of ‘inappropriate’ reliance by external auditors from non-compliance with professional external auditing standards (PCAOB, 2013:29; IAASB, 2012:4), implying questionable external audit quality (Ernst & Young, 2013:1).

In an alert announcement, the oversight body (PCAOB, 2013:35) urged external auditors to comply with external auditing professional standards when practising reliance. The PCAOB also urged external auditors to consider additional training for auditing personnel on how to practise reliance in an appropriate manner (PCAOB, 2013:35). Alarmingly, however, instances of inappropriate reliance continued to occur (PCAOB, 2013:29) despite the extensive requirements and guidance provided in previous and the most current version of external auditing professional standards (IAASB, 2018: ISA 610 (Revised 2013)).

The external auditing standard-setter (the International Audit and Assurance Standards Board (IAASB)) recognises that finding a balance between external audit effectiveness (quality) and efficiency (fees) is challenging. The standard-setter suggests that external auditors adopt a ‘balanced approach’, recognising the advantages and disadvantages of practising reliance (IAASB, 2012:5). The IAASB (2012:5) explains:

> Not only should the pitfalls of over and undue use of the work of the internal audit function for purposes of the audit be highlighted, but also the advantages to audit quality of a constructive and complementary relationship between external and internal auditors including, where appropriate, the possibility of coordination and cooperation.

Balancing external audit effectiveness (quality) and efficiency is challenging. Knechel (2016:215) used the metaphor of a ‘conundrum’. Explaining the reason for the challenge, Knechel (2016:215) highlighted the cost implications of increasing regulatory, governance and auditing requirements which continue to challenge external auditors’ effectiveness in a competitive audit market. Knechel (2016:215) explains that 'efforts to reduce prices (fees) may lead to a loss of quality unless significant effectiveness improvements can be realized … efforts to increase quality may lead to higher prices unless significant efficiency improvements can be realized'.

Unsurprisingly, following their study investigating external auditors' decision-making when practising reliance, Petherbridge and Messier (2016:14) speculate that external auditors 'may not be able to operationalize how to "balance" the trade-off of efficiency and effectiveness' required for 'a balanced approach' to practising reliance. Providing more clarity on the challenge faced by external auditors, Desai, Desai, Libby and Srivastava (2017:1) note that external auditors' reliance decisions were inconsistent when faced with conflicting evidence about the strength of internal audit. Various researchers confirm that the complexities inherent in decision-making during the reliance process complicate balancing the trade-off of external audit quality and efficiency, as the simultaneous consideration of a multitude of factors is required (for example, Singh *et al*., 2014:36; Bame-Aldred *et al.*, 2013:282-283; Brody, 2012:11; Desai *et al.*, 2010:538; Krishnamoorthy, 2001:499; 513; Maletta, 1993:508; Edge & Farley, 1991:77).

Views shared by internal auditors, external auditors and audit committee chairs during roundtable discussions held two years after the regulator's alert announcement (PCAOB, 2013), confirmed that the real-world challenges stemming from complexity and lack of understanding of reliance are not only persisting but worsening (CAQ & IIA, 2015). Participating internal auditors mentioned that tension between them and external auditors had increased, as external auditors reduced reliance following the PCAOB alert announcement (CAQ & IIA, 2015:9). Participating internal auditors also indicated that external auditors had changed reliance from relying on work performed independently by internal audit, to using internal audit's direct assistance work, with the latter requiring improved communication and coordination between the audit teams (CAQ & IIA, 2015:10). However, pointing to similar communication barriers as described by Thomas, Zolin and Hartman (2009:290), the internal auditors reported that the decreased reliance had changed the relationship between internal and external audit from 'very, very good' to 'strained', even leading to 'resentment between the [audit] teams' (CAQ & IIA, 2015:9).

External auditors participating in the roundtable discussions concurred with internal auditors' claims, explaining that they had interpreted the alert announcement as implying substantially reduced regulator (PCAOB) support for reliance from concerns about the effect thereof on external audit quality (CAQ & IIA, 2015:3, 9). They maintained that practising reliance was not automatic; appropriate reliance depended on the riskiness of the audit area, the effectiveness of internal financial controls and the scope and focus of internal audit work (CAQ & IIA, 2015:9):

> For us to use the work of internal audit, we've got to make sure the company has strong [accounting and internal control] systems and there's the level of detail [of internal audit work] we [external audit] need … I think the messaging here to external auditors [by the regulator (PCAOB)] is that, just because internal audit does something, it doesn't mean you can use it … If it's a high-risk area, we will not use the internal auditor's work.

As management were not present at the roundtable discussions, internal auditors conveyed management's increasing dissatisfaction with the decrease in reliance in light of their interest in external audit efficiency (CAQ & IIA, 2015:10). Internal auditors conveyed that management were 'upset', and had interpreted the 'changes' effected by the regulator's alert announcement as unfairly limiting external audit's 'ability' to practise reliance, causing 'audit fatigue' from widespread duplication of work by internal and external audit (CAQ & IIA, 2015:10). Consequently, management exerted 'significant budget pressure' on external auditors, expecting that fee increases should be 'washed away' by increasing reliance (CAQ & IIA, 2015:10). The academic literature also reported that management had interpreted practising reliance as a means for driving down external audit fees, causing them to put pressure on external auditors to increase reliance (Felix, Gramling & Maletta, 1998:66).

Interpreting management's purported stance on reliance and external audit fees, internal auditors participating in the roundtable discussions construed that management had failed to recognise the extent to which internal audit's work on internal controls generally reduced external audit fees (CAQ & IIA, 2015:12). The internal auditors sensed that management lacked understanding of the effort required by internal audit to meet the pre-requisites for reliance work (CAQ & IIA, 2015:12). In essence, real-world problems manifest themselves as difficulty balancing the trade-off between external audit effectiveness (quality) and efficiency in the reliance process to the satisfaction of all involved stakeholder groups.

1.3.2 Knowledge gaps about practising reliance

Assurance effectiveness and efficiency concerns are central to the reliance debate. When external auditors reduce reliance, management, who expect reliance to be practised, could question internal audit's effectiveness and value proposition (Sarens & De Beelde, 2006:219). For its part, management expect that external auditors' fair reliance would reduce, or at least stabilise, external audit fees for improving or maintaining assurance efficiency (Felix, Gramling & Maletta, 2005:31). The effectiveness (quality) of the external audit is paramount for external auditors, who carry the sole responsibility for the external audit opinion expressed (Petherbridge & Messier, 2016:3; IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). It requires external auditors to guard against inappropriate reliance, for example, when the external auditor's opinion relies on unreliable, irrelevant or insufficient evidence from internal audit work (IAASB, 2018: ISA 610 (Revised 2013) paragraph 17-27). While Petherbridge and Messier (2016:14) conclude that external auditors 'do not fully understand whether to focus on efficiency or effectiveness when deciding their reliance level', the literature reveals deeper insights about the complexities contributing to the real-world problem.

Firstly, the dilemma faced by external auditors is how to respond to management's pressure to increase reliance (Felix *et al*., 2005:36). This dilemma has two dimensions. On the one hand is the question whether external auditors should accede to management's pressure to rely, when an assessment of implicit engagement risk indicates that reliance may be inappropriate, with the potential to undermine external audit effectiveness (quality) (PCAOB, 2013:29; Ernst & Young, 2013:1; IAASB, 2012:4). The implicit engagement risk of interprofessional reliance lies in using unreliable, irrelevant or insufficient evidence produced by internal audit 'to modify the nature or timing, or reduce the extent, of procedures to be performed directly by the external auditor' (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13). There is a paucity of research on the direct effect of reliance on external audit effectiveness (quality) (Bame-Aldred *et al.*, 2013:251).

However, at an indirect level, internal audit effectiveness (quality) influences reliance (for example, IAASB, 2018: ISA 315 (Revised 2013) paragraph 15-37; Lee & Park, 2016; Pizzini, Lin & Ziegenfuss, 2015; Pilcher, Gilchrist, Singh & Singh, 2013). The challenge is that the involved stakeholder groups hold diverse interpretations of internal audit effectiveness, as internal audit's multiple roles (Roussy & Brivot, 2016:714; Lenz & Hahn, 2015:27; Lenz, Sarens & D'Silva, 2014:126) uniquely influence each user group's interpretations of internal audit effectiveness (Lenz & Hahn, 2015:17). A further challenge is external auditors' inconsistent interpretations of the influence of internal audit's structure and resourcing model on internal audit quality when making reliance decisions (Christ, Masli, Sharp & Wood, 2015:37; Messier, Reynolds, Simon & Wood, 2011:2131; Sarens & De Beelde, 2006:220).

On the other hand, when they do not accede to management's pressure to increase reliance, external auditors face the risk of being replaced, or at least having strained relationships with management. (Felix *et al.*, 2005:31). Bierstaker, Houston and Wright (2006) found the ongoing competitive market for external audit services could negatively affect external audit's planning decisions (likely to include decisions about practising reliance) and external audit quality. However, the influence of reliance on external audit fees is contentious. Research has produced mixed results on the effect of reliance on external audit fees (audit efficiency). While some studies report that reliance has decreased or stabilised external audit fees (for example, Zain, Zaman & Mohamed, 2015; Felix, Gramling & Maletta, 2001), others note that external audit fees have increased (for example, Singh *et al.*, 2014; Goodwin-Stewart & Kent, 2006), or were not significantly affected (Suwaidan & Qasim, 2010) by reliance. However, Hay, Knechel and Wong (2006:176) and Singh *et al.* (2014:27) contend that the variables used by researchers were behind inconsistencies in prior research findings about the impact of internal audit work on external audit fees.

Secondly, the involved stakeholder groups hold diverse interests in the trade-off between external audit effectiveness (quality) and efficiency, which taints their interpretations and practices influencing reliance. Felix *et al.* (1998:66) found external auditors adopted a conservative approach (evident as lower levels of reliance than expected by management) in contrast to management's progressive stance (evident as pressure on external auditors to increase reliance in order to reduce external audit fees), due to their different 'departure points'. In line with the latter finding, Pilcher *et al.* (2013:334, 336) maintain that a lack of communication between internal and external auditors exacerbates the misunderstanding of their roles, interpretations, interests and practices in the reliance process, causing 'confusion in what each function expected of the other'. Specifically, external auditors have failed to communicate to internal auditors the reasons for not relying on or not sharing information about actual reliance. This has caused internal auditors to believe that high levels of reliance have occurred, when in fact this was not the case (Pilcher *et al.*, 2013:334, 336). Pilcher *et al.* (2013:334, 336) speculate that a lack of mutual 'trust' was behind poor communication between internal and external auditors. Decades earlier, Wallace (1984:199-200) also linked poor communication between internal and external auditors to tension between internal and external auditors when practising reliance. Understandably, Zain, Subramaniam and Stewart (2006:15) call for research providing strategies to improve the relationship between internal and external auditors 'in order to gain a richer understanding of the processes involved in producing high quality financial reports'.

Thirdly, most studies have solicited viewpoints about reliance from external auditors only (evident from the synthesis of Bame-Aldred *et al.*, 2013), ignoring how management, internal audit and the audit committee interpret and influence the reliance. Consequently, several researchers have emphasised the need for further studies incorporating data from other stakeholder groups about practising reliance (for example, Mubako & Muzorewa, 2019). Some studies have called for research incorporating internal auditors' views about practising reliance. By way of example, based on their study of the relationship between internal and external audit fees in Australia, Singh *et al.* (2014:36) suggest that similar future qualitative studies consider the views of all 'key stakeholders (e.g., internal auditors, external auditors, audit committees, independent directors and executive management)'. Lenz and Hahn (2015:22) synthesised research on internal audit effectiveness and observed the prevalence of research considering internal audit effectiveness from the external auditor's perspective, a notion supported by Roussy and Perron (2018). Consequently, they (Lenz & Hahn, 2015:22) called for a broader scope of participant groups in studies on practising reliance, asking: ‘What can we learn from research about the collaboration between IA [internal auditors] and EA [external auditors] from an IA [internal auditor] point of view?’ Moreover, after their experiment assessing how external auditors’ work style and barriers to communication influenced their willingness to rely on the work of internal auditors, Brody (2012:18) suggested future studies should extend participant groups to include internal auditors, as ‘communications is a two-way street’.

Academic studies have also called for research incorporating the views of audit committees about reliance. For example, following their study on the interface between internal and external auditors, Pilcher *et al.* (2013:336) suggested future studies extend the participant groups to include the views of audit committees. The study of Pilcher *et al.* (2013:332) was one of only a few qualitative studies on reliance. This particular study used structured interviews with internal and external auditors representing a single public sector case, an Australian police unit responsible for a large geographical jurisdiction. Moreover, following their respective studies on the relationship between internal auditors and audit committees, and internal auditors and senior management, Sarens, De Beelde and Evereart (2009:90) and Sarens and De Beelde (2006:220) report that audit committees and senior management had specific expectations about their internal auditors’ collaborations with external auditors. Considering audit committee members and senior managers have had little opportunity to voice their views on practising reliance in academic studies, there is scant information on their interpretation of and influence on reliance.

Fourthly, the majority of studies have used deductive methods, mostly experiments with external auditors, to test relationships between factors (mainly originating from external auditing professional standards) in the reliance process (evident from the synthesis of Bame-Aldred *et al.*, 2013). While Pilcher *et al.* (2013:332) used a qualitative method in their study on the interface between internal and external auditors in the public sector in Australia, their objective was to identify factors determining the efficient and effective interrelationship between internal and external audit, and not an inductive comprehensive holistic understanding considering the influences of all stakeholder groups on reliance.

They (Pilcher *et al.*, 2013:332) pre-selected the principle / agent concept of the agency theory as a frame for the external auditors' role, as monitoring mechanisms of public accountability.

Fifthly, most prior studies have not sought to portray a conceptualised explanation of reliance. Instead, most studies have used quantitative methods and existing theory for testing, ranking or motivating specified variables influencing reliance rather than generating a new pattern of meaning. By way of example, DeZoort, Houston and Peters (2001:257, 263, 264) used attribution theory when testing the relationship between reliance and factors influencing internal auditors' personal and task objectivity. Krishnamoorthy (2001:503) used Schum's three major attributes of human source credibility in a normative framework suggesting how the external auditor should evaluate internal audit's work performance, competence and objectivity. Ettredge, Reed and Stone (2000:57) considered the 'implications of microeconomic theory of substitution' in models testing systematic substitution of internal for external audit work over a period of five years. Other examples of quantitative studies on reliance employing *a priori* theories include attribution theory (Messier *et al.*, 2011:2132; Glover, Prawitt & Wood, 2008:196; Munro & Stewart, 2010:377); group affiliation theory (Suwaidan & Qasim, 2010:513; Gramling & Vandevelde, 2006:27); source credibility theory (Arel, 2010) and the Dempster-Shafer theory of belief functions (Desai *et al.*, 2010:541).

Several authors have called for research to inductively develop a conceptualised explanation of reliance, and have suggested means for conducting such studies. For example, Singh *et al.* (2014:36) and Bame-Aldred *et al.* (2013:282-283) have called for in-depth interviews as a means of gaining insights into reliance. Prawitt, Sharp and Wood (2011:202) have identified the need for research transcending the limiting, prescriptive boundaries of external auditing professional standards, allowing insights contributing to 'a descriptive model of the external auditor's reliance decision'. Prawitt *et al.* (2011:202) maintain that such a model 'could prove both enlightening and useful'.

In summary, as evident above, knowledge gaps in the literature on reliance confirm the real-world problem of balancing the trade-off between external audit effectiveness (quality) and efficiency when practising reliance to the satisfaction of all involved stakeholder groups. Such balancing is not without complexity, which arises from the simultaneous consideration of numerous interacting factors. These factors relate to the roles, interpretations, interests and practices of the stakeholder groups. A conceptualised explanation of practising reliance is absent from extant literature, which is dominated by external auditor perspectives and mainly based on deductive methods. The shortcoming reflects the call of Bame-Aldred *et al.* (2013:251) for greater insights into the complex reliance process, addressing the real-world misunderstanding of the roles and overlapping work of internal and external audit (IIA, 2017:3).

1.4 RESEARCH PROBLEM

Reliance has been the subject of academic research for almost 40 years; indeed, Ward and Robertson conducted one of the first studies on the topic in 1980. However, the question still remains: Why does practising reliance remain contentious in the real world and why do knowledge gaps about practising reliance persist? Extant literature on reliance (for example, the studies included in the synthesis of Bame-Aldred *et al.*, 2013) provides clues explaining why a conceptualised explanation of practising reliance is still lacking. This then justifies the current study in spite of more than 50 previous studies on the subject.

Firstly, reliance is complex, requiring simultaneous consideration of numerous interacting factors (for example, Quick & Henrizi, 2018:26; Trotman & Duncan, 2018:254; Singh *et al.*, 2014:36; Bame-Aldred *et al.*, 2013:251-252, 282-283; Brody, 2012:11; Desai *et al.*, 2010:538; Krishnamoorthy, 2001:499; 513; Maletta, 1993:508; Edge & Farley, 1991:77).

Secondly, multiple stakeholder groups' roles, interpretations, interests and practices influence reliance. By way of example, the IIA (2017:3) highlights the potential for confusion among stakeholders when they misunderstand the blurred boundaries of internal and external audit work and their effect on the potential for overlapping internal and external audit work.

Thirdly, decades of academic research on reliance (for example, the studies included by Bame-Aldred *et al.*, 2013) did not provide a conceptualised explanation of reliance. Most extant studies (1) solicited viewpoints about reliance from external auditors only, (2) used deductive methods, mostly experiments with external auditors, for testing relationships between one or a few variables (mainly originating from external auditing professional standards) influencing reliance and / or (3) did not seek to conceptualise research findings about reliance.

Considering the complexity of reliance implicit in multiple stakeholder groups' roles, interpretations, interests and practices influencing reliance, as well as the limitations inherent in methodological choices of previous studies on the topic, a conceptual explanation of reliance would contribute novel insights, with potential for addressing real-world problems and knowledge gaps.

Babbie and Mouton (2001:78-79) suggest that a well-formulated research problem should (1) point out the aim of the study, and (2) specify the unit of analysis.

The *research problem* of this study can therefore be formulated as follows:

> *There is no conceptualised explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.*

1.5 RESEARCH AIM, RESEARCH QUESTION AND RELATED OUTCOME

In view of the research problem stated above, the *aim* of this study is to construct a theorised (conceptualised) explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

Stating the aim as a *research question*: How can reliance on internal audit work by external auditors be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors?

This research question provides an open 'point of departure' for the study (Charmaz, 2014:197). Charmaz (2014:197) explains that '[w]e cannot assume to know our categories in advance, much less have them contained in our beginning research questions'. Thus, the *outcome* of this study is a substantive theory providing a conceptual explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

Against the backdrop of this confusion among stakeholder groups as to reliance possibilities, this study considers all stakeholders' influence on practising reliance. References to all stakeholders or all stakeholder groups include corporate governance mechanisms whose roles, interpretations, interests and practices in the statutory financial reporting and external audit processes provide the context of their individual and reciprocal influences on reliance (see Chapter 2). These stakeholder groups include the chief financial officer (CFO[1]) and executive management (management) as a group, the chair of the audit committee (CAC) and the audit committee as a group, the chief audit executive (CAE) and internal auditors as a group, and, the engagement partner (EP) and external auditors as a group.

Since reliance occurs in the context of stakeholder groups' roles in the statutory financial reporting and external audit processes of organisations (see Chapter 2), five diverse Johannesburg Securities Exchange (JSE) listed companies were the sites of data collection. Data comprised interviews with the representing stakeholder with the highest level of role accountability from each stakeholder group at each site.

1.6 RESEARCH DESIGN AND METHODOLOGY

Charmaz (2014:27) advises that the research problem should shape the research methodology. In this case, the classic grounded theory method (Glaser, 1978; Glaser &

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[1] . Note, the abbreviated forms (CFO, CAC, CAE, EP and CEO) are used in this study only when presenting data. In textual discussions, the unabbreviated forms are used when reference is made to these participants.

Strauss, 1967) was used to purposefully address the research problem and the related gap in knowledge behind the research aim, research questions and objectives of this study.

Notwithstanding professional and governance pronouncements and numerous academic studies spanning almost four decades, a conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors, has not been forthcoming. The classic grounded theory methodology was deemed appropriate for this study as Glaser (1978:3, 10) points out that grounded theory studies 'in well-trodden fields' always generate new categories, thus 'transcend[ing] diverse previous works while integrating them into a new theory of greater scope than extant ones. This is a useful contribution'.

The study operationalised the classic grounded theory methodology in the following three phases:

Phase 1: Open coding interviews conducted with the chief financial officers, audit committee chairs, chief audit executives and external audit engagement partners involved in the statutory financial reporting and external audit processes of five diverse South African listed companies. These revealed the main concern with reliance and the core category, explaining how these stakeholder groups resolved their concerns influencing reliance.

Phase 2: Selective and theoretical coding, combined with memos, delimited the properties of the core and other categories as well as the relationships between these.

Phase 3: Theoretical sorting of memos and theoretical writing generated the theoretical constructs (properties) of the substantive theory. Comparison to relevant existing frameworks and theories shows how the theory broadens and transcends extant knowledge.

The unit of observation is the reliance process, while the units of analysis are statements conveying the participants' constructions of their own and other stakeholder groups' reciprocal influences on reliance, considering their roles, interpretations, interests and practices.

The coherent application of this formalised research methodology contributes to the trustworthiness of the research findings (De Vos, Strydom, Fouché & Delport, 2011:420).

1.7 SIGNIFICANT CONTRIBUTIONS

This study makes significant contributions to the professional practice and theory of auditing. Goode (1969:277-279) proposes that a distinctive attribute of a profession, as compared to other forms of work, is that it requires a body of abstract knowledge – derived from research – if it is to be practised competently. Accounting (including auditing) is recognised as one of the 'new professions'; its practices are thus guided by 'its own fundamental [research] studies' (De Vos *et al.,* 2011:14 from Carr-Saunders, 1955). Thus, research builds a knowledge base and strengthens the distinctive role of a profession in society (Dirsmith, Covaleski & Samuel, 2015:174). In this study, applying the grounded theory methodology implies that the researcher 'begin[s] with inductive logic, subject[s] data to rigorous comparative analysis, aim[s] to develop theoretical analyses, and value[s] grounded theory studies for informing policy and practice' (Charmaz, 2014:14-15).

This study conceptualises reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. The researcher thus anticipates that the conceptualisation of reliance could be useful to the real-world context of the internal and external auditing professions in several ways. The conceptualisation of reliance could inform the work of internal and external auditing standard setters, professional bodies and regulators when they review standards, develop training interventions or guidance documents and monitor the appropriateness of reliance practised, in line with the call of Bame-Aldred *et al.* (2013:280). Secondly, the conceptualisation of reliance could be useful when revising related, firm-specific, internal and external audit methodologies and training, as suggested by PCAOB (2013:29). External audit engagement partners, management, audit committees and internal auditors could use the conceptualised explanation of reliance in negotiations about reliance possibilities and practices, in line with the need identified by Petherbridge and Messier (2016:14), Desai *et al.* (2017:1) and Knechel (2016:215).

In terms of academic research, this study's conceptualised explanation of reliance transcends existing knowledge on this subject. Future studies about reliance could test the propositions in the conceptualised explanation of reliance, providing opportunity to modify the substantive theory. In addition, considering the adaptability (Charmaz, 2014:16) of the grounded theory methodology to the unique problems of diverse studies, this study's detailed account of its application advances the grounded theory methodology as a useful instrument for creating new knowledge in any field and context, including in studies dealing with the audit process.

Table 1.1 summarises the research design, methodology and knowledge created by the study compared to that of extant studies. Table 1.2 consolidates the methodology and original contributions of the study in relation to the methodologies of extant studies, real-world problems and knowledge gaps.

Table 1.1: Explicating the research design and methodology, and knowledge created by the study compared to extant studies

	Extant studies		This study	
	Method	**Knowledge created**	**Method**	**Knowledge created**
DESIGN	• Mostly positivist paradigm • Mostly quantitative / deductive approach	• Mostly deductive insights from testing *a priori* theories	• Interpretivism as paradigm • Qualitative approach	• Inductive insights from no use of *a priori* theories
METHODOLOGY	• Mostly experimental design • Mostly limited to testing relationships between reliance and preselected factors from extant knowledge and theories (*a priori* use of theory)	• Mostly fragmentary results indicating factors associated with reliance	• Classic grounded theory methodology	• A conceptualised explanation of reliance
DATA COLLECTED	• Mostly used external auditors as participants • A small number of studies used data from internal auditors and audit committee members	• Results mostly represented external auditors' opinions	• Intensive interviews performed with theoretical sensitivity • Theoretical sampling of the 'most knowledgeable people' at the most appropriate data sites (Glaser, 1978:45), specifically the chief financial officers, audit committee chairs, chief audit executives and external audit engagement partners involved in the statutory financial reporting and external audit processes of five diverse South African listed companies	• Insights from the perspectives of management, the audit committee and internal and external auditors

(cont. from previous page)	Extant studies		This study	
	Method	**Knowledge created**	**Method**	**Knowledge created**
DATA ANALYSIS	• Mostly experiments and quantitative analysis	• Mostly testing relationships between fragmentary factors influencing reliance	• Joint data collection, coding and analysis • Constant comparison and memo-writing • Emergence of a main concern and identification of a core category • Theoretical saturation and sorting • Integrating theoretical constructs as properties of the core category • Theoretical write-up • Comparing the new theory to extant knowledge and theories • Researcher subjectivity and reflexivity	• A substantive theory explaining how all stakeholder groups respond to their main concerns about practising reliance

***Source**: Own compilation*

Table 1.2: Consolidating the methodology and original contributions of the study in relation to the methodologies of extant studies, real-world problems and knowledge gaps

	Extant literature		**This study**	
	Methodology (see Bame-Aldred *et al.* (2013) for a synthesis)	**Real-world problems / Knowledge gaps** (see Bame-Aldred *et al.* (2013) for a synthesis)	**Methodology**	**Original Contribution**
OVERALL CONTRIBUTION TO THE BODY OF KNOWLEDGE ON RELIANCE	• Mostly *a priori* testing of relationships between preselected factors (usually related to the framework for reliance in external auditing professional standards) and reliance practised	• There is no conceptualised explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors	• Constructs a new substantive theory • Explains how the new substantive theory compares to and transcends existing knowledge, including relevant, existing formal theories	• Comparing the new substantive theory to existing knowledge, including relevant existing formal theories and explicating the novel contribution of this study (Glaser, 1978:9, 137, 138)
OVERALL METHODOLOGICAL CONTRIBUTION	• Mostly operationalised and reported on experiments	• Most studies have (1) solicited viewpoints about reliance practised from external auditors only; (2) used deductive methods, mostly experiments with external auditors, for testing relationships between variables (mainly originating from external auditing professional standards) in the reliance process; and (3) not transformed research findings into a comprehensive holistic explanation of reliance	• Operationalises the classic grounded theory methodology, using inductive and deductive reasoning for theory construction • Uses data from key participants from all stakeholder groups	• Explains the application of a methodology seldom used in the context of practising reliance, and indeed, auditing (Glaser, 1978; Glaser & Strauss, 1967)
PRACTICAL CONTRIBUTION TO PRACTISING RELIANCE	• Most studies added fragmentary insights about reliance	• Instances of inappropriate reliance by external auditors and dissatisfaction of non-external auditor stakeholder groups with reliance, manifesting as the stakeholder groups are having difficulty balancing assurance effectiveness and efficiency	• Explains how all stakeholder groups resolve their main concern about practising reliance	• Grounding the new substantive theory in empirical data ensures it is fit for purpose in practice, making it workable, relevant and modifiable (Glaser, 1978:4, 38, 134; Glaser & Strauss, 1967:2)

Source*: Own compilation*

1.8 DELIMITATIONS

Considering the scope of this study, a number of delimitations arises. Firstly, the focus is on external audit's reliance on internal audit work during statutory external audits. This study does not consider nor negate the other possible uses of internal audit work, as described in the definition of internal auditing (IIA, 2015a), the King Reports (IoDSA, 2016, 2009) and internal auditing professional standards (IIA, 2016).

Secondly, for the internal audit stakeholder group, the study participants were chief audit executives from in-house internal audit functions. Most of the site companies made use of co-sourced internal audit services, primarily from internal audit service divisions of Big 4 accounting firms (not the Big 4 accounting firm performing the external audit). However, as all the site companies had an in-house chief audit executive, this study did not include those performing co-sourced internal audit services as participants.

Thirdly, the study does not compare reliance in companies employing mostly 'career' internal auditors with relevant qualifications, aiming to remain in internal auditing, and companies using the internal audit function as a 'management training ground', rotating operational and management staff from the business into internal audit and back into the business to gain experience (Messier *et al.*, 2011:2137).

Fourthly, all individuals who participated in the interviews were familiar with the concept of practising reliance. Participants' subjective 'retrospective narratives' are accepted at so-called 'face-value', although the accuracy of interview data has generally come under scrutiny as '[w]hat people say may not be what they do, have done, and would do in the future' (Charmaz, 2014:78, 80).

Fifthly, this study is set in the private sector, particularly diverse South African listed companies.

Sixthly, the findings are derived from a process of exploration, interpretation and conceptualising of interview participants' 'retrospective narratives' (Charmaz, 2014:78). The researcher played an active role in all phases of the study, and together with the participants, co-constructed the interview data. However, following the grounded theory method, empirical evidence (data), and not logic, supports all reasoning underlying theoretical categories (Charmaz, 2014:345; Glaser & Strauss, 1967:5). The constructed substantive theory is therefore the product of the participants' and the researchers' constructions of meaning in a particular context and at a particular point in time (Charmaz, 2014:4). Other participants, researchers, contexts or times may produce different data, potentially requiring changes to the substantive theory.

Seventhly, the objective of the study was the construction of a substantive theory grounded in empirical data, not theory verification (Glaser, 1978:134).

1.9 BROADER RELEVANCE IN THE SOUTH AFRICAN CONTEXT

This study investigates reliance in South Africa. In comparison, most research has investigated reliance in other countries (evident from the synthesis of Bame-Aldred *et al.*, 2013). This study contributes insights addressing the paucity of research on reliance in the context of developing countries, as highlighted by Zain *et al.* (2015:135) and Mubako and Muzorewa (2019). Zain *et al.* (2015:135) maintain that globalisation and international trade demand comparability of corporate governance arrangements (for example, arrangements relating to internal audit) and the consistent application of external auditing standards (for example, relating to practising reliance) across national borders. It could, however, be argued that the maturity of business, corporate governance and auditing in South Africa highlighted in this section, make the lessons about practising reliance in the context of this emerging economy internationally relevant.

Considering the business sector, South Africa escaped the global financial meltdown relatively unharmed, largely due to conservative fiscal and monetary policies (South Africa.info, 2016; World Bank, 2016). The 2018 Global Competitiveness Report highlights South Africa's market size and well-developed financial system as strengths (WEF, 2018). South African businesses function in an established and carefully guarded legal system governing commercial activities, labour, competition, copyright, patents and trademarks in conformance with internationally recognised norms and standards (South Africa.info, 2016). The country has a dual economy, with a growing sophisticated financial and industrial economy functioning alongside a growing informal economy (South Africa.info, 2016; World Bank, 2016).

South Africa subscribes to internationally recognised governance and accountability institutions. Specifically, it was the second country in the world, after the United Kingdom, to introduce a formal code of corporate governance, generally known as the King Reports (IoDSA, 1994; Solomon, 2010). The most recent iteration, King IV, became effective for the financial period starting on or after 1 April 2017 (IoDSA, 2016:38). In an effort to showcase commitment to legitimised accountability in the world arena following years of apartheid, South Africa formally adopted the International Financial Reporting Standards (IFRS) in 2003/2004 (SAICA, 2009). In 2010, South Africa became the first country in the world with a mandatory integrated reporting requirement for listed companies (SAICA, 2011). The country's attention to corporate governance has inspired international recognition of its corporate reporting and governance strength (Solomon, 2010; IoDSA, 2009:6).

South Africa's statutory regulated external auditing profession is at the forefront of international auditing developments. The Independent Regulatory Board for Auditors (IRBA) regulates the external auditing profession in the country, in accordance with the Auditing Profession Act No. 26 of 2005. As an independent regulator, a maximum of 40% of IRBA board members may be registered auditors (IRBA, 2018a). The IRBA reports to the Minister of Finance, who appoints its board (IRBA, 2018a). The predecessor of IRBA, the Public Accountants' and Auditors' Board, adopted International Standards on Auditing (ISA) in 2004, making South Africa one of the first countries in the world to do so (Mail & Guardian, 2004). Reflecting its commitment to audit quality, the IRBA was one of the founding members of the International Forum of Independent Audit Regulators in 2008 (IFIAR) (IRBA, 2018a). From 2010-2011 to 2016-2017, the WEF consistently ranked South Africa first in the world out of 140 countries for the strength of its auditing and reporting standards (WEF, 2016; IRBA, 2015).

Unfortunately, recent indiscretions of some external auditors linked to alleged perpetrators of state capture of the South African government and government institutions, have tarnished the reputation of the external auditing profession in the country (Business Report, 2018). Consequently, South Africa slipped to 55th place in the Global Competitiveness Report 2018 for the strength of its auditing and reporting standards, scoring 4.9 out of 7 (WEF, 2018). In response to the volatility in South African auditing firms, the JSE amended its listing requirements, requiring the accreditation of audit firms and individual external auditors by the exchange (Business Tech, 2017). In addition, the IRBA board has adopted mandatory audit firm rotation every ten years, for implementation from 2023 (IRBA, 2018a).

The South African Institute of Chartered Accountants (SAICA) serves as the professional body for chartered accountants in the country. The Institute has different levels of membership agreements with accountancy professional bodies across the globe. These include reciprocal membership agreements (for example with Chartered Accountants Australia and New Zealand, CPA Canada and the Institute of Chartered Accountants of England and Wales), mutual recognition agreements (for example with the Institute of Chartered Accountants of Namibia) and pathway to membership agreements (for example with the accountancy profession in the United States of America and India). In certain jurisdictions, these agreements do not automatically give SAICA members audit rights, making conversion examinations necessary (SAICA, 2020).

A 2016 survey of SAICA showed that more than 75% of all JSE listed companies had chief financial officers or financial directors who were CAs(SA) (JSE Magazine, n.d.). Similarly, 80% of companies in the United States employ Big 4 accounting firms (Big 4 Accounting Firms, 2019). Academic research typically uses the Big 4 as a proxy for audit quality (Beisland, Mersland & Strøm, 2015:220; Schmidt & Wilkins, 2013:221). For example, based on their review of academic literature on audit quality, Knechel, Krishnan, Pevzner, Shefchik and Velury (2013:398, 403) highlight several indicators pointing to the superior quality of audits performed by Big 4 accounting firms. Specific benefits attributed to Big 4 accounting firms include comparatively less instances of significant earnings management by means of manipulated related party transactions than in companies employing non-Big 4 accounting firms (El-Helaly, Georgiou & Lowe, 2018:47). Moreover, it was found that 'the presence of a Big 4 auditor' reduced real earnings management (Choi, Choi & Sohn, 2018:2224). Consequently, the audit quality of the top 100 JSE listed companies is expectedly of a higher standard, as they have mostly employed Big 4 accounting firms.

The South African corporate governance regime, in line with international counterparts, recognises internal auditing's role in corporate governance (Adams, 1994). South Africa's first corporate governance code, *The King Report on Corporate*

Governance (King I) (IoDSA, 1994:21) emphasised the importance of internal audit as a corporate governance mechanism and recommended, *inter alia*, that every JSE listed company have an internal audit function.

The *King Report on Corporate Governance for South Africa 2002* (King II) (IoDSA, 2002:34) made an effective internal audit function a corporate governance principle for all South African companies. When companies did not have an internal audit function, King II required disclosure in the company's annual report of the full reasons for the non-adherence to the principle, including an explanation of alternatives to obtain assurance on the effectiveness of internal controls, processes and systems of the company (IoDSA, 2002:10). King II also recommended that internal audit functions coordinate their activities with other internal and external assurance providers to minimise duplication of assurance efforts (IoDSA, 2002:35).

The *King Report on Governance for South Africa 2009* (King III) (IoDSA, 2009) became effective on 1 March 2010. It contained extensive recommendations on the role of internal auditing in organisations. The ensuing *King IV Report on Corporate Governance for South Africa 2016* (King IV) (IoDSA, 2016:31) reiterates the 'pivotal' role of internal audit as an assurance provider to the organisation.

The internal auditing profession in South Africa is organised under the Institute of Internal Auditors South Africa (IIA SA), comprising eleven local regions and three regions in neighbouring countries (IIA SA, 2018). IIA SA strives to 'enhance the integrity, relevance and standing of the profession and the Institute, to the benefit of society and to provide outstanding service and valued products to its members' (IIA SA, 2018).

Focusing specifically on practising reliance, King III introduced the 'combined assurance model' in principle 3.5 (IoDSA, 2009:62). The aim of combined assurance was coordination of the assurance activities of management, and internal and external assurance providers, with oversight provided by the audit committee (IoDSA, 2009:62). King III declared that the aim of combined assurance was satisfying the audit committee's optimised assurance coverage by management, including risk management. Internal and external assurance providers (IoDSA, 2009:62).

The JSE listing requirements encapsulate South African corporate governance requirements. In particular, they mandate audit committee oversight of the integrity of the financial reporting function and annual financial reports as well as the effectiveness of internal financial controls (JSE, 2019: section 3.84, 16.10(u)). In addition, the listing requirements stipulate disclosure in a company's annual report and annual financial statements of 'the implementation of the King Code through the application of the King Code disclosure and application regime' (JSE, 2019: section 8.63(a)).

South African corporate governance recommends cooperation between internal and external audit. In particular, under principle 3.7 dealing with audit committee oversight of internal audit, King III recommends as best practice, cooperation between internal and external audit aimed at optimising their contributions to combined assurance by limiting assurance overlaps (IoDSA, 2009:63). King IV (IoDSA, 2016:31; part 5.4 recommended practice 46) retains the combined assurance model as a means of incorporating and optimising all assurance services and functions of an organisation to, *inter alia*, enable an effective control environment and support the integrity of the organisation's external reports.

Given that South Africa is a jurisdiction with globally recognised governance and accountability institutions, and given the emphasis in King III and IV on combined assurance, the insights from this study should be internationally relevant.

1.10 OUTLINE OF CHAPTERS

The structure of this thesis reflects the research process, as outlined below.

Chapter 1 introduces the study, specifically its importance and anticipated contributions. This is in the context of professional and governance pronouncements as well as over 40 years' academic research on reliance and its inability to prevent real-world problems. The chapter describes the research problem and states the consequent research aim, question and contributions in relation to real-world problems and related knowledge gaps.

Chapter 2 contextualises reliance, specifically what reliance is in relation the reciprocal influences of management's, the audit committee's and internal and external auditors' roles, interpretations, interests and practices in the statutory financial reporting and external audit processes *vis-à-vis* reliance.

Chapter 3 describes the design and methodology applied for theory construction, including the philosophical orientations, the role of the researcher, data collection, the analysis process, constructing the substantive theory and the norms for quality and rigour.

Chapter 4 describes the three phases of data coding and analysis, including the outcome of phase 1. An audit trail thereof is provided.

Chapter 5 presents the outcome of phase 2, the substantive categories developed from coded data.

Chapter 6 presents the outcome of phase 3, the substantive theory, using theoretical constructs grounded in the data. Then, compares the substantive theory to relevant existing theories, literature and professional standards.

Chapter 7 provides an overview of the research, reflecting on the rationale of the study, its contribution to literature, to research methodology in the field of reliance and to professional practice. The chapter also considers limitations and identifies avenues of future research.

1.11 LISTS OF ABBREVIATIONS AND KEY TERMS

The masculine form is used throughout, even when referring to female participants, in order to protect the identities of participants.

The clarity of the thesis requires a mutual understanding between reader and writer of the meaning of abbreviations and key terms used in relation to this study and the topic (Table 1.3) and the research method (Table 1.4).

Table 1.3: Abbreviations and key terms related to this study and reliance

Abbreviated form	What abbreviation represents
Ad hoc work for management (requests from management)	'From time to time, it's not uncommon for management to request internal audit's assistance to establish first-line controls or perform second-line risk management activities such as due diligence' (IIA, 2013:2) 'First line' refers to 'operating management', while 'second line' refers to 'risk and compliance functions' (IIA, 2013:2)
Appropriate reliance	External audit's audit opinion requires reliable, relevant and sufficient evidence, potentially including evidence-gathering from reliance on internal audit work (IAASB, 2018: ISA 500 paragraph 6, 7; PCAOB, 2013:2, 35)
Assurance effectiveness and efficiency	Include effectiveness (quality) and efficiency (effort and cost) of internal and / or external audit's work
Audit risk	The risk that the auditor expresses and inappropriate opinion when the financial statements are materially misstated (IAASB, 2018: ISA 200 paragraph 5)
Big 4 accounting firms	As 'the majority of the world's auditing services are performed by only four accounting firms', these firms 'known as the "Big 4" … completely dominate the industry' (Big 4 Accounting Firms, 2019)
Board	Board of directors of a company as defined in section 1 of the Companies Act (Republic of South Africa, 2008)
CAC	Chair of the Audit Committee
CAE	Chief Audit Executive (head of the internal audit function)
CAQ	Centre for Audit Quality
CA(SA)	Chartered Accountant (South Africa)
CBOK	Common Body of Knowledge Studies
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIA	Certified Internal Auditor
CISA	Certified Information Systems Auditor
COSO	Committee of Sponsoring Organizations of the Treadway Commission
Controls assurance work	Tests of controls 'to evaluate the operating effectiveness of controls in preventing or detecting and correcting, material misstatements at the assertion level' (IAASB, 2018: ISA 330 paragraph 4(b))
Direct assistance work	Refers to a form of reliance work, performed by internal auditors under the direction, supervision and review of the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 14 (b))
Engagement risk	The implicit risk of interprofessional reliance, specifically the risk of using unreliable, irrelevant or insufficient evidence produced by internal audit 'to modify the nature or timing, or reduce the extent, of procedures to be performed directly by the external auditor' (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13)

EP	Engagement partner (external auditor who signs the statutory audit report of a company)
F to F	Face-to-face (interviews)
FRC	Financial Reporting Council
IAASB	International Audit and Assurance Standards Board
IAF	Internal Audit Function
IAS	Head of Internal Audit Services at a Big 4 accounting firm (outsourced internal audit service provider)
IoDSA	Institute of Directors in Southern Africa
ICD Canada	Institute of Corporate Directors Canada
IFIAR	International Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
IIA	Institute of Internal Auditors
IIARF	Institute of Internal Auditors Research Foundation
IIA SA	Institute of Internal Auditors South Africa
IRBA	Independent Regulatory Board for Auditors
ISA	International Standard on Auditing
Inappropriate reliance	The external auditor's audit opinion relies on internal audit work providing unreliable, irrelevant or insufficient evidence (PCAOB, 2013:2, 35)
JSE	Johannesburg Securities Exchange
King I	*King Report on Corporate Governance in South Africa*
King II	*King Report on Corporate Governance for South Africa 2002*
King III	*King Report on Governance for South Africa 2009*
King IV	*King IV Report on Corporate Governance for South Africa 2016*
LESS reliance case(s)	A company or groups of companies where data from external auditors indicated that reliance was limited (companies A, C and D)
Management	Executive management – 'after the governing body, the highest decision-making authority in the organisation' (IoDSA, 2016:14)
Mid-tier A	Mid-tier accounting firm Head of Assurance
MORE reliance case(s)	A company or group of companies where data from external auditors indicated that reliance was not limited (companies B and E)
PCAOB	Public Company Audit Oversight Board
Participant(s)	Those representatives from all stakeholder groups directly involved in the statutory financial reporting and external audit process, who possess ultimate decision-making power and ultimate accountability for decisions about practising reliance, namely: - the chief financial officer (CFO) - chairperson of the audit committee (CAC) - chief audit executive (CAE)

	- external audit engagement partner (EP) In this study, ‘participants’ and ‘stakeholders’ interchangeably refer to interviewees
Peripheral support by internal auditors	External auditors use peripheral support by internal auditors, also known as ‘indirect reliance on tangential IAF [internal audit function] work’ (Bame-Aldred *et al.*, 2013:255) Such support work does not produce external audit evidence
Reliance / practising reliance / reliance practised	Refers to using internal audit work ‘to modify the nature or timing, or reduce the extent, of procedures to be performed directly by the external auditor’ on a statutory audit (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13), thus incorporating internal audit work into external audit evidence
Reliance work	Refers to two types of reliance work that are incorporated into external audit evidence, namely: (i) work performed in the normal course of an internal audit, and (ii) “direct assistance work” performed by internal auditors under the direction, supervision and review of the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13)
SAICA	South African Institute of Chartered Accountants
SA	South Africa
SOX	Sarbanes Oxley Act
(All) Stakeholder(s) or (all) stakeholder group(s)	Stakeholder(s) or (a) stakeholder group(s) include corporate governance mechanism(s) whose roles, interpretations, interests and practices in the statutory financial reporting and external audit processes provide the context of their individual and reciprocal influences on reliance, specifically: - the chief financial officer (CFO) and executive management (management) as a group - the audit committee chair (CAC) and the audit committee as a group - the chief audit executive (CAE) and internal auditors as a group - the engagement partner (EP) and external auditors as a group
Standard(s)	International Standards for the Professional Practice of Internal Auditing
WEF	World Economic Forum

Source*: Own compilation*

Table 1.4: Abbreviations and key terms related to the research method

Abbreviated form	What abbreviation represents
Category	An analytic (abstract) concept subsuming a single significant code or several codes with common meaning (Charmaz, 2014:341).
Code	A short label depicting what is happening in data (Charmaz, 2014:341).
Concept	Glaser (1978:43) refers to the combination of a category and its properties as a 'concept'. The term denotes a single mental unit, abstracted from integration of similar categories (Locke, 2007:881).
Dimension	Attribute of a property; could distinguish between top and bottom position of a range for a specific property; 'a range of measurements' (Locke, 2007:881).
Property	'Defining characteristics or attributes of a category', including its definition, boundaries and relevance, determined from analysis of data and codes (Charmaz, 2014:344).
Theoretical construct	A term used in this study to differentiate the theoretical concepts making up the substantive theory. The term denotes a conceptualisation of multiple related properties of the core category into a single unit.

***Source**: Own compilation*

1.12 ANNEXURES

The following annexures support this thesis:

Annexure A Interview guide

Annexure B Ethical approval

Annexure C Letter of introduction

Annexure D Background of the study

Annexure E Letter of consent

1.13 CONCLUSION

This chapter spelled out the research problem, aim, question and outcome of the study, after having considered reliance as a complex practice, encumbered by real-world problems and knowledge gaps which persist despite almost 40 years' professional and governance pronouncements and academic research. Specifically, this study responds to the lack of a conceptualised explanation of reliance, considering the reciprocal influences of all stakeholder groups' roles, interpretations, interests and practices. The chapter contains a motivation for using the classic grounded theory methodology and explicates anticipated practical, theoretical and methodological contributions, within the boundaries of its delimitations. The chapter furthermore reflects on the relevance of the study in the wider context of auditing practice and literature before concluding with lists of abbreviations, key terms and a list of annexures.

Next, Chapter 2 contextualises reliance.

CHAPTER 2

CONTEXTUALISING RELIANCE

CHAPTER 2

CONTEXTUALISING RELIANCE

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2.1 INTRODUCTION

Chapter 1 introduced this classic grounded theory study investigating reliance by external auditors on internal audit work during statutory external audits.

This chapter uses the literature to contextualise reliance. Although including a literature review chapter in a grounded theory study is unconventional, Suddaby (2006:634) points out that grounded theory is no excuse for ignoring the existing literature in the substantive field. He advises the researcher to 'achieve a middle ground between a theory-laden view of the world and an unfettered empiricism' (Suddaby, 2006:635).

The literature discussed here provides a general contextual perspective on reliance and should not be seen as representing *a priori* theory (Glaser, 1978:45).This chapter was written after completion of data collection and analysis when the researcher's general perspective on reliance was unstructured and served solely as a referential starting point of theoretical sensitivity (Charmaz, 2014:159; Glaser, 1978:39). At the time of data collection and analysis, the researcher's general perspective on reliance was unstructured and as such did not determine the study's substantive categories. All substantive categories developed in Chapter 5 are grounded in empirical data (Glaser, 1978:55). Consequently, this chapter follows the outline of the conceptualisations of reliance grounded in this study. Positioning this chapter in the front of the thesis affords readers a contextual understanding of reliance from the perspective of legal, governance and professional requirements and related literature.

First, the section on *what reliance is* considers the ways in which reliance is possible. Then, the foundational conditions of reliance are presented, considering influences on reliance by the distinct roles of internal and external audit determining the overlap between internal and external audit work, the relevance and credibility of internal audit work for statutory audit purposes and external audit quality and the external auditor's liability. Thereafter the operational conditions of reliance consider requirements for integrating and aligning internal and external audit work.

The complexity of reliance is discussed in the section dealing with reciprocal influences on reliance by management's, the audit committee's and internal and external auditors' roles, interpretations, interests and practices in statutory financial reporting and external audit processes. This is in relation to their influences on contextual, foundational and operational conditions of reliance. Although each stakeholder groups' influences are presented separately, their reciprocal influences on each other and on reliance are highlighted throughout the section. Lastly, the combined assurance concept is considered. Throughout the chapter discussion points included in the interview guide are linked to the discussion.

2.2 WHAT RELIANCE IS

This section contextualises *what reliance is*, considering the ways in which reliance is possible. In accordance with external auditing professional standards (IAASB, 2018: ISA 315 (Revised); ISA 610 (Revised 2013)), external auditors can use internal audit work in three ways. First, when internal audit is present in an organisation, the external auditor should annually gather information from internal audit. This information guides the external auditors' understanding of the organisation and its environment and the identification and assessment of the risk of material misstatement of financial statements (IAASB, 2018: ISA 315 (Revised) paragraph A9). Typical ways of gathering information include enquiries of internal auditors, reviewing the internal audit mandate, strategy and planning documents and the internal audit plan and/ or internal audit reports (IAASB, 2018: ISA 315 (Revised) paragraph A10, A116). Information is gathered from internal audit irrespective of planned incorporation of internal audit work into external audit evidence. This is not reliance work.

Second, when appropriate, the external auditor may incorporate work performed in the normal course of an internal audit into external audit evidence (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13). This is reliance work.

Third, unless prohibited by law or regulation, the external auditor may incorporate evidence from direct assistance work performed by internal auditors under the direction, supervision and review of the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13) into external audit evidence. This is reliance work.

External auditors may also use peripheral support by internal auditors, for example, for drawing audit samples or mapping processes. This type of assistance does not produce external audit evidence, thus, it is not reliance work. Bame-Aldred *et al.*

(2013:255) refer to the use of such work as ‘indirect reliance on tangential IAF [internal audit function] work’.

In this study, the term “reliance work” refers to (i) work performed in the normal course of an internal audit, and (ii) “direct assistance work” performed by internal auditors under the direction, supervision and review of the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13) that are incorporated into external audit evidence.

External audit evidence should be sufficient and appropriate, considering the risk of material misstatement of the financial statements (IAASB, 2018: ISA 200 paragraph13(b)). The appropriateness of audit evidence is assessed by determining its relevance and reliability in the circumstances (IAASB, 2018: ISA 500 paragraph A5). Thus, when internal audit work is incorporated into external audit evidence, meaning it forms an integral part of audit evidence on the statutory audit, the external auditor evaluates its relevance and reliability. External audit evidence is relevant when there is a ‘logical connection’ between the audit procedure and the objective of the test (IAASB, 2018: ISA 500 paragraph A27). Reliability of audit evidence refers to the credibility of the source and the nature of evidence ((IAASB, 2018: ISA 500 paragraph A31).

In line with these ways in which reliance is possible, the interview guide included the following discussion points for determining reliance and reliance work.

LINK TO DISCUSSION POINTS IN INTERVIEW GUIDE

Determining reliance and reliance work

DISCUSSION POINT 3: What are your views on external auditor use of the work of internal auditors for purposes of the external audit of a large listed company?

DISCUSSION POINT 5: How do you view the changes over the past five years in external auditors' use of internal audit function work of a large listed company? How do you expect it to change in future?

DISCUSSION POINT 11: Does your external auditor use your organisation's internal auditors as direct assistants on external audits and what motivates them to do so?

DISCUSSION POINT 12: Does your external auditor use work performed by your organisation's internal auditors for the external audit and what motivates them to do so?

2.3 FOUNDATIONAL CONDITIONS OF RELIANCE

The ISA includes a framework that sets out foundational conditions influencing reliance (IAASB, 2018: ISA 610 (Revised 2013)). These conditions apply when the external auditor expects that reliance will modify the nature or timing or reduce the extent of audit procedures performed directly by the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13), upon incorporating internal audit work into external audit evidence. These conditions ensure the appropriate nature and extent of reliance. This mitigates the risk of 'over or undue use' of internal audit work considering the external auditor's sole responsibility for the audit opinion, irrespective of reliance (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). Foundational conditions consider the distinct roles of internal and external audit determining the overlap between internal and external audit work as well as the relevance and credibility of internal audit work for statutory audit purposes (IAASB, 2018: ISA 315 (Revised) paragraph 23, A113-120); ISA 610 (Revised 2013) paragraph 15-16; 26-28). They also consider external audit quality and the external auditor's liability (IAASB, 2018: ISA 200 paragraph 5; 610 (Revised 2013) paragraph 17-19; 29-30).

2.3.1 Distinct roles of internal and external audit determining the overlap between internal and external audit work

Despite the mostly distinct roles of internal and external audit, internal and external auditing professional bodies have recognised the potential for practising reliance for the past 50 years (Brown, 1983:444). By implication, the professional bodies convey that overlap between internal and external audit work does exist. External auditing professional standard ISA 315 (Revised) paragraph A113 to 117 (IAASB, 2018), recognise the distinct roles of internal and external audit, particularly that reliance work is limited to internal audit work dealing with an organisation's financial reporting.

The IIA (2017:3) acknowledges that 'there are distinct differences in the roles, and certainly in the boundaries of the work that [internal and external audit] perform'. These differences 'are often under-recognized, and are perhaps even misunderstood and confused by stakeholders'. Statutory external audits focus exclusively on financial reporting (IAASB, 2018: ISA 200; Republic of South Africa, 2008: section 30(2)). In contrast, the focus of internal audits is not legislated or prescribed, meaning that it is organisation-specific (IIA, 2015a). Consequently, internal audit's work with a financial focus could fluctuate annually, in accordance with the scope and focus of work specified in the internal audit charter (CIIA, 2018:1 – 3; IoDSA, 2016: part 5.4 recommended practice 49; Christ *et al.*, 2015:47; IIA, 2015a; Lenz & Hahn, 2015:17). The literature highlights that the boundaries of reliance work can be misunderstood, considering the context-specific focus of internal audit work (Roussy & Brivot, 2016:714; Lenz & Hahn, 2015:26). This could cause disagreement between stakeholder groups about the fairness of reliance.

While the potential of reliance implies overlap between internal and external audit work, the distinct roles of internal and external audit and the context-specific focus of internal audit work means that overlap is not fixed. Confirming this overlap, the literature refers to reliance as 'internal audit['s] contribution to external audit' (Zain *et al.*, 2015), 'using the work of internal auditors' (IAASB, 2018:ISA 610 (Revised 2013)), 'reliance' (*c.f.* Bame-Aldred *et al.*, 2013), 'the interface between internal and external auditors' (Pilcher *et al.*, 2013; Brody, Golen & Reckers, 1998), 'internal audit assistance' (Abbott, Parker & Peters, 2012b), a 'joint audit approach' (Sarens *et al.*, 2009:90) and 'substitution between monitoring devices' (Ettredge *et al.*, 2000:57) when reporting research findings.

Over the last 15 years, several non-academic publications have re-emphasised the importance of effective and efficient external audits, considering coordination of the overlap between internal and external audit work within the context of the interrelated yet distinct roles of internal and external audit. These publications originated from the regulator of external auditors performing public interest audits in the United States of America (PCAOB, 2013; 2006), the international standard setter of the external auditing profession (IAASB, 2012), the United States-based global body advancing external audit quality and the United States-based global professional body for internal auditors (CAQ & IIA, 2015), the regulator of the external audit profession in the United Kingdom (FRC, 2016) and the Institute of Directors in Southern Africa (IoDSA, 2009, 2016).

Publications reveal two contrasting messages about reliance. On the one hand, the message encourages that (i) overlap between internal and external audit work should be minimised (IoDSA, 2009:62, 63), (ii) a 'constructive and complementary relationship between external and internal auditors including, where appropriate, the possibility of coordination and cooperation', could benefit external audit quality (IAASB, 2012:5) and (iii) from 2006, the focus of PCAOB inspections of external auditors' integrated audits (consisting of both an audit of internal control over financial reporting and a statutory audit of financial statements), changed, considering, in addition to effectiveness, also efficiency, particularly the 'efficient' use of 'the work of others' (including internal auditors) (Petherbridge & Messier, 2016:4; PCAOB, 2006:1). On the other hand, the message cautions that (i) the complexity of reliance decisions and knowledge gaps from the paucity of research on the effect of reliance on external audit quality (for example Bame-Aldred *et al.*, 2013:251) complicate reliance, (ii) reliance might constitute a 'key audit matter' requiring disclosure in statutory external auditors' reports (FRC, 2016:5), (iii) 'cautionary language' in ISA

610 (Revised 2013) (IAASB, 2018) aims to prevent ‘extensive use’ of internal audit work by external auditors which regulators view as ‘inappropriate’ (IAASB, 2012:4, 5) and (iv) disagreement about the fairness of reliance increased relational tension between the stakeholder groups (CAQ & IIA, 2015:9).

Recognising the controversy, IAASB (2012:5) urged ‘a balanced approach’ to reliance, taking into account the ‘pitfalls of over and undue’ (inappropriate) as well as potential ‘advantages’ (efficiency) of practicing reliance ‘where appropriate’. However, from their study focused on external auditors’ reliance decisions, Petherbridge and Messier (2016:14) speculate that external auditors ‘may not be able to operationalize how to “balance” the trade-off of efficiency and effectiveness’ required for ‘a balanced approach’ to reliance. Likewise, while the IIA asserts that total audit efforts improve when internal and external audit work together (IIA, 2017:7), the potential for not only substituting but also complementing each other’s work is underlined (IIA, 2017:3).

Overlapping internal and external audit work creates opportunities for substituting and complementing each other. By example, internal and external audit quality (effectiveness) could improve when knowledge shared complements each other’s knowledge of the business (Quick & Henrizi, 2018:2). In addition, internal and external audit efficiency could improve when the teams use each other’s overlapping work to substitute their own work (Quick & Henrizi, 2018:2). Some authors point out that audit committees value wider assurance from increased audit effort when internal and external audit’s work mutually complements rather than substitutes each other (Sarens *et al.,* 2009:102). However, Libby, Rennenkamp and Seybert (2015:38, 40) caution that increased efforts may merely increase the appearance of quality rather than actual quality.

The interview guide included the following discussion points, in line with the influence on reliance by the distinct roles of internal and external audit determining the overlap between the two functions.

LINK TO DISCUSSION POINTS IN INTERVIEW GUIDE

Influence on reliance by the distinct roles of internal and external audit determining the overlap between internal and external audit work in an organisation

DISCUSSION POINT 1: What are your general views on the role of an internal audit function in an organisation?

DISCUSSION POINT 2: How do you view the changes over the past five years in the role of an internal audit function in a large listed company?

2.3.2 The relevance of internal audit work for statutory audit purposes

A foundational condition for audit evidence, and thus reliance, is the relevance of internal audit work for statutory audit purposes (IAASB, 2018: ISA 315 (Revised) paragraph 23, A113-120; ISA 500 paragraph 6). The scope and focus of internal audit's mandate – set out in the audit committee approved internal audit charter (IIA, 2016: Standard 1000, Standard 2010.A2) and operationalised in the internal audit plan – determines the relevance of internal audit work for statutory audit purposes (IAASB, 2018: ISA 315 (Revised) paragraph A114, A116).

Internal audit's mandate may include a fluctuating configuration of assurance and consulting work, covering a varying combination of governance, risk management and internal control work with an operational versus financial focus (IIA, 2015a). Internal auditing professional standards and corporate governance principles require internal audits with a risk focus (IIA, 2016: Standard 2010; IoDSA, 2016: part 5.4 recommended practice 58). Management and the chief audit executive negotiate internal audit's charter, mandate and plans, while the audit committee provides oversight to support the independence of internal audit and ensure realistic internal audit resourcing (IoDSA, 2016: part 5.4 recommended practice 50-51). The chief audit executive manages the internal audit plan, including the related expectations of management, the board and other stakeholders as well as requests for consulting engagements (IIA, 2016: Standard 2010).

2.3.3 The credibility of internal audit work for statutory audit purposes

Reliance implies incorporating internal audit's reliance work into external audit evidence. A foundational condition for audit evidence and thus reliance work is reliable evidence (IAASB, 2018: ISA 610 (Revised 2013) paragraph 23; ISA 500, paragraph 6). Reliance is influenced by the outcome of external audit's assessment of the credibility of internal audit work for statutory audit purposes, considering internal audit's organisational status and objectivity, competence and performance (IAASB, 2018: ISA 610 (Revised) paragraph 16; 28). Various academic studies have used proxies to measure factors in attempts to rank the relative significance of these influences on reliance. However, the findings were inconclusive (Al-Sukker, Ross, Abdel-Qader & Al-Akra, 2018; Lee & Park, 2016; Pizzini *et al.*, 2015; Pilcher *et al.*, 2013; Desai & Desai, 2010; Krishnamoorthy, 2001; Messier & Schneider, 1988; Brown, 1983).

There are various explanations for the absence of a definitive ranking of factors influencing the credibility of internal audit work for statutory audit purposes. Concerning internal audit, it functions within an organisation, influenced by practices of management, including risk management, and the audit committee. These influences affect the credibility of internal audit work. Considering reliance, a multitude of factors requiring simultaneous consideration, complicates decision-making about reliance (Singh *et al.*, 2014:36; Bame-Aldred *et al.*, 2013:282-283; Brody, 2012:11; Desai *et al.*, 2010:538; Krishnamoorthy, 2001:499; 513; Maletta, 1993:508; Edge & Farley, 1991:77). As an example of simultaneous factors having a reciprocal influence on the credibility of internal audit work, Sarens and Lamboglia (2014:56) suggest that co-sourcing or outsourcing could overcome misfits between internal audit resourcing, for example, competence and planned internal audit work.

Complexity causes inconsistencies in external auditors' reliance decisions when various factors have opposing reciprocal influences on the credibility of internal audit work (Desai *et al.*, 2017:1). Trotman and Duncan (2018:253) explain that 'high quality inputs [into internal audits], while necessary for high quality processes, do not necessarily result in high quality processes, outputs, or outcomes [from internal audits]'.

2.3.4 External audit quality and the external auditor's liability

External audit quality is influenced by the quality of the evidence gathering process and the quality of the evidence produced. The aim of professional obligations and regulation of the auditor is to promote external audit quality. However, there are differences in the internal and external auditing professions' requirements and regulation. This section describes the differences and how they could influence reliance.

2.3.4.1 External audit quality considering the relevance and credibility of internal audit work for statutory audit purposes

External auditors' decisions about the nature and extent of reliance should remain cognisant of the profession's requirements for external audit quality. External auditors should express 'reasonable assurance' about the disclosures in the statutory financial reports (IAASB, 2018: ISA 200 paragraph 5). Reasonable assurance requires 'sufficient appropriate audit evidence to reduce audit risk [the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated] to an acceptably low level' (IAASB, 2018: ISA 200 paragraph 5).

When practising reliance, the external auditor determines the sufficiency and appropriateness of audit evidence provided by reliance work by considering the scope and focus of internal audit work; the subjectivity and risk of judgements, audit areas and audit procedures; the organisational status, objectivity and competence of internal audit; the sufficiency of the external auditor's involvement in the audit; the nature and extent of the external audit team's direction, supervision and review of internal audit's direct assistance work; the appropriateness of internal audit's conclusions about reliance work; and the outcomes of external audit's reperformance procedures on reliance work (IAASB, 2018: ISA 610 (Revised 2013) paragraph 17-24, 26-34; IAASB, 2012:4-5). Throughout the audit, the external auditor remains alert for indicators rendering decisions about the nature and extent of reliance inappropriate (IAASB, 2018: ISA 610 (Revised) paragraph 25).

Academic research maintains that external auditors' reliance decisions consider the subjectivity inherent in internal audit's reliance work (for example, Quick & Henrizi, 2018:25; Glover et al., 2008:193). External auditors prefer relying on internal audit's controls work rather than substantive procedures, as audit procedures on and conclusions about the effectiveness of controls are usually more objective (Glover *et al.*, 2008:198; DeZoort *et al.*, 2001:270; Margheim, 1986:202). In addition, circumstantial evidence about reliance experiences in previous audits in an organisation influenced external auditors' decisions (Quick & Henrizi, 2018:25). Particularly, more intense collaboration and communication between internal and external auditors in previous years increased the extent of reliance in the subsequent year (Quick & Henrizi, 2018:25).

The interview guide included the following discussion points, in line with the foundational influences of the relevance and credibility of internal audit work for statutory audit purposes on external audit quality.

LINK TO DISCUSSION POINTS IN INTERVIEW GUIDE

Determining influences on reliance of the relevance and credibility of internal audit work for statutory audit purposes

DISCUSSION POINT 6: What do you perceive as important considerations for your external auditor's initial decision whether or not to use the work of your IAF for the external audit?

DISCUSSION POINT 7: What are your views on the status of your IAF and how do you contribute to that status?

DISCUSSION POINT 8: What are your views on the objectivity of your IAF and how do you contribute to that objectivity?

DISCUSSION POINT 9: What are your views on the sufficiency of your IAF's competence and resources to fulfil the required duties and how do you contribute thereto?

DISCUSSION POINT 10: What are your views on your IAF's work performance and what role do you play in this regard?

2.3.4.2 Internal versus external auditors' liability

The external auditor makes the reliance decision and carries sole responsibility for the audit opinion, irrespective of reliance (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). Studies have concluded that external auditors are generally willing to practise 'some degree' (Quick & Henrizi, 2018:25) or 'a moderate extent' (Margheim, 1986:199) of reliance, or that internal audit's contribution to the external audit 'is rather low' (Zain *et al.*, 2015:139-140). Research ascribes reliance to expectations created by pronouncements and standards, for example, by the PCAOB (2013) and IAASB (2012) (Quick & Henrizi, 2018:25).

The philosophical, professional and regulatory premises of the internal versus external auditing profession influence concerns as to external audit quality and the external auditor's liability inherent in reliance. In their seminal work, Mautz and Sharaf (1961:49) highlight that 'the professional status of the independent auditor imposes commensurate professional obligations'. In line with the latter notion, academic studies report that legal consequences result when external auditors forego their professional obligations when practising reliance. For example, judges assign greater liability for an alleged audit failure to external auditors who practised reliance than to those who did not (Arel, Jennings, Pany & Reckers, 2012:516). Apparently, judges perceive that reliance reduces external audit quality. Comparing the internal and external auditing professions' 'professional obligations' could explain these verdicts.

First, the professional liability of internal and external auditors differs. The external auditor's assurance and reporting duties and commensurate legal liability for improper conduct are statutorily sanctioned by the Auditing Professional Act (Republic of South Africa, 2005: section 44, 46 and 48) and the Companies Act (Republic of South Africa, 2008: section 30, 90-93). In contrast, internal auditors' duties and related liability are not controlled by specific legal requirements. Rather, internal audit's charter, mandate and plans are negotiated between management and the chief audit executive and approved by the audit committee (IoDSA, 2009: principle 7.4).

Second, the auditor should act 'exclusively in the capacity of an auditor' (Mautz & Sharaf, 1961:49), thus independence requirements are implied in the 'commensurate professional obligations' of an auditor (IAASB, 2018: ISA 200 paragraph 14; IIA, 2016: Standard 1100). The external auditing profession's code of conduct (for example, IRBA, 2018b, section 600) prescribes detailed objectivity and independence requirements, including about the provision of non-assurance services to an audit client. Compliance with independence requirements is monitored through the regulator's inspections and non-compliant auditors are disciplined. In contrast, internal audit's typical 'dual role' (Gramling, Maletta, Schneider & Church, 2004:240) comprises a combination of assurance and consulting work, as defined by the profession (IIA, 2015a). Academic research reports that when internal auditors perform such a dual role, their objectivity is questionable and reliance decreases (Munro & Stewart, 2010:371, 385).

Third, the ‘commensurate professional obligations’ of an auditor require compliance with applicable professional standards (IAASB, 2018: ISA 200 paragraph 18-20; ISA 700:28; IIA, 2016:1). The external auditor should comply with all ISA relevant to the statutory external audit and declare such conformance in the auditor’s report (IAASB, 2018: ISA 200 paragraph 18-20; ISA 700:28). External auditors who express an unqualified external audit opinion have a legal duty to comply with all applicable ISA relating to the conduct of an audit (Republic of South Africa, 2005: section 44 (3) (a)). External auditors are disciplined if monitoring inspections by the IRBA identify any instances of non-compliance with ISA (Republic of South Africa, 2005: section 46).

In contrast, while the IIA issues International Standards for the Professional Practice of Internal Auditing (Standards) (IIA, 2016), which it describes as ‘principle-focused, mandatory requirements’ (IIA, 2016:1), actual compliance with the Standards is low to average (see Lenz, Sarens & Jeppesen, 2018:13 for a summary of research findings in this regard). Reflecting on the importance of internal auditors’ adherence to professional standards, Lenz *et al.* (2018:12) point out that ‘professional norms’, like the Standards, are critical drivers of professional identity and behaviour given the absence of statutory sanction mandating internal audit.

Furthermore, a comparison of the two professions’ standards reveals that the ISA are more comprehensive and prescriptive than the Standards. By way of example, the ISA include a dedicated standard on reliance, comprising 23 pages (IAASB, 2018: ISA 610 (Revised 2013)). In contrast, a general standard and three practice advisories deal with sharing information and coordinating activities with ‘other internal and external providers of assurance and consulting services’ (IIA, 2016: Standard 2050; IIA, 2015b: Practice Advisory 2050-1, 2050-2, 2050-3). Combined, these documents consist of eight pages.

Fourth, attributes of a profession include the regulation of members’ compliance with professional standards and a code of conduct (Segon, Booth & Pearce, 2018:7; Mautz & Sharaf, 1961:49; Goode, 1957:194). Independent regulators perform periodic inspections, monitoring external auditors’ compliance with ISA, the profession’s code of conduct and legislation (for example, IRBA, 2019;1; 2018b:12-15; Knechel, 2016:215; Samsonova-Taddei & Siddiqui, 2016:183; Baker, Bédard & Prat dit Hauret, 2014:371; Republic of South Africa, 2005: section 46). Non-conforming external auditors face disciplinary action, including further investigation, suspension and / or legal action (for example, IRBA, 2019:5). A body of case law is testimony of legal action against external auditors for alleged failure to honour their 'commensurate professional obligations' (Simpson, 2018). In contrast, internal auditors' compliance with professional standards and ethical requirements is not regulated (CIIA, 2018:3), thus related case law does not exist (Simpson, 2018).

Fifth, a foundational premise of audits is 'no conflict of interest between the auditor and the management of the enterprise under audit' (Mautz & Sharaf, 1961:49). However, independence is controversial for internal auditors who function in a service department within an organisation (reviewed by Dal Mas & Barac, 2018:812), away from independent scrutiny, other than audit committee oversight. When management influence the scope of internal audit work (Lenz *et al.*, 2018:28; Pilcher *et al.*, 2013:335) or demand censoring of internal audit reports (Roussy, 2015:259, 260), internal audit quality is compromised. Although audit committee oversight should address threats to internal audit's independence and objectivity (Abbott, Parker & Peters, 2010:2), symbolic oversight would not mitigate threats (Brennan & Kirwan, 2015:466).

Sixth, information should be 'verifiable' (Mautz & Sharaf, 1961:49). The ISA provide clear requirements and lengthy guidance on the attributes of sufficient appropriate audit evidence (IAASB, 2018: ISA 200 paragraph 17; ISA 500). In contrast, the introduction and glossary to internal auditing professional standards refer to 'an objective examination of evidence', without specifying requirements for such evidence (IIA, 2016:4, 22).

The interview guide included the following discussion point, in line with the potential influence on reliance by concerns for external audit quality and the external auditor's liability.

LINK TO DISCUSSION POINT IN INTERVIEW GUIDE

Determining the influence of reliance on external audit quality and the external auditor's liability

DISCUSSION POINT 4: How do you view the impact of external auditors' use of internal auditors' work on the external audit?

In summary, the foundational conditions of reliance are not a clinical list of objective rules. Considerable leeway for interpretation and subjectivity could result in diverse interpretations of their relative importance and how their reciprocal influences on reliance should be evaluated, thereby increasing the complexity of reliance.

2.4 OPERATIONAL CONDITIONS OF RELIANCE

Internal and external auditing professional standards include operational requirements and guidance for reliance (IAASB, 2018: ISA 315 (Revised); ISA 610 (Revised 2013); IIA, 2016: Standard 2050; IIA, 2015b: Practice Advisory 2050). A comparison of the two professions' requirements and guidance reveal similarities and differences.

First, Practice Advisory 2050-1 (IIA, 2015b) places the responsibility for coordinating internal and external audit work on the chief audit executive and recommends the chief audit executive seek board support in the process. The ISA emphasise that the external auditor has sole responsibility for all decisions involving reliance (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11).

Second, Practice Advisory 2050-1 (IIA, 2015b) recognises that internal audit may rely on external audit work falling within the scope of planned internal audits to eliminate duplication. ISA does not mention reliance by internal audit on external audit work. Academic research acknowledges potential mutual benefits for internal and external audit effectiveness and efficiency arising from reliance (Quick & Henrizi, 2018:2).

Third, when internal audit relies on external audit work, the chief audit executive should assess the appropriateness of such work for internal audit purposes by obtaining an understanding of the work performed and reviewing external audit's audit programmes and working papers (IIA, 2015b: Practice Advisory 2050-1). Similarly, when external audit intends to rely on internal audit work, the chief audit executive should provide them with information on internal audit work performed as well as access to all internal audit's work programmes, working papers and internal audit reports (IAASB, 2018: ISA 610 (Revised) paragraph 22; IIA, 2015b: Practice Advisory 2051-1).

Fourth, internal and external auditors should engage in timeous alignment planning to support efficient and timely completion of audit work (IAASB, 2018: ISA 610 (Revised 2013) paragraph 21; IIA, 2015b: Practice Advisory 2051-1). Alignment may include adjusting the nature, timing and / or scope of internal and / or external audit's individual planned audit work (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13; IIA, 2015b: Practice Advisory 2051-1). Sharing critical information between the two audit teams, particularly all reports and conclusions of the two audit functions as well as management's responses, informs their individual risk assessments, audit programmes and conclusions (IAASB, 2018: ISA 315 (Revised) paragraph A120, ISA 610 (Revised 2013) paragraph 22; IIA, 2015b: Practice Advisory 2051-1). The ISA require continuous communication between internal and external auditors to foster an environment which encourages internal audit to share critical information with external audit (IAASB, 2018: ISA 315 (Revised) paragraph A120). However, ISA do not refer to external audit sharing critical information with internal audit. External audit documentation should capture the procedures, conclusions and outcomes related to reliance (IAASB, 2018: ISA 610 (Revised 2013) paragraph 36-37).

Academic research dealing with operational conditions influencing reliance is rare. In a recent study considering how external auditors operationalise reliance, Pike, Chui, Martin and Olvera (2016:159) report an association between external auditors' involvement in the internal audit plan and reliance on internal audits' control work. Such involvement in the internal audit plan reduces external audit's time, budgets and planned level of reperformance of some of internal audit's work, even after discovering internal control weaknesses pointing to a deficiency in internal audit's work (Pike *et al.*, 2016:170). In the study of Zain *et al.* (2006:1), chief audit executives reported that reliance was influenced by the extent of audit committee oversight of internal audit's work programmes and coordination between the two functions. Pilcher *et al.* (2013:336) furthermore observe that poor communication between internal and external auditors cause ineffective alignment of internal and external audit work and less reliance.

The interview guide for this study included the following discussion point, in line with the influences of operational conditions on reliance.

LINK TO DISCUSSION POINT IN INTERVIEW GUIDE

Determining operational conditions influencing reliance

DISCUSSION POINT 15: How does the relationship between your company's external audit team and internal auditors influence use of internal auditors' work for the external audit?

2.5 STAKEHOLDER GROUPS' RECIPROCAL INFLUENCES ON RELIANCE

To understand the complex context of reliance, clarity is required on the roles, interpretations, interests and practices of the stakeholder groups (management, the audit committee and internal and external auditors) influencing statutory financial reporting and external audit processes. Reliance occurs within the statutory financial reporting and external audit processes; thus, it is influenced by these processes. The aim of this section is to provide a broad understanding of each stakeholder groups' roles, interpretations, interests and practices influencing reliance in the context of their reciprocal influences on each other and on reliance.

2.5.1 Management

Management's dominant role, interpretations, interests and practices as agents responsible for all business activity and the statutory financial reporting process have a pervasive influence on the foundational conditions of reliance. This section considers key influences.

2.5.1.1 Management's roles

Management has a dual role. In their primary role, management set organisational strategies. Management then formulate and implement policies and operational plans giving effect to those strategies (IoDSA, 2016:21). Management's secondary role requires the timely preparation and issue of independently assured, fair annual statutory financial reports (IoDSA, 2016: part 5.2; Republic of South Africa, 2008: section 30). This secondary role represents a key mechanism by which shareholders hold management accountable (Brennan & Solomon, 2008:887). Pointing out a reciprocal benefit from reliance, academic research indicates that timely reporting by management, which implies the external audit deadline was met, benefits from reliance. This benefit arises when reliance is placed on work performed in the normal course of internal audits (Pizzini *et al.*, 2015:25). It also arises when reliance includes direct assistance work of internal auditors (Abbott *et al.*, 2012b:3).

Through their primary and secondary roles, management influence the foundational conditions of reliance, particularly the reliance environment. First, linked to their primary role, management determine the business risk environment which, linked to their secondary role, influences the risk of material misstatement of financial statements (IAASB, 2018: ISA 315 (Revised) paragraph 11). Furthermore, through their characteristics – for example, integrity – management pervasively determine the control environment and the related risk of material misstatement of financial statements, including by fraudulent reporting practices (IAASB, 2018: ISA 240 paragraph 12; ISA 315 (Revised) paragraph 14, Appendix 1 paragraph 2(d)). When such misstatement is considered a key risk, the external auditor's detection risk increases (IAASB, 2018: ISA 200 paragraph 13(e)). Thus, sufficient external auditor involvement in the audit allows less reliance (IAASB, 2018: ISA 330 paragraph 5; ISA 610 (Revised 2013) paragraph 18, 29, 30). The literature confirms that external auditors reduce reliance when the risk of material misstatement increases (Munro & Stewart, 2011:464).

Second, implicit in management's secondary role requiring fair annual statutory financial reports, they should implement and maintain an effective financial reporting function, supported by governance, risk management and internal control processes, including internal audit (IAASB, 2018: ISA 240 paragraph 31; IoDSA, 2016: part 5.4 recommended practice 42; Anderson & Eubanks, 2015:2). Pointing out reciprocal influences between these processes, research confirms that stronger internal audit quality is associated with stronger internal controls (Mazza & Azzali, 2015:148; Rae & Subramaniam, 2008:119). Moreover, internal control weaknesses are remedied quicker when internal auditors are more competent and independent (Mazza & Azzali, 2015:156, 160). Cohen, Krishnamoorthy and Wright (2017:1204, 1205) add that managements' risk management processes directly influence the quality of internal controls and external audit quality. Pointing to reciprocal influences on reliance, research indicates that management's internal control practices (Donelson, Ege & McInnis., 2017:45) and internal audit's practices (Abbott, Daugherty, Parker & Peters, 2016; Anderson & Eubanks, 2015:2; Christ *et al.*, 2015) mitigate the risk of material misstatement of financial statements, leading to greater reliance (Quick & Henrizi, 2018:25).

2.5.1.2 Management's interests

Management's interests are linked to their agency role. Corporate governance mechanisms are used to mitigate the influences of management's self-interests. Recommendations and requirements in governance and legal pronouncements aim to ensure the effectiveness of the mechanisms. The mechanisms' effectiveness is also a function of their reciprocal influences on each other. Some question the effectiveness of the mechanism. This section considers the reciprocal influences on reliance by management's self-interests and the effectiveness of governance mechanisms.

(a) Management's self-interests

Management, as agents of shareholders, are likely to have different interests to those of their principles (ICAEW, 2005:6). Thus, the potential exists for management to act in self-interest rather than the best interests of the organisation and the shareholders

(ICAEW, 2005:6). As a consequence, management may then have an incentive to manipulate financial reporting to present statutory financial results in line with shareholders' expectations (ICAEW, 2005:6). Shareholders' remoteness from decision-making power behind business activities causes information asymmetry between them and management (Brennan & Solomon, 2008:887). Highly publicised corporate collapses caused by financial reporting frauds, a spike in earnings restatements and claims of earnings management provide evidence of management's general self-interest in maximising shareholder value (Libby *et al.*, 2015:26; Cohen, Krishnamoorthy & Wright, 2004:87-88). These incidents show that management sometimes resort to fraudulent manipulation of statutory financial reporting to protect their self-interests, for example, their compensation (Gaynor, Kelton, Mercer & Yohn, 2016:7-9; Libby *et al.*, 2015:26).

Fraudulent manipulation of statutory financial reporting compromises fair presentation (Gaynor *et al.*, 2016:7-9) and thus reduces financial reporting quality. Typical proxies used in academic research when studying these frauds include restatements (for example, Schmidt & Wilkins, 2013:221), earnings management (for example, Bajra & Cadez, 2018:152; Libby *et al.*, 2015:26), discretionary accruals (for example, Shepardson, 2019:59) or performance-based compensation for managers (Gaynor *et al.*, 2016:7-10). Such frauds usually involve management overriding internal controls (IAASB, 2018: ISA 240 paragraph 31-33), which points to a weak control environment (IAASB, 2018: ISA 315 (Revised) paragraph 14, Appendix 1) and higher risk of material misstatement of financial statements. Unsurprisingly, research found that the increased risk of material misstatement of financial statements from management's self-interest in earning-based compensation reduce reliance (Desai, Gerard & Tripathy, 2011:149; Glover *et al.*, 2008:193-194).

(b) Mechanisms for mitigating management's self-interests

Commissions of enquiry have investigated mechanisms for mitigating management's dominance (see Cohen *et al.* 2004:87-88 for an overview). Upon their recommendations, most jurisdictions adopted legislation and / or regulatory reforms aimed at monitoring management (Judge, Douglas & Kutan, 2008:765). Typical corporate governance mechanisms include an independent audit committee and internal and external audit (IoDSA, 2016). However, the expenses associated with these mechanisms conflict with management's self-interest in maximising shareholder value. Legislation contains requirements about the role and appointment of an independent audit committee and an external auditor (Republic of South Africa, 2008: section 90, 94). Separate disclosure of the related expenses must thus be included in a company's annual report.

Legislation does not mandate the role and appointment of internal auditors or any disclosure about expenses on internal audit. Management may thus interpret internal audit as a discretionary expense, which they may want to limit in order to maximise shareholder value. Thus, management's self-interest in maximising shareholder value may negatively affect the resourcing of internal audit. In terms of reciprocal influence on reliance, research points to an association between management's resourcing of internal audit and reliance (Cohen *et al.*, 2017:1204, 1205; Zain *et al.*, 2006:1). This is because the scope of internal audit work permitted by internal audit resourcing affects internal audit quality (Zain *et al.*, 2015:134, 136, 138; Christopher, Sarens & Leung, 2009:208). Governance requirements recommend audit committee oversight of internal audit's resourcing (IoDSA, 2016: part 5.4 recommended practice 50). Alzeban (2015:554) reports that independent audit committee members contributed to internal audit quality by mitigating management's 'agendas relating to funding' internal audit.

Considering reciprocal influences between management's control measures, research reveals an association between internal audit quality factors and the strength of internal controls (Mazza & Azzali, 2015:148; Lin, Pizzini, Vargus & Bardhan, 2011:287; Rae & Subramaniam, 2008:119). This association is relevant, as internal control strength influences reliance (Quick & Henrizi, 2018:25). When resourcing permits an increase in the number of annual internal audits, employees' adherence to internal control procedures improved, implying stronger controls (Rae & Subramaniam, 2008:119). Furthermore, management remedied significant internal control weaknesses sooner when internal audit was more competent, having a larger proportion of costlier internal auditors with postgraduate degrees and more years of internal audit experience (Mazza & Azzali, 2015:156, 160). In addition, having a larger number of internal auditors allow for greater internal audit objectivity as assurance and consulting work could be allocated to different internal audit team members (Mazza & Azzali, 2015:156, 160).

Bédard and Graham (2011:846, 851) observe that the mere presence of an internal audit function did not significantly improve the detection of internal control weaknesses. However, other research reports that specific internal audit qualities are associated with a smaller number of material weakness disclosures (an indication of stronger internal financial controls) in terms of the Sarbanes Oxley Act (SOX, 2002). These qualities include internal auditors with higher education levels, internal audit work with a financial focus, quality assurance practices for internal audit fieldwork, risk-based selection of audit areas and follow-up procedures on management's remediation of control problems. In terms of the reciprocal influence of internal control and internal audit on reliance, the combination of stronger internal controls and internal audit is associated with higher levels of coordination between the two audit parties. This is evident from them engaging in 'joint risk or planning sessions' and internal auditors performing direct assistance work (Lin *et al.*, 2011:287, 295).

Academic studies confirm the association between the effectiveness of monitoring mechanisms and financial reporting quality. For example, a stronger internal audit function – in terms of resourcing, independence, competence and involvement in financial audits, as well as an independent board – reduces earnings management to a statistically significant extent (Bajra & Cadez, 2018:161, 162). However, when management's involvement in the appointment and remuneration of audit committee members reduces the committee's independence, financial reporting quality is compromised, causing more financial statement restatements (He, Yang & He, 2018:219, 242). In South Africa, King IV recommends that the board as a whole should approve nominations of board members by the nomination committee (IoDSA, 2016: part 5.3 recommended practice 14). The nomination committee should consist of only non-executive directors, the majority of whom should be independent (IoDSA, 2016: part 5.3 recommended practice 61).

(c) The effectiveness of mechanisms for mitigating management's self-interests

Research reports opposing views about the effectiveness of corporate governance mechanisms for keeping management accountable. Most academic studies show corporate governance mechanisms effectively mitigate managements' self-interests by 'ensuring the quality of the financial reporting process' (Cohen *et al.*, 2004:87, 88, also see Bonetti, Magnan & Parbonetti, 2016 for a review). By way of example, research has linked internal control practices (Donelson *et al.*, 2017:45), audit committee practices (Kusnadi, Leong, Suwardy & Wang, 2016; Tanyi & Smith, 2015; He, Labelle, Piot & Thornton, 2009), internal audit practices (Abbott *et al.*, 2016; Anderson & Eubanks, 2015:2; Christ *et al.*, 2015) and external audit practices (Gaynor *et al.*, 2016) to quality financial reporting. Pointing to a reciprocal influence among corporate governance mechanisms, research reports that effective audit committee oversight aids internal audit quality and external audit quality (Beattie, Fearnley & Hines, 2013:56; Lenz *et al.*, 2014:126).

In terms of reciprocal influences between corporate governance mechanisms and reliance, research reports that external audit effort and fees decrease from increased direct assistance work from a more independent and better resourced internal audit function (Cohen *et al.*, 2017:1204-205; Abbott, Parker & Peters, 2012a:94). In line with these notions of reciprocity, Quick and Henrizi (2018:25) conclude that 'management can play an outstanding role in improving collaboration between the internal and external audit, by strengthening the quality of [internal] control systems and of corporate governance [for example, the audit committee]'. Highlighting the important influence of the audit committee, research describes these as 'the balance of power' (Turley & Zaman, 2007:779) between management and internal and external auditors, as they 'counterbalance' (Gendron & Bédard, 2006:224) management's self-interest.

Academic research highlights specific audit committee practices which serve as 'checks and balances' (Gendron & Bédard, 2006:233) for mitigating management's self-interests. These include having a direct functional reporting line between the chief audit executive and the audit committee, a majority of independent audit committee members, a minimum of one audit committee member with accounting financial expertise, audit committee involvement in the appointment, dismissal, evaluation and remuneration of the chief audit executive, regular private meetings between the chief audit executive and the audit committee chair, sufficient audit committee time spent on internal audit topics and inviting the chief audit executive to all audit committee meetings (Christopher *et al.*, 2009:200, 214, 215).

Concerning the influence of the relationship between management and internal audit on the effectiveness of internal audit's independent assurance role, Rose, Rose and

Norman (2013:1004, 1007) report that ‘internal auditors have incentives to please management because internal auditors’ compensation, performance evaluations and professional security tend to be heavily influenced by management’. Internal auditors’ reporting practices show instances when they defy the objective of their functional reporting duty to the audit committee, as they prefer reporting higher levels of risk directly to management instead, and even reduced risk levels reported to the audit committee (Norman, Rose & Rose, 2010:546). Internal auditors justified this by explaining that they feared personal threats, including management retribution and increases in work allocations by the audit committee, when they reported higher risks to the audit committee (Norman *et al.*, 2010:546-549). Such filtering of matters reported to the audit committee through management render internal audit ineffective as a monitoring mechanism of management’s self-interest (Norman *et al.*, 2010:549).

Some research views corporate governance mechanisms as ‘symbolic gestures’ that do not address the ‘substance of the interactions between different governing parties’ (Cohen, Krishnamoorthy & Wright, 2008:181). For example, highlighting ‘ritualistic ceremonial behaviours and symbolic endeavours vs substantive engagement by audit committees’, Brennan and Kirwan, (2015:466) question whether audit committees are genuinely focused on improving corporate governance. Noting the consequences of delinquent audit committees, Cohen, Krishnamoorthy and Wright (2010:752) deduce from interviews with external auditors that ‘management continue to be seen as a major corporate governance actor’, as ‘symbolic’ governance practices are ineffective against their dominance. In line with Cohen *et al.* (2010:752; 2008:181), Beattie *et al.* (2013:56) posit that ‘regulatory over-reaction’ leads to governance ‘regimes ... [becoming] largely process- and compliance driven, with high costs and limited benefits’. In addition, adopting a critical perspective, Clarke, Jarvis and Gholamshahi (2019:1) criticise the counterproductive effects of the internationalisation of agency theory and shareholder primacy entrenched in Anglo-American corporate governance requirements. They claim that these requirements compound inequality, which they define as the ‘explosion’ in executive management’s rewards in Anglo-American countries over the last two decades (Clarke *et al.*, 2019:1).

2.5.1.3 Management's interpretations

Management interpret that resourcing internal audit will generate reciprocal benefits, including reduced external audit effort and external audit fees from reliance (CAQ & IIA, 2015: 10), improved total audit coverage (Sarens & De Beelde, 2006:220) and support through *ad hoc* work for management (Pilcher *et al.*, 2013:335; Roussy, 2013:550; Lampe & Sutton, 1994:345). Contrary to these beliefs, however, research reports an association between higher external audit fees and management investing in stronger governance, risk management and internal control processes (Goodwin-Stewart & Kent, 2006:387), for example, higher internal audit quality (Zain *et al.*, 2015:140) and oversight by a stronger audit committee (Ali, Singh & Al-Akra, 2018:174). Abbott *et al.* (2012a:98) furthermore propose that this apparent anomaly arose from attempts to maximise benefits from the investments in both internal and external audit: 'The consequences of increased [internal audit] assistance … [to] external audit may include not only decreases in total audit scope (a concern to the audit committee), but also diminishment of non-financial statement activities by the IAF [internal audit function], such as consulting, risk management, and efficiency and effectiveness audits.'

Research maintains that higher external audit fees imply that audit committees demand greater use of internal audit (Goodwin-Stewart & Kent, 2006:387) and higher external audit quality (Ali *et al.*, 2018: 174), with internal audit complementing rather than substituting external audit work (Zain *et al.*, 2015:140). In line with these findings, Gramling *et al.* (2004:195) assert that the reciprocal benefit of reliance is improved corporate governance quality, rather than reduced external audit fees. However, management seem to focus on assurance efficiency rather than effectiveness benefits from reliance. This is evident as external auditors report that management put pressure on them to practise or increase reliance (Felix *et al.*, 2005:31). Corroborating this notion, Ettredge, Fuerherm and Li (2014:247) report a strong association between audit fee pressure and lower financial reporting quality as well as external audit quality, measured as unidentified accounting misstatements in statutory financial reports. Not surprisingly, in the context of management fee pressure on external auditors, chief financial officers were more sceptical than external auditors and audit committee chairs about the value of the external audit (Ettredge *et al.*, 2014:247; Beattie *et al.*, 2013:76).

Concerning management's expectation of internal audit support through *ad hoc* work for management, such work usually influences internal audit's ability to meet their financial focused audit plans (Pilcher *et al.*, 2013:335; Lampe & Sutton, 1994:345). Less reliance occurs when internal audit prioritise *ad hoc* work for management rather than completing reliance work with a financial focus included in the internal audit plan (Pilcher *et al.*, 2013:335), or are involved in value-adding controls consulting activities required by management (Munro & Stewart, 2010:371, 385).

2.5.1.4 Management's practices

Management's practices around the staffing of the internal audit function and sourcing of internal audit services influence the strength of internal audit, and thus reliance. Management opting to use internal audit as a management training ground (Sarens & De Beelde, 2006:220) and / or following a 'rotational staffing model' (Christ *et al.*, 2015:37) has both positive and negative implications. On the positive side, relations between senior management and internal audit improve (D'Onza & Sarens, 2018:9) as management appreciate the value added by internal audit serving as a management training ground (Christ *et al.*, 2015:54). On the negative side, using internal audit as a training ground for senior management threatens internal audit's independence (Hoos, Messier Jr, Smith & Tandy 2018:150; Abbott *et al.*, 2010:1) and competence (Christ *et al.*, 2015:37-38). This results in lower internal audit quality and higher external audit fees as less reliance is possible (Messier *et al.*, 2011:2131).

Particularly, internal auditors working in a management training ground 'feel much greater pressure not to issue negative reports for an auditee in an operating area where they may be transferred in future years' (Lampe & Sutton, 1994:345). As a result, less objective internal audit reports tend to favour management's preferences (Hoos *et al.*, 2018:150). Furthermore, new staff employed in internal audit with the intention of being rotated into operational management positions at a later stage, and / or operational staff rotated into internal audit positions before being promoted into operational management positions at a later stage, usually lack internal audit specific competence and objectivity (Christ *et al.*, 2015: 37-39, 45). As a result, they neglect 'traditional internal audit activities', causing a significant increase in the risk of material misstatement of financial statements prepared by management (Christ *et al.*, 2015: 37-39, 45).

Concerning the sourcing of internal audit services, management could choose from a full in-house internal audit structure or outsourced internal audit services – either in totality or partially. Management could also co-source internal audit services through in-house and outsourced internal auditors working on joint engagements instead of relying on a fully in-house internal audit function (IIA, 2018:3). Supplementing in-house internal auditors with outsourced or co-sourced internal auditors from a specialist outsourced internal audit service provider or an external auditing firm is a popular internal audit structuring choice, typically used in more than half of internal audit functions researched (Abdolmohammadi, 2013:70; Glover *et al.*, 2008:195). Management usually supplement in-house internal auditors with outsourced or co-sourced internal auditors when resource-intensive, value-adding internal audit activities are needed or when skills gaps exist in internal audit (Abdolmohammadi, 2013:69, 73). In instances where internal audit is fully outsourced, an individual employed in the organisation should act as internal audit director (for example, IIA, 2018:2; Glover *et al.*, 2008:201).

Research has identified quality variances associated with different internal audit sourcing structures influence reliance (for example, Davidson, Desai & Gerard, 2013; Desai *et al.*, 2011; Munro & Stewart, 2010; Glover *et al.*, 2008). In line with attribution theory and group affiliation constructs, external auditors prefer using work of a Big 4 internal audit service provider rather than work produced by either a high-quality in-house function or a non-Big 4 specialist internal audit services firm (Munro & Stewart, 2010:384-385). In an earlier study, Gramling and Vandervelde (2006:30-31) found that internal and external auditors are prone to group affiliation, with each group assessing their peers providing either in-house or outsourced internal audit services as being more objective than others. However, when the sampling and selection of internal audit work is determined more objectively, through technology rather than a conventional periodic rotational approach, external auditors are equally willing to rely on the work of in-house and Big 4 internal audit service providers (Davidson *et al.*, 2013:41, 48-49).

The literature associates several benefits with using an in-house internal audit compared to an outsourced structure. By way of example, in-house internal auditors' availability as a resource within the audit client results in greater use of in-house rather than outsourced internal auditors for direct assistance work (Munro & Stewart, 2010:371). Research also indicates that in-house internal auditors' superior, entity-specific knowledge (IIA, 2018:1) makes them more likely than outsourced internal auditors to detect and report misappropriation of assets (Coram, Ferguson & Moroney, 2008:543). Conceivably, this should encourage more reliance. However, Wan-Hassin and Bamahros (2013:19) report that similar effects on audit report lag when an in-house versus outsourced internal audit structure is used.

The interview guide included the following discussion point addressing the influence of management on reliance.

LINK TO DISCUSSION POINT IN INTERVIEW GUIDE

Determining management's influence on reliance

DISCUSSION POINT 13: How do the management of the company influence your external auditor's use of the work of internal auditors?

In summary, management's dominant role, interpretations, interests and practices as agents responsible for all business activity and the statutory financial reporting process have a pervasive influence on the foundational conditions of reliance. Management determine the reliance environment through their influence on risks and risk management, internal controls, the structure of the internal audit function and internal audit resourcing. Consequently, management influence the relevance and credibility of internal audit work. Management's pervasive influence on financial reporting quality and governance structures has the potential to undermine external audit quality and increase the external auditor's liability.

2.5.2 External auditors

External auditors have a statutory financial reporting assurance role. Concerns for external audit quality and the external auditor's liability are inherent in the role of external auditors. On the one hand, external auditors' role is pervasively influenced by management's influence on the risk of material misstatement of financial statements and financial reporting quality. This arises through management's influence on risk management and internal controls, including monitoring by internal auditors. On the other hand, audit committee oversight balances the influences of management on the statutory financial reporting and external audit processes. This section considers these reciprocal influences on reliance.

2.5.2.1 External auditors' role

The independent external auditor has a statutory assurance role as a corporate governance mechanism. Shareholders appoint an independent external auditor based on the recommendation of the audit committee (Republic of South Africa, 2008: section 94). The external auditor performs an annual, risk-based audit. This audit assesses whether the financial reporting function and related governance, risk management and internal control processes, including internal audit, (IAASB, 2018: ISA 315 (Revised)), have generated statutory financial reports considered fair in all material respects (IAASB, 2018: ISA 200 paragraph 11, 17; Republic of South Africa, 2008: section 30, 90). Irrespective of reliance, the external auditor's opinion conveys reasonable assurance to users about the fairness of management's statutory financial reports (IAASB, 2018: ISA 200 paragraph 11; ISA 610 (Revised 2013) paragraph 11).

A risk-based external audit requires the identification and assessment of financial statement level and assertion level risks of material misstatement, whether due to error or fraud. Misstatement due to fraud include those following misappropriation of assets and / or manipulation of financial reporting (IAASB, 2018: ISA 240; 315 (Revised)). The nature, timing and extent of external audit's procedures should respond to significant and assessed risks of material misstatement (IAASB, 2018: ISA 240; 315 (Revised); 330), by obtaining sufficient relevant and reliable audit evidence for reducing audit risk to an acceptable level (IAASB, 2018: ISA 200 paragraph 17; ISA

500 paragraph 6). Academic studies have found that a higher risk of financial reporting fraud by management is associated with weaknesses in the control environment (‘entity-wide controls’) rather than at the assertion level (‘process-level controls’) (Donelson *et al.*, 2017:45). As required by the ISA (IAASB, 2018: ISA 610 (Revised 2013) paragraph 18), external auditors adjust reliance in accordance with the risk of material misstatement of an area of financial statements, for example, by considering the influence of management’s self-interest in earning-based compensation (Desai *et al.*, 2011:149; Glover *et al.*, 2008:193-194). In terms of reciprocal influences of corporate governance mechanisms, while external auditors’ risk assessments of the effect of strategic risks do not sufficiently account for the effect of weaker risk management processes (Cohen *et al.*, 2017:1205), stronger audit committees consisting of members with financial expertise are associated with more effective, risk-mitigating internal controls (Hoitash, Hoitash & Bédard, 2009:863). Conceivably, external audit’s risk assessment at the financial statement level should consider audit committee expertise.

Irrespective of reliance intentions, external audit’s risk assessment procedures include obtaining an understanding of internal audit, particularly of the relevance of their work to financial reporting, the nature and scope of internal audit work and internal audit’s organisational status (IAASB, 2018: ISA 315 (Revised) paragraph 22-23). The external auditor’s understanding of internal audit is developed from enquiries of management, internal audit and the audit committee as well as reading internal audit’s strategy and planning documents and reports (IAASB, 2018: ISA 315 (Revised) paragraph A110-120). The academic literature reports that internal audit’s role typically includes work with a financial reporting focus, monitoring statutory financial reporting (for example, Abbott *et al.,* 2016:37).

The external auditor may, when assessed as appropriate, use work performed in the normal course of internal audits or direct assistance work as audit evidence supporting the statutory audit opinion (IAASB, 2018: ISA 315 (Revised) paragraph 23; ISA 610 (Revised 2013) paragraph 13). The appropriateness of reliance is assessed in accordance with the framework contained in ISA 610 (Revised 2013) (IAASB, 2018). While the literature confirms that some reliance occurs (Quick & Henrizi, 2018:25; Al-Sukker *et al.*, 2016:317), the multitude of factors requiring simultaneous consideration complicate the external auditor’s reliance decision (for example, Singh *et al.*, 2014:36;

Bame-Aldred *et al.*, 2013:282-283; Brody, 2012:11; Desai *et al.*, 2010:538; Krishnamoorthy, 2001:499; 513; Maletta, 1993:508; Edge & Farley, 1991:77).

2.5.2.2 External auditors' interpretations and interests

The ISA stipulate that the external auditor remains solely and fully responsible for the audit opinion, irrespective of any reliance on internal audit work (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). Thus, external auditors have a self-interest in practising reliance only when it is appropriate to do so. In response to an alert to this effect (PCAOB, 2013), external auditors decreased reliance (CAQ & IIA, 2015:3, 9). The literature indicates that reliance is moderated by concerns for external audit quality and the external auditor's liability (Arel *et al.*, 2012:516), linked to internal audit quality (Zain *et al.*, 2015:140) and losing audit firm clients and / or income (Felix *et al.*, 2005:31). Felix *et al.* (2005:31) specifically note that client pressure induces reliance when external auditors' concerns about losing fees for non-assurance services weigh heavier than the appropriateness of reliance in the circumstances. Such behaviour of external auditors indicates a strong self-interest in satisfying management, possibly for retaining an audit client, rather than preserving external audit quality. Pointing to a reciprocal influence by monitoring mechanisms on reliance, external auditors perceive the audit committee's commitment to 'pay the appropriate rate for a thorough audit' protects external audit quality (Beattie *et al.*, 2013:75).

2.5.2.3 External auditors' practices

Practising reliance implies incorporating internal audit work into external audit evidence. This may modify the nature, timing or extent of audit procedures performed directly by the external audit team (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13). Evidence shows that external auditors mostly rely on internal audit's control evaluation work rather than substantive procedures (Quick & Henrizi, 2018:25; Munro & Stewart, 2011:464; 2010:371; Whittington & Margheim, 1993:59; Ward & Robertson, 1980:64). The latter finding is aligned with internal audit's typical focus on assurance work covering governance, risk management and internal controls (IIA, 2015a).

Considering the reciprocal influences of corporate governance mechanisms, the external auditor supports the audit committee's oversight role by engaging in two-way communication with management and the audit committee about the external audit (IAASB, 2018: ISA 260:9; IAASB, 2016:51), while open and constructive interactions between management and external auditors contribute to external audit quality (IAASB, 2016:51). In the academic literature, audit committee chairs, chief financial officers and external audit partners confirm that interactions occur between external audit and the audit committee, including about key audit issues, and were an important contributor to external audit quality (Beattie *et al.*, 2013:56, 67). However, Compernolle (2018:900) observes that external auditors' aim, when communicating with the audit committees, was to convey an impression of consistency for the sake of preserving management's reputation. This therefore lacked the transparency required for effective audit committee oversight.

Concerning reliance, external auditors should communicate the nature and extent of reliance planned to the audit committee and engage in two-way communication with internal auditors about planned reliance (IAASB, 2018: ISA 610 (Revised 2013) paragraph 20-22, 33). However, several authors report that communication between internal and external auditors about planned reliance was poor, leaving internal auditors in the dark about the reasons for the lack of reliance (Pilcher *et al.*, 2013:334, 336; Wallace, 1984:199-200; Barrett & Brink, 1980:67).

The external auditor documents the justification for the nature and extent of reliance as well as the procedures performed to test the adequacy of reliance work for external audit purposes (IAASB, 2018: ISA 610 (Revised 2013) paragraph 36-37). Audit documentation is the property of the external auditor, who has a duty to protect its confidentiality (IRBA, 2018a: subsection 114). Consequently, as in the case of audit documentation supporting external audit quality at the engagement level, outsiders are not 'privy to the dialogue' (CAQ, 2016:13) contained in confidential audit documentation, making reliance unobservable in a 'black box' (Brivot, Roussy & Mayer, 2018:51; IRBA, 2018a: subsection 114).

In summary, inappropriate reliance will have serious legal consequences for the external auditor. Given the complexity of reliance and the lack of a mutual, conceptual explanation of the reciprocal influences on reliance by the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors, external auditors' reliance decisions are open to criticism of being inappropriate and / or unfair.

2.5.3 Internal auditors

Internal auditors have a governance role. This role both supports and is influenced by management and the audit committee. As a governance mechanism, internal auditors' monitoring of governance, risk management and internal control processes pervasively influence the risk of material misstatement of financial statements and financial reporting quality. This section considers these reciprocal influences on reliance.

2.5.3.1 Internal auditors' roles

Internal audit's variable support roles mainly includes objective assurance supporting the audit committee's oversight role and value-adding advice supporting management's business role. The role of internal audit in statutory external audits fits in with its objective assurance role. The variability of internal audit's roles affects expectations of internal audit and perceptions about its value. The resources used when performing its value-adding role influence its net capacity to fulfil other roles. The profile of the internal auditing profession is influenced by the gap in expectations and the services actually provided by internal audit. This section considers the roles of internal audit and the influence on perceptions of the value and profile of internal audit.

(a) Internal audit's variable support role

In contrast to external audit's statutory role most corporations worldwide do not have a statutory obligation to implement internal audit. For example, McNally (2013) highlights that neither the Committee of Sponsoring Organizations of the Treadway Commission's (COSO) Internal Control Framework nor the US Congress' Sarbanes Oxley Act passed in 2002 make internal audit a mandatory requirement. Similarly, Lenz *et al.* (2018:11) point out the European Union's 8th Directive also does not require internal audit. However, maintaining an internal audit function is mandatory for all companies listed on the New York Stock Exchange (Arel, 2010:171). In a South African context, neither the Companies Act (Republic of South Africa, 2008) nor the JSE listing requirements (JSE, 2019) mandate internal audit. However, the JSE listing requirements stipulate the disclosure of alternative measures used when internal audit is absent (JSE, 2019: paragraph 7.F.5). Consequently, unlike management (Republic of South Africa, 2008: section 30), the audit committee (JSE, 2019: section 3.84(g), 16.10(u); IoDSA, 2016: part 5.3 recommended practice 51, 59, Republic of South Africa, 2008: section 94), and external auditors (Republic of South Africa, 2008: section 30, 90), internal audit is not required to provide a signed report in the statutory annual report or the integrated report, explaining their role and the outcomes of their work. Instead, internal audit provides a service supporting the roles of management, the audit committee and external audit (Roussy & Brivot, 2016; Lenz & Hahn, 2015; Roussy, 2013; Sarens, Christopher & Zaman, 2013; Zaman & Sarens, 2013; Lenz & Sarens, 2012; Sarens, Abdolmohammadi & Lenz, 2012; Sarens *et al.*, 2009; Sarens & De Beelde, 2006; Gramling *et al.*, 2004).

(b) Internal audit's objective assurance role

In line with internal audit's role as a corporate governance mechanism used by shareholders to mitigate risks associated with management's agency role (Sarens & Abdolmohammadi, 2011:15), research reports the prominent use of internal audit in larger organisations (Anderson, Christ, Johnstone & Rittenberg, 2012; Goodwin-Stewart & Kent, 2006). Internal audit was also used in highly regulated financial organisations (Goodwin, 2004) and those with stronger control environments (Sarens & Abdolmohammadi, 2011) and stronger corporate governance (Beisland *et al.*, 2015).

Further to the agency perspective, internal audit has traditionally been part of an organisation's internal control system, specifically tasked with monitoring internal controls (IAASB, 2018: ISA 315 (Revised) paragraph 23; Anderson & Eubanks, 2015:7). In terms of internal audit's traditional role, it provides the audit committee and board with an annual overall statement attesting to the effectiveness of the organisation's governance, risk management and internal control processes (IoDSA, 2016: part 5.4 recommended practice 59). The audit committee and internal audit are thus ‘interdependent’, with both contributing to statutory financial reporting quality (Sarens *et al.,* 2013:307, 308). Their interdependence arises as internal auditors’ ‘insider knowledge’ of the business counters independent audit committee members’ lack of involvement in the operations of the organisation (Edge & Farley, 1991:70), including their lack of insider knowledge of related governance, risk management and internal control processes. Thus, audit committee members view internal audit as a ‘comfort provider’ (Sarens *et al.*, 2009:90) supporting their oversight role (Sarens *et al.*, 2013:322).

The introduction to the Standards states:

> Assurance services involve the internal auditor’s objective assessment of evidence to provide opinions or conclusions regarding an entity, operation, function, process, system, or other subject matters. The nature and scope of an assurance engagement are determined by the internal auditor (IIA, 2016:2).

When planning audit work, the chief audit executive considers the requirements of the board-approved internal audit charter, developed in conjunction with the audit committee (IIA, 2016: Standard 1000; IoDSA, 2009: principle 3.10 recommendation 85.5; principle 7.1 recommendation 5). However, the chief audit executive should also identify and consider expectations of management, the audit committee and external audit regarding internal audit opinions and conclusions (IIA, 2016: Standard 2010.A2) (set out in the internal audit charter) when designing internal audit work plans.

In terms of reciprocal influences between corporate governance mechanisms, several findings reported in literature and governance recommendations underline the importance of audit committee oversight of internal audit’s effectiveness. In line with governance recommendations (IoDSA, 2016: part 5.3 recommended practice 56), the literature specifies that a direct functional reporting line between the chief audit executive and the audit committee mitigates managements’ influence on internal audit (Christopher *et al.*, 2009:200, 214, 215). Moreover, in line with governance requirements (IoDSA, 2009: principle 3.7 recommendation 55), the literature reports that audit committee oversight enhances internal audit quality by ensuring that internal audit plans are reasonable in light of available internal audit resources (Abbott *et al.*, 2010:2).

Academic studies also report that there is greater senior management support for internal audit if those managers give input into internal audit plans (Sarens & De Beelde, 2006:219). However, such management involvement could create an independence ‘dilemma’ when management prescribe how internal audit should change the scope of their plans (Lenz *et al.*, 2018:28). Of concern is Roussy’s (2015:259, 260) finding (similar to that of Norman *et al.*, 2010:551, 555) that audit committee oversight does not sufficiently mitigate management’s influence on internal auditors’ objectivity. This caused internal auditors to use ‘coping tactics’ for managing their conflicting roles, for example, by censoring internal audit reports or limiting the scope of internal audit work in line with management’s interests. Conceivably, as audit committee oversight of internal audit’s resourcing and work plans influences the strength of internal audit, both influence reliance.

(c) Internal audit’s value-adding advisory role

Over the last two decades, the role of internal audit has evolved. Contemporary internal audit functions are expected to add value as ‘trusted advisors’ of management and the board, contributing insights on business activities, in addition to their traditional objective assurance role (Endaya & Hanefah, 2016:160; IoDSA, 2016: page 31, part 5.4 recommended practice 59; KPMG, 2016:3; PwC, 2016:5; Lenz & Hahn, 2015:10;Sarens & De Beelde, 2006:236). As a result, the IIA currently describes internal auditing as a combination of assurance and consulting services, which add value and improve an organisation’s operations (IIA, 2015a). In line with this definition, the Standards require that internal auditors not only to evaluate and conclude but also provide advice to management on the effectiveness of an organisation’s operations, including its governance, risk management and internal control processes, as well as making recommendations for improvement and action plans (IIA, 2016: Standard 2100, 2410). However, the literature reports that internal audit involvement in value-adding controls consulting activities causes LESS reliance as such involvement threatens internal audit’s objectivity (Munro & Stewart, 2010:371, 385).

(d) Internal audit’s role in the statutory external audit

The Standards require that the chief audit executive coordinate work with internal and external assurance providers, one of which is external audit (IIA, 2016: Standard 2050; IIA, 2015b: Practice Advisory 2050-1, 2050-2, 2050-3). Academic research indicates that management and audit committees value 'broader and better coverage of risk and internal control reviews' derived from active collaboration between internal and external audit as part of a 'joint audit approach' (Sarens *et al.*, 2009:102). Likewise, the IIA (2017:3) underlines the complementary and supplementary aspects of internal and external audit's work. With reference to the reciprocal influences between corporate governance mechanisms, Abbott *et al.* (2016:9) point out that opportunities for mitigating management's influences on statutory financial reporting improve when internal auditors perform direct assistance work for statutory audit purposes, compliance audits and special investigations.

(e) The value proposition of internal auditing

Professional publications identify a 'value gap' between audit committee's and chief financial officers' expectations of internal audit and the services actually provided by internal audit (KPMG, 2016:2). Although many senior managers and board members believe that internal audit adds significant value, even more of them expect internal audit to deliver greater value (PwC, 2016:3). Academic studies explain that stakeholder groups' perceptions of the value and effectiveness of internal audit vary (Trotman & Duncan, 2018:253; PwC, 2016; Roussy & Brivot, 2016:714), in line with fluctuations in the 'utilitarian benefit' each group expects from internal audit's role (Lenz & Hahn, 2015:17). Consequently, research points out that the role and capacity of internal audit is 'contextually bound … as IAFs may serve different purposes in their respective specific organizational context' (Lenz & Hahn, 2015:7; D'Onza, Selim, Melville & Allegrini, 2015:192).

Research attributes questions raised about the value of internal auditing to internal audit's 'dual role as a provider of assurance and consulting activities' (Stewart & Subramaniam, 2010:328). This dual role creates a 'complex relationship between the IAF and its various stakeholders' who do not understand internal audit's role (Lenz & Hahn, 2015:10). As an example of this complexity, management demand internal audit's assistance with 'achieving operational goals and generating cost savings', while the audit committee expects internal audit assistance in carrying out ‘heightened audit committee oversight expectations’ (Abbott *et al.*, 2010:2), leaving internal auditors exposed to ‘role conflicts’ (Roussy, 2015:240).

Expectations that internal audit should serve ‘two masters’, providing comfort to the audit committee and business insights to management, cause competing demands on internal audit resources (Abbott *et al.*, 2010:1, 23). This results in varying perceptions of internal audit effectiveness (Lenz & Hahn, 2015:17). Lenz *et al.* (2018:14) conceptualise internal audit’s dual role as ‘cognitive disconnect’, originating from internal audit’s ‘completely integrated and knowledgeable’ management support role versus their independent assurance provider role. The latter message is not new; years before, Gramling *et al.* (2004:235) cautioned that conflicting messages to internal audit as well as conflicting demands placed upon it, render internal audit ineffective.

As an example of the consequences of the ‘disconnect’ in views about internal audit, management and audit committees have expressed doubt about the value and effectiveness of internal audit (KPMG, 2016:3; PwC, 2016:4). Academic research ascribes this doubt to the ‘expectation gap’ arising when internal auditors’ perceptions of their value-adding activities differ from those of their various stakeholders (Sarens & De Beelde, 2006:220). In light of internal audit’s contrasting roles, Roussy and Brivot (2016:714) characterise internal audit effectiveness as a complex ‘polysemous notion’, while Lenz *et al.* (2018:4) see it as an ‘enigmatic phenomenon’. Conceivably, their opposing interpretations of internal audit’s role and effectiveness would cause disagreement among stakeholder groups about the fairness of reliance.

(f) The profile of the internal audit profession

Stakeholder groups’ opposing interpretations of internal audit’s effectiveness caused by internal audit’s dual reporting role negatively affect the profile of the internal audit profession. By way of example, Lenz and Hahn (2015:26) caution of a ‘relevancy threat faced by the IA [internal audit] community’ while Chambers and Odar (2015:34) note that ‘the internal audit profession has not been “fit for purpose” and can be enhanced’. Furthermore, stakeholder’s preference for internal auditors who are members of external auditing professional bodies rather than internal auditing professional bodies, for example in New Zealand (Van Peursem, 2004:379), reflects the challenges in fostering a professional identity for internal auditors. Conceivably, stakeholder groups' views about the internal audit profession could influence their interpretations about reliance.

Academic research suggests that as professionals, internal auditors should 'remain true to the core principles of the profession' (Nuijten, Van Twist & Van Der Steen, 2015:195). Thus, internal auditors should focus on evaluating and improving risk management and internal control systems (D'Onza *et al.*, 2015:192) by using 'factual data' responsive to conditions of 'interactive complexity' and '[l]ooking ahead and reporting [emerging] risks' (Nuijten *et al.*, 2015:202). These actions would add value from internal auditors' 'consolidation of … [their] core function' (Lenz & Sarens, 2012:532), namely, as the provider of 'comfort' to the audit committee (Sarens *et al.*, 2009:90) and as the provider of 'more dependable assurance to boards' (Chambers & Odar, 2015:34) on the effectiveness of risk management and internal controls (D'Onza *et al.*, 2015:192). D'Onza *et al.* (2015:192) suggest that the internal audit profession could also add value through a requirement to make 'external disclosures in the public interest when internal auditors are aware of serious wrongdoing not satisfactorily addressed internally'. The latter suggestion is not currently a requirement.

2.5.3.2 Internal auditors' interpretations and interests

Internal auditors emphasise that senior management support is crucial for internal audit's acceptance and effectiveness within an organisation (Endaya & Hanefah, 2016:169; Lenz & Hahn, 2015:9; Sarens & De Beelde, 2006:219). Chief audit executives consider the implementation of internal audit's recommendations by management as testimony of senior management's interest in and support for internal audit (for example, Arena & Azzone, 2009:48). Research indicates that the legitimacy of internal audit depends on the effectiveness of the working relationship between internal audit and senior management, evident from 'open and direct communication' between internal audit and management (Lenz *et al.*, 2018:17). Internal auditors and audit committee chairpersons mentioned that communication synchronises the views of internal audit and senior management on key organisational risks requiring internal audit attention and builds sound relationships between the two (Roussy & Brivot, 2016:728). Synchronisation enhances the contribution of internal audit to organisational performance as their reports include relevant findings (Roussy & Brivot, 2016:728). Conceivably, management support for internal audit would influence reliance.

Internal auditors perceive that management associate reliance and increased total audit coverage with internal audit effectiveness (Sarens & De Beelde, 2006:220). Internal auditors also perceive that management expect reliance to reduce external audit fees (CAQ & IIA, 2015: 10). Thus, reliance would support the interests of internal auditors, who would be regarded as more effective and as adding value to assurance efficiency. However, Lenz and Hahn (2015:17) caution that using reliance as an indicator of internal audit effectiveness could be misleading in light of external audit's narrower financial risk focus versus internal audit's typical wider business risk focus.

Internal auditors believe that reliance levels are much higher than those reported by external auditors (for example, Pilcher *et al.*, 2013:334). According to Pilcher *et al.* (2013:334), internal auditors perceive that external auditors use between 80% to 100% of internal audit work for statutory external audit purposes. Internal auditors base this view on extensive coordination occurring between internal and external audit, for example, coordination of work schedules or sharing of internal audit working papers and reports with external auditors. Contrary to internal auditors' interpretations, external auditors express that they 'probably don't rely a lot on internal audit', blaming these low reliance levels on external audit's 'methodology' and the small period covered by internal audit work, which made the scope of internal audit work insufficient for reliance (Pilcher *et al.*, 2013:334).

Pilcher *et al.* (2013:334) conclude that poor communication between internal and external auditors, particularly a lack of discussion about the level of reliance and motivation for it, pervasively contributed to their inconsistent replies. Pilcher *et al.* (2013:334-336) indicate that external auditors practise little reliance despite conveying that internal auditors were competent, internal audits had a risk focus, internal audit planned time for performing *ad hoc* work for management, external audit provided input on the internal audit plan and regular meetings occurred between internal and external auditors. Conceivably, the effectiveness of communication between internal and external auditors influences reliance.

2.5.3.3 Internal auditors' practices

In one of the more recent academic studies on internal audit effectiveness, Lenz *et al.* (2018:32) underline that the 'role and influence of the CAE is critical'. Chief audit executives should seize opportunities to improve corporate governance, notably by introducing or enhancing innovative risk management practices and practising combined assurance (Lenz *et al.*, 2018:31-32). Key in this regard are negotiating skills for gaining acceptance of recommended improvements and innovations as well as regular and timely communication between the chief audit executive and the audit committee (Lenz *et al.*, 2018:33). The relationship between the chief audit executive and the audit committee fosters 'shared knowledge and common goals', supporting greater audit committee appreciation for internal audit's contribution and a strong mandate for the chief audit executive to 'challenge senior management when that is needed' (Lenz *et al.*, 2018:33). Understandably, when management choose to rotate internal audit staff, keeping the chief audit executive position intact contributes to internal audit effectiveness (Christ *et al.,* 2015:37). Conceivably, the chief audit executive influences reliance.

In summary, the complexity in internal auditors' dual governance role pervasively influences the real and the perceived value of internal audit as an objective assurance provider on the effectiveness of governance, risk management and internal control processes. The complexity inherent in internal audit's role and the pervasive influences on that role exerted by management and the audit committee reciprocally influence the appropriateness and fairness of reliance decisions.

2.5.4 The audit committee

The audit committee oversees all aspects of the statutory financial reporting and external audit processes and it thus has a pervasive influence on reliance. The effectiveness of the audit committee is of particular concern.

2.5.4.1 The audit committee's role

The audit committee has specific oversight and reporting responsibilities. Legislation includes requirements and governance codes recommendations on the composition and functioning of audit committees. This section considers how and when these influence reliance.

(a) Audit committee oversight

The board of directors typically delegates oversight of assurance and statutory financial reporting to the audit committee, usually consequent to a statutory requirement (for example, Republic of South Africa, 2008: section 94). Legal requirements and governance principles set out recommendations for the role of the audit committee (for example, section 94 of the Companies Act (Republic of South Africa, 2008) and parts 5.3 and 5.4 of King IV (IoDSA, 2016)). In their review of a decade of evidence from the United Kingdom, Untied States and Australia on the governance role of audit committees, Ghafran and O'Sullivan (2013:381-382) recognise the 'powerful' contribution of audit committees to improved governance.

Both the current and previous corporate governance codes of South Africa include specific principles and recommendations applicable to audit committee oversight. King III principles (IoDSA, 2009) require independent audit committee oversight of (i) management's integrated reporting (principle 3.4), (ii) the application of the combined assurance model (principle 3.5), (iii) the expertise, resourcing and experience of the organisation's finance function (principle 3.6), (iv) the independence, resourcing, standing, audit plan and quality of internal audit (principle 3.7), (v) the risk management process (principle 3.8) and (vi) the appointment, independence and remuneration of the external auditor as well as the quality and effectiveness of the external audit process (principle 3.9). King IV (IoDSA, 2016: Part 5.3) recommends independent audit committee oversight of (i) the effectiveness of assurance functions and services, particularly combined assurance arrangements, internal and external assurance providers and the finance function (recommended practice 51.a), (ii) the integrity of the annual financial statements (recommended practice 51.b) and (iii) the management of financial and other risks which may influence the integrity of reports issued by the organisation (recommended practice 54). Considering the focus of audit committee oversight is the statutory financial reporting and external audit processes, such oversight is likely to influence reliance.

Academic studies report that effective audit committee oversight requires 'asking challenging questions and assessing responses provided by managers and auditors' (Gendron, Bédard & Gosselin, 2004:153). Audit committees base the trustworthiness of managers' and auditors' responses on the 'degree of consistency across responses provided by the diverse parties that [audit committees] question, and the credibility that these parties develop over time with regard to the validity of their previous answers' (Gendron *et al.*, 2004:169).

The audit committee has several reporting duties. It should report to the shareholders in the statutory financial reports about the integrity of the financial reporting function and statutory financial reports, the effectiveness of internal financial controls and the independence of the external auditor (JSE, 2019: section 3.84(g), 16.10(u); IoDSA, 2016: part 5.3 recommended practice 51, 59). In addition, King IV (IoDSA, 2016: part 5.3 recommended practices 53-54, and 59; part 5.4 recommended practice 48-61) specifically requires audit committee oversight of and reporting in the annual report on the effectiveness of management's risk management processes, the chief audit executive and internal audit, as well as on the quality of the external audit. Academic research mostly associates the audit committee's oversight role with financial reporting quality (for example, Shepardson, 2019), external audit quality (for example, He *et al.*, 2018) and internal audit effectiveness (Alzeban, 2015). The annual report should also include a declaration by the audit committee chair explaining how the committee discharged its duties (IoDSA, 2016: part 5.3 recommended practice 50, 59).

(b) Audit committee effectiveness

Legislation includes requirements and governance code recommendations on the composition and functioning of audit committees. These are fundamental to the effectiveness of the oversight role of audit committees (Cohen *et al.*, 2010:765). Typically, audit committees should consist of a minimum of three members (IoDSA, 2016: part 5.3 recommended practice 46; Republic of South Africa, 2008: section 94), all of whom should be independent non-executive directors (Republic of South Africa, 2008: section 94). As directors, audit committee members incur personal liability when performing their duties negligently or maliciously (Republic of South Africa, 2008: section 77). In addition, the audit committee as a whole should possess the financial skills and experience required for effective oversight (IoDSA, 2016: part 5.3 recommended practice 55). In South Africa, however, the skills and experience requirements for audit committees have not yet been defined (Republic of South Africa, 2008: section 94). The draft of the Sarbanes Oxley Act initially proposed that audit committee members should all possess 'accounting financial expertise'; thus, they should hold professional designations such as Chartered Professional Accountants or Chartered Financial Analysts (Bilal, Chen & Komal, 2018:253-254). However, in the adopted version, section 407 actually refers to the appointment of at least one 'audit committee financial expert', who may have experience as a financial analyst or investment banker (Bilal *et al*., 2018:253-254).

Research findings support the appropriateness and effectiveness of the requirements for effective audit committees (Ghafran & O'Sullivan, 2013:381). Turley and Zaman (2007:779) explain that 'the ability of the audit committee to influence the power relationship between external auditors and executive management is a function of the standing, quality and experience of its members'. Academic research confirms that the audit committee's adherence to requirements for their effectiveness influences reliance (Krishnamoorthy & Maletta, 2016:62).

In terms of the reciprocal influences between corporate governance mechanisms, independent audit committee members are supported in their oversight role by internal auditors' independent and objective assurance reports. These attest to the effectiveness of risk management and internal control processes implemented by management (IoDSA, 2009: principle 7.4; Edge & Farley, 1991:70). Additional support is provided by the external auditors' communications about the scope, timing and significant findings of audits, for example, external auditors' conclusions about the fairness of management's 'subjective judgments' (IAASB, 2018: ISA 260; Cohen *et al.*, (2017:1204).

Academic studies confirm that audit committee oversight and requirements contribute to the quality of internal controls (for example, Naiker & Sharma, 2009:559), internal audits (for example, Alzeban, 2015:539) and external audits (for example, Ghafran &

O'Sullivan, 2013:381) and financial reporting (for example, Bilal *et al.*, 2018:253). A framework developed by Gaynor *et al.* (2016:8, 11) includes the audit committee, internal controls and internal audit as the primary determinants of 'pre-audit financial reporting quality'. Financial reporting quality is a determinant of external audit quality. Conceivably, the individual and reciprocal influences of the strength of internal controls, internal audit's assurance role and the audit committee's oversight role influence reliance as each of them influence external audit quality.

Concerning the influence of audit committee oversight and effectiveness on internal controls, Krishnan (2005:649, 670) reports that significantly less internal control weaknesses occurred in companies where all audit committee members were independent and at least one had financial expertise. Furthermore, Naiker and Sharma (2009:559) observe that less internal control deficiencies are reported in terms of SOX when the audit committee included former external auditors, irrespective of whether the former partners were from audit firms affiliated with the organisation's current external auditor or not, confirming the value of audit committee accounting expertise even when social ties were present.

Academic studies report associations between a strong internal audit role and the audit committee's oversight and effectiveness. For example, audit committee independence and expertise contribute to internal audit's independence and work performance. Specifically, the presence of only independent auditing and accounting experts on the audit committee contribute to internal audit's compliance with the Standards (Alzeban, 2015:539). In a study by Zain *et al.* (2006:1), the chief audit executives confirmed an association between accounting financial expertise on the audit committee and more intensive oversight of internal audit's work programmes and greater coordination of internal and external audit work. Fully independent audit committees with at least one accounting or finance expert have been linked to longer private meetings between the audit committee and the chief audit executive, as well as audit committee oversight of internal audit work (Raghunandan, Read & Rama, 2001:105). Notably, Christopher *et al.* (2009:200) report that internal audit's independence can come under threat in an audit committee without at least one member with accounting financial expertise.

Audit committee composition influences external audit quality. By way of example, greater audit committee size, independence from management and financial expertise are associated with wider external audit coverage and assurance (Ghafran & O'Sullivan, 2013:381). However, despite meeting the requirements for audit committee composition, some audit committees conceded some power to management, such as the power to appoint and dismiss the external auditor (Cohen *et al.*, 2010:777). In a study by Beattie *et al.* (2013:75), external auditors conveyed that audit committee independence and audit experience contributed to external audit quality, but some suggested that the independence requirements should improve as they had experienced the need to 'fight' with the audit committee chair on key matters of principle. From another perspective, He *et al.* (2018:63, 67, 69, 73) report that when audit committee members lacked independence from external auditors on the basis of common social ties (similar qualifications, family connections and / or education and employment affiliations), external auditors were less likely to issue modified audit opinions when material financial reporting irregularities requiring modification surface after the audit opinion had been issued.

A stream of research relates requirements for the composition of audit committees to management's financial reporting quality. Audit committee financial expertise moderated earnings management, with accounting expertise contributing even more to earnings quality (Bilal *et al.*, 2018:253). Lee and Park (2019) conclude that audit committees' financial expertise curtailed management's tendency for overly opportunistic disclosures, while audit committees' accounting financial expertise curtailed such disclosures even more. Shepardson (2019:59) affirms that audit committee members' prior experience in decision-making about complex, subjective accounting estimates induced conservative rather than contagion oversight of management's financial reporting practices by the audit committee as a group. In addition, Schmidt and Wilkins (2013:221) note that companies with more financial experts on their audit committees as well as companies with audit committee chairs who were accounting financial experts issued restated financial statements significantly sooner after the need for restatement was identified than others. However, Tanyi and Smith (2015:59) report that audit committee chairs and audit committee financial experts who held numerous appointments in audit committees were less effective at monitoring and overseeing statutory financial reporting. In addition, audit committee independence from the chief executive officer moderated earnings restatements (He *et al.*, 2018:242).

Several studies have examined the effects of combinations of audit committee requirements on financial reporting quality. For example, Ghafran and Yasmin (2018:13) conclude that audit committee chairs' financial expertise, longer tenure and involvement in additional board committees determined timeliness of statutory financial reporting. However, while Beasley (1996:443) concludes that audit committee members with longer board tenure benefit from firm-specific knowledge gained, Vafeas (2003:1043) cautions that longer board tenure compromises audit committee members' independence from management. In another study, Abbott, Parker and Peter (2004:69, 71, 76) affirm that significantly less financial restatements occurred in companies where the audit committee consisted entirely of independent directors, at least four audit committee meetings took place annually (a proxy for diligence) and the audit committee included at least one member with financial expertise.

2.5.4.2 The audit committee's interpretations and interests

Libby *et al.*'s (2015:26) review of academic literature highlights that audit committee members' general interest in self-protection moderated their interest in satisfying management. Audit committee are particularly interested in mitigating the risks of claims associated with litigation and reputational damage from their role as audit committee members. Audit committees have been found to use internal and external audit as protection against reputational damage; they particularly value higher-quality external audits with internal audit complementing rather than substituting external audit work (Zain *et al.*, 2015:140). However, audit committees encourage chief audit executives to actively pursue a 'joint audit approach' with external auditors; this is because 'combining the knowledge and expertise of internal and external auditing via well-considered collaboration, [offers] a way of combining both sources of comfort, thereby enhancing the overall level of comfort for the audit committee' (Sarens *et al.*, 2009:102).

2.5.4.3 The audit committee's practices

Academic studies have been conducted on audit committee practices influencing reliance. For example, in the study of Abbott *et al.* (2012a:96), chief audit executives reported that external audit fees decreased from more reliance when a strong relationship existed between an in-house internal audit function and the audit committee rather than management. In the study of Zain *et al.* (2006:1), chief audit executives also reported that the extent of audit committee oversight of internal audit work programmes and coordination with external audit influenced reliance. In a similar vein, external auditors indicated that internal audit's reporting relationship with the audit committee, particularly private meetings between the audit committee and internal audit, influenced reliance (Munro & Stewart, 2011:465-466). In contrast, external auditors stated that 'passive' audit committees were unable to resolve disagreements between management and external auditors, for example about contentious accounting practices (Cohen *et al.*, 2010:752, 767). Clearly, audit committee oversight practices influence reliance.

Some authors debated whether audit committees' oversight practices substantively contributed to corporate governance or were applied as a mere ritual or ceremony to propagate the belief that corporate governance was sound (Brennan & Kirwan, 2015:474). As an example of ritualistic oversight, Spira (1999:248) provides evidence that 'the process of questioning was a necessary formality … [and] questions posed by audit committee members were not sufficiently penetrating to address the underlying issues'. Such symbolic oversight practices are concerning given the finding of Gendron *et al.* (2004:169) that 'a key aspect of the work carried out by audit committee members consists of asking challenging questions and assessing responses provided by managers and auditors'. Beasley, Carcello, Hermanson and Neal (2009:65, 73) report that a combination of substantive and ceremonial or ritualistic practices was present in public company audit committees.

The interview guide included the following discussion point considering the influence of the audit committee on reliance.

LINK TO DISCUSSION POINT IN INTERVIEW GUIDE

Determining the audit committee's influence on reliance

DISCUSSION POINT 14: How does the audit committee of the company influence your external auditor's use of the work of internal auditors?

In summary, the audit committee's oversight role and the antecedents of effectiveness are clearly defined. Although research supports the pervasive influence of audit committee oversight on financial reporting quality, internal audit quality and external audit quality, concerns have been expressed about the effectiveness of audit committees in reality.

2.6 COMBINED ASSURANCE

Providing further support of the reciprocal influences of corporate governance mechanisms on each other, King III and IV refer to the involvement of management as well as internal and external audit in the risk management and control processes as the 'combined assurance model' (IoDSA, 2016: page 10, 31, part 5.4 recommended practice 48-61; IoDSA, 2009: principle 3.5). Zhou, Simnett and Hoang (2019:235-236) characterise combined assurance as a 'novel', 'innovative, credibility-enhancement mechanism … to optimize the assurance coverage obtained from management, internal assurance providers and external assurance providers'. The audit committee oversees combined assurance arrangements and reports on their effectiveness in the annual report (IoDSA, 2016: part 5.3 recommended practice 51, 59; part 5.4 recommended practice 40-43).

Academic studies have been conducted on the benefits and practices of effective combined assurance. For example, Decaux and Sarens (2015:58) note that effective combined assurance depends on specific practices. These include implementing mature organisational risk management processes, appointing a ‘combined assurance champion’ (typically the chief audit executive), creating a combined assurance strategy and awareness, reporting on combined assurance findings and mapping assurance activities to specific assurance providers (Decaux & Sarens, 2015:58). Zhou *et al.* (2019:235) furthermore conclude that participants in capital markets valued information about combined assurance in integrated reports of companies for decision-making.

King III specifically associates combined assurance with cooperation between internal and external audit for preventing unnecessary overlap between the two (IoDSA, 2009: principle 3.7 recommendation 56). King IV, however, does not include such a specific link. Moreover, academic studies on combined assurance (for example, Zhou *et al.*, 2019; Decaux & Sarens, 2015) do not highlight such an association. A possible explanation for this absence may be a preference for complementary rather than supplementary use of assurance from internal and external audit. For example, Goodwin-Stewart and Kent (2006:387, 388) point to an association between higher external audit fees and more frequent audit committee meetings and the presence of internal audit. They conclude that firms with more internal monitoring ‘recognize the importance of both types of audit as mechanisms to strengthen corporate governance’. Similarly, Hay, Knechel and Ling (2008:9) report that internal audit is a complementary control measure associated with higher external audit fees.

In summary, from the above discussion and supporting sources, the reciprocal influences of the corporate governance mechanisms on the statutory financial reporting and external audit processes, including reliance, are as follows:

Summary of reciprocal influences of corporate governance mechanisms on statutory financial reporting and external audit processes, including reliance:

Management should:

- adopt a combined assurance approach for
- maintaining effective governance structures,
- including a finance function,
- risk management,
- internal financial controls, and
- an **internal audit function**,
- supporting the preparation of credible statutory financial reports,
- for audit by the organisation's independent **external auditor**,
- and issue the statutory financial reports,
- approved by the board and signed by an authorised director,
- approved by the **audit committee**,
- within 4 months of a company's financial year-end date and a minimum of 15 business days prior to the company's annual general meeting.

The independent **external auditor** should:

- audit the statutory financial reports prepared by **management**,
- within the combined assurance approach,
- cognisant of the risk of material misstatement of financial statements,
- including from account subjectivity and management's control environment,
- anchored in management's governance, risk management and internal control processes, including monitoring controls provided by **internal audit's** compliance audits,
- and, if appropriate, practice reliance in accordance with the related framework,
- while engaging in two-way communication with the **audit committee** about the external audit and reliance,
- before issuing an audit report containing an appropriate audit opinion.

Internal audit should:

- participate in combined assurance,
- including through compliance audits,
- by sharing information and coordinating activities with the external audit team,
- and, should annually provide the **audit committee** and board with an overall statement attesting to the effectiveness of the organisation's governance, risk management and internal control processes.

The **audit committee** should:

- oversee the effectiveness of **management**'s statutory financial reporting,
- including the finance function,
- risk management and internal financial controls, and
- the **internal audit** function.

2.7 CONCLUSION

The unconventional inclusion of this chapter provides some understanding of reliance and the complexity of the reliance decision. It highlights the potential for misunderstanding the reciprocal influences on reliance by multiple stakeholder groups' diverse roles, interpretations, interests and practices and, ultimately, the serious implications of the reliance decision for external audit quality and the external auditor's liability. Central to this complexity is the question: How can external auditors' reliance on internal auditors' work be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors?

Chapter 3 explains how the research methodology of this study addresses this question.

CHAPTER 3

RESEARCH DESIGN AND METHODOLOGY

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RESEARCH DESIGN AND METHODOLOGY

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3.1 INTRODUCTION

Chapter 2 contextualised reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee, internal and external auditors.

This chapter starts off by considering and explaining the appropriateness of the design and methodology chosen for this study, namely, the interpretivist paradigm and the qualitative classic grounded theory methodology. A brief overview of the grounded theory methodology is provided. This is followed by notes on theoretical sensitivity, theoretical sampling and constant comparison as part of the characteristic joint collection, coding and analysis of data in grounded theory studies.

The remainder of the chapter conveys how the classic grounded theory methodology was implemented in this study to construct a substantive theory. Charmaz (2014:344) defines a substantive theory as 'a theoretical interpretation or explanation of a delimited problem in a particular area'. This study was conducted in three phases. For phase 1, the sampling requirements are explained, considering the unit of observation and analysis, and appropriate cases (data sites) and participants. This is followed by a description of joint initial data collection, open coding and analysis and an indication of how these processes delimited the main concern and substantive categories, including the core category. For phase 2, joint further theoretical sampling, selective and theoretical coding and analysis to saturate the substantive categories and their connections to the core category are described. The explanation of phase 3 considers the sorting of the substantive categories into theoretical constructs and how the theory is reported. The purpose of comparing the substantive theory to extant knowledge is also considered.

In qualitative studies, the researcher is the research instrument, hence researcher subjectivity and their interpretive role are also addressed. The chapter concludes with a brief reflection on the choice of the grounded theory methodology.

Some quotations included in this chapter are in italics, similar to their presentation in the original texts.

3.2 SELECTING THE APPROPRIATE RESEARCH DESIGN AND METHODOLOGY

This section justifies the suitability of the selected research design and methodology, considering the research question of this study.

3.2.1 Understanding what the study requires

The research design connects the ‘point of departure’ of the study to the ‘kind of results’ sought from the study (Babbie & Mouton, 2001:75). Brennan (2019:693) advises that the researcher should ‘synchronise’ the ‘complex system of moving parts’ of the research design, meaning that ‘the literature review, research questions, research methods, results / findings and contribution must be “all-singing, all-dancing” coherent and internally consistent.’

The point of departure of this study is the research question: How can reliance on internal audit work by external auditors be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors (stakeholder groups)?

Breaking down the research question provides clues for selecting the appropriate research design and methodology. First, this study is concerned with reliance. Reliance and factors which influence it are not fixed; they cannot be independently determined by outsiders to nor by observation from within the statutory external audit process. Second, this study is concerned with the reciprocal influences on reliance by the roles, interpretations, interests and practices of each of four stakeholder groups. Third, qualitative data in the form of intensive interviews with participants representing all four stakeholder groups realistically could provide useful empirical data about reliance. Fourth, the unit of analysis is the reliance process, while the units of observation are the participants’ statements conveying their constructions of reliance, within the context of the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups.

Thus, it is proposed that the qualitative classic grounded theory methodology, falling within the interpretivist paradigm, would generate a substantive theory able to provide a conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups.

The next two sub-sections justify the appropriateness of an interpretivist paradigm and the qualitative classic grounded theory methodology.

3.2.2 Justifying the choice of an interpretivist paradigm

Accounting (including auditing) is categorised as a ‘new profession’ (De Vos *et al.*, 2011:14). The scientific study of professionals falls into the realm of the social sciences. Social sciences study human ‘beliefs, behaviour, interaction, institutions’ (Neuman, 2000:6 in De Vos *et al.*, 2011:5). Thus, according to Babbie and Mouton (2001:22), studying social sciences is ‘complex’ compared to studying ‘simple’ natural sciences. This is because human beliefs, interactions, behaviours and institutions constantly change, are hard to observe and are difficult to accurately measure with laboratory instruments (De Vos *et al.*, 2011:5). Comparing reliance to these complexities of social science research guides the most appropriate orienting frame for the design of this study.

Considering constant change, observability and measurement of reliance, reliance and influences on reliance are not fixed, and not independently observable, nor objectively measurable factors. Reliance occurs within a specific organisation’s statutory external audit process at a given point in time. It is subject to the reciprocal influences of numerous, mostly subjective, requirements embedded in the framework provided in external auditing professional standards (IAASB, 2018: ISA 610 (Revised 2013)).

The literature indicates that reliance can be complex, as numerous changing factors linked to the statutory financial reporting process and the roles, interpretations, interests and practices of four stakeholder groups require simultaneous consideration when making the reliance decision (Quick & Henrizi, 2018:26; IAASB, 2018: ISA 610 (Revised 2013) paragraph 25; Trotman & Duncan, 2018:254; Singh *et al.*, 2014:36; Bame-Aldred *et al.*, 2013:251-252, 282-283; Brody, 2012:11; Desai *et al.*, 2010:538; Krishnamoorthy, 2001:499; 513; Maletta, 1993:508; Edge & Farley, 1991:77). Given the complexity of the study of social sciences, it is not surprising that most prior research has not attempted to portray a conceptualised understanding of reliance. Instead, most studies have been deductive, using quantitative methods and existing theory to test relationships between reliance and one or a small number of preselected factors from extant knowledge and theories (*a priori* use of theory). As a consequence, no conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups have been developed by previous studies.

In response to the complexities of social science research, various paradigms better suited to social research, have been developed. These paradigms vary in their degree of objectivity / subjectivity. Quantitative positivist paradigms are closely aligned to the notions of objectivity and precision that are characteristic of the natural sciences (De Vos *et al.*, 2011:5; Babbie & Mouton, 2001:15). Interpretive qualitative paradigms, including post-positivism, interpretivism and constructivism, each rely on progressively increasing levels of researcher and participant participation and subjectivity in the interpretive knowledge creation process (De Vos *et al.*, 2011:5; Babbie & Mouton, 2001:15). A brief reflection on the most critical epistemological and methodological features of these paradigms confirms the suitability of the interpretivist paradigm to the research question.

The positivist paradigm maintains that social science research should apply the same 'logic' as the natural sciences (Babbie & Mouton, 2001:21). Key features of positivist research include '[e]xperimental control, structured and replicable observation and measurement, quantification, generalization, and objectivity [independence between the researcher and the research object]' (Babbie & Mouton, 2001:27). Knowledge created by a positivist methodology provides a single, conclusive and replicable answer (De Vos *et al.*, 2011:6). Considering this study, deductive, quantitative, positivist methodologies would not be appropriate for inductively developing a conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups.

'Qualitative research paradigms' use an 'insider perspective on social action' as departure point (Babbie & Mouton, 2001:53). Recognised qualitative research paradigms include post-positivism, interpretivism and constructivism (De Vos *et al.*, 2011:7). Geertz (1980:165) explains that in the interpretive 'turn', following the earlier dominance of positivist research, ‘many social scientists have turned away from a laws-and-instances ideal of explanation toward a cases-and-interpretations one’.

Contrary to objectivist notions of positivism, post-positivism accepts participants’ interpreted reality, meaning that ‘multiple perspectives from participants rather than a single reality’ is possible. This is because ‘reality can never be fully apprehended, only approximated’ (De Vos *et al.*, 2011:7). Key aspects of post-positivist research include using small sample sizes and ‘qualitative’ or ‘multiple methods’. These aim to capture ‘reality’ using ‘evaluation criteria’ or ‘variables’ for ‘discovery and verification of theories’. The researcher is an instrument, working with ‘freedom’ and ‘subjectivity’, designing their own ‘measuring instruments’ for ‘structured’ even ‘statistical’ analysis (Charmaz, 2014:6; De Vos *et al.*, 2011:7).

Interpretivism seeks to understand human beings ‘in the process of making sense of their worlds’ as they subjectively ‘continuously interpret, create, give meaning, define, justify and rationalise daily actions’ (Babbie & Mouton, 2001:28, 33). Key traits of interpretivist research include using observable and non-observable data (for example, transcribed textual documents containing descriptions of interactions, actions and meanings of ‘self and others’ in their ‘daily life’). Interpretivism also favours a qualitative approach and views data from an ‘insider’ rather than an ‘objective’ perspective (Babbie & Mouton, 2001:28-29, 33). In the interpretivist paradigm, the researcher uses detailed reading of the data text to discern, albeit subjectively, the true meaning behind messages and the interconnections between them (De Vos *et al.*, 2011:8). Babbie and Mouton (2001:31, 32) mention hermeneutics and symbolic interactionism as interpretive approaches which frame interpretive knowledge creation.

Constructivism, on the other hand, allows the active involvement of both the researcher and the participants in all phases of the research process, starting from the formulation of the research problem (De Vos *et al.*, 2011:7-8). Constructivism explicitly recognises the role of the researcher as well as the research participants as co-constructors or partners in the process of gaining ‘an understanding of the world in which [the participants] live and work’ (De Vos *et al.*, 2011:7-8). This approach is considered ‘radical’ as it relinquishes ‘tight control’ over the research process (typical of the post-positivist and interpretivist paradigms), allowing ‘full empowerment of the participants' in an 'open and democratic' relationship between researcher and participants (De Vos *et al.*, 2011:8). The researcher makes a statement about their own subjectivity and efforts to temper personal influences and biases with regard to the research findings (Charmaz, 2014:14).

Deciding on a qualitative research paradigm appropriate for this study rested on the increasing levels of interpretation as well as researcher and participant participation inherent in each of the qualitative research paradigms (Babbie & Mouton, 2001:53). The interpretivist paradigm was deemed most appropriate, considering this study's focus on detailed reading of data text (De Vos *et al.*, 2011:8) to discern context relevant (Charmaz, 2014:113) influences on reliance, exerted by multiple stakeholders' 'human action from the insider's perspective' (Babbie & Mouton, 2001:53) as they 'continuously interpret, create, give meaning, define, justify and rationalise daily actions' (Babbie & Mouton, 2001:28, 33).

Choosing the interpretivist paradigm for this qualitative classic grounded theory methodology is aligned with the views of Babbie and Mouton (2001:31-32), who regard symbolic interactionism as interpretive knowledge creation. This notion is supported by Grbich (2013:80) and Charmaz (2014:14), who recognise the social interactionist underpinning of grounded theory, which 'presumes that reality is a constructed and shifting entity' and that 'social processes can be created and changed by interactions among people'. Although Charmaz (2014:13-14) refers to 'constructivist' grounded theory, she does not necessarily imply 'open and democratic' active participant involvement in every phase of the research process (De Vos *et al.*, 2011:8). She uses the term 'constructivist' to 'acknowledge subjectivity and the researcher's involvement in the construction and interpretation of data', while distancing herself from 'radical subjectivism' (Charmaz, 2014:14).

Glaser (2002) openly distances himself from Charmaz's labelling of grounded theory as 'constructivist'. He is adamant that the researcher does not participate in co-constructing data (Glaser, 2002:2). He explains that 'the participant not only tells what is going on, but tells the researcher how to view it correctly-his/her way. I do not mean that they mutually build up interpretations' (Glaser, 2002:3). Rather than co-construction of data, Glaser (2002:2) holds that the grounded theory researcher overcomes complexity inherent in 'multiple perspectives among participants [which] is often the case' by 'rais[ing] these perspectives to the abstract level of conceptualization', thus reducing and integrating them around a 'core variable'. In subsequent sections of the chapter, the researcher of this study reflects on potential subjectivity in interpreting the meaning and actions of the participants' statements.

3.2.3 Justifying the choice of the classic grounded theory methodology

This study uses the classic grounded theory methodology (Glaser, 1978; Glaser & Strauss, 1967) in an area which, over the last 50 years or so, has received extensive attention in professional and governance pronouncements as well as the academic literature. The choice of classic grounded theory is based on the current lack of a conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups. The choice of this methodology is supported by Glaser (1978:10), who points out that grounded theory is not only suited to studying 'untouched' areas of investigation. However, when researchers study 'well-trodden' areas, their work should remain 'grounded' in data and not fall back on extant knowledge (Glaser, 1978:10). Specifically, the grounded theory methodology book *Theoretical sensitivity* (Glaser, 1978) is used throughout this thesis as the dominant methodological text. This choice is supported by Glaser (1998:13, 14) asserting that 'grounded theory is a package. It is a revolving-step method … You can read what the total package is in "Theoretical Sensitivity" (Sociology Press, 1978)'.

Glaser (1978:10) asserts that grounded theory studies 'in well-trodden fields' (*sic*) always offer a 'useful contribution' as they generate new categories, increasing understanding, by transcending extant literature and theories. The inductive nature of the grounded theory methodology (Glaser, 1978:37) implies that a study starts out by collecting empirical data, enabling the construction of abstract theoretical explanations of what is occurring in a substantive area. Thus, conceptualisations of data inherent in grounded theory transcend what is known as they explicate and resolve problems by interpreting patterns of behaviour addressing problems (Glaser, 1978:3). The outcome is a substantive theory that 'fits' the data and has 'relevance' (Glaser, 1978:4-5). This is because it explains and predicts past, current and future events occurring in the substantive area (Glaser, 1978:4-5). Contributions to substantive practice arise as those involved in the area clearly understand the theory (Glaser & Strauss, 1967:3). These contributions of grounded theory studies are coherent with this study's research question.

Researchers support Glaser's strong contention that the classic grounded theory methodology implies emergence rather than forcing in the process of theory development (as discussed in Bello, 2015; Sutton, Reinking & Arnold, 2011; Gurd, 2008, Glaser, 1998, 1992, 1978; Parker & Roffrey, 1997). These authors associate emergence with Glaser's classic grounded theory and forcing with the 'Straussian School' of grounded theory (for example Bello, 2015:42). Two main differences are cited as examples of emergence versus forcing. Firstly, the Straussian School studies a 'pre-determined phenomenon' while Glaser's classic ground theory sets out to develop a substantive theory addressing the 'main concern of the participants', unbeknown to the researcher prior to data analysis (Bello, 2015:42; Sutton *et al.*, 2011:60-61; Gurd, 2008:123; Parker & Roffrey, 1997:214).

Secondly, the Straussian School adopts a more rigid approach using 'preconceived tools and techniques … to shape theorising' (Bello, 2015:42). Particularly, Corbin and Strauss (2015:156) recommend using a coding 'paradigm' as 'an analytic tool to help analysts carry out axial coding … around a category'. The 'features' of the 'paradigm' are 'conditions', 'actions-interactions' and 'consequences or outcomes' (Corbin & Strauss, 2015:156). Contrariwise, Glaser (1998:165) posits that 'there could be 100's' of theoretical codes for achieving grounded theory integration. Thus, Glaser (1998:166-168) strongly opposes using such 'preconceived theoretical codes' as he opines they 'are forced on the concepts as the ONLY way to see them theoretically … It is too forcing and specific compared to the immense scope and power of yield to the full variable, emergent use of ANY of the theoretical codes that may emerge'. Glaser (1998:163) holds that relying on emergence ensures that 'theoretical codes implicitly conceptualize how the substantive codes … relate to each other as interrelated, multivariate hypotheses in accounting for resolving the main concern'. While Glaser mentions as examples a 'very comprehensive' list of theoretical codes in *Theoretical Sensitivity* (1978:72-82), his later work supplements the list (Glaser, 1998:170-175).

Gurd (2008:123) analysed 23 accounting studies' adherence to 'four key canons' of the grounded theory method; these canons are regarded as 'uncontested' as they are imbedded in the works of several researchers, including the originators of various different grounded theory 'traditions'. These canons are: (1) 'an iterative process of data collection and analysis', (2) 'theoretical sampling', (3) 'the constant comparative method' and (4) 'the explanation of coding and the theory building process'. (In the current study adherence to these key canons are explicated in sections 3.5 to 3.8.) Overall, Gurd (2008:129) concludes that only one of the 23 studies consistently adhered to the key canons. The analysis of Gurd (2008:129) revealed that accounting researchers tend to favour using the 'functionalist approach' providing a 'step by step approach' of the Straussian School. Sutton *et al.* (2011:60) suggest that the 'Strauss' approach is attractive in terms of the guidance and structure it provides', yet they point out that the 'Strauss' approach is also potentially limiting, and the theory development … may not be as rich'. They (Sutton et al., 2011:61) concluded:

> The Glaserian method requires a depth of data discovery within the theoretical sampling phase, and requires the researcher to analyse and classify the data into categories. This should not be seen as either a quick or easy challenge. Rather, the researcher should allow the research problem and the research questions to emerge as he or she immerses him or herself in the richness of the environment. The researcher should sample, categorize, sort, re-visit, sample more data, and renew the process over and over until the theory emerges with clarity that is supported by the data categorizations'.

In light of the different outcomes achieved by the different grounded theory traditions, this study's choice of the classic grounded theory for overcoming the current lack of a conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups, is strongly supported.

3.3 UNDERSTANDING GROUNDED THEORY

This section outlines a methodological background to grounded theory, including its discovery and subsequent development, key distinctions of the methodology, key characteristics of a substantive theory as well as a brief note on the use of *a priori* theory – a contested point in grounded theory studies.

3.3.1 What is grounded theory?

Grounded theory studies deal with ‘action and processes’ within a specific context (Charmaz, 2014:113). The aim of a grounded theory study is the systematic construction of theory from qualitative data (Charmaz, 2014:1; De Vos *et al.*, 2011:318). Methodologically, grounded theory offers systematic and flexible guidance for collecting, analysing and conceptualising qualitative data (Charmaz, 2014:1). Thus, using a grounded theory methodology advances qualitative studies from simply describing a substantive area to explaining what is occurring in the area in abstract theoretical terms (Charmaz, 2014:8).

Grounded theory studies mostly produce substantive theories addressing specific problems in substantive areas. The report of a grounded theory study ‘explains the [phenomenon] in new theoretical terms, explicates the properties of the theoretical categories [constructs] and often demonstrates the causes and conditions under which the process emerges and varies, and delineates its consequences’ (Charmaz, 2014:10).

The grounded theory methodology is inductive, implying that the theory is a conceptualisation of data (Glaser, 1978:37). However, the method also uses deduction; first when sampling for comparative data related to inductively derived codes, and second when comparing the emerging theory to extant theories (Glaser, 1978:38).

3.3.2 Developments in the grounded theory methodology

The introduction of grounded theory provided new opportunities for creating scientific knowledge in the social sciences. At the time of the ‘discovery’ and description of grounded theory as a research methodology by Glaser and Strauss (1967), most social researchers applied positivist quantitative approaches to test hypotheses developed by prior studies. As a result, they ignored human problems that did not fit positivist designs (Charmaz, 2014:7). While grounded theory studies ‘fit emerging theories with data’ from theoretical sampling, quantitative studies ‘test preconceived hypotheses’ using a representative sample, to make generalisations (Charmaz, 2014:198).

Knowledge created from the inductive approaches which were used before grounded theory were viewed as ‘impressionistic’, ‘anecdotal’, ‘unsystematic’ and ‘biased’ (Charmaz, 2014:6). The literature credits Glaser and Strauss (1967) with demystifying qualitative data analyses from being a product of ‘oral traditions’ to ‘written guidelines’, making qualitative studies ‘credible’ and ‘rigorous’ (Charmaz, 2014:4, 8). In comparison to qualitative analysis using logical deduction, analysis in grounded theory begins with data, raises the conceptual level of the data through systematic analysis, and retains a strong connection with the data (Charmaz, 2014:8).

Since the first publication of the seminal work by Glaser and Strauss (1967), grounded theory has evolved. The two authors’ paths separated; Corbin joined Strauss in writing several books on grounded theory (for example Corbin & Stauss, 2015). While books co-authored by Strauss and Corbin incorporated additional technical analysis procedures with the promise of easier theory development, Glaser’s subsequent books (for example Glaser, 1978, 1998) preserved the fundamental aspects of the classic grounded theory (Charmaz, 2014:11). Charmaz (for example, 2014), who herself worked on grounded theory studies with Glaser as well as Strauss, became another proponent of grounded theory as methodology.

Charmaz (2014:12) argues that over time, grounded theory studies moved away from the ‘positivism’ reflected in earlier descriptions of the methodology towards what she refers to as ‘constructivist’ grounded theory. Charmaz (2014:17) sees grounded theory as building on ‘pragmatist underpinnings’ and ‘interpretive analysis’. She clarifies her interpretation of the term ‘constructivist’, stating that grounded theorists should recognise that the knowledge they create is not an ‘accurate rendering’ of the worlds studied, but constructions of those worlds interpreted by the researcher and participants, tempered by ‘structural and situational’ context (Charmaz, 2014:14, 17).

Thus, ‘constructivist’ grounded theorists emphasise context, interpreted understanding, researcher and participant interaction and the sharing of ideas. They do not argue against their subjectivity, but acknowledge and manage it by means of reflection on the researcher’s influence on the findings (Charmaz, 2014:14). According to Charmaz (2014:12), ‘constructivist’ grounded theory adheres to the original properties of grounded theory first proposed by Glaser and Strauss (1967), namely, being ‘inductive, comparative, emergent and open-ended’.

Considering the changing conceptions of grounded theory, Charmaz (2014:14-15) views the 'major versions' of grounded theory as 'a constellation of methods'. This implies that studies begin with 'inductive logic' and 'rigorous comparative analysis … to develop theoretical analyses'. Thus, Charmaz (2014:16) suggests that grounded theorists 'can adopt and adapt' grounded theory guidelines to 'solve varied problems and to conduct diverse studies'.

In summary, guided by the interpretivist paradigm, which is aligned to notions of the constructivist grounded theory advanced by Charmaz (2014:13-14), the rest of this chapter and Chapter 4 explains explicates how the 'flexible guidelines' of the classic grounded theory methodology were adopted and adapted in the process of constructing the substantive theory proposed in this study.

3.3.3 Distinctive characteristics of grounded theory research

This study adheres to the distinctive characteristics of grounded theory research proposed by Charmaz (2014:15), Glaser and Strauss (1967) and Glaser (1978). These include:

i. Conducting data collection and analyses simultaneously in an iterative process.
ii. Analysing interview data for implicit constructions by individual participants of their own and others' influences on reliance, rather than influences from underlying frames and structures.
iii. Using comparative methods in each stage of data collection and analysis.
iv. Grounding all substantive categories in data.
v. Systematic delimitation of the core category from successively higher levels of conceptualisation of data and codes using memos to describe substantive categories. (As memos capture the descriptions of substantive categories, including their properties, dimensions and connections to other categories, references to memos imply substantive categories (Glaser, 1978:87, 90)).
vi. Remaining focused on theory construction rather than description or application of current theories.

vii. Comparing, clarifying and saturating properties of and relationships between developing theoretical constructs using empirical data generated from theoretical sampling.

viii. Comparing the theoretical constructs to extant frameworks and formal theories to determine resonance and extensions.

ix. Developing a core category rather than covering all aspects of the empirical topic of reliance.

3.3.4 What is a substantive theory?

Grounded theory studies are useful for producing so-called ‘middle-range’ theories, including substantive and formal theories (Glaser & Strauss, 1967:32). Middle-range theories ‘fall between the “minor working hypotheses” of everyday life and the “all-inclusive” grand theories’ (Glaser & Strauss, 1967:33). At the outset of the study, the researcher should choose to develop either one substantive and / or a formal theory or a specific combination of both. They should then adapt the research methodology accordingly (Glaser & Strauss, 1967:33). In this study, the aim was to construct a substantive theory explaining reliance.

A substantive theory serves ‘a substantive’ or ‘empirical’ area, while formal theory is developed for a ‘conceptual’ area (Glaser & Strauss, 1967:32), beyond the substantive area. Thus, when constructing a substantive theory, the focus is comparative analysis among groups in the same substantive area, whereas constructing a formal theory requires comparison between different kinds of substantive areas falling within the formal area, without relating the cases to a single substantive area (Glaser & Strauss, 1967:33). Thus, for this study, data collection focused on data from the substantive area of reliance.

3.3.5 Using *a priori* theory

Two distinctive characteristics of grounded theory research provide guidance on the role of *a priori* theory in a grounded theory study. These distinctions are (i) grounding all substantive categories in data (Glaser, 1978:55) and (ii) systematically delimiting the core category from successively higher levels of conceptualisation of data, codes and categories using memos (Glaser, 1978:85). These distinctions imply that the grounded theorist does not simply apply theoretical ideas from extant literature during data collection and analysis. From a logic perspective, using *a priori* theory constitutes deduction, whereas interpretivist studies like grounded theory, start out with an inductive approach using data (Charmaz, 2014:14-15).

Initially, Glaser and Strauss (1967:34) explained that it is 'presumptuous to assume that one begins to know the relevant categories and hypotheses until "the first days in the field" at least are over'. Thus, comparison to other formal theories should wait until the substantive theory is formulated from the data. Later in their book, Glaser and Strauss (1967:46) reiterate that using *a priori* theory implies deduction, since committing to one exclusive 'preconceived' theory makes the researcher 'insensitive' to emerging ideas in the data, as all data is interpreted from the perspective of the preselected theory and all data and insights not fitting such *a priori* theory are disregarded as 'irrelevant'. Thus, Glaser and Strauss (1967:34, 37) advised that extant literature and theories should not be applied at the start of a grounded theory study; instead, similarities and convergences with the literature could be established after the 'analytic core' of categories became known.

However, in a later book, Glaser (1978:45) declares that having a 'general perspective' on a 'basic problem and social process[es]' is 'fine' as it would seldom 'derail the emerging analysis'. Glaser (1978:4) adds that 'we do not have to discover all new categories nor ignore all categories in the literature that might apply in order to generate a grounded theory' provided that the researcher 'refit[s]' all constructed categories back to data; otherwise, the 'theory and empirical world will mismatch' (Glaser & Strauss, 1967:6). Thus, extant literature and theories could inform the conceptualisation of data from the start of data analysis throughout the process of theory construction (Glaser, 1978:4).

Glaser (1978:32) suggests that literature which 'relates to the emerging theory' from the substantive field is used in the 'saturation stage', as the researcher 'reconciles, judges and imbues his work with the field as he compares' 'to show his contribution' once he 'knows his own categories quite well'. Thus, comparison of the grounded substantive theory to literature and theories related to the specific main concern and core category constructed from the data usually coincide with the later phases of theory development (Glaser, 1978:5, 93; Glaser & Strauss, 1967:34). However, the constructed grounded theory should not 'synthesize' with extant literature and theories; rather extant 'variables of relevance' should be compared to the grounded theory (Glaser, 1978:7). Particularly, 'similarities and convergences' identified when comparing the substantive theory to extant literature and theories could be useful pointers for refining and saturating the categories of the substantive theory, but only if the data allows it (Glaser & Strauss, 1967:37).

Given the researcher's background and professional involvement, it was not possible to approach the study with a 'clean slate' (*tabula rasa*) (Glaser & Strauss, 1967:3). However, conscious attempts were made to ensure that data collection and analysis were conducted inductively and constant comparison was used to 'refit' the constructed codes and categories to data (Glaser, 1978:4, 84).

3.4 THE RESEARCHER

This section first reflects on the role and influence of the researcher as an interpretive instrument on the research process, as is the case in qualitative studies. Then, the researcher's potential preconceptions are acknowledged and the processes used to limit these preconceptions are discussed.

3.4.1 The researcher as interpretive instrument

In positivist social studies, the researcher maintains a neutral attitude, objectively observing, measuring, quantifying and generalising quantitative data in a structured, controlled and replicable manner (Babbie & Mouton, 2001:27). In contrast, interpretivist social studies require a 'qualitative approach', with the researcher seeking an 'insider's perspective' by engaging with participants in the field, while collecting unstructured data through observation or interviews in order to delve into individual cases or events (Babbie & Mouton, 2001:33, 53). Glaser (2002:3) points out that researcher bias is 'just another variable' which is mitigated using 'constant comparative analysis'. He (Glaser, 2002:3) explains that interpretation implies that the participant does not merely share information, but also explains to the researcher how to interpret same. However, Glaser strongly points out that the researcher does not co-construct interpretations (Glaser, 2002:3).

In accordance with the interpretivist paradigm and qualitative classic grounded theory methodology of this study, the researcher of this study acted as an active instrument in every phase of this study. Thus, the researcher conceptualised the research problem, aim, question and design of the study from the ‘core category’ emerging from the data (Glaser 2002:2) and applied various forms of logic to the data initial and theoretical sampling, coding and analysis (Glaser, 1978:36-37).

Although the grounded theory methodology is inductive, a deductive approach was followed, as suggested by Glaser (1978:41), especially during selective coding, theoretical sampling and when comparing extant literature and formal theories to the emergent theory (1978:40). Glaser (1978:41) notes that the use of deduction in grounded theory studies ‘serves the inductive method; it is subservient to it, and ideas arrived at deductively must be discarded unless grounded’. Throughout this study, abduction was applied, with inferences about the meaning of data always fitted back to empirical data through constant comparison (Glaser, 2002:3).

As the researcher was not a ‘distant analyst’ but applied ‘insider knowledge’ (Charmaz, 2014:175), various strategies were used to temper any subjectivity, in accordance with the interpretivist paradigm. Charmaz’s (2014:132) suggestion was paramount in this regard: ‘What you see in your data relies in part upon your prior perspectives. Rather than seeing your perspectives as truth, try to see them as representing one view among many’.

3.4.2 The researcher’s preconceptions from experience, literature and theories

The interpretivist nature of this study implies that the researcher interprets qualitative data from an ‘insider’s perspective’ (Babbie & Mouton, 2001:33, 53). Thus, the researcher’s own preconceptions and theoretical ideas may come into play. Glaser (1978:2) explains that ‘[g]enerating theory is done by a human being who is at times intimately involved with … the data … [and has] … a long-term biographical and conceptual build up’. Such background makes the researcher ‘wise’ about the data and ‘how to detail its main problems and processes and how to interpret and explain them theoretically’ (Glaser, 1978:2).

Glaser and Strauss (1967:3, 6) emphasise that the researcher should ‘not approach reality as a *tabula rasa*’. Like Glaser & Strauss (1967), Charmaz (2014:156) also acknowledges that all grounded theory researchers start their research with ‘preconceptions’ and ‘ideas’ from earlier studies and experiences. However, while Glaser’s mostly positivist stance fails to acknowledge researcher subjectivity (Charmaz, 2014:9), Charmaz (2014:155) suggests a more realistic strategy for dealing with researcher preconceptions. The researcher should remain conscious of the influence of their preconceptions and theoretical ideas on their interpretations and assumptions when constructing codes, especially during selective coding, as ‘these codes shape our analyses’ (Charmaz, 2014:155). In keeping with the ‘constructivist turn’ in interpretivist qualitative research, Charmaz (2014:12-13, 155-160, 165, 167) advises that rather than ignoring possible biases, the researcher should write reflective memos or journals on the influence of any preconceptions on data collection and analyses. Thus, presented below are the researcher’s own preconceptions which arose in this study and how their impact on theory development was mitigated. This is conveyed in the first person for ease of understanding.

First, I used my earlier acquired professional, academic and research experience or ‘theoretical understandings’ as ‘starting points’ for theoretical sensitivity when collecting data, listening to voice recordings and reading and analysing transcripts (Charmaz, 2014:159). These understandings ‘sensitize[d]’ me to ‘broad questions’ raised during the interviews and data analysis as ‘guidelines and reference points’ about reliance (Glaser, 1978:39). However, all substantive categories, properties and dimensions were conceptualised from or fitted to data during the three phases of this study (Charmaz, 2014:159; Glaser, 1978:39). Probing questions raised during the interviews and the subsequent data analysis assisted me in grounding my conceptualisations in data (Glaser, 1978:48).

Second, I interrogated the data in an iterative and constantly comparative manner over an extended period of time. Thus, I developed an ‘intimate familiarity’ and an ‘in-depth … understanding’ of the data. This assisted in identifying and managing my own preconceptions as well as those of the participants (Charmaz, 2014:159). More specifically, I deepened my familiarity with the data through numerous rounds of coding and recoding, writing and rewriting memos on substantive categories, considering each statement as well as conceptualising and reconceptualising from different angles when making sense of the data. Thus, throughout, I engaged in iterative sampling, coding and analysis, using constant comparison, diagramming and memo-writing on substantive categories in the process (Glaser, 1978:22, 49-52, 83).

Third, during coding I used several strategies to ensure that the codes accurately reflected the data as opposed to what I believed it represented. I open-coded interview transcripts on a line-by-line basis (Charmaz, 2014:125; Glaser, 1978:57) and I observed and analysed the participants' statements conveying their constructions of reliance. I maintained a critical view of the data by questioning myself about what it represented (Charmaz, 2014:117, 160). I refrained from judging the participants' statements, constantly reminding myself to 'see the world through their eyes' (Charmaz, 2014:133). I triangulated my understanding of the data by comparing it with codes and 'refitting' those codes with the data several times, checking whether the participants' interpretive statements were aligned within and across interviews, participant groups and cases (Charmaz, 2014:159; Glaser, 1978:4). I extensively used *in vivo* codes to 'preserve' the participants' meanings of their views and actions (Charmaz, 2014:134). I also checked the codes containing my interpretations of participants' intentions, motivations and strategies back to supporting data (Charmaz, 2014:159).

Fourth, I often reflected on my evolving study in writing and in thinking exercises while alone doing household chores, in the shower or while driving (Charmaz, 2014:158). These entailed questioning myself about what was going on in my data and how my memos on substantive categories reflected the data – contemplating, diagramming, reviewing and refining the developing substantive categories using data.

Overall, I am satisfied that these reflective practices mitigated any preconceptions I may have had of the data and the topic.

3.5 UNDERSTANDING JOINT COLLECTION, CODING AND ANALYSIS OF DATA

'Joint collection, coding and analysis of data is the underlying operation' of a grounded theory study (Glaser & Strauss, 1967:43). The contribution of a grounded theory transcends extant knowledge by capturing 'seemingly separate incidences' in a small number of higher order conceptualisations (Glaser, 1978:7). This is achieved through joint data collection, coding and analysis. The researcher's growing theoretical sensitivity and theoretical sampling together stimulate the process of conceptualisation, while through continuous constant comparison, the researcher saturates and integrates substantive categories into theoretical constructs (Glaser, 1978:6, 7). Starting with an idea with 'theoretical power' from the data, the researcher constantly compares it to existing and further data by 'fitting and working' it into conceptualisations (Glaser, 1978:6, 10). Thus, Glaser (1978:31) advises that 'we collect the data in the field first. Then [we] start analysing it and generating theory'. Reading the literature is delayed until 'the theory seems sufficiently grounded and developed, *then* we review the literature in the field and relate the theory to it through integration of ideas' (Glaser, 1978:31). However, Glaser (1978:31) adds that '[i]f there is a particularly good theory in the field, one may cover this earlier and look for emergent fit'.

3.5.1 Theoretical sensitivity

Theoretical sensitivity implies that the researcher remains open to 'what is actually happening' in the data, rather than build theory using extant categories from logically derived preconceptions, ideas and hypotheses about solving the problems in the substantive area (Glaser, 1978:3). Glaser (1978:3) asserts that the researcher's theoretical sensitivity to the 'kinds of categories to generate' improves from 'intensive reading' of literature dealing with 'variables and their associated general ideas' related to problems in the area studied (Glaser, 1978:3-4; 32). However, Glaser (1978:4) emphasises the importance of 'refitting' all categories to more data by constant comparison. In the process of 'refitting', 'explicit, consistent and persistent' application of theoretical sampling and constant comparison cumulatively build dense theoretical sensitivity about the emerging theory (Glaser, 1978:37).

In this study, professional, academic and research competence and knowledge from reading about reliance over many years fostered the researcher's initial theoretical sensitivity. Yet, considering the complexity of reliance and the lack of an extant conceptualisation required a fully inductive approach, devoid of preconceived ideas on stakeholder groups' main concerns and their ways of resolving it. This meant it was necessary to focus on finding 'theoretical leads' to generate novel conceptualisations (Glaser, 1978:44). From the first interview, theoretical sampling and constant comparison deepened the researcher's initial theoretical sensitivity.

3.5.2 Theoretical sampling

Glaser (1978:36) views all sampling in a grounded theory study as 'theoretical sampling', although he distinguishes between initial and further data collection. The aim of theoretical sampling in a grounded theory study is 'conceptual elaborating' of substantive categories, their properties and connections as building blocks of the developing theory (Charmaz, 2014:212; Glaser, 1978:40). In contrast, other qualitative approaches use sampling for 'logical elaboration' of predetermined constructs obtained from extant theories (Glaser, 1978:40). Thus, while sampling usually focuses on collecting data representative of a population to obtain statistically generalisable results, theoretical sampling focuses on collecting data to develop substantive categories rather than finding recurring patterns from different sources (Charmaz, 2014:198-199).

Glaser (1978:36) explains that '[t]heoretical sampling is the process of data collection for generating theory whereby the analyst jointly collects, codes, and analyses his data and decides what data to collect next and where to find them, in order to develop his theory as it emerges'. Consequently, theoretical sampling means initial and further data collection is controlled by the emerging theory (Charmaz, 2014:197; Glaser, 1978:36). Earlier in a study, the principles of theoretical sampling are useful for checking 'emerging ideas' and 'emerging questions' by comparing 'data with data' (Charmaz, 2014: 200, 210). Then, for further data collection, theoretical sampling generates data that develops and delineates substantive categories, their properties, the dimensions of properties and connections (Charmaz, 2014:198-200).

The purpose of theoretical sampling is to iteratively generate and code initial and further raw data in the process of conceptualising (Glaser, 1978:36). Theoretical sampling is furthermore enhanced by applying constant comparative analysis to data and codes when developing substantive categories, their properties and connections (Glaser, 1978:36). Thus, continuous comparison and theoretical sampling develop, delimit and refine emerging theoretical ideas into substantive categories and compare them back to data. This continues to the point where categories and their properties are saturated (Charmaz, 2014:197). Theoretical sampling ceases when a category is saturated; this is where it can be delimited into a theoretical construct of the emerging theory (Charmaz, 2014:199; Glaser, 1978:36).

Regarding coherence between the research problem and sampling data, Glaser (1978:36) explains that grounded theory studies do not initially sample data about a 'preconceived problem'. Rather, initial theoretical sampling locates data covering a 'general … perspective about a substantive area within a population' (Glaser, 1978:36). Thus, when seeking to construct a substantive theory, theoretical sampling should first align the broader substantive topic and purpose of the study with accessible people in familiar settings (Charmaz, 2014:23, 197; Glaser, 1978:36; Glaser & Strauss, 1967:51, 54). During early initial data collection in the field, the researcher immediately starts the iterative process of generating codes and delimiting them into substantive categories and properties (Glaser, 1978:36-37). During further sampling, the relevance of categories and properties to the emerging theory can be 'checked and elaborated by asking top informants to appraise and give more data on [the] categories proving to become core to the analysis' (Glaser, 1978:47).

Glaser (1978:42) advises that sampling comparable groups should consider the purpose of comparison and the relevance of the groups to the broader research topic. He continues that sampling should ensure '*the variable to be compared has a value in each group*'. Glaser (978:42) even proposes flexible theoretical sampling for comparison across apparently non-comparable groups, as long as the groups share the experience. Thus, he contends that a flexible sampling strategy is appropriate for dealing with 'natural groups' whose exposure to the same experience cannot be determined or controlled at the time of sampling (Glaser, 1978:44).

In this study, theoretical sampling was conducted in several ways. First, initial sampling was not flexible but controlled, focused on theory development about the broader area of reliance. This was in the context of the statutory external audit of a specific organisation and reciprocally influenced by the roles, interpretations, interests and practices of four stakeholder groups – simultaneously influencing and influenced by reliance. Thus, from initial sampling, participants were chosen for their 'theoretical purpose and relevance' (Glaser, 1978:42).

Second, from the first interview, particular focus was placed on the participants' statements and explanations of the reciprocal influences on reliance by the roles, interpretations, interests and practices of the stakeholder groups. Theoretical ideas, pointing to the 'main concern' and 'core category', 'what sums up the pattern of behaviour' 'going on in the data' caught the researcher's attention from the first interview (Glaser, 1978:44, 94). These ideas impelled continuous theoretical sampling for data which was useful for fitting ideas as part of comparative analyses. Thus, ideas were continuously strengthened and reconfirmed with more data collected from within and across initial and further interviews. In the process, the researcher's theoretical sensitivity deepened, allowing the identification and coding of 'behavioural and attitudinal patterns' pointing to the core category (Charmaz, 2014:108; Glaser, 1978:44).

Third, from the first interview, probing and clarifying questions were important sources of theoretical sampling (Charmaz, 2014:191, 194, 200, 206; Glaser, 1978:44, 49).

Fourth, quotations with theoretical promise were also noted and compared to data collected earlier and later as well as the codes related to those quotations (Charmaz, 2014:194). As the theoretical ideas were refined, refocused and sharpened with data, the explicit and 'implicit behavioural and attitudinal patterns' in participants' statements were repeatedly reconsidered and recoded (Glaser, 1978:44). Following the first draft of the substantive theory, follow-up interviews with 'top informants' were theoretically sampled from the initial round of interviews. This was done to fit the emergent theory to more data (Glaser, 1978:39).

Fifth, concerning sampling for comparable groups, this study's selection was not flexible. This was because the focus of the study was not on constructing a theory fitting 'unanticipatable' (*sic*) 'natural groups [which] cannot be controlled' (Glaser, 1978:44, 50). Rather, the controlled focus of theoretical sampling geared for theory development was comparing the reciprocal influences on reliance of the roles, interpretations, interests and practices of four specific stakeholder groups involved in the statutory external audits of specific listed companies at a given point in time. Thus, theoretical sampling did not consider apparently non-comparable natural groups.

3.5.3 Constant comparison

In a grounded theory study, comparison drives sampling, analysis, theory construction and bringing in the literature (Glaser, 1978:38, 41; 49). The focus of comparison is not on identifying '*themes*' but on explaining 'patterns' of behaviour visible in the data (Charmaz, 2014:199).

From the first interview and coding, open codes capture 'incidents' describing participants' meanings and actions. During open coding, comparison initially focuses on iteratively comparing incidents to one another and to open codes, and then open codes to open codes. This is done in order to delimit open codes into 'concepts' embedded in substantive categories as properties, the dimensions of each property and the connections between substantive categories and properties. Open codes are delineated into substantive categories based on the '*concept-indicator model*' based on their 'underlining uniformity' (Glaser, 1978:49, 57, 62, 64). When deciding on codes' underlying uniformity, 'similarities, differences, and degrees of consistency of meaning' are considered (Glaser, 1978:62). As data collection and coding progresses, 'concepts' are compared to more open codes ('incidents' in the data), aiding further development of substantive categories (Glaser, 1978:49-50).

Considering the order of comparison, Glaser and Strauss (1967:55-56) recommend that data from largely similar groups or cases should be compared first, as doing so assists in identifying similarities and important differences as the basis of substantive categories and their properties. Subsequent comparisons to different groups or cases then highlight dimensions of properties (Glaser & Strauss, 1967:55-56).

As suggested by Glaser and Strauss (1967:55-56), first, the interviews from the four participants (representing each of the four stakeholder groups) of a single (thus similar) case (case B) were purposefully open-coded. Coding data from a single case first maximised opportunities to discern similarities pointing to theoretically relevant substantive categories and their properties. Then, coding interviews of other cases continued, allowing comparison across cases. Comparison of open codes not only delineated similarities and differences within and across cases, but also within and across stakeholder groups (Glaser, 1978:44). These comparisons highlighted fundamentally similar and different properties as well as the dimensional variations in properties across cases and groups (Glaser, 1978:43, 50, 120; Glaser & Strauss, 1967:51, 57, 62, 64). When theoretical constructs are developed, the properties of substantive categories are compared on a *'concept to concept*' basis to the core category. The properties are delineated based on 'best fit' to theoretical constructs (Glaser, 1978:50, 62-64, 84-85).

Glaser and Strauss (1967:54) also mention that the researcher can 'create groups' for comparison during data analysis. Data analysis revealed that two unique 'groups' were represented in the data of this study. First, the MORE reliance cases, consisting of a 'group' of data from two companies (B and E) where external auditors indicated that reliance was not limited. Second, the LESS reliance cases, that consist of a 'group' of data from three companies (A, C and D) where external auditors indicated that only limited reliance occurred.

Glaser (1978:50) further distinguishes between theoretical sampling 'in and out of a substantive area' for comparison. He advises that while 'going outside' a substantive area 'is usually stimulating', it is 'dangerous for its undermining effects on relevance' (Glaser, 1978:50-51). Thus, he concludes that it is only a 'must' for comparison when 'generating formal theory'. Considering sampling within a substantive area, Glaser (1978:52) distinguishes between sampling when generating a 'general substantive theory' (for example, a theory about a variety of chronic diseases) compared to a specific substantive theory (for example, diabetes as a single chronic disease). Thus, using the latter example, when generating a general substantive theory, theoretical sampling should include many chronic illnesses (Glaser, 1978:52). As the purpose of this study is to construct a substantive theory, and not to generate a formal theory or a general substantive theory, there was no theoretical sampling for comparison outside of the specific substantive area of reliance.

Concerning comparison to extant literature, Glaser (1978:38) advises comparing a new substantive theory to ‘a number of diverse theories which touch upon various aspects and levels of the emerging theory … [and] place the generated theory within a body of existing theories’. He explains that such comparison ‘often’ ‘transcends’ ‘part’ of the existing theories, adding ‘new perspectives and understandings … and highlight[ing] their processes’ (Glaser, 1978:38). However, comparison does not prove nor disprove the other or the emergent theory (Glaser, 1978:38). In this study, the emergent theory is compared to the stakeholder theory and the relational coordination theory, the summation model and organising framework developed from the most recent synthesis study on reliance (Bame-Aldred *et al.*, 2013) and internal and external auditing professional standards.

3.5.4 Overview of classic grounded theory data analysis

Joint collection, coding and analysis of data constructs a conceptualisation of reality in a substantive field, (Charmaz, 2014:79; Glaser, 1978:7; Glaser & Strauss, 1967:43). This section provides a holistic understanding of the three phases of grounded theory conceptualisation.

The aim of the first phase is to use open coded data to develop substantive categories and to choose one of those as the core category. At the start of the first phase, the researcher ‘simply reads data, lots of it, and gives common sense *impressions* in theoretical language as they may occur to him. He is completely unsystematic as to his approach to data or to how he arrives at impressions’ (Glaser, 1978:15). Glaser (1978:23) advises that the researcher should continue reading, coding, memo-writing (about developing substantive categories) and re-examining data, codes and categories as they analyse, despite being unsure and even unconscious of what they are doing.

While reading data, the researcher quickly notices and begins to systematically develop a ‘few major categories’ and connections between them (Glaser, 1978:15). Glaser (1978:20) points out that ‘in grounded theory, much happens fast … Categories emerge before a few interviews are over … one or two can be overriding or core concepts … integrations appear that seem to fit the data perfectly … The “real” problem seems to emerge quickly’. Yet, he advises that ‘theoretical pacing’ is needed to prevent rushed theory construction without a ‘true’ understanding of what the data holds (Glaser, 1978:20).

A true understanding of data can be gained through coding (Glaser, 1978:24). Memo-writing is an implicit part of coding; memos capture the developing substantive categories, which are later used to construct the substantive theory (Glaser, 1978:83-85, 116). Coding includes open coding, followed by selective and theoretical coding; however, the types and phases of coding ‘most often go on simultaneously’ (Glaser, 1978:56).

Open coding captures ‘incidents’ of meaning and action in the participants’ statements (Glaser, 1978:49-50). Using ‘indicators’ of ‘underlying uniformity’, open codes are delimited into substantive categories (‘conceptual code[s]’), with their properties, dimensions and connections (Glaser, 1978:62-64). While delimiting categories, open codes ‘force the generation of a core category’ and ‘some of its properties’ (Glaser, 1978:57, 59). With the core category established, the researcher is ready to progress to the second phase of conceptualisation.

The aim of the second phase is ‘further data collection and theoretical sampling’ to saturate the substantive categories and their connections to the core category (Glaser, 1978:61). Selective coding focuses the analysis on saturating substantive categories which are related to the core category ‘in sufficiently significant ways’ (Glaser, 1978:61). Analytic memos capture the development of substantive categories (Glaser, 1978:84-88). Theoretical codes conceptualise relationships between the core category and the substantive categories (Glaser, 1978:72). Theoretical memos capture the relationships between substantive categories and the core category (Glaser, 1978: 84).

Theoretical sampling, selective and theoretical coding and memo-writing continue until the substantive categories are saturated, meaning that the data does not produce any new properties, dimensions or connections (Glaser, 1978:16). Theoretical saturation indicates that the researcher is ready to progress to the third phase of conceptualisation.

The aim of the third phase is to delineate the analytic and theoretical properties in memos into an outline of the substantive theory. ‘Theoretical sorting’ of substantive categories (captured in memos) ‘put[s] the fractured data back together’, delineating the theoretical constructs of a coherent substantive theory (Glaser, 1978:16, 116).

3.5.5 Developing substantive categories in memos

During the first and second phases of conceptualisation, the outcomes of the joint process of collecting, coding and analysing data are captured in analytic and theoretical memos (Glaser, 1978:84-88). Analytic memos depict the properties, dimensions and connections of each substantive category (Glaser, 1978:84-88). ‘Theoretical memos’ capture the relationships between substantive categories and the core category (Glaser, 1978:84).

During the third phase of conceptualisation, theoretical memos are sorted into a ‘theoretical outline’ of the constructs of the emergent theory, which guides the write-up of the theory (Glaser, 1978:84-85, 94, 116). Given the grounded nature of substantive categories and their implicit connection to the core category, most properties of the substantive categories captured in analytic memos – indeed, up to 90% – should be connectable to the core category (Glaser, 1978:94, 123).

Rules for memo-writing ensure the usefulness of the memos during theoretical sorting and when reporting the theory (Glaser, 1978:87). The rules require that each analytic memo should (i) indicate the title of the substantive category or property it is about, (ii) highlight and (iii) discuss their relationship to other categories and / or properties mentioned in the memo (based on data, not ‘logical elaboration’), (iv) be kept separate from data, other than ‘clearly demarcated, useful illustrations’ referenced to the underlying data to enable writing the theory ‘straight from the memo’ and (v) be modified as insights and realisations of the researcher grow (Glaser, 1978:87, 90).

The typical content of an analytic memo used to develop a substantive category includes the conceptual properties and dimensions of the category, the ‘conditions’ under which a dimension ‘emerges or is evident’ and theoretically coded ‘connections’ between ‘categories and / or their properties’ as well as the ‘significance’ of those connections (Glaser, 1978:84).

The next three sections explain how the characteristics of theoretical sensitivity, theoretical sampling and constant comparison were applied during joint collection, coding and analysis in the three phases of theory construction of this study. The outcomes of the three phases are presented in Chapter 4 to 6.

3.6 PHASE 1: INITIAL THEORETICAL SAMPLING, JOINT COLLECTION, OPEN CODING AND ANALYSIS

This section describes the first phase of the study. It starts off by considering all aspects of initial sampling and data collection. It then briefly considers open coding and analysis aimed at delimiting the main concern and choosing the core category from the developing substantive categories. A detailed description and the outcomes of coding and analysis are presented in Chapter 4.

3.6.1 Initial theoretical sampling

This section describes how and where initial data were sampled.

3.6.1.1 Unit of analysis and observation

Glaser (1978:3, 44) refers to grounded theory analysis as a comparison of the characteristics of groups for similar and diverse meanings and actions linked to processes and underlying problems. For this study, the unit of analysis is the reliance process, while the units of observation are the participants' statements conveying their constructions of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups.

3.6.1.2 The nature of data required

Constructing a 'strong' substantive theory requires 'rich data' which allows the researcher to 'get beneath the surface of social and subjective life' (Charmaz, 2014:22-23). In line with this study's interpretivist frame, the empirical basis of theory construction is qualitative data providing an insider view of the phenomenon in the context of the participants' worlds (Charmaz, 2014:24; Babbie & Mouton, 2001:53). Grounded theorists use interviews as the 'main tool' for data collection (Charmaz, 2014:22). The flexibility of interviews provides the opportunity to discern new insights about a phenomenon as well as immediate follow-up of ideas, gaps and hunches from the first interview as a means of clarifying emerging theoretical ideas (Charmaz, 2014:25). These requirements and the study's aim of constructing a conceptualised explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of all the stakeholder groups, meant intensive interviews were the only means allowing the collection of relevant, rich data.

3.6.1.3 Cases (data sites) and participants

Glaser (1978:36) suggests that the 'process of data collection is *controlled* by the emerging theory'. Thus, participants and cases which the researcher believes to be the most knowledgeable and experienced in the topic are likely to provide maximum opportunity for collecting theoretically relevant data (Glaser, 1978:45). Moreover, sampling should allow for comparison of similar and different cases and / or groups (Glaser & Strauss, 1967:51).

(a) Cases

In this study, sampling purposively focused on cases with key 'informants' who were experienced in reliance (Charmaz, 2014:210). Guidance in governance and professional pronouncements and the academic literature formed the basis for identifying cases with experience of reliance. King III and IV (IoDSA, 2016; 2009) suggest that organisations should have an internal audit function and adopt combined assurance practices to optimise assurance coverage. In addition, King III and IV recommend that organisational disclosures should include information about internal audit as well as provide an indication of whether or not combined assurance was practised. However, neither the King Reports nor external auditing professional standards (IAASB, 2018: ISA 610 (Revised 2013)) require disclosure about reliance in the annual report or the external auditor's report, except where reliance is considered to be a key audit matter (IAASB, 2018: ISA 701).

Internal audit is more prevalent in larger companies (Anderson *et al.,* 2012; Goodwin-Stewart & Kent, 2006). In a South African context, private sector companies listed on the JSE have to explain in their annual reports how they adhered to recommended practices contained in King III and IV (JSE, 2019: paragraph 7.F.5). Thus, the *first* sampling decision was to focus on JSE-listed companies rather than public sector organisations as cases. All listed companies need to adhere to the JSE listing requirements (JSE, 2019). All the companies included in this study declared in their 2013 annual reports that they had internal audit functions and implemented combined assurance.

Next, consideration was given to which JSE companies should be used as cases. Risks and assurance needs vary across industries. Tiessen and Colson (1990:22) note that external auditors' reliance assessments significantly differ across industries. External auditors usually rely on internal audit's controls assurance work performed in the normal course of internal audits for companies in the manufacturing sector (Tiessen & Colson, 1990:22). However, for companies in the banking sector, external auditors preferred using the direct assistance work of internal auditors, rather than work performed in the normal course of internal audits (Tiessen & Colson, 1990:18). Thus, the *second* sampling decision was to purposively collect data on JSE-listed companies from different industries as cases. The selected companies represent the highly regulated financial services industry (a large banking group (case A) and a large insurance group (case B), the resources / manufacturing industry (case C), the telecommunications industry (case D) and the retail industry (case E)).

Next, the selection focused on the auditors of JSE-listed companies, which are mostly the Big 4 accounting firms. Consideration was given to the fact that each Big 4 accounting firm proudly adopts a distinct audit methodology or approach framing assurance work, although all have to adhere to the requirements of external auditing professional standards (KPMG, 2019; PwC, 2019; Deloitte, 2017; EY, 2017:4). In order to ensure variances in audit firm methodologies were accounted for in the data, the *third* sampling decision was to purposively include cases representing all the Big 4 accounting firms in this study. Each company selected for the study used a different external audit engagement partner with at least one such partner coming from a Big 4 accounting firm. In addition, the large bank (case A) used joint auditors (two Big 4 accounting firms) in terms of local regulation for banks (Republic of South Africa, 1990:

section 61(1)(b)). The telecommunications company (case D) and the retail company (case E) voluntarily appointed joint auditors, which resulted in each company having a Big 4 accounting firm and a national external auditing firm as auditors. Thus, the eight external audit engagement partner participants represented six external auditing firms. Details of these interviews appear in the interview schedule in Table 3.1 below.

(b) Participants

The focus of this study is on participants' statements conveying their constructions of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups involved in the statutory financial reporting and external audit processes. Thus, sampling had to allow for comparing data from participants representing each stakeholder group. In particular, given the complexity of reliance, the *fourth* sampling decision was to focus on five key data sets, including the individual with the highest level of role accountability from each stakeholder group at each selected company – the chief financial officer (CFO), the audit committee chair (CAC), the head of internal audit, commonly known as the chief audit executive (CAE), and the external audit engagement partner (EP) for each company. One audit committee chair participant held such appointments in two of the case companies. This study refers to the combination of data from the four stakeholder groups from each company as a key data set. These participants were all involved in the 2013 statutory external audits of their companies. Section 3.7.1 below describes the further theoretical sampling conducted in 2019, consisting of three follow-up interviews. These interviews form part of each company's key data set.

For purposes of triangulation of conclusions in Chapter 7, the *fifth* sampling decision was to use a further data set, derived from seven interviews with other knowledgeable senior internal and external audit professionals. These included a group interview with the inspection team leaders of the IRBA (who provided guidance and oversight to inspectors performing regulatory inspections on audits of South African external auditors) (RSA, 2005: section 48), four interviews with the national heads of internal audit services at the Big 4 accounting firms and two interviews with national heads of assurance at two mid-tier international accounting firms.

In conclusion, five key data sets (22 initial interviews and three further interviews) were used, representing five diverse South African listed companies. A further data set, consisting of seven interviews were used for triangulation of conclusions. Thus, the total number of interviews was 32. Details of these interviews appear in the interview schedule in Table 3.1 below.

Table 3.1 Interview schedule

	Date	Participant	F to F / Telephone	Interview venue	Length of interview
1	5 June 2014	EP D1	F to F	Participant office	57:42
2	9 June 2014	CAC A	Telephone		122:51
3	12 June 2014	CAE E	Telephone		46:48
4	13 June 2014	CAE C	F to F	Participant office	85:09
5	18 June 2014	EP A1	F to F	Participant office	68:17
6	19 June 2014	CAC C/E	F to F	Participant home	43:03
7	19 June 2014	EP E2	F to F	Participant office	82:51
8	20 June 2014	CAE A	F to F	Participant office	60:41
9	24 June 2014	EP D2	F to F	Participant office	69:57
10	26 June 2014	CAC D	Telephone		43:56
11	27 June 2014	CAE D	Telephone		42:31
12	1 July 2014	EP E1	Telephone		50:09
13	3 July 2014	EP C	F to F	Participant office	53:27
14	3 July 2014	Mid-tier 1	F to F	Participant office	38:08
15	7 July 2014	CAC B	F to F	Country club	21:38
16	7 July 2014	Mid-tier 2	Telephone		45:16
17	16 July 2014	IAS 1	Telephone		56:01
18	18 July 2014	EP A2	F to F	Country club	69:00
19	21 July 2014	EP B	Telephone		59:38
20	22 July 2014	CAE B	Telephone		79:03
21	28 July 2014	CFO B	Telephone		19:44
22	30 July 2014	IAS 2	F to F	Participant office	67:28
23	15 August 2014	CFO A	Telephone		59:32
24	3 September 2014	CFO C	F to F	Participant office	48:52
25	11 September 2014	CFO E	Telephone		30:25
26	11 September 2019	IAS 3	F to F	Participant office	64:01
27	17 September 2014	CFO D	Telephone		17:20
28	18 September 2014	IAS 4	F to F	Participant office	64:25
29	5 June 2015	IRBA Team	F to F group meeting	IRBA office	71:14
	TOTAL INITIAL INTERVIEW DATA				28 hours and 07 minutes
30	4 February 2019	CAE C 2019	F to F	Coffee shop	67:04
31	16 July 2019	EP C 2019	Telephone		28:13
32	19 July 2019	CAE B 2019	Telephone		67:04
	TOTAL FURTHER INTERVIEW DATA				2 hours and 42 minutes
	COMBINED TOTAL INTERVIEW DATA				30 hours And 49 minutes

Key: CAC – audit committee chair; CAE – chief audit executive; CFO – chief financial officer; EP – engagement partner; IAS – head of internal audit services at a Big 4 accounting firm; IRBA Team – IRBA inspection team leaders, quality reviewers, and director of inspections; Mid-tier – head of assurance at a mid-tier accounting firm. A, B, C, D, E are case company identifiers.

***Source**: Own compilation*

3.6.1.4 Number of interviews

Views about the appropriate number of interviews required in a grounded theory study are 'contested' as grounded theorists have taken 'contradictory positions' in this regard (Charmaz, 2014:105; 107). This is not surprising given the general misconceptions about the meaning of saturation in grounded theory studies and the different requirements when theoretically sampling for comparisons as opposed to sampling for generalisation.

The aim of qualitative analysis (not theory building) is to saturate data in the process of identification and description of themes, often from 'standardized interviews' with homogeneous participants (Charmaz, 2014:106-107). In contrast, the aim of a grounded theory study is saturating the properties of substantive categories, adding density from 'differences and distinctions' highlighted by 'comparative analysis' of data (Charmaz, 2014:106-107). However, deciding on the appropriate number of interviews is 'complex', as the grounded theorist is 'unlikely to know what you need to find out until you grapple with analyzing your data' (Charmaz, 2014:105-106). Charmaz (2014:107) advises that the contribution of grounded theory studies is not solely a function of the number of interviews conducted. Analytic depth is also dependent on the significance of the interview data and the researcher's interviewing and analytic skills (Charmaz, 2014:88-91; 108) Particularly, saturation of substantive categories is a function of '*selective*' theoretical sampling focused on the 'central issues' of the emerging theory (Glaser, 1978:46).

Charmaz (2014:105) furthermore cautions that using 'a very small number of interviews' could lead to questions about the quality of 'grounded theory-lite' studies. She explains that the research aim influences the number of interviews required; this means that for 'straightforward research questions to resolve problems in local practice in applied fields [thus requiring a specific substantive theory], a small number of interviews may be enough', while constructing general substantive and formal theories would require more extensive data (Charmaz, 2014:106). Charmaz (2014:108) notes that supplementing initial interviews with further interviews conducted with key participants helps to delineate theoretical constructs.

Given the complexity of deciding on the appropriate number of interviews for a grounded theory study, the advice of Charmaz (2014:108) was followed: 'Do the best you can with the material you can construct or already have. Like grounded theorists who have worked with documents, you may create something grand.' This study uses interview data from 29 initial interviews (22 representing key data sets and 7 from a comparable data set) and 3 further interviews (part of the key data sets), comprising more than 30 hours of voice recordings. Details of these interviews appear in the interview schedule in Table 3.1 (section 3.6.1.3).

3.6.1.5 Constructing an interview guide

The interview guide (Annexure A) should contain 'broad, open-ended' 'non-judgmental' discussion points soliciting participants' interpretations about the reciprocal influences on reliance by the roles, interpretations, interests and practices of the stakeholder groups (Charmaz, 2014:65). Chapter 2 substantiates the discussion points included in the interview guide. Initially, two interview guides were constructed – one for engagement partners and one for other participants. However, since the points were generic, the same guide was used for all interviews.

The researcher's initial theoretical sensitivity from professional, academic and research experience guided the phrasing of initial, probing and clarifying questions (Charmaz, 2014:60). Direct and simple language was used while the terminology was aligned to that used in governance and professional guidance (Charmaz, 2014:63). Care was taken to avoid 'wrong questions' to ensure that rich data was collected about the participants' interpretations and experiences (Charmaz, 2014:63)

The initial interview guide was presented to the role of director of standards at the IRBA at the time, for input and guidance. The main supervisor as well as a qualified chartered accountant from a Big 4 accounting firm also provided feedback on the initial interview guide. Only minor changes were required based on the feedback, notably, closer alignment of the second part of the interview guide with the external auditing professional standard on reliance.

3.6.1.6 Formalities

In February 2014, approval was granted for the initial research proposal and the title of the study by the relevant committees of the Faculty of Economic and Management Sciences of the University Pretoria. Written confirmation of ethical approval was also received at this time (Annexure B). In 2019, the Faculty confirmed that the additional interviews would be covered under the original ethical approval as all interviews followed the same procedure. Approval to change the title of the thesis was also confirmed at this time.

3.6.2 Initial data collection

This section provides details of interviews, the interviewing process and the transcription of interviews.

3.6.2.1 Scheduling interviews

A grounded theory study starts with data collection as soon as the researcher meets institutional research requirements (Charmaz, 2014:22). After approval of the research proposal and the research ethics application, work began on scheduling the initial interview appointments. As the participants were all professional elites in the highest position of their roles, considerable efforts were made to accommodate their busy schedules. All initial interviews were scheduled well in advance to ensure timeous access by the participants. The first of the initial round of interviews was conducted on 5 June 2014 while and the last occurred on 18 September 2014. A group interview was conducted with the IRBA inspectors on 5 June 2015.

All participants were personally approached with interview requests. The names of the specific participants to contact were identified from the 2013 annual and integrated reports of the case companies. The telephone and email contact details of these participants were then located using the internet or by contacting the relevant company or audit firm. In some instances, the contact details of one participant were obtained from another participant in the same company. All participants were contacted by telephone first. The interview request and scheduled appointments were lodged either through the personal assistant or, in most instances, directly with the participant. The telephonic requests were followed up by a confirmation email, with files containing a letter of introduction (Annexure C), the background to the study (Annexure D) and the interview guide (Annexure A). Once an interview date, time, mode and venue were agreed upon with the participants, either the participant's personal assistant or the researcher scheduled the interview electronically.

However, some difficulty was experienced in securing interview time slots with the chief financial officer participants, as their time availability was limited. It was necessary to follow up with their personal assistants for several times to secure times and dates. As a result, the requested interview time for these interviews was reduced to 20 minutes each (for the other interviews it was 60 minutes) and the interview guides were modified accordingly. Thus, only the two main open discussion points in the guide (points 1 and 3, requesting the participant to share their perspective on the role of internal audit in an organisation and reliance respectively) was used during these interviews. Given the initial challenges when scheduling interviews with chief financial officers, most of these interviews occurred later in the data gathering process. In reality, three of these interviews lasted much longer than 20 minutes. Despite their shorter length, they provided rich theoretically relevant data. This was enabled by the participants' excellent communication skills and the researcher's deepened theoretical sensitivity during the later stages of data collection.

While most participants preferred face-to-face (F to F) interviews at their offices, some were conducted telephonically or at other venues, for reasons of practicality and participant preference. Details of the interviews appear in the interview schedule in Table 3.1 (section 3.6.1.3).

3.6.2.2 Conducting intensive interviews

The term 'intensive interviewing' implies 'complementary data collection and analysis methods' (Charmaz, 2014:84), with analysis commencing from the first interview onwards (Charmaz, 2014:90, 111). To this aim, the theoretically sensitive researcher enters the field open-minded – on the one hand, ready to learn from the participants about their experiences and actions, and on the other, ready to pick up from the participants' statements and explanations any points indicating 'analytic issues'

(Charmaz, 2014:2-3, 111) or ‘theoretical leads’ (Glaser, 1978:44). Intensive interviewing is well-suited to the open-ended nature of a grounded theory study (Charmaz, 2014:85). During interviews, the researcher clearly ‘expresses interest and wants to know more’ about the topic (Charmaz, 2014:68). The interview is ‘open-ended yet directed, shaped yet emergent, and paced yet unrestricted’, facilitating the ‘interactive space and time’ for ‘in-depth exploration of an area in which the interviewee has substantial experience’ (Charmaz, 2014:85).

Upon first contact, most participants expressed genuine interest in the topic of the study. Many voiced how important a study of this nature was, given the complexity and expectations surrounding this topic. During joint sampling, coding and analysis, attention was focused on any data offering ‘*theoretical direction*’ and with potential *‘theoretical centrality*’ (Charmaz, 2014:90). This was done keeping in mind the point made by Glaser and Strauss (1967:36) that tentative categories can emerge rather quickly, even during the early phases of data collection. The suggestion of Charmaz (2014:90) was also heeded, namely, that the research should remain ‘open to what you hear, see, and learn in an interview’, as ‘specific data may not recur but might instead represent a tacit recurring pattern that went unmarked and, likely, heretofore unnoticed’.

In several interviews and even at several times during the same interview, ‘statements’ by the participant ‘capture[d] or crystallize[d]’ theoretical leads providing new understanding of earlier and / or subsequently collected interview data (Charmaz, 2014:89-90). These statements increased the theoretical sensitivity of the researcher in terms of their potential contribution to theory development. In this manner, joint sampling, coding and analysis became seamless.

Heeding the suggestion of Charmaz (2014:55, 58) that the ‘grounded theory methods work best when the grounded theorist engages in data collection as well as data analysis’, all interviews and data analysis were personally conducted by the researcher. As indicated by Charmaz (2014:58), this has many benefits, notably, ‘explor[ing] nuances of meaning and process’ when participants share theoretically relevant information during interviews. This process served to heighten the researcher’s theoretical sensitivity.

In preparation for the interviews, several strategies were used to create an open, courteous and positive interview climate. These included familiarity with the topic and using a flexible interview guide to elicit participants' interpretations and experiences (Charmaz, 2014:59-63). The interview participants were treated with respect (Charmaz, 2014:62). Interview times and venues were scheduled to suit the participants' diaries and background information and the interview guide were emailed to them before the interview. The researcher arrived punctually at the interviews and was professionally dressed and groomed. Open-ended discussion points and a semi-structured intensive interviewing approach were used, mirroring the 'tone and pace' of the participant (Charmaz, 2014:65, 72).

At the start of each interview, the interview procedure was explained to the participant, and it was reiterated that their participation was voluntary and that they could withdraw at any point. A signed letter of consent to participate in the study was obtained from each participant (Annexure E). Consent was also obtained to make voice recordings of the interviews and to conduct the interviews in English.

During the interviews, the researcher paid attention to how the participants perceived the interview situation, keeping any personal preconceptions, assumptions or judgements out of the interview, while showing sincere, respectful interest in the participants' explanations (Charmaz, 2014:68, 72). Intensive interviewing requires active listening and unobtrusive researcher responses (Charmaz, 2014:69). Follow-up and probing questions were used for clarification, for example 'Tell me more about that?', 'How do you define that?', 'How do you feel about that?', 'How would you do that?' or 'What do you consider for that?' (Charmaz, 2014:69). These questions aimed at theoretical sampling clarified, confirmed and saturated the substantive categories (Charmaz, 2014:210).

Allowances were made for brief silences when the participant was clearly thinking about what to say next. Moreover, as pointed out by Charmaz (2014:79), each participant was not asked the 'same questions in the same way'. Since the first discussion point lets 'stories tumble out' in most interviews, it was not necessary to directly raise each and every discussion point in the interview guide (Charmaz, 2014:65). It was noted that the participants appreciated eye contact during face-to-face interviews. At one or two appropriate points in each interview, the researcher's understanding of the participants' main points was verbally summarised. This aided data analysis as it effectively 'check[ed] and refin[ed]' understanding, and the participant could add 'a more complete explanation' in cases where gaps and 'partial interpretations' became apparent in the summaries (Charmaz, 2014:210). Charmaz (2014:210-211) points out that presenting a participant with their 'tacit actions' 'resemble[s] theoretical sampling'.

As suggested by Charmaz (2014:62), the interview guide was consciously used as 'a flexible tool' and not a document of formal structure for interviews. The participants appreciated receiving an interview guide before interviews as it informed them of what to expect. It was also clear from notes scribbled on printed copies of some of the interview guides, that some participants had reflected on areas for discussion before the actual interview. However, one interviewee (an external audit engagement partner) was uncomfortable when the strict order of discussion points in the interview guide was not followed. It was explained that the interview guide was merely that, a guide. However, for the rest of that interview, it became apparent that he appreciated a more structured approach. The participant openly shared valuable insights during the interview, after a more structured line of discussion was adopted. This participant had made detailed notes on a printed copy of the interview guide which he brought to the interview. He also brought some publications of his audit firm along to the interview, which he used to support some of his views.

As mentioned in section 3.7.1, the same procedure was followed prior to, during and after the further interviews as for the initial interviews, particularly focusing on changes in the role of internal audit and reliance since 2014.

All participants were in the highest position of authority of their roles, and they all represented 'elites' in their field. Charmaz (2014:73) cautions that interviewing elites could mean influences on the conversation from 'taken-for-granted hierarchical' differences between participants and the researcher. Reflecting on the interview situations, several factors created mutual respect and trust between participants and the researcher, fostering frank and in-depth discussion (Charmaz, 2014:62, 72-73, 74). These are discussed below in the first person, for ease of understanding.

I am a conscious and secure woman in my mid-fifties with a 'disarming demeanor'. At the time of the interviews, I had previous managerial, interviewing and research experience. I also hold a professional external auditing qualification and have a combination of extensive auditing practice and academic experience. I have a sound understanding of the roles and interests of the stakeholder groups involved in the statutory financial reporting and external audit processes. Consequently, I did not experience nor foresee any negative influences on data collection by ‘relative differences in power and status’ between the participants and me (Charmaz, 2014:73). On the contrary, being secure and experienced allowed me to sincerely adopt the role of an ‘interested learner’ who understood the technicalities shared by the participants; my understanding allowed relevant and appropriately worded clarifying and probing questions (Charmaz, 2014:73). I found that my attitude and attributes added richness to the conversation and data collection (Charmaz, 2014:73). My experience in the field reflects the observation of Charmaz (2014:73) that ‘[o]nce the interviewer has established a common ground and built trust, elites may become remarkably frank and give the interviewer substantially more time and detail than expected by either party’. Thus, many of these ‘elite’ participants, evidently highly interested in this study, willingly continued talking and sharing their experiences and views beyond the allocated interview time (Charmaz, 2014:74). While most of the interview participants explicitly mentioned the importance of a study of this nature, they were also appreciative of the opportunity to contribute their knowledge and experience to the study.

An example of participants’ keen interest in the topic were incidences where non-external auditor participants frankly conveyed how disillusioned they were with the lack of reliance. Two participants (a chief financial officer and a chief audit executive from two different companies) explained that they were implementing strategies to increase reliance, as they were very dissatisfied with the lack of reliance and could not understand it. The chief financial officer mentioned that the company was implementing expensive internal control improvements with the main aim of achieving increased reliance. However, when asked whether he had discussed with the external auditors the potential impact of the planned, expensive changes on reliance and the external audit fee, the chief financial officer replied that he had not.

At the end of the interviews, the participants were thanked for their contribution to the study.

3.6.2.3 Transcribing interviews

After each interview, the interview recording was immediately sent to an independent professional transcriber for transcription. Between interviews, the researcher repeatedly listened to recordings of interviews and read the transcribed interviews. Once transcribed, the voice recordings were compared to the transcribed text of the interview for correctness of the transcripts. These continuous repeated engagements with the data in multiple formats (listening to the participant during the interview itself, listening to the voice recording after the interview, comparing the voice recording to the transcribed text of the interview, reading transcribed interviews) familiarised the researcher with the data and heightened theoretical sensitivity. The stakeholder groups' reciprocal 'pattern[s] of behaviour' linked to their roles became increasingly apparent, reflecting their related interpretations, interests and practices influencing reliance (Glaser, 1978:93-94).

The decision to use voice recordings and transcribed interviews was based on the advice of Charmaz (2014:136), who states that 'coding relies on having solid data'. Glaser, on the other hand, is not in favour of voice recordings and transcriptions, preferring instead to rely on 'field notes' which he calls 'jots'; these should be made 'as soon as possible after leaving the field' (Glaser, 1978:52-53). However, in line with the opinion of Charmaz (2014:136), verbatim transcriptions of interviews were used to ensure that all relevant 'ideas and understandings' were incorporated, contributing to a more thorough and systematic analysis rather than 'superficial analysis'.

3.6.3 Open coding and analysis to delimit the main concern and choosing the core category

Section 4.2 presents the description and audit trail of open coding and analysis to delimit the main concern. It also describes how the core category was chosen from the developing substantive categories. The reader is thus able to 'audit' the dependability of the study based on a detailed account of the analytical process and tables showing how the data was conceptualised (De Vos *et al.,* 2011:427).

3.7 PHASE 2: JOINT FURTHER THEORETICAL SAMPLING, SELECTIVE AND THEORETICAL CODING AND ANALYSIS

This section describes how further theoretical sampling, selective and theoretical coding and analysis were applied to saturate substantive categories and their connections to the core category.

3.7.1 Further theoretical sampling

Charmaz (2014:108) advises that it is useful to conduct follow-up interviews with key participants who are already familiar with the researcher, the interview process and topic. These interviews can be used to obtain additional data to saturate substantive categories. Thus, in 2019 three follow-up interviews were conducted with 'top informants' from two of the original case companies (B and C) (Glaser, 1978:47). These interviews were with the chief audit executives from companies B and C (the same individuals as in 2014), and the external audit engagement partner from case C (not the same individual as in 2014, as the company had changed audit firms). These three interviews are listed in the interview schedule in Table 3.1 and form part of the five key data sets.

The same procedure prior to, during and after these interviews was followed as for the initial interviews. In addition, the emergent visual analytic model and theoretical propositions were shared with these participants prior to the interviews. These interviews had a strong theoretical sampling focus, particularly examining the changes in the role of internal audit and reliance since 2014. Although the initial interview guide was used, these interviews turned out to be less structured, with participants eagerly sharing their interpretations of changes in the role of internal audit and reliance in the period since the first interview (discussion points 1, 2, 3 and 5 in the initial interview guide).

3.7.2 Selective and theoretical coding and analysis to the point of saturation of substantive categories

Section 4.3 presents the description and audit trail of the process of selective and theoretical coding and analysis to the point of theoretical saturation of substantive categories. This presentation supports the auditability of the conceptualisations, as explained in 3.6.3 above.

Chapter 5 provides a narrative description of the data supporting the saturated substantive categories.

3.8 PHASE 3: THEORETICAL SORTING AND REPORTING

In the last phase of conceptualisation, the substantive categories were sorted into a theoretical outline of the substantive theory. The outline of theoretical constructs and supporting analytic and theoretical memos indicating the properties of each construct were the basis for reporting the theory. In this phase, the substantive theory was compared to extant knowledge, followed by reflections on the quality of the theory.

3.8.1 Theoretical sorting into theoretical constructs and their properties

Section 4.4 presents the description and audit trail of the process of theoretical sorting into theoretical constructs and their properties. This presentation supports the auditability of conceptualisations, as explained in 3.6.3 above.

Once the substantive categories are theoretically sorted and the theoretical constructs named and delimited, the next step is reporting the substantive theory.

3.8.2 Reporting the substantive theory

The theoretically sorted analytic and theoretical memos are used when reporting the theory (Glaser, 1978:84-85, 94). Incorporating conceptual properties and dimensions of substantive categories into the report on the theory as properties of theoretical constructs, connects the theory to the data (Glaser, 1978:84, 94).

3.8.2.1 *'The little logic' or main storyline*

Glaser (1978:129) suggests using a 'little logic' or several 'little logics' (storylines), consisting of 'no more than a paragraph or two, and often just one long sentence' as the basis for the grounded theory write-up .The little logic should state that the core category will explain a behaviour related to the main concern, using theoretical constructs and / or theoretical codes (Glaser, 1978:129-130). Glaser (1978:130) advises that the little logic 'is written realistically and with awareness so that it can be followed throughout' the write-up of the substantive theory.

The little logic (main storyline) of this study is presented in section 6.2.

3.8.2.2 *Outline of the grounded theory report*

The grounded theory report is an analytic rather than a descriptive account of the data (Charmaz, 2014:15; Glaser, 1978:134). Thus, the theoretical writing of a grounded theory study uses conceptualised data rather than descriptive data (Glaser, 1978:39, 84). Explanations using logic are not permitted (Glaser, 1978:34), as a substantive theory should 'correspond closely to the "real-world"' (Glaser & Strauss, 1967:42).

The introduction of a grounded theory write-up should commence with an 'outline paragraph' stating the main concern and the core category developed from the data, and not preconceived from practice or literature (Glaser, 1978:131) (section 6.2). Perspectives from practice and literature could be included as 'supplements or contrasts, if at all' (Glaser, 1978:131). Then, an outline of the integrated theoretical constructs and how they are connected should follow, reflecting the 'cumulative build-up' of each section of the report (Glaser, 1978:131-132) (section 6.3). The main storyline provides a sound basis for the introduction as well as individual sections of the write-up (Glaser, 1978:129).

Separate sections should deal with each theoretical construct (section 6.4). The introduction of each section connects the construct to the core category, explaining how the construct resolves the main concern through its connections to other constructs (Glaser, 1978:131-132). The introductory paragraph of each section 'may have relevant literature and perspectives woven into them … but *only* as supplements or contrasts, not as sources of derivation' (Glaser, 1978:131). This study did not use in-text references to literature but rather a separate section was devoted to comparing the substantive theory to relevant professional, academic and theoretical frameworks (section 6.5).

The sections of the report may include a small number of quotations from the data ‘when needed’ in support of conceptualisations; a ‘massive grounding effort’ in the report is not necessary as the grounding is implicit in its analytic nature (Glaser, 1978:134). Selected, impactful quotations may be included when introducing certain key conceptualisations in aid of ‘illustration and imagery’, as well as vivid ‘understanding’ (Glaser, 1978:134). This study used *in vivo* words depicting the underlying action behind the properties for conveying vivid imagery and connecting the theory to the data (Glaser, 1978:64). Tables in section 4.5 furthermore contain impactful quotations used as ‘illustrations and imagery’ of the properties and dimensions of substantive categories which were delineated into the theoretical constructs (Glaser, 1978:134).

The ending of the write-up should not include a summary. Glaser (1978:133) contends that a ‘summary is redundant and an affront to those readers who have actually read’ the write-up; however, relevant ‘recommendations’ for ‘practitioners’ are ‘worthwhile’ (section 7.6).

3.8.2.3 Conceptual writing and reworking

Maintaining an analytic rather than descriptive writing style is the greatest challenge of the grounded theory write-up (Glaser, 1978:133). Glaser (1978:133) suggests that analytic writing consists of ‘theoretical statements about the relationships between concepts, rather than writing descriptive statements about people’. The write-up should explicate properties and connections between constructs (Glaser, 1978:133).

Once written, the draft should be ‘corrected by reworking’ (Glaser, 1978:135). Reworking should focus on parsimony (Glaser, 1978:136). Glaser (1978:136) also suggests that starting paragraphs with the name of a theoretical construct adds emphasis and shows the ‘cumulative build-up’ and integration of the theory.

Ultimately, the report should make it clear that theoretical constructs were conceptualised from data and that these were not tested or proven as they are suggestions (Glaser, 1978:134). Thus, hypotheses integrate the theory into statements, explaining how constructs connected to the core category resolve the main concern emerging from the participants' interpretations of their 'life-worlds' (Glaser, 1978:134).

3.8.2.4 Bringing in the literature

Glaser (1978:9) asserts that the researcher's analysis should be 'preserved as his own', as the author of the work. He cautions against creating the impression that the researcher's findings are attributable to other scholars 'who did not do it' (Glaser, 1978:9, 137-138). Moreover, as the new theory was constructed from data, it was therefore derived independently of extant knowledge (Glaser, 1978:138).

Excessive references to other scholars could also interrupt the presentation of the theory (Glaser, 1978:9, 137-138). Thus, Glaser (1978:138) suggests that the researcher should rather provide brief footnotes when comparing the theory to work of other scholars, while longer comparisons should be placed at the end of the report (Glaser, 1978:9).

The purpose of bringing literature into the report is to compare the theory to 'previous descriptions *and* theories about an area' to show how the theory conceptually 'transcends' what was known (Glaser, 1978:7, 38). The purpose of comparisons is not to prove or disprove the new theory nor extant knowledge (Glaser, 1978:7, 38); comparisons merely position the new theory in relation to extant knowledge and highlight how extant theories could be extended (Glaser, 1978:38).

Ultimately, the emphasis of the comparison should be the contribution implicit in the new theory. Glaser (1978:137) declares that the 'contribution remains truly original' as conceptualisation of data, and not deductions from extant knowledge, produce a dense theory that works (Glaser, 1978:137).

As suggested by Glaser (1978:138), in-text references to literature were not used, but rather a separate section was devoted to comparing the substantive theory to relevant professional, academic and theoretical frameworks (section 6.5). The aim of the comparison was to highlight the original contribution of this study, showing how each construct of the theory matched, broadened and transcended existing knowledge.

3.8.2.5 Quality of the theory

Glaser (1978:5, 8) points out that ‘immaculate conceptions are not necessary’ as ‘generation is an ever-modifying process and nothing is sacred’ (*sic*). He adds that the core category usually remains constant, while the relevance of its properties varies, in line with changes in the world. Thus, new data could dictate that a ‘recasting’ of the theory is needed or it may be necessary to address ‘gaps’ in the properties of the theory (Glaser, 1978:5, 10).

Quality considerations are linked to the emergent nature of the new theory. The researcher should be sure that the theory fits, is relevant and works; it should also be easy to modify to reflect changing circumstances Glaser (1978:4). In line with Glaser (1978), Charmaz (2014:337) refers to four quality considerations, namely, ‘credibility’, ‘originality’, ‘resonance’ and ‘usefulness’. Glaser and Strauss (1967:3) associate the quality of a grounded theory study with its contribution, noting that construction from data makes a theory understandable to ‘laymen’ as well as those working in the area (Glaser & Strauss, 1967:3).

Below, each of these quality considerations is defined and motivated.

(a) Fit (credibility)

According to Glaser (1978:4), credibility or ‘fit’ implies that substantive categories should be developed from data, and not from ‘forcing’ or pre-conception. Glaser (1978:4) states that the emphasis on data makes the theory accurate as it resembles reality. Fit is not difficult to achieve, as conceptualisations from data imply that ‘fit is automatically met’ (Glaser, 1978:4, 38). However, fit is enhanced by constant refitting – this means the comparison of conceptualisations to ‘successive data’ (Glaser, 1978:4). When a ‘pre-existant’ (*sic*) category from the literature is incorporated into the theory, its ‘emergent fit’ should be carefully determined by comparison to data (Glaser, 1978:4).

When reporting a grounded theory, certain guidelines related to fit apply. First, incorporating extensive quotations from the data does not prove the credibility of a substantive theory; rather the credibility is implicit in the relevance and workability of the conceptualisations of the theory (Glaser, 1978:134). Second, examples and explanations should originate from data, meaning that speculation by the researcher is unnecessary (Glaser & Strauss, 1967:5).

(b) Work (originality) and relevance (resonance)

Theories work when their relevance is supported by data, meaning that the theory is 'able to explain what happened, predict what will happen and interpret what is happening' in a substantive area (Glaser, 1978:4-5; Glaser & Strauss, 1967:3). Such relevance is dependent on the 'emergence' of the main concern and the identification of a core category with 'explanatory power' from the data, rather than a preconception about it (Glaser, 1978:5, 95).

(c) Modifiable (usefulness)

As a grounded theory fits data, it should not be fully refutable or replaceable by more data or another theory (Glaser & Strauss, 1967:4). At the most, the theory should be modifiable by new data or changed circumstances (Glaser, 1978:5).

In this study, the theoretical constructs fit, work and are relevant as they originate from delineated 'analytic properties' and dimensions of substantive categories (Glaser, 1978:84). Being grounded, the theoretical constructs could possibly be modified but not refuted by more data (Glaser, 1978:5). It is reassuring to note that a substantive theory does not have to be, nor can be, perfect.

3.9 A REFLECTION

The following reflection is written in the first person for ease of understanding. Looking back on this study, Glaser's (1978:6) contention comes to the fore:

> The growth and maturity over his data that occurs, as the analyst persists in his research, constantly puts him beyond his previous analysis … we call this the delayed action effect - it takes time to transcend one's data with a theory, but it surely happens. And when it does happen, the analyst feels transcended with excitement over the theoretical mastery of his data.

I can confirm that this study was indeed hard and time-consuming or, as Glaser (1978:136) puts it, ‘exhaustion and growing personal saturation’ were part of my grounded theory journey.

I resonate with the purpose of a grounded theory study insofar as it offers ‘a way to understand what is going on in a substantive area and how to explain and interpret it’ (Glaser, 1978:3). The grounded theory methodology chose my study, not I it, and it kept me engaged over many years. My stubbornness to persist with grounded theory, contrary to most advice from experienced researchers is reflected in the following quote from Glaser (1978:3): ‘Others [I take this to mean grounded theorists] may feel, even *know* in their hearts, that data could be handled more profitably in other ways’. This quote describes so well how I felt. I was advised to present the data from this study as themes, like in most other qualitative studies. However, I kept feeling the data was hiding a deeper story. That feeling grew stronger as I became fully immersed in iterative joint data collection, coding and analysis. Being so close to the data made me ‘know’ in my heart that it was hiding deeper insights about reliance, waiting to be discovered by conceptualisation (Glaser, 1978:3).

Persisting knowledge gaps, despite much earlier research on reliance, piqued my curiosity about what other studies were missing. I wanted to get behind what was obvious, I wanted to listen to the interpretations of all the stakeholders in the real world who mutually influence and are influenced by reliance. I wanted to get the full picture of reliance – not only pre-selected snippets. I wanted to contribute a workable explanation of reliance, considering all stakeholder groups’ perspectives (Glaser, 1978:3-5).

However, this was my first encounter with the grounded theory methodology. I did not even know anyone who had attempted this methodology. Thus, for the most part, I instinctively followed my gut, working by trial and error. Although I read and reread the works of Glaser and Strauss (1967), Glaser (1978) and Charmaz (2014), most of the time I found it hard to understand their guidance, possibly due to the seemingly ‘interchangeable’ use of terminology and the non-linear nature of the grounded theory building process. Only towards the end of this research process did I feel somewhat more at ease with the methodology. I attempted to use terminology consistently in the process of giving a credible account of the grounded theory methodology applied in this study.

I am satisfied with the theory constructed from this study and am comforted by the words of Glaser (1978:16-17):

> …skill development takes time and cannot be fully developed in one study. The analyst should look forward to new studies to say, develop his skills at memoing. He should not redo memos in an already memoed study on the grounds that his skill was so poor, that it was like skipping the step. Nor should he switch data before completing all stages, for he would then miss the necessary experience of going from start to finish and thereby experientially seeing, and feeling how well the grounded theory method works.

As this thesis confirms, I went from start to finish!

3.10 CONCLUSION

This chapter described and justified how this interpretivist classic grounded theory study was conducted, demonstrating the appropriateness of the chosen design and methodology for the stated research question.

Next, Chapter 4 provides an audit trail of the coding and analysis of the three phases of this study. It includes the outcome of phase 1: choosing the core category.

CHAPTER 4

AUDIT TRAIL OF CODING AND ANALYSIS: OUTCOME OF PHASE 1

CHAPTER 4

AUDIT TRAIL OF CODING AND ANALYSIS: OUTCOME OF PHASE 1

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4.1 INTRODUCTION

Chapter 3 described and justified how this interpretivist classic grounded theory study was conducted.

One of the quality measures of a qualitative study is dependability. Dependability refers to repeating a study with the same or similar participants in the same or similar contexts and arriving at similar findings (Babbie & Mouton, 2001:278). Key to dependability is a logical, well-documented and auditable research process (De Vos *et al.*, 2011:420). Readers are able to 'audit' the dependability of the study if the researcher has provided a detailed account of the analytical process used in the interpretation and conceptualisation of the data (De Vos *et al.,* 2011:427). For these reasons, this chapter provides an audit trail of the process of coding and analysis in the three phases of this study. The outcome of phase 1 is also included.

Phase 1 describes the open coding and analysis of the key initial data sets to delimit initial substantive categories and the main concern. The selection of the core category is also outlined. This is the outcome of phase 1. Tables are provided to explicate the logic of the coding process and the initial substantive categories.

Phase 2 describes the selective and theoretical coding and analysis of initial and further data to the point where substantive categories are saturated. This outcome of phase 2 is presented in chapter 5. Tables are included to explicate this process. Illustrative quotations from the data are also provided.

Phase 3 describes the theoretical sorting to delimit the saturated substantive categories into theoretical constructs. A table is included to explicate this process. This sorted list of theoretical constructs (made up of delimited substantive categories and their properties and dimensions) carries forward to the structure of the presentation of the substantive categories in Chapter 5 and the presentation of the substantive theory in Chapter 6. This is the outcome of phase 3.

Some quotations included in this chapter are in italics, similar to their presentation in the original texts.

4.2 PHASE 1: OPEN CODING AND ANALYSIS

The aim of open coding and analysis of the key initial data sets was to delimit the initial substantive categories and the main concern and choose the core category, as outcome of phase 1. At the start of the analysis, reading and annotating transcripts provided a holistic understanding of the data. This was followed by oden coding to develop the initial substantive categories and refit them to more data. When the main concern emerged, the core category was chosen from the developing substantive categories. The process of open coding and analysis provides an overall understanding of the cases.

4.2.1 Reading and annotating transcripts

As recommended by Glaser (1978:15) to start analysis with reading, all the transcripts were read upon receipt and any impressions of what was happening in the data were annotated in the margins. This continued until a data set of interviews from all four stakeholder groups from a single case had been collected. This first complete data set was from case company B.

Two unique groups emerged from reading transcripts across cases and participants (Glaser & Strauss, 1967:54). First, the MORE reliance case(s), consisting of a 'group' of data from two companies (B and E), where external auditors indicated reliance was not limited. Second, the LESS reliance case(s), consisting of a 'group' of data from three companies (A, C and D) where external auditors indicated reliance was limited. The data indicated that dimensional differences of the properties influencing reliance was behind MORE or LESS reliance. This was a key consideration during all data analysis.

4.2.2 Open coding

The aim of open coding is 'fracturing the data' to identify the emergent 'main concern' and 'core category' (Glaser, 1978:93-94). The main concern required identifying the participants' key concern or problem with reliance while the core category required explaining participants' 'pattern of behaviour' to resolve their main concern (Glaser, 1978:94). The goal of conceptualising reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of the four stakeholder groups, was kept paramount in this regard.

4.2.2.1 Initial substantive categories

Glaser and Strauss (1967:55, 56) recommend coding similar groups first. Thus, open coding commenced with the data set of interviews from all four stakeholder groups from a single case, case B. Coding these four interviews as a data set enabled the comparison of similarities and some differences in 'incidents' (Glaser, 1978:57), namely, the participants' statements conveying their constructions of reliance, within the context of the reciprocal influences of the roles, interpretations, interests and practices of the stakeholder groups.

Atlas.ti is a tool for organising transcribed interview data, coding data and retrieving information about coding, as well as the quotations linked to a specific interview or code (Friese, 2012). The programme also offers a functionality for creating memos and notes about coding and analysis. This programme was used for the open coding.

Data was coded line by line, with open codes allocated to statements conveying the participants' constructions of their own and other stakeholder groups' reciprocal influences on reliance, considering their roles, interpretations, interests and practices. Comparison focused on similarities and differences within and across participants' constructions (Glaser, 1978:55, 57). Descriptive and *in vivo* code names were used. One and even two or three qualifiers were added at the front of each open code name, denoting the underlying uniformity of codes. Table 4.1 presents the list of qualifiers used.

Coding the data set from case B produced 778 open codes. These codes were delimited into nine substantive categories, considering their 'underlying uniformity' captured in code name qualifiers (Glaser, 1978:49, 57, 62, 64). Table 4.2 presents the initial list of substantive categories and sub-categories from case B. The list includes notes and some important quotations as indicators of incidents subsumed in each category.

The same steps were followed for the other four cases (Glaser, 1978: 44, 3), with earlier and later coded incidents, codes and categories being constantly compared (Glaser, 1978:57). The combined codes of all of cases saturated the substantive categories and sub-categories that were integrated into the substantive theory (see Table 4.4). Table 4.4 also indicates how the initial categories and sub-categories were subsumed into the saturated categories.

Table 4.1 List of qualifiers used during open coding: Case company B

Reliance	**Audit committee**	**CAE**	**IA**	**Magnitude**
Areas	Effectiveness	Profile	Approach	AC oversight
Interactions	Oversight	Status	Budget	AC support
Practised	Role	Strength	Capacity	AC debates
Consequences		Tenure	Competence	AC role
Extent			Coverage	IA accountability
How			Independence	CAE profile
Conditions			Experience	Future
Nature of work	**Process**	**EA**	Importance	IA/EA relationship
Overall			Methodology	IA/EA working together
Satisfaction	AC oversight	Tenure	Plan	IA budget
'Top up'	Combined assurance	Approach	Role	IA capacity
CAE views	IA		Status	IA competence
Causal condition	Reliance		Strength	IA coverage
Expectations		**Coder**	Structure	IA methodology
Management influence			QAR (quality assurance review)	IA responsibilities
Factors		Very important	Purpose	IA role
Intent	**Case company**		IAF	IA scope and focus
Relationship			Changes	IA size
	Industry	**Emotion**	Objectivity	IA status
	Length of interview		Performance	Organisation size
	Number of internal auditors excluding CAE		Profession	Combined assurance approach
	Number of subsidiaries	**Pattern – extent of reliance**	Professional liability	Reliance
	Participant role		Quality	Reliance extent
			Reports	Reliance consequence
		Data analytics	Risk	Reliance extent conditions
			Size	Reliance future
			Value	Reliance interaction critical
		Financial industry	Independent quality reviews	Reliance interventions
			Management expectations	Reliance driver
				Reliance factor

***Source**: Own compilation*

Table 4.2 Initial substantive categories and sub-categories: Case company B

A Planning reliance
A1 Combined assurance approach (‘combined assurance programme’)
A2 Participation in planning meetings (Full participation = IA/EA/risk and executive management in an annual joint meeting)
A3 Consensus about assurance plan (all risks identified and linked to coverage by each of three lines of defence)
A4 Shared understanding of audit context (shared understanding of the risks / controls / business operations that impacts audits)
A5 Shared understanding of audit roles / objectives (shared understanding of the mandated roles / objectives / responsibilities of IA vs EA)
A6 Aligned audit plans (lengthy discussions, frank questions, upfront, compare plans, EA gives input in IA plans, adjustments, ‘reshuffle’, reciprocal reliance, no gaps, address duplication, some duplication to prevent ‘blind spots’, timing, extent, sample sizes (methodology); discuss with management)
A7 Risk-based adjusted audit plans (for internal and external audits)
B Overseeing reliance
B1 Independent oversight (fixed meetings; private / closed sessions with IA and EA without management present; discuss IA scope, management influence on IA/EA work, IA budget, whether management prescribe to IA, IA competence vs responsibilities; annual assessment of IA / EA; has knowledge of quality assurance review outcome)
B2 Well-established (independent; serious about oversight role; emphasis on proper functioning corporate governance; strong risk view; industry, regulatory, financial knowledge)
C Considering the CAE
C1 Business / industry insight (understand business and industry; deep understanding of risks and their impact; commercial understanding; understand processes)
C2 Trusted CAE (weekly meetings with CFO; not at exco level but review exco minutes)
C3 Strong independent CAE (stand their ground against management about the scope of IA work)
C4 Competent CAE (‘hands-on experience’; understand processes and controls; lead and manage the IA team; can communicate at all levels)
C5 Work close to business (‘different’ networking approach; truly understand all areas; know the risk areas to focus IA effort on)
D Considering internal audit
D1 Risk-focused (management expect risk focus; networking to identify risks / problem areas / remain informed; focus on general control environment rather than detailed testing of specific controls; focus on changes / high risk areas / significant areas / complex areas / regulatory aspects; oversee strategic projects; work with risk management and forensics)
D2 Resourcing (‘resource pressure’; retention and attraction challenges; in the last ten years the IA structure was never filled; constraints are budgetary and difficult to find the right level of staff to employ in the IAF; IAs ‘stuck in a

corporate structure' – promotion opportunities limited; IAF 'never have enough' capacity for desired coverage; IA profession: 'there aren't that many people that will stay within internal audit for a number of years')
D3 Competence ('a good mix' of skills; auditing knowledge superior, then the rest; experience; understand the industry and business – ability to identify risks; understand processes and controls; data analytic and forensic skills; communication skills; 'we grow them up' = on the job training; importance of IA depend on the people employed in IAF)
D4 Performance (CAE influence; substance of findings; root cause analysis; active follow-up of control breakdowns; quality of recommendations; prioritisation of work; supervision and review; quality assurance reviews)
D5 Maturity of IA role ('significant role'; 'major stakeholder'; trusted / respected by staff and management; facilitate inter-stakeholder problems; 'starts off with the directors' and management's attitude towards the value of an IAF'; remain focused on their responsibilities; 'truly risk based approach'; 'quality of people' interacting with management;
D6 Independence (reporting lines; CAE actively manages independence risks: rotation of IAs, wary of IA staff relationships that threaten independence, never make business decisions, never prescribed to management, management do not dictate to IA)
E Reflecting on outcomes
E1 Improved audit efficiency (possible saving of 10% to 15% in EA fees; when EA rely on IA work on controls, EA time spent on control testing and detailed substantive tests is reduced and replaced with more substantive analytical procedures; 'if there weren't an internal audit department, what work would external audit have done and now that there is one, what do [EA] do now' – CFO B; IA rely on relevant work of EA; IA and EA rotate audit areas)
E2 Improved financial controls
E3 Increased assurance / quality of assurance (less duplication; higher level of assurance that controls are in place; gaps from IA/EA assuming that work is done by the other audit function are eliminating assumptions clarified; provide management with a view on the quality of the work of IA; in some areas IA and EA choose to cover the same work)
F Evaluating conditions for relying
F1 Timing of IA work (IA cover 'the majority of the period')
F2 Assessment of IAF and its work
F2.1 IA stability (most important factor; using outcome of EA's assessment; baseline assessment of IA controls, policies and methodologies; updated annually; focus on changes in company or 'thinking' from EA's side; work and reports of IA reviewed; reperformance levels)
F2.2 IA independence (consider management influence; if not independent it 'makes their work hard to rely on')
F2.3 IA status ('as the IAF proves their value, so their status in the organisation increases'; management and the directors understand the potential benefits of the IAF to the organisation; quality of IA reflected in the substance of findings reported)
F2.4 IA competence (level of IA skills and qualifications; how well IAs understand processes and controls; standard of IA work depends on qualifications of IAs)
F2.5 IA quality control processes (EA review quality assurance review outcomes to reduce their work on assessing IA or to get further assurance about IA; QAR report less important than IAs' understanding of processes and controls)
F2.6 Standard of IA work ('it depends on the work that they do and the findings that come out of that' – EP B; 'IA need to do [work] at a level and standard that [EA] can rely on that'- CAE B; 'do [IA] do [work] properly' – CAC B; 'audit reports … that

is what [IA] are usually judged against'; 'if [IA] do it correctly then external audit has to redo the entire thing [work]'; sampling methodology critical;
F3 Risk and subjectivity of audit area (controls weaknesses; significant risks / material / judgement areas – EA will never let IA do the whole section; these areas require a high level of reperformance by EA which make reliance inefficient)
F4.1 Accessibility of IA working papers for EA (EA reviews IA work on IA's software package)
F4.2 Accessibility of audit area / data for EA
F5 Previous reliance (reliance in the past)
F6 Focus of IA (when IA focus change to more operational the result is less reliance and higher EA fees; 'we never want perfect alignment, because we [IA] should look at other things than external audit' – CAE B; 'perfect alignment' causes a 'blind spot' – CAE B; IA work that does not have 'a material impact from a financial perspective' is of 'limited value for the external auditors' – EP – B; 'I think they look at the organisation from a much wider perspective where we might focus predominantly on financial controls, I think they focus on both financial, the financial environment as well as the operating environment' – EP B)
F7 Outcome of joint planning process ('It is about that upfront agreement on sample sizes and audit approach and ja, it is my communication and planning.' – CAE B)
F8 EA approach (substantive vs combined audit approach)
F9 Alignment of IA / EA methodology (including sampling) ('the main critical thing that is a maker-breaker is the sampling methodology' – CAE B; 'you need to be upfront about the way in which you test' – EP B; 'that the objectives and the sampling and the methodology is consistent because if not then they can perform certain tests which are not in line with what we were wanting' – EP B)
F10 Size of entity ('I think we worked at the smaller companies that where the external audit fee is still like a huge expense there, the external audit fees are very expensive, there combined assurance is very much to bring your fee down to a manageable level' – CAE B)
G Considering reliance environment
G1 Active risk management function ('It also depends very highly on your efficiency of your risk management process because in the theory side, internal audits should audit where it is, where there is, where it is perfect, where the management already has said, we have done everything and everything is working and you can come independently assure.' – CAE B; 'risk management functions that formally runs loss registers to do root cause analysis and see what needs to, what problems is being experienced' – CAE B)
H Expecting reliance
H1 Management emphasis on audit efficiency (Management 'would want to know that [IA and EA] are working together' – CAC B; Management 'like [reliance] obviously because they see the cost [of EA] and they get fed up for being audited' CAE B; 'If you don't align [IA and EA] external audit can come and ask [management] exactly the same question than your internal auditor did two months ago … it takes management time away from what they are supposed to do' – CAE B; IA 'can do [audit work] much more cheaper or at a much better rate then [EA] do it' - CAE B)
H2 King III on combined assurance and ISA 610 (In a company where combined assurance works well, that is where the company gets the maximum benefit from the combination of internal audit and external audit' – EP B; King III and ISA 610 result in more structured reliance than in the past)

I Adopting reliance
I1 Intention / openness to rely (EA 'work so closely with [IA] I think it's always a discussion around what is the overall assurance that needs to be given, who is best placed to give that assurance' – EP B; CAE is of the opinion there is 'lots of value' in reliance; 'I just think [IA and EA] work together to try and use whatever internal audit work is doing, external audit is trying to use as much of [IA work] as possible.' - CAC B)
I2 Frankness of reliance relationship (EA share reliance plans as well as changes in plans 'for whatever reason' with management, AC and IA; EA does not give detailed feedback about the outcome of the assessment of IA – mostly verbal and one paragraph in EA plan; CAE unsure how EA assesses the IAF; 'We have done that within the business for a few times, at least, either myself or the head of financial reporting, sitting with internal audit, sitting with external audit in one meeting and that we talk through all what is in the plans, what we want to cover in the year and making very sure we are on the same page' – CFO B); The relationship between IA and EA 'is much more open in terms of what [EA] are concerned about and what [IA] are concerned about. ' CAE B; 'if there is any issue that crops up, [IA and EA] talk to each other about whatever comes along' CAC B)
I3 Frequency of reliance interactions (IA and EA 'meet frequently, speak even more frequently and we make sure that we both understand … each other's, what is the areas that we both need to look at, what we are giving assurance on. ' - EP B; regular formal and informal meetings between IA and EA; IA and EA 'meet about every three months before we finalise the audit to make sure that we don't, we all know about each other, each other's areas of concern or whatever but before each big sign off there is an intervention.' - CAE B)
I4 From forcing to habit ('In the beginning it might be something that you consciously do and later on I think it's just the way that you work' – EP B; 'predominant reason where it has worked better is because the two divisions [IA and EA], that it has just been a closer working relationship between the two' – EP B)
I5 Function as one team ('how do [IA and EA] approach [the audit] combinedly' – CAE B; 'really having this combined approach where you plan your work together' – EP B; 'You [EA] do see yourselves as a greater part of an assurance given to the company' – EP B; 'if [IA and EA] can really work together as a team on the assurance' – EP B)
I6 Mutual respect (IA and EA have a high regard for each other)

Key: IA – internal audit; EA – external audit.

***Source**: Own compilation*

4.2.2.2 Brief overview of the five key cases

In the process of open coding, a brief overview of the five key cases was developed, as presented in Table 4.3.

Case A had a large internal audit function, while the others had much smaller internal audit functions. Cases A and B operated in the highly regulated financial sector. Having dual external auditors was mandatory for case A, where external auditors were appointed from two Big 4 accounting firms. In cases D and E, a second audit firm was voluntarily appointed from two national accounting firms.

Notably, the external auditors in cases B and E practised MORE reliance, meaning they indicated reliance was not limited. For example, EP B explained: 'The [external audit] plans upfront … are based on maximum reliance … obviously based on the work that internal audit have done'. In contrast, the external auditors in cases A, C and D practised LESS reliance, meaning they indicated that reliance was limited (or even totally absent). For example, EP D1 declared: 'Reliance is something which I've never done so far'.

Table 4.3: Brief overview of the five key cases

	CASE A	CASE B	CASE C	CASE D	CASE E
Level of reliance in each case	LESS reliance case: Reliance is limited	MORE reliance case: Reliance is not limited	LESS reliance case: Reliance is limited	LESS reliance case: Reliance is limited	MORE reliance case: Reliance is not limited
Reliance work	Limited to reading internal audit reports and using peripheral support by internal auditors	Mostly direct assistance work comprising controls assurance work and substantive procedures	Limited to reading internal audit reports and complementary work providing wider assurance, for example, on indirect taxes	Limited to reading internal audit reports	Mostly direct assistance work comprising controls assurance work and substantive procedures
Listing sector	Financial services – banking	Financial services - insurance	Resources	Telecommunications	Retailer
External auditors	Dual auditors – by law Both Big 4 auditors	Single Big 4 auditor	Single Big 4 auditor	Dual auditors – by choice. One Big 4 auditor and one from a national audit firm	Dual auditors – by choice. One Big 4 and one from a national audit firm
Number of internal auditors at group level (excluding the chief audit executive)	200+	14	13	7	6 internal auditors at head office (at the retail outlets of the group, a large number of internal auditors performed operational audits

Pertinent facts about the internal audit team	Ten vacancies occurred per month, however, this was not cause for concern as it was below the industry benchmark Sporadically, business staff rotated from the business into internal audit and then back to the business	The staff complement was slowly increasing, with drawn-out appointment processes In the last ten years, the company had not been able to fill all internal audit vacancies due to the lack of available senior competent internal auditors (CAE-B) The internal audit team struggled to keep up with increasingly complex regulatory requirements The internal audit team worked with a forensics team and collaborated with the risk management function	The company did not often recruit internal auditors Only individuals with auditing experience (especially from an external audit environment) were appointed as internal auditors Downsizing internal audit was not considered by management	The internal audit team consisted of a dedicated team of industry experts The chief audit executive pointed out skills gaps existing in the internal audit team Some internal auditors previously worked as external auditors of the company	The chief audit executive considered the internal audit budget and staff as sufficient Some internal auditors started their career in the business and then moved into internal audit After 2013, the audit committee and management decided to refocus internal audit attention on operational matters – causing a decrease in direct assistance work – all stakeholder groups agreed the changed focus would result in increased external audit fees

***Source**: Own compilation*

4.2.3 Outcome of phase 1: Choosing the core category

The last step in the first phase of conceptualising the substantive theory was choosing the core category from among the initial substantive categories created during open coding and analysis. Glaser (1978:93) emphasises the importance of the core category, noting that 'without a core category', the theory produced will 'drift in relevancy and workability'.

When choosing the core category, analytic rules must be applied. Foremost, the core category should be 'central', as 'most other categories and their properties are related to it', implying that 'it accounts for a large portion of the variation in a pattern of behavior' (Glaser, 1978:93-95). The underlying meaning of the core category should be frequently present in the data as a stable driver of meaning and action (Glaser, 1978:95). Thus, it is easy to meaningfully relate the core category to other substantive categories, without the need to force (Glaser, 1978:95). The core category is thus '*completely variable*' and 'readily modifiable' in 'degree, dimension and type' as '[c]onditions vary it easily' (Glaser, 1978:96). While the core category accounts for 'problematic behavior' present in the data, it is '*also a dimension of the problem*', meaning 'in part it explains itself and its own variation' (Glaser, 1978:96).

In the process of open coding, the main concern emerged as:

> *Disconnect between stakeholder groups' reciprocal influences on reliance*.

The central theme of all the initial substantive categories indicated the core category that resolved stakeholder groups' main concern. Clearly disconnect was resolved when:

> *All stakeholder groups mutually agree that reliance is appropriate and fair (balanced), whatever the reliance decision*.

With the core category known, the second phase could be embarked upon.

4.3 PHASE 2: SELECTIVE AND THEORETICAL CODING AND ANALYSIS

Selective and theoretical coding and analysis builds on open coding and developing substantive categories. The point of this phase is to saturate the properties and dimensions of substantive categories and to show relationships between the categories.

4.3.1 Selective coding

With the core category known, coding continued on a selective basis, focusing on data to saturate the substantive categories and their connections to the core category (Glaser, 1978:61). At the time of open coding, the main concern and core category were not known yet. Thus, the initial categories were preliminary. During selective coding, the emergent main concern and the chosen core category were used to refit the initial substantive categories (Table 4.2) into the substantive categories and subcategories with theoretical reach. This refitting was based on the '*concept-indicator model*', considering the 'underlining uniformity' of open codes to the core category (Glaser, 1978:49, 57, 62, 64).

The already coded transcripts were reviewed, and their coding was checked and altered in light of the core category. In the latter process of 'refitting', the nine initial categories developed from open codes were reallocated into six substantive categories and five sub-categories (presented in section 4.5). Table 4.4 lists the substantive categories and sub-categories and the initial categories subsumed in them. Categories were thus more closely and parsimoniously aligned to the core category (Glaser, 1978:60-61). The earlier analytic memos about the substantive categories and the conceptualisations of each category's properties, dimensions and connections, were revised as needed (Glaser, 1978:62, 84-85). Glaser (1978:71) advises that '10 to 15' substantive categories are 'typically enough' for a 'parsimonious substantive theory'. He cautions that having a larger number of categories could mean using irrelevant ones, thus diluting the impact of the most relevant ones (Glaser, 1978:71).

In the process of selective coding and analysis, the number of new properties, dimensions and connections identified came to an end. Glaser (1978:47) defines 'saturation' as 'the end of discovering new properties on a category'. Given this specific context of reliance, the theoretical saturation of properties was easier to determine than in more flexible studies. In this study, all the data collected (32 interviews) was open-coded; the researcher is confident that the substantive categories and their properties ‘exhaust[ed] the data’ (Glaser, 1978:64). Clearly, the substantive categories were saturated.

Table 4.4 List of substantive categories and sub-categories and the initial categories subsumed in them

	Categories and sub-categories	Initial categories and sub-categories
Category 1	**Communication**	I2: Frankness of reliance relationships I3: Frequency of reliance interactions
Category 2	**Stakeholder groups’ roles, interpretations, interests and practices influencing reliance**	
Sub-category 1	*Stakeholder groups’ assurance needs and responsibilities*	A2: Participation in planning meetings A3: Consensus about assurance plan A5: Shared understanding of audit roles / objectives
Sub-category 2	*The reliance environment*	F10: Size of entity G1 Active risk management function A4: Shared understanding of audit context D2: Resourcing D5: Maturity of internal audit’s role F2.3: Internal audit’s status C: Considering the CAE
Sub-category 3	*The relevance of internal audit work for statutory audit purposes*	D1: Risk focused F6: Focus of internal audit
Sub-category 4	*The credibility of internal audit work for statutory audit purposes*	D3: Competence F2.4: Internal audit competence D6: Independence F2.2: Internal audit independence D4: Performance F2.1: Internal audit stability F2.5: Internal audit quality control processes F2.6: Standard of internal audit work
Sub-category 5	*External audit quality and the external auditor’s liability*	F3: Risk and subjectivity of audit area F5: Previous reliance F8 EA approach
Category 3	**Working mindset**	A1: Combined assurance approach H2: King III on combined assurance and ISA 610 I5: Function as one team I6: Mutual respect

Category 4	**Integrating work**	E1: Improved audit efficiency E2: Improved financial controls E3: Increased assurance / quality of assurance F4.1: Accessibility of internal audit working papers for external audit F4.2: Accessibility of audit area / data for external audit H1: Management emphasis on audit efficiency I1: Intention / openness to rely I4: From forcing to habit
Category 5	**Aligning work**	A6: Aligned audit plans A7: Risk-based adjusted audit plans F1: Timing of internal audit work F7: Outcome of joint planning process F9: Alignment of internal and external audit methodology (including sampling)
Category 6	**Overseeing reliance**	B1: Independent oversight B2: Well-established

Source*: Own compilation*

4.3.2 Theoretical coding

Theoretical coding was done at the same time as selective coding. Use was made of indicators of connections between substantive categories and the core category evident in the data (Glaser, 1978:73). The theoretical coding was conducted while remaining cognisant of the relevant rules. These ‘flexible’ codes depicting connections between the core category and substantive categories weave fractured data back into a conceptualised explanation of the studied phenomenon (Glaser, 1978:72). Glaser asserts that a vast supply of theoretical codes exists in the world, with more emerging ‘continually’ (Glaser, 1978:82). However, theoretical codes should be relevant to what is happening in the data, thus they should not come from ‘logical elaboration’ (Glaser, 1978:82). The theoretical codes were captured in theoretical memos and in a visual representation (Figure 6.1), as Glaser (1978:82) suggests presenting theoretical codes ‘pictorially’.

Section 4.5 explicates how the substantive categories were delimited from the data. For each substantive category and sub-category, it also presents the properties and their dimensions influencing MORE and LESS reliance of each category. Illustrative quotations supporting dimensions of MORE or LESS reliance are included. Chapter 5 provides a narrative description of the data supporting the saturated substantive categories.

4.4 PHASE 3: THEORETICAL SORTING AND REPORTING

Once substantive categories are saturated, theoretical sorting delimits them into the properties of theoretical constructs. Combined, the theoretical constructs form the substantive theory.

4.4.1 Theoretical sorting into theoretical constructs and their properties

In the last phase of conceptualisation, substantive categories are sorted into a theoretical outline of the substantive theory.

Theoretical memos depicting the connections between substantive categories and the core category form the input used for theoretical sorting (Glaser, 1978:116-117). This ensures that only those substantive categories which are connected to the core category are used in 'the most parsimonious theory of greatest scope' (Glaser, 1978:10). 'Theoretical sorting' orders conceptualisations in theoretical memos into a 'conceptual' 'theoretical outline' which represents the substantive theory (Glaser, 1978:117). Thus, theoretical sorting does not commence with a preconceived outline. It is inductive, relying on the comparison of substantive categories for 'similarities, connections and conceptual orderings' of patterns associated with the core category (Glaser, 1978:117). It requires 'creativity' and 'theoretical sensitivity' from the researcher (Glaser, 1978:117-118).

Glaser suggests that theoretical sorting can be started 'anywhere' and recommends drawing a visual model of the theory to facilitate sorting (Glaser, 1978:123). Glaser and Strauss (1967:41) advise that 'integration of the theory is best when it emerges'; it should never 'just be put together'. The theoretical outline should ensure that the theory is 'open-ended', readily able to accommodate new categories and properties (Glaser & Strauss, 1967:41).

Glaser provides broad guidelines for theoretical sorting. As theoretical sorting 'can start anywhere' (Glaser, 1978:121), it was started using the memos of theoretically coded saturated substantive categories, in no particular order (Glaser, 1978:118, 121). Throughout the sorting, corrections and modifications were made, ensuring that 'everything fits' (Glaser, 1978:118). While sorting, a linear model was drawn and corrected, depicting the emergent substantive theory (Glaser, 1978:123).

Theoretical sorting was challenging and required thought and several back-and-forth attempts to ensure that each substantive category was included in the most appropriate position in relation to the core category. Drawing and explaining a visual model of the theory assisted in the process of sorting, as did the writing of the main storyline, the propositions and the thick descriptions.

The outcome of theoretical sorting is theoretical constructs of the theory supported by properties. The properties of the theoretical constructs are delineated conceptualisations of the properties and dimensions of the substantive categories (Glaser, 1978:118, 121). The name of each theoretical construct conceptualises the underlying uniformity of its properties (1978:64). Glaser (1978:70) suggests that the names of theoretical constructs should have two components, namely, one conveying 'analytic ability' and the other based on 'imagery'. Glaser (1978:64) explains that the component of the name capturing analytic ability should reflect the construct's properties. The imagery component serves to illustrate the meaning of the construct in the context of the theory as a whole, thus carrying the construct forward within the theory (Glaser, 1978:64). *In vivo* words depicting the underlying action binding the properties are useful for conveying vivid imagery while they also connect the construct to the data (Glaser, 1978:64). Glaser (1978:70) suggests that a study can tolerate one, but perhaps up to three, 'sociological constructions' and 'many *in vivo*' constructs.

The sorted substantive categories yielded six theoretical constructs. Five construct names contain forms of *in vivo* words. Table 4.5 presents the six theoretical constructs and brief explanations of their names.

Table 4.5 Theoretical constructs and brief explanations of their names

Theoretical construct	Brief explanation and in vivo words
Facilitative communication	All participants reiterated the important influence of communication on reliance. The data showed the quality of communication facilitated reliance.
Reciprocal synchronisation	Participants noted that their 'mutual' influences determined reliance. The synonym for mutual was used, i.e. reciprocal. Participants highlighted the importance of stakeholder groups being 'in sync' about their assurance needs and responsibilities.
A team mindset	Participants highlighted the importance of internal and external auditors working as a 'team' on reliance. Participants expressed 'mindset' determined whether internal and external auditors worked as a team or not.
Habitual integration	A participant indicated that over time, reliance becomes a 'habit', causing internal and external audit to 'integrate' work to an optimum degree.
Fair alignment	Participants indicated how internal and external auditors should 'align' reliance work.
Balancing oversight	Participants underlined the role of the audit committee to 'balance' the influence of management on reliance including the reliance environment, the relevance and credibility of internal audit work for statutory audit purposes and pressure on external auditors to increase reliance to reduce external audit fees.

***Source**: Own compilation*

4.4.2 Reporting the substantive theory

Chapter 6 presents the substantive theory, including the storyline, a visual representation depicting the propositions of the theory and a thick description of each construct. A comparison of the theory to extant theories is also included in the same chapter.

4.5 SORTED SUBSTANTIVE CATEGORIES

The next ten sub-sections each start by explaining how a substantive category or sub-category was delimited from the data. The initial substantive categories and properties (from Table 4.2) that were refitted into the saturated substantive categories are also mentioned. Each section includes a table indicating the category's properties and their dimensions influencing MORE and LESS reliance. The tables include illustrative quotations supporting dimensions of MORE and LESS reliance and the concept indicators used during data coding. These quotations came from case companies where either MORE or LESS reliance occurred, as participants also indicated influences that would change reliance. Although quotations are linked to specific properties, many include concept indicators of relevance to more than one property and / or substantive category.

Specific mention is made of concept indicators used when identifying and coding data with underlying uniformity (Glaser, 1978:62). Using these concept indicators ensured that data with an underlying uniformity pointing to a particular concept was coded to a category in line with 'similarities, differences and degrees of consistency in meaning' between indicators (Glaser, 1978:62). Chapter 5 provides a narrative description of each saturated category and sub-category, structured under the properties of each.

4.5.1 Communication

This substantive category includes two properties, reflecting two distinct levels and objectives of communication. These (referred to as property 1 and property 2) were (a) stakeholder groups' communication about planned and achieved reliance and (b) communication between internal and external auditors to coordinate work.

Two properties of the initial category 'I: Adopting reliance' were refitted into this substantive category, namely 'I2: Frankness of reliance relationships' and 'I3: Frequency of reliance interactions' (Table 4.2).

Table 4.6 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for each property. The concept indicators are also indicated.

Table 4.6: Communication

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: Stakeholder groups' communication about planned and achieved reliance Concept indicators: Data incidents conveying the importance, participants, objectives, quality (considering the mood, attitude, frequency, structure, timing and depth) and outcomes of stakeholder groups' communication about planned and achieved reliance, and their influence on reliance			
Management 'are pretty reasonable and accept that [external audit] know what we are talking about when we say whether we can or can't place reliance on a piece of [internal audit] work' (EP E1).	All stakeholder groups engage in extensive, open discussions about planned and achieved reliance Stakeholder groups' focus during discussions is on assurance effectiveness and efficiency, yet favouring effectiveness over efficiency External auditors perceive that management, the audit committee and internal auditors are reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance	Management's and some audit committees' primary focus is on assurance efficiency during communication about planned and achieved reliance Interactions are difficult discussions, including interrogation, questioning and challenging external auditors by management and some audit committees, who expect external auditors to provide detail about improving assurance efficiency as well as action plans to achieve this; they also expect the external auditors to justify objectively why they practise no or limited reliance External auditors' response is diplomacy, providing very limited, generic written feedback and some informal verbal feedback about the outcome of the ISA 610 assessment and the reasons for no or limited reliance - this is done to preserve the relationship between internal and external auditors Due to external auditors' limited communication about the reasons for no	External audit 'would … firstly have discussions and management will … ask [external audit] … how can [we] use whatever [work of internal audit] and then also challenge [external audit] … if they see that there is something that internal audit could or should do for [external audit]; the audit committee the same' (EP A1). 'There's a conflict there for [external audit] in terms of trying to manage good relationships with internal audit, but being open and honest with both them and [the] executive in the business around the quality of their teams and their people' (EP A2). 'At every audit committee [meeting] … external audit actually in their packs, they've got a specific section called reliance on the work of internal audit ... so they have to report on that formally … So [reliance] is monitored and the views are shared if they [the audit committee] are not happy with the level [of reliance] or they feel it should have been more … there is no question on what [the audit committee's] view is [on reliance], it is quite clear' (CAE C).

		or limited reliance and a tick-box approach prevailing during reliance interactions, management and internal auditors are often frustrated as they struggle to make sense of no or limited reliance by external auditors	'Everyone comes there [to the combined assurance meeting] and say we've done the forum and tick, done' (CFO A).
Property 2: Communication between internal and external auditors to coordinate work Concept indicators: Data incidents conveying the importance, participants, objectives, quality (considering the mood, attitude, frequency, structure, timing and depth) and outcomes of communication between internal and external auditors to coordinate work, and their influence on reliance			
'We [internal and external auditors] have that opportunity to call each other on any matter or basis' (EP E1). 'We [internal and external auditors] meet frequently … [and] speak even more frequently' (EP B). Internal and external audit met 'to make sure that … we [they] all know about … each other's areas of concern' (CAE B). 'You [internal and external audit] look back and say what have been duplicated and what have we done efficiently, … then identify that, and then change it going forward' (CFO A). 'The 'external audit team [and] internal audit team [were] just sitting on a quarterly basis and sharing lessons' (CAE A).	In-house internal and external auditors engage in: - Unrestricted, confident and easy communication - Consisting of open, formal and informal communication - Frequent conversations and regular meetings throughout the year - Covering mutual knowledge sharing on areas of concern - Reflection on lessons learned and ways to improve assurance effectiveness and efficiency	The communication between in-house internal auditors and external auditors becomes forced and cautious However, subsequent to automatic reliance on work of outsourced internal auditors from Big 4 accounting firms, communication between outsourced internal auditors and external auditors commences with an immediate reliance request from the newly appointed outsourced partner to the external auditor, followed by extensive upfront discussions to clarify mutual expectations	Communication between internal and external auditors 'was kind of more forced' (CAE C).

***Source**: Own compilation*

4.5.2 Stakeholder groups' assurance needs and responsibilities

Stakeholder group's assurance needs and responsibilities is a sub-category of the substantive category entitled stakeholder groups' roles, interpretations, interests and practices influencing reliance. This sub-category includes three properties, (a) assurance meetings, (b) the distinct roles of internal and external auditor and (c) pressure to increase reliance.

Three properties of the initial category 'A: Planning reliance' were refitted into the sub-category, stakeholder group's assurance needs and responsibilities, namely, 'A2: Participation in planning meetings', 'A3: Consensus about assurance plan' and 'A5: Shared understanding of audit roles / objectives' (Table 4.2).

Table 4.7 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for each property. The concept indicators are also indicated.

Table 4.7: Stakeholder groups' assurance needs and responsibilities

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: Assurance meetings Concept indicators: Data incidents conveying the participation in and the frequency, format, mood, purpose and outcomes of assurance discussions and the influence thereof on reliance			
'All three [management and internal and external audit] … [forming] a nice complete triangle' (CFO A). 'More collaboration and more conversation with practical and pragmatic deliverables [about] … who is doing what, and who is delivering what [assurance]' (EP A2). 'All three lines [management, internal and external audit] working in sync with each other' (CAE A). 'Around risk identification, acceptance of those identified risks in the business, and what [management, internal and external audit] are doing from a combined perspective to manage those risks' (EP A2). Assurance stakeholders have 'got to have a clear goal that you're working towards' (CFO E).	Holding regular combined assurance meetings, with triangular participation by management and internal and external auditors to develop a combined assurance mapping, synchronising stakeholder groups' assurance needs and responsibilities into shared goals and an integrated risk and assurance view	Misunderstanding of each group's assurance needs and responsibilities as management meet separately with internal and external auditors about assurance plans	'It has never crossed my mind to actually bring these two together' (CFO C). External audit 'are pressurised by the audit committees who say they cannot pay both parties, there's got to be a synergy between the two and we have to rely on internal audit; and it's difficult. It's extremely difficult because … internal audit focus on operational efficiency aspects where we focus on misstatement of numbers' (EP C). 'There's a disconnect between definitions' (EP C).

Property 2: Distinct roles of internal and external audit Concept indicators: Data incidents: - Contrasting the roles of internal and external audit - Justifying their influence on reliance			
'I don't see [internal and external audit] as the same at all ... if you didn't have an internal audit department … then the external auditors have to do a hell of a lot more different work to give you [management] the comfort that [external audit] would need as well … the fact that you've got that [internal audit] just makes their [external audit] job a little bit different, but it doesn't take away what they have to do' (CAC C / E).	All stakeholder groups mutually understand internal and external audit's interrelated distinct roles, implying that neither internal nor external audit can substitute each other's role	Management and some audit committees perceive, through reliance, that internal audit should reduce external audit work and fees	'I would either optimise my internal audit department or optimise my external audit department to get to the right … level of control' (CFO C). 'There's still a long way to go for lots of companies to understand the role of internal audit … from management's point of view … their understanding is that internal audit is there to reduce the work of external audit' (EP E2).
Property 3: Pressure to increase reliance Concept indicators: Data incidents conveying information about management's and audit committee's pressure to increase reliance, including their motivations, the consequences and moderators, and the influence on reliance			
'Our requirement is just that the external auditor does a good job and is completely independent and they must be efficient as well ... if [external audit] provide good service, we're not going to force them to cut fees … it doesn't pay us and the audit committee wouldn't welcome that at all' (CFO E). 'I think [management] would leave it up to the external auditors. They would want to know that they are working together and they are, we know that … but I don't think they actually impose on the external	All stakeholder groups' focus is on balancing assurance effectiveness and efficiency, yet always favouring effectiveness over efficiency	Management and some audit committees exert pressure on external auditors to increase reliance Management expect that large investments in internal financial controls will translate into greater reliance as external auditors would change from extensive substantive procedures to a combined approach focused on controls assurance work External auditors often feel that management's pressure to increase reliance is inappropriate	'ISA 610 implies that [reliance] has to happen' (CAC A). 'Management won't allow it and the audit committee won't allow [internal and external audit working in silos]' (CAE C). 'Where [external audit] are forced to do it [rely], I think people will do it, and you know, you're going to have to live with it otherwise you don't do the audit [lose the audit client]' (EP D1). 'I actually, in my private meetings, challenge [external audit] … are you using the internal auditor sufficiently' (CAC A).

auditor in terms of the extent of the work they use' (CAC B). Management 'are coming to understand that what internal audit does and the assurance that they give is not going to overwrite … the assurance external audit needs to give' (EP E1)		External auditors maintain that appropriate reliance is extremely difficult to achieve and therefore they mostly practise no or limited reliance despite management's and some audit committees' pressure to the contrary External auditors attempt to increase reliance on an *ad hoc* basis only on those audit clients exerting pressure	'There is a lot of pressure … on some clients, [the external auditor is] moving towards [reliance] … On other clients there's pressure to actually move towards that … from management … So obviously as a firm we would be looking [only] at those specific clients [exerting pressure] to see … can we rely and where we can work with management to reduce their cost' (EP D1). 'We are pressurised by the audit committees who say they cannot pay both parties, there's got to be a synergy between the two and we have to rely on internal audit; and it's difficult. It's extremely difficult' (EP C). 'Given the fact that I'm the guy that stands in the dock, I'm the guy that has to make the insurance claim, I'm the guy that's sued at the end of the day, there is a reticence on our part to work too much with internal audit. Even though there's pressure on us, we tend to resist and we will do the bare minimum and on the very unsexy, less risky stuff' (EP A2).

***Source**: Own compilation*

4.5.3 The reliance environment

The reliance environment is a sub-category of the substantive category entitled stakeholder groups' roles, interpretations, interests and practices influencing reliance. This sub-category includes seven properties, (a) the size and regulation of the organisation as well as the reciprocal influences of each stakeholder group's roles, interpretations, interests and practices (particularly that of management) on (b) the maturity of risk management, (c) the effectiveness of internal financial controls, (d) the structure of the internal audit function, (e) internal audit budget / capacity / resourcing, (f) the status of internal audit and the value it adds and (g) the profile and role of the chief audit executive.

Seven properties of a number of initial categories were refitted into this sub-category, namely, 'F10: Size of entity', 'G1 Active risk management function', 'A4: Shared understanding of audit context', 'D2: Resourcing', 'D5: Maturity of internal audit's role', and 'F2.3: Internal audit's status' (Table 4.2). In addition, the initial category 'C: Considering the CAE' was refitted to the sub-category 'the profile and role of the chief audit executive' (Table 4.2).

Table 4.8 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this sub-category. The concept indicators are also indicated.

Table 4.8: The reliance environment

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: The size and regulation of the organisation Concept indicators: Data incidents contrasting how and motivating when organisation size and regulation influence reliance			
'In an organisation of significant size, my view is that it would almost always be beneficial to rely on [internal audit]' (EP B). 'At the smaller companies [in a larger group] where the external audit fee is still like a huge expense … there combined assurance is very much to bring your fee down to a manageable level' (CAE B). 'Management is not just driving profit and growth, they're not just driving numbers anymore. They have realised … with this whole set of regulations … their responsibility is actually to govern this environment' (CAE B (2019))	Larger, well-regulated organisations with a strong audit committee where management realise that they should balance profitability and good governance, thus: - A strong risk management function is present - A strong internal audit function is present - An effective combined approach to assurance is present, with internal audit's role as a provider of combined assurance more formalised and regulated - Management and the audit committee have a better understanding of the distinct roles of internal and external audit and the ideal scope and focus of internal audit mandates and plans - Management and the audit committee usually ensure realistic resourcing in line with internal audit's mandate and plans External auditors perceive that the benefit of assessing internal audit and its work usually exceeds the cost in larger, well-regulated organisations	Smaller, less well-regulated organisations with a weak audit committee, implies that management's practices are usually profit-orientated rather than governance-focused, thus: - A weaker risk management function is present - Internal audit is ineffective - The use of internal audit is less formalised - Management and the audit committee lack an understanding of the distinct roles of internal and external audit and the ideal scope and focus of internal audit mandates and plans - The value of internal audit is only recognised in response to control failures External auditors perceive that the fixed cost of assessing internal audit and its work exceeds the audit fee saving, in smaller, less well-regulated organisations	'When you have less regulated institutions where, maybe, the risk function is not as strong, the combined assurance process, I think, doesn't work as well in those kinds of environments. So, in the businesses I'm involved in, where there's a strong risk function in the business at a senior level, and there is good collaboration between management through risk and the internal audit and external audit, I find that the collaboration, the use of work between, or external audit using the work of internal audit, kind of improves' (EP A2).

	Reliance mostly occurs in smaller components (subsidiaries) of larger organisations where a combined approach to assurance is present and internal audit follows a transactional, end-to-end, integrated business process approach		
Property 2: The maturity of risk management Concept indicators: Data incidents contrasting how and when the maturity of risk management in an organisation influences reliance			
'A strong risk function in the business at a senior level' (EP A2).	A strong risk management function with senior management collaboration (usually larger, well-regulated organisations)	A weaker risk management function which is not functioning optimally (usually smaller, less well-regulated organisations)	'The risk function is not as strong' (EP A2).
Property 3: The effectiveness of internal financial controls Concept indicators: Data incidents contrasting how and motivating when the effectiveness of internal financial controls in an organisation influence reliance			
'Effective and operating for the entire financial period' (CFO A).	Strong internal financial controls which function effectively for the entire financial period (usually larger, well-regulated organisations)	Weak internal financial controls are not operating fully (usually smaller, less well-regulated organisations)	'Not operating fully' (CFO A).
Property 4: The structure of the internal audit function Concept indicators: Data incidents contrasting how and motivating when the structure of the internal audit function in an organisation influence reliance			
'If it's a very strong internal audit department, and then I put more reliance on … internal [in-house] audit departments' (EP E2).	External auditors prefer reliance on a strong, in-house internal audit function with a superior understanding of the business, including its key risks (usually larger, well-regulated organisations)	External auditors favour reliance on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm, on grounds of their superior competence and independence	'When it's an outsourced function, and the outsourced partner is one of the accounting firms, then it makes it much more palatable [for external audit] to actually rely' (EP D1).

Property 5: Internal audit budget / capacity / resourcing Concept indicators: Data incidents: - Contrasting how and motivating when the internal audit budget / capacity / resourcing in an organisation influence reliance - Describing and motivating factors influencing the allocation to internal audit budget / capacity / resourcing			
'The right balance' (EP A2) of 'benefit versus reward' (EP B). Internal audit's 'limited focus on financial controls means that external audit and internal audit have had to work more closely with each other as time has gone on in a sense that both of us will need assurance over a number of areas of control; and given that internal audit would generally adopt a rotational focus to that testing, we would look to cover key areas of [financial] control in years in between their three year rotational cycle. So in that sense it has forced us to work very closely with them in planning the audits and the audit plan' (EP E1).	Realistic resourcing, in line with internal audit's mutually agreed realistic mandate and plans (usually larger, well-regulated organisations) The CAE balances internal audit's resourcing and work by: - Negotiating sufficient budget and appointing a sufficient number of competent internal auditors - Using technology, including data analytics - Carefully considering opposing demands on internal audit resources, including by *ad hoc* work for management	Internal audit's budget, capacity and resourcing are too limited to fulfil internal audit's mandate and plans (usually smaller, less well-regulated organisations)	'A whole mixture of lack of skills, lack of resources, lack of capacity' (CAC D) implied that internal auditors] won't be able to do what they have got to do' (CAC B).
Property 6: Status of and value added by internal audit Concept indicators: Data incidents: - Contrasting how and when the status of internal audit and the value it adds in an organisation influence reliance - Motivating how the status of internal audit and the value it adds in an organisation are determined and changed			
'I think [the status of the internal audit function], obviously it definitely does contribute [to reliance]. I think, the fact that [internal audit] are a trusted advisor and seen to add value within the organisation, I think that adds … credibility to them, it really helps them in identifying the risk areas and I think it probably gives	Internal audit is effective (usually larger, well-regulated organisations): - Internal audit reports contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems - The chief executive officer and management openly acknowledge	Internal audit is ineffective (usually smaller, less well-regulated organisations): - Internal audit reports contain the same simplistic recommendations every year - Management ignores internal audit findings and recommendations	Internal audit is tolerated as a 'grudge cost' (CFO C). Internal audit 'would report and then [it would] take three, four months to get comments on their management letter' (EP C).

them wider access into the business and I think because they are there all year round and they are also focussing on operational risks and therefore also have a lot of exposure to the operating people and at very high levels then if they are regarded … as a major stakeholder, I think that definitely does … assist us [external audit] in the reliance' (EP B). Internal audit reports are 'realistic and practical' (EP E2), addressing 'the real root cause' of problems (CAE B). Internal audits deliver the 'right findings' that are 'critical to the business' (EP E1).	and support the value of internal audit to the business - External auditors prefer relying on work of the strong in-house rather than outsourced internal auditors	- External auditors favour reliance on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm	'So, if there were to be a fraud, for example … in a sensitive area of the business. If [management] were to turn away from the internal audit [function] and rather go externally, that would give me some concerns [about the status of internal audit]' CAC D). 'Superficial' reports with 'the same recommendations every year' (CAE B).
Property 7: The profile and role of the chief audit executive Concept indicators: Data incidents: - Contrasting how, when and why the profile and role of the chief audit executive in an organisation influence reliance - Describing the desired profile of the chief audit executive			
'A very strong head of internal audit' (EP B).	A very strong head of internal audit: - A senior independent influential leader with: ○ Business and industry insights ○ A commercial orientation ○ Hands-on assurance experience and qualifications ○ The ability to communicate and contribute to the business at all levels ○ The ability to accept and drive change - Appointed by the audit committee	The wrong person in the role of chief audit executive, with the risk of being discarded by management and the audit committee	'If you've got the wrong person [as CAE] … [the internal auditors] really are going to face an uphill battle' (CAC D)

	- Has direct access to the audit committee, the chief executive officer and the chairperson of the board - Effectively manages internal audit's budget, capacity and resourcing and the relevance and credibility of internal audit work, thus contributing to the status of internal audit and the value it adds - Receives minutes of all executive committee meetings, incorporates work on new and evolving risks in internal audit plans and guides the audit committee about questioning management during meetings		

***Source**: Own compilation*

4.5.4 The relevance of internal audit work for statutory audit purposes

The relevance of internal audit work for statutory audit purposes is a sub-category of the substantive category entitled stakeholder groups' roles, interpretations, interests and practices influencing reliance. This sub-category includes five properties, (a) the scope and focus of internal audit's mandate and plans, (b) the type of internal audit, (c) the internal audit approach, (d) collaboration between internal audit and risk management and (e) the external audit approach.

Two properties of initial categories were refitted into this sub-category, namely 'D1: Risk focused' and 'F6: Focus of internal audit' (Table 4.2).

Table 4.9 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this sub-category. The concept indicators are also indicated.

Table 4.9: The relevance of internal audit work for statutory audit purposes

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: The scope and focus of internal audit's mandate and plans Concept indicators: Data incidents: - Specifying and motivating the ideal scope and focus of internal audit's mandate and plans - Describing and contrasting how and motivating when and why the scope and focus of internal audit's mandate and plans influence reliance - Specifying influences on the scope and focus of internal audit's mandate and plans - Specifying implications (particularly risks) for the business and reliance when changing the scope and focus of internal audit's mandate and plans			
'Make it very clear what [management] is expecting [from internal audit] … so, you understand where does the internal audit team fit in' (CFO A). 'Add[ing] value by bringing a strong sound assessment and testing process around controls' (EP A2). 'In the past … internal audit would do work specifically for external audit ... So it wouldn't necessarily be the areas of control that internal audit would focus on if you are looking at the risk universe, or universe of potential testing from a risk perspective, but they had completed that testing because it was testing that otherwise an external auditor would need to do, and we were able to give them a reduction in their audit fee because their internal auditors were doing the work instead. Now internal audit is entirely driven by a risk directed plan, and if they happen to test in an area that we [external audit] can rely on, then that's great, but	Management, the audit committee and internal audit mutually agree on a realistic mandate and plan for internal audit which balances the benefit versus reward of work both included and excluded from internal audit's mandate and plans, by prioritising risk-based audits Internal audit performs work outside the typical scope and focus of internal audit mandates and plans captured in the definition of internal auditing, including: - A large proportion of direct assistance work (including controls assurance work and extensive substantive procedures) for statutory audit purposes are edited into internal audit plans during alignment planning - Internal audits have a strong financial focus	Internal audit is often faced with conflicting demands on internal audit resources by too many bosses, for example, special investigations and *ad hoc* work for management A larger proportion of internal audit work and plans have mostly an operational focus	'Internal audit's eye [is] off their key value' (EP A2). 'Too many *ad hoc* requests, too many special investigations that impact on the normal assurance work [of internal audit]' (CAE C). 'Sometimes audit committees … feel that internal audit is there to do some work of external audit, which is not the case' (EP E1). 'Internal audit is there to reduce the work of external audit' (EP E2). 'More operational, not financial[ly] linked' (EP D2).

that's certainly not their role, and I agree with that change of perspective ... it should be internal audit's role to understand the risks of the business and to ensure that there is appropriate control over those risks and test those controls are all in place effectively; and if that happens to overlap with what external audit needs, all the better, but it won't always happen' (EP E1). 'Quite a strong financial focus' (CFO B).			
Property 2: The type of internal audit Concept indicators: Data incidents specifying and contrasting the types of internal audits performed and outlining and motivating their influence on reliance			
'Cover the right areas on a risk-based approach' (CFO B).	Internal audit focuses on risk-based audits, including key and evolving risks and process changes, assessed while internal and external auditors work closely together on joint risk assessments	Internal audits consist mostly of routine, conventional, rotational internal audits and random 'ticking and bashing'	'Ticking and bashing … not looking at risks' (EP C).
Property 3: The internal audit approach Concept indicators: Data incidents specifying and contrasting the internal audit approaches and outlining and motivating their influence on reliance			
Moved from a 'transactional approach' to a holistic 'governance process' approach (CAE B) OR Moved to an 'end-to-end … integrated audit approach' (CAE E).	Internal audits cover key risks annually as part of a base audit plan or internal and external audit rotate coverage of key risks Most reliance is possible at subsidiary level rather than at group level of larger listed companies, as internal audits at subsidiary level usually incorporate a large volume of audit work, in accordance with a transactional, end-to-	Most Internal audits consist mostly of routine, conventional, rotational, internal audits and random 'ticking and bashing'	A 'transactional approach' (CAE B).

Internal audit should rather focus on 'the auditing of culture and the auditing of people … it is all about that actually because if you look at it, it is all about the people and if you do a bit of a debrief over the [control] environment and it significantly changed … there is usually a change in leadership or a change in the system or a change in the structure or process … then there is like a quantum leap in terms of the control environment, otherwise it is structural changes maybe to the control environment' (CAE B (2019)).	end, integrated business process approach rather than the holistic governance process approach, with emphasis on the control environment and significant risks associated with management's financial reporting culture, applied at group level		
Property 4: Collaboration between internal audit and risk management Concept indicators: Data incidents specifying and contrasting collaboration between internal audit and risk management outlining and motivating their influence on reliance			
'Risk and internal audit work closely together' (CAC B).	Risk management and internal audit work closely together, meaning they share an integrated risk view	Risk management remain on the side, without mutual sharing of information on key risks between internal audit and risk management	'Risk management almost sits on the side' (CAC C).
Property 5: The external audit approach. Concept indicators: Data incidents: - Specifying and contrasting the internal and external audit approaches and their influence on reliance - Describing and contrasting the views of different stakeholder groups about the external audit approach and their influence on reliance			
'[For] … a great working internal control environment and processes … they [external audit] … can … rely on this internal control environment [and if] … internal audit [has] done work [use that as part of a combined approach] ..., if not we [external audit] need to do [substantive] work' (CFO A).	External audit incorporates controls assurance work on key risks as part of a combined audit approach and / or direct assistance work his includes tests of controls and extensive substantive procedures, meaning that the external audit	The external auditor performs extensive substantive procedures rather than a combined audit approach	'If there isn't [a great working internal control environment and processes], [there] … is unfortunately nothing [external audit] can do other than … doing a lot of substantive work to validate the financial position at that point in time [year end] [and] … there is no point then bringing internal auditors [on board]' (CFO A).

	approach is somewhat irrelevant for reliance purposes		

Source: *Own compilation*

4.5.5 The credibility of internal audit work for statutory audit purposes

The credibility of internal audit work for statutory audit purposes is a sub-category of the substantive category entitled stakeholder groups' roles, interpretations, interests and practices influencing reliance. This sub-category includes four properties, (a) the competence of internal audit, (b) the independence of internal audit, (c) the standard of internal audit work and (d) meeting and changing the internal audit plan.

Eight properties of initial categories were refitted into this sub-category, namely 'D3: Competence', 'F2.4: Internal audit competence', 'D6: Independence', 'F2.2: Internal audit independence', 'D4: Performance', 'F2.1: Internal audit stability',, 'F2.5: Internal audit quality control processes' and 'F2.6: Standard of internal audit work' (Table 4.2).

Table 4.10 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this sub-category. The concept indicators are also indicated.

Table 4.10: The credibility of internal audit work for statutory audit purposes

<table>
<tr><th colspan="2">MORE reliance</th><th colspan="2">LESS reliance</th></tr>
<tr><th>Illustrative quotations</th><th>Dimensions</th><th>Dimensions</th><th>Illustrative quotations</th></tr>
<tr><td colspan="4">Property 1: The competence of internal audit

Concept indicators: Data incidents:
- Specifying, contrasting and motivating how the competence of internal audit influences reliance
- Specifying and contrasting attributes of a competent internal audit team and auditor
- Describing and motivating challenges in filling internal audit positions
- Describing and motivating the competence of the internal audit team in each case</td></tr>
<tr><td>‘The right [mix of] skills to perform the work’ (EP E1).

‘We [external audit] will do an assessment as part of our audit planning process, but its relatively straightforward because it’s [internal audit] a pretty stable team’ (EP E1).

‘I might have a smaller, nimbler … more specialised, more senior team that maybe didn’t look too much at the detail … but [followed] more of the kind of high-level structure and system, process [approach]’ (EP A2).</td><td>The internal audit team has unquestionable competence:

- The right mix of skills to fulfil its risk-focused mandate
- A smaller, stable team consisting of:
○ Mostly senior level internal auditors
○ Sufficient management level internal auditors
○ A majority of professional career internal auditors
○ Some internal auditors with specialist industry and operational skills
○ Some business staff on a rotational basis</td><td>Internal audit lacks competence as skills gaps exist in the team, particularly in larger teams consisting of mostly junior internal auditors with insufficient managerial skills

External auditors favour reliance on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm, who they believe are more competent than in-house internal auditors as they possess specialised and acknowledged skills</td><td>‘Not at a level where you can start relying on that [internal audit] work’ (EP D1).

‘The internal audit teams that I have seen in South Africa there is a skills gap at that level … that manager level (EP A2).</td></tr>
</table>

<table>
<tr><td colspan="4">Property 2: The independence of internal audit

Concept indicators: Data incidents:
- Specifying, contrasting and motivating how the independence of internal audit influences reliance
- Describing and motivating indicators of independence and red flags indicating threats to independence
- Describing and motivating the independence of the internal audit team in each case</td></tr>
<tr><td>‘Able to do their job unimpeded and their findings are taken seriously’ (EP D2).

‘It is a fine balance … the [internal] auditors shouldn’t be afraid to get close to business … It’s one thing to be independent in mindset and in the way you [internal audit] work … and another thing to be … so independent that you don’t want to do good’ (CAE B).</td><td>Management acknowledge they should not dictate the scope and focus of internal audit’s mandate and plans

Internal audit’s mandate, plans and reports are of unimpeded scope:

- The chief audit executive effectively balances the relevance and unimpeded scope of internal audit’s mandate, plans and reports, without isolating internal audit from business realities
- The chief audit executive refrains from accepting operational and / or managerial activities
- The chief audit executive is supported by a direct reporting line and direct access to the audit committee chair
- The chief audit executive trusts the audit committee chair will address internal audit challenges and honour the confidentiality of information shared
- The chief audit executive actively manages relationships between internal auditors and business staff, including by:
○ Rotating internal audit teams, areas and auditees</td><td>External auditors express general doubt about internal audit’s ability to remain independent

Indicators of independence problems:

- In smaller organisations management dictate the scope and focus of internal audits and reports by involving internal auditors in operational and / or managerial activities
- In larger internal audit functions, flexible internal auditors manipulate audit findings to suit management
- The absence of disagreement between internal audit and management about internal audit findings
- The absence of internal audit findings, particularly in areas highlighted as problematic by external audit procedures
- Management and internal audit openly share a close symbiotic relationship.

External auditors favour reliance on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm, on grounds of their automatic</td><td>‘Internal audit is being directed by senior management’ (CAE D).

‘What worries me in a sense is when you get to the lower levels in the (internal audit) organisation and then you have auditors that are probably a little bit more flexible in their approach, and they may change ratings just to suit management’ (CAE A).</td></tr>
</table>

	○ Continuous actions to raise awareness of and provide training on the importance of independence ○ The internal quality assurance programme - The chief audit executive is willing to report even uncomfortable findings verbally and in writing	independence when compared to in-house internal auditors.	
Property 3: The standard of internal audit work Concept indicators: Data incidents: - Specifying, contrasting and motivating how the standard of internal audit influences reliance - Specifying and contrasting attributes of the standard of internal audit work - Describing and motivating practices influencing and proxies indicating the standard of internal audit work - Describing and motivating the internal and external quality assurance reviews to determine the quality of internal audit and its work (including the external auditor's ISA 610 assessment)			
'Internal processes [of the internal audit function] … are well developed and fairly stable' (EP B).	The chief audit executive ensures that internal audit work is of a credible standard, as evident from: - A stable internal audit team - Well-developed, stable, risk-based internal audit processes focused on key risks / controls - Compliance with the Standards - Quality audit documentation - Quality control procedures - Internal audit reports which: ○ Contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems	External audit questions the credibility of the in-house internal audit team's work, for example, when in prior years internal auditors' reliance work was of a lower quality than initially anticipated due to a skills gap in the team External auditors favour extensive substantive procedures and reliance on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm, as no doubt exists as to the credibility of their work	'The quality and standard of work that is done by internal audit is not up to standard' (CAE D).

	○ Appropriately incorporate all conclusions anticipated by the external auditor - Management relying on internal audit reports and recommendations		
Property 4: Meeting and changing the internal audit plan Concept indicators: Data incidents: - Specifying, contrasting and motivating how meeting internal audit's plans influences reliance - Describing and motivating why internal auditors find it difficult to meet their plans and how they overcome these challenges			
'The [internal audit] plans are met … [as internal audit] gets through the work' (CAC B). 'This audit plan that is prepared three months before the start of your financial year, [it] is a plan at a point in time and in line with our internal auditing standards. It has to be reviewed actually formally during the year. You can't sit with that plan for fifteen months … So, it has got to be flexible because it must be risk based. Things happen during the year; you can't plan for everything that will happen' (CAE C).	Internal audit mostly meets their flexible internal audit plans, which uses an 80 / 20 principle to allow for internal audit's responses to changing and emerging risks Audit committee oversight provides the 'balance' needed to ensure internal audit capacity allows risk-based audits and meeting the internal audit plan in spite of changes	Uncompleted internal audit plans are the norm, as: - The audit plan is too optimistic, quality is compromised for quantity as internal audit is used as a tick exercise - Too many special investigations and *ad hoc* work for management impact on normal assurance work	'The audit plan is too optimistic … either can't be done or … compromise on quality' (CAE C). 'Very often … the internal audit function … they'll start with a whole audit plan and only do a bit of it' (EP D1).

***Source**: Own compilation*

4.5.6 External audit quality and the external auditor's liability

External audit quality and the external auditor's liability is a sub-category of the substantive category entitled stakeholder groups' roles, interpretations, interests and practices influencing reliance. This sub-category includes two properties, (a) the riskiness of reliance and (b) sufficient external auditor involvement in the audit of key risks.

Three properties of the initial category 'F: Evaluating conditions for relying' were refitted into this sub-category, namely 'F3: Risk and subjectivity of audit area', 'F5: Previous reliance' and 'F8 EA approach' (Table 4.2).

Table 4.11 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this sub-category. The concept indicators are also indicated.

Table 4.11: External audit quality and the external auditor's liability

<table>
<tr><th colspan="2">MORE reliance</th><th colspan="2">LESS reliance</th></tr>
<tr><th>Illustrative quotations</th><th>Dimensions</th><th>Dimensions</th><th>Illustrative quotations</th></tr>
<tr><td colspan="4">Property 1: The riskiness of reliance

Concept indicators: Data incidents:
- Specifying, contrasting and motivating influences on interprofessional reliance
- Specifying and contrasting attributes of the two professions contributing to and mitigating engagement risk
- Describing and motivating practices that mitigate engagement risk</td></tr>
<tr><td>'As long as [external auditors] are careful in the work they rely [on], [and] … as long as the internals [internal auditors] are independent and seen to be independent, and have the support of the audit committees … [all four stakeholder groups] can move together closer, but it is going to be an uneasy relationship' (CAC D).</td><td>The external auditor carefully selects reliance work independently of external influences, considering:

- Whether the combined approach to assurance, including alignment between internal and external auditors, mitigates undue reliance and minimises assurance gaps
- The relevance of internal audit work for statutory audit purposes
- The credibility of internal audit work for statutory audit purposes
- Support of the audit committee

External auditors do not limit reliance on grounds of their sole liability for the audit, as they do not question the relevance of internal audit work nor the credibility of internal audit work</td><td>External auditors perceive that reliance is difficult and focus on the complexity of an audit and the riskiness of reliance, considering the differences in the professionalism of the two professions and the distinct roles of internal and external audit

External auditors also consider:

- Management's practices which compromise the relevance and credibility of internal audit work
- Management often expecting reliance despite internal audit reports concluding internal financial controls are not operating fully
- The risk of not meeting their reporting deadlines when reliance does not materialise as planned, particularly when issues arise later in the reporting period, including when:
  ○ Internal audit's reliance work finds internal financial controls are not operating fully and the external audit approach has to</td><td>'As an external auditor that signs those accounts, that takes responsibility … it's difficult enough working within your own firm … Nine times out of ten … [management] don't even give thought to the fact … [they] don't have a proper internal audit department or have not allowed [internal audit] to do what they need to do. Or they don't have the tools that they need to actually perform their work. So, I think there's a bit of a contradiction in terms of what management expects and what they're prepared to do in terms of coming to the party' (EP D1).

'There is no statutory duty by the internal auditor, and especially no statutory sanction on the internal auditor' (CAC A).

Internal auditors 'are moving up the curve, whether they are there [at the level of trusted advisor] yet, I'm not sure that they are quite there yet' (EP A1).

'Getting the right people is the key challenge I think in terms of internal audit. It's not</td></tr>
</table>

		change to extensive substantive procedures o Internal auditors do not compete all planned work as too many special investigations and *ad hoc* work for management impact reliance work amidst internal audit budget / capacity / resourcing constraints and evolving risks o External auditors have to redo internal audit work of a poor quality o External auditors have to reassume responsibility for delayed or transferred work originally allocated to internal audit - The contrast between the superior professionalism and credibility of work of the external audit profession and teams against the inferior professionalism and credibility of work of the internal audit profession and in-house internal audit teams External auditors limit reliance to the bare minimum on grounds of their sole responsibility for the external audit and plan to keep on limiting reliance until there is a sharing of liability between internal and external auditors External auditors favour working with their own teams or relying on work of outsourced internal audit partner peers	sexy, it's not exciting, it's not fun, you know, so to try and find the right people or to try and raise the profile of the internal auditor and process … attracting and retaining the right people so that the internal audit process receives the right kind of attention from the right kind of people' (EP A2). 'It is hard to find those, … that level of staff and the level of staff that are willing to stay as an internal audit manager for a substantial amount of time … there aren't that many people that will stay within internal audit for a number of years. So, I think that's quite a special kind of person that will stay there' (EP B). Internal auditors 'are stuck in a corporate structure. So, you can't just make them a senior auditor, because you now [already] have a senior auditor' (CAE B).

		from Big 4 accounting firms rather than using the work of the in-house internal audit team	
Property 2: Sufficient external auditor involvement in the audit of key risks Concept indicators: Data incidents: - Specifying, contrasting and motivating sufficient external auditor involvement in the audit of key risks when practising reliance - Describing and motivating practices that support reliance in higher risk areas			
‘External audit needs to also audit certain areas from time to time … [they] can't just always place reliance on internal audit because they cover an area’ (CFO B). ‘We [external audit] would also look at the level of reperformance [of internal auditors’ work required in lieu of reliance]. So, where [the audit area] is so critical for us, the level that we would be reperforming, … makes it more efficient for us [external auditors] to look at it then [rather than relying on internal auditors]’ (EP B).	The external auditor carefully considers sufficient external auditor involvement in the audit as a whole, taking into account sufficient external audit coverage and the efficiency of reperformance levels, considering: - External audit wants to cover very significant risks themselves, usually by means of extensive substantive procedures - When a significant risk is present, external audit does not use internal audit work on the complete area Rotating assurance work on key risks between internal and external audit to avoid unnecessary duplication of audit work while ensuring sufficient external auditor involvement in the audit	Sufficient external auditor involvement in the auditing of key risks is not problematic as they practise no or limited reliance.	No quotations, as sufficient external auditor involvement is redundant in light of no or limited reliance.

***Source**: Own compilation*

4.5.7 Working mindset

The substantive category entitled working mindset includes five properties, namely (a) the assurance approach, (b) internal and external auditors working together, (c) internal and external auditors substituting versus only complementing each other's work, (d) the quality of the relationship between internal and external auditors and (e) the working mindset of the two audit teams.

Four properties of various initial categories were refitted into this sub-category, namely 'A1: Combined assurance approach', 'H2: King III on combined assurance and ISA 610', 'I5: Function as one team' and 'I6: Mutual respect' (Table 4.2).

Table 4.12 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this sub-category. The concept indicators are also indicated.

Table 4.12 Working mindset

<table>
<tr><th colspan="2">MORE reliance</th><th colspan="2">LESS reliance</th></tr>
<tr><th>Illustrative quotations</th><th>Dimensions</th><th>Dimensions</th><th>Illustrative quotations</th></tr>
<tr><td colspan="4">Property 1: The assurance approach

Concept indicators: Data incidents:
- Specifying, contrasting and motivating how different assurance approaches influence reliance
- Describing and motivating assurance approaches and practices which promote and moderate reliance</td></tr>
<tr><td>‘Combined assurance is very much to bring your fee down to a manageable level. That is why [internal and external audit] work together, so that any work that we do can be relied on by external audit and then … they [external audit] don’t have to do any work in that cycle again’ (CAE B).

‘In a company where combined assurance works well, that is where the company gets the maximum benefit from the combination of internal audit and external audit’ (EP B).

‘The combined assurance approach … King created quite a vibe around that. So, it really had been quite a bit of work being done and at our company level, to understand all the key risks and who gives assurance on that’ (CAE B).

‘[A] very clear and detailed understanding about what each other [internal and external audit] would be doing [by] really [following] a combined assurance programme’ (CFO B).</td><td>A combined approach to assurance is possible as a voluntary, closer, professional working relationship formed between internal and external auditors over time

Thus they:

- Have very clear and detailed shared knowledge of each other’s work, as they
- Synchronise the stakeholder groups’ assurance needs and responsibilities
- Understand each party’s responsibilities within the context of an integrated risk and assurance view
- Plan reliance around key risks of interest to internal and external audit included in rotational internal audit plans
- Ensure external audit cover key controls in the years in-between internal audit’s rotational audits
- Minimise unnecessary duplication
- Minimise assurance gaps</td><td>A silo approach to assurance implies distance between internal and external auditors

King III triggered changes to a combined approach, which is still under-developed, especially in less well-regulated organisations which have a weaker risk management function

Moving from a silo to a combined approach requires regular, triangular combined assurance meetings between management, internal and external auditors</td><td>‘Silo approach to assurance’ (CAE A).

‘There’s been a marked shift in [case A’s] combined assurance process … in the last eighteen months. I still think we’ve still got some way to go’ (EP A2).

‘The distance that has existed in the more recent past between internal and external audit, [adopting combined assurance] will bring them a bit more together’ (CAE D).</td></tr>
</table>

'Internal and external audit have been working well together pre-King' (EP B). Internal and external audit 'work very well together and they've got a history of working well together' (CFO E).	This approach mitigates engagement risk and mediates optimal habitual integration of internal and external audit work		
Property 2: Internal and external auditors working together Concept indicators: Data incidents specifying, contrasting and motivating how internal and external auditors working together influence reliance			
Responding to a question on what caused more reliance in some companies than in others, EP B replied: 'I think probably working more closely together … between the two [internal and external audit]'. 'We [internal and external audit] … look at each other together, and when the [internal and external audit] plans are presented to the audit committee, we make sure that we have a combined approach' (EP B). 'I think, if I look at this company [case B], I think we [internal and external audit] are quite far down the combined assurance line … [external audit] certainly do … follow a very combined approach with internal audit … But I think that there are plenty of other companies, which I have seen, which are not so far down … which are still getting there … those are probably companies where combined assurance only really came into play post-King. So, I think, those companies might be a year or two behind us. So, I think, there especially, the role between internal audit	Internal and external auditors have a history of working together well, following a combined approach in their aligned individual plans	Cooperation between internal and external auditors is still developing The balance between internal and external audit work is not yet optimal as unnecessary duplication of audit work occur	'My personal view is … I think [internal and external audit working together] have come a long way, but I think the journey is still significant to climb, because I don't think there is 100% alignment [of internal and external audit work] yet. I think there is some duplication at present' (CFO A). 'The end goal that everybody wants to get to [with combined assurance is the point where everyone agrees] … this is how we divided up the pie [audit work] … whether we are at that point right now, I don't think so. But it's still developing but my sense is that parties sit together mutually and agree what needs to happen, and I think that's happening a lot more than what we used to see in the past' (EP D2).

and external audit will become even closer' (EP B). 'So, we really worked as an integrated audit approach, we work together in that sense' (EP E2). 'I haven't seen it [the relationship between internal and external auditors] change dramatically, but they are working very closely together' (CAC B).			
Property 3: Internal and external auditors substituting versus only complementing each other's work Concept indicators: Data incidents: - Specifying, contrasting and motivating how internal and external auditors substituting versus only complementing each other's work influences reliance - Describing and motivating practices which promote and moderate internal and external auditors substituting versus only complementing each other's work			
'The [audit firm's] methodology [ensured] we [external audit] cover these areas here [and] [internal audit] cover those areas there … So, we really worked as an integrated audit approach, we work together in that sense and that's it' (EP E2). 'If there is areas where internal audit will look at a certain function [and] it is an area where external audit can place reliance… but if you [internal audit] can expand your scope slightly, it would help them [external audit] a lot [in relying], clearly we must … identify those opportunities … [Also if] it is in areas where external are saying …we already need to cover it from our perspective [and] … it is [also] in [internal audit's] rotation … then maybe internal audit don't … need to do the same work in the same year' (CFO B).	Internal and external auditors substitute rather than simply complement each other's work. Internal auditors facilitate substitution by: - Making slight adjustments to the scope of their work - Identifying overlapping work included in both teams' audit plans and, when appropriate, relying on work performed by external audit.	External audit tend to practise no or limited reliance as they: - Follow a silo approach to assurance - Ignore integrating work or aligning their plans with internal audit - Seek more comfort to mitigate high external audit engagement risk - Thus, internal audit work complements rather than substitutes external audit work Management and internal auditors: - Are dissatisfied with inefficiency inherent in unnecessary duplication of audit work - Question what reliance is, particularly its wider definition used by external auditors	External audit 'would not say [reliance on internal audit work] reduce the work [of external audit], it just assists in mitigating the [external audit engagement] risk. So, all I'm saying is if external audit has looked at it and internal audit has looked at it, because of the high [external audit engagement] risk factor, we just get more comfort that it's okay' (EP C).

<table>
<tr><td colspan="4">Property 4: The quality of the relationship between internal and external auditors

Concept indicators: Data incidents:
- Specifying, contrasting and motivating how the quality of the relationship between internal and external auditors influences reliance
- Describing and motivating characteristics of and consequences from the quality of the relationship between internal and external auditors</td></tr>
<tr>
<td>‘The predominant reason where it [reliance] has worked better [it] is because the two divisions [internal and external audit] … has … a closer working relationship between the two’. (EP B).</td>
<td>The enduring, voluntary, closer, professional working relationship formed between internal and external auditors is the predominant mediator of reliance, characterised by:

- Regular, open, less formal, confident knowledge-sharing on areas of concern
- Total acceptance that they have distinct roles</td>
<td>An uneasy professional relationship between internal and external auditors is still developing despite the two teams moving towards reliance

External auditors focus on their habitual working relationship with outsourced partners from Big 4 accounting firms</td>
<td>Reliance ‘is a learning curve and as a relation[ship] develops, you find that [reliance] improves steadily around the process. But it’s a give and take as well. It doesn’t help every time internal audit comes, to say guys I don’t like whatever you’ve done, sorry I’m not willing to work on it [rely] and move away. But if it’s an interactive session where we both sit down and discuss why, what has happened, etcetera, it helps in building the overall process and I think both parties will benefit in the long term and both parties are learning’ (EP D2).

‘The increasing professionalism of internal auditors … as they become more proficient and seen to be more proficient, so the acceptance by external auditors is increasing … going back a number of years they [internal audit] were seen … as fairly junior staff members doing a very routine function, but … adding risk to the work of internal audit, which I think is a good thing … certainly has added to their lustre and to their kind of influence in the organisation. So I think it [the relationship between internal and external auditors] is going in the right direction. As it [internal audit] becomes more professional, it [reliance] becomes … an easier thing to achieve’ (CAC D).</td>
</tr>
</table>

Property 5: The working mindset of the two audit teams Concept indicators: Data incidents: - Specifying, contrasting and motivating how the working mindset of the two audit teams influences reliance - Describing and motivating characteristics of and consequences for reliance from the working mindset of the two audit teams			
'If [internal and external audit] can really work together as a team on the assurance … in the beginning it might be … forced habit, but what do they say you know it is every now and again you have to force yourself to do something then it becomes habit and I think, … in the beginning it might be something that you consciously do and later on … I think it's just the way that you work' (EP B). 'It's important that [internal and external audit] basically see each other … as giving a combined assurance. Obviously, ultimately [external audit] sign [their] own opinion, but [internal and external audit] do see … [themselves] as a greater part of an assurance given to the company' (EP B).	Having a team mindset changes reliance from being 'forced habit' into 'just the way that you work' Internal and external auditors view themselves as: - A joint team - Speaking the same language - Providing combined assurance - Often issuing a single report to management and the audit committee on specific areas of the audit, although the external auditor signs the statutory auditor's report - The external auditors from Big 4 accounting firms offer continuous development opportunities to the internal auditors of their clients Reliance is expected to have a positive influence on external audit quality when: - Internal and external auditors engage in regular meetings and constructive debate throughout the year - Internal auditors share their deep insights, gained from daily involvement in the business, with external auditors - Internal and external auditors learn	A competitive mindset prevails between internal and external auditors Despite progress made, the uneasy relationship and competitive mindset between internal and external auditors continues, characterised by: - Rivalry - Tension - Competition - Some external auditors focusing on their habitual working relationship with outsourced partners from Big 4 accounting firms and working with their own external audit teams - Some external auditors contrasting their superior professionalism against the inferior professionalism of the internal audit profession, with specific reference to the external auditor's sole legal liability for the external audit and insufficient regulation of internal auditors - Some external auditors contrasting the superior credibility of the external audit team's work against the inferior credibility of the in-house internal audit team, considering they lack the support typically	CFO A referred to a 'competitive mindset' prevailing between internal and external auditors. He suggested that internal and external audit should use 'constructive debate' to 'cross' the 'competitive' 'mindset'. 'We [internal and external auditors] can move together closer, but it is going to be an uneasy relationship' (CAC D). 'I just feel that collaboration between internal audit and external audit, in general, has improved. There … are more meetings taking place, and [internal and external audit] realise that we need each other' (CAE C). 'It's going to be a mindset change to some extent … From an external audit perspective. It's going to be a mindset change in terms of how one operates' (EP D2). '[When] there's rivalry between … [internal and external audit]' (EP D1). 'So it's [reliance] difficult for us [external audit] … trying to manage our relationship with internal audit yet still accede to the demands and the requests of both management and audit committees to reduce costs by using internal audit more …

	from each other - Work together in the face of increasing assurance requirements and demands on internal and external audit and their budget / capacity / resourcing constraints - Ensure management and the audit committee get efficient comfort in totality A team mindset mediates: - Internal audit work habitually forming an 'integral' part of evidence on the statutory audit - An aligned 'audit methodology' on reliance areas	available to networks of global Big 4 accounting firms Although there is a slow movement towards some cohesion, internal auditors are impatient about the change happening too slowly	There is a tension there, and I think we'll [external audit] accede to a certain point and then say that's all we're prepared to do given the fact that we [external audit] don't share risk with them [internal audit]. This is where we're going to stop [relying]' (EP A2). 'We [the internal audit profession] will never attract the right kind of skill into that [internal audit] environment ... So that's a massive challenge [for reliance]' (EP A2). 'Some of my clients have sort of gone out and got these [external] bodies to come in and help with [their] internal audit department … I think there's a lot more that needs to be done [to improve internal audit] … if you look at what they [professional bodies for internal auditors] do as opposed to what the IRBA [regulator of external auditors] would do, or what our firm [does] … we've quality reviews that is done globally … we have guys that will come from any part of the world looking at the files'. (EP D1).

***Source**: Own compilation*

4.5.8 Integrating work

The substantive category entitled integrating work includes nine properties, namely, views on (a) what reliance is, (b) internal and external auditors' commitment to reliance, (c) the nature of reliance work, (d) the cost-benefit of assessing internal audit and its work, (e) who is best placed to provide the assurance, (f) the influence of the external audit firm software and methodologies on reliance, (g) the overlap between internal and external audit work, (h) duplication of audit work and (i) assurance effectiveness and efficiency, including external auditors' propensity for protecting audit firm fee income.

Eight properties of various initial categories were refitted into this category, namely, 'E1: Improved audit efficiency', 'E2: Improved financial controls', 'E3: Increased assurance / quality of assurance', 'F4.1: Accessibility of internal audit working papers for external audit', 'F4.2: Accessibility of audit area / data for external audit', 'H1: Management emphasis on audit efficiency', 'I1: Intention / openness to rely' and 'I4: From forcing to habit' (Table 4.2).

Table 4.13 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this category. The concept indicators are also indicated.

Table 4.13: Integrating work

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: What reliance is Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating what reliance is and how these influence reliance			
‘The [internal audit] team is integral and part of the [statutory audit] process’ (EP D2).	Internal audit work forms an integral part of evidence on the statutory audit	External auditors limit reliance to reading internal audit reports to inform the external audit approach and peripheral support by internal auditors – they perceive internal and external auditors’ definitions of reliance are misaligned Management and internal auditors are dissatisfied with the wider definition of reliance used by external auditors and the consequent lack of assurance efficiency – they perceive internal and external auditors’ definitions of reliance are misaligned	‘Reading [internal audit] reports and just putting it aside’ (EP D2). ‘I still feel there is more [reliance] that can be done; and also [internal audit’s vs external audit’s] definition of reliance, I think that is important. What is the definition of reliance? Because, there is a difference between taking into account for your [external] audit approach and relying. There is a difference for me in terms of that’ (CAE C).
Property 2: Internal and external auditors’ commitment to reliance Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating internal and external auditors’ commitment to reliance and how these influence reliance			
External audit: ‘The integral part of our [external] audit approach [and] methodology is reliance on their [internal audit] work ... it’s a given nowadays’ (EP E2). Internal audit:	All external auditors read internal audit reports and hold discussions with internal auditors prior to external audits External auditors habitually practise optimal integration of internal and external audit work, relying as much as they can, as doing so is an integral part	All external auditors read internal audit reports and hold discussions with internal auditors prior to external audits External auditors resist reliance and thus practise no or limited reliance Pressure to increase reliance does not necessarily change external auditors’	External audit: ‘There is a reticence on our [external audit] part to work too much with internal audit’ (EP A2). Reliance is something which ‘I’ve (external audit) never done so far’ (EP D1).

‘So the control work they prefer to give it to us, but we need to do it to a level and standard that they can rely on that’ (CAE B). ‘I’m very much a supporter of that [reliance] and [internal and external audit] really try and do that … [internal and external audit] work together to try and use whatever internal audit work is doing, external audit is trying to use as much of it as possible’ (CAE B). ‘The [external audit] plans upfront … are based on maximum reliance … obviously based on the work that internal audit have done’ (EP B). ‘I am absolutely for the use of internal audit [work] wherever possible … if internal audit has already tested it’ (EP E1). ‘I don’t think it’s consistent from one partner to the next … the experience between the two is very different’. CAE B (2019). CAE B (2019) predicted that compulsory audit firm rotation (in terms of legislation requiring audit firm rotation for South African listed companies from 2023) ‘is going to create a nightmare for combined assurance and reliance’ as the new firm will be unfamiliar with internal audit’s ‘approach’.	of the external audit firm’s audit approach and methodology Upfront alignment planning discussions and workshops make integration possible	general commitment to reliance as external auditors’ respond to pressure by *ad hoc* reliance attempts by focusing on those audit clients exerting pressure Reliance is not consistent across partners working on the same audit client of a firm External auditors’ commitment to reliance is decreasing, in parallel with the increasing professional risks they face Compulsory audit firm rotation is expected to render combined assurance and reliance more difficult as the new firm will have no reference point for making a reliance decision Management and internal auditors desperately seek greater reliance and are frustrated with reliance happening so slowly - they struggle to make sense of no or limited reliance and are dissatisfied with assurance efficiency Management believe that external audit firms’ internationally developed audit methodologies hamper reliance	‘I think there’s still a fair amount of resistance [by external auditors to rely]’ (EP D1). ‘So it’s [reliance] difficult for [external audit] … trying to manage our relationship with internal audit yet still accede to the demands and the requests of both management and audit committees to reduce costs by using internal audit more … There is a tension there, and I think [external audit] accede to a certain point and then say that’s all we’re prepared to do given the fact that we [external audit] don’t share risk with them [internal audit]. This is where we’re going to stop [relying]’ (EP A2). Internal audit: Internal and external audit ‘need to work together. We can’t afford the silo approach anymore’ (CAE C).

Property 3: The nature of reliance work Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating the nature of reliance work and how these influence reliance			
'So just the fact that [internal audit] work is in their plan, doesn't necessarily mean it's … something that we have agreed between the two parties that they will be doing and therefore our approach has been edited into it and adjusted. So I do think that it makes the lines quite burred, where you really have a combined assurance approach that you pre-plan together' (EP B). 'Sometimes they [internal audit] might even do substantive work for us [external audit] which is purely mandated where we actually ask them to do work on our behalf' (EP B). 'Some [direct assistance work] of it was substantive' (EP E1). 'They [internal audit] can do their work and [external audit] use their work, or, sometimes, what happens is that they do work that we specifically mandate them to do so it is almost an extension of the external audit' (EP B).	Reliance work includes a large proportion of direct assistance work for statutory audit purposes, which includes controls assurance work with a financial focus and extensive substantive procedures - this is edited into internal audit plans	External auditors limit reliance to reading internal audit reports and using peripheral support by internal auditors and make no or limited use of internal auditors for direct assistance work (however the chief audit executive regards inventory counts which internal audit conduct on behalf of external auditors as direct assistance work) External auditors' reasons for not using internal auditors' direct assistance work include: - It will not improve assurance efficiency as it would not reduce external audit fees - Limited internal audit budget / capacity / resourcing does not allow it (however the internal auditor indicates that internal audit plans do allow time for direct assistance work) - Internal audit's lack of access to and understanding of the external audit firm software and methodologies - Management expect a reduction in external audit fees - A preference for working with external audit's own teams rather than using internal audit staff	Asked about using direct assistance work, EP D1 replied: 'No, not at all'. 'At this large banking group … I don't think [external audit] have used them [internal audit] as direct assistance' (EP A1). 'No, [internal audit] resources are just too limited … I've never had an internal auditor on the [external audit] team…' (EP C).

Property 4: The cost-benefit of assessing internal audit and its work Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating how the cost-benefit of assessing internal audit and its work influence reliance			
'[In] a big place like this listed company, it's very cost effective using internal audit' (EP E2). 'We [external audit] will do an assessment as part of our audit planning process, but its relatively straightforward because [internal audit is] a pretty stable team; but of course if there were significant changes to the [internal audit] team, or the way in which they go about doing their work, I am sure we would have more cause for concern [about the cost-benefit of the assessment]' (EP E1).	External auditors perceive that the benefit of assessing internal audit and its work usually exceeds its cost, particularly when a stable internal audit team performs well-developed stable internal audit processes in larger organisations	The fixed cost of assessing internal audit and its work exceeds the audit fee saving Cheaper and less formal assessments of work by outsourced internal auditors compared to in-house internal auditors are performed Some managers view external auditors' assessments as onerous hurdles leading to over-auditing rather than reliance while others perceive that the benefits of assessing internal audit and its work outweigh the costs Some managers propose that external auditing standards should be simplified to make reliance easier and more efficient	'Ninety percent of the problem is … these big four auditing firms, have designed tests and assurances internationally. So they can only work in a certain ambit … and if they don't work within the standards their quality review will tell them they haven't done a fair audit and they will be brought to task … They are stuck in this paradigm and they would rather over-audit than actually audit the most effective things' (CFO C). The assessment requirements of ISA 610 posed 'onerous … hurdles … [that should be made] more efficient and easier for external auditors to rely on the work of internal auditors' (CFO D). 'We [external audit] do … a cost-benefit analysis … [in] a lot of small listed companies … it will take us longer to assess whether we can rely on the work of internal audit, than actually just do the work ourselves … [but in] a big place like this listed company, it's very cost effective using internal audit' (EP E2). 'It's not just getting their [internal audit] working papers, put it on file and say Bob's your uncle; you've [external audit] got to do more and that's what the audit committees don't understand' (EP C).

Property 5: Who is best placed to provide the assurance Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating how who is best placed to provide the assurance influence reliance			
‘Sometimes it's more beneficial for internal audit to look at it, whether it is that they have easier access to the data or for … some other reason, and then we [external audit] … will use that … kind of work’ (EP B). ‘The cost [external audit fees] is just driving [reliance] up, so [external audit] have to work with us … If we [internal audit] can do it much more cheaper or at a much better rate then [external audit] do it [rely]’ (CAE B).	All the stakeholder groups focus on ensuring that assurance comes from the most effective and efficient provider, considering: - The combined cost of internal and external audits - The level of assurance - Whether the internal audits had mostly an operational focus versus a strong financial focus - The geographical location of audit sites - Planned visits by internal audit to sites of third-party service providers of audit clients	Instead of relying on work of in-house internal auditors, external auditors favour working with their own teams and relying on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm	‘Our [external audit] staff go through a huge training process when they join us, and throughout the training period, so … to go in and pick up staff from internal audit, to come and do that, I don’t think it’s very feasible’ (EP D1).
Property 6: The influence of the external audit firm software and methodologies on reliance Concept indicators: Data incidents specifying, contrasting and motivating interpretations and practices indicating how the external audit firm’s audit software and methodologies influence reliance			
EP participants from MORE reliance cases did not refer to the use of audit software.	External auditors do not perceive audit firm software and methodologies to hamper reliance	External auditors perceive that reliance is hampered by internal audit’s lack of access and understanding of external audit firm software and methodologies	‘It is quite difficult … if you want the people [internal auditors] to do it [audit work] on the same basis, [external audit] need to … give [internal audit] one of our machines [computers] … [and] the training behind that and so on’ (EP A1).

Property 7: The overlap between internal and external audit work Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating how the overlap between internal and external audit work influence reliance			
'It is really about planning' (EP B). Internal audit work is 'all usable or feasible, but it doesn't mean that we don't have an external audit … You still have to have [an external audit]. You can use the base of what they [internal audit] do for you to enhance your external audit, I mean all the work that internal audit must do, should impact on the external audit. Whatever they do is going to give these guys [external audit] a feeling around, well is this one where they are really going to get fully into substantive or they can use control based, etcetera. But I don't think much of this [internal audit work] will eliminate the things that they [external audit] have to do' (CAC C / E).	Alignment planning identifies overlapping work in internal and external audit plans Reliance respect the distinct roles of internal and external audit, in particular the effect of reliance on internal audit's business-wide risk focus, concentrating on controls assurance work with mostly an operational focus Internal audit rely on relevant overlapping work of external audit	External auditors perceive that the distinct roles of internal and external audit mean that limited reliance is possible as overlap between the two is actually very small, and most likely to occur on controls assurance work Management and some audit committees believe that internal audit is there to reduce external audit work and fees	'That [overlap between internal and external audit work] is a limited thing' (EP A1). 'I think there should be good reliance placed because otherwise you just duplicating all over the show … I would either optimise my internal audit department or optimise my external audit department to get to … the right level of control' (CFO C). 'You [external audit] can't expect internal audit to go and do all the work and you come and sign your financial statements … there's still a lot of work that you as external auditors will still have to … do' (EP D1).
Property 8: Duplication of audit work Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating how duplication of audit work influences reliance			
'There isn't duplication of work unless there is a specific reason why we [external audit] are doing it' (EP B).	Aligned individual audit plans minimises unnecessary duplication of internal and external audit work and audit queries for management's attention Some internal audit work is duplicated or extended to ensure sufficient external auditor involvement in the audit of key risks	Management perceive extensive unnecessary duplication of work as the norm, leaving them sceptical about external auditors' commitment to reliance and dissatisfied with assurance efficiency	'There is probably about twenty to thirty percent in the middle, being duplicated' (CFO C).

	Alignment planning ensures as much cross-coverage as possible instead of duplicating audit work		
Property 9: Assurance effectiveness and efficiency, including external auditors' propensity for protecting audit firm fee income Concept indicators: Data incidents specifying, contrasting and motivating interpretations about and practices indicating how assurance effectiveness and efficiency, including external auditors' propensity for protecting audit firm fee income, influence reliance			
'Where they [internal audit] would do work which will … not [have] a material impact from a financial perspective, clearly then that would have limited value for the external auditors' (CFO B). 'From [case B's] perspective the internal audits have got quite a strong financial focus … a lot of the work they do impacts from a financial result [perspective] … it is not that there is a lot of work being done by internal audit which is complete and it has got no financial impact' (CFO B). 'So the control work [external audit] prefer to give it to [internal audit], but we need to do it to a level and standard that they can rely on that. Then if they can place reliance on the controls, then it reduces the amount of substantive work that they are doing. And with the pressure on cost in the organisations, they have to do it like that because otherwise the external audit fees just increase too much' (CAE B). 'But we just have to recognise that management does have a different agenda and although they all want … superb accounts and unsuspect reliance on what they are producing, they are also	Direct assistance work specifically included for statutory audit purposes reduces external audit fees All stakeholder groups focus on balancing assurance effectiveness and efficiency, yet favouring effectiveness over efficiency - this includes improving assurance coverage and reducing external audit fees and work Suggestions for increased efficiency: - External audit rely on internal audit's routine work, allowing external auditors to concentrate on more complicated or risky work - Assurance efficiency assessments should also acknowledge internal audit's implicit contribution to external audit effectiveness by considering what work external auditors are doing and what work they would have done if no internal audit had been present When either team uses data analytics assurance effectiveness and efficiency improve	No or limited reliance does not necessarily translate into reduced external audit fees Some managers and some audit committees strongly focus on increasing reliance to reduce external audit fees and work. They are thus: - Dissatisfied with assurance efficiency - Believe some external auditors unfairly act in their own self-interest instead of considering assurance efficiency - Believe external audit firms' internationally developed audit methodologies hamper reliance Some external auditors believe that management's general focus on profit margins means that they put excessive focus on reducing external audit fees by increasing reliance rather than considering the effect of reliance on external audit quality and the external auditor's liability	Reliance 'doesn't drive down your [statutory] external audit fee, it drives down the fee to sign off on SOX [related work] … it definitely drives down our SOX [related] work but not [the statutory] external [audit fee] … in reality no, but what we [external audit] tell our clients … there's a one or a two or a three percent saving' (EP C). 'The moment we [external audit] bring them [internal audit] in, management or the client wants a deduction in their [external audit] fee' (EP C). 'I don't think that external audit ever wants to rely willingly on internal audit … I mean … it's not in their interest to do less work' (CAE E). 'I can crudely say it is fee issues [causing limited reliance] … But I don't think it is that only … hopefully it is ten percent of the issue' (CFO C).

very cost conscious and returns conscious, so it is a balancing act to some extent and the audit committee obviously plays an important role here' (CAC D)	The audit committee's oversight of assurance effectiveness and efficiency is important	Ignoring their own influence on reliance, some managers hope to increase reliance through: - An external assessment of the internal audit function and its work to identify any shortcomings preventing reliance - Seeking guidance on the redesign of internal audit tests to align the audit methodology on reliance areas to requirements for both internal and external audit - Open discussion of reliance in quarterly meetings with the incoming engagement partner to actively promote alignment planning.	

***Source**: Own compilation*

4.5.9 Aligning work

The substantive category entitled aligning work includes nine properties, namely (a) alignment planning of internal and external audit's (b) focus, (c) objectives and approaches and (d) methodologies, particularly (e) the period covered by reliance work, (f) sampling and selection, (g) response (time) to audit exceptions, and (h) the timing of internal audit work as well as (i) meeting the aligned audit plans.

Five properties of various initial categories were refitted into this sub-category, namely 'A6: Aligned audit plans', 'A7: Risk-based adjusted audit plans', 'F1: Timing of internal audit work', 'F7: Outcome of joint planning process' and 'F9: Alignment of internal and external audit methodology (including sampling)' (Table 4.2).

Table 4.14 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this sub-category. The concept indicators are also indicated.

Table 4.14: Aligning work

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: Alignment planning Concept indicators: Data incidents specifying, contrasting and motivating when and how alignment planning influences reliance			
'I think [aligning internal and external audit work] is really about planning so I think it is where, I think if you can have workshops and … understand … what does internal audit do … and what do we [external audit] do … and … where are there overlaps, where are there potentially gaps between the two processes … once you understand that then there can be a reshuffle … I think it is working closer together. So really having this combined approach where you plan your work together. You discuss upfront, you agree, so I think it's important that you basically see each other, you see yourselves as giving a combined assurance' (EP B). 'The parties are planning upfront early' (EP D2). 'They [internal audit] meet regularly with the external auditors and they sit down and look at the plans, the internal audit plans for the year and obviously work together to, to make it as efficient as possible' (CAC B).	Structured upfront alignment planning discussions and workshops with good communication well before the beginning of the financial year – indicating that external auditors move their audit planning earlier than usual to accommodate alignment planning Internal and external audit work closely together as part of a combined approach to assurance – however, external audit does not prescribe to internal audit what to do Internal and external audit mutually understand each other's work and plans. After reviewing internal audit plans, external audit liaise with internal audit about incorporating specific additional work in their own plans to increase reliance opportunities Internal and external audit agree on reshuffled and aligned individual audit plans, taking into account requirements for sufficient external auditor involvement in the external audit	Management acknowledge that alignment planning is important and that they do not spend enough time on it Insufficient alignment planning: - No structured upfront alignment planning discussions and workshops - Planning of internal and external audits does not happen simultaneously - No sharing of information about the focus of and progress made with internal audits during informal discussions with external auditors - Instances where the 'balance' between internal and external audit work is 'not 100% - Instances when internal auditors are not willing to change their plans - Internal audit's planning is 12 months ahead of external audit's planning - Approval of internal and external audit plans by the audit committee does not occur simultaneously - Internal audit presents their plan for audit committee approval significantly before external audit	'The balance is not 100% … internal audit and … external audit need to get closer together to talk more actively during the year and plan better' (CFO A). 'I mean in the past you know we internal / external audit would do, I mean an internal audit would do work on the revenue sort of cycle. They would do work on the debtors or creditors. You will find that external audit would look at what work was done by internal audit in the areas of creditors/debtors, revenue, fixed assets etc and would take that into account, ja, in determining how much reliance they can place on the work of internal audit, and reduce the amount of external audit work that is done in those particular areas and I don't see that happening now. Ma'am, there is hardly any discussion that we have in that area' (CAE D). '[External audit] need to address it [perform audit work] … because the planning wasn't happening simultaneously' (EP D2). 'Instances where they [internal audit] are not willing to change [their plans]' (EP D2).

	Reshuffled and aligned individual audit plans are presented to management and the audit committee well before the beginning of the financial year The audit committee approves internal and external audit's aligned individual audit plans simultaneously well before the beginning of the financial year Assurance effectiveness and efficiency benefit from planning as: - Overlaps in internal and external audit plans are addressed - Assurance gaps are minimised Value-adding increased assurance coverage is possible when time saving is used to perform additional work of significance to the business	Suggestions for improving alignment: - Internal and external audit need to get closer together to talk more actively during the year and plan better as part of a continuous path of improvement of alignment - Retrospective pre-planning to identify overlaps which should be avoided in future periods - Identifying direct assistance work which internal audit can do	
Property 2: Aligning internal and external audit's focus Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning of internal and external audit's focus influences reliance			
'So I think it is important that [internal and external audit] work together **…** and you understand together what are the risks and how are those addressed and then I think once you, once you understand that then there can be a reshuffle' (EP B). 'We [external audit] sit down with [internal audit], and say … there's your audit program … we'd like you to cover these areas in your audit program as well. So you can have … we have like ten procedures to be covered. You can have twenty in your programme … So we don't	Internal and external auditors' reshuffled plans reflect a joint focus on key financial risks - external audit plan reliance around internal audits' 'three-year rotational plan' by using internal audit's work on 'key areas of control' in years when internal audit test them, while the external audit team audit those controls in the 'years in-between'	Instead of discussion with external auditors, internal auditors use external audit's management letters when doing risk assessments as part of their audit planning	'If there is sufficient time … you [external audit] may well ask [internal audit] to do … additional work which they may have scoped out, and if they are unable then … [external audit] would say look we have to do it' (EP A1).

actually prescribe to them what to do, but we tell them we'd like you to include this in your [audit plan] … for us to rely on it, please include these procedures as well' (EP E2). 'They [external audit] are very much concerned in terms of our financial reporting [while] internal audit [has a] much wider view on risk. So you should never have perfect alignment … otherwise you can just have one audit team. It is very-very risky to have complete alignment' (CAE B).			
Property 3: Aligning internal and external audit's objectives and approaches Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning of internal and external audit's objectives and approaches influences reliance			
'We [internal and external audit] engage in … discussion and say … now we can do it better … so it is an ongoing process from our side and their side to understand the approach better' (CAE B).	Internal and external audit's aligned approaches concentrate on controls assurance work on key risks Discussion fosters a shared understanding of their respective objectives and approaches, allowing the two parties to identify areas where external audit inadvertently performs extensive substantive procedures in cases where reliance on internal audit's controls assurance work should be possible	Less reliance occurs when internal audits follow a simple transactional approach Unaligned objectives and approaches - as different sets of professional standards accommodate the distinct roles and unique objectives of the two teams	'It is difficult to really match [internal and external audit] approaches completely because the viewpoint [objectives] [of internal and external audit] is different' (CAE C).

Property 4: Aligning internal and external audit's methodologies Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning of internal and external audit's methodologies influences reliance			
'We [internal audit] need to do [audit work] to a level and standard that [external audit] can rely on' (CAE B).	Internal and external auditors' reshuffled plans reflect aligned audit methodologies meeting external audit requirements on reliance areas When agreeing upfront on methodologies, internal auditors discuss their methodology with external auditors, who then provide input and recommendations to improve reliance Discussion fosters a shared understanding of each other's requirements for professional work and plans influencing reliance Internal audit identifies opportunities for 'slightly' changing internal audit work to improve reliance	External auditors point out methodological differences between the two types of audit limited reliance Management criticised external auditors for using methodological differences between internal and external audits 'too quickly'; they viewed these as 'ridiculous' excuses for not relying	'Sometimes that's [methodological differences are] used too quickly, as an excuse [by external audit for not relying]' (CFO A)
Property 5: Aligning internal and external audit's methodologies – the period covered by reliance work Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning the period covered by reliance work influences reliance			
'The work … [external audit] rely on heavily to give us [them] maximum coverage [was] done towards the latter part of the year so that they [internal audit] cover as much of the financial year as possible' (EP B).	The period covered by reliance work is aligned as timeous alignment planning ensures internal audit covers the majority of the financial year - this includes moving internal audit work earmarked for reliance to the latter part of the year	External auditors maintain that dissimilarities between the period covered by internal and external audit work imply reliance on internal audit's work covering part of the financial period does not necessarily improve audit efficiency Management suggest external audit should cover the period excluded from internal audit work instead of repeating	'The period [internal audit] look at … it's not the same as [external audit's] period, [internal audit] would look at a month a year, [external audit] would look at 12 months' (EP C).

		work on the part of the year covered by internal audit	
Property 6: Aligning internal and external audit's methodologies – sampling and selection Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning internal and external audit's sampling and selection influences reliance			
'We [external audit] were able to influence sample sizes and of selection and so on' (EP E1). External audit enters into discussion with internal audit 'long before they started planning that audit … to ensure that in that planning [they are] able to influence [internal audit's] sample sizes and selection' (EP E1). Otherwise, external audit would be 'unable to use it' (EP D2).	Sampling and selection are aligned as internal and external audit engage early on the extent of tests, sample sizes and selection of audit items, based on an integrated view of key risks fostered through knowledge sharing Internal audit adjust sample sizes in line with external audit's minimum sample sizes to increase reliance Reading internal audit reports improves external audit's understanding of the effectiveness of internal financial controls as a basis for the external audit approach and sample sizes External auditors determine the net sample size for testing by the external audit team by deducting the number of tests conducted by internal audit from the total sample size required for their purposes. They conveyed that external audit's sample sizes are increased as they 'added on an additional sample', comprising the number of reliance items requiring 'reperformance testing'.	External auditors are unable to persuade internal auditors to increase their sample sizes Internal auditors note they adjust internal audit sample sizes to improve reliance	'If [internal audit's] sample size is ten, that's ten, [external audit are] not going to persuade them to test twenty' (EP C).

Property 7: Aligning internal and external audit's methodologies – response (time) to audit exceptions Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning internal and external audit's response (time) to audit exceptions influences reliance			
'We [external audit] don't always have that luxury of time, so [they] might need to extend testing or conduct other testing to give [them] the comfort [they] have decided on' (EP E1).	Internal and external audit's responses to audit exceptions are aligned due to direct assistance work	External auditors automatically know they should change to extensive substantive procedures when they encounter audit exceptions Conversely, internal audit would typically 'test everything', meaning that they test the full population of the related control When the end of the financial year is approaching and exceptions are not appropriately redressed by management, external audit needs sufficient time to perform alternative audit procedures in response to the risk exposure, which makes reliance impractical	'If [the audit exception was identified by internal audit by] 1 July and [the year-end] is 31 December, [external audit] can still say, okay' (EP A1).
Property 8: Aligning internal and external audit's methodologies – timing of internal audit work Concept indicators: Data incidents specifying, contrasting and motivating when and how aligning internal and external timing of audit work influences reliance			
'The most risky entities, [internal audit] will plan to perform those general financial controls, as close as possible to year-end … to have the information available to external audit, when they come in to perform their work' (CAE C).	Internal audit's controls assurance work on key risks is done as close as possible to year-end	When postponing internal audit work towards the period end in the hope of increasing reliance, external audit may have to finish off uncompleted work or re-do substandard reliance work allocated to internal audit - this creates risks for meeting external audit's deadlines When internal audit findings arising from postponed internal audit work contain control exceptions, external audit may	'Their [external audit's] plan for the current financial year is approved at that meeting, where [internal audit's] plan for the next financial year is approved' (CAE C).

		have to change to extensive substantive procedures - this creates risks for meeting external audit's deadlines	
Property 9: Meeting the aligned audit plans Concept indicators: Data incidents specifying, contrasting and motivating when and how meeting the aligned audit plans influences reliance			
'It [reliance] is really about planning' (EP B).	As internal auditors complete agreed reliance work, reliance does not influence meeting external audit's reporting deadlines	When internal audit prioritises *ad hoc* work for management due to changing the internal audit plan to accommodate 'specific requests', external audit has to do work initially earmarked for reliance - this has repercussions for meeting external audit's deadlines Instances where the external audit team had to redo reliance work after finding that its credibility was lower than initially anticipated, with repercussions on audit effectiveness and efficiency, including for meeting external audit's deadlines	'Delays in internal audit work, that obviously impacts what external audit do' (EP A1).

***Source**: Own compilation*

4.5.10 Overseeing reliance

The substantive category entitled overseeing reliance included two properties, namely (a) audit committee oversight of assurance effectiveness and efficiency, considering (b) the audit committee's inherent strength and closeness to the business.

Two properties of the initial category 'B: Overseeing reliance' were refitted into this category, namely, 'B1: Independent oversight' and 'B2: Well-established' (Table 4.2).

Table 4.15 presents the properties, dimensions of MORE and LESS reliance and illustrative quotations for this category. The concept indicators are also indicated.

Table 4.15: Overseeing reliance

MORE reliance		LESS reliance	
Illustrative quotations	**Dimensions**	**Dimensions**	**Illustrative quotations**
Property 1: Audit committee oversight of assurance effectiveness and efficiency Concept indicators: Data incidents: contrasting how, when and why audit committee oversight of assurance effectiveness and efficiency influences reliance			
Compared to ten years ago, the audit committee 'now take their role very seriously and audit committee meetings are robust and there is a lot of discussions about things that are happening and they are concerned about' (CAE B).	Overseeing implementation of a formalised combined approach to assurance as a means of synchronising stakeholder groups' assurance needs and responsibilities and achieving assurance effectiveness, including minimising assurance gaps and improved coverage Balancing the influence of managements' general focus on profit margins on having: - Strong internal financial controls - A strong internal audit function, including by approving the internal audit budget - A competent independent chief audit executive Balancing management's influence on the relevance of internal audit work, including by approving changes to the scope and focus of internal audit's mandate and plans which threaten internal audit's risk-based focus, for example, *ad hoc* work for management Balancing management's influence on the credibility of internal audit work, including by evaluating the competence	Some audit committee members have a different mindset about reliance; they are tokens who support management in applying pressure to increase reliance on external auditors, ignoring the influence of reliance on external audit quality and the distinct roles of internal and external audit	'The people that sit on the audit committee really are just tokens that have been appointed' (EP D1). 'What if management, who do not necessarily see the internal auditors as playing a very specific function, might be tempted to see [internal audit] as, extra bodies, or for *ad hoc* tasks. Now if that's the attitude of management … the audit committee … would ask [questions] … if management is constantly interfering [with internal audit's role] if [the audit committee] is sufficiently close to the business' (CAC A).

	of the internal audit team annually, giving the chief audit executive direct access to the audit committee, reviewing the outcomes of external assessments of internal audit quality and monitoring whether internal auditors meets their plans Although it exert a degree of pressure on external auditors to increase reliance, it balances management's pressure to increase reliance for efficiency purposes against the effect of reliance on external audit quality and the external auditor's liability Being reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance		
Property 2: The audit committee's inherent strength and closeness to the business Concept indicators: Data incidents contrasting how, when and why the audit committee's inherent strength and closeness to the business reflected in its profile influence reliance			
'A balancing act' (CAC D). 'In a big listed company it's easy for the chairman of the audit committee to remind management, which we do on many occasions, why it is that you do need an external auditor, why it is that you do need a top external auditor, and why you have to pay for that, and then equally so, why you want an internal audit' CAC C / E). Oversight 'has a lot to do with the skill of the audit committee so if you have an audit committee with the appropriate skills, then	A strong audit committee: - Shares members with the risk committee or engages in joint meetings with internal audit and risk management prior to quarterly audit committee meetings about risks and controls - Knows and understands the trustworthiness of the management of organisation - Has the support of the strong head of internal audit	A weak audit committee: - Finds it difficult to gain closeness to the business - Receives 'data dumps' in internal audit reports - Feels that management view 'healthy tension' (as part of audit committee oversight) as 'interference' - When it requests clarifications, it is labelled as an activist audit committee by management who	The audit committee 'support management'. (CAE C). Asked about the audit committee's active oversight of internal audit, CAC A responded: 'That's not always possible, because management will see that as interference … as an activist audit committee. But, they don't understand the liabilities and responsibilities that not only the Companies Act, but the Banks Act and the Stock Exchange for a listed bank … that the actual role [of the audit committee] is

they can play a significant role in the assurance … [they should] … understand …the real business …the industry … that is integral especially where there is significant operating risk and it's a very complex environment … also understand … the financial side of things as well … So I think it's important that whatever the significant risks of the business are, that there are people on the audit committee that understand those risks and can ask the right questions of management, as well as internal audit and external audit (EP B).	- Asks the right questions of management, internal and external audit - Engages in 'focused conversation' during robust audit committee meetings where there is extensive discussion of areas of concern, for example, as highlighted in internal audit reports - Is empowered by: o A 'business sense' o Knowledge of governance requirements o A mix of appropriate financial and operational training and experience o A strong risk view grounded in business, financial and industry insights o An uncompromising emphasis on sound governance o Strong upfront succession-planning of audit committee members o Is updated on the state of risks and controls and questions to raise with management by internal audit by way of: ▪ Internal audit reports containing detail about risk and control problems, their impact and who should take responsibility for addressing them ▪ Sharing documentation 'packs' and whether	misunderstand the stakeholder groups' assurance needs, risks and responsibilities	defined, and fairly harsh responsibilities and tasks are laid upon the audit committee.'

	management is taking findings seriously ▪ 'Closed sessions' with internal audit without management present		

***Source**: Own compilation*

4.6 CONCLUSION

This chapter provided an audit trail of coding and data analysis in the three phases of this study. In phase 1, the process, the participants' main concerns about reliance emerged and the core category was chosen from the nine initial substantive categories developed from the open codes. The core category is the outcome from phase 1. In phase 2, the core category focused selective and theoretical coding, refitting and saturating the initial substantive categories into six substantive categories and five sub-categories with the properties and dimensions of each category. The outcome of phase 2 is presented in Chapter 5. In phase 3, theoretical sorting delimited the saturated substantive categories into theoretical constructs of the emergent theory. The theory is presented in Chapter 6.

Next, Chapter 5 presents a narrative description of the data supporting the saturated substantive categories.

CHAPTER 5

OUTCOME OF PHASE 2:
SUBSTANTIVE CATEGORIES

CHAPTER 5

OUTCOME OF PHASE 2: SUBSTANTIVE CATEGORIES

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5.1 INTRODUCTION

Chapter 4 provided an audit trail of coding and data analysis in the three phases of this study. It also presented the outcome of phase 1, namely the chosen core category.

This chapter presents the data of this study in the form of substantive categories and sub-categories, structured in accordance with the theoretical outline. Open coding and analysis of the key initial data sets delimited the initial substantive categories and the main concern, leading to the selection of the core category. Then, selective and theoretical coding and analysis of further data sets saturated the substantive categories. Theoretical sorting delimited the theoretical outline of the substantive categories.

The substantive categories are all interrelated to each other as well as to the core category. Stakeholders groups' main concern is disconnect between their reciprocal influences on reliance. The core category explaining most variation between stakeholder groups' patterns of behaviour is stakeholder groups' central desired outcome from reliance, namely, *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

This chapter provides a comprehensive account of the data about reliance in the five key cases. This includes the reciprocal influences on reliance by the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. Under each property of a substantive category and sub-category, conceptualisations of dimensions influencing MORE and LESS reliance are presented in *italics*. In the MORE reliance cases – B and E – the external auditors indicated reliance was not limited. In the LESS reliance cases – A, C, and D – external auditors indicated that reliance was limited. Tables that summarise the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations for each category and sub-category is presented in chapter 4 (Table 4.6 to 4.15).

The conceptualisations of dimensions influencing MORE and LESS reliance form the properties of the emergent theory's theoretical constructs. The comprehensive detail provided in this chapter has three purposes. First, it explicates the empirical grounding of conceptualisations. Second, it explicates the interrelationships between and among categories and properties. Third, it serves as support for the credibility of this study's findings. This chapter does not make any reference to literature other than when mentioned by participants. The theoretical context of the emergent theory is presented in Chapter 6. Conceptual dimensions from this chapter are used to define and integrate the constructs of the emergent theory in Chapter 6.

5.2 SUBSTANTIVE CATEGORIES

This section presents the substantive categories and sub-categories related to the core category of this study, derived from interview data. The theoretical ordering of coded data revealed six categories and five sub-categories (Table 4.4). These categories explain how stakeholder groups' *mutual agreement that reliance was appropriate and fair (balanced), whatever the reliance decision* was viable and practicable. The six categories were (a) communication (5.2.1), (b) stakeholder groups' roles, interpretations, interests and practices influencing reliance (5.2.2), (c) working mindset (5.2.3), (d) integration (5.2.4), (e) alignment (5.2.5) and (f) oversight (5.2.6).

The five sub-categories related to the second substantive category are (i) stakeholder groups' assurance needs and responsibilities (5.2.2.1), (ii) the reliance environment (5.2.2.2), (iii) the relevance (5.2.2.3) and (iv) the credibility of internal audit work for statutory audit purposes (5.2.2.4) and (v) external audit quality and the external auditor's liability (5.2.2.5). Sub-headings denote the properties of each category and sub-category.

For each property, dimensions influencing MORE or LESS reliance are conceptualised and interrelationships between and among properties and categories are explicated. The latter conceptualisations are empirically grounded in the participants' constructions of their own and other stakeholder groups' reciprocal influences on reliance, considering their roles, interpretations, interests and practices. The conceptualised dimensions of each property are indicated in *italics* and illustrated by quotations from the interviews (De Vos *et al*., 2011:427).

5.2.1 Communication

Communication had a pervasive influence on reliance, as it provided the context sustaining all other influences on reliance. Communication occurred at two levels. At an overall level (5.2.1.1), the focus was on stakeholder groups' communication about planned and achieved reliance. At a more detailed level (5.2.1.2), the focus was on communication between internal and external auditors to coordinate work. The dimensions of the broader characteristics and the prevailing mood of communications influencing MORE and LESS reliance were included under this substantive category. The nature, objectives and content of interactions / communications were included under the substantive categories influenced by the communication. Table 4.6 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this category.

5.2.1.1 Stakeholder groups' communication about planned and achieved reliance

Participants from MORE and LESS reliance cases mentioned that management and the audit committee regularly interacted with external auditors about planned and practised reliance (EP A1, A2, B, C, D1, D2, E1, E2; CAE C, D; CFO C, D; CAC A). During interactions, management and audit committees usually sought information about internal and external auditors' alignment planning procedures to determine whether assurance effectiveness and efficiency was achieved.

In MORE reliance cases, management, the audit committee and internal and external auditors engaged in *extensive open discussions about planned and achieved reliance* included in internal and external audit plans (EP B; CAE B). Discussions usually *focused on assurance effectiveness and efficiency, yet all stakeholder groups favoured effectiveness over efficiency*. At every audit committee meeting where audit plans were tabled, external auditors had to 'justify' (EP E2) why they did not rely in certain areas. Internal audit plans tabled had to contain 'ticks' (EP E1) indicating reliance work. However, EP 1 interpreted that *management and the audit committee were reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance*. EP E1 commented that 'generally people [management] are pretty reasonable and accept that we [external audit] know what we are talking about when we say whether we can or can't place reliance on a piece of [internal audit] work'*.*

*In LES*S reliance cases, EPs reiterated that *management's and some audit committee's primary focus was on audit efficiency* (EP C, D1). *EPs conveyed that interactions with management and the audit committee about planned and achieved reliance were 'difficult' (EP A2), consisting of 'interrogation', 'questioning' and 'challenge' (EP A1, D2) by management and some audit committees, who expected that external auditors should provide detail about and action plans (CFO D) for improving assurance efficiency, and 'justify objectively' (CAE D) why they practised no or limited reliance.*

Participants from LESS reliance cases provided extensive detail about the characteristics and mood of stakeholder groups' communication about planned and achieved reliance. EPs explained that management's and the audit committee's questioning sought 'confirmation and comfort' that internal and external auditors engaged in 'mandatory' alignment planning. This was to ensure that their 'seamless effort' minimised unnecessary duplication of audit work (EP D2). EP A1 maintained that management and the audit committee challenged him when he did not meet their expectations of feasible ways of using the direct assistance work of the internal auditors. EP D2 found questioning was particularly intense when management incurred costs for improving the effectiveness of internal financial controls, which external auditors had previously cited as reasons for performing extensive substantive procedures and practising no or limited reliance (EP D2). EP D2 suggested management's and the audit committee's impression of internal and external auditors become negative when no or limited reliance occurred.

CFO C and D from LESS reliance cases confirmed management's and some audit committees' primary focus was on assurance efficiency during communication about planned and achieved reliance with external auditors. This was because management 'always try and reduce audit fees and [expect that internal and external audit should] be more efficient' (CFO D). CFO C and D expected detailed discussion on reliance work included in the audit fee breakdown, and required action plans for changing the external audit approach from extensive substantive procedures to more controls assurance work (tests of controls). CAE D strongly supported managements' focus on assurance efficiency; he called on external auditors to 'justify objectively' when they practised no or limited reliance.

In LESS reliance cases, the external auditors' response to difficult communication about planned and achieved reliance was *diplomacy* when sharing the reasons for no or limited reliance with management, internal audit and the audit committee (EP A2). EPs provided *very limited generic written feedback and some informal verbal feedback about the outcome of the ISA 610 assessment and the reasons for no or limited reliance in their attempt to preserve the relationship between internal and external auditors* (CAC B; EP A2, B, C, D2, E1, E2).

Motivating external auditors' limited and cautious interactions with management and the audit committee about planned and practised reliance in LESS reliance cases, EP A2, who repeatedly described interactions with management, the audit committee and internal auditors about the reasons for no or limited reliance as 'difficult', reported that sharing those reasons created 'a little bit of animosity' between internal and external auditors. EP A2 explained that when management appointed a very strong head of internal audit, motivating no or limited reliance was 'a difficult road to navigate'. EP A2 found that it was difficult to be 'open and honest' with internal auditors and management about shortcomings as to the credibility of internal audit work while 'manage[ing]' the good relationship between internal and external auditors. By way of example, EP A2 recalled instances when, in previous years, internal auditors' reliance work was of a lower quality than initially anticipated due to a skills gap in the internal audit team. In those instances, where external audit had to redo work initially earmarked for reliance, EP A2 conveyed that 'how you [external audit] share that message in the organisation is difficult'.

Due to LESS reliance case EPs' limited communication about the reasons for no or limited reliance, *management and internal auditors were often frustrated as they struggled to make sense of no or limited reliance practised by external auditors* (CFO C, D; CAE C, D; CAC A, D). CFO A noted that *a tick-box approach prevailed during reliance communication*, where 'everyone comes there [to the combined assurance meeting] and say[s], we've done the forum and tick done', without truly interacting about stakeholder groups' assurance needs and responsibilities.

5.2.1.2 Communication between internal and external auditors to coordinate work

Internal and external auditors explained that communication between them for coordinating work had a pervasive influence on reliance. From a MORE reliance perspective, EP E1 observed that communication between internal and external auditors had ‘always been good’, and indeed, it was even improving (EP E1; CAC B, C / E; CAE B). As in MORE reliance cases, participants from LESS reliance cases (EP A1, A2, C, D2; CAE A, D) perceived that the quality of communication between internal and external auditors had improved; the participants’ explanations thus revealed significant improvements. Examples included that communication between internal and external auditors had ‘absolutely’ improved (EP A2); ‘the level of collaboration has increased, I think, tenfold …, talking to each other’ (EP C); ‘so communication, collaboration, I would say it’s improved four hundred percent in the last two or three years’ (CAE A); ‘I think the level of engagement has been there in the past, but you’re finding a lot more engagement presently’ (EP D2); and ‘significant’ improvement in the eighteen months prior to the interview (mid-2014) (CAE D). Thus, from a LESS reliance perspective, CAE A and D claimed that the improving quality of communication between internal and external auditors was ‘definitely’ contributing to greater reliance in their companies.

In MORE reliance cases, communication between internal and external auditors was unrestricted as ‘we have that opportunity to call each other on any matter or basis’ as part of working closely together (EP E1). Communication became more *open* and *informal*, incorporating telephone consultations between internal and external auditors (CAC B; EP E2, as well as CAE A, C, D from LESS reliance cases). The participants explained that MORE reliance required more *frequent* communication between internal and external auditors. CAE B remarked that ‘the more they [external audit] rely on us [internal audit], the more interventions there [are]’. Participants from all cases mentioned communication between internal and external auditors occurred regularly or had become more *regular*. EP E1 observed that ‘over time the communication between ourselves and internal audit has probably become more structured in the sense that we *meet more regularly throughout the year*’. Participants described that communication between internal and external auditors occurred ‘more often’ (EP A1), as ‘we [internal and external auditors] talk all the time’ (CAE A) and meet ‘very, very regularly' (EP E1). CAE E reported that he met with the external auditors 'more … towards the latter part of the year, but we do meet regularly … we [also] meet at the planning phase'. CAE B and C observed they met with external audit at least every three months. CAC B corroborated that internal and external auditors met 'every quarter'.

From a LESS reliance perspective, CAE C experienced the improving quality of the relationship between internal and external auditors had changed communication between them from being *'forced*' to '*easier*' and '*informal*'. Consequently, CAE C had 'the *confidence* to call up the [external audit] partner' when needed. EP D2 predicted the quality of communication between internal and external auditors would improve in future with commensurate benefits, like improved assurance coverage. However, EP A2 qualified this improvement for the purposes of reliance was 'dependent' on the competence of the internal audit team.

Communication between outsourced compared to in-house internal auditors and external auditors differed. Differentiation between reliance on outsourced compared to in-house internal auditors was prevalent in LESS reliance cases only. EP A1 expressed that *external auditors could 'automatically' rely on work of outsourced internal auditors from Big 4 accounting firms*, indicating he had no doubt about the credibility of the work from those providers. EP A1 added that communication between internal and external auditors facilitated reliance on the work of outsourced internal audit service providers. He further indicated reliance was *'immediately'* initiated by a *reliance 'request' from the newly appointed outsourced partner to the external auditor*, requesting the latter 'to try and rely on the [outsourced provider's] work'. Then, '*lots of discussions' 'upfront'* followed *to clarify the auditors' mutual 'expectations'*, 'what they're going to be looking at, what they're not going to be looking at, what we [external audit] need them to look at, [and] what management wants them to look at' (EP A1).

Participants highlighted a strong interactive effect on MORE reliance from the quality of communication between internal and external auditors to coordinate work and their working mindset. This included internal and external auditors' propensity for working closely together and the quality of the relationship between internal and external auditors. While CAE E maintained he initiated improved communication between internal and external auditors, EP E2 opined that external auditors were initiating communication with internal auditors to meet management's and audit committees' expectations on increasing reliance.

Participants from MORE and LESS reliance cases maintained that reliance required *mutual knowledge sharing on areas of concern* as part of communication between internal and external auditors. EP D2 explained that 'a lot more sharing of knowledge between the parties [internal and external audit]' occurred as part of reliance efforts. Examples of information shared include each stakeholder groups' 'areas of concern' (CAE B), 'issues that crop up' (CAC B), 'any matter or basis' (EP E1), 'important information' (CAE C) and 'knowledge' (EP D2).

CAE A and CFO A indicated that practising reliance as part of a combined approach to assurance benefitted from internal and external auditors *reflecting on lessons learned and ways to improve assurance effectiveness and efficiency*. CAE A explained that reflection meant the 'external audit team [and] internal audit team [were] just sitting on a quarterly basis and sharing lessons'. CFO A opined that reflection provided the opportunity to internal and external auditors to periodically 'look back' at instances where assurance efficiency was not optimal due to duplication of audit work, while it also highlighted opportunities for improvements 'going forward'.

In conclusion, dimensions describing the quality of reliance and its outcomes (as derived from stakeholder groups' communication about planned and achieved reliance and communication between internal and external auditors to coordinate work), pervasively sustained stakeholder groups' perceptions of the appropriateness and fairness of MORE compared to LESS reliance.

5.2.2 Stakeholder groups' roles, interpretations, interests and practices influencing reliance

Stakeholder groups' roles, interpretations, interests and practices were foundational conditions influencing reliance. These conditions were represented in five sub-categories, namely, (a) stakeholder group's assurance needs and responsibilities (5.2.2.1), (b) the reliance environment (5.2.2.2), (c) the relevance and (5.2.2.3), (d) credibility of internal audit work for statutory audit purposes (5.2.2.4) and (e) external audit quality and the external auditor's liability (5.2.2.5). The quality of communication during all stakeholder groups' interactions about planned and practised reliance as well as oversight by the audit committee pervasively determined these influences on MORE or LESS reliance.

5.2.2.1 Stakeholder groups' assurance needs and responsibilities

The roles, interpretations, interests and practices of the stakeholder groups influencing the statutory financial reporting and external audit processes forms the context of their influences on reliance.

Three properties linked to stakeholder groups' assurance needs and responsibilities influenced reliance, namely, (a) assurance meetings, (b) the distinct roles of internal and external audit and (c) pressure to increase reliance. Table 4.7 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this sub-category.

(a) Assurance meetings

The participants indicated that holding 'annual' (EP A1 and B, CAE A), 'collective' (CAE A) assurance meetings as part of a combined approach to assurance influenced reliance. Participants used different terms when referring to assurance meetings, notably, 'vigorous discussion sessions' (CAE C), 'audit planning workshops' (CAE A), 'combined assurance forum[s]' (CFO A) and 'planning meetings' EP B. Some participants held assurance meetings **'**once a quarter' (CFO A) while others had 'quite a few' (EP B). CAE A was 'proud' to mention he, representing internal audit, 'spearheaded' and chaired assurance meetings in the form of a 'combined assurance forum'.

Several participants provided insights about participation in and the format, mood, purpose and outcomes of the assurance meetings. Descriptive snippets from the data include: 'all sitting in the room' (CAE A), 'sitting around the table' (CFO A), where 'we would talk about issues' (EP A1), as part of 'constant collaboration, conversations and discussions, and then management' of the assurance process (EP A2), ensuring each stakeholder group ended up 'having a good understanding and acceptance of [their] role in the process … in a combined programme' (EP A2). Thus, by 'partnering' (CFO A), 'we really look at the full spectrum of assurance that's given' (EP B), and 'we've driven the level of reliance and openness and sharing in the organisation' up (CAE A). Participants at assurance meetings included management (CAE A, C; EP A2, B; CAC A; CFO A), internal auditors (CAE A, C; EP A2; CFO A), external auditors (CAE A, C; EP A2, B; CFO A), risk management officers (CAE A, C; EP A2, B), compliance officers (CAE A, C) and 'IT people' (CAE A).

Participants elaborated on ideal participation in assurance meetings supporting MORE reliance. CFO A spelled out that *combined assurance meetings* should be characterised by *triangular participation by management and internal and external auditors*, forming a 'a nice complete triangle'. He clarified that management included 'financial [management], … the risk managers and senior managers'. Likewise, EP A2 (as well as CAE B and CAC C / E) emphasised 'combined assurance needs active involvement from management', particularly from a risk management perspective.

Participants maintained that triangular participation by management and internal and external auditors in combined assurance meetings was a platform for *synchronising stakeholder groups' assurance needs and responsibilities* (EP A1, A2; CFO A), based on the 'three lines of defence' principle (CFO A, E). Synchronisation was captured in a combined assurance 'mapping' (CAC D). Such synchronisation arose from 'greater coordination and alignment of thinking' about 'critical issues' 'using the collective and combined understanding of the business' of management, internal and external auditors (EP A2). Thus, the main agenda points covered during combined assurance meetings were 'key risks throughout the organisation' (CAE D), 'concerns' and 'problematic areas' (EP A1) and 'the key pressure points in the business' (CFO A). CAE A and D explained that combined assurance meetings were the ideal means for agreeing on key risks and each groups' related assurance needs and responsibilities. This would then ensure that 'all three lines [of defence] work[ed] in sync with each other' (CAE A).

Synchronising stakeholder groups' assurance needs and responsibilities ensured that management, internal and external auditors were 'working in sync with each other' (CAE A) on 'practical and pragmatic' assurance 'deliverables' (EP A2) centred on clear, *shared goals* (CFO E) and *an integrated risk and assurance view* (EP A2). Thus, internal and external audit's risk-based audits focused on the 'right areas', including management's self-disclosed risks (CAE A). This was because synchronisation enabled 'the best and most efficient assurance' (EP B) by minimising unnecessary duplication of audit work (EP A1) and reducing assurance gaps (CAE B).

From a LESS reliance perspective, participants reflected on management's 'slow uptake' of triangular participation in combined assurance meetings, as CAE A and EP A2 conveyed that management's participation often only became a reality following a 'serious control breakdown', which could have been prevented by awareness, through management's participation in combined assurance meetings. CFO A acknowledged management's involvement in combined assurance meetings added value to every component of the business as well as every participant in the business. This was because it improved the maturity of risk management and the effectiveness of internal financial controls. CAE A also commented that combined assurance meetings could highlight control 'inefficiencies', thus allowing management to improve the effectiveness of internal financial controls. To demonstrate case A management's commitment to operational managers' participation in combined assurance meetings, CAE A mentioned that executive management required feedback about the level of participation and understanding of risks displayed by operational managers during combined assurance meetings.

From a LESS reliance case perspective, CFO C indicated *misunderstanding of each group's assurance needs and responsibilities* as *management met separately with internal and external auditors about assurance plans*. CFO C bemoaned '[t]he sad part' that it 'never crossed [his] mind to actually bring these two [internal and external auditors] together'. CFO C planned to include the company's chief audit executive in future discussions with external auditors about audit plans. From a LESS reliance perspective, EP C explained that he had prepared and used a combined assurance mapping to rationalise no or limited reliance. EP C maintained that 'schematically showing' management and the audit committee the distinct roles of internal and external audit attenuated management and audit committee pressure to increase reliance on external audit. This is because it clarified the overlap between internal and external audit work.

(b) *The distinct roles of internal and external audit*

According to the participants, stakeholder groups' assurance needs and responsibilities encompassed an understanding of the distinct roles of internal and external audit (EP A1, B, C, E1; CAC C / E; CAE E; CAC D). External auditors regarded such an understanding as a foundational condition influencing reliance.

From a MORE reliance perspective, CAC C / E indicated that *stakeholder groups mutual understanding of internal and external audit's interrelated distinct roles implied that neither internal nor external audit could substitute each other's role*. CAC C / E explained that 'the fact that you've got that [internal audit] just makes their [external audit's] job a little bit different, but it doesn't take away what they [external audit] have to do'.

From a LESS reliance perspective, EP A1 and C observed *management's and some audit committees'* reliance interpretations and practices often disregarded the distinct roles of internal and external audit. This is because they *perceived, through reliance, that internal audit should reduce external audit work and fees*. Like CAC C / E and EP E2, EP E1 claimed that 'sometimes audit committees … feel that internal audit is there to do some work of external audit, which is not the case'. CFO C confirmed that the latter observation was correct. He indicated that 'I would either optimise my internal audit department or optimise my external audit department to get to the right … level of control'.

EP C summed up that 'a disconnect between definitions' meant stakeholder groups misconstrued the distinct roles of internal and external audit. He added that audit committees expected 'synergy' between internal and external audit due to assurance efficiency concerns, yet practising appropriate reliance was 'extremely difficult' due to some stakeholder groups misunderstanding the distinct roles of internal and external audit. EP C clarified that these distinct roles meant that 'internal audit focus on operational efficiency aspects where we [external audit] focus on misstatement of numbers'. EP C advised that 'we must educate the powers at the top [management and the audit committee] to understand who's doing what' in terms of assurance.

(c) Pressure to increase reliance

EP and non-EP participants, particularly from LESS reliance cases, acknowledged that *management's and some audit committees'* concerns over assurance efficiency, coupled with their lack of understanding of the distinct roles of internal and external audit, were causing them to *exert pressure on external auditors to increase reliance* (EP A1, A2, C, D1, E1; CAE A, C, D; CFO C). EP A1, A2, C and D noted that this pressure was increasing and believed it would continue to do so in the future. CAE C and EP A1 ascribed the pressure to King III's emphasis on a combined approach to assurance. Furthermore, CAC A explained that management and audit committees interpreted ISA 610 as 'implying' that reliance 'had to happen'.

From a LESS reliance case perspective, CAC D expressed 'fear' that 'if management had its way, it would probably drive external audit to using the work of internal audit to quite a large extent'. Thus, CAC A, C / E and D emphasised the importance of audit committee oversight of assurance effectiveness and efficiency. Highlighting the perception of management and some audit committees that reliance should reduce external audit work and fees, CFO C indicated that he planned on playing a more proactive role in reliance decisions in the future by holding quarterly meetings with the external audit engagement partner to track reliance.

Again from a LESS reliance perspective, EP D2 associated the pressure to increase reliance with costs incurred by management to improve the effectiveness of internal financial controls. EP D2 cited this as a source of comfort supporting management's and the audit committees' reporting roles. According to EP D2, *management expected that large investments in internal financial controls would translate into greater reliance as external auditors changed from extensive substantive procedures to a combined approach focused on controls assurance work.* However, CAE E pointed out that external audit fees did not necessarily drop when external audit changed to controls assurance work, as the latter work required more expensive external audit resources.

Confirming that the 'fears' about pressure to increase reliance were warranted, LESS reliance case EPs (EP A1, E2) conveyed that *management's pressure to increase reliance was often inappropriate*, for example when 'management [were] not serious about it [internal audit]' (EP D1). Confirming the latter, CAE D acknowledged the existence of a skills gap in the internal audit team of case D. However, he opined that this did not justify external auditors ‘dispensing’ with internal audit work when making reliance decisions.

EP participants from LESS reliance cases indicated *appropriate reliance is extremely difficult to achieve and therefore, they practised no or limited reliance, despite pressure* to the contrary. EP D1, who was open about the fact ‘audit firms … try to resist [reliance] as much as they can’, explained that his firm responded to pressure by *attempting to increase reliance on an* ad hoc *basis only on those audit clients exerting pressure*. EP D1 added that his firm was investigating ways of improving assurance efficiency, including a ‘move towards’ reliance. CAE D justified pressure to increase reliance on external auditors was limited to areas where he, as CAE, considered reliance achievable.

From a MORE reliance perspective, CFO B and E declared that *the focus of all stakeholder groups’ (including management’s and the audit committee’s) was on balancing assurance effectiveness and efficiency, yet always favouring effectiveness over efficiency*. CFO E asserted that ‘our [management’s] requirement is just that the external auditor does a good job and is completely independent and they must be efficient as well ... if they [external audit] provide good service, we’re not going to force them to cut fees … it doesn’t pay us and the audit committee wouldn’t welcome that at all’. CAC B concurred with CFO E, stating that ‘I think they [management] would leave it up to the external auditors. They would want to know that … [internal and external audit] are working together and they are, we know that … but I don’t think [management] actually impose on the external auditor in terms of the extent of the [internal audit] work [external audit] use’.

EP E1 clarified that management’s improved understanding of internal and external audit’s interrelated yet distinct roles reduced management’s and the audit committee’s pressure to increase reliance on external auditors. EP E1 emphasised that management ‘are coming to understand that what internal audit does and the assurance that they give is not going to overwrite … the assurance external audit needs to give’. EP E2, like all the other EP participants, ascribed management’s improving understanding to triangular participation in combined assurance meetings by management, internal auditors and external auditors. EP C noted that the external audit team had initiated combined assurance meetings and provided training to internal auditors on this topic in response to management's 'pressure' to increase reliance. EP C added that a combined assurance mapping gave management and the audit committee a 'tangible' view to facilitate their understanding of internal and external audit's interrelated yet distinct roles. EP C expected that internal audit would gradually take over control of the combined assurance process in future as they were 'catching up'. All EP participants acknowledged that a combined approach to assurance mitigated pressure to increase reliance.

Interestingly, CAE D believed that CFOs and CAEs (who were chartered accountants) had grasped reliance possibilities better than others. However, it should be noted that all CAEs of the LESS reliance cases (A, C and D) were chartered accountants, while the CAE E from the MORE reliance case (E) was not. Furthermore, CFO A (LESS reliance case) and CFO E (MORE reliance case) were previously the external audit engagement partners of the cases. Thus, it seems having a CFO and / or a CAE with a thorough understanding of internal and external audit's interrelated distinct roles did not necessarily temper pressure to increase reliance and / or induce MORE reliance.

In conclusion, the synchronisation of stakeholder groups' assurance needs and responsibilities was a foundational condition which determined their interpretations of the appropriateness and fairness of MORE compared to LESS reliance.

5.2.2.2 The reliance environment

The properties of the reliance environment were (a) the size and regulation of the organisation as well as management's influence on (b) the maturity of risk management, (c) the effectiveness of internal financial controls, (d) the structure of the internal audit function, (e) internal audit budget / capacity / resourcing, (f) the status of and value-added internal audit, and (g) the profile and role of the chief audit executive. Table 4.8 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this sub-category.

(a) Size and regulation of the organisation

EP participants reported that MORE reliance occurred in *larger organisations and well regulated-organisations* as they associated these kinds of organisations with *a strong audit committee* (CAC C / E), *a strong risk management function* (EP A2), *a strong internal audit function* (EP A2, B) and *a more effective combined approach to assurance* (EP A2). In addition, external auditors claimed that management and the audit committees of larger, well-regulated organisations had *a better understanding of the distinct roles of internal and external audit and the ideal scope and focus of internal audit mandates and plans* compared to those from smaller or less well-regulated organisations (EP D1). Thus, in larger organisations, *management and audit committees usually ensured realistic resourcing, in line with internal audit's mandate and plans* (EP B).

EP B explained that *the use of internal audit was less formalised* in smaller, less well-regulated organisations, where *the value added by internal audit was usually only recognised in response to control failures*. In contrast, CAE B (2019) maintained that in the financial sector *(*comprising *well-regulated organisations), internal audit's role as provider of assurance on combined assurance had become more formalised and regulated*. Moreover, in larger, more well-regulated organisations, the past prevalence of *management having a general focus on profit margins* (CAC C / E) changed, as now *management realised that they should balance profitability and good governance* (CAE B (2019)). CAE B (2019) asserted that 'management is not just driving profit and growth, they're not just driving numbers anymore. They have realised … with this whole set of regulations … their responsibility is actually to govern this environment'.

From an assurance efficiency perspective, EP B perceived that reliance was 'always' beneficial in the 'majority' of larger organisations where *the benefit from assessing internal audit and its work usually exceeded the cost*. On the other hand, in smaller organisations, *the fixed cost of assessing internal audit and its work exceeded the audit fee saving*. Yet CAE B specified that *reliance mostly occurred in smaller components (subsidiaries) of larger organisations where a combined approach to assurance was present*. CAE B stressed that the aim of reliance was to reduce external audit work and fees for the component. In 2019, CAE B explained that reliance was 'more challenging' at 'group level' were the scope and focus of internal audit's mandate required a holistic governance approach, focused on the control environment and significant risk of judgmental manipulation driven by management culture. CAE B mentioned that reliance was easier at subsidiary level, where *internal audit could follow a transactional end-to-end integrated business process approach*. This was also suggested by EP E1.

(b) The maturity of risk management

EP A2, D2 and CAE B (2019) highlighted that *a strong risk management function with senior management collaboration* was a foundational condition for an effective, combined approach to assurance and hence reliance. CFO A and CAE A explained that the maturity of risk management benefitted from triangular participation by management and internal and external auditors in combined assurance meetings, as these meetings provided a platform to foster stakeholder groups' integrated risk and assurance views. EP D2 opined that when *a weaker risk management function* was present, contemplating reliance was senseless.

From a MORE reliance perspective, CAE B confirmed the presence of a strong risk management function with senior management collaboration, supported by an effective combined assurance approach to assurance. From a LESS reliance perspective, CFO C and CAE C (2019) indicated that the company's *risk management function was not functioning optimally*, while CAE C (2019) confirmed that the combined approach to assurance was under-developed.

(c) The effectiveness of internal financial controls

CFO A explained that practicing reliance depended on the effectiveness of the organisation's internal financial controls. He asserted that MORE reliance was possible when *strong internal financial controls were 'effective and operating for the entire financial period'* whereas LESS reliance was possible when *weak internal financial controls were 'not operating fully'*. EP D2 perceived management's increased need for comfort and assurance generally resulted in greater management and internal audit focus on the effectiveness of internal financial controls of companies. EP D2 added that since companies were spending large amounts on improving the effectiveness of internal financial controls, management believed that external auditors would increase reliance, even exerting pressure to increase reliance on external auditors. This was done in the expectation that the external audit approach should change to controls assurance work instead of extensive substantive procedures.

(d) The structure of the internal audit function

From a MORE reliance perspective, EP E2 declared that he *preferred relying on work of a strong in-house internal audit function as such functions had a superior understanding of the business, including its key risks,* rather than outsourced internal auditors who lacked such an understanding. CFO A and EP A2 explained that organisations benefitted when using an in-house / co-sourced combination internal audit function rather than a fully outsourced internal audit function. This was because in-house internal auditors' superior understanding of the business, including its key risks, surpassed that of their outsourced counterparts. It therefore ensured relevant, risk-based audits. However, EP A2 and C pointed out that the competence of the internal audit team of an in-house internal audit function required careful consideration when practising reliance, as the absence of the international support commonly available to Big 4 accounting firms' audit teams could imply that a skills gap in the internal audit team existed.

In contrast, several EP participants from LESS reliance cases (EP A1, C, D1) *favoured reliance on outsourced internal audit work, particularly when the outsourced partner was a peer from a Big 4 firm*. They believed that staff from Big 4 firms providing outsourced internal audit services were *more competent and 'independent'* (EP A1, C) than in-house internal auditors. In particular, they perceived that outsourced providers of internal audit services had more 'specialised' (EP C) skills, as their teams often included individuals with 'acknowledged skill' in specific areas (EP A1). Consequently, these EPs (EP A1, C, D1) were less concerned about the credibility of internal audit work for statutory audit purposes of staff from Big 4 firms.

CFO A, C and E, as well as EP A2 asserted that the competence of the in-house internal audit team benefitted when they had the opportunity to develop and learn when working with the external audit team. The in-house team also benefitted when working on co-sourced internal audit projects with specialist internal auditors, mostly from Big 4 accounting firms. Similarly, attending training courses (CFO A) bridged the isolation of a completely in-house internal audit function, with limited associations with other internal auditors. CAE A and C mentioned that they had benefitted from active involvement in and benchmarking against the local and internal audit profession. CAE C and E conveyed that their Big 4 firms provided professional development and benchmarking opportunities to them in their roles as CAEs. This was corroborated by CAC C / E.

(e) Internal audit budget / capacity / resourcing

Participants from MORE and LESS reliance cases mentioned that reliance depended on *realistic resourcing, in line with internal audit's mandate and plans* as it determined *inter alia* the probability of internal audit meeting internal audit plans. Internal audit's mandate and plans would include planned reliance work. From a MORE reliance perspective, EP B explained that reliance benefitted when internal audit budget / capacity / resourcing made fulfilling a realistic mandate possible, in line with internal audit's realistic mandate and plans.

CAC D (from a LESS reliance perspective) associated internal audit's 'lack of maturity' with limited reliance occurring in case D. When probed, CAC D clarified that the 'maturity' of internal audit included 'a whole mixture of lack of skills, lack of resources, lack of capacity'. Thus, CAC D indicated that LESS reliance occurred when *internal audit's budget / capacity / resources were too limited to fulfil internal audit's mandate and plans*.

Several participants highlighted that internal audit budget / capacity / resourcing should be balanced against the scope and focus of internal audit's mandate and plans, yet doing so was 'always' (CAE B; EP B; CAC D) challenging. Considering the budget allocations to the internal audit functions of the MORE reliance cases, CAE E noted that it had increased 'significantly' over the last years. CAE B, on the other hand, proclaimed that 'it does increase, [but] not significantly'. CAE C (from a LESS reliance case) reported an increase in the size (number of internal audit staff) of the internal audit function of case C, as did CFO E and EP E1 for case E. However, when probed, CAE E explained that the increase in the internal audit budget allocation of case E was the result of a combination of an increase in controls assurance work performed by the internal audit function, as well as the growth and expansion of the organisation. EP A2 emphasised that the chief audit executive was responsible for managing the balance between internal audit budget / capacity / resourcing and the scope and focus of internal audit's mandate and plans. He recommended that using technology, including data analytics, could assist in balancing internal audit resourcing and work.

The participants mentioned two factors that influenced management's allocation to the internal audit budget / capacity / resourcing. First, management having a general focus on profit margins impacted the internal audit budget / capacity / resourcing. In this regard, CAC B highlighted the underlying dichotomy: although management understood the need to grow internal audit, they 'try and keep costs down'. Explaining the challenge brought about by this dichotomy, EP A2 indicated that determining the adequacy of the internal audit budget / capacity / resourcing 'depended [on] who you ask. If you ask the financial director [the response is] of course they're given enough money. If you ask the chief audit executive [the response is] it's never enough money … So where the right balance is on that, I'm not so sure'.

The second factor influencing management's allocation to the internal audit budget / capacity / resourcing depended on management's interpretations of the status of internal audit and the value it added. EP E2 and CAE A and C explained that when management viewed internal audit as a 'not so critical … support function' (EP E2), financial support for it may fluctuate as the economic climate improves or worsens (CAE C).

Participants motivated three determinants of the reasonableness of internal audit budget / capacity / resourcing. First, *the size and competence of the internal audit team in relation to the scope and focus of internal audit's mandate and plans* (CAE B, EP B) determined the reasonableness of the internal audit budget / capacity / resourcing. Since a 'standard' (CAE B) or 'benchmark' (EP A1) for determining the appropriate size of internal audit's staff did not exist, assessing the presence of realistic resourcing in line with internal audit's mandate was complicated.

Second, participants expressed concern that the expanding scope and focus of internal audit's mandate and plans, which was common in larger, regulated organisations, did not always consider internal audit budget / capacity / resourcing, and particularly the size of the internal audit team. Thus, despite the growth of the internal audit team, internal audit budget / capacity / resourcing could not ‘catch up’ with the expanding scope and focus of internal audit’s mandate and plans (CAE B). EP D2 commented that *ad hoc work for management, as part of conflicting demands on internal audit resources by too many bosses*, meant unmet internal audit plans were a regular occurrence. He thus advised the chief audit executive to carefully consider taking on such work.

Third, EP B mentioned that companies experienced difficulty attracting and retaining good internal auditors. EP B explained that the internal auditors in case B overcame internal audit budget / capacity / resourcing constraints by working very long hours. EP B and A2 opined that problems with the professionalism of internal auditors, particularly the poor image and limited career opportunities of this profession, meant that it was difficult to attract and retain competent internal auditors. This was because people were generally unwilling to remain in internal auditing. CAE A and B explained that the limited promotion and / or salary growth possibilities within internal audit functions created stiff competition in the market for acquiring scarce internal audit skills. Supporting these views, CAC D opined that internal auditing was not an attractive profession for people with specialised skills. EP A2 highlighted that larger internal audit teams typically consisted of mostly junior internal auditors and lacked managerial skills, compromising the standard of internal audit work.

The participants emphasised that audit committee oversight of internal audit budget / capacity / resourcing balanced the interests of management, internal audit and the audit committee (CAC B, C, D; CAE C). CAC B maintained that audit committee oversight compared internal audit budget / capacity / resourcing to the scope and focus of internal audit’s mandate and plans. Thus, ‘we [the audit committee] ask the question: Can we do what we have to do? And we look at who’s in the team and what they are doing … in terms of progressing with their qualifications and things’ (CAC B). Likewise, CAC A noted that ‘the first question… I ask, is not… whether… they’re [internal audit] spending too much money; I’m saying, are you spending enough?’ CAE A declared that ‘if I don’t have enough money, I’ll definitely shout.’ CAC D indicated that audit committee oversight was cognisant of the expanding scope and focus of internal audit’s mandate and that plans required growth rather than a reduction in internal audit budget / capacity / resourcing.

(f) Status of and value added by internal audit

Like most participants, EP B declared that the status of and value added by internal audit ‘definitely does contribute’ to reliance. This category contained the most data incidents – 113 quotations covering 44 pages. CAE C and EP D1 and E2 credited King III requirements and training provided to management and audit committee members improved their understanding of the value added by internal audit. This improvement led to improvements in internal audit budget / capacity / resourcing. Moreover, EP and CAC participants perceived that the status of and value added by internal audit was generally improving in light of their ‘critical role’ in a combined approach to assurance.

EP B mentioned that MORE reliance was possible when management believed that internal audit was ‘a trusted advisor and seen to add value within the organisation’. LESS reliance in organisations occurred where management believed that the internal audit function was ‘secondary’. EP B motivated that reliance was conditional on the status of and value added by internal audit as the latter determined internal audit’s continuous access to all levels of operating staff and management. Such access increased risk identification of internal audits’ risk-based audits. CAC D explained that internal audit was ‘discounted’ unless management and the audit committee underscored the status of internal audit and the value it added.

Several participants emphasised that the ‘tone’ determining the ‘respect’ for the status of internal audit and the value it added depended on *the CEO and management ‘open[ly]’ acknowledging and ‘support[ing]’ ‘the value of internal audit’ to the business* (EP A1, B, D2, E2). Once the relationship between internal audit and the CEO was strong, the value added by internal audit to the business increased. This was because management reacted more ‘swiftly’ to risks and recommendations contained in internal audit reports (EP B, D1, E2). CAE D stressed that he constantly engaged with the CEO and senior management about the role and contribution of internal audit. He also took the CEO through all internal audit reports, highlighting key findings of control weaknesses requiring corrective action.

Although EP A1 acknowledged that internal audit contributed to the maturity of risk management and the effectiveness of internal financial controls (as being ‘on-site’ made them part of the ‘control fibre’ of the organisation), he declared that most internal auditors did not function at the trusted advisor level, even in highly regulated organisations like those in the financial sector. EP B noted since the benefits of having internal audit were not always immediately observable by management as 'direct' cost savings, management's need for 'getting more comfort over controls' after a failure in internal controls was often what persuaded them of the value of internal audit reports.

CAC A and CFO B mentioned that management and the audit committee valued reliance as 'an external view' (CFO B) of the credibility of internal audit work. Thus, reliance contributed to the status of internal audit and the value it added in the eyes of management and the audit committee.

CAC C / E as well as EP D1 and D2 also linked the status of internal audit and its value to the quality of internal audit reports, observable in the way management responded to internal audit reports. Particularly, this was questionable when *management ignored internal audit findings and recommendations* (EP C, E1, E2) and were reluctant to use their own internal audit team for 'sensitive investigations' (CAC D).

CAC C / E explained that the seriousness with which management dealt with internal audit reports was reflected in a number of ways, namely, do internal audit reports 'go to the right level … who gets the report, what do they do with the report, what follow-up do they have, what do they do'. EP D1 concurred with the latter view and added that evidence of management's serious consideration of internal audit reports was reflected where management 'reviewed [internal audit] reports and [took] corrective action wherever necessary, dealing with the issues that came up from internal audit, appropriately'. In addition, EP D2 specified that management which took internal audit reports seriously, required corrective action by the operational management and linked operational managers' key performance indicators and bonus calculations with actions taken in response to internal audit findings.

Like CACs, CAE participants opined that the 'quality' (CAE B) of internal audit reports determined the status of internal audit and the value it added. CAE participants shared their insights about the type of internal audit findings and recommendations that management took seriously. CAE B mentioned that internal audit had to display their business 'insight' when verbally interacting with management and in the selection of matters that they included in their reports. CAE E considered that management took *internal audit reports* seriously if they *reflected findings and recommendations which were 'pragmatic… risk based…* and not textbook-based'.

CAE B explained that he realised that internal audit needed to 'start thinking differently' if they wanted to get away' from reporting '*the same recommendations every year*'. He realised that 'internal control problems' often occurred from 'a problem with structure, leadership, management, systems or some form of training'. This was not easy to fix with *simplistic,* 'easy, connecting the dots' recommendations. Thus, CAE B focused on building a closer 'relationship' with auditees in the business. The changed approach aided internal auditors' understanding of the *'real root causes of control problems'* instead of them making simplistic conclusions. CAE E asserted that management and business valued assistance from internal audit work and reports from risk-based audits. CAE D also analysed the root causes of control problems and reminded management when breakdowns resulted from internal audit findings which had been reported earlier but which had been ignored. The approaches of CAE B and E aligned with the expectations of CFO A, who valued internal audit's 'ideas' for addressing problems. He maintained that internal audit should, when they 'see something wrong, not just report on it, but actually give ideas'.

Various participants from each of the case companies described the status of internal audit and the value it added to their respective companies in mostly positive terms. However, in each of the case, participants conveyed an element of management doubt about the status of and value added by internal audit. EP D2 explained that this was a product of management's motivation for having an internal audit function, 'whether it's [internal audit] seen as a very viable and important part of the business or whether it's a nice to have and we have to have it, so therefore we have it'.

Doubt was greater in LESS reliance companies and lower in MORE reliance companies. For example, from a LESS reliance perspective, CFO C, whose general view of internal audit was less approving than that of CFO A and B, mentioned that **'**large companies have always had internal audit departments'. Yet, he argued, 'if King III was not around, I promise you there will be businesses that wouldn't have it'. CFO C jokingly added that sometimes internal audit was tolerated as a 'grudge cost', while CAE D perceived that '30% to 40% of the people' in case company D did not ‘see the value’ of internal audit. In comparison, in MORE reliance case B, CAE B opined that 80% of managers appreciated internal audit’s contribution to the business.

CAC D emphasised that internal audit budget / capacity / resourcing, the status and value of internal audit as well as the competence of the internal audit team all complemented each other. He maintained that the appreciation of management, the audit committee and external audit ‘for the things they [internal auditors] are doing and the things that they are saying [internal audit findings and reports]’ determined the ability to attract ‘the right sort of people’ into the internal audit function’. Likewise, EP D2 expressed internal audit’s ‘significance and its role in the organisation’ ‘dictates’ the internal audit budget / capacity / resourcing. EP B and E1 also emphasised the interrelatedness of the status of and value added by internal audit and its budget / capacity / resourcing, which stemmed from the CEO and management openly recognising the useful role of internal audit in the business. However, EP B suggested that management support for internal audit ‘requires a certain leap of faith in terms of the… budget… that they put towards it’.

The participants highlighted factors that influenced management’s judgements of the status and value of internal audit. The factors relate to (i) the scope and focus of internal audit’s mandate and plans, (ii) the competence of the internal audit team, (iii) the adequacy of internal audit budget / capacity / resourcing and (iv) the credibility of the chief audit executive. These are discussed in more detail. First, management linked the usefulness of internal audit to the scope and focus of internal audit’s mandate and plans. The participants also conveyed the specific type of internal audit work that adds value. EP A2 cautioned that ‘management try and take internal audits’ eye off their key value by saying, ‘well, you need to add value here, here, here, when, fundamentally, if you have a strong internal audit process, there is value in that’. Thus, EP A2 and CAE A (like CFO A, B, C, D, as well as CAE B, E) emphasised that the value added by internal audit to the business arose when they concentrated on the ‘basics’, namely controls assurance work as part of risk-based audits. Participants specified that internal audit’s controls assurance work should address operational processes and controls, including new strategic projects as well as internal financial controls and compliance with management’s policies and procedures.

While he acknowledged that the value of internal audit was showcased by controls assurance work, CFO C described how changing from routine conventional rotational internal audits to risk-based audits benefitted the status of internal audit and the value it added in case C. CFO C explained that previously, 'the general role of internal audit was really just to check internal controls, it was a function that management left on the side and only responded to… when there was something wrong'. The 'changed' risk-based 'role' meant internal audit played 'more of a value-added type role', with 'specialist' internal auditors providing 'value-added comments to the business' by identifying problems in the operational 'processes of the business and people… that management never picked up before' (CFO C). Thus, CFO C attributed the status of internal audit and the value it added to its reports, which focused on areas and risks that management also viewed as key and risky.

CAE A was conscious of potential misalignment of stakeholder groups' views about the type and extent of work associated with the value added by internal audit. Thus, CAE A used a 'memorandum of understanding' with internal audit clients for ensuring 'we [internal audit] know exactly what we need to do [as] there is a lot of upfront expectations' that the parties need to agree on. In addition, CAE A consciously used wording in internal audit reports 'to drill home' the importance of 'operational risk management'. This was in order to emphasise that the adequacy and design of organisational processes was not internal audit's responsibility.

Second, management linked the status of internal audit and the value it added to the competence of the internal audit team, which was displayed during interactions with management (CAE B and EP B). EP B and CAE B explained that the status of internal audit 'comes down to the quality of the people you put down in front of management', particularly their business insight. By way of example, in case E (MORE reliance), many internal auditors previously worked in the business, thus they had a sound understanding of the business. CAE A suggested that internal auditors should showcase their skills and the business 'intelligence' they had built up over the years. However, he pointed out that this was only possible if management gave internal auditors a 'seat at the table'. This was, in turn, earned through the perceived status and value of internal audit demonstrated to the business by internal auditors. From a LESS reliance case perspective, CAE D expressed concern about his internal audit teams' understanding of the business and mentioned that it hampered their ability to make appropriate recommendations and offer appropriate advice to the business.

CAE D was implementing training to improve his team's ability to 'sit down and provide good constructive advice [to management] when they [internal audit] did pick up control weaknesses or issues in the internal audit'.

In addition to internal auditors' business insight, CAE A stated that having 'confident' internal auditors who communicated well with management was key in shaping management's perceptions of the status of and value added by internal audit. CAE A used 'continuous assessment'; this included 'customer satisfaction surveys' completed by business unit managers after every audit and a 'bi-annual report card' for completion by non-executive and executive management. These documents conveyed auditees' views on the performance of the internal audit team. CAE A also recognised the importance of clear verbal and written communication when conveying internal audit findings to management as this affected management's perceptions of the value added by internal audit. Thus, CAE A changed the wording in internal audit reports from 'recommendations' to 'agreed management action', thus ensuring business 'heard' internal audit findings and understand their 'accountability and ownership' for control weaknesses reported by the internal audit team. CAE A observed that the change in wording had a positive impact on management's response to internal audit findings. He elaborated that internal audit 'gets better buy-in' from management who understand their responsibility for taking 'action' (CAE A). Moreover, as part of emphasising the value added by internal audit, CAE A actively managed the accountability of internal auditors for their work. CAE A included as a key performance indicator in internal auditors' performance agreements 'control failures post audit'. He traced such failures back to internal audit working papers and 'if my people have not picked it up, then they're penalised from a performance perspective'.

However, EP A2 opined that the key challenge hampering the status of and value added by internal audit was the competence of the internal audit team. EP A2 explained that 'getting the right people is the key challenge… of internal audit… attracting and retaining the right people, so that the internal audit process… receives the right kind of attention from the right kind of people [management]'. In particular, EP A2 noted internal audit functions generally faced 'a massive challenge… to try and fill more senior level' internal audit positions with individuals who are able to 'put something together, manage it, lead it, guide it'.

Third, EP B and A2 as well as the CAC participants were concerned about the implications for the status of and value added by internal audit from the interplay between the expanding scope and focus of internal audit's mandate and plans, particularly for assurance services, and the adequacy of internal audit budget / capacity / resourcing. EP A2 explained that over the 'last five years', increasing business complexity was causing exponential growth in 'what internal audit needs to understand and be involved in' which made the role 'far more demanding'. Thus, careful consideration of internal audit budget / capacity / resourcing required for fulfilling the expanding scope and focus of internal audit's mandate and plans was needed. In a similar vein, EP B called for realistic resourcing, in line with internal audit's mutually agreed realistic mandate and plans. EP C clarified that the perceived status of internal audit and the value it added was compromised when conflicting demands on internal audit resources from 'too many bosses', coupled with insufficient internal audit budget / capacity / resourcing, meant that unmet internal audit plans were a regular occurrence.

Fourth, CAC A equated the status of and value added by internal audit to the 'personal credibility' of the chief audit executive, explaining that it created the grounding for the 'trust' that management placed in internal audit. EP E1 conveyed that having a very strong head of internal audit determined the value added by internal audit reports, as the chief audit executive was instrumental in ensuring internal audit delivered 'the right findings' to the audit committee that were 'critical to the business' (EP E1). Similarly, EP D2 expressed that 'if business buys into the internal audit function, the importance, *etc* which is driven by the head of that department, then it will flow through the entire organisation'.

At a broader level, all the CAC participants reported that the 'credibility' and 'influence' (CAC D) attached to the professionalism of the internal audit profession and the scope and focus of internal audit's mandate and plans had generally been increasing over the last few years, as demands for assurance by internal audit increased. CACs ascribed the enhanced status of internal audit and the value it added to the positive influence of King III on the role of the internal audit profession. In particular, CACs perceived that internal audit professional bodies were playing a more active role, leading to more internal auditors attaining professional qualifications and being – or at least appearing to be − more independent. While this enhanced perception of the profession supported increasing levels of reliance (CAC D), this had, in turn, boosted the status and value of internal audit (CAC C / E). CAE C confirmed that 'there is a much bigger emphasis on internal audit' due to King III, which has resulted in the board realising 'how they have to rely on internal audit'. He also commented that 'the whole reputation, the whole image of the [internal audit] profession has changed'.

Although EP participants as well as CFO A and B opined that internal audit had 'quite a significant presence' (EP B) and an 'elevated' role (EP D1) in larger regulated organisations, they nonetheless indicated that the role of internal audit in smaller organisations was less pronounced. Thus, EP B associated MORE reliance with larger rather than smaller organisations.

CAC D highlighted that audit committee oversight considered the status and value of internal audit, particularly how management responded to internal audit reports. EP C pointed out that audit committees had an interest in overseeing the status and value of internal audit as its work provided it with comfort in terms of its oversight of risk management and internal controls.

(g) The profile and role of the chief audit executive

EP E 2 noted that having the 'right person to lead internal audit' was critical to the reliance decision, positing that 'if the [right internal audit] leader's not there then you [the external auditor] are wasting your time [when attempting to rely]'.

Participants associated *the way that the chief audit executive managed the internal audit budget / capacity / resourcing allocations received from management with the relevance and credibility of internal audit work, and thus, the status of internal audit and the value it added.* By way of example, CAC D and EP A2 pointed out that the credibility of internal audit work could suffer when *the wrong person was in the role of chief audit executive*. CAC D observed that 'if you've got the wrong person, you [internal audit] really are going to face an uphill battle … you've got *the risk of being discarded by management and by the audit committee* to some extent'. CAE B described the reciprocal effect of the status of and value added by internal audit on the audit committee's closeness to the business and strong audit committee oversight. Particularly, as he *received and reviewed all minutes of the company's executive* *committee, he could 'tell them [the audit committee] how to direct their questions [to management during audit committee meetings]'*.

CAC, CFO and EP participants from MORE and LESS reliance cases expressed their satisfaction with the profile and role of the chief audit executive appointee in the respective case companies. CAC participants described their chief audit executive appointees as 'ideal' (CAC D) and 'really good and competent' (CAC C / E). EP participants from MORE and LESS reliance cases described the chief audit executive appointees as a 'very good head of internal audit' (EP A2) and '*a very strong head of internal audit*' (EP B).

Participants pointed to the characteristics of the chief audit executive that have significant influences on internal audit work, reports and status. Important characteristics included (i) insights into the business and industry as well as a commercial orientation, (ii) independent influential leadership supported by communication and change management skills, (iii) technical skills and (iv) the seniority attached to the CAE position. These are discussed in more detail. First, all EP participants as well as various CFO, CAC and CAE participants, indicated that the chief audit executive influenced the relevance of internal audit work and the value added by internal audit reports. This was done by focusing on risk-based audits of key risks as a basis for risk-focused findings and pragmatic recommendations, addressing the real root cause of control problems. The chief audit executive should possess *insights into the business and industry of the company* (CFO B; CAC C / E; CAE D) as well as a '*commercial bias*' (EP A2; CFO B; CAE D). Participants explained that such a chief audit executive would be able to identify key risks as part of the internal audit process (CFO B; EP C), 'delve very deep into the rationale behind what's presented' in internal audit reports (CAC A) and, escalate 'the right findings' that are 'critical to the business' to the audit committee (EP E1). Thus, EP D2 clarified that the chief audit executive should not be 'somebody who has a tick box mentality, standing with a clipboard and ticking numbers'. EP A2 linked the status and value of internal audit to these insights, explaining that the chief audit executive with 'an interest and a contribution to the commercial piece of the business, goes a long way towards creating acceptance for the internal audit function within the business generally'.

Second, participants emphasised that the chief audit executive should demonstrate strong and *independent leadership* in the internal audit function and in the organisation (CFO A; CAC A, D; EP A1,B, C, D2, E2; CAE D) to bolster the credibility of internal audit work. In this regard, 'not negotiable' qualities of the chief audit executive included 'good leadership in internal audit [and being] a good manager, a good head of internal audit' (EP A2) and being 'an effective leader and not just a leader, someone with *influence*, someone who can sit on the executive committee and make a *contribution to the business*, I think is essential. I think it is not negotiable' (CAC D). Specific leadership qualities for the chief audit executive highlighted by the participants included the ability to put together and lead an effective internal audit function (CAC A), motivate internal audit staff (CAE D), build relationships (CAC A), *communicate effectively with staff and management at all levels* (EP B) and the *ability to accept and drive change* (CAC A).

EP E2 linked the need for a 'strong' chief audit executive to the *independence* of internal audit, explaining that 'if the chief audit executive is a strong individual, it just adds more value'. He added that the chief audit executive appointee should not be 'very soft … to protect [their] job', observing that many chief audit executives 'just keep quiet'. Like EP E2, several other participants linked being a 'strong' chief audit executive to the independence of internal audit (CAC D; EP A1, B, D2). In particular, EP B contended that a strong chief audit executive would be able to challenge management and raise concerns with the directors in cases where management placed unacceptable limitations on the scope and focus of internal audit plans and internal audit reports.

Third, the participants underlined the important link between the *technical competence* and experience of the chief audit executive and the credibility of internal audit work. Participants tended to link the technical competence of the chief audit executive to professional certification, particularly the chartered accountant (South Africa) and certified internal auditor certifications. Considering the professional certifications of the participating CAEs, CAE A, B, C and D held the chartered accountant (South Africa) certification, while CAE C was also a certified internal auditor. Although CAE E did not hold any professional certification, he had extensive external auditing experience as he had previously worked at a Big 4 accounting firm. Furthermore, CAE A and CAE C were actively involved in activities of the IIA, both locally and abroad.

Several participants favoured the chartered accountant (South Africa) certification over the certified internal auditor certification for the chief audit executive (CAC A, D; EP A1, C, D1; CAE C; CFO C). These participants described the chartered accountant (South Africa) as an 'essential qualification' (EP D1), and 'the right qualification' as it 'add[ed] a lot of value' (EP A1). Particular reasons given for these views included the perceived 'gap' between internal and external audit professional certifications (EP D1) and the broader business experience gained while working on various clients during external audit training compared to working in a corporate internal audit function (EP D1).

Interestingly, CAE C (who held both the chartered accountant (South Africa) certification and the certified internal auditor certification) explained that he favoured the former certification for a chief audit executive, as the external audit background supported interaction with external audit as well as a better understanding of it. Other participants were more accepting of either the chartered accountant (South Africa) certification or the certified internal auditor certification for the chief audit executive (EP B; CFO B). These participants rather valued the chief audit executive's understanding of 'processes and controls' (EP B) and 'a good industry understanding' (CFO B). While EP E2 stated that the chartered accountant (South Africa) certification or certified internal auditor certification was acceptable for the chief audit executive, he favoured having the former, which 'just adds value'.

The participants had strong views on the importance of experience for the chief audit executive. Experience was described as 'lots of detailed hard experience, *hands-on experience, in investigations and controls, in weaknesses*' (CAC D); the chief audit executive must 'have done audit work, from either internal audit or external audit work, in [their] career … that would be very useful. You almost need to have done some of the stuff yourself to have a good understanding, when I manage this function, what works and what wouldn't work … that sort of hands on experience' (CFO B). Participants mentioned that experience allowed CAEs to identify risks and quantify the impact of risks (CFO C), thus influencing the relevance of internal audit work and ensuring that internal audit reports contained risk-focused findings and pragmatic recommendations addressing the real root causes of control problems (CFO B).

Fourth, participants (for example, CAC A) highlighted that the '*seniority*' attached to the position of the chief audit executive should attract board and CEO support for the CAE and trust in their competence, endowing them with the ‘stature to be able to deliver unpleasant news without being intimidated’. CAE A declared that the display of support by the board chairperson of case A made him ‘willing to put my neck on the line if I [saw] a governance process failing’. EP A1 observed that management ‘relied’ on and ‘trusted’ the company’s chief audit executive. In turn, board and CEO support for the chief audit executive protected the independence of internal audit, as the CAE had backing in making sure internal audit work and reports were of unimpeded scope (CAE A, B, C, D, E; EP B, D2, E2; CAC D; CFO D). Providing evidence of management support for and trust in the chief audit executive, CFO B shared ‘I meet with him on a weekly basis’.

Using attendance of executive committee meetings as a benchmark of the chief audit executive’s seniority, in cases A, B, C and E the chief audit executive did not serve on the executive committee, while CAE D did. However, CAE A , B (2019) and E attended executive meetings as invitees while CAE B (2014) and C received copies of the minutes of executive meetings. At the time when the interview of this study was conducted, the chief audit executive appointee of case D was a highly respected individual, whose prior appointments had given him high-level international and local exposure. None of the five companies described the position of head of internal audit as ‘chief audit executive’. CAE B and CAE C opined that their companies were not yet ready to view them as senior executives. However, CAE C added that ‘[i]n our entity specifically the standing [of the chief audit executive] has increased quite a lot. I mean, I’m part of senior management. So, I attend… all the senior management conferences.’ CAE E conveyed that he was part of the ‘leadership team’ of the company. Thus, no link was evident between MORE reliance and whether the chief audit executive had a position on the executive committee of the organisation. Obviously, the chief audit executive’s knowledge of strategy, policy and other decisions enhanced the relevance of internal audit work in risk-based audit plans and reported findings.

CAC D highlighted the importance of audit committee oversight of the appointment of the chief audit executive and giving the appointee direct access to the audit committee, thus preserving the independence of internal audit.

Ultimately, EP A2 underlined having the ‘right person’ as the chief audit executive contributed to the status and value of internal audit, as such an individual was ‘respected’ giving him ‘access to and conversations with the chief executive, and the financial director, and … the chairman of the board’.

In conclusion, the reliance environment was primarily influenced by management’s governance choices. Synchronising stakeholder groups’ roles, interpretations, interests and practices influencing the reliance environment was a foundational condition determining stakeholder groups’ interpretations of the appropriateness and fairness of MORE compared to LESS reliance.

5.2.2.3 The relevance of internal audit work for statutory audit purposes

The properties determining the relevance of internal audit work for statutory audit purposes related to the influence of stakeholder groups’ roles, interpretations, interests and practices on (a) the scope and focus of internal audit’s mandate and plans, (b) the type of internal audit undertaken, (c) the internal audit approach, (d) collaboration between internal audit and risk management and (e) the external audit approach. Table 4.9 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this sub-category.

(a) The scope and focus of internal audit’s mandate and plans

While participants from all the cases underlined that the scope and focus of internal audit’s mandate and plans influenced reliance decisions (e.g. EP A1, B, C, D1, D2, E1, E2; CAE C, D, E; CFO E, CAC D), EP participants from MORE and LESS reliance cases considered it a ‘key’ condition of reliance (EP E2, D2)’. Participants explained that reliance depended on stakeholder groups’ understanding of the distinct roles of internal and external audit and how that understanding was reflected in the scope and focus of internal audit’s mandate and plans (EP A2, B, D1). This was especially so, considering stakeholder groups’ demands for assurance by internal audit were increasing, particularly in larger well-regulated organisations (for example EP A2, B). Thus, EP B, C and D2 emphasised that when expecting additional work from internal audit to assist external audit, internal audit’s ‘entire portfolio’ included in the scope and focus of internal audit’s mandate and plans should be balanced against internal audit budget / capacity / resourcing.

CAC D acknowledged events like global corporate collapses and the passing of the Sarbanes Oxley Act in the United States had changed audit committees’ interpretations of the distinct roles of internal and external audit, as well as the typical scope and focus of internal audit mandates and plans. CAC D elaborated that whereas management and some audit committees previously believed that internal audit was there to reduce external audit work and fees, most now recognised that internal audit should ideally concentrate on independent controls assurance work with a business-wide risk focus. CAC D contended that audit committees’ changed interpretation of internal audit’s role arose from the realisation that internal audit was a resource assisting audit committees in fulfilling their oversight responsibilities, thereby managing audit committee members’ personal liability. From a South African perspective, CAE C and EP E2 credited King III regulations and training provided to audit committee members and management for their improved understanding of the distinct roles of internal and external audit.

In line with CAC D’s explanation, participants from MORE reliance cases stressed that reducing external audit work and fees should not be the primary determinant of the scope and focus of internal audit’s mandate and plans. EP B as well as CAE B and C cautioned that management’s decisions should consider how they ‘balanced’ the influence on internal audit’s ideal business-wide risk focus when they incorporated work for statutory audit purposes into internal audit’s mandate and plans. EP B explained that ‘ultimately … internal audit must make sure that the mandate that they have received … from the audit committee and in terms of their own [risk] assessment, that that mandate is fulfilled’. CAC C / E and EP E2 found that some managers ignored the implications for internal audit’s work with a business-wide risk focus when incorporating work for statutory audit purposes in internal audit’s mandate and plans. However, EP E1 and E2 observed that management’s understanding of the difference in focus inherent in the distinct roles of internal and external audit was improving.

From MORE reliance cases, EP E1, CAC C / E and CFO B confirmed that management and the audit committee understood that neither internal nor external audit could substitute each other’s work, meaning they understood that internal audit was not there to reduce external audit work and fees. EP B and E1 as well as CAE B and E emphasised that the typical scope and focus of internal audit mandates and plans should be on controls assurance work with a business-wide risk focus. Considering the possibility of stakeholder groups' misaligned interpretations of the role of internal audit, EP B (from a MORE reliance perspective) stressed the need for *a mutually agreed, realistic mandate and plans for internal audit*. He described a realistic mandate as one that *balances the benefit versus reward of work both included and excluded from internal audit's mandate and plans, by prioritising risk-based audits*. EP A2 considered that finding the 'right balance' between benefit and reward of internal audit work was difficult, noting that internal audit's realistic mandate should ideally concentrate on the 'basics', namely, controls assurance work. EP A2 associated internal audit's controls assurance work with the value it added, asserting that 'a strong sound assessment and testing process around controls, including the testing of internal control processes', was 'the value they [internal audit] bring to the business'.

From a LESS reliance case perspective, EP C pointed out that *internal audit often faced conflicting demands on internal audit resources by 'too many bosses'*, yet they 'try their best'. *These demands include special investigations and ad hoc work for management* (EP A2 and C). Thus, CFO A called for a mutually agreed, realistic internal audit mandate, as management should 'make it very clear' what they were 'expecting' from internal audit, while remembering where 'the internal audit team fitted in', namely performing controls assurance work, not for control implementation as part of risk management.

Participants from MORE and LESS reliance cases explained that although internal audit's business-wide risk focus included operational, financial, strategic and reputational risks (CAE E; CFO E), *a larger proportion of internal audit work and plans had mostly an operational focus* (EP A1, C, D1, E1; CAE C, E; CAC C / E). Most participants contrasted internal versus external audit's focus, emphasising that external audit's strong financial focus meant that they 'really focused on financial statements', while internal audit focused on doing an 'enterprise-wide risk-based audit' (CAE D, as well as EP A1, C, D1, E1). These participants pointed out that when a larger proportion of internal audit work and plans had mostly an operational focus, the proportion of internal audit work relevant to the external audit decreased.

Internal audit work supporting MORE reliance (reliance work) fell outside the typical scope and focus of internal audit mandates and plans. First, EP B and E1 indicated that reliance work included *a large proportion of direct assistance work for statutory audit purposes edited into internal audit plans*. EP B referred to the latter as 'work that we [external audit] specifically mandate them [internal audit] to do so it is almost an extension of the external audit'. Second, direct assistance work which external audit 'mandated' internal audit to perform, included *controls assurance work and extensive substantive procedures* (EP B).

Third, MORE reliance occurred when *internal audit concentrated on work with a strong financial focus* rather than the ideal of controls assurance work with a business-wide risk focus. For example, CFO B declared that 'from … this company's perspective, the internal auditors have got quite a strong financial focus … a lot of the work they do impacts … [on the] financial result. It is not that there is a lot of work being done by internal audit, which … has got no financial impact'. However, CAE B cautioned against 'perfect alignment' of internal and external audit' focus, as 'blind spots' could arise when internal audit neglected controls assurance work with a business-wide risk focus. EP B emphasised even when internal and external audit work shared a financial focus, reliance depended on the competence of the internal audit team to 'really do work on the financial side of things'.

Participants from case E explained that they recently reconsidered the impact of direct assistance work on the typical scope and focus of internal audit mandates and plans. Subsequently, they reduced the extent of direct assistance work done by internal audit specifically for statutory audit purposes, in order to prioritise controls assurance work with a business-wide risk focus. This led to a greater operational focus. However, CAE E revealed management and some audit committee members opposed this reduction of direct assistance work for statutory audit purposes due to the implication of higher external audit fees. All participants from case E confirmed and were satisfied that external audit fees would increase due to changing the typical scope and focus of internal audit mandates and plans.

CAE B found that the expanding scope and focus of internal audit's mandate and plans made meeting internal audit plans difficult to achieve. Thus, CAC B suggested that expansions should keep internal audit budget / capacity / resourcing in mind.

Furthermore, EP A2 and EP C cautioned that including special investigations and *ad hoc* work for management as part of conflicting demands on internal audit resources by too many bosses made meeting internal audit plans difficult. In some companies, a percentage of internal audit's time remained unplanned for accommodating this type of *ad hoc* work for management during the year (CAE A and C; EP E2). EP D2 pointed out that the chief audit executive should ensure changes and additions to the scope and focus of internal audit's mandate and plans would not jeopardise meeting internal audit plans. EP E2 underscored the need for audit committee oversight and approval when expanding the scope and focus of internal audit's mandate and plans or adding conflicting demands on internal audit resources, in addition to the mutually agreed realistic mandate for internal audit.

(b) The type of internal audit undertaken

Participants from all the cases highlighted that MORE reliance was conditional on internal auditors performing *risk-based audits* rather than *routine conventional rotational internal audits* (EP A1, B, E1; CAE A, B, E; CFO B, E; CAC C / E). EP C explained that when making the reliance decision, the external auditor considers 'the scoping of their [internal audit] work, did they focus on the real stuff or did they just do a blanket … normal audit'. CAE B pointed out that risk-based audits enhanced the value added by internal audit reports, as internal audits excluded areas 'where everything is perfect'.

Participants' explanations revealed internal audits were progressively changing from extensive *random 'ticking and bashing'* (CAE A, EP C) as part of 'compliance type auditing' (CAE A), to focused 'risk-based auditing' (CFO A, B; CAE A; EP B, C, E1, E2). From a MORE reliance case perspective, CFO B expected internal audits to focus on key risks, including areas of management concern, rather than random ticking and bashing. CFO B mentioned that the internal audit team was following 'a truly risk-based approach' which meant that they were not randomly 'pulled into sort of doing work, just because we [internal audit] haven't done a section before'. CAE B commented that risk-based audits of internal audit added much value when they included work on changing business processes. However, he noted that auditing changing processes was challenging, as the internal auditing profession's Standards mostly focused on auditing 'stable and working' processes (CAE B).

CFO A and B mentioned that having internal audits focused on key risks depended on the risk identification 'ability' of the chief audit executive and internal auditors. CFO B highlighted that internal audit's awareness of key risks requiring attention during risk-based audits benefitted when management invited the chief audit executive to attend operational management meetings. CAE B found that having a forensics team and data analysts on the internal audit team kept internal audit 'close to the business', thus contributing to the identification of key risks or 'problems' requiring attention. In addition, CAE B (2019) found that risk-based audits which focused on key risks benefitted when *internal and external auditors were working closely together on 'joint risk assessment[s]'*, as 'we'll do the risk assessments together with [external] audit and the output we'll both use for risk assessment so we're both on the same page'. EP D2 argued that the pace of business made an integrated risk view among stakeholder groups 'difficult' to attain. He suggested that 'the openness of management' for *getting internal auditors involved at an early stage in projects involving process changes improved internal audit's risk awareness*.

Changes in key risks as well as *internal audit's responsiveness to evolving risks* also influenced reliance (EP A1, CAE C). CAE C underlined that internal audit adjusted plans as risks evolved. EP A1 clarified that when changes in key risks required additional audit effort, external audit usually audited those risks as meeting external audit's reporting deadlines in the presence of tight audit deadlines was paramount.

(c) The internal audit approach

Although internal audit's move to risk-based audits could be interpreted as an increasing overlap between internal and external audit work, EP C pointed out that internal audit work with an operational focus rather than a strong financial focus was the norm. However, EP C acknowledged that despite differences in internal and external audit's focus, 'there's definitely an overlap' between internal and external audit's risk-based audit work.

Neither CAE B nor CAE E fully abandoned 'conventional' (CAE B) 'rotational' (EP E1) internal audits, in spite of them advocating risk-based audits. CAE B explained that the internal audit team 'stick[s] to the conventional part at the end'. Participants from MORE and LESS reliance cases elaborated that internal audit usually embedded their work on key risks in their three-year routine conventional rotational internal audits (EP A1, E1; CFO E; CAE B). Thus, the external auditor's reliance decision considered whether *internal audits covered key risks annually as part of a 'base audit plan'* (CFO E) or attended to them on a cyclical, three-year rolling basis. In cases where internal audit did not cover key risks annually, *internal and external audit rotated coverage of key risks*, with external audit covering key risks in the 'in-between years' (EP E1) when they were not included in routine conventional rotational internal audits (EP A1). EP E1 stressed that achieving reliance on internal audit's work on key risks incorporated in routine conventional rotational internal audits required internal and external audit working closely together, engaging in structured, upfront alignment planning discussions and workshops. EP E1 explained that combining 'rotational' and risk-based audits affected internal audit's sampling and selection of financial controls for testing. Particularly, EP E1 maintained that 'I don't think they [the internal audit team] abandon the financial controls entirely but, they would be conducting a rotational approach to controls testing and testing each key area, maybe once every three years, whereas in the past I have seen more coverage [of a given key financial control] in a given year'. Thus, when internal audit covered key risks annually as part of a base audit plan, MORE reliance was possible. For example, CAE B stated that 'we [internal audit] do structure [audit work] into especially high-risk areas, to go there and audit it [annually] … irrespective if there is problems or not'. None of the CAEs of the LESS reliance cases (CAE A, C and D) described or named unconventional ways in which they ensured their routine conventional rotational internal audits focused on key risks.

CAEs of the two MORE reliance companies (CAE B and CAE E) provided specific details of the internal audit approach followed; CAEs from the LESS reliance companies did not share such detail. CAE B and B (2019) described the complexity inherent in the changing business environment, which was plagued by instances of executive fraud and therefore required a change in the internal audit approach at the group level (larger organisation). This would involve moving from *a 'transactional' (CAE B)* '*end-to-end … integrated [business process] approach*' *(CAE E)* to *a more holistic 'governance process' approach with emphasis on the control environment and significant risks associated with management's financial reporting 'culture' (CAE B*

(2019)).

CAE B elaborated that the change in internal audit approach at group level implied auditing the detail of ‘a few transactions’ and increased focus on the ‘general control environment’, including the ‘tone at the top’ and ‘governance structures’. CAE B (2019) described the internal audit approach at subsidiary level as transactional ‘business process audit[s]’. CAE E clarified that internal audit in case company E changed to an end-to-end integrated audit approach ‘because we are such a system-driven company … we look at all controls whether it’s IT, financial, manual … all controls are looked at, we look end-to-end basically … from the till point all the way through to the general ledger; … so, … we’ve got a strong computer audit focus in our team, so … I think we’re quite best practice in that regard’.

At group level, CAE B implemented strategies supporting the internal audit approach and risk-based audits, while overcoming ever-present internal audit budget / capacity / resourcing constraints. CAE B explained that these strategies meant internal audit ‘covered the same amount of work … [but] the quality of the work that we cover [increases] … because we go where there is problems; we know there is high risks [and] change’. CAE B explained that each internal auditor was assigned to keep ‘close’ to an area of business by building a ‘network’ of ‘relationships’. Thus the internal auditor remained ‘informed’ of developments and problems as ‘people’ [staff working in the area of the business] trusted the internal auditor would respect confidentiality and oversee appropriate interventions (CAE B).

(d) Collaboration between internal audit and risk management

The participants’ explanations revealed collaboration between internal audit and risk management aided risk-based audits, leading to MORE reliance. From a MORE reliance perspective, CAC B explained that ‘in this company [case B], there is a risk committee as well; so risk and internal audit work closely together. They talk about, very often, the same sort of things and both are represented in … all departments of the organisation … so they are well respected’. CAE B confirmed that *risk management and internal audit worked closely together, thus they shared an integrated risk view*, enhancing the relevance of internal audit’s risk-based audits.

In contrast, participants from LESS reliance cases did not emphasise collaboration between internal audit and risk management. For example, in case C, CFO C mentioned that '*risk management almost sits on the side* [as] our risk management function reports into our company secretary, who takes more of a governance type role in the business'. CAE C and C (2019), as well as CFO C, confirmed that risk management in company C was not functioning optimally. This meant that there was *no mutual sharing of information on key risks between internal audit and risk management*.

(e) External audit approach

The external audit approach dictated whether the external auditor tested and relied on internal controls; it also dictated the nature and extent of the external auditor's substantive procedures (IAASB, 2018: ISA 330 paragraph A3). Concentrating on controls assurance work (a combined approach) implied that the external audit approach relied on strong internal financial controls in the external audit process. In contrast, performing extensive substantive procedures implied that the external audit approach ignored internal financial controls. As a foundational condition, an external audit approach focused on controls assurance work would only be possible when strong internal financial controls were effective and operated for the entire financial period. However, extensive substantive procedures were inevitable when internal financial controls were not operating fully.

CFO A explained that once the external auditor's preliminary audit procedures indicated that strong internal financial controls were effective and operated for the entire financial period, controls assurance work became a viable external audit approach. CAE B commented that the external audit approach in case B had changed to include controls assurance work as a basis for increasing reliance and improving assurance efficiency. CAE A and EP B indicated that external auditors relied on findings in internal audit's reports when deciding on the external audit approach. When concentrating on controls assurance work, external audit either relied on relevant controls assurance work of internal audit or they performed such work. However, participants representing MORE and LESS reliance cases indicated when internal or external audit concluded that internal controls were not operating fully, the external audit team the external audit team reverted to extensive substantive procedures (CFO A, E; CAE A, ,B C; EP A1, D2, E2).

CFO A and E as well as CAE E, representing MORE and LESS reliance cases, expressed that business benefitted when external auditors performed controls assurance work on key controls, irrespective of whether reliance was intended or not. However, CFO A and E, CAE C and EP D1, representing MORE and LESS reliance cases, observed that in certain instances extensive substantive procedures rather than controls assurance work increased assurance efficiency.

From a LESS reliance perspective, EP D1 mentioned that weak internal financial controls in the company precluded external audits from focusing on controls assurance work, thus *the external audit team performed extensive substantive procedures, rather than a combined approach*. From a MORE reliance perspective, EP B and E1 indicated that *direct assistance work included controls assurance work and extensive substantive procedures, meaning that the external audit approach was somewhat irrelevant for reliance purposes*. EP B mentioned that he 'mandated' internal audit to perform extensive substantive procedures as part of the direct assistance work that internal audit did for statutory audit purposes. EP E1 also mentioned that external audit was using internal audit's direct assistance work on extensive substantive procedures. However, EP E2 perceived that concentrating on extensive substantive procedures when auditing larger organisations with listings hampered assurance effectiveness and efficiency. Thus, he urged management to implement strong internal financial controls as basis for external audits concentrating on controls assurance work in larger organisations (EP E2).

From a MORE reliance perspective, EP B and CAE B explained the interplay between an external audit approach, which included both controls assurance work and reliance. First, external audit determined whether controls assurance work incorporated into internal audit plans had a strong risk-based financial focus, aligned to external audit's sampling and selection for controls assurance work. Second, the external auditor reperformed a sample of internal audit's work for ensuring sufficient external auditor involvement in the audit of key risks and decided on the credibility of internal audit's conclusions about the effectiveness of internal financial controls. Third, when the external auditor concluded that the combination of internal and external audit's controls assurance work provided sufficient evidence of the operational effectiveness of internal financial controls, the external audit team performed less substantive procedures.

Participants from all LESS reliance cases confirmed that internal audit was not involved in external audit's extensive substantive procedures (EP A1, D2; CFO A; CAE C). EP A1 and D2 explained that having to revert mid-way in an external audit from controls assurance work to extensive substantive procedures made meeting reporting deadlines difficult to achieve and jeopardised the assurance efficiency. This was because the change increased external audit fees. In particular, such a change usually required increased audit coverage by extensive substantive procedures on balances at year-end, thus external audit – and not internal audit – usually performed such work (EP A1). EP D2 highlighted the need for open discussion with management and the audit committee when the external audit approach changed, including discussion of related audit fee implications. Furthermore, CFO A pointed out that extensive substantive procedures were beyond the controls assurance work mandate of internal audit and impractical, considering external audit's reporting deadlines. Moreover, concerns for the independence of internal audit dictated sufficient external auditor involvement in the audit of key risks (CFO A). However, CAE A interpreted that peripheral support by internal auditors – in the form of internal audit extracting data required for external audit's extensive substantive procedures – constituted substantive reliance work. CAE C found that when management addressed control weaknesses highlighted by internal audit work, the external audit team, and not internal audit, usually tested the effectiveness of the changed controls for deciding on the appropriate external audit approach.

CAC D and CFO D seemed frustrated as external auditors were 'ignoring' costly control improvements by 'redoing' audit work. They believed that external audit ignored internal audit's controls assurance work as the external audit team performed extensive substantive procedures. Thus, management were 'pushing' external audit to change their 'methodology' from extensive substantive procedures to controls assurance work (CFO D).

Also visibly frustrated, CFO C asserted that external auditors should 'just place more reliance' on internal audit's controls assurance work instead of duplicating work performed by internal audit doing extensive substantive procedures. In addition, CFO C perceived that external audit was not reducing extensive substantive procedures when they relied on controls and the work of internal audit. Providing insight into CFO C's frustration, EP C explained that when external audit relied on internal audit's controls assurance work, the related reduction in external audit effort was reassigned, allowing external audit to perform additional work not included in their original plan. Thus, the budgeted external audit time allocated to extensive substantive procedures was not reduced. EP C confirmed that reliance on internal audit's controls assurance work was not reflected in reduced external audit fees. EP C and CAE C confirmed that external audit practised no or limited reliance in company C.

In conclusion, all stakeholder groups' roles, interpretations, interests and practices influenced the relevance of internal audit work for statutory audit purposes. Synchronising stakeholder groups' influences on the relevance of internal audit work for statutory audit purposes was key in determining stakeholder groups' perceptions as to the appropriateness and fairness of MORE compared to LESS reliance.

5.2.2.4 The credibility of internal audit work for statutory audit purposes

The properties determining the credibility of internal audit work for statutory audit purposes related to the influence of stakeholder groups' roles, interpretations, interests and practices on (a) the competence of internal audit, (b) the independence of internal audit, (c) the standard of internal audit work and (d) meeting and changing the internal audit plan. Table 4.10 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this sub-category.

(a) The competence of internal audit

CAC participants pointed out the competence of the internal audit team was 'critical' (CAC C / E) and 'absolutely key' (CAC A) to the role played by internal audit. This category attracted the second greatest number of data incidents, with 102 quotations covering 32 pages allocated to it during substantive coding. EP D1 associated internal audit 'reports that don't make sense' with skills gaps in the internal audit team affecting the standard of internal audit work. He stressed that not having 'the right people …

would have a direct impact on the quality of their work’ and ‘the quality of the reports’ issued by internal audit.

Participants from all stakeholder groups linked the competence of the internal audit team to reliance. From the perspective of EP participants, EP E2 explained that the competence of the internal audit team was a ‘critical’ condition of reliance, noting that ‘their competence is critical, especially from whether we can rely on their work’. EP B added that reliance depended on ‘the skillset [of the internal audit team]’, while EP C considered ‘the qualifications of the internal audit team, their experience’ before relying.

From a non-EP participant perspective, CAC, CAE and CFO participants displayed a sound understanding of the link between the competence of the internal audit team and reliance. CAC D explained that external auditors assessed internal auditors’ ‘proficiency … before they would make use of the work of internal audit’. CAC B speculated: ‘I think they [external audit] look at the qualifications of the people that are there [in the internal audit function]; have they got the qualifications to do the work that is required?’ CAE participants mentioned that that ‘the quality and skills and expertise of the people in the internal audit department that do the work’ (CAE D) and ‘the right combination of [internal audit] staff’ influenced reliance. CFO B mentioned that the lack of appropriate ‘competence and skills’ of the internal audit team may cause external audit to conclude ‘that internal audit is not in a position to … give … the detailed comfort that is required’ for reliance.

EP participants from MORE reliance cases (B and E) were satisfied with the *unquestionable competence* of the internal auditors in those companies, while the EPs of the LESS reliance cases (A, C, and D) noted *skills gaps in the internal audit teams* of these companies. EP B affirmed that the company’s internal auditors possessed ‘a very high level of competence’. EP E1 declared: ‘I haven’t ever been in a position where I’ve said to internal audit: “Sir, I can’t rely on this because I don’t think the people who did it had understood what they were doing”. They have generally been very good.’ Similarly, EP E2 noted: ‘I don’t recall a competence issue’ as a reason for not relying. In contrast, EP D1 commented: ‘Now, I’m not saying don’t use internal audit, but seven times out of ten, the internal audit department, the majority of the internal audit department is not at a level where you can start relying on that work.’ EP A2 continued that ‘gaps … around qualifications, capability … industry capability, industry understanding, technical competence’ were generally present in internal audit teams. Thus, several EP participants from LESS reliance cases (EP A1, C, D1) *favoured reliance on outsourced internal audit work, particularly when the outsourced partner was a peer from a Big 4 firm, who they believed were more competent than in-house internal auditors*. Outsourced teams included ‘*specialised*’ (EP C) skills, often having members with ‘*acknowledged* skill’ in specific areas (EP A1).

The participants specified the attributes of *a competent internal audit team*. EP E1 underlined that the internal audit team should have *‘the right [mix of] skills to perform the work’*, while EP B highlighted that internal audit’s *ability to perform credible risk-based audits* was important. However, EP B explained that the competence of the internal audit team as a whole was important, as ‘you don’t necessarily need one person that can do it’.

The participants explained that an internal audit team with the right mix of skills to fulfil its mandate meant that *the majority of the team should be professionals ‘who are internal auditors and are going to be that for the rest of their life’*. The participants further specified that *other members of the internal audit team should be business staff who should have been attracted to the internal audit team and then rotated back into the business ‘at some stage’*. This would have improved their understanding of the business (CAC C / E); otherwise, new internal audit staff should start off in the business where they would gain a good understanding ‘from the operational point of view’, before they were moved into internal auditing (EP E2). The participants indicated that internal audit’s mix of skills could include ‘people with no financial background’, but with *relevant specialist operational skills* (EP A2).

In terms of the specific skills required in an internal audit team, participants enumerated a list of requirements, notably, (a) an understanding of ‘audits and the [related] disciplines’ (EP A2, EP E1), (b) ‘genuine analytical auditing skills’ (CAC A), (c) an understanding of ‘the objectives of internal audit’ (EP E2), (d) an understanding of the ‘COSO Framework (EP E2), (e) knowledge of industry-specific technical requirements (EP D1), (f) a strong understanding of the operational requirements of the relevant industry (CAC A, EP A2, B), (g) the ‘ability to go through an analytical thought process’, (h) an understanding of ‘business processes and functions’ (EP E1) and (i) related ‘controls’, (j) a sound grasp of the ‘financial side’ of the business (EP B), (k) internal auditors who are ‘good communicators [and are able to] listen to management’ (CAC A, CAE B), (l) IT skills (CAC A), (m) project management skills (CAC A) and (n) forensic skills (EP B).

In terms of the internal audit team’s understanding of the business, participants mentioned that it should be familiar with ‘the nature of its operations as well as its financial controls’ (EP E1), ‘the account structure, … the business complexity, what can go wrong, [by] listen[ing] to management about what worries them’ (CAC A), and ‘the risk overall’ (EP A1). EP E2 cautioned that a lack of understanding of the business and related risks might result in ‘impractical’ recommendations, thus negatively affecting the value added by internal audit reports.

Participants associated the competencies lacking in some internal audit teams with (i) the size of internal audit teams, (ii) nature of internal auditing and (iii) specialised skills requirements. First, EP A2 observed that *larger internal audit teams typically consisted of mostly junior level internal auditors and lacked managerial skills*, with negative effects on the standard of work. This was because part of the role of an internal audit manager was to provide on-the-job training and supervision of more junior internal auditors. EP A2 described larger internal audit teams had ‘very bottom-end heavy’ skills and a ‘skills gap’ of ‘manager level’ internal auditors who held a ‘degree’ and had ‘three to six years … experience … [and were] able to engage, lead, manage’ more junior internal auditors. EP A2 continued that the problem was ‘structural’, linked to the professionalism of the internal audit profession, as ‘internal audit struggles to attract and retain that level of people’. This was because being an internal auditor was ‘not sexy, it’s not exciting, it’s not fun’. EP A2 cautioned that the lack of individuals at ‘that manager level’ of internal audit teams had several negative effects. These included ‘the skills transfer in terms of how you engage at a more senior level’ and the standard of internal audit work. Thus, EP A2 found that ‘when we [external audit] start to look at the actual work delivered at the lower levels in that internal audit function, you find it’s of far poorer quality than what you would have expected’. EP A2 suggested that having *smaller* internal audit teams *consisting of mostly senior level internal auditors* would add more value to the business. This was because they possessed the requisite skills for following a more relevant, transactional, end-to-end, integrated business process approach, focused on auditing ‘high level’ ‘structure[s] and system[s]’ (EP A2). EP A2 also suggested such internal audit teams were more capable of using technology for increased effectiveness and efficiency.

Second, EP B pointed out that attracting and retaining *management level internal auditors* was also problematic in smaller internal audit teams, as few people were 'willing to stay as an internal audit manager for a substantial amount of time'. CAE B elaborated that limited promotion opportunities in smaller in-house internal audit teams made retaining senior level internal auditors difficult, considering 'we [internal auditors] are stuck in a corporate structure. So, you can't just make them a senior auditor, because you now [already] have a senior auditor'.

Third, participants reported that several specialist skills, depending on the industry of the company, could be lacking in internal audit teams. These included IT skills (EP A2, EP E1), forensic skills (CFO C), data analytic skills (EP A2), complex financial instrument skills (EP A2), taxation skills (EP A2, EP B) and actuarial skills (EP B). EP A2 perceived that the isolation of in-house internal audit functions and growing business complexity challenged the ability of organisations to put together internal audit teams with the relevant mix of skills. Participants indicated, however, that outsourcing specialist internal audit work overcame skills gaps in the competence of the internal audit team (CFO A, C, D, E).

The participants offered their views on what constituted a competent internal auditor, notably, the individual should hold a 'relevant qualification' (EP E2) which should be complemented by 'an audit background' (EP A2). Explaining the meaning of a 'relevant qualification' (EP E2), the participants mostly mentioned a financial accounting degree and external audit articles at a Big 4 accounting firm (EP A1; A2, C, D2; CAC B, C / E; CAE C, E). However, the participants conceded that individuals with other qualifications such as a 'higher diploma in internal auditing' (EP E2) or a 'BCom in Internal Auditing' (CAE B) could be appointed as junior level internal auditors, as long as 'they continue to be trained' (CAC C / E) after appointment. EP E1 called this a process which could 'grow their [internal audit's] own timber'. The participants specified that the CIA (Certified Internal Auditor) professional certification was also important (CAE C; EP E2). Some participants commented that internal audit could benefit from appointing specialists, like a relevant engineer who also held the CIA professional certification (CAE C; CAC C / E; CFO C) or other specialists such as a

Certified Financial Analyst (CFA) or a professional actuary (EP A1). However, the participants emphasised that without the appropriate experience, academic and professional qualifications did not make a competent internal auditor (EP A1).

The participants added that audit committee oversight of the competence of the internal audit team was important, for example, conducting an annual review of the experience and background of the internal audit team (CAC C / E).

Participants shared their perspectives on the competence of the internal audit team of their case companies.

Case A

Case A had a larger team, consisting of more than 200 internal auditors. Around 16% of these were chartered accountants (CAE A). CAE A mentioned that this team's average years of experience amounted to 8.4. There were around ten vacancies (5% of internal audit staff) in the team per month. CFO A clarified that the internal audit function operated as a business unit, like all other parts of the company, in line with the company's 'federal' approach. He was positive about the continuous need to hire new internal audit staff to fill vacancies which he saw as an opportunity to 'bring in new blood and new thinking'. In line with the 'federal' approach, CAE A conveyed that each business unit was being charged for the cost of their internal audits.

CAE A mentioned that high-level individuals with 'key skills' had rotated from the business into internal audit and back to the business in the past. He perceived that these individuals' improved understanding of internal audit raised the status of internal audit as some of these individuals had expressed the desire to join the internal audit team on a permanent basis.

CAE A opined that having internal auditors with IT skills and others with auditing skills aided 'skills transfer' when 'jointly' 'interrogating data'. CAE A implemented initiatives for improving the competence of the internal audit team. First, he required internal auditors to do research and presentations on allocated audit areas at the annual audit planning workshops of the company. The presentations had to address area-relevant 'key risks, key processes and key controls'. CAE A asserted that he preferred such training 'on the ground … in the face of business' more than training 'behind a desk …

or in a lecture room'. Second, he specified that the internal audit team had access to an international database of material on internal auditing from the 'Audit Director Roundtable' website.

CAC A observed that over the three years prior to the interview, the internal audit team of case A had displayed improved professionalism, a wider range of skills and a better understanding of the business. Thus, CAC A declared: 'Nobody can tell me anymore, that [internal auditors] do not have the skills.' He ascribed the improvement in internal audit's skills and professionalism to a greater emphasis on internal financial controls in the Sarbanes Oxley Act. Similarly, EP A1 observed that the in-house internal audit team of case A had 'up-skilled' in certain areas, although he acknowledged that 'credit modelling', 'valuation of financial instruments' and 'actuarial' work was still being outsourced.

EP A2 expressed sympathy with the 'tough job' faced by internal auditors, considering the expanding scope and focus of internal audit's mandate and plans. He pointed out that although 'some' internal audit functions were able to meet users' expectations, most 'struggle to deal with' conflicting demands on internal audit resources by too many bosses due to a skills gap in the internal audit team.

EP A2 believed that the competence of the internal audit team of case A would benefit from having a smaller team that includes sufficient 'management level' internal auditors. He explained that a smaller team with mostly senior level internal auditors would benefit assurance effectiveness and efficiency given the 'cost and management time' required to manage a larger team consisting mostly of junior level internal auditors. EP A 2 also proposed that the relevance of internal audit work and the value added by internal audit would benefit from having a smaller team consisting mostly of senior level internal auditors, as they would produce 'a far better internal audit' based on 'a more effective internal audit programme' and would 'engage with management' better.

Case B

Case B employed a smaller internal audit team, consisting 14 mostly senior level internal auditors, as proposed by EP A2. EP B linked MORE reliance to the competence of the internal audit team in performing risk-based audits and the standard of internal audit work.

At group level, the internal audit team in case B focused controls assurance work on the control environment rather than simplistic transactional audits of detail (CAE B). CAE B explained that most internal audit findings could be traced back to ‘a problem with structure, leadership, management, system or some form of training’. He argued that internal audit teams needed to ‘start thinking differently’. Hence, he suggested that the internal audit team should place greater emphasis on auditing the control environment rather than spending the bulk of its time on simplistic transactional audits.

CAE B remarked that most of the internal audit team started off studying towards the CA(SA) certification, but then diverted to internal auditing after completing the practical external auditing traineeship. He believed that the mostly audit focus of the qualifications and experience of internal audit appointees meant that they had a sound grasp of auditing principles as well. Furthermore, CAE B added all the audit managers in the internal audit team held either the CIA certification or the MBA (Master’s in Business Administration) academic qualification, or both. Also, CAE B emphasised having internal audit team members with ‘*industry experience*’ was ‘extremely valuable’.

Although the internal audit team of case B was highly competent, CAE B experienced the challenges experienced in attracting and retaining such highly competent internal auditors (also mentioned by EP A2). He attributed these challenges to the scarcity of highly skilled internal auditors.

EP B described company B’s internal audit team as having ‘a very high level of competence’. However, he mentioned that the recruitment process for appointing highly competent senior internal auditors was often long, as ‘the right people take three or four of five or six months longer to employ’. EP B agreed with the practice followed in company B of postponing internal audit appointments until ‘the right people’ were available. However, he was concerned that this drawn out appointment process caused strain on internal auditors who had to cope with work in periods when the internal audit budget / capacity / resourcing were too limited to fulfil their mandate and plans. CAC B mentioned that most of this company’s internal auditors remained in internal auditing rather than opting to move out into the business.

Case C

Since CAC C / E was the CAC of two case companies, he was able to compare the competence of the internal audit teams of cases C and E. CAE C / E observed that the internal auditors of LESS reliance case C had 'better accounting qualifications' than those of MORE reliance case E. He indicated that the internal audit team of case C mostly consisted of internal auditors with an accounting background and 'minimum internal audit experience … post articles [after the external audit training period] at a Big 4 [accounting] firm'. CAE C perceived that the skill set of internal auditors who underwent external audit training contributed to the performance of the internal audit team. Specific skills mentioned by CAE C were 'attention to detail', 'discipline [in] … meeting deadlines' and 'understanding the impact [of audit findings]'. He stressed that 'probably the biggest thing that I have seen in terms of your persons who have done the accounting side and completed the articles … is attention to detail'. CAE C added that appointing either accounting or internal auditing graduates with postgraduate qualifications implied 'either of these [appointees] could go all the way to CIA'. The internal audit team of case C included an engineer who was also a CIA.

CAE C stated that his internal audit team was 'not that big', as it consisted of 13 internal auditors, excluding the CAE. He added that the small size of the internal audit team meant that recruitment did not occur 'often'. When appointments became necessary, CAE C preferred appointing experienced internal auditors. Furthermore, CAE C and the audit committee emphasised initiatives for further developing internal auditors in order to 'lift the standard of the whole department'. CAE C used an annual 'coaching and development plan', setting out the areas of professional development identified by management and agreed with each internal auditor for tracking the development of internal auditors.

CFO C reported that the internal audit team members had 'some skills', however, they lacked forensic skills. CFO C explained that he purposely refrained from employing all the required skills within the in-house internal audit function as he used co-sourcing as an opportunity to expose his internal auditors to 'what the market [outsourced internal audit functions] is doing, for free'. CAE C mentioned that the internal audit function relied on co-sourced information technology specialists. CFO C encouraged the chief audit executive to attend local and international internal auditing conferences to learn more about the ‘technology and mindsets’ prevalent in the profession. In addition, CFO C encouraged the chief audit executive to set up meetings with academics in the internal auditing field ‘to give input’ in order to ‘build a solid profession’. CFO C remarked that CAE C took the initiative to network with four or five ‘other internal audit managers around the patch’ to strengthen their internal audit functions. EP C declared a preference for working with internal audit’s own teams.

Case D

CAC D noted that the internal audit function of case D had appointed a small ‘dedicated team’ of seven internal auditors. They were industry specialists who possessed the technical knowledge to understand and audit parts of the highly technical communication systems that generated the income of this company. He believed that the appointment of these specialists contributed to more reliance, as external auditors were increasingly making use of the specialists’ internal audit work on parts of the company’s systems. However, CAE D expressed concern about the external auditors’ reluctance to rely on the work of his internal audit team on the grounds of them not being competent.

CAE D pointed out that his internal audit team included individuals who had worked as external audit team members for case D in the past. Thus, CAE D could not understand why the current external auditors were refusing to rely on the work of his internal audit team, yet they had relied on these individuals when they were part of the external audit team. However, CAE D did ‘concede and accept’ that some members of his internal audit team ‘required a bit more training and a bit more maturity’ before external audit could rely on their work. He was also concerned about some internal audit team members’ lack of business insight. EP D1 said he preferred to work with internal audit’s own teams as he believed the skills gaps in the internal audit team made reliance too risky.

Case E

CAE E mentioned that his head office internal audit team consisted of one CIA and six CA(SA)s. This retail company also employed a large number of internal auditors who performed operational audits at its retail outlets. CAC C / E, EP E1 and E2 mentioned that over recent years, the company had successfully moved some internal auditors from finance-related operational functions into the internal audit function. These individuals then either remained in internal audit and pursued internal audit qualifications or they rotated back into the business. EP E1 and E2 emphasised that internal auditors with operational experience elevated the internal audit team's understanding of the business, while those rotating back into the business created an awareness in the business of the role of internal audit. EP E1 considered that the result of rotation was 'a win on both sides'.

The practice of rotating staff between internal audit and business was less prevalent in the other cases compared to case E. EP E1 confirmed that rotation occurred 'often'. From case A, CAE A remarked that operational staff members with 'key skills' had on occasion worked as 'guest auditors' with the internal audit team on 'particular' audits. Thus, like EP E1, CAE A claimed that rotation offered reciprocal insights, allowing the business to better understand internal audit, and *vice versa*. However, none of the other participants from case A mentioned rotation. EP E1 stated that he was never in a position where the competence of the internal audit team prevented reliance on this client.

(b) The independence of internal audit

The participants highlighted that the independence of internal audit played a role in reliance decisions (EP B, D1; CFO B; CAC D). By way of example, EP B explained that reliance was conditional on the independence of internal audit, noting that if internal audit was 'not fully independent of management … their work [would be] hard to rely on'. EP D2 declared that internal audit should be 'able to do their job *unimpeded*'. CAE B and C emphasised that independence was 'crucial' for maintaining the relevance of internal audit work. CAE B linked the independence of internal audit to auditing 'the right areas and … find[ing] the real issues', while CAE C warned that when the independence of internal audit is in doubt, 'your whole reputation is at risk', as 'trust' in internal audit as 'an independent source of information' was lost.

Merely based on the number of times participants referred to it, the independence of internal audit (45 quotations on 15 pages) attracted much less participant attention than the status and value of internal audit (113 quotations on 44 pages) and the competence of the internal audit team (102 quotations on 32 pages). A possible reason for this lesser emphasis could be the view that the independence of internal audit was a standard practice in most listed companies. As CFO B remarked: 'I wouldn't expect [independence] of the internal audit function to be a reason for them [external audit] not to rely on internal audit'. Although EP A1 expressed *general doubt about internal audit's ability to remain 'independent'*, EP D2 observed that most internal auditors were able to work 'unrestricted' consequent to their access to the audit committee and the board.

CAC D opined that remaining separate from the operations of the company and their colleagues was difficult for internal auditors as they were part of the company. CAE B and C attributed the complexity of the independence of internal audit to challenges posed by the complexity and evolving nature of the business environment and processes demanding innovative strategies for ensuring internal audit was *not isolated from business realities*. CAE B explained that the complexity, saying that 'it's one thing to be independent in mindset and in the way you [internal audit] work … and another thing to be … so independent that you don't want to do good'. Thus, CAE B acknowledged that managing the independence of internal audit was complicated, as 'it is a very, very fine line that you have to walk … you have to actively manage it', otherwise internal audit 'becomes quite irrelevant to the business and frustrating'. CAE B and C found that internal audit had to keep 'a fine balance' between remaining 'independent' and keeping sufficiently 'close to business' to maintain a relationship built on 'trust' with management and auditees. This was to ensure that the business would 'share whatever their concerns are', enabling relevant risk-based audits. CAE C advised that internal auditors should remain 'constantly' alert for transgressions of independence, and should rather be 'too strict' as this was 'safer' than being too lenient. He continued that he 'always' 'test[ed]' the objectivity of his decisions taken as CAE against what he believed 'a completely outside internal audit function' would do.

EP B found that *the independence of internal audit was often lacking in smaller organisations*, causing 'a major constraint' when making reliance decisions. However, CAE A stated that at 'lower levels', *internal auditors in larger internal audit functions were 'a little bit more flexible in their approach' to the independence of internal audit and could 'change ratings just to suit management'*. EP A1 and C perceived that *internal auditors providing outsourced internal audit services were more 'independent' than in-house internal auditors.* They explained that *outsourced providers' independence 'would automatically be there'* (EP A1), as they were 'more independent, like an external auditor' (EP C). CAC D expressed that he understood external auditors' perception that internal auditors lacked independence.

The participants from all cases alluded to measures linked to the independence of internal audit. First, most participants from all stakeholder groups started the conversation about the independence of internal audit with a reference to internal audit's reporting lines, noting that functionally, *internal audit should report to the audit committee* (CAE A; CFO B, C; EP B, D1, EP D2) and administratively, to the CEO (CAE A; CFO C; EP D1). EP D1 observed that most larger organisations set down reporting lines supporting the independence of internal audit.

Second, several participants underlined *the chief audit executive's direct access to the audit committee chair*, the CEO (CAC C / E; CFO C; EP A2) and the chairperson of the board (CAE A; EP E2), which strengthened the independence of internal audit. The participants declared that the chief audit executive of their company had interacted directly with the CAC in the past, when it was necessary to raise an internal audit issue or obtain advice when an issue was suspected (CAC B, C / E; CAE C; EP C, D2; CFO C). CAE C emphasised the importance of the relationship between the chief audit executive and the chairperson of the audit committee, stressing that *the chief audit executive should 'trust' that the CAC would support internal audit and the chief audit executive*, *honour the confidential nature of information shared*.

Third, participants cautioned that *internal audit should not accept work of an operational or managerial nature*. For example, CAC D sternly advised that internal auditors 'have got to be seen to be objective and independent … They've got to keep themselves apart to an extent from the operations'. Similarly, EP B suggested that internal auditors should not 'perform roles other than internal audit roles'. EP E2 also underscored careful consideration of 'the type of audit assignments they actually perform … you [internal audit] don't start doing management functions'. CAE E mentioned that *ad hoc* work for management could potentially undermine the independence of internal audit, warning that '*ad hoc* requests can't be … any management function, it's purely to do a review … we [internal audit] are not there to

… backfill in terms of there’s a shortage of people here or accountants there’.

Fourth, CAE A, B and C as well as CAC D highlighted that *the chief audit executive had to ‘actively manage’ (CAE B) relationships between internal audit and business staff*. CAE A and C were ‘constantly checking’ (CAE C) audit decisions of junior internal audit staff for independence transgressions. Preventative measures to manage the independence of internal audit involved *rotating internal auditors* (including internal audit managers) *between audit teams, audit areas and auditees*, making sure to ‘change all of the areas all together’ every three or four years (CAE B). They also involved ‘talk[ing] about this [independence] on a *continuous basis’, including ‘coaching and training’ about independence*. Lastly, these measures included ‘a rigorous *internal quality assurance programme* to ensure the [internal audit] methodology is applied consistently across the various [internal audit] teams’ (CAE A).

Fifth, CFO B highlighted that *the independence of internal audit meant management should not dictate the scope and focus of internal audit’s mandate and plans*, saying that ‘we can’t dictate what they must be doing … I can’t tell him [the chief audit executive] what areas he must be focusing on and what not’.

The participants pointed out the indicators of the independence of internal audit as well as red flags indicating threats to independence. Several participants (EP D2; CAC C / E; CAE C, D) observed that *internal audit’s willingness to report even ‘uncomfortable’ findings, verbally and in writing*, and to keep their findings unchanged even when pressurised to make inappropriate changes, reflected the independence of internal audit. CAE D explained that the independence of the chief audit executive was evident when he was ‘able to put [out] a report and stand by the report’ as proof that he was not ‘being directed by senior management’.

Concerning red flags indicating threats to independence, the participants conveyed that the *absence of disagreement between internal audit and management about internal audit findings* (EP E1) could be an indication of compromised independence of internal audit. EP E1 explained that internal audit findings issued ‘very quickly with very little debate over them’ could point to independence issues; he found that intensive consultation between management and internal audit about audit findings prior to tabling internal audit reports was the norm. Moreover, *the absence of internal audit findings (EP E2), particularly in areas highlighted as problematic by external audit* *procedures*, could also be an indication of compromised independence of internal audit. Lastly, EP C observed that when *management and internal audit openly shared a close symbiotic relationship*, the independence of internal audit was questionable.

Some additional insights about the independence of internal audit in the cases were apparent.

Case A

CAE A perceived that internal audit occupying offices in a 'corporate centre' away from the businesses they audited reflected the independence of internal audit.

Case B

CAE B reflected on the influence of the internal audit function's approach of staying close to the business on the independence of internal audit. CAE B explained that: 'I think you can be so independent that you are irrelevant but I think closer doesn't mean that we are influenced by management'. CAC B observed that he had no concerns about the independence of the internal audit function.

Case C

CAE C elaborated that the company had contracted two independent individuals (not internal auditors or part of management) who assisted management in the implementation of internal audits' recommendations. He added that internal audit worked closely with these 'implementation officials'.

Although CAE C was clearly aware of the independence requirements for his internal audit function, a very assertive CFO C declared that he managed internal audit from a 'strategic point of view … how they should approach the [internal] audit, what resources [management] brings on board and some of the focus areas that management may feel that they need a lot more assurance on'. CFO C also mentioned his intention of actively managing reliance as part of the external audit process through quarterly meetings with the external audit partner.

Case D

CAC D observed that the objectivity and independence requirements of internal audit were set out in the company's internal audit mandate.

Case E

EP E2 opined that 'the head of internal audit' was instrumental in ensuring the independence of internal audit, stating: 'This company is getting it [the independence of internal audit] right, definitely'.

(c) The standard of internal audit work

Participants observed that the standard of internal audit work was a condition of reliance (CFO A; CAC B; CAE A, B, C, D, E; EP C, D1, D2, E1, E2). These participants pointed out that LESS reliance resulted when *external auditors questioned the credibility of work produced by the in-house internal audit team*. EP A2 and D1 emphasised the interplay between the competence of the internal audit team and the standard of internal audit work determined whether 'the quality' of internal audit work was 'going to be of a standard that external audit [could] rely on' (EP D1). EP A2 recalled instances when, *in previous years, internal auditors' reliance work was of a lower quality than initially anticipated due to a skills gap in the internal audit team*.

EP A1 observed that *external auditors could 'automatically' rely on work of outsourced internal auditors from the Big 4 firms, indicating that he had no doubt about the credibility of their work*. MORE reliance was possible when *a stable internal audit team followed well-developed stable internal audit processes*. EP B remarked that 'we are in the fortunate position that those *internal [audit] processes of the internal audit function … are well-developed and fairly stable*', while EP E1 mentioned that internal audits were performed by a 'stable team'.

EP D1 and E1 underlined *the pervasive influence of the chief audit executive on the credible standard of internal audit work* who ensured that internal auditors had 'the right skills to do [the] work' (EP D1), that the risk-based audits were 'covering the right areas' based on 'a proper evaluation of the risks in the business' (EP E1) and played *'a quality role' by overseeing the review of internal audit work and files* (EP E1).

CAE D described the link between LESS reliance and the standard of internal audit work, explaining that 'when external audit evaluates the work of internal audit and clearly the quality and standard of work that is done by internal audit is not up to standard and therefore we [external audit] are unable to place reliance on the work of internal audit'. CAE D acknowledged that in case D, 'there is room for improvement in the quality of the work'. Paradoxically though, CAE D found it hard to understand why external audit 'dispense[d]' with the work of the internal audit function of case D, stating that 'I do believe that more effort needs to be put in by external audit to place reliance on the work that internal auditors do'.

Non-EP participants from MORE reliance cases elaborated that their external auditors reperformed a sample of internal audit's work when assessing the standard of internal audit work. CFO E explained that 'there's a certain amount of testing or retesting that they [external audit] would do … to test the quality of the work that gets done'.

Participants mentioned that several internal audit practices influenced the standard of internal audit work. First, participants linked the standard of internal audit work to the type of audit that they performed. EP D1 and CFO A explained that the standard of internal audit work was dependent on internal auditors 'effectively understanding [the] business and business risks … and adapting your [internal audit] work programme to make sure you are testing the right controls and effectiveness around those', thus *risk-based audits focused on key risks / controls*.

Second, participants representing all the case companies underscored that internal audit's *quality control procedures* ensured the standard of internal audit work, particularly 'monitoring' of staff while performing audits (EP E1), 'proper review' of audit work completed (EP D1, E1; CAE C) and pre- and post-issuance reviews of audit files and audit reports (CAE A).

Third, CAE and EP participants linked the standard of internal audit work to the internal audit function's *compliance with the Standards* (EP D1; CAE D; EP E1). CAE A observed that the Standards should be 'embedded in my [internal audit] methodology'. CAE C suggested that employing internal auditors familiar with the 'curriculum' of CIA certification examinations and 'internal training' ensured internal auditors were familiar with the Standards.

However, CAC A criticised the Standards as being vague and lacking detail, remarking that audit procedures were 'woefully badly described in the internal audit profession's Standards'. He continued that 'I want them [internal auditors] to do analytic reviews of any of their findings, tell me what's happened, why it happened, what's the impact of what's happened, and what we should do about it; that's just not in the internal audit Standards. It's there, it's there, but it's there only if you know what you're looking for'. He even advised that 'they [internal auditors] could do well to actually have the external audit standards amended for the internal audit role'.

Participants used several proxies as indicators of the standard of internal audit work. First, CAC B (like CAC D) mentioned that that '*the quality of the reporting that comes through*' was a reflection of the standard of internal audit work. EP participants used *the external audit approach* (EP D1) and *the external audit team's anticipated findings* as benchmark for assessing the standard of internal audit work (EP A1, D1). EP D1 expected internal audit should 'produce the same result at the same quality' as if the work was done by external audit.

Second, EP and CAE participants observed that reliance depended on 'evidence' not 'perception' of the standard of internal audit work reflected in *the 'quality of documentation*' (EP D1) and 'how is the work documented' (EP E1) (CAE C, E; EP D1, D2, E1, E2). EP E2 explained that 'we [external audit] look at the evidence we have at the end of the day, so we look at the [internal] audit working papers. That's what guides us. Yes, initially we look at the audit plan, but at the end of the day what's important is what [internal audit] documented … does it comply with the international Standards. That's it. Look at the evidence, not on perception'.

CAE E shared internal audit's documentation with the external audit team 'on request' in cases of reliance. In addition, CAE E shared the team's 'process and control documentation [and] our risk and control matrixes' with the external audit team 'to guide them' in planning the external audit. However, CAE C warned that internal audit needed to balance time spent on preparing internal audit documentation specifically for the purposes of reliance *vis à vis* performing audit work, being sensitive not to 'overdo' documentation. Clearly, improved communication between internal and external auditors could clarify such documentation requirements.

Third, EP D1 opined that *management's response to internal audit reports and recommendations* provided an indication of the standard of internal audit work. CFO A explained this interplay, saying that 'if I've got an ineffective [internal audit] team then I'm not going to rely on them'. CAE E considered that management took *internal audit reports* seriously if they *reflected findings and recommendations which were 'pragmatic… risk based…* and not textbook-based', *addressing the real root causes of control problems* (CFO B). CAE A used wording in internal audit reports to emphasise that the adequacy and design of organisational processes was not internal audit's responsibility.

The participants shared details of quality assessments performed by (i) the audit committee, (ii) an independent external quality assurance reviewer and (iii) the external audit team in terms of ISA 610 to determine the standard of internal audit work. First, CAC D mentioned that the audit committee's annual assessment of internal audit considered (a) whether the internal audit function fulfilled its 'mandate', (b) the 'number of [internal] audits completed … how they are doing against their planned number of audits for the year', (c) 'the quality of the report' and (d) the outcome of the independently performed external assessments of internal audit's quality (CAC D, C / E).

Second, participants from all the case companies confirmed that their internal audit functions were subjected to periodic external assessments of internal audit quality (CAE A, C, E; CAC B, C / E, D; CFO E). Case company A, B and E used Big 4 accounting firms to perform the external quality assurance reviews on their internal audit functions (CAE A; CAC B; CFO E). CAE C observed that 'we don't want to get one of the Big 4 accounting firms to perform that', and CAE D declared that 'we are in the process of getting the IIA to come and do a quality assurance review on the work that … my internal audit department is doing'.

Several participants commented on the outcomes of the external quality assurance reviews performed on their internal audit functions. From a MORE reliance perspective, CAC B recalled 'we came out very well', while CAE E said 'we were completely in line' and CFO E noted internal audit did 'very well'. From a LESS reliance perspective, CAE C used the outcome of external quality assurance reviews as well as IIA SA training offerings for improving the standard of internal audit work, although he had to ‘balance’ training attendance by internal auditors with ‘operational pressures and deadlines’. CAE A preferred in-house training of internal auditors, planned around operational pressures and deadlines.

CAE A was investigating the overlap between the ISA 610 assessment performed by external audit and the external assessments of internal audit’s quality, pondering whether either could be adapted for serving a dual purpose. He opined that external audit was not performing ISA 610 assessments on an annual basis, although he and CFO C expressed that they would welcome having such assessments, followed by feedback containing reasons why reliance was not possible.

From an external audit perspective, EP C mentioned that his company used the independently performed external assessment of internal audit’s quality as ‘part of our exercise’ (the ISA 610 assessment). Likewise, EP A1, B, D2 and E1 used the external assessment of internal audit quality to support external audit’s annual ISA 610 assessment of internal audit, for example, regarding internal audit’s compliance with individual Standards (EP E1). However, EP B and D2 stressed that the ISA 610 assessment performed by the external auditor carried more weight than the external assessment of internal audit’s quality when making reliance decisions, particularly ‘the stability of that [ISA 610] assessment’ (EP B) from one year to the next. Clearly the objectives and interpretation of outcomes of multiple assessments of internal audit were causing confusion. CFO C and CAE C were frustrated as they struggled to make sense of no or limited reliance by external auditors, considering the high ratings received following the external assessment of internal audit’s quality.

Third, participants from all cases shared extensive information about ISA 610 assessments of the standard of internal audit work by external audit. Data dealing with the cost-benefit of assessing internal audit and its work for reliance purposes are included in section 5.2.4.4.

EP D2 noted the objective of the ISA 610 assessment was making decisions about ‘reliance on [internal audit’s] work’, while EP E2 used it to ‘review [internal audit’s] work and comply with [external auditing] standards’. CAE A, B, C and E believed that their external auditors used the ISA 610 assessment for determining the standard of internal audit work and making reliance decisions. However, CAE D perceived that ISA 610 assessments were ‘not being done at all at the moment … The reason why is … they [external audit] have concluded that they are not placing any reliance on the work of internal audit, but I don't know what the basis of that conclusion was'. EP D1 confirmed that he practised no or limited reliance in case D as there were skills gaps in the internal audit team. EP D1 emphasised that management did not rely on the work of their own internal auditors. EP participants explained that the ISA 610 assessment was 'a formal process' (EP A2) requiring an 'integrated approach' as the outcome of the review 'depends on a host of factors … not a single factor' (EP D2).

From a LESS reliance perspective, EP D2 described these assessments as 'very hard', requiring 'discussions with the internal audit [team] [and] discussions with management' to determine what internal audit's function 'is about, how it operates, what is it achieving, and how much does the organisation accept all [their findings] … So I think it's a multitude [of factors] … [external audit] need[s] to jump through all the hurdles to achieve that'. CFO D described the assessment requirements of ISA 610 as 'onerous … hurdles' leading to over-auditing rather than reliance. He suggested that external auditing standards should be simplified to make reliance 'easier' and 'more efficient'.

From a MORE reliance perspective, EP E1 explained that external audit 'will do an assessment as part of our audit planning process, but it's relatively straightforward because [internal audit is] a pretty stable team; but of course, if there were significant changes to the team, or the way in which they go about doing their work, I am sure we would have more cause for concern [about the cost-benefit of the assessment]'. Similarly, EP B clarified that 'once you have the baseline assessment you can then easily, relatively easier … update it on an annual basis' for 'changes'.

Although EP participants used the reports from external quality assurance reviews to 'inform' (EP E1) and 'limit' (EP B) their ISA 610 assessments, external audit's assessments carried more weight when making the reliance decision (EP B, E1). External auditors' ISA 610 assessments typically considered (a) the competence of the chief audit executive: 'observing [during audit committee meetings] what [the CAE as head of internal audit] does'. The external auditor would 'look at [the CAE] and say well, … does he know what he is talking about?' (EP A1), (b) the relevance of internal audit's sampling and selection for statutory audit purposes: '[external audit] would read [internal audit] reports … where they would test financial controls that we would be testing as part of our process' (EP A2), (c) the standard (credibility) of internal audit work: 'we would go with them, observe their process and review some of their working papers' (EP A2), review the 'internal processes' and 'methodologies' of internal audit (EP B), review the 'planning' and 'credibility' of 'work done and documented' by internal audit (EP D2), (d) internal audit budget / 'capacity' / resourcing (EP B, D2), (e) the status of and value added by internal audit: management's acceptance of internal audit findings (EP D2), (f) whether risk-based audits are performed by internal audit, including internal audit's responsiveness to changing risks: 'if [internal audit is] finding that there are things happening, [and it] carries on doing whatever they're doing, then really, what's the point?' (EP D2) and (g) the competence of the internal audit team (EP D2).

Although CAE B and C initially indicated that they 'don't know' and were 'not sure exactly' how external auditors made reliance decisions, they were able to provide detailed accounts of the ISA 610 assessments performed by their external auditors. CAE C described this assessment as 'a mini quality assessment on our department', while CAE B speculated that external audit 'must have some checklist that they go through'. CAE A affirmed that he knew what the ISA 610 assessment was about, explaining that, 'I already know what [external audit's] scope is in the 610 assessment … so, up front, they call for information. I've got a support services team that works with them … they review … looking for evidence in the audit files … it's quite detailed'. CAE E merely observed that external auditors performed assessments 'in accordance with [external audit's] professional standards and they've got guidelines that they do that in accordance with'. CAE C elaborated that external audit 'send[s] in the dedicated internal audit department [of their audit firm] to assess the work that [internal audit] perform[s]', while CAE B suggested that it was 'probably the audit manager' of the external audit team who performed the assessment.

Describing the ISA 610 assessments, the CAE participants explained that external auditors focused on (a) the standard of internal audit work: 'a selection of audit files, to look at the quality controls that [internal audit] perform' (CAE C); 'they definitely do some form of assessment on each file' (CAE B); 'they select probably about 10 – 12 different files, and they'll review those files … but they review it against the IIA Standards. They review looking for our sample testing, our sample sizes, etc' (CAE A); 'they have access to our external quality assessment [report] … And then they will ask us questions about who does our quality assurance' (CAE B); 'they will look at our methodology' (CAE B); 'our quality assurance processes' (CAE B); (b) the scope and focus of the internal audit's mandate and plans: 'the [internal] audit charter' (CAE C); (c) the competence of the internal audit team: 'the composition of the team, the skills that we've got, the training' (CAE C); 'they ask a few questions about qualifications and things like that and then, mostly qualifications is what they are asking, we have to yearly give all the qualifications of the department' (CAE B).

CAE C associated a positive outcome from external audit's ISA 610 assessment of internal audit with the possibility of reliance, noting that 'if [external audit] give … positive feedback, then external audit can make use of our [internal audit] reports and files'. CAE A observed that the internal audit team performed well in the ISA 610 assessments, stating that no 'concrete' issues were identified, while past issues which 'affected the level of reliance that external audit could place' on internal audit work, particularly around internal audit's 'partial conformance' to the Standards, were resolved. CAE A acknowledged that ISA 610 assessments provided some useful recommendations, for example, on improving 'evidence on audit files', although these recommendations were 'not something that's stopped [external audit from] placing reliance'. EP C perceived that 'the internal audit departments that [external audit] evaluated over the last past years, just to say we can rely on their work, came out above average, not exceptional just above average'. However, CAE A found that external auditors' ISA 610 assessments of work of in-house internal audit functions were more extensive than those of outsourced internal audit work, particularly when the outsourced partner was a peer from a Big 4 accounting firm.

CAE A and B opined that external auditors performed ISA 610 assessments annually, CAE D stated that they did not take place, CAE E was unspecific about the frequency while CAE C indicated that they did not occur annually. However, CAE C noted that he would feel more comfortable if external audit conducted reviews annually for the comfort they might provide about the standard of internal audit work.

External auditors explained that the norm was limited feedback by external audit about the outcome of the ISA 610 assessment and the reliance decision. Feedback was mostly informal, very limited, generic and verbal (CAC B; EP A2, B, C, D2, E1, E2). The overall conclusion from the ISA 610 assessment was usually shared with the audit committee verbally (EP A2, B) or as ‘one sentence in audit committee presentations’ (EP C; CAE C) or as ‘a paragraph or so’ in the external audit plan presented to the audit committee (EP B), or generically dealt with in the management letter as part of the external auditor’s report on internal control weaknesses (EP E2). EP A2 explained that such limited written reporting was usually high-level and carried a positive message about internal audit, usually stating ‘from a structural perspective, it looks good, their remit, mandate, the people we’ll kind of say, it’s okay … overall … the package looks good to us … we can rely on you here, here, here, here. And management go okay, that’s fine’.

In addition, any ‘gaps’ identified in internal audit during external audit’s ISA 610 assessments were usually discussed informally with the chief audit executive (EP A2, D2, E1). EP A2 explained that external audit ‘kind of skirt around the hard conversations that we should be having with internal audit’. Thus, external auditors kept conversations about ‘gaps’ in internal audit out of the limelight, noting that they ‘don’t have them in committee or in public or for management to see’ (EP A2). Since ‘gaps’ were ‘difficult to communicate’, EP A2 was ‘careful’ and ‘diplomatic’. He clarified that his approach considered the possibility of a ‘tit for tat’ reaction by management and internal audit, who might react to external auditors ‘pointing fingers at internal audit’ by ‘look[ing] for any holes or any cracks in [external audit’s] armour’ by saying ‘well … external audit really don’t do a very good job here, and external audit didn’t do a very good job here’. However, EP A2 mentioned that the external audit team was in fact, well aware of the ‘gaps’ in internal audit’s ‘work and processes’, thus they relied selectively ‘where [external audit] know [internal audit is] doing the better job, [where] we know the quality of their work is better’.

EP E2 found that companies used feedback from ISA 610 assessments to improve the quality of their internal audit, although he underlined that improvements were dependent on the inherent strength of the audit committee.

CAC B and CFO C provided insights from their MORE and LESS reliance case perspectives about the limited feedback from external auditors on the outcome of ISA 610 assessments and reliance decisions. From a MORE reliance case perspective, CAC B observed that ‘external audit does not specify shortcomings in the internal audit function that prevents reliance’, however. he added that the audit committee ‘just know[s] that [external audit] … will be using the work of internal audit generally'. From a LESS reliance perspective, the limited feedback left CFO C frustrated as he struggled to make sense of no or limited reliance by external auditors despite positive, high-level feedback on the outcome of the ISA 610 assessment. He noted that 'the question begs to our external auditors why aren't you using [the work of internal audit]' when the assessment outcome indicated that the company's internal audit was 'in the top quartile' and in spite of improvements made to internal audit in response to prior assessment reports. CFO C declared that external audit 'must tell us where the shortcomings are, so that our CAE can redesign his tests'.

(d) Meeting / changing the internal audit plan

The participants mentioned that reliance was conditional on internal audit meeting the internal audit plan (CAE A, C; CAC B; EP D1, D2). CAC B explained that reliance decisions considered whether internal audit work 'is properly planned … [and internal audit] plans are met, that [the internal auditors] get through the work'. However, CAE C warned that the standard of internal audit work and internal audit's propensity for meeting the internal audit plan was a product of the scope and focus of internal audit's mandate and plans and internal audit budget / capacity / resourcing. He explained that when '*the audit plan is too optimistic … [it] either can't be done or … compromise[s] on quality' (CAE C), as internal audits became 'a tick exercise' focused on 'quantity' instead of 'quality'. CAE C added that 'too many ad hoc requests, too many special investigations … impact on the normal assurance work'.*

The participants acknowledged that audit plans were not static, they were changed from time to time (EP A1, B, D1; CAE A, C; CAC B), usually due to changes in operational and business risks or due to special investigations and *ad hoc* work for management. An example of this would be fraud and due diligence investigations or increasing reliance work.

CAE A and C pointed out that their *'flexible' internal audit plans* accommodated the need for formally changing the plans originally prepared for a 15-month period. This ensured that their risk-based audits were *'responsive' to changing and emerging risks*. CAE A explained that the 'agile' internal audit plan worked *on a '80 / 20 principle'* as ‘risks … evolve every day in an organisation, so hence [the internal audit] plan needs to be fluid’, *balancing ‘capacity considerations’* with the audit of evolving risks.

Several participants (CAC A, D; CFO E; EP B, E2) commented that *audit committee oversight provided the ‘balance’ needed to ensure internal audit capacity allowed risk-based audits and meeting the internal audit plan in spite of changes* for accommodating evolving risks, increasing reliance and special investigations and *ad hoc* work for management. From a MORE reliance perspective, EP B highlighted that the ‘experience’ of audit committee members (the inherent strength of the audit committee) ensured that they ‘understand the risks’ when changing internal audit plans in order to increase reliance. He added that audit committee oversight ‘provided a balance between the progress of internal audit work against approved internal audit plans and the impact of changes to … plans presented to the audit committee for approval [on internal audit’s ability to meet plans]’. This ensured that internal audit continued following ‘a risk-based approach’. CAC B acknowledged that although ‘one or two’ audits in the internal audit plan might be ‘carried forward to the next year’ when internal audit ‘prioritise’ ‘a big fraud’, *internal audit mostly met their flexible internal audit plans*.

From a LESS reliance perspective, EP D1 found that *unmet internal audit plans were a regular occurrence*, as internal audit ‘often’ ‘start[ed] with a whole audit plan and only [did] a bit of it’, particularly when they prioritised special investigations or *ad hoc* work for management. EP A1 explained that when internal audit ‘delays’ or ‘defer[s]’ reliance work ‘to the new financial year’, for example, to perform special investigations or *ad hoc* work for management, ‘if there is a problem in a specific area’, meeting external audit’s reporting deadlines also became a challenge.

CAE A and C as well as EP A1 and CAC B highlighted that changing internal audit plans required audit committee approval. CAE C asserted that he was in ‘continuous communication’ with the audit committee about changing internal audit plans. He also indicated that audit committee oversight of changed plans took the internal audit budget / capacity / resourcing into account.

In conclusion, all stakeholder groups’ roles, interpretations, interests and practices influenced the credibility of internal audit work for statutory audit purposes. Synchronising stakeholder groups’ influences on the credibility of internal audit work for statutory audit purposes was a foundational condition determining stakeholder groups' interpretation of the appropriateness and fairness of MORE compared to LESS reliance.

5.2.2.5 External audit quality and the external auditor's liability

The properties influencing external audit quality and the external auditor's liability related to the influences of stakeholder groups' roles, interpretations, interests and practices on (a) the riskiness of reliance and (b) sufficient external auditor involvement in the audit of key risks. Table 4.11 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this sub-category.

(a) The riskiness of reliance

All CAC participants were well aware that reliance decisions were complex and external auditors had to consider the effect of reliance on external audit quality and the external auditor's liability, when deciding on appropriate reliance. *External auditors from LESS reliance cases perceived reliance was 'difficult' (EP A1) and focused on the riskiness of reliance, considering the distinct roles of internal and external audit (EP C)* and differences in professionalism of the two professions *(EP C). Thus, they limited reliance to the 'bare minimum'* (EP A2) *on grounds of their sole responsibility for the external audit (EP D1)*.

From a MORE reliance perspective, CAE B highlighted that following *a combined approach to assurance* meant 'a much better understanding' of each other's assurance needs and responsibilities, including the interrelated distinct roles of internal and external audit. Consequently, *aligned individual audit plans mitigated 'undue reliance'* (EP B), *while internal and external audit minimised 'assurance gaps'* (EP B; CAE B). CAE B explained that audit committee oversight focused on minimising 'assurance gaps', namely, areas not covered by internal nor external audit as each one perceived that the other had covered those areas. Typically, 'undue reliance' and 'assurance gaps' equated to ineffective (inappropriate) reliance, undermining external audit quality. According to CAC D (like CFO E), preserving external audit quality when practising and increasing reliance required *'careful' 'independent' selection of reliance work* by external audit as well as '*support' through audit committee oversight*. CFO E emphasised that the effect of reliance on external audit quality meant that external audit had to *carefully assess the quality of the internal audit function and its work when practising appropriate reliance*. Thus, CFO E stated that external audit would remain accountable when relying inappropriately.

Although CAC D opined that all four stakeholder groups could 'move together closer' in terms of reliance possibilities, he predicted that 'it is going to be an uneasy relationship'. All EP participants from LESS reliance cases ascribed the uneasy relationship to stakeholder groups' misaligned interpretations about reliance. External auditors explained that practising appropriate reliance was extremely 'difficult' (EP A1, A2, C, D1, D2) with 'tension' (EP A2) prevailing due to misunderstanding of the distinct roles of internal and external audit. EP C noted that 'management and the audit committee doesn't have the same view [as external audit]' about the distinct roles of the two functions. Adding to the misunderstanding, EP D1 perceived that there was a 'contradiction in terms of what management expects [from reliance] and what they're prepared to do' to make reliance possible, for example, their influence on internal audit budget / capacity / resourcing and the independence of internal audit work *threatened the relevance and credibility of internal audit work*. EP D1 also mentioned instances where *management exerted pressure to increase reliance on external audit despite internal audit reports concluding that internal financial controls were not operating fully*.

Contrasting the external auditor's *sole responsibility for the audit* against *the professionalism of the internal audit profession*, EP D1 explained that 'there's a lot more that needs to be done [to improve internal audit] … if you look at what they [professional bodies for internal auditors] do as opposed to what an IRBA [regulatory board for registered auditors] would do, or what our firm [does] … we've got quality reviews that is done globally … we have guys that will come from any part of the world looking at the files. So, I think from what [external audit] do and what [internal audit] do, there's a huge gap'.

EP participants from LESS reliance cases (EP A1, D1) repeatedly highlighted that the external auditor's 'sole responsibility' for the external audit influenced reliance decisions. Although EP D1 acknowledged internal and external audit 'will have to end up working together', he was acutely aware of the importance of balancing his 'huge responsibility' for the external audit against the effect of reliance on external audit quality and the external auditor's liability, particularly since he *questioned the credibility of work produced by and skills of the in-house internal audit team*. Conversely, he (EP D1) perceived his team possessed unquestionable competence and he could 'place reliance on everything those people have done'. Consequently, EP D1 resisted reliance, declaring that external auditors had to 'put [their] foot down and say, I'm not going to rely, these are the reasons' as 'management need to be told' why reliance was not possible. He added that 'in a few instances, [external audit] were asked those questions [why are you not relying] … and we put whatever the issues were on the table and we work with the audit committees'. EP A2 also declared that external audit will 'accede to a certain point … to the demands and the requests of both management and audit committees to reduce costs by using internal audit more … and then say that's all we're prepared to do'.

LESS reliance case external auditors were *contrasting the superior professionalism and credibility of work of the external audit profession and teams against the inferior professionalism and credibility of work of the internal audit profession and in-house internal audit teams*. Thus, EP C stressed that '*I would rather work with my own people*'. EP D1 explained that the *complexity of an audit* of a 'large listed client', requiring a 'multi-national audit' team of 'hundreds of people and dozens of partners working on this job that all report to you [the engagement partner]', even complicated relying on the work of individuals from 'your own firm [external audit]'. However, EP D1 indicated he was more accepting of the quality of work produced within the external audit 'firm environment' as he perceived that the firm's quality control procedures and staff appointment criteria mitigated external auditor's liability.

Several other participants from LESS reliance cases also contrasted external auditors' sole responsibility for the audit against the professionalism of internal audit when they explained why external auditors practised no or limited reliance. These participants (CAC A; EP A2, D2) mentioned that the difference in internal auditors' versus external auditors' liability influenced reliance. They noted that internal audit did not have a 'statutory duty' (CAC A) and was not subjected to the same level of regulation, 'accountability' (EP A2), 'sharing of risk' (EP A2) and 'statutory sanction' (CAC A) as external auditors. In particular, EP D2 pointed out that limited information about internal audit findings were contained in annual reports, while EP A2 and D1 specified that the chief audit executive did not have a duty to officially sign off on a report for inclusion in the annual report.

Given this contrast between the two professions, EP A2 expressed that ‘there will always be a reluctance or a reticence on [external audit’s] part to take [internal audit] too seriously’. He averred that he would limit reliance to ‘the bare minimum … until there’s a sharing of risk [liability]’ between internal and external auditors. EP D1 added that it would become ‘easier for external audit to go and rely on something that internal audit does’ when the chief audit executive was regulated by a professional body and signed-off a ‘standard form report’. EP D1 commented that he would be willing to rely when internal audit functioned similarly to an external audit firm (‘almost like [internal audit] running an audit practice within an organisation’), as ‘then and only then [external audit could] … get comfort’. He specified the importance of risk-based audits, the independence of internal audit and factors associated with the standard of internal audit work (EP D1). Contrasting the external auditor’s sole responsibility for the external audit against the professionalism of internal audit, he reiterated that ‘unless [internal audit] can [function like an external audit firm], … for somebody externally to rely on the work of internal audit, is going to be taking a huge risk … from the external audit partner’s point of view’ (EP D1).

CAC participants (A and D) from LESS reliance cases understood that concerns linked to external auditors’ liability were behind their ‘reluctance’ to accede to management and the audit committee ‘encouraging external audit to make more use of internal audit’s work’, expecting reliance to happen as this would, in turn, reduce external audit fees consequent to ‘the efficiencies of using internal audit work’. CAC A explained that external auditors had ‘specific liabilities as well as tasks, which the internal auditor does not have’, thus ‘liability issues’ of the external auditor were behind reliance decisions. On a similar note, CAC D observed that ‘there has always been some reluctance [by external audit] to [rely], … and I thought I’d put it down to the fact that the risk in terms of … something going wrong on the audit, and the reputational damage that would [ensue for external audit], probably supersedes the efficiencies of using internal audit work’. In a similar vein, CAE A remarked that the cost of external audit’s professional indemnity insurance made reduced external audit fees consequent to reliance unlikely.

However, despite concerns for external auditor's liability, CAC A and D claimed 'I have seen a change', observing that external auditors had started relying more on the work of internal auditors. CAC A relayed that external audit does 'use [internal audit's work] where they can … they absolutely do' while CAC D added that 'I have seen more positive comments coming out of external auditors in terms of making use of internal audit work'. CAC D attributed increasing reliance to 'the increased professionalism of internal audit … over the last few years'.

In contrast, from a MORE reliance case perspective, *none of the EP participants mentioned that external auditor's sole responsibility for the external audit affected reliance, as none of them questioned the relevance of internal audit work nor the credibility of internal audit work*. Furthermore, EP B opined that internal audit could only attract liability for their work when the scope and focus of internal audit's mandate and plans were truly under their own control, including securing sufficient and appropriate internal audit budget / capacity / resourcing for performing all work that they deemed necessary. EP B continued that in practice, the internal audit budget / capacity / resourcing meant that they worked on a 'benefit versus reward' basis, performing risk-based audits in line with risk prioritisation in accordance with management's risk appetite.

EP participants from LESS reliance cases indicated that *reliance amidst the need to address evolving (changing) risks, internal audit budget / capacity / resourcing constraints and external auditors having to redo internal audit work of a poor quality or reassume responsibility for delayed or transferred work originally allocated to internal audit posed challenges in meeting external audit's reporting deadlines, particularly when these issues arose later in the reporting period* (EP A1, D2). For example, when *internal audit's reliance work found internal financial controls were not operating fully and the external audit approach had to change from focusing on controls assurance work to extensive substantive procedures*, meeting its reporting deadlines became problematic (EP A1, D2). EP A1 explained that internal audit budget / capacity / resourcing and the need to meet external audit's reporting deadlines influenced whether or not they could assist with external audit's work responding to any evolving risks. CFO A indicated that expecting internal audit to assist with extensive substantive procedures was impractical, considering the typical scope and focus of internal audit mandates and plans and the need to meet external audit's reporting deadlines. Furthermore, EP A2 recalled instances when the external audit team had to redo reliance work initially allocated to internal audit in aligned individual audit plans, which had hindered external audit from meeting its deadlines. Moreover, EP A1 explained that when internal audit 'delay[ed]' or 'defer[red]' reliance work 'to the new financial year', for example 'if there was a problem in a specific area', reliance posed challenges for meeting external audit's reporting deadlines.

(b) Sufficient external auditor involvement in the audit of key risks

Participants representing all cases acknowledged that sufficient external auditor involvement in the audit of key risks was a condition of reliance (EP A1, B, D2; CFO B; CAC D). EP B explained that external audit should reperform a sample of internal audit's work as a basis for concluding on the credibility thereof. CFO A underlined that 'ultimately, external audit cannot whole-heartedly only rely on internal audit; they have to do their own procedures to come up with their opinion'. Likewise, EP D1 pointed out that external audit 'can't expect internal audit to go and do all the work and you come and sign your financial statements'. CAC C / E reiterated that the external auditor's sole responsibility for their opinion meant that 'they can't turn around and say no we rely on internal audit to do that'.

EP A1 justified that sufficient external auditor involvement in the audit of key risks always necessitated the extension of internal audit's samples to the level required by external audit's methodology. He noted that internal audit 'have done certain amounts of work, and say we were going to do a hundred, we can reduce that. But … the answer is never nil'. In instances where 'controls are good', EP A1 and EP D2 determined the net sample size for testing by the external audit team by deducting the number of tests conducted by internal audit from the total sample size required for their purposes. They conveyed that they 'added on an additional sample', comprising the number of reliance items requiring 'reperformance testing'. EPs from MORE reliance cases did not follow this approach, possibly as reliance work chiefly consisted of direct assistance work, in accordance with alignment planning. Thus, the external audit team performed reperformance testing but no extensions. CAE A was aware of occasions when external audit deemed it necessary to extend internal audit's work for obtaining *sufficient external audit coverage*. Resisted reliance by external auditors from LESS reliance cases meant that *sufficient external auditor involvement in auditing key risks was not problematic as they practised no or limited reliance*.

From a MORE reliance perspective, CFO B explained that sufficient external auditor involvement in the audit of key risks means that 'external audit needs to also audit certain areas from time to time'. He asserted that *rotating assurance work on key risks between internal and external audit avoided unnecessary duplication of audit work*. Likewise, EP E1 explained that rotating assurance work on key risks between internal and external audit overcame limitations of internal audit's routine rotational audits on reliance, while ensuring sufficient external auditor involvement in the external audit of key risks. However, EP B declared that sufficient external auditor involvement meant that higher reperformance levels on significant risks could make reliance inefficient. He maintained that external audit 'would also look at the level of reperformance [of internal auditors' work required in lieu of reliance]. So, where [the *audit area*] is so critical for us, the level that we would be reperforming, … makes it more efficient for us to look at it [rather than relying on internal auditors]'.

Furthermore, EP B elaborated that *external audit was not using reliance or direct assistance work from internal audit for a complete area where significant risk was present*, noting that 'we wouldn't mandate [internal audit] to do a whole section; the very significant risk areas, we would want to cover ourselves'. Thus, *external auditors audited the riskiest parts of significant risks themselves* (EP B). From a LESS reliance perspective, EP D2 explained that less reliance occurred in 'significant risk area[s]' as *the external audit team typically performed 'more substantive work' on significant risks*, in contrast to internal audit's usual focus on controls assurance work.

In conclusion, all stakeholder groups' roles, interpretations, interests and practices influenced external audit quality and the external auditor's liability. Synchronising stakeholder groups' influences on external audit quality and the external auditor's liability was a foundational condition determining stakeholder groups' perceptions as to the appropriateness and fairness of MORE compared to LESS reliance.

Combined, synchronising stakeholder groups reciprocal influences on reliance made stakeholder groups' *mutual agreement that reliance was appropriate and fair (balanced), whatever the reliance decision* viable. Synchronising considered stakeholder groups' assurance needs and responsibilities, as well as their influences on the reliance environment, the relevance and credibility of internal audit work for statutory audit purposes, as well as external audit quality and the external auditor's liability.

5.2.3 Working mindset

The properties determining internal and external auditors' working mindset are the (a) assurance approach (5.2.3.1), (b) internal and external audit working together (5.2.3.2), (c) internal and external auditors substituting versus complementing each other's work (5.2.3.3), (d) the quality of the relationship between internal and external auditors (5.2.3.4) and (e) the working mindset of internal and external auditors (5.2.3.5). The quality of communication between internal and external auditors as well as oversight by the audit committee pervasively sustained these influences on MORE or LESS reliance. Table 4.12 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this category.

5.2.3.1 The assurance approach

Most participants from MORE as well as LESS reliance cases mentioned that the assurance approach mediated reliance. They pointed to the link between King III requirements and reliance, noting that the combined approach to assurance introduced by King III gave 'structure' (CAE E) and raised awareness of the assurance approach practised (CAE B). The participants ascribed the relation between MORE reliance and a combined approach to assurance. EP B and CAE B found that *optimal integration of internal and external audit work (integrating work) was the outcome when internal and external audit worked closely together, in accordance with a combined approach to assurance*. This *minimised unnecessary duplication* as the two 'combine[d]' their work 'as much as possible' (EP B), while *minimising assurance gaps* (CAE B).

The participants revealed that MORE reliance occurred when stakeholder groups practised a combined approach to assurance, in accordance with King III (EP B, E1). For example, EP A2 posited that a combined approach was the 'most effective way' of obtaining ‘more and more use of internal audit’ work by external audit. CAE A and C regarded *a silo approach to assurance* as the opposite of a combined one. CAC A used different terminology; he contrasted an ‘isolated’ assurance approach against an ‘integrated’ and ‘holistic’ one. CFO B explained that ‘there needs to be [a] *very clear and detailed understanding about what each other would be doing*. And in that process … external audit can place a lot of reliance on internal audit because it is sort of really a combined assurance programme’.

From a MORE reliance perspective, the participants linked a combined approach to assurance to *synchronising stakeholder groups’ assurance needs and responsibilities*. CAE B explained that implicit in a combined approach was ‘quite a bit of work … to understand all the *key risks* and who gives assurance on that’. Consequently, triangular participation by management, internal and external audit when allocating responsibilities and setting out an *integrated risk and assurance view*, mitigated engagement risk. CAC A relayed that the combined approach had raised the ‘credibility’ of internal audit work, as ‘it … forced the various assurance providers and the role players … to get together constructively’.

EP E1 found that the combined approach to assurance *mitigated engagement risk* as it ‘forced [external audit] to work very closely with [internal audit]’ (a) to develop a shared understanding of the split in focus of internal audit plans between ‘financial’ and ‘operational’ controls, (b) to determine how plans of ‘rotational’ internal audits covered ‘key’ controls of interest to internal and external audit and (c) to align individual audit plans. EP E1 explained that in such plans, *external audit planned reliance around internal audits’ ‘three-year rotational plan’ by using internal audit’s work on ‘key areas of control’ in years when internal audit audited them*. The *external audit team, on the other hand, audited those controls in the ‘years in-between’*. CAE A predicted that the King III recommendations about internal audit’s role in the ‘assessment of internal financial controls’ would result in internal audit performing more controls assurance work with a ‘financial’ focus relevant to ‘financial reporting’. Thus, he foresaw increasing opportunities for ‘external auditors looking to internal audit on what are the financial control issues that [were] picked up’ (CAE A).

From a LESS reliance perspective, EP A2 observed that *the combined approach to assurance was under-developed in less well-regulated organisations which had a* *weaker risk management function*. He added that, despite improvements since 2013, the combined approach was also under-developed in the large banking group he was auditing at the time of the interview in 2014 (EP A2). During a follow-up interview in 2019, CAE C concluded that the combined approach was still under-developed in his company.

CAE D proposed that changing from a silo approach to a combined approach to assurance would reduce the '*distance' between internal and external audit*, thus mediating MORE reliance. He claimed that this would 'bring [internal and external audit] a bit more together', implying that internal and external audit would be working closely together. EP A1 and A2 as well as CAE A and CFO E found that *moving from a silo approach to a combined approach required 'constant' triangular participation by management, internal and external auditors in combined assurance meetings*.

There was a noticeable difference in the motivation behind the combined approach to assurance in MORE and LESS reliance cases. From a MORE reliance perspective, EP B observed that *internal and external auditors have a history of working together well*, as this 'was always there'. In addition, he asserted that 'internal and external audit had been working well together pre-King', implying that *a voluntary, closer working relationship had been formed between the two groups over time*.

Data from LESS reliance cases indicated that *King III had triggered the change to a combined approach*. EP D2 advised that external auditors should change their approach in this regard. He maintained that reliance was 'easiest' when external auditors took a 'practical' approach to arrive at a 'base minimum' 'end result' where internal and external auditors shared with the audit committee a document showing how they had 'divided up the pie' of assurance work.

5.2.3.2 Internal and external audit working together

EP B indicated that internal and external audit working closely together when following a combined approach to assurance was the key mediator of aligned individual audit plans and hence, MORE reliance. EP B explained that working closely together meant that internal and external audit 'look at each other together, and when the [internal and external audit] plans are presented to the audit committee, we make sure that we have a combined approach'. Participants from MORE reliance cases averred that internal and external audit habitually worked closely together as a means for integrating work. By way of example, EP B explained that internal and external audit 'follow[ed] a very combined approach' even since 'pre-King' (EP B). This was confirmed by CAC B who commented that 'I haven't seen [the relationship between internal and external auditors] change dramatically, but they are working very closely together'. From case E, CFO E remarked that *internal and external audit had a 'history of working together well'*. This was corroborated by EP E2, who explained that internal and external audit followed 'an integrated audit approach; we work together in that sense'.

From a LESS reliance case perspective, CFO A, EP D2 and CAC D acknowledged improvements in cooperation between internal and external audit, albeit this *cooperation was still developing; the balance between internal and external audit work was not yet optimal as unnecessary duplication of audit work still occurred*. CAC D explained that 'people are more keen now to try and work together', while EP D2 relayed that 'it's still developing, but my sense is that parties sit together mutually and agree what needs to happen, and I think that's happening a lot more than what we used to see in the past'.

5.2.3.3 Internal and external auditors substituting versus complementing each other's work

In MORE reliance cases, participants revealed that internal and external audit habitually worked closely together to integrate work. They commented that when following a combined approach to assurance, optimal integration of work and minimising unnecessary duplication was their objective. Thus, *internal and external audit sought to substitute rather than simply complement each other's work* (EP B, E1, E2). EP E2 explained that his audit firm's methodology ensured that internal and external audit's work substituted instead of complemented each other. Thus, aligned individual audit plans indicated that external audit 'cover[ed] these areas here [while internal audit] cover[ed] those areas there'. Accordingly, work was allocated either to internal or external audit, but not both (EP E2). CFO B added that *internal audit made slight adjustments to the scope of their work earmarked for reliance, thus further assisting substitution*. He also noted that *internal audit identified overlapping work* *appearing in both teams' audit plans and, when appropriate, relied on external audit's work instead of duplicating the work.*

In LESS reliance cases, *external audit tended to follow a silo approach to assurance without integrating work or aligning their plans with internal audit*. By way of example, EP D2 explained that 'as external audit [thus on their own], also we want to try and see how we can actually use it [the work of internal audit] and what we can do and what they can do as well'. EP C conveyed that 'internal audit and external audit must complement each other; we mustn't duplicate the effort'. However, he added that *internal audit work was complementing rather than supplementing external audit work, as external auditors were seeking 'more comfort' to mitigate high external audit engagement risk*. EP C stated that he gained 'more comfort' if 'external audit has looked at it and internal audit has looked at it'. Thus, EP C confirmed that *no or limited reliance* did not yield reduced external audit fees. Unsurprisingly, in light of this statement, *CFO C and CAE C were dissatisfied with assurance efficiency, perceiving that unnecessary duplication of audit work had occurred* and *questioning what reliance was*, *particularly its wider definition as used by external auditors*.

5.2.3.4 The quality of the relationship between internal and external auditors

The participants from MORE and LESS reliance cases specified that the quality of the relationship between internal and external auditors mediated reliance (EP B, D2; CFO B, E). EP B declared that '*the predominant reason where [reliance] has worked better, is because the two divisions … have … [formed] a closer working relationship between [each other]'*. EP D2 observed that reliance increased as the quality of the relationship between internal and external auditors improved.

The participants from MORE reliance case companies (EP B; CAE B, E) associated internal and external audit as 'always' working closely together (EP B). They noted a voluntary, closer, professional working relationship formed between internal and external auditors, as the two groups had 'always had a very good relationship and collaboration' (CAE E). EP B observed that the quality of this relationship did not change much after the adoption of King III, as they had 'worked well together' before 2009. In contrast, however, CAC B and CAE B opined that the quality of the relationship had in fact improved over the years. CAE B pointed out that as the voluntary, closer, professional working relationship between the two parties developed, *the communication between internal and external audit became closer and more open*. This was because the propensity for *knowledge-sharing on areas of concern had increased* between internal and external auditors. CAC C / E ascribed this closer, professional working relationship to their mutual understanding of internal and external audit's interrelated but distinct roles. He observed that internal and external auditors' relationship was not hostile nor competitive, as there was '*total acceptance that they do different things*' (CAC C / E).

From a LESS reliance perspective, CAE A noted that he had a 'very open relationship' with the company's external auditors, as they 'talk to each other all the time'. CAE C asserted that the quality of the relationship between internal and external auditors 'is stronger now', saying that it was *a 'professional relationship'*. He added that 'there is no problem in terms of that'. Likewise, EP C declared that external auditors 'have a good relationship, a working relationship with [internal auditors]'. CAE C perceived that the improved quality of the relationship between internal and external auditors improved the quality of the communication between the two, with *a shift from greater formality to less formality*. This included 'email and telephone conversations', which gave him 'the *confidence* to call up the [external audit] partner' when required (CAE C).

The participants from LESS reliance case D held different views to those from case A and C about the quality of the relationship between internal and external auditors. While participants from case A and C perceived that it was 'good' and 'stronger', those from case D perceived that reliance and *the relationship between internal and external auditors was still developing*. Although CFO D described the relationship as 'quite good', EP D1 and D2 as well as CAC D opined that they expected the quality of the relationship and reliance would improve in future, as part of them pursuing 'combined assurance' (EP D1). Although CAC D asserted that 'we [internal and external auditors] can move together closer', he predicted 'it is going to be *an uneasy relationship'*. However, EP D2 stressed that this was dependant on external auditors' willingness to engage with internal auditors in an 'interactive session' on the basis of 'give and take' and viewing the two parties as 'a combined team'.

CAC D attributed MORE reliance and the improving quality of the relationship between internal and external audit to the heightened status and value added by internal audit arising from internal auditors' and the profession at large's improved professionalism. He surmised that reliance was increasing and would become 'an easier thing to achieve' in future, as 'the acceptance [of internal audit work] by external auditors is increasing'. CAC D had noticed improvements in the competence of internal audit teams and the standard of their work as well as changes in their approach to risk-based audits.

As confirmed by external auditors (EP A1, D1) from LESS reliance cases, CAE A observed the differential treatment of reliance work performed by in-house and outsourced internal audit service providers. This stemmed from a *habitual working relationship existing between the outsourced partners from Big 4 accounting firms and external auditors*. This was because the latter favoured reliance on outsourced internal audit work, particularly when the outsourced partner was a peer from a Big 4 firm. EP A1 bore out that external auditors could 'automatically' rely on the work of outsourced internal auditors from Big 4 firms, indicating that he had no doubt about the credibility of their work.

5.2.3.5 The working mindset of internal and external auditors

EP B explained that a team mindset mediated MORE reliance 'if [internal and external audit] can really work together as a team on the assurance'. He continued that MORE reliance was possible in case B as *having a team mindset changed reliance from being 'forced habit' into 'just the way that you work'*. From a LESS reliance perspective, CFO A referred to *a 'competitive mindset' prevailing between internal and external auditors*. EP D2 opined that *external auditors required a 'mindset change' about working with internal auditors* before MORE reliance could be achieved. EP D2 stressed the importance of internal and external auditors seeing themselves as a 'combined team', anticipating that companies might in future link reliance to 'the key performance indicators of internal audit'.

Participants from LESS reliance cases confirmed that an uneasy relationship existed despite the two parties 'evolving' towards reliance (CFO A). CFO A conceded that there was an 'evolution happening between the partners, between internal and external audit', although CAC D surmised that 'it is going to be *a slow movement towards some cohesion*, but not in a hurry'. Although CAE C acknowledged this evolving trend, *he expressed the wish that it would 'happen faster'*. He added that increasing *collaboration required regular meetings throughout the year* as internal and external audit 'realise that we need each other'.

Statements by participants from the LESS reliance cases provided *evidence of a continuing uneasy relationship despite progress made*. By way of example, EP D1 believed that '*rivalry'* between internal and external auditors undermined reliance. Thus, he concluded that reliance was difficult and challenging, with *tension* prevailing between the two stakeholder groups. However, CFO A perceived that *competition* between internal and external audit 'is normal human nature' as reliance implied external audit 'checking' the work of internal audit, with internal audit feeling the need to 'defend' themselves. CFO A suggested that internal and external audit should use *'constructive debate'* to 'cross' *the 'competitive' 'mindset'*.

CAE C made a strong case for internal and external audit changing to a team mindset to achieve MORE reliance. He speculated that *the effect of reliance on external audit quality would be positive if internal auditors shared their deep insights, gained from daily involvement in the business, with external auditors*. Consequently, CAE C proposed that the two teams should be working closely together, as 'the more we … talk to each other and rely on each other's work, the stronger you can become and also *learn from each other*'. In addition, CAE C urged *internal and external audit 'to work together' in the face of increasing assurance requirements and demands on internal and external audit*. EP D2 also viewed practising MORE reliance as a means of balancing increasing assurance requirements and demands on internal and external audit against *their budget / capacity / resourcing constraints*. He expected that it would 'help in the capacity side of both parties. It's going to help in terms of the comfort levels and *management should be getting comfort in totality* on their processes'.

The participants provided explanations of the meaning of a 'team mindset', which they saw as internal and external audit working as *a 'joint team'* (EP E2). They also viewed it as *'giving a combined assurance'* (EP B), often contained in *a single report to management and the audit committee on specific areas of an audit* (CAE B (2019)), *even though it was the external auditor who had signed the statutory auditor's report*

(EP B). By *having a team mindset*, *internal audit work would habitually form an 'integral' part of evidence on the statutory audit* (EP D2) and *an aligned 'audit methodology' on reliance areas*, as *internal and external auditors 'speak the same language*, we are pulling in the same direction' (CAE E).

From a LESS reliance perspective, *a competitive mindset* caused *some external auditors to contrast their superior professionalism against the inferior professionalism of the internal audit profession*. This was made with specific reference to *the external auditor's sole legal liability for the external audit*. Some external auditors also contrasted *the superior credibility of the external audit team's work against the inferior credibility of the in-house internal audit team*. EP A2 described internal auditing as an unexciting, dull profession, struggling to attract appropriately skilled individuals. EP D1 and EP C believed that external audit teams were simply better qualified than internal audit teams. EP C declared a preference for working with external audit's own teams, which he referred to as 'my own people'. He also questioned the credibility of work produced by the in-house internal audit team as he thought that loose-standing internal audit functions lacked opportunities for backing, support and benchmarking typically available to networks of global Big 4 accounting firms. Moreover, he felt that insufficient regulation of internal auditors by the internal audit profession was the norm. Consequently, atypical of a team mindset, EP A1 and D1 indicated that external auditors favoured reliance on outsourced internal audit work, particularly when the outsourced partner was a peer from a Big 4 firm.

CAE C believed that internal and external auditors had made progress towards a team mindset, however, he noted 'room for improvement'. EP D2 predicted that in future, internal and external audit would be working as a 'combined team and viewed as a combined team'. Reflecting a team mindset, CAC C / E mentioned that in MORE reliance case E, the external auditors from *Big 4 firms offered continuous development opportunities to the internal auditors of their clients*. These opportunities included access to seminars, conferences and benchmarking. CAE C and E confirmed that they made use of these opportunities.

In conclusion, the quality of the working relationship between internal and external auditors was the predominant mediator of MORE or LESS reliance through the influence on integration and alignment of internal and external audits. Mediation was conditional on mitigated engagement risk arising from synchronising the stakeholder groups' roles, interpretations, interests and practices, all of which influenced reliance. This made appropriate and fair reliance viable. Ultimately the quality of the working relationship between internal and external auditors mediated the practicability of appropriate and fair reliance.

5.2.4 Integrating work

The properties determining the integration of internal and external audits consider each stakeholder groups' views on (a) what reliance is (5.2.4.1), (b) internal and external auditors' commitment to reliance (5.2.4.2), (c) the nature of reliance work (5.2.4.3), (d) the cost-benefit of assessing internal audit and its work (5.2.4.4), (e) who is best placed to provide the assurance (5.2.4.5), (f) the influence of the external audit firm software and methodologies on reliance (5.2.4.6), (g) the overlap between internal and external audit work (5.2.4.7), (h) the duplication of audit work (5.2.4.8) and (i) assurance effectiveness and efficiency, including external auditors' propensity for protecting audit firm fee income (5.2.4.9). The quality of communication between internal and external auditors as well as oversight by the audit committee pervasively sustained these influences on MORE or LESS reliance. Table 4.13 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this category.

5.2.4.1 What reliance is

EP D2 placed reliance on a continuum with an extreme at either end: 'You're finding instances where the two extremes are happening where [external auditors] are reading [internal audit] reports and just putting it aside. [Then] there are those [cases] where the [internal audit] team is integral and part of the [statutory audit] process'.

In LESS reliance cases, *a wider definition of reliance was used*, with EP C lamenting that *internal and external auditors' definitions of reliance were misaligned*. CAE C was *dissatisfied with reliance. He believed that limiting reliance to reading internal audit reports to inform the external audit approach was not reliance*. In contrast, in MORE reliance cases, internal and external auditors practised a team mindset, meaning that *internal audit work formed an integral part of evidence on the statutory audit* (EP B, E1, E2; CAE B, E).

As further evidence, a wider definition of reliance was used in LESS reliance cases, with *some participants from all stakeholder groups considering that peripheral support by internal auditors was reliance work*. This meant that they viewed any support by internal audit as reliance work, irrespective of whether contributions by internal audit resulted in external audit modifying the nature or timing, or reducing the extent of audit procedures performed directly by the external audit team. Examples of support mentioned included: external audit relying on the system of internal control and following a combined audit approach (CFO A, D); external audit relying on internal audit reports to determine the external audit approach; external audit using system descriptions prepared by internal audit (EP A1); external audit relying on work performed by internal audit for the purposes of the Sarbanes Oxley Act (CFO D; EP C); internal audit extracting data for external audit's substantive procedures (CAE A); and internal and external audit collectively performing special purpose audit work outside the scope of the statutory audit (CAE A). When describing how he was practicing reliance, EP A1 commented that he sometimes 'forg[ot] to almost mention' to 'management' that external auditors used peripheral support by internal auditors, which he interpreted was evidence of reliance.

5.2.4.2 Commitment to reliance

In both MORE and LESS reliance cases, *all external auditors read internal audit reports and held discussions with internal auditors prior to external audits*. This contributed to external audit's risk assessments and informed their approach and scope (EP B, D2).

From a MORE reliance case perspective, EP E2 (like EP B, E1) expressed commitment to *optimal integration of internal and external audit work* and mentioned that *in his firm, reliance was an 'integral part' of the audit firm's audit approach and methodology*. Optimal integration implies 'maximum reliance' (EP B) 'whenever possible' (EP E1) occurred as internal and external 'pre-plan' reliance worked together (EP B) during structured, *upfront alignment planning discussions and workshops*. CAE B and E confirmed their external auditors' and their own commitment to reliance, and expressed their intention to increase reliance. These internal auditors described themselves as ‘very much a supporter’ (CAE B) and ‘a strong supporter’ (CAE E) of reliance. CAE B found that external auditors tried to use ‘as much of [internal audit work] as possible’; this meant that external auditors usually relied on internal audit’s control assurance work. However, CAE B stressed that reliance was conditional on the ‘level and standard’ of internal audit work. CAE B felt that practicing reliance on internal audit’s controls assurance work reduced external audit’s substantive procedures. CAC C / E expressed satisfaction with reliance in case C and E, noting that *external audit relied ‘as much as they can’*.

In the follow-up interview with CAE B (2019), he indicated that ‘there is definitely not similarities’ in the commitment to reliance of the new EP and the previous EP (both from the same Big 4 accounting firm), reiterating that ‘*I don’t think it’s consistent from one partner to the next … the experience between the two is very different*’. CAE B (2019) sensed that *external auditors’ commitment to reliance was decreasing in parallel with the increasing professional risks faced by external auditors*. CAE B (2019) also *predicted that compulsory audit firm rotation* (in terms of legislation requiring audit firm rotation for South African listed companies from 2023) ‘*is going to create a nightmare for combined assurance and reliance’ as the new firm will be unfamiliar with internal audit’s ‘approach’*.

In contrast to the MORE reliance cases, in the LESS reliance cases, *external auditors resisted reliance and thus practised no or limited reliance*. Although EP A1 remarked that ‘you’ve got to be able to rely’, EP A2, D1 and D2 were outspoken in their strong ‘reticence’ (EP A2) and ‘resistance’ (EP D1) to reliance. In the LESS reliance cases, EP A2, C and D1 stated that they *responded to pressure to increase reliance by ad hoc reliance attempts, focusing on those audit clients exerting pressure*. Thus, *pressure to increase reliance did not necessarily change external auditors’ general commitment to reliance*. CFO C and CAE C, who were *desperately seeking greater reliance, were frustrated with reliance happening so slowly* (CAE C). They were *struggling to make sense of no or limited reliance*. CFO C and D were *dissatisfied with assurance efficiency; they believed that external audit firms’ internationally developed audit methodologies hampered reliance*.

5.2.4.3 The nature of reliance work

EP B, E1 and E2 indicated that in MORE reliance cases, internal audit work habitually formed an integral part of evidence on the statutory audit. In these two cases, *reliance work included a large proportion of direct assistance work for statutory audit purposes, which was edited into internal audit plans*. *This included controls assurance work and extensive substantive procedures* (EP B, E1). EP B referred to direct assistance work as work that external audit 'mandated' internal audit to perform, while EP E1 and CAE E described it as work performed by internal audit 'on behalf of external audit' (EP E1). EP B explained that structured, upfront, alignment planning discussions and workshops made it difficult to distinguish between reliance work included in the normal course of internal audits and direct assistance work, as aligned planning 'makes the lines quite blurred'.

In contrast, in LESS reliance cases *external auditors limited reliance to reading internal audit reports and using peripheral support by internal auditors and made no or limited use of internal auditors for direct assistance work* (EP A1, A2, C, D1, D2).

Reliance in Case A

EP A1 mentioned that 'there was a slight pick-up in what has been done over the last five years in terms of the use of [internal audit work for] the external audit'. CAE A confirmed that reliance has 'come a long way from where it was'. EP A1 claimed that *(a) using internal auditors for direct assistance work would not improve assurance efficiency as it would not reduce external audit fees, (b) limited internal audit budget / capacity / resourcing precluded using internal auditors for direct assistance work and (c) internal audit's lack of access and understanding of the external audit firm software and methodologies hampered reliance*.

Responding to an interview question about the impact of reliance on external audit fees, EP A1 merely underlined external audit's 'maturity' in keeping external audit fees 'realistic'. However, he added that he had to remain aware of 'new [developments in auditing] that come out' as he could not afford to 'stop learning'; he had to respond to the 'challenge' by internal audit and management to increase reliance for reducing external audit fees.

CFO A and CAC A expressed satisfaction with external auditors' efforts to practise reliance in light of their sole responsibility for the external audit compared to the professionalism of the internal audit profession. CAC A explained that he 'engaged with the external auditors… off the record … they can tell me anything', which made him understand that 'this [non-reliance] is not personal, … it's the liability … it's not something that external auditors can say in public … think of it from their perspective, … they will stand in the dock [if there is an audit failure] and the internal auditor won't'. CFO A was content that internal and external auditors followed a combined approach to assurance, asserting that 'there must be intent [to rely] and I think the intent is [there] … we've got [a] combined assurance forum'.

<u>Reliance in Case C</u>

Internal audit in case C had mostly an operational focus, reducing the likelihood of reliance work (CFO C; CAE C). EP C expressed a lack of commitment to reliance. He indicated that he did not use internal auditors for direct assistance work as (a) limited internal audit budget / capacity / resourcing did not allow direct reliance work, *(b) he was weary of management expecting a reduction in external audit fees due to reliance and (c) he declared a preference for working with external audit's own teams rather than using internal audit staff.* Contradicting EP C's view, *CAE C stated the internal audit resource plans made provision for direct assistance work and he considered that internal auditors were doing direct assistance work in the form of annual inventory counts at 'different locations' in the format required by external audit.* EP C was seemingly protecting audit firm fee income by not relying, thus acting in self-interest rather than considering assurance efficiency. However, EP C indicated that external audit is 'now sitting with internal audit and say[ing] … where can we rely on you? Number one is … stock counts. If [internal audit] attend periodical stock counts then we can say okay, we can rely on it'.

CAE C expressed commitment to making reliance possible and desired a combined approach to assurance. He pointed out that internal and external auditors needed each other, that they should 'learn from each other' and could not 'afford the silo approach anymore'. He welcomed the improved communication between internal and external auditors, yet was frustrated as he struggled to make sense of no or limited reliance by external auditors.

Concerning the effect of reliance on assurance efficiency, EP C indicated that reliance on internal audit's work stipulated in the Sarbanes Oxley Act reduced the related external audit effort, although it did not reduce the fees for the external audit. However, on the client's account for assurance services, EP C marginally reduced the audit fee, and added that amount to the fee for work required in terms of the Sarbanes Oxley Act. This reallocation satisfied the audit client that reliance reduced the external audit fee.

EP C proposed that work should not be duplicated, explaining 'internal audit and external audit must complement each other'. EP C focused on the riskiness of reliance on internal audit work, thus he sought more comfort for mitigating high external audit engagement risk. He explained that external auditors trained internal auditors to perform work as part of their 'normal testing' on indirect taxes, to mitigate risks associated with indirect taxes. He confirmed that this work by internal auditors did not reduce external audit work; instead, it provided 'more comfort' as a result of both internal and external auditors working on certain areas, for example indirect taxes.

Responses by CAE C revealed that internal and external auditors' definitions of reliance were unaligned in case company C. Although CAE C mentioned that some reliance had occurred in case C, he was dissatisfied with it. He interpreted reliance as meaning internal audit work which habitually formed an integral part of evidence on the statutory audit. CAE C conveyed that 'there is a difference between taking into account for your [external] audit approach and relying'. Thus, CAE C opined that reliance was under-utilised as internal and external auditors' definitions of reliance were misaligned.

CFO C expressed dissatisfaction with reliance by external audit. In line with management's general focus on profit margins, he was hoping that reliance would assist in minimising the unnecessary duplication of audit work as he estimated that 20-30% of duplication of audit work occurred. Ignoring the distinct roles of internal and external audit, CFO C declared that he would 'either optimise [his] internal audit department or optimise [his] external audit department to get to the right level of control'. Furthermore, he expressed dissatisfaction with external audit's unwillingness to rely, despite the internal audit function's satisfactory rating received after the last external quality assurance review.

Reliance in Case D

Reflecting a lack of commitment to reliance, EP D1 declared that this was something 'which I've never done so far'. Responding to the interview question of whether he used internal auditors for direct assistance work, EP D1 responded: 'No, not at all'. EP D1 rationalised that no reliance, including no use of internal auditors for direct assistance work, was inevitable given the skills gap in the internal audit team. Thus, he declared a preference for working with external audit's own teams.

CAE D was clearly dissatisfied with the lack of reliance of external auditors in case D, admitting that it left him 'sad' and 'disappointed'. However, he conceded that internal audit's lack of credibility was the reason for limited reliance potential. CAC D expressed empathy for external auditors' sole responsibility for the audit, noting 'in principle, the external auditors are normally willing to and certainly cooperative in that regard'. However, CFO D called for an increase in reliance, noting his concern for external audit performing extensive substantive procedures in spite of focusing on controls assurance work, even when relying on internal audit's controls assurance work. Contrary to CFO D's views, EP D1 stated that external audit favoured performing extensive substantive procedures rather than carrying out controls assurance work and practising reliance.

5.2.4.4 The cost-benefit of assessing internal audit and its work

EP participants highlighted that reliance depended on the outcome of the assessment of internal audit and its work. EP E1 explained that the external auditor has to assess whether reliance is possible and needs to decide whether 'we [can] rely on this particular piece of work'. Participants from all the cases mentioned that the cost-benefit of assessing internal audit and its work influenced reliance. The requirements for these assessments are contained in external auditing professional standard ISA 610 (IAASB, 2018: ISA 610 (Revised 2013)). Since the external auditor retains sole responsibility for the audit irrespective of reliance, EP participants from all cases indicated that these assessments mitigated the effect of reliance on external audit quality and the external auditor's liability.

From a MORE reliance case perspective, EP B, E1 and E2 observed that *the presence of a stable internal audit team and well-developed internal audit processes in larger listed organisations meant that the benefit of assessing internal audit and its work usually exceeded the cost.* EP E2 qualified that reliance was costly in smaller organisations. In LESS reliance cases, EP D1 and C believed that *the fixed cost of assessing internal audit and its work exceeded the audit fee saving*.

Two CFO participants from LESS reliance cases disagreed as to the cost-benefit of assessing internal audit and its work. On the one hand, CFO D viewed *external auditors' assessments as onerous hurdles leading to over-auditing rather than reliance*. Thus, *he proposed that external auditing standards should be simplified to make reliance 'easier' and 'more efficient'*. In contrast, CFO C *perceived that the benefits of assessing internal audit and its work outweighed the costs*. He was willing to incur the cost of the 'cross-over report' as basis for ensuring that reliance was possible.

CFO C was frustrated as he struggled to make sense of no or limited reliance practised by external auditors. He hoped that the outcome of external audit's assessment of internal audit and its work would shed light on the reasons for limited reliance given that the external quality assessment reported that the internal audit function fell into 'the top quartile'. Thus, CFO C averred that he would gladly incur the cost of the ISA 610 assessment.

CAE A found that *cheaper and less formal assessments of work by outsourced internal auditors compared to in-house internal auditors were performed*. He rationalised that the latter, less formal assessments occurred as external auditors viewed those working in the internal audit services divisions of Big 4 accounting firms as their 'peers' whom they did not need to 'criticise'.

5.2.4.5 Who is best placed to provide the assurance

From a MORE reliance perspective, EP B indicated that to determine who was best placed to provide the assurance it was necessary to consider *the 'combined fee* *between internal and external audit', the 'level of assurance' and whether the internal audits had mostly an operational focus versus a strong financial focus*. EP B concluded that *all the stakeholder groups' focus was on ensuring assurance came from the most effective and efficient provider*. In addition, the reliance decision considered *the geographical location of audit sites and planned visits by internal audit to sites of third-party service providers of audit clients* (EP A2, B). CAE A suggested external auditors should be mindful of in-house internal auditors' superior understanding of the business and its key risks, fostered while they worked in the business full-time (CAE A).

In LESS reliance cases, on the other hand, *external auditors expressed a preference for working with external audit's own teams and favoured reliance on outsourced internal audit work, particularly when the outsourced partner was a peer from a Big 4 accounting firm*. This was the preferred course of action, as *opposed to placing reliance on in-house internal auditors* (EP A1, C, D1). However, CAE C opined that assurance efficiency benefitted when internal audit performed inventory counts. He reasoned that in-house internal auditors could perform inventory counts 'cheaper', meaning that they were the best placed assurance provider on inventory counts.

5.2.4.6 The influence of the external audit firm software and methodologies on reliance

From a LESS reliance case perspective, EP A1 and D1 explained that *internal audit's lack of access and understanding of external audit firm software and methodologies hampered reliance*. They elaborated that external auditors received training on the use of their firm-specific, internationally developed, access-restricted electronic audit methodologies and working paper packages (audit software). Audit software was generally not accessible by internal auditors or even known by them. EP A1 relayed that audit software enhanced external audit's assurance effectiveness and efficiency as the embedded project management tools allowed for continuous review of the team's work by the engagement partner and audit managers. Thus, EP A1 and D1 maintained that relying on work of internal audit, who did not use such software, would affect external audit's assurance effectiveness and efficiency negatively.

In MORE reliance cases, technological and methodological alignment was not an issue affecting reliance.

5.2.4.7 The overlap between internal and external audit work

CAC C / E and CAE A was of the view that all work of internal audit contributed to the external audit. However, CAC C / E explained that while all internal audit work could inform the external audit approach and scope, the distinct roles of internal and external audit limited overlap. From a MORE reliance perspective, EP B clarified that the '*planning' identified overlapping work in internal and external audit plans*. EP B and CAE B cautioned that *reliance should respect the distinct roles of internal and external audit*, as 'perfect alignment' of internal and external audit work might hamper fulfilling the scope and focus of internal audit's mandate and plans. In particular, it could jeopardise *internal audit's business-wide risk focus, concentrating on controls assurance work with mostly an operational focus*. Thus, EP B advised that balance was required when allocating internal audit resources to reliance work included in internal audit's mandate and plans. CAE C and B noted that *internal audit relied on certain work of external audit overlapping with internal audit's planned work too*.

From a LESS reliance perspective, EP A1 asserted that *the distinct roles of internal and external audit meant limited reliance was possible as overlap between the two was 'actually very small'*. EP A1 and C emphasised that overlap between internal and external audit work was *mostly possible on controls assurance work* as internal audit plans usually excluded work on 'financial reporting'. From a LESS reliance non-EP perspective, *management and some audit committees believed that internal audit was there to reduce external audit work and fees*. By way of example, CFO C claimed that internal and external audit work was interchangeable, thus suggesting that 'good reliance' was important, otherwise internal and external audit would 'just [be] duplicating all over the show'. However, EP D1 advised that despite potential overlap between internal and external audit work, external auditing professional standards required sufficient external auditor involvement in the audit of key risks, even when relying.

5.2.4.8 Duplication of audit work

All categories of participants representing all the cases expressed that minimising unnecessary duplication of internal and external audit work was a priority (CFO C; EP B, C, D1, E2; CAE D). These participants associated this objective with pressure to increase reliance, assurance efficiency, the overlap between internal and external audit work and, ultimately, stakeholder groups' satisfaction with reliance. Thus, CAC C / E advised that *internal and external audit should 'get as much cross-coverage as possible', instead of duplicating audit work*.

From a MORE reliance case perspective, EP B and CFO B stressed that despite relying, external audit might judge it necessary to obtain additional audit evidence by *duplicating or extending some internal audit work*. The objective of this would be *to ensure sufficient external auditor involvement in the audit of key risks*. Several other participants also understood some duplication of audit work might occur for this reason (CFO A, B; CAC C / E; EP A1, D1).

From a MORE reliance case perspective, EP B explained that the right mindset could *minimise unnecessary duplication*. This was because the *aligned individual audit plans*, developed during structured, upfront planning discussions and workshops, were the product of the two teams working closer together as part of a combined approach to assurance. CAE B added that such plans contributed to efficiency by minimising unnecessary duplication of internal and external audit queries raised with management, thereby reducing frustration. Lastly, EP B indicated that reliance could increase even more in case B should internal and external audit more closely to align the timing of audit work.

From a LESS reliance case perspective, CFO C explained that *unnecessary duplication occurred in the order of 20-30%*. He was therefore *sceptical about external auditors' commitment to reliance and felt dissatisfied with assurance efficiency*.

5.2.4.9 Assurance effectiveness and efficiency, including external auditors' propensity for protecting fee income

Participants from MORE and LESS reliance cases acknowledged that 'fee pressure' was a reality (CAC B; EP A1, B, C). CAC C / E declared: 'At the end of the day, your management always would be looking at their costs … they're not happy to pay internal audit, they're not happy to pay external. So, it's always going to be – where can we get it cheaper'. However, CAC D underlined that the main consideration should be assurance effectiveness when considering reliance, while assurance efficiency should always be a 'secondary factor'. He continued that stakeholder groups' diverse interests influenced their interpretations of assurance effectiveness and efficiency. Typically, in MORE reliance cases, *all stakeholder groups focused on balancing assurance effectiveness and efficiency, yet favouring effectiveness over efficiency* (EP B, E1; CAE B, E; CAC B, CAC C / E; CFO B, E).

In LESS reliance cases, *management and some audit committees strongly focused on increasing reliance to reduce external audit fees and work* (CAC C / E, D). Considering management's strong desire to minimise external audit fees, CAC D emphasised *the importance of the audit committee's oversight of assurance effectiveness and efficiency*. He rationalised that 'we just have to recognise that management does have a different agenda … they are also very cost-conscious and returns-conscious, so it is a balancing act to some extent and the audit committee obviously plays an important role here'. CAC C / E acknowledged that increases in the assurance costs of internal and external audit over the five to seven years prior to the interview had heightened the focus on audit efficiency.

Although CFO A considered reliance 'a good idea', he maintained that assurance efficiency should not only consider actual reliance, but suggested that *assurance efficiency assessments should also acknowledge internal audit's implicit contribution to external audit effectiveness*. He argued that 'internal audit is an expensive exercise'; 'the value of internal audit' comes from them seeing 'the underbelly of the organisation', which 'in itself is valuable for external audit'. The views of CFO B corresponded with those of CFO A. Although CFO B expected lower external audit fees from reliance, he asserted that the investment in internal audit would not result in a 'rand-for-rand' reduction in external audit fees. CFO B proposed *assurance efficiency assessments should rather ask 'if there [was not] an internal audit department, what work could external audit have done and now that there is [an internal audit function], what do they do now'*.

Concerning assurance efficiency, EP B and E1 confirmed that when the scope and focus of internal audit's mandate and plans incorporated *direct assistance work specifically included for statutory audit purposes, reduced external audit fees* did materialise. However, in LESS reliance cases, *no or limited reliance did not necessarily translate to reduced external audit fees* (EP A1, A2, C, D1, D2).

CAE B explained that reduced external audit fees were possible as reliance on internal audit's controls assurance work reduced external audit's substantive procedures. EP B contended that reliance 'can result in a reasonable decrease in [external audit] fees'. He noted that upon introducing reliance for the first time, the reduction 'can be significant … a saving of 10-15% would be significant'. However, he qualified that the impact of reliance on fees would depend on the relevance of internal audit work for statutory audit purposes and the competence of the internal audit team, particularly 'the ability [of internal auditors] to really do work on the financial side of things'.

In case B, the relevance of internal audit work for statutory audit purposes was met as most of its work had a 'strong financial focus' (CFO B). Moreover, internal audit specialists used 'data analytics' as a 'supplement' to ensure that their risk-based audits 'get to the real problems' (CAE B). EP A1 and C also alluded to *data analytics (performed by internal or external audit experts) as a means of balancing assurance effectiveness and efficiency* in light of audit fee pressure. CAC B suggested that *external audit should rely on internal audit's 'routine work', allowing external auditors to concentrate on more complicated or risky work*.

From a LESS reliance perspective, while EP A1 acknowledged fee pressure was a reality, he felt that management and the audit committee of case A understood that external auditors kept audit fees 'realistic'. However, CFO C and D as well as CAE C and D were *dissatisfied with assurance efficiency*. CFO C suspected that no or limited reliance meant that *some external auditors were unfairly acting in their own self-interest instead of considering assurance efficiency*. He moreover claimed that *external audit firms' internationally developed audit methodologies hampered reliance*. However, EP D1 opined that *management's general focus on profit margins meant that they put excessive focus on reducing external audit fees by increasing reliance rather than considering the effect of reliance on external audit quality and the external auditor's liability*. CAE C maintained that he contributed to assurance efficiency by remaining aware of planned external audit work; thus internal audit was minimising unnecessary duplication by relying on the relevant work of external audit.

CFO C described several *initiatives which were being implemented to address no or limited reliance* as a result of external auditors unfairly acting in their self-interest rather than considering assurance efficiency. These initiatives aimed to increase reliance through *(a) an external assessment of the internal audit function and its work to identify any shortcomings preventing reliance, (b) seeking guidance on the 'redesign' of internal audit tests to align the audit methodology on reliance areas to requirements for both internal and external audit and (c) open discussion of reliance in quarterly meetings with the incoming engagement partner, to actively promote alignment planning.*

CAE E also proposed that external auditors would probably prefer doing their own work to protect audit fee income, as reliance would reduce external audit hours and thus, external audit fees. From a LESS reliance case perspective, EP C confirmed that he was weary that management would once again expect a reduction in external audit fees due to reliance.

In conclusion, the working mindset between internal and external auditors facilitated the integration of internal and external audits. Together with alignment, integration made appropriate and fair reliance practicable, thus influenced stakeholder groups' interpretations of the appropriateness and fairness of MORE compared to LESS reliance.

5.2.5 Aligning work

The properties determining alignment of internal and external audits consider stakeholder groups' reciprocal influences on (a) alignment planning (5.2.5.1), (b) aligning internal and external audit's focus (5.2.5.2), (c) aligning internal and external audit's objectives and approaches (5.2.5.3), (d) aligning internal and external audit's methodologies (5.2.5.4), including the period covered by reliance work, sampling and selection, the response (time) to audit exceptions and the timing of internal audit work and (e) meeting the aligned audit plans (5.2.5.5). The quality of communication between internal and external auditors as well as oversight by the audit committee pervasively sustained these influences on MORE or LESS reliance. Table 4.14 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this category.

The participants explained the overall flow of the process of aligning work. As background to alignment, several participants mentioned that external audit received the internal audit plan and gave input on it (EP C, E2; CAE C, D; CAE C / E; CAC B). Other participants noted that internal audit reports were shared with external auditors (CAC A, C / E; EP B, E1; CAE A) as findings about the 'control environment [and] major risks' (CAE C) informed the external auditors' (a) risk identification (EP B, C, E2), (b) external audit approach (CAE A) and (c) reliance decisions (EP A1, B), including the specific audit work earmarked for reliance.

The participants enumerated the attributes of alignment planning. Particularly, internal and external auditors (a) entered into 'lengthy discussions' (EP B) (b) 'in the first quarter of the financial year' (EP D2), (c) compared their individual audit plans (EP B, D2; CFO A), (d) agreed on items selected for testing (including the key controls to be tested) (EP C, E1), (e) agreed on areas of planned reliance (EP C), (f) identified assurance gaps (CAE B; EP B) (g) and overlaps (EP B). Specific attention was given to planned internal and external audit work on (h) new areas requiring audit attention (CAE B), (i) key risks identified by the internal and external auditors (CAE A, D; CFO E; EP B, D2), (j) key processes (CAE A; EP B), (k) key controls (CAE A; EP B) and (l) 'areas that [external audit] felt uncomfortable with (CAE C).

Furthermore, internal and external auditors discussed (a) 'the findings coming out of internal audit work' (CFO A), (b) other pertinent information about the organisation which might affect audit risk (CAE C), (c) the areas internal auditors planned on covering (EP B, D1), (d) the areas internal auditors did not plan on covering (EP D1), (e) the areas external auditors planned on covering (EP B, D1), (f) the areas external auditors did not plan on covering (EP D1), (g) the areas of importance to external auditors (EP C), (h) the areas that the external auditors wanted internal auditors to cover (EP D1, E2), (i) the areas that management wanted internal auditors to cover (EP D1) and (j) the conclusions reached about the areas of reliance (EP C).

During alignment planning, the two parties discussed details of reliance, including (a) 'how external audit can rely on the work of internal audit' (EP D1), (b) 'the detail of who looks at what' (CAE B), 'what [internal audit] do versus what the external auditors do and when they actually do that' (CFO E), 'what [internal audit] are doing' (CAE D), assurance 'gaps' (CAE B, EP B), assurance 'overlaps' (EP B), (c) if the case company has 'got a new financial system that has been implemented, … how do [internal and external audit] approach it combinedly [to make reliance possible]' (CAE B), (d) 'year-end [external] audit programmes' (CFO E), 'before their year-end audit, [external audit] will interact with us' about the external audit plan (CAE C), (e), 'the quality of [internal audit] work that has been done' (CAE D), (f) the planned external audit approach (CAE C) and (g) 'where [internal audit] are [with their audit plan] and audits [they] are busy with' (CAE C).

CAE D noted that internal audit plans shared with external audit included information about 'the quality of the people that we have in the internal audit department and again who in the internal audit department will be doing work in the various areas that we have identified in our internal audit plan', thus aiding external audit's assessment of the expected standard of internal audit work.

5.2.5.1 Alignment planning

Participants representing MORE and LESS reliance cases underlined that MORE reliance required 'upfront' engagement in alignment planning by internal and external auditors (EP B, D1, D2, E1; CAE B, D; CFO A, C). EP D2 believed that in some instances MORE reliance was possible, as upfront planning by internal and external audit delivered aligned individual audit plans, while CFO A associated LESS reliance with *instances when the 'balance' between internal and external audit work was 'not 100%*'. EP D2 explained that LESS reliance could occur *as 'planning wasn't happening simultaneously or you have instances where [internal audit] are not willing to change [their plans].* EP D2 indicated that 'audit partners and the heads of internal audit' were involved in alignment planning.

In MORE reliance cases key attributes of alignment planning were *'structured' 'upfront' alignment 'planning' 'discussion[s]' and 'workshops', with 'lots of good communication' 'well before the beginning of our financial year'* (EP B, E1, E2; CAE B, E). By way of example, EP B explained that reliance 'is really about planning', while CAE B echoed that 'it is all about planning I would say, planning processes. It is about that upfront agreement'. Participants related that alignment planning required *internal and external audit to work closely together as part of a combined approach to assurance* (EP B, E1). Thus, *external audit understood 'what does internal audit do … and what do we do'* (EP B). In addition, *internal and external audit's aligned individual audit plans were approved simultaneously, 'well before the beginning of the financial year'*. The outcome of such planning was a 'reshuffle' of individual audit plans of internal and external audit, producing *reshuffled and aligned individual audit plans* (EP B). *Assurance effectiveness and efficiency benefitted from planning, as the two parties identified 'overlaps' in internal and external audit plans (EP B; CAE B) and minimised assurance 'gaps'* (EP B; CAE B; CAC B). CAE B explained that assurance 'gaps' implied that controls, even key controls, may have not been audited, as each assurer believed the other had audited it.

In contrast, although they were clearly aware of the importance of alignment planning for reliance, participants from all LESS reliance cases pointed out *insufficient alignment planning was occurring*. CFO A explained that some alignment planning was taking place, however, *the 'balance [between aligning internal and external audit work] is not 100%'*. CAE C and D found that there was progressively less alignment planning in their companies over the years prior to the interviews, while CFO C believed that *it was 'important [but] we don't spend enough time on it'.* CAE C ascribed decreasing levels of formal alignment planning to external audit's familiarity with the company. CAE C added that *internal audit was not sharing information about the focus of or progress made with internal audits during informal discussions with external auditors and there were no structured upfront alignment planning discussions and workshops*. CAE D observed that 'hardly any discussion' aimed at alignment planning occurred between internal and external audit, yet he was expecting that reliance should increase in the next financial year.

EP E2 underlined that *alignment planning did not imply that external auditors were prescribing to internal auditors what to do*. Rather, *after reviewing internal audit plans, external audit liaised with internal audit about incorporating specific additional work in their plans to increase reliance opportunities* (EP E2). EP A1 recalled instances when he had asked internal audit to perform 'additional work which they may have scoped out [of their internal audit plan]', to make reliance possible. Demonstrating the potential consequences of insufficient alignment planning for reliance, EP A1 indicated that such requests had to take into account external audit's reporting deadlines. EP D2 affirmed that internal audit usually obliged external auditors' requests for additional work in 'key areas', as internal audit had to provide 'comfort' to the board in those areas too.

The participants from LESS reliance cases offered suggestions to increase reliance. CFO A recommended that '*internal audit and … external audit need to get closer together to talk more actively during the year and plan better … on a continuous path of improvement*' (CFO A). He added that the two teams should engage in *retrospective 'pre-planning', reflecting on overlap between internal and external audit work in order to 'plan [reliance] around it for [the] next year*'. Furthermore, CFO A suggested that retrospective alignment planning should focus on *identifying direct assistance work, namely, 'tests that internal audit can do for [external audit] during the year that give you comfort in order to rely on their work'*. Although CFO A acknowledged that the *requirements for sufficient external auditor involvement in the audit of key risks* had to be met, he proposed MORE reliance, based on improved alignment planning, could increase assurance efficiency by reducing external audit fees. CFO A also linked alignment planning to assurance effectiveness, explaining that *value-adding improved assurance coverage* as time savings could be used to do 'the bits and pieces on other stuff that goes deeper and then, [internal and external audit] start *adding significant value to the business'*. EP D1 and D2 acknowledged the importance of alignment planning consisting of 'lots of discussion' towards 'finding a better solution'.

CAE E noted that reshuffled and aligned individual plans were approved by the audit committee as part of its oversight responsibilities. From a MORE reliance perspective, EP B observed that internal and external audit first discussed and agreed on their 'formalised', reshuffled and aligned individual audit plans with management, before *seeking simultaneous early audit committee approval of the reshuffled and aligned individual audit plans*. EP B specified that as the external auditor, '*I don't present the plan in isolation and neither does internal audit*'. In addition, he explained that the *reshuffled and aligned individual audit plans were presented to management and the audit committee 'well before the beginning of our financial year', indicating that external auditors moved their audit planning earlier than usual to accommodate alignment planning*.

From a LESS reliance perspective, CAE C noted that *the approval of internal and external audit plans by the audit committee did not occur simultaneously*, as internal audit was 'always kind of 12 months ahead of them'. EP D2 reiterated that LESS reliance was possible when *internal audit presented their plan for audit committee approval significantly before external audit*. He explained that 'you find that [external audit would] need to address it [audit work] … because the [internal and external audit] planning wasn't happening simultaneously'.

5.2.5.2 Aligning internal and external audit's focus

From a MORE reliance case perspective, EP B explained that alignment planning should ensure *a joint focus on key financial risks* in internal and external audit's reshuffled and aligned individual audit plans. He stressed that it was 'important that you work together … and you understand together what are the risks and how are those addressed and then, I think … once you understand that, … there can be a reshuffle'. As an example of such reshuffling, EP E1 clarified that *external audit planned reliance around internal audits' 'three-year rotational plan' by using internal audit's work on 'key areas of control' in years when internal audit tested them, while the external audit team audited those controls in the 'years in-between'* (EP E1).

While *insufficient alignment planning* was prevalent in LESS reliance cases, CAE C used *external audit's management letters when doing risk assessments*, to make sure 'there is nothing critical that we [internal audit] miss … to make sure we cover all the basis [risks]'. EP C was of the opinion that internal audit only used the company's 'risk register' for determining the focus of internal audit plans.

5.2.5.3 Aligning internal and external audit's objectives and approaches

MORE reliance was possible when *internal and external audit's aligned approaches concentrated on controls assurance work on key risks* (EP B, E1; CAE B, E). *LESS reliance was possible when internal audits followed a simple transactional approach* (EP C).

Participants from LESS reliance cases accentuated internal and external audit's *unaligned objectives and approaches*. These participants opined that *different sets of professional standards accommodating the distinct roles of the two teams complicated reliance*. Consequently, CAE A and CAC A found that reliance depended on *internal audit's compliance with external audit's professional standards*. However, CFO A asserted that using the same professional standards for both types of audit was inappropriate as each profession had unique objectives reflecting their distinct roles. CAE C posed 'it is difficult to really match those [differing] approaches completely because the viewpoint [objectives] [of the two] is different'.

While participants from the MORE reliance cases also alluded to differences in approach, they would 'discuss' this when aligning their objectives and approaches (CAE B; EP E1). CAE B noted that '*discussion' fostered a shared understanding of their respective objectives and approaches, allowing them to identify areas where external audit was inadvertently performing extensive substantive procedures in cases where reliance on internal audit's controls assurance work should be possible*.

5.2.5.4 Aligning internal and external audit's methodologies

The participants used the term 'methodology' when referring to detailed audit procedures and related decisions of internal and external audit. Four specific aspects of these methodologies critically influenced reliance, namely, (a) the period covered by audit work, (b) sampling and selection, (c) response (time) to audit exceptions and (d) timing of internal audit work.

From a MORE reliance case perspective, CAE B acknowledged that reliance required an aligned audit methodology on reliance areas. He remarked that *internal audit 'needs to do [audit work] to a level and standard that [external audit] can rely on'*. CFO B mentioned that *internal audit identified opportunities for 'slightly' changing internal audit work to improve reliance*.

From a LESS reliance case perspective, EPs explained that *methodological differences between the two types of audit limited reliance*. However, CFO A and C *criticised external auditors for using methodological differences between internal and external audits 'too quickly'; they viewed these as 'ridiculous' excuses for not relying*.

CFO A suggested that *'agreeing upfront'* would assist in aligning the two methodologies.

CAE C communicated internal audit's methodology with external audit, who then provided input and recommendations. However, he observed that this type of alignment was not always possible. He cited external audit's use of materiality limits to determine sample sizes as irrelevant to internal audit, who usually 'audit a full population'.

(a) Aligning the period covered by reliance work

Participants from MORE and LESS reliance cases mentioned that the period covered by internal audit's control testing 'critically' (CAE C) influenced reliance as it 'could lead to a constraint between internal audit and external audit' (EP B). While internal audit usually tested the operational effectiveness of the full population of a control over a two- or three-month period of the year, external auditing standards required testing each control over the full period of intended control reliance, on a sample basis (EP B, C, D2; CAC C / E; CAE C). Although the participants mostly referred to 'timing' issues, their descriptions of the problem revealed that they were referring to the misalignment of the period covered by reliance work.

From a LESS reliance case perspective, EP D2 explained that *dissimilarities between the period covered by internal and external audit work placed external auditors in a 'predicament' as reliance 'doesn't necessarily help' audit efficiency*. However, CFO C suggested *external audit should cover the period excluded from internal audit work instead of repeating work on the part of the year covered by internal audit*. Echoing this suggestion, EP D2 recommended that adopting a 'combined approach' to assurance could assist in aligning the period covered by reliance work, where internal audit 'would say, well, we'll do the first half of the year, [external audit] will do the second half of the year'. However, CAE B claimed that such 'top-up' by external audit of the period covered by internal audit to the full financial year was no longer allowed in terms of a 'new [external audit] standard [ISA 610 (Revised 2013)]'. He contended that this change meant that external audit would 'have to do all the testing [completed by internal audit on a part of the financial period] over again'. EP B confirmed CAE B's opinion, noting that 'what has made [reliance] slightly harder for some companies is that … [external audit] would require [internal audit] – if they are doing control testing for us – to cover the majority of the period'.

From a MORE reliance case, EP B explained that *timeous alignment planning assisted in moving internal audit work earmarked for reliance to 'the latter part of the year', thus ensuring that internal audit covered 'as much of the financial year as possible'*. EP C observed that MORE reliance occurred in companies reporting in terms of the Sarbanes Oxley Act, as their internal audit was required to test controls over the whole financial period.

(b) Aligning sampling and selection

The participants highlighted that reliance depended on internal and external audit's aligned sampling and selection of reliance work, particularly how internal audit determined the extent of tests, sample sizes and selection of audit items. CAE B emphasised that 'the main critical thing that is a maker-breaker [of the reliance decision] is the sampling methodology'. CAE A and EP E2 indicated that *reading internal audit reports improved external audit's understanding of the effectiveness of internal financial controls as a basis for the external audit approach and sample sizes*. EP E2 explained that 'if there's no weaknesses [identified in internal audit's findings], obviously our risk is lower, our sample sizes will be low as well'.

From a MORE reliance perspective, CFO E confirmed that *internal and external audit engaged early on the extent of tests, sample sizes and audit items selected for audit, based on knowledge-sharing of key risks*. EP E1 and D2 stressed that aligning sampling and selection of reliance work demanded 'discussion with [internal audit] long before they started planning that audit … to ensure that in that planning we were able to influence [internal audit's] sample sizes and selection'; otherwise, external audit would be 'unable to use it'. CAE A also found that external audit would 'inform' internal audit when they needed to 'extend testing on the basis that [we] picked up issues or control failures'.

From a LESS reliance perspective, EP C claimed that 'there's push back from internal audit, that's their way'. Thus *external auditors were unable to 'persuade' internal auditors to increase their sample sizes*. However, CAE C countered that internal audit would do ‘whatever we can do to assist them to rely better’. CAE C specifically noted that *he adjusted internal audit sample sizes to improve reliance, ensuring external audit’s minimum sample size[s] were met*.

In instances where ‘controls are good’, EP A1 and EP D2 *determined the net sample size for testing by the external audit team by deducting the number of tests conducted by internal audit from the total sample size required for their purposes. They conveyed that they ‘added on an additional sample’, comprising the number of reliance items requiring ‘reperformance testing’*. EPs from MORE reliance cases did not follow this approach, possibly as reliance work chiefly consisted of direct assistance work, in accordance with alignment planning. Thus, external auditors did reperformance tests but did not extend sample sizes as direct assistance work was done to external audit requirements.

EP E1 and CAE C mentioned that external audit shared their materiality levels with internal audit. External audit generally determined their sample sizes based on pre-determined materiality levels. However, CAE C explained that materiality levels were of lesser importance for internal audit’s controls assurance work.

(c) Aligning response (time) to audit exceptions

The participants explained that internal audit’s response to audit exceptions differed from external audit’s thus influenced reliance. EP A1 commented that external audit teams would ‘*automatically know* … it is just the next step in that process … we’ve got to expand our sample’ in response to audit exceptions (ineffective controls). External audit would conduct limited further testing of the control, not ‘retest[ing] [the whole population]’ of controls assurance work (EP A1). Rather, they *changed to extensive substantive procedures*. Conversely, *internal audit would typically ‘test everything’, meaning that they tested the full population of the related control* (EP A1)

EP E1 observed that the difference in internal and external audit’s response time to audit exceptions complicated reliance. He clarified that internal audit’s response to audit exceptions could be referral to management and follow-up by internal audit in terms of their ‘rolling plan’, while external audit required evidence sooner, as audit conclusions should be made in time to meet their reporting deadlines. CAE B and C confirmed that internal audit's response to audit exceptions was drawn out. CAE C added that internal audit's response was testing the 'full population' or engaging an in-house or outsourced 'forensic audit' for investigating the exceptions. CAE B explained that internal audit did not pursue exceptions but reported them to management, who had to 'fix it'. Internal audit also reported exceptions to the 'risk management function', who performed 'root cause analyses' and updated the 'loss register'. Internal audit would then obtain confirmation every quarter from management about progress in addressing the problem and performed follow-up tests in accordance with the planning of internal audit's risk-based audits (CAE B).

EP A1 explained that the part of the financial year left for management to redress exceptions and for internal audit to test those redressed controls determined whether reliance was possible on internal audit's follow-up tests. However, he pointed out that *when the end of the financial year was approaching and exceptions were not appropriately redressed, external audit needed sufficient time to perform alternative audit procedures in response to the risk exposure, which could make reliance impractical*. Thus, the point in time in the audit when internal or external audit identified control weaknesses affected external audit's response and reliance decisions as external audit had to meet its deadlines.

(d) Aligning the timing of internal audit work

In LESS reliance cases, the participants highlighted that the timing of (internal) audit work influenced reliance, explaining that 'if the timing is not there … you're not going to achieve [reliance]' (EP D2). CAE A found that reliance improved when internal audit performed reliance work closer to the year-end, 'in the last quarter of the financial year'. Thus, CAE C planned work he expected external audit could rely on 'as close as possible to year-end' to avoid (internal) audit's timing from preventing reliance. However, CAE C underlined that it was 'physically impossible' to postpone all internal audit work to the end of the financial year, thus in anticipation of reliance, he changed the planned timing of (internal) audit work *to ensure that internal audit's controls assurance work on key risks was done 'as close as possible to year-end'*.

EP A1 highlighted that two potential problems could arise when postponing *internal audit work towards the period end in the hope of increasing reliance*. First, *when* *internal audit findings contained control exceptions, the external audit approach should change to extensive substantive procedures. Yet, the short timeframe posed a 'huge risk' to external audit, who might not be able to complete those extensive substantive procedures in time to meet their deadlines*. Second, *when internal audit did not manage to complete reliance work postposed toward the period end, external audit would have to step in to complete it, again potentially hampering their ability to meet deadlines*. Thus, while internal audit believed that they could increase reliance by performing their controls assurance work 'as close as possible to year-end' (CAE C), external auditors cited the engagement risk inherent in this postponement as having the opposite effect, and effectively decreasing reliance (EP A1).

5.2.5.5 Meeting the aligned audit plans

In LESS reliance cases, the external auditors focused on the riskiness of reliance, particularly when external audit had to do or redo work initially earmarked for reliance. EP A1 underlined the importance of internal and external audit diligently meeting the aligned audit plans. EP A1 explained that 'if there were delays [in the timing of internal audit's performance of reliance work]', for example, *when internal audit prioritised ad hoc work for management due to changing the internal audit plan for accommodating 'specific requests', external audit had to do work initially earmarked for reliance. This had repercussions for meeting external audit's deadlines*. EP A2 recalled *instances where the external audit team had to redo reliance work after finding that its credibility was lower than initially anticipated, with repercussions on audit effectiveness and efficiency, including for meeting external audit's deadlines.*

In MORE reliance cases, the participants did not identify meeting the aligned audit plans as an influence on reliance.

In conclusion, the working mindset between internal and external auditors facilitated the alignment of internal and external audits. Combined with integration, alignment made appropriate and fair reliance practicable, thus influenced stakeholder groups' interpretations of the appropriateness and fairness of MORE compared to LESS reliance.

5.2.6 Overseeing reliance

Oversight of internal and external audit, including reliance, had an extensive influence on reliance. The quality of oversight as well as the quality of communication about reliance and coordinating work had a strong impact on either MORE or LESS reliance. The properties related to oversight were (a) audit committee oversight of assurance effectiveness and efficiency (5.2.6.1) and (b) the audit committee's inherent strength and closeness to the business (5.2.6.2). Table 4.15 contains a summary of the properties, dimensions of MORE and LESS reliance, concept indicators and illustrative quotations of this sub-category.

5.2.6.1 Audit committee oversight of assurance effectiveness and efficiency

Participants from all the cases underlined that the assurance context created by effective audit committee oversight influenced reliance. Audit committee oversight included separate 'closed sessions' (CFO B; CAE A) with the two teams before every audit committee meeting (CAC A, B). CAE E stressed the importance of audit committee oversight, stating that it 'sets the tone' of governance, while EP D2 believed that it was 'intrinsic' to reliance, as audit committees required internal and external audit 'to come together'. Thus, EP D2 described audit committee oversight as 'the thread that binds [a combined approach to assurance]', ensuring that both auditors were 'on the same page and not misalign[ed]'. This was because planning identified any overlap in plans, while minimising assurance gaps. EP C mentioned that audit committees expected external auditors should practise reliance to achieve reduced external audit fees while minimising unnecessary duplication.

Historically, the overarching *need for audit committee oversight arose from management having a general focus on profit margins, meaning that they did not always recognise the value of investing in internal and external audit as well as internal controls* (CAC C / E). From a MORE reliance perspective, CAE B (2019) experienced a change in management's attitude, noting that management had recently realised that they should balance profitability and good governance.

The participants from most cases confirmed that audit committees understood their oversight role and balanced the oversight of assurance effectiveness and efficiency.

In particular, some participants (EP A1, A2, D1, E1) confirmed that audit committees understood the need for balancing the effect of reliance on external audit quality with pressure to increase reliance despite their quest to reduce external audit fees. EP A1 ascribed the 'reality check' displayed by audit committees to the 'global financial crisis'. EP A1 explained that the CEO and audit committee even requested external audit to increase the scope of work in certain areas, while EP D1 noted some audit committees valued obtaining assurance in the same area from the distinct perspectives of internal and external audit.

Participants from MORE reliance cases noted that audit committee oversight of assurance effectiveness and efficiency mitigated engagement risk, *balancing management's pressure to increase reliance to reduce fees against the effect of reliance on external audit quality and the external auditor's liability*. EP B pointed out that *audit committee oversight emphasised a combined approach to assurance as a means for achieving assurance effectiveness, including minimising assurance gaps and improved coverage*. EP E2 explained that King III focused attention on strong internal financial controls, a strong internal audit function, and a combined approach to assurance as sources of comfort to audit committees.

CAE B indicated that King III raised audit committees' awareness of their role in a combined approach to assurance, resulting in *more formalised oversight of reliance* (CAC C / E). CFO E highlighted that 'audit committee and board buy-in' and 'the audit committee chairperson's open support for and direction' was crucial for *synchronising stakeholder groups' assurance needs and responsibilities* as part of a combined approach.

Concerning management's influence on internal controls, CAE C experienced audit committee oversight *balanced management's decisions about investments in strong internal financial controls*, considering the determined risk 'tolerance level'.

With regard to internal audit, audit committee oversight *supported a strong internal audit function*. At an overall level, the audit committee *approved the internal audit budget* / capacity / resourcing (CAC A, C / E). (CAC A, B, C / E; D). CAE C as well as EP D1 and E2 credited King III requirements and training provided to management and audit committee members with their improved appreciation of the value of internal audit and the consequent improvements in internal audit budget / capacity / resourcing.

The clear focus of the audit committee's oversight of internal audit was on *keeping internal audit work relevant and credible by balancing management's influences*. To ensure the relevance of internal audit work, audit committee oversight *included approving changes to the scope and focus of internal audit audit's mandate and plans* (CAC A, B, C / E, D; CAE C; CFO E; EP E2). EP D1 found that audit committees and management of larger organisations had a better understanding of the typical scope and focus of internal audit mandates and plans than those of smaller organisations.

Audit committees particularly *considered internal audit's ability to perform risk-based audits* in light of the influence of management pressure on internal audit to perform special investigations and *ad hoc work for management* on internal audit budget / capacity / resourcing (EP B; CAC A, D). EP B and C noted that even when internal audit planned their work in conjunction with management, the audit committee approved internal audit plans.

To ensure the credibility of internal audit work, audit committee oversight focused on (a) *evaluating the competence of the internal audit team on an annual basis* (CAC C / E; EP D1); (b) supporting the independence of internal audit by *giving the chief audit executive direct access to the audit committee* (CAC D; CFO B); (c) monitoring the outcomes of external assessments of internal audit quality (CAC A, B, C / E, D), and (d) *monitoring whether internal auditors were meeting their plans* (EP B).

With regard to external audit and reliance, CAC D explained that audit committee oversight should balance management's influence on increasing assurance 'efficiency' versus external audit's concerns for 'effectiveness', including the effect of reliance on external audit quality and the external auditor's liability. Several EP and non-EP participants (EP A1, C, D2, E1, E2; CAC A; CAE C, D) described audit committee oversight of the external audit. Most EPs found that *audit committees exerted a degree of pressure to increase reliance* as they, like management, expected 'synergy' (EP C) between internal and external audit, expecting that increasing reliance would lead to reduced external audit fees (EP C and E2).

In particular, audit committees (a) 'challenge[d]' (EP A1, E1; CAC A) external auditors' reliance decisions, (b) 'monitored' reliance, requiring external auditors to 'formally' report on ‘the level’ of reliance at every audit committee meeting (CAE C), (c) required justification when reliance did not happen in areas where they had expected reliance to occur (CAE D), (d) required detail about reduced external audit fees from reliance (EP C), (e) required confirmation of communication between internal and external auditors (EP E2), (f) placed a premium on management’s role in risk management as part of a combined approach to assurance (CAC C / E) and (g) required verbal confirmation from internal and external auditors that their individual audit plans submitted for audit committee approval were aligned (CAE C).

Except for EP D1 and C for LESS reliance cases, most EP participants (EP A1, B, E1) experienced that *audit committee oversight was reasonable, accepting and understanding of external auditors’ motivations provided for planned and achieved reliance*. However, EP D1 found that *some audit committee members had a different ‘mindset’ about reliance; they were ‘tokens’ supporting management instead of accepting external auditors’ motivations provided for not relying*. EP D1 explained that ‘some [audit committees] are supportive, others are not. It just depends, some of the people have a totally different mindset … obviously [external audit is] at [the audit committee’s] mercy’. CAE C also mentioned that some audit committees were supporting management.

EP D1 elaborated that external auditors had two choices when pressure to increase reliance ‘forced’ their reliance decision – either they relied and then ‘live[d] with [the potential consequences of inappropriate reliance]’ or they ‘don’t do the audit [and lose the audit client]’. Thus, EP D1 predicted that a problem with external auditor’s liability might arise when external auditors ‘assume that engagement risk [inherent in relying]’ by giving in to pressure to increased reliance, to reduce fees for the external audit, despite concerns over the relevance of internal audit work and the credibility of internal audit work.

EP C indicated that audit committees *joined management in applying pressure to increase reliance on external audit*, due to a lack of understanding of *the distinct roles of internal and external audit*. However, CAE C opined that audit committees did understand the distinct roles of internal and external audit. In line with EP C’s view, CAE A mentioned that ‘there will always be misunderstandings and misperceptions’ by boards and management about each stakeholder groups’ assurance needs and responsibilities. He therefore conducted training on this topic at ‘the board induction session’.

5.2.6.2 The audit committee’s inherent strength and closeness to the business

The participants explained that effective audit committee oversight depended on the committee’s inherent strength and closeness to the business. The participants offered their insights about attributes contributing to audit committee effectiveness. EP B emphasised that ‘if you have an audit committee with the appropriate skills, then they can play a significant role in the assurance’. He continued that *a strong audit committee* with ‘appropriate skills’ possessed *a strong risk view grounded in business, financial and industry insights*; it was therefore able to balance oversight of assurance effectiveness and efficiency. Particularly, such skills and insights enabled audit committee members to ‘*ask the right questions of management as well as of internal audit and external audit*’ (EP B). EP D1 detailed that audit committee members with ‘*business sense*’, ‘*a general understanding of [accounting and auditing] standards*’ and *knowledge of governance requirements* are better equipped for their oversight role.

The participants also underlined that the audit committee’s *uncompromising emphasis on sound governance* influenced audit committee oversight. CAE B asserted that compared to ten years ago, the audit committee took its ‘role very seriously and *audit committee meetings are robust* and *there is a lot of discussions about things that are happening and they are concerned about’*. This was confirmed by CAC B, who noted that his audit committee ‘put a lot of emphasis on corporate governance and the way things are working properly’. CAE E also mentioned that the composition of his organisation’s audit committee complied with best practice, thus it ‘ticks all the boxes’. EP A1 expressed that ‘the boards of companies and banks in particular, … realise[d] the huge, huge responsibility on them’. Similarly, CAC A pointed to the importance of *strong upfront ‘succession-planning’ of audit committee members*. In contrast, however, EP D1 opined that some *weak audit committees consisted of ‘tokens’ providing symbolic oversight*.

CAC A perceived that the audit committee’s closeness to the business enabled effective oversight. From a MORE reliance perspective, CAE B acknowledged internal audit’s role in fostering the audit committee’s closeness to the business. *Internal audit* *supplied the audit committee with documentation ‘packs’ and shared their insights and concerns about ‘what was really happening’ with risks and controls in the entity with audit committee members during ‘closed sessions’ without management present* (CAE B).

Furthermore, CAE B described the reciprocal effect of the status of and value added by internal audit on the audit committee’s closeness to the business, strong risk view grounded in business insight and audit committee oversight. Particularly, as he received and reviewed all minutes of the company’s executive committee, *he could ‘tell them [the audit committee] how to direct their questions [to management during audit committee meetings]’*. CAE C ensured the audit committee’s closeness to the business by sharing information about ‘*outstanding [internal audit] findings*’, the ‘status’ of the internal audit function, particularly *whether ‘management [were] taking [internal audit findings] seriously*’ with the audit committee.

Confirming the views of CAE B, CFO B (who was previously the external audit engagement partner of company B) asserted that the audit committee’s closeness to the business and strong risk view enhanced audit committee oversight. As audit committee members knew ‘what should be addressed’, ‘good and active debate’ was the norm during audit committee meetings. He attributed the audit committee’s understanding of the company’s risks to *shared membership of the company’s audit and risk committees*. CAC B confirmed that *the audit committee had joint meetings with internal audit and risk management before every quarterly audit committee meeting*, which *fostered audit committee members’ strong risk view* grounded in business insight.

Providing further insight, CAC C / E argued that *knowing and understanding the management of the company* was pivotal in ensuring his closeness to the business and strong risk view. He believed that the audit committee’s ‘real protection’ did not come from assurance provided by internal audit, but rather from *the trustworthiness of management* who directly influenced the inherent and control risks in the organisation’s control environment. In this regard, EP A1 recalled instances where the audit committee of case company A had ‘asked the internal audit to expand their procedures and do the extra bit’ on high risk areas identified by external auditors.

These requests formed part of the audit committee’s attempts at gaining closeness to the business and a strong risk view.

In contrast to specific attempts at advancing the audit committee’s closeness to the business in MORE reliance case B, CAC A (from a LESS reliance case) had experienced *difficulty in gaining closeness to the business* when fulfilling his role as audit committee chairperson. He found that *management viewed ‘healthy tension’ occurring as part of audit committee oversight as ‘interference’*. *When the audit committee sought clarifications to attain closeness to the business, it was labelled as ‘an activist audit committee’ by management* (CAC A). CAC A attributed such labelling to *management’s misunderstanding of stakeholder groups’ assurance needs, risks and responsibilities*. Consequently, CAC A pleaded that ‘management should understand that when [the audit committee] interrogates, we probe and we challenge, that we’re not interfering’, but seeking closeness to the business and a strong risk view for effective audit committee oversight.

CAC A linked the audit committee’s closeness to the business to the value added by internal audit reports, particularly the way in which internal audit reported its findings. He clarified that audit committees received ‘data dumps’ in internal audit reports. CAC A suggested that *internal audit reports should include detail needed for ‘focused conversation’ about what was reported, what its impact was and who should take responsibility for addressing it*. Thus, CAC A’s unmet desire was accessing such an internal audit report and engaging in an in-depth discussion on this with the chief audit executive. From a MORE reliance perspective, EP E1 explained that internal audit reports tabled at audit committee meetings usually covered key findings, showing progress made by the business in implementing corrective action.

In conclusion, the quality of audit committees’ reliance oversight significantly balanced the effectiveness and efficiency of assurance provided by internal and external audit. As such, oversight created a context sustaining appropriate and fair reliance influencing stakeholder groups’ interpretations of the appropriateness and fairness of MORE compared to LESS reliance.

Combined, the conceptualisations of the dimensions influencing MORE and LESS reliance of each substantive category’s and sub-category’s properties explain how stakeholder groups achieve mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision. These conceptualisations form the properties of the theoretical constructs of the emergent theory explicated in Chapter 6.

5.3 CONCLUSION

This chapter presented the conceptualised and theoretically sorted data of this study in the format of six substantive categories and five sub-categories. These distinguished between stakeholder groups' roles, interpretations, interests and practices influencing MORE and LESS reliance. All substantive categories and sub-categories were central to the core category of this study as they explained how stakeholder groups achieved mutual agreement that reliance was appropriate and fair (balanced), whatever the reliance decision.

The conceptual dimensions of the properties of each substantive category and sub-category (indicated in italics in this chapter and summarised in tables 4.6 to 4.15 in Chapter 4) are carried forward into Chapter 6, where they are used to define and integrate theoretical constructs into the substantive theory emerging from this study.

CHAPTER 6

OUTCOME OF PHASE 3:

SUBSTANTIVE THEORY

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SUBSTANTIVE THEORY

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6.1 INTRODUCTION

Chapter 5 presented the analysed data of this study as six substantive categories and five sub-categories, structured under the six theoretical constructs of the theory proposed in this study. The chapter conceptualised and explained the properties and dimensions of MORE and LESS reliance of each substantive category and sub-category.

This chapter integrates the six theoretical constructs into a comprehensive holistic substantive theory of balanced reliance. The constructs of the theory are *facilitative communication*, *reciprocal synchronisation*, *a team mindset*, *habitual integration*, *fair alignment* and *balancing oversight*. The emergent theory explains how stakeholder groups achieve *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

The emergent substantive theory is presented first as a storyline, second as a visual representation depicting the propositions of the theory and third, as a thick description of each theoretical construct, with its definition and integration into the theory. Then, the constructs of the theory are compared to extant theories, specifically the stakeholder theory and the relational coordination theory, the summation model and organising framework developed from the most recent synthesis study on reliance and lastly, internal and external auditing professional standards.

6.2 THE MAIN STORYLINE OF *THE SUBSTANTIVE THEORY OF BALANCED RELIANCE*

In response to the research question – How can reliance on internal audit work by external auditors be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors? – this study proposes the following:

Stakeholder groups' *main concern* is *disconnect* between their reciprocal influences on reliance. Willing *reciprocal synchronisation* resolves disconnect between the stakeholder groups' roles, interpretations, interests and practices influencing reliance, rendering viable their *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. With *reciprocal synchronisation* as a foundation, a voluntarily formed *team mindset* is the predominant mediator of *habitual integration* and *fair alignment* of internal and external audit work. These co-variant conditions change stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* from being viable to practicable, as the disconnect between internal and external audits is resolved. Stakeholder groups' participation in *facilitative communication* and a strong audit committee's *balancing oversight* create the context for sustaining *reciprocal synchronisation*, *a team mindset*, *habitual integration* and *fair alignment*. The outcome is balanced reliance, all stakeholder groups *mutually agree that reliance is appropriate and fair, whatever the reliance decision*.

6.3. VISUAL REPRESENTATION OF THE PROPOSITIONS EMBEDDED IN *THE SUBSTANTIVE THEORY OF BALANCED RELIANCE*

Figure 6.1 below visually depicts the theoretical constructs of *the substantive theory of balanced reliance* and their interrelationships, explaining the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors on reliance.

The substantive theory of balanced reliance proposes the following:

Stakeholder groups' *main concern* is *disconnect* between their reciprocal influences on reliance. Disconnect increases engagement risk. Balanced reliance resolves disconnect, rendering viable and practicable all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

1. Willing *reciprocal synchronisation* (B) (depicted as the central upside-down triangle) between all stakeholder groups'
    a. assurance needs and responsibilities, and
    b. influences on
        i. the reliance environment,
        ii. the relevance and credibility of internal audit work for statutory audit purposes, and

iii. external audit quality and the external auditor’s liability

is a foundational condition for resolving disconnect between stakeholder groups’ roles, interpretations, interests and practices influencing reliance. Thus, stakeholder groups’ *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* becomes viable.

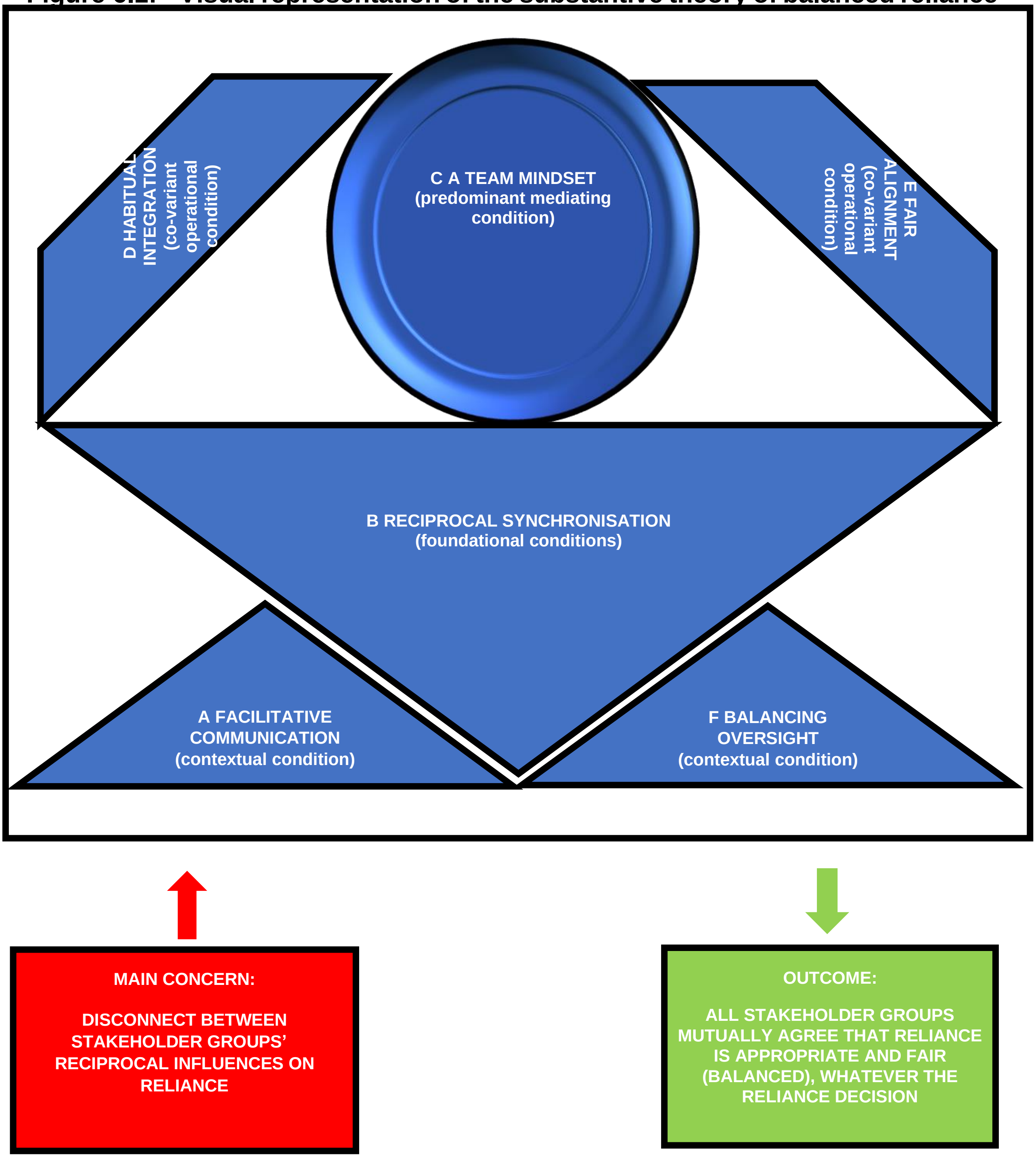
2. With *reciprocal synchronisation* (B) as a foundation, a voluntarily formed *team mindset* (C) (depicted as the circle balanced on top of the upside-down triangle) is the predominant mediator of
   a. *habitual integration* (D) of internal and external audit work, and
   b. *fair alignment* (E) of internal and external audit work,

   the co-variant conditions that resolve the disconnect between internal and external audits. These conditions change all stakeholder groups’ *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* from being viable to being practicable.

3. Stakeholder groups’ participation in *facilitative communication* (A) and a strong audit committee’s *balancing oversight* (F) (depicted as two smaller triangles keeping the upside-down triangle and all the structures above it in position) create a context sustaining *reciprocal synchronisation*, *a team mindset*, *habitual integration* and *fair alignment*.

The outcome is that *all stakeholder groups mutually agree that reliance is appropriate and fair (balanced), whatever the reliance decision*.

Figure 6.1: Visual representation of the substantive theory of balanced reliance



6.4 FOR EACH THEORETICAL CONSTRUCT: A THICK DESCRIPTION AND INTEGRATION INTO *THE SUBSTANTIVE THEORY OF BALANCED RELIANCE*

The theoretical constructs of *the substantive theory of balanced reliance* form an analytic account of reliance. These constructs are *A. facilitative communication, B. reciprocal synchronisation, C. a team mindset, D. habitual integration, E. fair alignment* and *G. balancing oversight*. Integrated into the theory, the constructs explain how stakeholder groups resolve *disconnect* between their reciprocal influences on reliance, rendering viable and practicable their *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. Thus, while increased engagement risk from *disconnect* is synonymous with *resisted reliance*, *balanced reliance* mitigates the risk. This, in turn, makes optimal *habitual integration* of internal and external audit work practicable. Below, thick descriptions define the six constructs, and explain their integration into the theory.

6.4.1 Facilitative communication (A)

In conjunction with *balancing oversight*, the context created by the quality of communication between stakeholder groups pervasively influences all other constructs of balanced reliance. *Unproductive communication* leads to *misunderstanding, a silo approach to assurance, resisted reliance* and *misaligned work* as the norm from *disconnect* between stakeholder groups' reciprocal influences on reliance. *Facilitative communication* is essential for sustaining *reciprocal synchronisation*, *a team mindset*, *habitual integration* and *fair alignment* as well as for resolving *disconnect.* Communication at two levels is essential – (A1) stakeholder groups' communication about planned and achieved reliance, and (A2) communication between internal and external auditors to coordinate audit work.

6.4.1.1 Stakeholder groups' communication about planned and achieved reliance (A1)

Unproductive communication about planned and achieved reliance (i) focuses primarily on assurance efficiency. Interactions are (ii) difficult discussions, including

(iii) interrogation, (iv) questioning and (v) challenging external auditors (vi) by management and some audit committees, who expect external auditors to provide detail about and (vii) action plans for improving assurance efficiency, and to (viii) justify objectively why they practise no or limited reliance. External auditors (ix) practise diplomacy, (x) providing very limited, generic written feedback and some informal verbal feedback about the outcome of the ISA 610 assessment and (xi) the reasons for no or limited reliance. This is done to preserve the relationship between internal and external auditors. Due to external auditors' limited communication about the reasons for no or limited reliance and (xii) a tick-box approach prevailing during reliance interactions, (xiii) management and internal auditors are often frustrated as they struggle to make sense of no or limited reliance by external auditors.

In contrast, all stakeholder groups' participation in *facilitative communication* about planned and achieved reliance (i) creates a context which sustains the *reciprocal synchronisation* of influences on reliance by the roles, interpretations, interests and practises of each group. *Facilitative communication* means that (ii) all stakeholder groups engage in (iii) extensive (iv) open discussions about planned and achieved reliance, and (v) focus on assurance effectiveness and efficiency, yet favouring effectiveness over efficiency. As a result, (vi) external auditors interpret management, the audit committee and internal auditors as being reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance.

6.4.1.2 Communication between internal and external auditors to coordinate work **(A2)**

Unproductive communication (i) between in-house internal auditors and external auditors (ii) sustains *disconnect* between internal and external audits, as the communication is (iii) forced and (iv) cautious. However, (v) consequent to automatic reliance on work of outsourced internal auditors from Big 4 accounting firms, (vi) communication between outsourced internal auditors and external auditors commences with an immediate reliance request from the newly appointed outsourced partner to the external auditor, (vii) followed by extensive upfront discussions to clarify mutual expectations.

In contrast, f*acilitative communication* (i) between internal and external auditors to coordinate work (ii) creates a context sustaining *a team mindset*, *habitual integration* and *fair alignment* as it is (iii) unrestricted, (iv) confident and (v) easy, consisting of (vi) open (vii) formal and (viii) informal communication (ix) as needed, (x) with frequent conversations and (xi) regular meetings throughout the year, (xii) covering knowledge-sharing on areas of concern, and (xiii) reflecting on lessons learned and ways to improve assurance effectiveness and efficiency.

6.4.2 Reciprocal synchronisation (B)

The reciprocal influences of each stakeholder group's roles, interpretations, interests and practices determine engagement risk. They are thus foundational conditions influencing reliance. *Disconnect* between the stakeholder groups increases engagement risk, causing *resisted reliance*. *Balance* and stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* only becomes viable if willing *reciprocal synchronisation* of stakeholder groups' influences resolves the disconnect between them. *Reciprocal synchronisation* considers (B1) each stakeholder group's assurance needs and responsibilities as well as the reciprocal influences of each stakeholder group on (B2) the reliance environment, (B3) the relevance and (B4) the credibility of internal audit work for statutory audit purposes and (B5) external audit quality and the external auditor's liability.

6.4.2.1 Each stakeholder group's assurance needs and responsibilities **(B1)**

Explanations dealing with (a) assurance meetings, (b) the distinct roles of internal and external audit and (c) pressure to increase reliance reveal insights about mutual (mis)understanding of each group's assurance needs and responsibilities.

Misunderstanding of each group's assurance needs and responsibilities is evident when (i) management meet separately with internal and external auditors about assurance plans and (ii) management and some audit committees perceive, through reliance, that internal audit should reduce external audit work and fees. They therefore (iii) exert pressure on external auditors to increase reliance. This includes (iv) pressure to change from a substantive to a combined external audit approach, focused on controls assurance work, especially (v) when management invested large amounts in internal control improvements. As (vi) external auditors often feel that management's pressure to increase reliance is inappropriate, (vii) they maintain that appropriate reliance is extremely difficult to achieve and (viii) they therefore mostly *resisted reliance* despite management's and some audit committees' pressure to the contrary. Thus, external auditors (ix) attempt to increase reliance on an *ad hoc* basis only on those audit clients exerting pressure.

In contrast, *reciprocal synchronisation* of all stakeholder groups' assurance needs and responsibilities implies (i) holding regular combined assurance meetings, (ii) with triangular participation by management as well as internal and external auditors (iii). This is to develop a combined assurance mapping, (iv) clearly reflecting stakeholder groups' shared goals and (v) an integrated risk and assurance view. As all stakeholder groups (vi) mutually understand internal and external audit's interrelated yet distinct roles, (vii) they agree neither internal nor external audit can substitute each other's role. Instead, (viii) their focus is on *balancing* assurance effectiveness and efficiency, yet always favouring effectiveness over efficiency.

6.4.2.2 The reliance environment (B2)

The reliance environment is determined by (a) the size and regulation of the organisation as well as the reciprocal influences of each stakeholder group's roles, interpretations, interests and practices (particularly that of management) on (b) the maturity of risk management, (c) the effectiveness of internal financial controls, (d) the structure of the internal audit function, (e) internal audit budget / capacity / resourcing, (f) the status of internal audit and the value it adds and (g) the profile and role of the chief audit executive.

Misunderstanding the reciprocal influences of each stakeholder group on the reliance environment, (i) which is particularly prevalent in smaller, less well-regulated organisations (ii) with a weak audit committee, implies that (iii) management's practices are usually profit-orientated rather than governance-focused and (iv) management and the audit committee lack an understanding of the distinct roles of internal and external audit and (v) the ideal scope and focus of internal audit mandates and plans. Management's (vi) insufficient budget allocation to governance mechanisms is reflected in (vii) a weaker risk management function which is not functioning optimally, (viii) weak internal financial controls that do not operate fully, (ix) less formalised use of internal audit with (x) the wrong person in the role of chief audit executive. The (xi) the risk of internal audit being discarded by management and the audit committee is high, thus (xii) internal audit's budget, capacity and resourcing are too limited to fulfil its mandate and plans, (xiii) given the conflicting demands on internal audit by too many bosses and (xiv) the required competence of the internal audit team. As (xv) internal audit is ineffective, (xvi) its reports contain the same simplistic recommendations every year and (xvii) management ignore internal audit findings and recommendations. Instability of internal audit mean (xviii) external auditors perceive the fixed cost of assessing internal audit and its work exceeds the audit fee saving and (xix) favour reliance on outsourced internal audit work, (xx) particularly when the outsourced partner is a peer from a Big 4 accounting firm, on grounds of their superior competence and independence.

In contrast, *reciprocal synchronisation* of the influences of each stakeholder group on the reliance environment, (i) which is mostly prevalent in larger, well-regulated organisations (ii) with a strong audit committee (iii) where management and the audit committee have a better understanding of the distinct roles of internal and external audit and (iv) the ideal scope and focus of internal audit mandates and plans. This implies that management in these organisations (v) realise they should balance profitability and good governance. Thus, (vi) they implement a strong risk management function with senior management collaboration, (vii) strong internal financial controls which function effectively for the entire financial period and (viii) a strong in-house internal audit function (ix) with a superior understanding of the business and its key risks. Management also supports the appointment of (x) a very strong head of internal audit who is (xi) a senior (xii) independent (xiii) influential (xiv) leader with (xv) business and (xvi) industry insights, (viii) and has (xvii) a commercial orientation, (xviii) hands-on assurance experience and (xix) qualifications, (xx) the ability to communicate and (xxi) contribute to the business at all levels and (xxii) to accept and (xxiii) drive change.

The chief audit executive (xxiv) with the support of the audit committee (xxv) balances internal audit's resourcing and work by (xxvi) negotiating sufficient budget and (xxvii) appointing a sufficient number of (xxviii) competent internal auditors, (xxix) using technology, including data analytics and (xxx) carefully considering opposing demands on internal audit resources, including by *ad hoc* work for management. This individual, (xxxi) who is appointed by the audit committee, (xxxii) has direct access to the audit committee, (xxxiii) the chief executive officer and (xxxiv) the chairperson of the board. In addition, this individual (xxxv) receives all minutes of executive committee meetings, (xxxvi) incorporates work on new and evolving risks in internal audit plans and (xxxvii) guides the audit committee about questioning management during meetings. Management allocate (xxxviii) realistic resourcing in line with internal audit's mutually agreed, realistic mandate and plans.

As (xxxix) internal audit is effective, (xl) its role as provider of assurance on combined assurance is more formalised and regulated and (xli) its reports contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems. As a result, (xlii) the chief executive officer and management openly acknowledge and support the value of internal audit to the business and (xliii) external auditors prefer relying on work of the strong, in-house auditors (xliv) rather than outsourced internal auditors as they perceive (xlv) the benefit of assessing internal audit and its work exceeds the cost.

6.4.2.3 The relevance of internal audit work for statutory audit purposes (B3)

The relevance of internal audit work for statutory audit purposes depends on the reciprocal influences of each stakeholder group's roles, interpretations, interests and practices on (a) the scope and focus of internal audit's mandate and plans, (b) the type of internal audit, (c) the internal audit approach, (d) collaboration between internal audit and risk management and (e) the external audit approach.

Misunderstanding the reciprocal influences of each stakeholder group on the relevance of internal audit work for statutory audit purposes means that (i) internal audit faces conflicting demands on internal audit resources (ii) by too many bosses, including, (iii) special investigations and *ad hoc* work for management and / or (iv) a large proportion of internal audit work has an operational focus. Moreover, (v) most internal audits consist of routine conventional rotational internal audits and random 'ticking and bashing', and (vi) risk management remain on the side, without mutual sharing of information on key risks between internal audit and risk management.

Consequently, (vii) internal audit work becomes irrelevant for statutory audit purposes and (viii) the external auditor performs extensive substantive procedures rather than following a combined audit approach.

In contrast, *reciprocal synchronisation* of stakeholder groups' influences on the relevance of internal audit work for statutory audit purposes means that (i) management, the audit committee and internal audit mutually agree on a realistic mandate and plans for internal audit (ii) which balances the benefit versus reward of work both included and excluded from internal audit's mandate and plans, (iii) by prioritising risk-based audits. Risk-based audits include(iv) testing of key and (v) evolving risks and (vi) process changes (vii) assessed while both internal and external auditors work closely together (viii) on joint risk assessments. As a result, (ix) internal audits cover key risks annually as part of a base audit plan, or (x) internal and external audit rotate coverage of key risks. Risk management (xi) and internal audit work closely together, meaning they (xii) share an integrated risk view and (xiii) external audits incorporate controls assurance work on key risks as part of a combined audit approach and / or (xiv) direct assistance work includes tests of controls and extensive substantive procedures. Consequently, (xv) internal audit work is relevant for statutory audit purposes.

Relevance improves even further when (xvi) internal audit performs work outside the typical scope and focus of internal audit mandates and plans captured in the definition of internal auditing. First, (xvii) while the typical scope and focus of internal audit mandates and plans defined by the profession concentrates on governance, risk management and internal control assurance work, reliance increases when a large proportion of direct assistance work (including controls assurance work and extensive substantive procedures) for statutory audit purposes is edited into internal audit plans during alignment planning. Second, (xviii) while the definition of the profession refers to internal audits with a business-wide risk focus, internal audits with a strong financial focus increase reliance. Furthermore, (xix) most reliance is possible at subsidiary level rather than at group level of larger listed companies. This distinction arises as internal audits at subsidiary level usually incorporate a large volume of audit work, in accordance with a transactional, end-to-end integrated business process approach. In contrast, at group level the norm is complex internal audits in accordance with a holistic governance process approach, with emphasis on the control environment and significant risks associated with management's financial reporting culture.

6.4.2.4 The credibility of internal audit work for statutory audit purposes (B4)

The credibility of internal audit work for statutory audit purposes depends on the reciprocal influences of each stakeholder group's roles, interpretations, interests and practices on (a) the competence of internal audit, (b) the independence of internal audit, (c) the standard of internal audit work and (d) meeting and changing the internal audit plan.

Misunderstanding the reciprocal influences of each stakeholder group on the credibility of internal audit work for statutory audit purposes means that (i) internal audit lacks competence as skills gaps exist in the internal audit team, (ii) particularly in larger internal audit teams (iii) consisting of mostly junior level internal auditors (iv) with insufficient management level skills. Mostly in some smaller organisations, (v) external auditors express general doubt about internal audit's ability to remain independent (vi) as management dictate the scope and focus of internal audits and reports and (vii) involve internal auditors in operational and / or managerial activities. Mostly in some larger internal audit functions, (viii) flexible internal auditors manipulate audit findings to suit management.

Further indicating internal audit's threatened independence, (ix) there is an absence of disagreement between internal audit and management about internal audit findings and / or (x) an absence of internal audit findings in areas highlighted as problematic by external audit procedures, while (xi) management and internal audit openly share a close symbiotic relationship. Furthermore, (xii) uncompleted internal audit plans are the norm, as (xiii) internal audit plans are too optimistic, (xiv) meaning quality is compromised for quantity and (xv) internal audit become a tick exercise. Too many (xvi) special investigations and *ad hoc* work for management further impact on the internal audit's normal assurance work. As a result, (xvii) the credibility of the in-house internal audit team's work for external audit purposes is questioned by external audit, including (xviii) when in prior years internal auditors' reliance work was of a lower quality than initially anticipated. External auditors (xix) favour extensive substantive procedures and (xx) reliance on outsourced internal audit work, particularly (xxi) when the outsourced partner is a peer from a Big 4 accounting firm, on grounds of their superior competence, including specialised and acknowledged skills, and automatic independence in comparison to in-house internal auditors, meaning no doubt exist about the credibility of their work.

In contrast, *reciprocal synchronisation* of the influences of each stakeholder group on the credibility of internal audit work for statutory audit purposes means that (i) the internal audit team has unquestionable competence, (ii) which is characterised by the right mix of skills to fulfil its risk-focused mandate. Such a team is (iii) typically smaller, (iv) stable, (v) consists mostly of senior level internal auditors (vi) with sufficient management level internal auditors and (vii) a majority of professional career internal auditors, (viii) complemented by internal auditors with specialist operational skills, as well as (ix) business staff on a rotational basis. Moreover, (x) internal audit's mandate, plans and reports are of unimpeded scope, as (xi) management acknowledge they should not dictate the scope and focus of internal audit's mandate and plans. The chief audit executive (xii) effectively balances management's influences on the relevance and scope of internal audit's mandate, plans and reports, (xiii) without isolating internal audit from business realities. This includes (xiv) refraining from accepting operational and / or (xv) managerial activities and (xvi) actively managing relationships between internal auditors and business staff, including by (xvii) rotating internal audit teams, (xviii) audit areas and (xix) auditees, (xx) continuous actions to raise awareness of and (xxi) provide training on the importance of independence and (xxii) an internal quality assurance programme.

The chief audit executive (xxiii) is supported by a direct reporting line and (xxiv) access to the audit committee chair, who is (xxv) trusted by the chief audit executive to address internal audit's challenges and (xxvi) honour the confidentiality of information shared. Thus, the chief audit executive (xxvii) is willing to report even uncomfortable findings, verbally and in writing. The chief audit executive ensures that (xxviii) internal audit work is credible, from having the stable internal audit team (xxix) applying well-developed, (xxx) stable, (xxxi) risk-based (xxxii) internal audit processes focused on key risks and controls, (xxxiii) in compliance with the Standards, including (xxxiv) the keeping of quality audit documentation and the application of quality control procedures.

Management (xxxv) relies on internal audit's reports and recommendations which contain (xxxvi) risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems and appropriately incorporate all conclusions anticipated by the external auditor. Internal audit (xxxvii) mostly meets its (xxxviii) flexible internal audit plans, which (xxxix) uses an 80 / 20 principle (xl) to allow for internal audit's responses to changing and (xli) emerging risks. Audit committee oversight (xlii) provides the balance needed to ensure internal audit capacity allows risk-based audits and meeting the internal audit plan, in spite of changes. Consequently, internal audit work is credible for statutory audit purposes.

6.4.2.5 External audit quality and the external auditor's liability (B5)

Given the external auditor's sole responsibility for the audit, managing the reciprocal influences of each stakeholder group's roles, interpretations, interests and practices on external audit quality and the external auditor's liability is a foundational condition of reliance. It considers (a) the riskiness of reliance and (b) sufficient external auditor involvement in the audit of key risks.

Misunderstanding the reciprocal influences of each stakeholder group on external audit quality and external auditors' liability means that external auditors (i) perceive that reliance is difficult and (ii) focus on the complexity of an audit, (iii) the riskiness of reliance, (iv) considering the differences in professionalism of the two professions and (v) the distinct roles of internal and external audit. They explain reliance (vi) amidst the need to address evolving (changing) risks, (vii) internal audit budget / capacity / resourcing constraints and (viii) external auditors having to redo internal audit work of a poor quality or (ix) reassume responsibility for delayed or transferred work originally allocated to internal audit (x) pose challenges in meeting external audit's reporting deadlines, particularly (xi) when these issues arise later in the reporting period. Moreover, external auditors consider meeting their deadlines will be hampered when (xii) they revert to extensive substantive procedures upon internal audit's postponed work finding internal financial controls are not operating fully. Furthermore, these external auditors consider (xiii) management's practices compromise the relevance and (xiv) credibility of internal audit work and (xv) that management often expect reliance despite internal audit reports concluding internal financial controls are not operating fully.

Therefore, the external auditors (xvi) declare they will limit reliance to the bare minimum (xvii) on grounds of their sole responsibility for the external audit and (xviii) plan to keep limiting reliance until there is sharing of liability between internal and external auditors. They (xix) favour working with their own teams or (xx) relying on work of outsourced internal audit partner peers from Big 4 accounting firms rather than using the work of the in-house internal audit team. They motivate this is due to (xxi) their teams' and peers' superior professionalism, compared to the inferior professionalism of internal auditors and (xxii) the superior credibility of their teams' work, compared to that of in-house internal auditors. Sufficient (xxiii) external auditor involvement in the auditing of key risks is not problematic as no or limited reliance occurs.

In contrast, *reciprocal synchronisation* of the influences of each stakeholder group on reliance preserves external audit quality and mitigates threats to the external auditors' liability. This is possible if the external auditor (i) carefully selects reliance work (ii) independently of external influences, considering (iii) whether the combined approach to assurance, (iv) including alignment between internal and external auditors, (v) mitigates undue engagement risk. He also considers (vi) the relevance and (vii) credibility of internal audit work for statutory audit purposes, and (viii) the support of the audit committee. Furthermore, (ix) the external auditor carefully plans sufficient involvement in the audit as a whole, (x) taking into account sufficient external audit coverage and (xi) the efficiency of reperformance levels associated with (xii) the risk of material misstatement. External audit (xiii) covers very significant risks themselves, (xiv) usually by means of extensive substantive procedures and (xv) when a significant risk is present, external audit does not use internal audit work on the complete area. Rotating (xvi) assurance work on key risks between internal and external audit avoids unnecessary duplication of audit work while ensuring sufficient external auditor involvement in the audit. These external auditors (xvii) do not limit reliance on grounds of their sole liability for the audit, (xviii) as they do not question the relevance nor the credibility of internal audit work.

6.4.3 A team mindset (C)

With *reciprocal synchronisation* of the influences of each stakeholder group's roles, interpretations, interests and practices on reliance, the voluntary adoption of a *team mindset* is the predominant mediator of *habitual integration* and *fair alignment* of internal and external audit work. The latter co-variant conditions change stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* from being viable to being practicable.

In contrast, *misunderstanding* the influences of each stakeholder group on reliance means that *a silo approach to assurance*, *resisted reliance* and *misaligned work* are inevitable. Specifically, internal and external auditors' assurance mindset is evident from (a) the assurance approach, (b) internal and external auditors working together, (c) whether internal and external auditors substitute or simply complement each other's work, (d) the quality of the relationship between internal and external auditors and (e) the working mindset of the two audit teams.

A silo approach to assurance creates (i) an uneasy relationship with (ii) distance between internal and external auditors (iii) despite the two parties moving towards reliance (iv) upon King III's emphasis on a combined approach to assurance. However, (v) combined assurance is under-developed (vi) as cooperation between internal and external auditors and (vii) the relationship between the two teams is still developing, especially (viii) in less well-regulated organisations which (ix) have a weaker risk management function. Consequent to the *silo approach to assurance*, (x) external auditors ignore integrating work and (xi) aligning their plans with internal audit as they (xii) practise no or limited reliance. As (xiii) the balance between internal and external audit work is not yet optimal, (xiv) unnecessary duplication of audit work occur, (xv) internal audit work simply complements rather than substitutes external audit work and (xvi) external auditors seek greater comfort to mitigate high engagement risk.

Sustaining *the silo approach to assurance*, (xvii) external auditors adopt a competitive mindset, characterised by (xviii) rivalry and (xix) tension as (xx) some external auditors focus on their habitual working relationship with outsourced partners from Big 4 accounting firms and (xxi) working with their own teams. They (xxii) contrast their superior professionalism against the inferior professionalism of internal auditors, (xxiii) with specific reference to the external auditor's sole legal liability for the external audit and (xxiv) insufficient regulation of internal auditors. They also contrast (xxv) the superior credibility of external auditors' work against the inferior credibility of the in-house internal auditors' work, with specific reference to (xxvi) the lack of support typically available to networks of global Big 4 accounting firms. Management and internal auditors are left behind, (xxvii) dissatisfied with the inefficiency inherent in (xxviii) unnecessary duplication of audit work and (xxix) questioning what reliance is, (xxx) particularly its wider definition used by external auditors. Although there is a (xxxi) slow movement towards some cohesion, (xxxii) internal auditors are impatient about the change happening too slowly. Moving (xxxiii) from a silo to a combined approach would require a mindset change from external auditors about working with internal auditors and (xxxiv) regular triangular combined assurance meetings between management, internal and external auditors.

In contrast, *a team mindset* means (i) a combined approach to assurance and (ii) an enduring, (iii) voluntary, (iv) closer, (v) professional (vi) working relationship formed between internal and external auditors. This (vii) developed over time, (viii) since before King III introduced combined assurance. The relationship (ix) grew from 'forced habit' (x) to 'just the way' internal and external auditors work closely together, (xi) in total acceptance that they have distinct roles. Engagement risk (xii) is mitigated (xxiii) as stakeholder groups' assurance needs and responsibilities are synchronised (xiv) in the context of their (xv) shared goals and (xvi) integrated risk and assurance view. Internal and external auditors (xvii) have very clear and detailed shared knowledge of each other's work, (xviii) allowing them to align reliance work on key risks of interest to both of them in their individual audit plans. They consider (xix) key risks included in internal audit's base audit plans or (xx) rotational internal audit plans, ensuring (xxi) external audit covers those controls in the years in-between. This planning (xxii) minimises unnecessary duplication of work and (xxiii) assurance gaps.

Following their (xxiv) history of working together well, internal and external auditors (xxv) substitute rather than simply complement each other's work, further facilitated when (xxvi) internal auditors make slight adjustments to the scope of their work and (xxvii) identify and (xxviii) rely on overlapping work included in both teams' audit plans which (xxix) external audit performed or plans to perform.

From having a team mindset, internal and external auditors (xxx) view themselves as a joint team, (xxxi) speaking the same language and (xxxii) providing combined assurance. This is (xxxiii) often presented in a single report to management and the audit committee (xxxiv) on specific areas of the audit (xxxv) although the external auditor signs the statutory auditor's report. In addition, (xxxvi) the external auditors from the Big 4 accounting firm offer continuous development opportunities to the internal auditors of their clients.

The effect of the *team mindset* on (xxxvii) external audit quality is positive. Internal and external auditors (xxviii) engage in regular meetings and (xxix) constructive debate throughout the year, (xxx) internal auditors share their deep insights, gained from daily involvement in the business, with external auditors, (xxxi) internal and external auditors learn from each other while (xxxii) they jointly face increasing assurance requirements and demands on them (xxxiii) to mitigate their budget / capacity / resourcing constraints. Ultimately, (xxxiv) management and the audit committee get efficient comfort in totality (xxxv) from internal audit work habitually forming an integral part of evidence on the statutory audit and (xxxvi) an aligned audit methodology on reliance areas implying (xxxvii) as much cross-coverage as possible between them.

6.4.4 Habitual integration (D)

Adopting *a team mindset* is the predominant mediator of *habitual integration* of internal and external audit work, changing stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* from being viable to being practicable. In contrast, *a silo approach to assurance* means that external auditors *resisted reliance*. Specifically, *integrating work* considers each stakeholder group's views on (a) what reliance is, (b) internal and external auditors' commitment to reliance, (c) the nature of reliance work, (d) the cost-benefit of assessing internal audit and its work, (e) who is best placed to provide the assurance, (f) the influence of external audit firm software and methodologies on reliance, (g) the overlap between internal and external audit work, (h) duplication of audit work and (i) assurance effectiveness and efficiency, including external auditors' propensity for protecting audit firm fee income. At a minimum, all external auditors read internal audit reports and hold discussions with internal auditors prior to external audits.

Resisted reliance means (i) external auditors prefer to work with their own teams opposed to working with in-house internal auditors and (ii) favour reliance on outsourced internal audit work, (iii) particularly when the outsourced partner is a peer from a Big 4 accounting firm, (iv) which allow for cheaper and less formal assessments of internal audit and their work compared to those on in-house internal audit functions. Thus, they (v) practise no or limited reliance.

External auditors justify this by emphasising that (vi) management focus on reducing external audit fees by increasing reliance rather than considering the effect of reliance on external audit quality and the external auditor's liability, (vii) overlap between internal and external audit work is actually very small and (viii) the fixed cost of assessing internal audit and its work exceeds the audit fee saving, particularly in smaller organisations. Thus, (ix) external auditors apply a wider definition of reliance, meaning that (x) they limit it to reading internal audit reports and discussions with internal auditors prior to external audits and (xi) using peripheral support by internal auditors (xii) while they do not use internal auditors for performing direct assistance work. They motivate using internal auditors for direct assistance work (xiii) will not reduce external audit fees and improve assurance efficiency and (xiv) is not possible as internal auditors' limited budget / capacity / resourcing does not allow it. In addition, external auditors assert (xv) internal auditors do not have access to nor understand external audit firm software and methodologies needed for performing direct assistance work, while reliance (xvi) will raise management's expectations of an audit fee reduction.

Pressure (xvii) to increase reliance does not necessarily change external auditors' general commitment to reliance as they respond by *ad hoc* reliance attempts, focusing on those audit clients exerting pressure. In addition, (xviii) external auditors' commitment to reliance is decreasing in parallel with their increasing professional risks. This (xix) trend is expected to gain momentum as compulsory audit firm rotation is expected to render combined assurance and reliance more difficult as the new firm will have no reference point for making a reliance decision.

Considering assurance effectiveness and efficiency, *resisted reliance* means that (xx) no or limited reliance does not yield lower external audit fees, (xxi) leaving management and internal auditors, who desperately seek greater reliance to reduce external work and fees, frustrated with reliance happening so slowly and (xxii) sceptical of external auditors' commitment to reliance. They (xxiii) perceive internal and external auditors' definitions of reliance are misaligned(xxiv) as they struggle to make sense of no or limited reliance and (xxv) are dissatisfied with external auditors' wider definition of reliance and the consequent lack of assurance efficiency. While (xxvi) management, whose primary focus is on assurance efficiency, and some audit committees (xxvii) believe that internal audit should reduce external audit work and fees, (xxviii) they also perceive that extensive unnecessary duplication of audit work is the norm. Some managers consider that (xxix) external audit firms' internationally developed audit methodologies hamper reliance, and (xxx) their assessments of internal audit are onerous hurdles leading to over-auditing rather than reliance, while (xxxi) others perceive that the benefits of assessing internal audit and its work outweigh the costs. Moreover, they note (xxxii) reliance is not consistently applied across partners working on the same audit client of a firm.

As a result, (xxxiii) management believe that external auditing standards should be simplified to make reliance easier and more efficient, and (xxxiv) that some external auditors are acting in self-interest rather than focusing on assurance effectiveness and efficiency. Some (xxxv) managers are devising plans to increase reliance. These plans (xxxvi) ignore management's influence on reliance. The plans focus on (xxxvii) having an external assessment of the internal audit function and its work done to identify any shortcomings preventing reliance, (xxxviii) seeking guidance on the redesign of internal audit tests to align the audit methodology on reliance areas to requirements for both internal and external audit, and (xxxix) entering into open discussion of reliance in quarterly meetings with the engagement partner to actively promote alignment planning.

In contrast, *habitual integration* means that (i) habitually, (ii) internal audit work forms an integral part of evidence on the statutory audit as (iii) optimal integration of the two types of audit work (iv) is an integral part of the external audit firm's audit approach and methodology, which (v) focus on relying on internal audit work as much as possible. In addition, external auditors perceive that (vi) the benefit of assessing internal audit and its work usually exceeds the cost and (vii) do not see external audit firm software and methodologies as hampering reliance. This is particularly so when (viii) a competent (ix) stable internal audit team (x) conducts well-developed, (xi) stable

(xii) internal audit processes (xiii) in larger organisations. Moreover, (xiv) all stakeholder groups strive to ensure that assurance comes from the most effective and efficient provider, considering (xv) the combined cost of internal and external audits, (xvi) the level of assurance required, (xvii) whether internal audit's focus is operational or financial, (xviii) the geographical location of audit sites and (xix) planned visits by internal audit to sites of third party service providers of the organisation.

Typically, (xx) reliance work includes a large proportion of direct assistance work for statutory audit purposes, (xxi) edited into internal audit plans, (xxii) including controls assurance work with a financial focus and extensive substantive procedures. In this way (xxiii) external auditors rely on internal audit's work of a routine nature, (xxiv) allowing external auditors to concentrate on more complicated or risky work.

Overall, (xxv) all stakeholder groups focus on balancing assurance effectiveness and efficiency, yet favouring effectiveness over efficiency, (xxvi) supported by *balancing oversight* of the audit committee. Assurance effectiveness and efficiency benefit as (xxvii) alignment planning discussions and workshops identify overlapping work in internal and external audit plans, and (xxviii) aligned individual audit plans of internal and external auditors minimise unnecessary duplication of work and audit queries for management's attention, (xxix) including by internal audit relying on relevant overlapping work of external audit. Moreover, (xxx) either team uses data analytics to balance audit effectiveness and efficiency.

At the same time, they (xxxi) improve assurance coverage by ensuring as much cross-coverage as possible instead of duplicating work and (xxxii) reduce external audit fees and work, while (xxxiii) respecting the distinct roles of internal and external audit, in particular (xxxiv) the effect of reliance work on internal audit's business-wide risk focus, concentrating on controls assurance work with mostly an operational focus. They also (xxxv) understand some internal audit work is duplicated or extended to ensure sufficient external auditor involvement in the audit of key risks. Additionally, (xxxvi) assurance efficiency assessments acknowledge internal audit's implicit contribution to external audit effectiveness by considering what work external auditors are doing and what work they would have done if no internal audit was present.

6.4.5 Fair alignment (E)

Adopting *a team mindset* is the predominant mediator of *fair alignment* of internal and external audit work, changing stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* from being viable to being practicable. In contrast, *a silo approach to assurance* means that *misaligned work* of internal and external auditors prevails. Specifically, alignment considers the reciprocal influences of each stakeholder group on (a) alignment planning of internal and external audit's (b) focus, (c) objectives and approaches and (d) methodologies, particularly the period covered by reliance work, sampling and selection, response (time) to audit exceptions, and timing of internal audit work, as well as (e) meeting the aligned audit plans.

Misaligned work of internal and external audit stems from (i) insufficient alignment planning, characterised by (ii) the absence of structured alignment planning discussions, (iii) no sharing of information about the focus of and progress made with internal audits during informal discussions between auditors, (iv) instances where the balance between internal and external audit work is not 100% and (v) instances when internal auditors are not willing to change their plans. As alignment efforts is absent, (vi) internal audit's planning is 12 months ahead of external audit's planning, thus (vii) internal and external audit planning is happening it different times and (viii) internal audit presents its plan for audit committee approval significantly before external audit presents its plan.

The (ix) unaligned focus, objectives, approaches and methodologies between internal and external audit plans imply (x) misaligned internal and external audit work, for example (xi) when their different sets of professional standards exclusively accommodate the distinct roles and unique objectives of the individual teams, (xii) when internal audit's risk assessments as part of their audit planning uses external audit's management letters instead of discussion with external auditors, and / or (xiii) when internal audit follows a simple transactional instead of a risk-based approach. However, management (xiv) disapprove of external auditors using methodological differences between the two audits too quickly, seeing them as 'ridiculous' excuses for not relying.

In terms of methodological differences between internal and external audits, (xv) considering the period covered by reliance work, external auditors maintain that dissimilarities between the period covered by the two teams means that reliance on internal audit's work covering part of the financial period does not necessarily improve audit efficiency. However, management suggest that external auditors should cover the part of the financial period excluded from internal audit work instead of repeating work on the part of the financial period covered by internal audit. Considering (xvi) sampling and selection of reliance work, external auditors maintain that they are unable to persuade internal auditors to increase their sample sizes, in line with their own requirements. However, internal auditors declare that they do whatever they can to assist reliance; they even adjust their sample sizes. Regarding (xvii) the response to audit exceptions, external audit teams automatically change to extensive substantive procedures while internal audit tests the full population of the relevant control. Internal and external auditors confirm that internal audit's drawn-out responses to audit exceptions complicate reliance. Furthermore, when the end of the financial year is approaching and exceptions are not appropriately redressed, external audit needs sufficient time to perform alternative audit procedures in response to the risk exposure, which makes reliance impractical.

Considering (xviii) the timing of audit work, external auditors cite the risk of not meeting their deadlines when internal audit work is postponed towards the end of the reporting period (to enable internal audit to cover the majority of the financial period). This hampers reliance, for example, when external audit (xix) must revert to extensive substantive procedures when postponed internal audit work identifies control exceptions, (xx) must finish off uncompleted work (arising from internal audit prioritising special investigations or *ad hoc* work for management) or (xxi) re-do substandard reliance work allocated to internal audit. Moreover, (xxii) when the end of the financial year is approaching and exceptions are not appropriately redressed by management, external audit needs sufficient time to perform alternative audit procedures in response to the risk exposure, which makes reliance impractical.

In contrast, *fair alignment* of internal and external audit work means that (i) external auditors move their audit planning earlier than usual to accommodate alignment planning when (ii) internal and external auditors engage in structured, (iii) upfront (iv) alignment planning discussions and workshops (v) well before the beginning of the financial year. Planning involves (vi) lots of good communication (vii) as internal and external auditors work closely together (viii) on a combined approach to assurance, for (ix) developing a shared understanding of each other's requirements for professional work and plans influencing reliance, (x) without external auditors prescribing to internal audit what to do. In the planning process, (xi) internal auditors and external auditors liaise about incorporating specific additional work in and (xii) making slight changes to internal audit's plans to increase reliance opportunities. They also (xiii) identify areas where external audit are inadvertently performing extensive substantive procedures where reliance on internal audit's controls assurance work should be possible and (xiv) plan reliance around internal audit's three year rotational plan by using internal audit's work on key areas of control in years when internal audit tested them, while the external audit team audited those controls in the years in between. At the end of the planning process internal and external auditors (xv) agree on reshuffled and aligned individual audit plans. These plans (xvi) reflect an aligned focus on controls assurance work (xvii) addressing key financial risks and (xviii) meet external audit requirements for sufficient external auditor involvement in the external audit. Moreover, (xix) aligned plans consider internal audit's findings on the effectiveness of internal financial controls. In addition, (xx) internal and external auditors present their reshuffled and aligned individual audit plans simultaneously for review by management and approval by the audit committee, (xxi) well before the beginning of the financial year. As (xxii) internal auditors complete agreed reliance work as planned, reliance does not pose challenges in meeting external audit's reporting deadlines.

Concerning *fair alignment* of specific methodological differences between internal and external audits, (xxiii) the period covered by reliance work is aligned. This is because timeous alignment planning ensures that internal audit covers the majority of the financial year, including by moving internal audit work earmarked for reliance to the latter part of the year. Early planning meetings (xxiv) allow external audit influence on the extent of tests, sample sizes and selection of audit items in internal audit plans based on their aligned focus on key risks. Internal auditors (xxv) adjust sample sizes in line with external audit's minimum sample sizes to increase reliance. External audit plans (xxvi) reflect reduced total sample sizes per test considering the number of items for testing indicated in internal audit plans. Internal and external audit's (xxvii) timing of work and responses to audit exceptions are mostly aligned as reliance work includes a large proportion of credible direct assistance work planned, supervised and reviewed by external auditors.

6.4.6 Balancing oversight (F)

In combination with *facilitative communication*, the context created by the quality of audit committee oversight of internal and external audit's assurance roles, including oversight of reliance, pervasively sustains all the other constructs determining the appropriateness and fairness of reliance.

When *symbolic oversight* fails to mitigate the *disconnect* between stakeholder groups' reciprocal influences on reliance, external auditors *resisted reliance*. However, *habitual integration* and *fair alignment* of internal and external audit work is practicable when *balancing oversight* of assurance effectiveness and efficiency means that *reciprocal synchronisation* resolves *disconnect* between stakeholder groups' reciprocal influences on reliance. *Balancing oversight* implies (a) audit committee oversight of assurance effectiveness and efficiency, considering (b) the audit committee's inherent strength and closeness to the business.

Symbolic oversight of assurance effectiveness and efficiency means that (i) some audit committee members of (ii) a weak audit committee (iii) have a different mindset about reliance. They are (iv) tokens (v) who support management (vi) in applying pressure to increase reliance on external auditors, (vii) ignoring the influence of reliance on external audit quality and (viii) the distinct roles of internal and external audit. A weak audit committee (ix) finds it difficult to gain closeness to the business. It (x) receives data dumps in internal audit reports and (xi) feels that management view 'healthy tension' (as part of audit committee oversight) as 'interference'. Consequently, it is (xii) labelled as an activist audit committee by management when it requests clarifications. The audit committee's (xiii) oversight role is encumbered by management who misunderstand the stakeholder groups' assurance needs, risks and responsibilities.

In contrast, *balancing oversight* of assurance effectiveness and efficiency means (i) a strong audit committee (ii) mitigates engagement risk by (iii) overseeing the implementation of a formalised, combined approach to assurance (iv) as a means for synchronising stakeholder groups' assurance needs and responsibilities and achieving (v) assurance effectiveness, including minimising assurance gaps and improved coverage. In the oversight process, the strong audit committee balances (vi) the influence of managements' general focus on profit margins on having strong governance in the form of (vii) strong internal financial controls, (viii) a strong internal audit function, including by approving (ix) the internal audit budget, (x) internal audit's mandate and plans, and (xi) the appointment and functioning of a competent, independent chief audit executive. Considering reliance, although it exert a degree of pressure on external auditors to increase reliance, (xii) it balances management's pressure to increase reliance for efficiency purposes against the effect of reliance on external audit quality and the external auditor's liability, including when it is (xiii) reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance. Audit committee oversight (xiv) balances management's influence on the relevance of internal audit work for statutory audit purposes, including when it (xv) approves changes to the scope and focus of internal audit's mandate and plans which threaten internal audit's risk-based focus, for example special investigations and *ad hoc* work for management. Moreover, it (xvi) balances management's influence on the credibility of internal audit work for statutory audit purposes, including when it (xvii) evaluates the competence of the internal audit team annually, (xviii) gives the chief audit executive direct access to the audit committee, (xix) reviews the outcomes of external assessments of internal audit quality and (xx) monitors whether internal audit meets their plans.

A strong audit committee (xxi) shares members with the risk committee or engage about risks and controls in joint meetings with internal audit and risk management prior to quarterly audit committee meetings. It (xxii) knows and understands the trustworthiness of the management of the organisation, (xxiii) has the support of the strong head of internal audit, (xxiv) asks the right questions of management, internal and external audit, and (xxv) engages in 'focused conversation' (xxvi) during robust audit committee meetings where there is (xxvii) extensive discussions about areas of concern, for example as highlighted in intern audit reports. Such an audit committee is empowered by (xxviii) a 'business sense', (xxix) knowledge of governance requirements, (xxx) a mix of appropriate financial and (xxxi) operational (xxxii) training and (xxxiii) experience, (xxxiv) a strong risk view grounded in (xxxv) business, (xxxvi) financial and (xxxvii) industry insights, (xxxviii) an uncompromising emphasis on sound governance, and (xxxix) strong upfront succession-planning of audit committee members. Moreover, the committee is (xl) supported by internal audit who provides it with (xli) internal audit reports detailing risk and control problems, their impact and who should take responsibility for addressing them, (xlii) updates on the state of risks and controls, (xliii) questions to raise with management, and (xliv) whether management take internal audit findings seriously. Internal audit shares such information with the audit committee (xlv) in documentation 'packs' and (xlvi) during 'closed sessions' without management present.

6.4.7 The emergent theory

The emergent substantive theory of balanced reliance explains reliance on internal audit work by external auditors, taking into consideration the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. The theory explains how stakeholder groups achieve *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. This explanation is based on six theoretical constructs. *Facilitative communication* and *balancing oversight* create a context which sustains balanced reliance; *reciprocal synchronisation* is a foundational condition of balanced reliance, *a team mindset* is the predominant mediating condition of balanced reliance, mediating *habitual integration* and *fair alignment* as co-variant operational conditions of balanced reliance.

6.5 THEORETICAL CONTEXT OF THE EMERGENT THEORY

This section compares the substantive theory of balanced reliance to relevant extant theories, literature and internal and external auditing professional standards. The theory explains how all stakeholder groups influencing and influenced by reliance achieve *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. This comparison does not imply that the theory was derived from or tested against extant knowledge. The aim of the comparison is to position the theory in extant knowledge to highlight its contribution to the theory and practice of reliance. To this end, the constructs of the theory are compared to those of the stakeholder theory (for example, Parmar, Freeman, Harrison, Wicks, Purnell & Colle, 2010), the relational coordination theory (for example, Gittell, 2012b), the summation model and organising framework developed from the most recent synthesis study on reliance (Bame-Aldred *et al.*, 2013) and relevant internal and external auditing professional standards (IAASB, 2018: ISA 610 (Revised 2013); IIA, 2016: Standard 2050).

6.5.1 The stakeholder theory

Reliance occurs in the context of the roles, interpretations, interests and practices of various stakeholder groups involved in the statutory financial reporting process of organisations. The literature and the data analysis indicate that the complexity of reliance often causes confusion and disconnect between stakeholder groups as to reliance possibilities and their reciprocal influences on reliance. A review of literature on the stakeholder theory revealed its relevance to the theory developed in this study. This section briefly considers the relevance of stakeholder theory to this study. In the overview which follows, brackets are used to indicate where constructs of the emergent theory resonate with stakeholder concepts.

6.5.1.1 Overview of the relevance of the stakeholder theory to this study

The stakeholder theory is regarded as a significant development in the field of business ethics (Wicks, Gilbert & Freeman, 1994:475). However, the exact origin of the stakeholder theory is unknown (Freeman & Reed, 1983:89). Freeman (1984) advanced the stakeholder concept as an ethical means for firms to achieve a predetermined outcome (Wicks *et al.*, 1994:476).

Freeman and Reed (1983) associate the work of several authors with the development of the stakeholder theory. First, Igor Ansoff (in Freeman & Reed, 1983:89) explains the ethical roots of the stakeholder theory as ‘balancing the conflicting claims or the various “stakeholders”’ who each have “responsibilities” and “objectives” that are not ‘synonymous’. Second, Russell Ackoff (in Freeman & Reed, 1983:89), a systems theorist, suggests that the ‘social problems’ associated with unmatched responsibilities and objectives can be overcome by ‘the support and interaction of stakeholders’ involved. Third, William Dill suggests a need for moving from ‘stakeholder influence to stakeholder participation’ (Freeman & Reed, 1983:90). In line with the latter view, Eden and Ackermann (1996:508) suggest that participation by all ‘key actors’ in the decision-making process would result in ‘a better outcome in the sense of progress having been made in relation to the substantive issue’, as the interests (or power) of the diverse stakeholder groups would be considered.

The stakeholder theory has evolved over a period of time. A more recent work by Parmar *et al.* (2010:406) on developments, points out that the theory is useable in ‘an array of settings … [to] serve different purposes’ as a ‘framework’ centrally focused on fairly addressing stakeholder groups’ conflicting interests in their ‘cooperative’ activities [for example practising reliance]. This description of the stakeholder theory resonates with the aim of this study – to construct a theorised (conceptualised) explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

Jones and Wicks (1999:215) emphasise that stakeholder theory is ‘a theory of relationships’ [*a team mindset*], which considers several, often diverse, interrelated groups’ (or individuals’) multiple, and often incompatible, interests on moral grounds [*reciprocal synchronisation*] (Donaldson & Preston, 1995:70, 71). It allows morally acceptable [*habitual integration*] yet practically viable [*fair alignment*] approaches to managing stakeholder groups’ interests (Jones & Wicks, 1999:206, 210, 214-215). Consequently, stakeholder groups’ conflicting interests are addressed by ‘rethink[ing] problems [*reciprocal synchronisation*] so that the needs of a broad range of stakeholders are addressed … [through] trade-offs … improving … [outcomes for] all sides’ [*balanced reliance*] (Parmar *et al.*, 2010:406). Thus, stakeholder theory guides the structure [*a team mindset*] and working [*reciprocal synchronisation*] of interrelated groups’ cooperative activity [*habitual integration* and *fair alignment*] (Donaldson & Preston, 1995:70; Phillips, Freeman & Wicks, 2003:481). This fosters ethically sound cooperative interrelationships, cognisant of ‘values, choice, and potential harms and benefits for a large group of groups or individuals’ (Parmar *et al.*, 2010:406), through stakeholder groups’ aligned relationships [*a team mindset*].

Stakeholder theory's focus on ethically fair relationships implies consideration of a broader spectrum of interrelated parties, transcending the shareholder theory's exclusive focus on the interests of shareholders (Phillips *et al.*, 2003:481). Thus, Parmar *et al.* (2010:412) propose that the definition of a stakeholder should not be 'singular and fixed'; they suggest that instead, the ideal is 'different definitions serving different purposes'.

Researchers propose several definitions of a stakeholder. They distinguish between (i) 'legitimate stakeholders' (groups or individuals who influence or are influenced by the achievement of predetermined objectives) (Donaldson & Preston, 1995:85; Freeman, 1984:46; Mitchell, Agle & Wood, 1997:857), (ii) 'normatively legitimate stakeholders' vs 'derivative stakeholders' (those who have a direct moral claim to consideration of their wellbeing, in contrast to those holding no moral claim but with the power to harm or aid achievement of outcomes) (Phillips *et al.*, 2003:481, 489, 496), (iii) primary and secondary stakeholders (vital parties holding specific rights, in contrast to unconnected parties with claims only on 'regular moral' grounds) (Clarkson, 1995:92) and (iv) direct (those with relationships leading to direct exchanges and direct influence) and indirect stakeholders (those with an interest in outcomes in the absence of direct control and exchanges) (Hahn, 2015:15). Donaldson and Preston (1995:81) emphasise two normative propositions for stakeholder identification, namely, 'stakeholders are identified by *their* interest in the affairs of the corporation' and 'all stakeholders have intrinsic value'.

In the context of this study, the stakeholder groups which influence and are influenced by reliance are management, the audit committee and internal and external auditors.

Donaldson and Preston (1995) describe three separate yet interrelated approaches to applying stakeholder theory. First, following a descriptive / empirical approach, researchers often use the theory simply to describe the characteristics and behaviours of corporations, and how management think about and manage the interests of stakeholder groups and the corporation 'in the external world' (Donaldson & Preston, 1995:70, 74; Kaler, 2003:72-74). Such studies usually rely on the central idea of satisfying a broad set of stakeholder groups, reaching beyond the interests of shareholders (Donaldson & Preston, 1995:75).

Second, an instrumental stakeholder approach can be followed. This generates predictions of connections (usually ‘implications’) between stakeholder management strategies and the achievement of corporate objectives using descriptive / empirical data, direct observations or interviews and ‘if … then’ reasoning (Donaldson & Preston, 1995:71, 74). Thus, the instrumental stakeholder approach analyses stakeholder relationships for their influence on achieving a stated objective to obtain guidance on stakeholder relational principles and practices associated with achieving the objective (Donaldson & Preston, 1995:72). Jones and Wicks (1999:206) explain that stakeholder theory considers the reciprocal influences (cause and effect) on the success of a practice or idea by parties with a connected interest in the outcome (Donaldson & Preston, 1995:71-72; Kaler, 2003:72-74; Phillips *et al.*, 2003:479). Donaldson and Preston (1995:71, 81) furthermore observe that studies adopting an instrumental stakeholder approach usually omit details of the linkage between cause and effect, although they highlight that ‘broad normative principles’ were behind effects.

Third, a normative stakeholder approach implies an ethical perspective to stakeholder relationships, focusing on categorical ‘moral or philosophical guidelines’ for corporate operations and management on the basis of the ‘intrinsic’ importance of each stakeholder group (Donaldson & Preston, 1995:71, 72, 74). Norms refer to guidelines of the proper ‘thing to do’ (Donaldson & Preston, 1995:71, 72). However, Donaldson and Preston (1995:72) observe that ‘the fundamental normative principles involved are often unexamined’ in studies adopting such an approach.

Parmar *et al.* (2010:414), Freeman (1999) and Jones and Wicks (1999:210) discourage strict categorisation in accordance with Donaldson and Preston’s (1995) triad of approaches for applying stakeholder theory. Parmar *et al.* (2010:411) assert that combining stakeholder approaches enables ‘story-telling’, which facilitates cooperation and value creation. Jones and Wicks (1999:210) maintain that ‘shared values and shared understandings driving stakeholder research render fundamentally incomplete any theory that is either exclusively normative or exclusively instrumental’. They compare characteristics of instrumental and normative theories, claiming that even instrumental stakeholder theory is grounded in ‘morally sound principles’ (Jones & Wicks, 1999:214). This idea is shared by Donaldson and Preston (1995:74), who view the three approaches to stakeholder theory as ‘nested’, moving from an outer ‘descriptive’ layer to the central normative ‘core’. In addition, Jones and Wicks (1999:214) argue that although not a critical component of ethical theory, ‘practicability’ is vital for stakeholder theory. Thus, they propose ‘convergent stakeholder theory’ as a ‘superior’ ‘hybrid’ of instrumental and normative stakeholder theory, allowing morally acceptable yet practically viable approaches to managing stakeholders’ interests (Jones & Wicks, 1999:206, 210, 214-215).

A limited number of studies in the auditing field apply a stakeholder approach, mostly focusing on corporate social responsibility or environmental reporting and assurance decisions of management. Most of these apply the theory for descriptive purposes (for example Funnell, Wade & Jupe, 2016; Ewelt-Knauer, Gold & Pott, 2013; Whitehorn & Barac, 2015) as a means of indicating that interests of various parties were considered. Some auditing studies use stakeholder theory to describe the influences of various stakeholder pressures on management decisions or organisational outcomes (for example, Khan, Muttakin & Siddiqui, 2015; Liesen, Hoepnes, Patten & Figge, 2015; Mir & Rahaman, 2011). A very small number of auditing studies apply the theory in a normative way to evaluate and conclude on the morality of management’s approach to stakeholder management (for example, Williams & Adams, 2013; Edgley, Jones & Solomon, 2010).

In the context of this study, stakeholder theory is considered from a normative perspective. The comparison of the constructs of the emergent theory to those of the stakeholder theory aims to determine how the new theory resonates with recognised constructs of ‘practically viable’ (appropriate) and ‘normatively sound’ (fair) stakeholder relationships (Jones & Wicks, 1999:217) in a way that appropriately and fairly balances their power and interests (as discussed in Chapter 2).

6.5.1.2 Comparing key constructs of the stakeholder theory to the emergent theory

From a review of literature on stakeholder theory, three constructs are discernible as central tenets explaining how stakeholder groups balance their conflicting interests in and reciprocal influences on cooperative activity aimed at achieving a central desired outcome in an ethical way.

The first construct of the stakeholder theory is: stakeholder groups willingly balance their benefits and obligations [roles, interpretations, interests and practices] to protect the viability of the process [reliance] (Jones & Wicks, 1999:214, 216; Phillips, 1997: 56-57, 63) for no reason other than doing so is the right thing to do (Donaldson & Preston, 1995:72; Phillips *et al.*, 2003:481). Thus, each stakeholder group acts fairly, putting the central desired outcome [achieving *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*] ahead of their own (selfish) interests and well-being (Hahn, 2015:21-23; Bosse, Phillips & Harrison, 2009:454; Jones & Wicks, 1999:214, 216) as part of balancing their conflicting interests (Freeman & Reed, 1993:89). This construct implies that stakeholder groups become 'partners', willingly adopting 'a cooperative mindset' 'for the achievement of mutual advantage', resolving conflict within and between stakeholder group(s) by 'searching for alternatives that achieve mutual gain or lessen the negative impact for all stakeholders', ensuring that 'the success of each is intertwined with the success of all others' (Phillips, 1997:56-57, 63-64).

Consistent with Phillips (1997), Bosse *et al.* (2009:454) assert that stakeholder relationships perceived as normatively fair from a distribution, procedural and / or intentional perspective, create 'a pattern of positive reciprocity' among stakeholder groups. Consequently, the 'means employed' in the process of cooperative endeavour and the 'ends sought' as outcome fairly balance stakeholder groups' benefits and obligations, making convergence of stakeholder groups' interpretations of the fairness of the outcome 'practically viable' (Jones & Wicks, 1999:216-217).

This first construct of the stakeholder theory resonates with willing *reciprocal synchronisation* (section 6.4.2) of the influences of each stakeholder group on reliance. Thus, each stakeholder group puts the central desired outcome of *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*, ahead of their own interests, resolving disconnect between their reciprocal influences on reliance. In a recent study Lin, Ho and Shen (2018:553-554) developed a matrix as instrument for synchronising stakeholder groups' power and interest on strategic environmental projects. Upon testing their matrix, Lin *et al.* (2018:562) concluded that the balancing of stakeholder groups' responsibilities 'helps stakeholders to quickly find their roles and relations'. Thus, the latter mentioned study matches the current study's emphasis on *reciprocal synchronisation* of responsibilities as foundation for *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

The second construct of the stakeholder theory is: stakeholder groups voluntarily form relationships resulting in reciprocal consideration of their interrelated interests and well-being (Phillips *et al.*, 2003:481, 493; Donaldson & Preston, 1995:72), ensuring that the central desired outcome is practically viable (Jones & Wicks, 1999: 216-217; Phillips, 1997:63). Thus, a stakeholder approach anchors processes of decision-making to achieve the central desired outcome in voluntary reciprocal interrelationships as the basis for morally sound, logically persuasive, theoretically rational and empirically viable outcomes (Hahn, 2015:22; Jones & Wicks, 1999:216). Bearing evidence of atypical stakeholder behaviour, Frooman (1999:203) uses resource dependency theory to explain that stakeholder groups' self-interest and power rather than norms could influence outcomes, while Rowley and Moldoveanu (2003:204) contend that stakeholder groups' desire to express or protect a certain identity could influence outcomes.

With *reciprocal synchronisation* as a foundation, this second construct of the stakeholder theory resonates with the voluntary adoption of *a team mindset* (section 6.4.3) as the predominant mediator of *habitual integration* (section 6.4.4) and *fair alignment* (section 6.4.5) of internal and external audit work. These constructs make achieving stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* practicable. Matching the latter constructs of the substantive theory, Lin *et al.* (2018:562) conclude that the balancing of stakeholder groups' responsibilities [*reciprocal synchronisation*] builds trust and relieves conflict among stakeholder groups, fostering common goals and shared objectives.

The third construct of the stakeholder theory is: all stakeholder groups participate in decision-making to achieve a central desired outcome (Phillips *et al.*, 2003:487), meaning that whatever the outcome, the participating groups accept it as fair (Phillips *et al.*, 2003:487). Explaining this construct, Phillips *et al.* (2003:487) state that '(w)ho gets how much of the organizational outcomes pie is an important question, but so is who gets a say in how the pie is baked'. Phillips *et al.* (2003:487) point out that perceptions of fairness are linked to perceived control stemming from participation in decision-making, meaning participants are prone to accepting even poor outcomes as fair. Consistent with Phillips *et al.* (2003), the study on reciprocal stakeholder behaviour by Hahn (2015:21, 23) concludes that the 'procedural fairness' of their counterparties' decision-making processes influence stakeholder groups' practices. Hahn (2015:21, 23) explains that stakeholder groups willingly sacrifice strict transactional fairness, even at their own expense, when they perceive that a 'strong' reciprocal relationship exists from their counterparties' display of 'friendly' intentions.

The third construct of the stakeholder theory resonates with *facilitative communication* (section 6.4.1) and *balancing oversight* (section 6.4.6) as a means of sustaining *reciprocal synchronisation*, *a team mindset*, *habitual integration* and *fair alignment*. Thus, stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* is viable. Matching the latter constructs of the substantive theory, Lin *et al.* (2018:562) conclude that the process of balancing stakeholder groups' responsibilities was associated with efficient information sharing through open communication.

In conclusion, the close alignment between the constructs of the stakeholder theory and the emergent theory positions (Glaser, 1978:38) the latter as a coherent and plausible frame for balancing the reciprocal influences of each stakeholder group on reliance in order to make their *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* viable.

6.5.2 The relational coordination theory

Constructs central to the emergent theory resolve stakeholder groups' main concern about reliance by achieving stakeholder groups' central desired outcome: *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. Constructs central to the stakeholder theory are stakeholder groups' participation in decision-making to achieve a central desired outcome, willingly balancing stakeholder groups' benefits and obligations and a voluntarily adopted reciprocal relationship which considers stakeholder groups' interrelated interests and well-being. The central theme underlying the constructs of the emergent theory and the stakeholder theory is coordinating the reciprocal influences of each stakeholder group's roles, interpretations, interests and practices on reliance in a manner that makes achieving their shared goal viable.

A review of literature on the relational coordination theory reveals that its constructs resonate with those of the stakeholder theory and the emergent theory. This section briefly considers the relational coordination theory's relevance to this study and compares constructs of relational coordination to those of the emergent theory. The overview indicates, using brackets, how the constructs of the emergent theory resonate with those of the relational coordination theory.

6.5.2.1 Overview of the relevance of the relational coordination theory to this study

Gittell (2002:301) defines relational coordination as 'a mutually reinforcing process of interaction between communication and relationships carried out for the purpose of task integration' [for example reliance]. Relational coordination addresses intensive, role-based [reciprocal influences of each stakeholder group's roles on reliance] rather than individual-based coordination, in the context of highly interrelated tasks [for example, reliance work], performed under conditions of uncertainty [complexity requiring simultaneous consideration of numerous interacting factors] and time constraints [meeting external audit's reporting deadlines] (Gittell, 2012a:402; 2012b:28, 34). Following Thompson's work (1967), Gittell (2006:74) explains that coordinating a loop of highly interrelated work [reliance work], where information created from one role [internal audit] feeds back as input into related roles [external audit], requires 'mutual adjustment' between roles [as described in the emergent theory].

Relational coordination of interrelated roles and work [reliance work] is credited with mitigating the 'opposition' between the effectiveness (quality) and efficiency [internal and external audit's assurance effectiveness and efficiency] reported in the operations management research (Gittell, 2012b:23; Lapré & Scudder, 2004; Schmenner & Swink, 1998:97). The contention is that changing the effectiveness or efficiency of performance requires either changes in production assets or altered operational choices (Schmenner & Swink, 1998:108). Based on evidence that relational coordination decreases errors, overlaps, delays and gaps, Gittell (2012b:24) proposes that relational coordination simultaneously improves efficiency (by removing inefficiencies) and effectiveness (by enabling effective seamless work processes across roles utilising existing assets).

Gittell (2012b:21) maintains that the ‘mutual influence between communication [*facilitative communication*] and relationships [*reciprocal synchronisation* and *a team mindset*] lies at the heart of relational coordination’. For example, effective coordination is compromised when stakeholder groups lack a mutual understanding of their shared goals, stakeholder groups do not understand the urgency or the need for sharing critical information due to a lack of shared knowledge of each other’s role and / or disrespect across stakeholder groups causes them to avoid communication (Gittell, 2012b:21).

In an auditing context, a multiple case study of Lenz and Sarens (2012) uses a combination of role theory and relational coordination theory to investigate internal audit effectiveness, particularly considering interpersonal factors. Lenz and Sarens (2012:2) conclude that interpersonal factors enhance perceptions of internal audit customers (particularly senior management as the ‘chief stakeholder’ of internal audit) about internal audit effectiveness. This is because having shared goals, shared knowledge and mutual respect facilitates internal auditors’ frequent, timeous and problem-solving communication to senior management. A subsequent publication by the IIA (Abdolmohammadi, Ramamoorti & Sarens, 2013) emphasises relational coordination constructs as key focus areas when the chief audit executive interacts with senior management.

In the context of this study, the relational coordination theory resonates with the aim of resolving stakeholder groups’ *disconnect* between their reciprocal influences on reliance, ensuring *their mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* becomes practicable.

6.5.2.2 Comparing the key constructs of the relational coordination theory to the emergent theory

Initially, Gittell (2006:75) links three constructs to relational coordination, namely, shared goals, shared knowledge and mutual respect. She explains that these constructs ensure that those in interrelated roles share a collective identity, engage in coordinated collective action and achieve a common desired outcome. Consistent with Gittell (2012b), the conceptual framework of interprofessional activity developed by Xyrichis *et al.*, (2018:417) proposes that shared goals across roles created by coordination foster a shared identity and some shared accountability. Gittell (2012b:8) adds the construct of communication to the theory of relational coordination, specifying four dimensions – frequent communication, timely communication, accurate communication and problem-solving communication. Combined, these constructs and dimensions embody mutual adjustments by those working at the role level to improve the effectiveness and efficiency of their interrelated performance (Gittell, 2012b:8).

The 'mutually reinforcing' effects between relational coordination constructs and the communication construct have been underlined by different researchers (Gittell, 2012b:21; Rubenstein, Barth & Douds, 1971:56-57; Newcomb, 1956:578). For example, on the one hand, inter-group communication is more effective when members of all groups understand their interrelated roles and distinct responsibilities – each other's decision-making responsibilities (shared goals) and technical know-how (mutual respect), as well as the importance of sharing 'change-relevant' information on a voluntary and frequent basis (shared knowledge) (Rubenstein *et al.*, 1971:56-57). On the other hand, having a strong relationship supports 'confrontation' style communication for decision-making, implying that 'open exchange' about the reasons for and ways to overcome intergroup conflict is possible, instead of '"forcing" one side's solution or "smoothing over" the situation' (Rubenstein *et al.*, 1971:56-57). Considering the interactions between communication and relational coordination constructs of the emergent theory, a context characterised by *facilitative communication*, in conjunction with *balancing oversight*, sustains *reciprocal synchronisation*, *a team mindset*, *habitual integration* and *fair alignment*.

Considering communication as the first construct of relational coordination, dimensions of communication (frequent, timely and problem-solving) are similar to those of *facilitative communication* in the emergent theory (section 6.4.1), while the relational coordination theory also mentions accurate communication. Scholars claim that frequent [regular] communication aids task-orientated information sharing while building stronger relationships (Gittell (2012b:17; Granovetter, 1973:1362). In an auditing context, frequent communication between the audit committee and external auditors improves external audit quality (Brown & Popova, 2016:27). Delayed rather than timely communication decreases the effectiveness and efficiency of performance, causing errors and / or delays (Gittell, 2012b:8; Waller, 1999:135). Similarly, rapidly changing environments benefit from face-to-face communication (Weick, 1993:642).

Inaccurate communication can cause errors or delays (Gittell, 2012b:18) and can undermine trust, making those who received such communication reluctant to use further information from the source of inaccurate or misleading information (Levin & Cross, 2004:1481). Written communication is most effective for sharing details about interrelated work (Hustoft, Hetlevik, Aßmus, Størkson, Gjesdal & Biringer, 2018:8). Problem-solving communication, also referred to as 'open communication' [extensive, unrestricted, confident, easy, covering reflection on lessons learned and ways to improve] (Gladstein,1984:500, 508), aligns stakeholder groups' distinct roles and conflicting goals (Pondy, 1967:298, 318). Its absence may result in blaming rather than a search for mutual agreement (Wageman, 1995:175). In an auditing context, sharing tacit knowledge from experiences working on global group audits improves audit quality (Downey & Bédard, 2019:123).

The second construct of the relational coordination theory is shared goals as a basis for a shared reality (Wentworth, 1980:103) and a collective responsibility (Wageman, 1995:174) when working towards a common desired outcome. Comparing the relational coordination theory construct of shared goals to the emergent theory, *reciprocal synchronisation* similarly creates a shared reality and collective reciprocal responsibility among stakeholder groups (section 6.4.2). Wentworth (1980:97) distinguishes between '*shared'* and '*common'* reality, explaining that shared reality implies compatibility, 'a working relationship coordinating and containing differences in subjective vantage points'. Thus, Wentworth (1980:103) contends that shared reality creates a 'sense of mutual presence', encouraging stakeholder groups' 'adherence to the rules of the context, whether or not one agrees with them fully', rather than adopting common values or beliefs.

The third construct of the relational coordination theory is shared knowledge as a basis for a 'collective mind' engaging in aligned effort to achieve a common desired outcome (Gittell 2012b:21; Weick & Roberts, 1993:357). Comparing shared knowledge as a construct of the relational coordination theory to the emergent theory, the collective identity fostered by *a team mindset* similarly mediates coordinated collective action in the form of *habitual integration* and *fair alignment* of internal and external auditors' interrelated work (sections 6.4.3, 6.3.4, 6.3.5). Gittell (2012b:19, 21) explains that '[s]hared knowledge informs participants of how their own tasks and the tasks of others contribute to the overall work process, enabling them to act with regard for the overall work process', making groups more appreciative of the need to share information required to effectively perform each other's role. Dougherty (1992:186,187) observes that different stakeholder groups' training and expertise may differ due to their different functional backgrounds, leaving them in different 'thought worlds' and 'systems of meaning', implying that they may lack understanding of critical issues requiring sharing (Dougherty, 1992:186, 187, 189). Shared knowledge creates a 'collective mind' about stakeholder groups' reciprocal influences on achieving a central desired outcome (Weick & Roberts, 1993:357).

The fourth construct of the relational coordination theory is mutual respect as a mediator of a collective mind engaging in coordinated collective action (Gittell, 2012b:21; Weick & Roberts, 1993:371). Comparing mutual respect as a construct of the relational coordination theory to the emergent theory, *a team mindset* implies mutual respect, as stakeholder groups view themselves as working as a joint team. Gittell (2012b:21) explains that '[r]espect for the work of others encourages participants to value the contributions of others and to consider the impact of their actions on others, further reinforcing the inclination to act with regard for the overall work process'. Weick (1993:642) posits that respect for others and their work builds enduring partnerships, strengthening interrelated performance as individual partners become more open to using information from other partners. 'Trust' is synonymous with 'respect' (Weick, 1993:642).

Conversely, Weick and Roberts (1993:371) point out that absence of the 'collective mind' associated with partnerships results in disrespectful behaviour among stakeholder groups. Group reactions to errors are slow or non-existent and / or they disregard the implications of changes in circumstances for other groups. Eisenberg (1990:160) also maintains that respect is a key concept in coordination. Weick (1993:638) underlines that 'respectful interaction' fosters a feeling of resilience rather than vulnerability between stakeholder groups, supporting interactions based on joint meaning or understanding. In contrast, Gittell (2012b:20) associates 'disrespect' with division among stakeholder groups, cautioning that 'occupational identity' could cause pride and discriminatory comparison between stakeholder groups.

In conclusion, the close alignment between the constructs of the relational coordination and the emergent theory positions (Glaser, 1978:38) the latter as a coherent and practicable means for balancing the reciprocal influences of each stakeholder group on reliance in order to achieve their *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

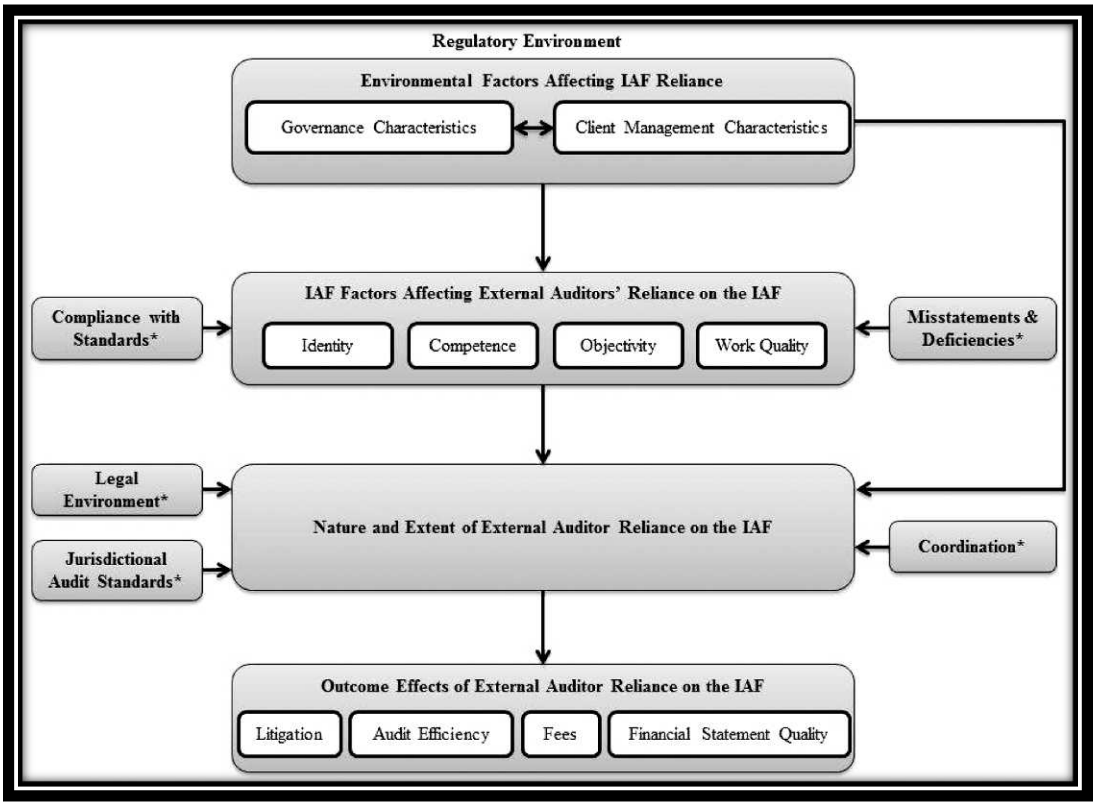
6.5.3 The summation model and organising framework developed from the most recent synthesis study on reliance

Reliance has been the focus (according to article titles) of more than 50 academic studies published in peer-reviewed journals over the last five decades. Two comprehensive synthesis studies have considered reliance and are relevant to this study. First, from the pre-SOX period, Gramling *et al.* (2004:199-209; 210-232) summarised 11 studies on external auditors' evaluations of internal audit quality and 23 reporting on internal audit's contribution to the financial statement audit (reliance). Second, Bame-Aldred *et al.* (2013) summarised 28 studies on reliance in the post-SOX period. A Google Scholar search conducted on 14 December 2019 sought to identify articles published since 2012 with all the words 'reliance', 'internal' and 'external' in their titles. A small number of articles was identified (for example Breger, Edmonds & Ortegren, 2019; Quick & Henrizi, 2019; Al-Twaijry, 2017; Pike *et al.*, 2016; Farkas & Hirsch, 2016; Malaescu & Sutton, 2015; Davidson *et al.*, 2013; Mohamed, Zain, Subramaniam & Yusoff, 2012). However, none of the studies following that of Bame-Aldred *et al.* (2013) considered reliance in a comprehensive manner. Consequently, the emergent theory is compared to the latest summation model and organising framework of extant knowledge of and knowledge gaps about practising reliance, namely that of Bame-Aldred *et al.* (2013).

Figure 6.2 below reflects the framework of reliance constructed by Bame-Aldred *et al.* (2013). The study raises 26 questions about practising reliance warranting research attention.

A comparison of the constructs of the emergent theory to the summation model and organising framework reveals similarities, mainly relating to the governance and internal audit function characteristics, influencing the credibility of internal audit work for statutory audit purposes. However, the emergent theory contributes practicable conceptualisations of governance and internal audit characteristics influencing reliance (sections 6.4.2.4 and 6.4.6).

Figure 6.2 Summation model and organising framework of external auditors' reliance on internal audit work



***Source**: Bame-Aldred et al. (2013:254)*

Several constructs of the emergent theory transcend the summation model and organising framework of Bame-Aldred *et al.* (2013). Specifically, the figure above does not consider communication between reliance stakeholders (section 6.4.1), aligning stakeholders groups' interpretations, interests and practices influencing reliance (section 6.4.2.1), certain factors linked to the reliance environment, including the size and regulation of the organisation, the maturity of risk management, the effectiveness of internal financial controls, the status of internal audit considering the value added by internal audit (reports), the profile and role of the chief audit executive (section 6.4.2.2), any factors influencing the relevance of internal audit work for statutory audit purposes (section 6.4.2.3), managing external audit quality and the external auditor's liability (section 6.4.2.5), inter-relational factors (section 6.4.3) and how internal and external auditors integrate and align their work (sections 6.4.4 and 6.4.5).

Given that key elements of the emergent theory are absent or incomplete in the work of Bame-Aldred *et al.* (2013:283), the emergent theory proposes leads which could be tested in future studies investigating the 26 questions listed by Bame-Aldred *et al.* (2013). Table 6.1 links key elements of the emergent theory and other insights from this study to each of the 26 questions for future research listed by Bame-Aldred *et al.* (2013:282-283).

Table 6.1 Link between key elements of the emergent theory and the 26 questions of Bame-Aldred *et al.* (2013)

Question No	Question of Bame-Aldred *et al.* (2013)	Key elements of the emergent theory
1	How does a client's compliance (or lack thereof) with the IIA Standards (in whole or in part) influence reliance decisions, audit efficiency, and fees?	External auditor participants indicated that differences between internal and external auditing professional standards and methodologies, as well as the competence of internal auditors has a greater influence on reliance than internal audit's compliance with internal auditing professional standards (EP B).
2	How do communications with appropriate internal audit function personnel, required by external auditing standards (IAASB, 2018: ISA 315 (Revised), influence external audits' nature, extent, and timing of audit procedures?	External auditors mostly consider the focus of internal audit work, evident from the mandate and plans, as well as problems highlighted in internal audit reports in this regard.
3	To what extent does management influence the internal auditor's work negatively, and how does the external auditor identify such cases?	The emergent theory specifies direct and indirect influences of management affecting the relevance and credibility of internal audit work for statutory audit purposes. These include management's influences on the maturity of risk management, the effectiveness of internal financial controls, the structure of the internal audit function, internal audit budget / capacity / resourcing, the status of internal audit considering the value added by internal audit (reports) and the profile and role of the chief audit executive. The value added by internal audit reports is indirectly impacted by management through their influence on the scope and focus of internal audit's mandate and plans, including by special investigations and *ad hoc* management requests, the competence of the internal audit team, the independence of internal audit, the standard of internal audit work and meeting internal audit plans (sections 6.4.2.2, 6.4.2.3 and 6.4.2.4).

4	How do cross-cultural variables influence the external audit decision process to rely on internal audit function?	Not addressed.
5	Why do some countries prohibit reliance on the internal audit function, and what influence does the prohibition have on audit quality, audit fees, and audit efficiency?	Not addressed.
6	How do governance quality factors (e.g., audit committee strength, tone at the top) interact to influence the external auditor's potential reliance on internal audit function?	The emergent theory specifies the quality of oversight by the audit committee as a key contextual condition influencing reliance (section 6.4.6).
7	How do internal audit function oversight decisions (employment arrangements, budget allocations, etc.) influence external audit reliance?	The emergent theory specifies realistic resourcing in line with internal audit's mutually agreed realistic mandate and plans which balances the benefit versus reward of work both included and excluded from internal audit's mandate and plans is a condition of reliance (sections 6.4.2.2 and 6.4.2.3) .
8	How do situations that simultaneously impact internal audit function competence, objectivity, and work quality impact external audit reliance?	Considering the number of quotations allocated to each influence on reliance, external auditors' reliance decisions put most emphasis on the status of internal audit considering the value added by internal audit reports, followed by the competence of the internal audit team and the independence of internal audit. The emergent theory specifies key indicators of the value added by internal audit reports include whether internal audit reports contain risk-focused findings and pragmatic recommendations addressing the real root causes of control problems leading to open acknowledgement and support for the value of internal audit to the business by the chief executive officer and management (section 6.4.2.2).
9	What is the appropriate model that incorporates audit risk, control risk, internal audit function competence, and internal audit function objectivity into potential external audit reliance on internal audit function work?	Not addressed.

10	How do external audits assess the competence/objectivity of the internal audit function work product, and what are the key factors that are examined in that assessment?	The emergent theory specifies an internal audit team with unquestionable competence consist of the right mix of skills to fulfil the internal audit's risk-focused mandate. Such teams are typically smaller, stable, consist mostly of senior level internal auditors with sufficient management level internal auditors and a majority of professional career internal auditors, complemented by internal auditors with specialist operational skills and business staff on a rotational basis (section 6.4.2.2). The emergent theory specifies that the chief audit executive effectively balances the relevance and unimpeded scope of internal audit's mandate, plans and reports, including by refraining from accepting operational and / or managerial activities, supported by a direct reporting line, direct access to and trust in the audit committee chair to address internal audit's challenges and keeps shared information confidential (section 6.4.2.2).
11	Do assessments of competence and/or objectivity vary by whether the external audits are contemplating (1) direct or indirect support, or (2) audits of financial statements or audits of internal control over financial reporting?	Not addressed.
12	What factors or biases, in addition to competence, objectivity, and work quality, drive the effect of internal audit function sourcing?	This study identifies that when external auditors reject a team mindset, they prefer working with external audit's own teams and favour reliance on outsourced internal audit work, particularly when the outsourced partner is a peer from a Big 4 accounting firm (section 6.4.3). In these circumstances, external auditors are prone to contrasting the superior credibility of their work compared to in-house internal auditors' work, as well as the superior professionalism of their profession against the inferior professionalism of the internal audit profession.
13	Has there been, or should there be, reliance on other activities that are audit-like, such as SOX groups within a company?	Although this study only considers reliance in the context of a statutory external audit, participants mentioned reliance occurred on internal auditors' SOX work as well, particularly when internal and external auditors collaborate on areas of the business affected by changes.
14	Does the perceived value of reliance differ between chief audit executives and audit committees when the external auditors rely on the internal audit function either directly or indirectly?	This study establishes that chief audit executives and chairs of audit committees did not distinguish between direct and indirect reliance (section 6.4.4). However, it does find optimal reliance requires a large proportion of direct reliance work edited into internal audit's reshuffled and aligned individual audit plans.

15	In which scenarios may external auditors be most likely to over-rely on the internal audit function?	Not addressed.
16	What internal audit function quality levels lead to external auditors' reliance for substantive tasks versus objective tasks such as testing controls?	This study identifies that when external auditors regard internal audit as weak, they limit reliance to reading internal audit reports and using peripheral support by internal auditors; they do not use internal auditors for direct assistance work (section 6.4.4). However, when internal audit is strong, external auditors mostly use internal auditors' direct assistance work consisting of controls assurance work and extensive substantive procedures.
17	Under what conditions do the external auditors rely on internal audit function work previously performed versus using the internal audit function as direct assistance?	The emergent theory associates *habitual integration* of internal and external audit work with work falling outside the internal auditing profession's definition of the typical scope and focus of internal audits. Such direct assistance work, specifically for statutory audit purposes, is edited into internal audit's reshuffled and aligned individual audit plans during alignment planning. Direct assistance work includes controls assurance work and extensive substantive procedures. Contrary to the typical business-wide risk focus of internal audit work, work with a strong financial focus increases reliance. Furthermore, most reliance is possible at subsidiary level where the usual internal audit approach is a transactional, end-to-end, integrated business process approach. This is as opposed to group level work of larger listed companies where the usual internal audit approach is a holistic governance process approach focusing on the control environment and significant risk of judgmental manipulation driven by management culture (section 6.4.2.3).
18	To what extent does the extent and nature of external auditors' reliance on internal audit function influence litigation outcomes?	Not addressed.
19	Do the internal audit function's competence and reporting lines influence judges' and jurors' determinations of external auditors' liability in audit failures in which external auditors relied directly or indirectly on, or utilised work done by, the internal audit function?	Not addressed.
20	What factors mitigate/exacerbate audit efficiency gains when relying on the internal audit function?	The emergent theory indicates that audit efficiency gains from *habitual integration* arise from habitually making internal audit work an integral part of evidence on the statutory audit, particularly when optimal integration of internal and external audit work is an integral part of the external audit firm's audit approach and methodology. In addition, efficiency gains from reliance are heightened when external auditors perceive the benefit from assessing internal audit and its work usually exceeds the cost, (particularly when a stable internal audit team performs well-developed stable internal audit processes in larger organisations) and does not experience technological and methodological alignment as issues

Source: *Own compilation*

		hampering reliance. Moreover, efficiency gains from reliance are amplified when all the stakeholder groups' focus on ensuring that assurance comes from the most effective and efficient provider. This means: a large proportion of direct assistance work was edited into internal audit plans for statutory audit purposes, consisting of controls assurance work with a financial focus and extensive substantive procedures; internal and external auditors identify overlap in their plans and minimise unnecessary duplication of internal and external audit work and audit queries through reshuffled and aligned audit plans (which improve assurance coverage and reduce external audit fees and work) (section 6.4.4, 6.4.5).
21	What is the relationship between internal audit function reliance and audit fees over time?	Not addressed.
22	Is there a differential effect on fees if the external auditors rely on the work of the internal audit function compared to using internal auditors as assistants?	The emergent theory holds that audit efficiency gains from *habitual integration* arise mostly from direct assistance work edited into internal audit plans for statutory audit purposes. In addition, the current study identifies that when direct assistance work is decreased, external audit fees increase. Furthermore, given that the emergent theory states that most reliance work has a financial rather than an operational focus, it is unlikely that internal audit's typical work with an operational focus would exacerbate audit efficiency gains to the same extent as dedicated direct assistance work (for example, as described in case E).
23	What is the relationship between the perceived quality characteristics of the internal audit function and the reduction in audit fees?	Not addressed individually.
24	What effects arise out of the over-reliance on the internal audit function?	Not addressed.
25	Are there any financial statement quality or audit quality issues that arise from various levels of internal audit function reliance?	Not addressed.
26	How does the disclosure of material weaknesses and/or restatements in a preceding year influence the external auditors' reliance on internal audit function work in subsequent years?	Not addressed.

Source: *Own compilation*

In conclusion, key elements of the emergent theory as well as general insights from the study transcend extant knowledge on reliance as described in the work of Bame-Aldred *et al.* (2013:283). Thus, future studies on reliance could test the key elements of the emergent theory, particularly focusing on the 26 questions of Bame-Aldred *et al.* (2013:282-283).

6.5.4 Internal and external auditing professional standards related to reliance

Internal and external auditing professional standards include requirements and guidance about reliance (IAASB, 2018: ISA 610 (Revised 2013); IIA, 2016: Standard 2050; IIA, 2015b: Practice Advisory 2050-1). This section considers how the requirements and guidance about reliance in the internal and external auditing professional standards compare to the constructs of the emergent theory.

6.5.4.1 Requirements in internal and external auditing professional standards related to reliance

This section briefly outlines the requirements and guidance in internal and external auditing professional standards dealing with reliance. At an overall level, external auditing professional standards contain a framework with requirements dealing with communicating planned reliance to management and the audit committee, discussing planned reliance with internal auditors, assessing the relevance and credibility of internal audit work for statutory audit purposes and reading internal audit reports. The standards also deal with procedures conducted on internal audit work and reports to determine their adequacy and quality for statutory audit purposes and to ensure sufficient external auditor involvement in the external audit as well as using direct assistance work of internal auditors (IAASB, 2018: ISA 610 (Revised 2013).

Internal auditing professional standards and practice advisories consider coordination of work by the chief audit executive with external assurance providers, particularly external auditors. At an overall level, the requirements and guidance mention information-sharing with external auditors and discussions and meetings between internal and external auditors. Meetings facilitate coordination of work, including about the timing of work and audit plan adjustments indicated by completed work and access to and follow up on matters included in external auditor's management letters and presentations (IIA, 2016: Standard 2050; IIA, 2015b: Practice Advisory 2050-1). Information sharing with external auditors should include the internal audit methodology and techniques, giving external auditors access to internal audit programmes, working papers, internal audit's communications to management and internal audit reports (IIA, 2015b: Practice Advisory 2050-1). In addition, the chief audit executive should evaluate and report to senior management and the board on the effectiveness and efficiency of coordination between internal and external auditors (IIA, 2015b: Practice Advisory 2050-1).

6.5.4.2 Comparing reliance requirements in internal and external auditing professional standards to the emergent theory

This section highlights differences between the individual constructs of the emergent theory and the requirements and guidance in internal and external auditing professional standards.

(a) Facilitative communication

The emergent theory incorporates *facilitative communication* at two levels – (A1) stakeholder groups' communication about planned and achieved reliance and (A2) communication between internal and external auditors to coordinate work. These are pervasive contextual conditions of stakeholder groups, sustaining their *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* (section 6.4.1). While the external auditing professional standard requires the external auditor to communicate how they plan to rely on internal audit work to those charged with governance (in accordance with ISA 260 (Revised) (IAASB, 2018) (IAASB, 2018: ISA 610 (Revised 2013) paragraph 20, 31)), such one-way factual transfer of information does not correspond with the emergent theory's conceptualisation of stakeholder groups' communication (section 6.4.1.1). Transcending the external auditing professional standard, the emergent theory posits that all stakeholder groups should participate in extensive and open discussions about planned and achieved reliance.

Furthermore, the external auditing professional standard emphasises that the external auditor should regularly engage with internal auditors to align internal and external audit work and to obtain information from internal auditors about significant matters that may affect the external audit (IAASB, 2018: ISA 610 (Revised 2013) paragraph 20, 31). Transcending the external auditing professional standard, the emergent theory submits that communication between internal and external auditors should incorporate mutual knowledge sharing on areas of concern as well as reflection on lessons learned and ways to improve assurance effectiveness and efficiency (section 6.4.1.2). While the internal audit practice advisory (IIA, 2015b: Practice Advisory 2050-1) does mention discussions between internal and external auditors to coordinate work, like external auditing professional standards, it is silent on stakeholder groups' communication about planned and achieved reliance and mutual knowledge-sharing between internal and external auditors about areas of concern.

(b) Reciprocal synchronisation

In the emergent theory, *reciprocal synchronisation* focuses on synchronising all stakeholder groups' assurance needs and responsibilities as well as the reciprocal influences of each stakeholder group on the reliance environment, the relevance and credibility of internal audit work for statutory audit purposes, and external audit quality and the external auditor's liability (section 6.4.2). First, the emergent theory transcends internal and external auditing standards as neither consider *reciprocal synchronising* of all the stakeholder groups' assurance needs and responsibilities (section 6.4.2.1).

Second, concerning the reliance environment, the external auditing professional standard refer to appropriate and adequate internal audit resourcing only in light of the organisation's size and nature of operations (IAASB, 2018: ISA 610 (Revised 2013) paragraph A8). The emergent theory also associates realistic internal audit resourcing with internal audit's mandate and plans. Furthermore, the extant theory transcends the external auditing professional standard by specifying additional environmental influences on reliance, including the maturity of risk management, the effectiveness of internal financial controls, the structure of the internal audit function, the status of internal audit considering the value added by internal audit (reports) and the profile and role of the chief audit executive (section 6.4.2.2).

Third, regarding the relevance of internal audit work for statutory audit purposes, the emergent theory and the external auditing professional standard consider the scope and focus of internal audit's mandate and plans (IAASB, 2018: ISA 610 (Revised 2013) paragraph 17) (section 6.4.2.3). However, the emergent theory transcends the external auditing professional standard by specifying additional determinants of the relevance of internal audit work for statutory audit purposes. These include the type of internal audit undertaken, the internal audit approach, collaboration between internal audit and risk management and the external audit approach (section 6.4.2.3). Providing additional novel insights, the emergent theory holds that reliance benefits when the scope and focus of internal audit's mandate and plans include a large proportion of direct assistance work and a large proportion of controls assurance work with a strong financial focus as well as following a transactional, end-to-end integrated business process approach (section 6.4.2.3).

Fourth, concerning the credibility of internal audit for statutory audit purposes, the emergent theory and the external auditing professional standard consider the competence of the internal audit team, the independence / objectivity of internal audit and the standard of internal audit work. In addition, the emergent theory considers internal audit's propensity for meeting and changing the internal audit plan (IAASB, 2018: ISA 610 (Revised 2013) paragraph 15-16, 27-28) (section 6.4.2.4).

For internal audit's competence, the external auditing professional standard considers the adequacy and appropriateness of resources, policies for hiring and assigning internal audit staff and technical training and professional certification of internal auditors (IAASB, 2018: ISA 610 (Revised 2013) paragraph A5-9). However, transcending the external auditing professional standard, the emergent theory holds that the meaning of adequate and appropriate internal audit competence is the product of the right mix of skills to fulfil the internal audit's risk-focused mandate, having a smaller, stable internal audit team consisting mostly of senior level internal auditors, including sufficient management level internal auditors, constituted by a majority of professional career internal auditors, complemented by internal auditors with specialist operational skills and business staff on a rotational basis (section 6.4.2.4).

For independence, the emergent theory and the external auditing professional standard mention internal audit's reporting lines and direct access to the audit committee. They also specify that internal audit should not accept conflicting internal audit responsibilities and that oversight of internal audit's employment decisions should be balanced against constraints or restrictions by management on internal audit. In addition, the external auditing professional standard mentions ethical requirements embedded in internal auditors' professional qualifications (IAASB, 2018: ISA 610 (Revised 2013) paragraph A5-9) (section 6.4.2.4). Transcending the external auditing professional standard, the emergent theory highlights that the chief audit executive's trust in the audit committee chair to resolve challenges faced by internal audit and to keep shared information confidential supports internal audit's independence (section 6.4.2.4). This is reflected in the chief audit executive's willingness to report even uncomfortable findings, verbally and in writing.

To gauge the standard of internal audit work, the emergent theory and the external auditing professional standard consider internal audit's audit documentation and quality control procedures. Transcending the external auditing professional standard, the emergent theory considers additional influences on and measures of the standard of internal audit work, including the role of the chief audit executive, the stability of the internal audit team, the stability and design of internal audit processes, the quality of the internal audit report and management's response to internal audit reports and recommendations (section 6.4.2.4).

Fifth, considering external audit quality and external auditor's liability, the emergent theory and the standard incorporate similar requirements (IAASB, 2018: ISA 610 (Revised 2013) paragraph 13, 15-20, 27-28, 31-32, A24). Transcending the external auditing professional standard, the emergent theory considers whether the combined approach to assurance and support by the audit committee mitigate undue reliance and minimise assurance gaps. The theory also contributes several factors that promote and moderate reliance in the context of external audit quality and external auditor's liability concerns (section 6.4.2.5).

(c) A team mindset

The emergent theory transcends internal and external auditing standards as neither explicitly consider the mindset of internal and external auditors, including inter-relational aspects influencing reliance (section 6.4.3). The emergent theory specifically refers to a combined approach, internal and external audit working together, internal and external auditors substituting and not simply complementing each other's work, the quality of the relationship between internal and external auditors and the working mindset of internal and external auditors.

(d) Habitual integration

The emergent theory and the internal auditing professional standard mention the possibility of improving assurance efficiency from reliance by reducing duplication (IIA, 2015b: Practice Advisory 2050-2). In contrast, the exclusive focus of the external auditing professional standard is audit effectiveness, ensuring appropriate reliance by preventing 'over and undue use' of internal audit work (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). In all other aspects, the emergent theory's conceptualisation of *habitual integration* of internal and external audit work transcends internal and external auditing professional standards (section 6.4.4). The emergent theory specifically considers stakeholder groups' interpretations of what reliance is, their commitment to reliance, the nature of reliance work, the cost-benefit of assessing internal audit and its work, who is best placed to provide the assurance, the external audit firm software and methodologies, overlap between internal and external audit work, duplication of audit work, and assurance effectiveness and efficiency, including a propensity for protecting audit firm fee income.

(e) Fair alignment

The external auditing professional standard recommends that external auditors should have access to internal audit reports and hold planning discussions with internal auditors at appropriate intervals throughout the audit period about the timing, nature and extent of internal audit's work. External auditors should share materiality levels for the financial statements as a whole, as well as at the account balance, class of transaction and disclosure level, and performance materiality levels with internal auditors. Internal and external audit should align their planned sampling and selection of audit items, documentation of work, and review and reporting procedures (IAASB, 2018: ISA 610 (Revised 2013) paragraph A24-25).

The internal auditing profession's practice advisory recommends that the chief audit executive should take steps to evaluate potential reliance on external audit work (IIA, 2015b: Practice Advisory 2050-1). This should include a review of external audit's methodology and working papers. Both standards mention that internal and external auditors should inform each other of significant matters affecting their assurance work (IAASB, 2018: ISA 610 (Revised 2013) paragraph A24-25; IIA, 2015b: Practice Advisory 2050-1).

While the emergent theory mentions all alignment actions referred to in internal and external auditing professional standards, it transcends these standards by providing additional conceptualisations of *fair alignment* (section 6.4.5). The emergent theory proposes that external auditors should move their audit planning earlier than usual to accommodate alignment planning with internal auditors and to allow simultaneous audit committee approval of their reshuffled aligned individual audit plans. Furthermore, internal and external auditors should engage in structured, upfront alignment planning discussions and workshops to reshuffle audit plans, reflecting both teams' aligned focus on key financial risks of control assurance work, aligned audit methodology on reliance areas and how internal audit could slightly change their work for increasing reliance.

Furthermore, the emergent theory proposes that methodological differences between internal and external audits should be addressed by ensuring that internal audit work earmarked for reliance is moved to the latter part of the year. It also proposes that early discussions should be held on the extent of tests, sample sizes and selection of audit items required for statutory audit purposes and that information should be shared on key risks. Lastly, the theory recommends aligning internal and external audit's responses to audit exceptions as well as securing internal audit's commitment to ensuring that they complete reliance work by agreed dates.

(f) Balancing oversight

While the emergent theory and the external auditing professional standard deal with specific aspects of oversight, including communication about planned reliance to those charged with governance and oversight of the independence of internal audit (IAASB, 2018: ISA 610 (Revised 2013) paragraph 20, 31, A7), the emergent theory also proposes pre-requisites for *balancing oversight* of the effectiveness and efficiency of reliance (section 6.4.6). These pre-requisites link audit committee strength to audit committee members' mix of financial and operational skills, risk view considering their business, financial and industry experience and insights, independence and orientation to sound governance.

In conclusion, the external auditor has sole responsibility for making the reliance decision and expressing an audit opinion (IAASB, 2018: ISA 610 (Revised 2013) paragraph 11). New conceptualisations in the emergent theory transcend external auditing professional standards, bridging knowledge gaps about reliance by explaining how all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* is viable and practicable.

In summary, the comparison between the emergent theory and extant theories, relevant literature and professional standards on reliance underscores that the emergent theory transcends extant knowledge in several ways. First, new theoretical constructs reflecting all stakeholder groups' reciprocal influences on reliance are proposed. Second, the new theoretical constructs are integrated into a substantive theory, providing a comprehensive holistic explanation of how all stakeholder groups achieve *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. Third, thick descriptions of each theoretical construct provide a comprehensive holistic understanding of the variables influencing reliance, considering the reciprocal influences of all stakeholder groups' roles, interpretations, interests and practices. Fourth, the new theory fits the data and is workable and relevant as it explains what is happening in practice. This means that it adds pragmatic knowledge to ensure the aim of achieving all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision,* is viable and practicable.

6.6 CONCLUSION

This chapter presents the fitting, workable and relevant theory which emerged from this study. The theory is presented in various formats, including as a storyline, a visual representation and a thick description of each construct and how it is integrated into the theory. Conceptualised dimensions of MORE and LESS reliance developed in

Chapter 5 and summarised in Table 4.6 to 4.15 form the basis of the theoretical constructs of the theory. The emergent theory explains how stakeholder groups resolve disconnect between their reciprocal influences on reliance to achieve *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*. The theory considers the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors on reliance.

In addition, the theory is compared to relevant extant theories, particularly the stakeholder theory and the relational coordination theory, the summation model and organising framework developed from the most recent synthesis study on reliance as well as internal and external auditing professional standards. This comparison highlights the contribution of the emergent theory to the literature and practice of reliance.

In the next and final chapter, the study is summarised and a conclusion is provided.

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CHAPTER 7

CONCLUSION AND RECOMMENDATIONS

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The published word is not the final one,
but only a pause in the never-ending process of generating theory.
(Glaser & Strauss, 1967:40)

7.1 INTRODUCTION

This final chapter concludes this classic grounded theory study explaining reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. The chapter starts with an overview of the study, considering the research problem and subsequent research question. Then, with the aim of the study in mind, the chapter presents the study's contribution to theory (literature) on reliance and to research methodologies applied when studying reliance. Thereafter, the chapter puts forward recommendations for professional bodies, auditing practitioners and each stakeholder group involved in reliance. Throughout this chapter, conclusions are triangulated to illustrative quotations from the further data set, comprising interviews with seven other knowledgeable senior internal and external audit professionals. Reflections on the quality of the study, its findings and its limitations are then presented. This is followed by suggestions for future research. The chapter concludes with a short concluding reflection.

Some quotations included in this chapter are in italics, similar to their presentation in the original texts.

7.2 ADDRESSING THE PROBLEM STATEMENT, RESEARCH AIM, RESEARCH QUESTION AND RELATED OUTCOME

Reliance refers to the incorporation of internal audit work into external audit evidence. Reliance is complex. This study responded to real-world implementation problems and prevailing academic knowledge gaps about practising reliance. Addressing the problems and knowledge gaps was important as they result in uncertainty about the effectiveness (quality) and efficiency of external audits, while they also raise questions about the value of internal audits.

The research problem which this study addressed was: There is no conceptualised explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. This problem persisted despite decades of academic research on reliance (for example, the studies included by Bame-Aldred *et al.*, 2013). However, these studies did not provide a conceptualised explanation of reliance. Most extant studies (1) solicited viewpoints about reliance from external auditors only, (2) used deductive methods, mostly experiments with external auditors, for testing relationships between one or a few variable(s) influencing reliance and / or (3) did not seek to conceptualise research findings about practising reliance.

In response to the research problem, *the aim* of this study was to construct a theorised (conceptualised) explanation of reliance on internal audit work by external auditors, which considered the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. This aim implied several methodological contributions. In contrast to prior studies' predominant focus on external auditors, this study solicited viewpoints from all stakeholder groups whose roles, interpretations, interests and practices in the statutory financial reporting and external audit processes provide the context for their reciprocal influences on reliance, namely the chief financial officer, the external audit engagement partner, the head of internal audit (commonly known as the chief audit executive) and the audit committee chair. Furthermore, in contrast to prior studies' predominant use of deductive methods, this study used the classic grounded theory methodology in three phases for inductive discovery of stakeholder groups' main concern about reliance and how they resolved it.

With the research aim in mind, *the research question* of this study was: How can reliance on internal audit work by external auditors be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors? The research question was addressed using data from 32 interviews. Five key data sets

(22 initial and three follow-up interviews) represented five diverse South African listed companies (cases). Each data set comprised data from the key stakeholder groups of the company, namely, the chief financial officer, audit committee chair, chief audit executive and external audit engagement partner. A further data set of seven interviews involved other knowledgeable audit professionals. Joint data collection, coding and analysis focused on the reliance process as the unit of analysis and participants' statements conveying their constructions of reliance, within the context of the reciprocal influences of the stakeholder groups' roles, interpretations, interests and practices, as the unit of observation. This study identified that stakeholder groups' main concern about reliance was the *disconnect* between their reciprocal influences on reliance. The core category, explaining how these stakeholder groups resolved their concerns influencing reliance was achieving *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

The outcome of this study was the substantive theory of balanced reliance, providing a conceptual explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors. This substantive theory fills the theoretical gap in knowledge, namely the lack of such a conceptual explanation. Methodologically, this inductive classic grounded theory study contributed a comprehensive holistic explanation of reliance, transcending extant fragmented deductive knowledge. Furthermore, this theory could prove useful to those encountering reliance in practice, including regulators, professional bodies and institutes, internal and external auditors and their organisations and firms, management and directors, when they evaluate, practise or oversee reliance, or develop related guidance or training.

A more detailed explanation of the study and its findings and contributions follows in the rest of this chapter.

7.3 OVERVIEW OF THIS STUDY

This study evolved from a general interest in explaining reliance, towards contributing a substantive theory of balanced reliance to the body of knowledge on the topic. In **Chapter 1**, a review of literature highlighted that reliance is complex. It is complicated by simultaneous, reciprocal influences of multiple stakeholder groups' roles, interpretations, interests and practices, and subject to ongoing debate about the value of internal auditing and the quality of external audits. On the one hand, this complexity gave rise to the real-world problem of inappropriate reliance, with the potential to reduce external audit quality. On the other hand, persisting knowledge gaps impeded fair balance between concerns for assurance (audit) effectiveness (quality) and efficiency (fees) when practising reliance. Highlighting the detrimental effect of these knowledge gaps, Krishnamoorthy (2001:512) states that improving reliance practices would improve the effectiveness and efficiency of assurance, and hence, the quality of financial reporting. A review of literature revealed that the central research problem was the absence of a conceptualised explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

Informed by the research problem, the research question addressed in this classic grounded theory study is:

> *How can reliance on internal audit work by external auditors be conceptually explained, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors?*

Chapter 2 contextualised reliance, considering what reliance is and the reciprocal influences on reliance by management's, the audit committee's, internal and external auditors' roles, interpretations, interests and practices in the statutory financial reporting and external audit processes *vis-à-vis* reliance.

Chapters 3 to 6 explicated the research process followed in addressing the research question.

Chapter 3 explained how interview data was obtained from the chief financial officers, chairs of audit committees, external audit engagement partners and chief audit executives of five diverse listed South African companies and other individuals knowledgeable about the subject of reliance. This data was then sampled, collected, compared, coded and analysed. Specifically, the participants' statements conveying their constructions of reliance, within the context of the reciprocal influences of the stakeholder groups' roles, interpretations, interests and practices perceptions of their own and other stakeholder groups' influences on reliance were elicited. These were the focus of initial and further theoretical data sampling, collection comparison and analysis. The study was done in three phases.

Chapter 4 provided an audit trail of the process of coding and analysis in the three phases of this study and explicated the outcome from phase 1.

For *phase 1*, the open coding and analysis of the key initial data sets to delimit the initial substantive categories and the main concern were explicated. This allowed the selection of the core category as the outcome of phase 1. Table 4.1 and 4.2 explicated the logic of the initial coding process and the initial substantive categories, while Table 4.3 presented a brief overview of the five key cases.

For *phase 2*, the selective and theoretical coding and analysis of initial and further data to the point where the substantive categories were saturated were explicated. Table 4.4 explicated the saturated categories and sub-categories showing how they subsumed initial categories refitted into them.

For *phase 3* the theoretical sorting delimiting the saturated substantive categories into theoretical constructs was explicated. Table 4.5 explained the theoretical construct names, while Table 4.6 to 4.15 explicated each category's properties and their dimensions influencing MORE and LESS reliance. The tables also included illustrative quotations supporting dimensions of MORE and LESS reliance and the concept indicators used during data coding. The theoretically sorted theoretical constructs (made up of delimited substantive categories and their properties and dimensions) carried forward to the presentation of the substantive categories in Chapter 5 and the presentation of the substantive theory in Chapter 6.

The data analysis revealed that the stakeholder groups' main concern was *disconnect* between their reciprocal influences on reliance, while the core category explaining most variation in their influences was achieving all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision*.

In **Chapter 5**, the analysed data was integrated into six substantive categories and five sub-categories, incorporating the properties of each category. For each property, the conceptualised dimensions influencing MORE and LESS reliance were then explicated. In **Chapter 6**, the conceptualised constructs of the emergent theory were described and integrated, using dimensions influencing MORE and LESS reliance explicated in Chapter 5.

Glaser (1978:7) contends that a grounded theory study ‘assumes a future contribution to a field … it assumes it can hold up in the world of evaluation and critique’. He adds that grounded theorists ‘*contribute a great deal by providing* [a] … *substantive theory*’, incorporating ‘conceptualized’ ‘indicators’ for testing by other scholars (Glaser, 1978:12, 13). The three sections below reflect on the contribution of the study in terms of its aim – to construct a theorised explanation of reliance on internal audit work by external auditors, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

7.4 THEORETICAL CONTRIBUTION OF THE STUDY

The overarching theoretical contribution of this classic grounded theory study is a substantive theory of balanced reliance offering a conceptualised explanation of reliance, considering the reciprocal influences of the roles, interests, interpretations and practices of management, the audit committee and internal and external auditors.

The theory defines and integrates constructs derived from inductive conceptualisations of qualitative empirical data (Glaser, 1978:3-4). The constructs comprise contextual, foundational, mediating and operational conditions for achieving all stakeholder groups’ *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision.* Chapter 6 contains the thick descriptions defining and integrating the constructs.

The comprehensive holistic insights provided by the theory make a valuable contribution to literature on reliance. First, the theory explains how all stakeholder groups can *achieve mutual agreement reliance that reliance is appropriate and fair, whatever the reliance decision*. Thus, the substantive theory matches and extends several knowledge gaps in the reliance literature discussed in Chapter 1. In particular, the substantive theory achieves (1) appropriate and fair responses by external auditors to management's pressure to increase reliance, (2) thus balancing the trade-off between external audit effectiveness (quality) and efficiency, (3) providing each stakeholder group (4) with a holistic (5) conceptualised explanation of their reciprocal influences on reliance.

Second, central to reliance is the debate about the value and effectiveness of internal audit and the quality of external audits. This study confirmed that reliance has implications for both these issues.

Participants (particularly audit committee chairs) viewed reliance on internal audit work during statutory external audits as evidence of the value and effectiveness of internal audits. Related illustrative quotations from the further data set of other knowledgeable senior internal and external audit professionals include:

Quotation 1: The relationship between reliance and the value of internal audit:

> 'I don't think internal audit is solely there to accommodate external audit, but I do think that where we can get to an agreement, especially where the coverage is a high risk, let's say it's a high-risk area and it's been assessed as a high-risk area by … management and the audit committee, and … where internal audit can play a role I think they should' (IAS 2).

Quotation 2: The relationship between reliance and the effectiveness of internal audit:

> 'The management must understand, all the stakeholders must understand. Because the more external auditors say no we are not relying on the work of internal audit, they think internal audit is not performing, which is wrong … We need to train management so that at least they understand that, both of us have a role to play in this whole governance and oversight. But the role is different' (IAS 3).

In terms of external audit quality, both external and non-external auditors highlighted that the reliance decision should consider the implications for external audit quality and the external auditor's liability. Related illustrative quotations from the further data set of other knowledgeable senior internal and external audit professionals include:

Quotation 3: Reliance (can) influence external audit quality:

> 'So maybe that force is on the [external] auditor to make use of the work of an internal auditor [and it] is driven by the companies wanting to bring down the cost of [external] audit but I think it's to the detriment of [external] audit quality' (IRBA TEAM).

Quotation 4: Reliance (can) influence the external auditor's liability:

> ‘I think the auditing standards are pushing more, especially with the new auditing standard on reliance on internal audit, that external audit is the sole firm [party] expressing an opinion on the financial statements, and the level of work that you need to do when you rely on another party is quite onerous and there’s quite a lot of procedures that you have to perform on it, that it becomes almost … the standard is pushing you … away from having reliance and that interaction with internal audit’ (Mid-tier 2).

The theory developed in this study puts forward several propositions. These propositions describe how theoretical constructs are related to each other and coherently fit into the theory, as discussed below.

OVERARCHING PROPOSITION: Balancing all stakeholder groups’ reciprocal influences on reliance is a condition of all stakeholder groups’ *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision.*

The overarching proposition can be broken down into five secondary propositions. Each secondary proposition is supported by a comprehensive list of dimensions associated with balanced reliance. Combined, these dimensions provide a comprehensive holistic explanation of stakeholder groups’ reciprocal influences on reliance.

Secondary Proposition 1: Willing *reciprocal synchronisation* of each stakeholder group’s roles, interpretations, interests and practices influencing reliance is a foundational condition which makes balanced reliance viable. Table 7.1 below summarises Secondary Proposition 1.

Table 7.1: Summary of Secondary Proposition 1

SECONDARY PROPOSITION 1	***Reciprocal synchronisation* addresses:**	**Dimensions depicting *reciprocal synchronisation* of each stakeholder group’s roles, interpretations, interests and practices influencing reliance:**

Stakeholder groups’ assurance needs and responsibilities	Assurance meetings	Holding regular combined assurance meetings:
		
		- With triangular participation by management and internal and external auditors
		- To develop a combined assurance mapping
		- For synchronising stakeholder groups’ assurance needs and responsibilities into:
		  o Shared goals
		  o An integrated risk and assurance view

	Distinct roles of internal and external audit	All stakeholder groups: - Mutually understand internal and external audit's interrelated distinct roles - Realise neither internal nor external audit can substitute each other's role
	Pressure to increase reliance	All stakeholder groups: - Focus on *balancing* assurance effectiveness and efficiency - Always favouring effectiveness over efficiency
Reliance environment	Size and regulation of the organisation	Larger, well-regulated organisations with: - A strong audit committee - Management who realises that they should balance profitability and good governance
	Maturity of risk management	A strong risk management function with senior management collaboration
	Effectiveness of internal financial controls	Strong internal financial controls which function effectively for the entire financial period
	Structure of internal audit function	A strong in-house internal audit function with a superior understanding of the business, including its key risks
	Internal audit budget / capacity / resourcing	Realistic resourcing, in line with internal audit's mutually agreed realistic mandate and plans
	Status of and value added by internal audit	The strong internal audit function is effective: - Internal audit's role as provider of assurance on combined assurance is formalised - Internal audit reports contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems - The chief executive officer and management openly acknowledge and support the value of internal audit to the business - External auditors prefer relying on work of the strong in-house rather than outsourced internal auditors

	Profile and role of the chief audit executive	A very strong head of internal audit:
		
		- Is a senior independent influential leader with:
		    o Business and industry insights
		    o A commercial orientation
		    o Hands-on assurance experience and qualifications
		    o The ability to communicate and contribute to the business at all levels
		    o The ability to accept and drive change
		- Is appointed by the audit committee
		- Is given direct access to the audit committee, the chief executive officer and the chairperson of the board
		- Effectively manages the relevance and credibility of internal audit work
		- Balances internal audit's resourcing and work by:
		    o Negotiating sufficient budget and appointing a sufficient number of competent internal auditors

		○ Using technology, including data analytics ○ Carefully considering opposing demands on internal audit resources, including by special investigations and *ad hoc* work for management - Receives all minutes of executive committee meetings and guides the audit committee about questioning management during meetings

Relevance of internal audit work for statutory audit purposes	Scope and focus of internal audit's mandate and plans	Management, the audit committee and internal audit: - Mutually agree on a realistic mandate and plan for internal audit - Ensures a balance between the benefit versus reward of work both included and excluded from internal audit's mandate and plans Internal audit plans include a large proportion of direct assistance work which: - Includes controls assurance work and extensive substantive procedures - Is included specifically for statutory audit purposes - Is edited into internal audit plans during alignment planning Internal audits have a strong financial focus
	Type of internal audit undertaken	Internal audits focus on risk-based audits, which address: - Key and evolving risks - Changing processes - Risks identified while internal and external auditors worked closely together on joint risk assessments
	Internal audit approach	Internal audits cover key risks: - Annually as part of a base audit plan, or - Internal and external audit rotate coverage of key risks Most reliance is possible at subsidiary level rather than at group level of larger listed companies as: - At subsidiary level reliance is simpler as internal audits usually incorporate a large volume of audit work, in accordance with a transactional, end-to-end, integrated business process approach - At group level reliance is hampered as the norm is complex internal audits in accordance with a holistic governance process approach, with emphasis on the control environment and significant risks associated with management's financial reporting culture
	Collaboration between internal audit and risk management	Risk management and internal audit work closely together, meaning they share an integrated risk view
	External audit approach	External audits: - Incorporate controls assurance work on key risks as part of a combined audit approach, and / or - Direct assistance work includes tests of controls and extensive substantive procedures

Credibility of internal audit work for statutory audit purposes	Competence of the internal audit team	The internal audit team consist of a sufficient number of internal auditors who possess unquestionable competence: - The right mix of skills to fulfil internal audit's risk-focused mandate - A smaller, stable team consisting of: o Mostly senior level internal auditors o Sufficient management level internal auditors o A majority of professional career internal auditors o Some internal auditors with specialist operational skills o Some business staff on a rotational basis
	Independence of internal audit	Internal audit's mandate, plans and reports are of unimpeded scope, as: - Management acknowledge they should not dictate the scope and focus of internal audit's mandate and plans - The chief audit executive: o Effectively balances the relevance and unimpeded scope of internal audit's mandate, plans and reports, without isolating internal audit from business realities o Refrains from accepting operational and / or managerial activities o Actively manages relationships between internal auditors and business staff, including by: ▪ Rotating internal audit teams, areas and auditees ▪ Continuous actions to raise awareness of and provide training on the importance of independence ▪ The internal quality assurance programme o Is supported by a direct reporting line and direct access to the audit committee chair o Trusts the audit committee chair will address internal audit challenges and honour the confidentiality of information shared o Is willing to report even uncomfortable findings, verbally and in writing
	Standard of internal audit work	Internal audit work is credible, as evident from: - A stable internal audit team - Well-developed, stable, risk-based internal audit processes (including the use of technology) - Compliance with the Standards - Quality audit documentation - Quality control procedures - Quality internal audit reports that contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems - Internal audit reports which incorporate all conclusions anticipated by the external auditor - Management relies on internal audit reports and recommendations
	Meeting and changing the internal audit plan	Internal audit mostly meets their flexible internal audit plans

External audit quality and the external auditor's liability	Riskiness of reliance	The external auditor carefully selects reliance work independently of external influences - the selection considers: - Whether the combined approach to assurance and support by the audit committee mitigate undue reliance and minimise assurance gaps - The relevance of internal audit work for statutory audit purposes - The credibility of internal audit work for statutory audit purposes
	Sufficient external auditor involvement in the audit of key risks	The external auditor carefully considers sufficient external auditor involvement in the audit as a whole, taking into account: - Sufficient external audit coverage - The efficiency of reperformance levels - The risk of material misstatement at the assertion level associated with the reliance environment - External audit wants to cover very significant risks themselves, usually by means of extensive substantive procedures - When a significant risk is present, external audit does not use internal audit work on the complete area - Rotating assurance work on key risks between internal and external audit to avoid unnecessary duplication of audit work while ensuring sufficient external auditor involvement in the audit

***Source**: Own compilation*

Secondary Proposition 2: With *reciprocal synchronisation* as a foundation, a voluntarily formed *team mindset* is the predominant mediating condition of balanced reliance which changes all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* from being viable to being practicable. Table 7.2 below summarises Secondary Proposition 2.

Table 7.2: Summary of Secondary Proposition 2

SECONDARY PROPOSITION 2 ***A team mindset***	**Attributes influencing *a team mindset*:**	**Dimensions depicting the presence of *a team mindset*:**

	Assurance approach	A combined approach to assurance:
		
		- Synchronise stakeholder groups' assurance needs and responsibilities in the context of their integrated risk and assurance view
		- Internal and external auditors have very clear and detailed shared knowledge of each other's work
		- Align reliance work on key risks of interest to both internal and external audit in their individual audit plans, considering:
		    o Key risks included in internal audit's rotational internal audit plans
		    o The need for external audit to cover these controls in years in-between

	Internal and external auditors working together	Internal and external auditors have a history of working well together

	Internal and external auditors substituting versus complementing each other's work	Internal and external auditors:
		
		- Substitute rather than simply complement each other's work, facilitated by:
		  o Internal auditors editing a large proportion of direct assistance work specifically for statutory audit purposes into their audit plans during alignment planning discussions and workshops
		  o Internal auditors making slight adjustments in the scope of their work
		  o Internal auditors identifying and relying on overlapping work included in both teams' audit plans which external audit performed or plan to perform

	Quality of the relationship between internal and external auditors	An enduring, voluntary, closer, professional working relationship formed between internal and external auditors is present, developed over time, growing from 'forced habit' to 'just the way' internal and external auditors work Internal and external auditors accept they have distinct roles
	Working mindset of internal and external auditors	Internal and external auditors: - View themselves as a joint team - Speak the same language - Provide combined assurance - Often issue a single report to management and the audit committee on specific areas of the audit, although the external auditor signs the statutory auditor's report - Engage in regular meetings and constructive debates throughout the year where internal auditors share their deep insights, gained from daily involvement in the business, with external auditors - Learn from each other - Jointly face increasing assurance requirements and demands on them and their budget / capacity / resourcing constraints - The external auditors offer continuous development opportunities to the internal auditors of their clients

***Source**: Own compilation*

Secondary Proposition 3: *A team mindset* is the predominant mediator of *habitual integration* of internal and external audit work, as a co-variant operational condition of balanced reliance, which is essential for making all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* practicable. Table 7.3 below summarises Secondary Proposition 3.

Table 7.3: Summary of Secondary Proposition 3

SECONDARY PROPOSITION 3 *Habitual integration*	Attributes influencing *habitual integration*:	Dimensions depicting *habitual integration*:
	What reliance is	Internal audit work forms an integral part of evidence on the statutory audit
	Internal and external auditors' commitment to reliance	The external auditor: - Habitually practises optimal integration of internal and external audit work - Accepts reliance on internal audit work as much as possible as an integral part of the external audit firm's audit approach and methodology
	Nature of reliance work	Reliance work includes a large proportion of direct assistance work for statutory audit purposes, which: - Includes controls assurance work with a financial focus - Includes extensive substantive procedures - Is edited into internal audit plans - Implies external auditors rely on internal audit's direct assistance work of a routine nature - Allows external auditors to concentrate on more complicated or riskier work
	Cost-benefit of assessing internal audit and its work	External auditors perceive that the benefit of assessing internal audit and its work usually exceeds its cost, particularly when: - A stable internal audit team - Performs well-developed stable internal audit processes - In larger organisations
	Who is best placed to provide the assurance	All the stakeholder groups focus on ensuring that assurance comes from the most effective and efficient provider, considering: - The combined cost of internal and external audits - The level of assurance required - Whether internal audit's focus is operational or financial - The geographical location of audit sites - Planned visits by internal audit to sites of third-party service providers of the organisation
	Influence of external audit firm software and methodologies on reliance	External auditors do not perceive external audit firm software and methodologies as hampering reliance
	Overlap between internal and external audit work	Alignment planning identifies overlapping work in internal and external audit plans
	Duplication of audit work	Aligned individual audit plans minimise: - Unnecessary duplication of internal and external audit work

		- Unnecessary duplication of audit queries for management's attention - Assurance gaps - Ensure as much cross-coverage as possible

	Assurance effectiveness and efficiency, including external auditors' propensity for protecting audit firm fee income	All stakeholder groups:
		
		- Focus on balancing assurance effectiveness and efficiency, yet favouring effectiveness over efficiency, including by either team using data analytics to:
		  o Improve assurance coverage
		  o Reduce audit fees and work
		- Respecting:
		  o The distinct roles of internal and external audit, in particular the effect of reliance work on internal audit's business-wide risk focus, concentrating on controls assurance work with mostly an operational focus
		  o The need to duplicate or extend some internal audit work to ensure sufficient external auditor involvement in the audit of key risks
		  o Internal audit's implicit contribution to external audit effectiveness, considering what work external auditors are doing and what work they would have done if no internal audit was present

***Source**: Own compilation*

Secondary Proposition 4: *A team mindset* is the predominant mediator of *fair alignment* of internal and external audit work, as a co-variant operational condition of balanced reliance, which is essential for making all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* practicable. Table 7.4 below summarises Secondary Proposition 4.

Table 7.4: Summary of Secondary Proposition 4

SECONDARY PROPOSITION 4 ***Fair alignment***	**Attributes influencing *fair alignment*:**	**Dimensions depicting *fair alignment*:**

	Alignment planning	External auditors move their audit planning earlier than usual, to before the start of the financial year, to accommodate alignment planning
		
		Internal and external auditors hold structured, upfront alignment planning discussions and workshops well before the beginning of the financial year
		
		Alignment planning involves:
		
		- Lots of good communication
		- Internal and external auditors working closely together to:
		  o Ensure a combined approach to assurance
		  o Develop a shared understanding of each other's requirements for professional work and plans influencing reliance
		  o Liaise about incorporating specific additional work in and making slight changes to internal audit's plans to increase reliance opportunities

		○ Identify areas where external audit was inadvertently performing extensive substantive procedures where reliance on internal audit's controls assurance work should be possible ○ Plan reliance around internal audit's three-year rotational plan by using internal audit's work on key areas of control in years when internal audit tested them, while the external audit team audited those controls in the years in between ○ Reshuffle and align their individual audit plans ○ Present their reshuffled and aligned plans simultaneously for review by management and approval by the audit committee, well before the beginning of the financial year Aligned plans: - Consider internal audit's findings on the effectiveness of internal financial controls - Reflect an aligned focus on controls assurance work - Address key financial risks - Meet external audit requirements for sufficient involvement in the external audit
	Alignment planning of internal and external audit's focus	Internal and external auditors' reshuffled plans reflect an aligned focus on key financial risks
	Alignment planning of internal and external audit's objectives and approaches	Internal and external auditors' reshuffled plans reflect aligned objectives and approaches focused on control assurance work
	Alignment planning of internal and external audit's methodologies	Internal and external auditors' reshuffled plans reflect aligned audit methodologies meeting external audit requirements on reliance areas
	Alignment planning of internal and external audit's period covered by reliance work	The period covered by reliance work is aligned as: - Timeous alignment planning ensures that internal audit covers the majority of the financial year - Internal audit moves internal audit work earmarked for reliance to the latter part of the year
	Alignment planning of internal and external audit's sampling and selection	Sampling and selection are aligned as: - Early planning meetings allow external audit influence on the extent of tests, sample sizes and selection of audit items - External audit plans reflect reduced total sample sizes per test in line with the number of items for testing indicated in internal audit plans
	Alignment planning of internal and external audit's	Internal and external audit's responses to audit exceptions are mostly aligned as: - Internal and external auditors work closely together

	response (time) to audit exceptions	- Reliance work includes a large proportion of credible direct assistance work planned, supervised and reviewed by external auditors
	Alignment planning of internal and external audit's, timing of internal audit work	The timing of internal audit work does not jeopardise the meeting of external audit's reporting deadlines as: - Internal and external auditors work closely together - Reliance work includes a large proportion of credible direct assistance work planned, supervised and reviewed by external auditors
	Meeting the aligned audit plans	Aligned audit plans are met as: - Internal and external auditors work closely together - Reliance work includes a large proportion of credible direct assistance work planned, supervised and reviewed by external auditors

Source*: Own compilation*

Secondary Proposition 5: Stakeholder groups' participation in *facilitative communication* and a strong audit committee's *balancing oversight* jointly create a context sustaining *reciprocal synchronisation*, *a team mindset*, *habitual integration* and *fair alignment*. Table 7.5 below summarises Secondary Proposition 5.

Table 7.5: Summary of Secondary Proposition 5

SECONDARY PROPOSITION 5	Attributes influencing ***facilitative communication* and *balancing oversight*:**	**Dimensions depicting *facilitative communication* and *balancing oversight*:**
Facilitative communication	Stakeholder groups' communication about planned and achieved reliance	All stakeholder groups engage in extensive, open discussions about planned and achieved reliance Stakeholder groups' focus during discussions is on assurance effectiveness and efficiency, yet favouring effectiveness over efficiency External auditors perceive that management, the audit committee and internal auditors are reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance
	Communication between internal and external auditors to coordinate work	Internal and external auditors engage in: - Unrestricted, confident and easy communication - Consisting of open, formal and informal communication - Frequent conversations and regular meetings throughout the year - Covering mutual knowledge sharing on areas of concern

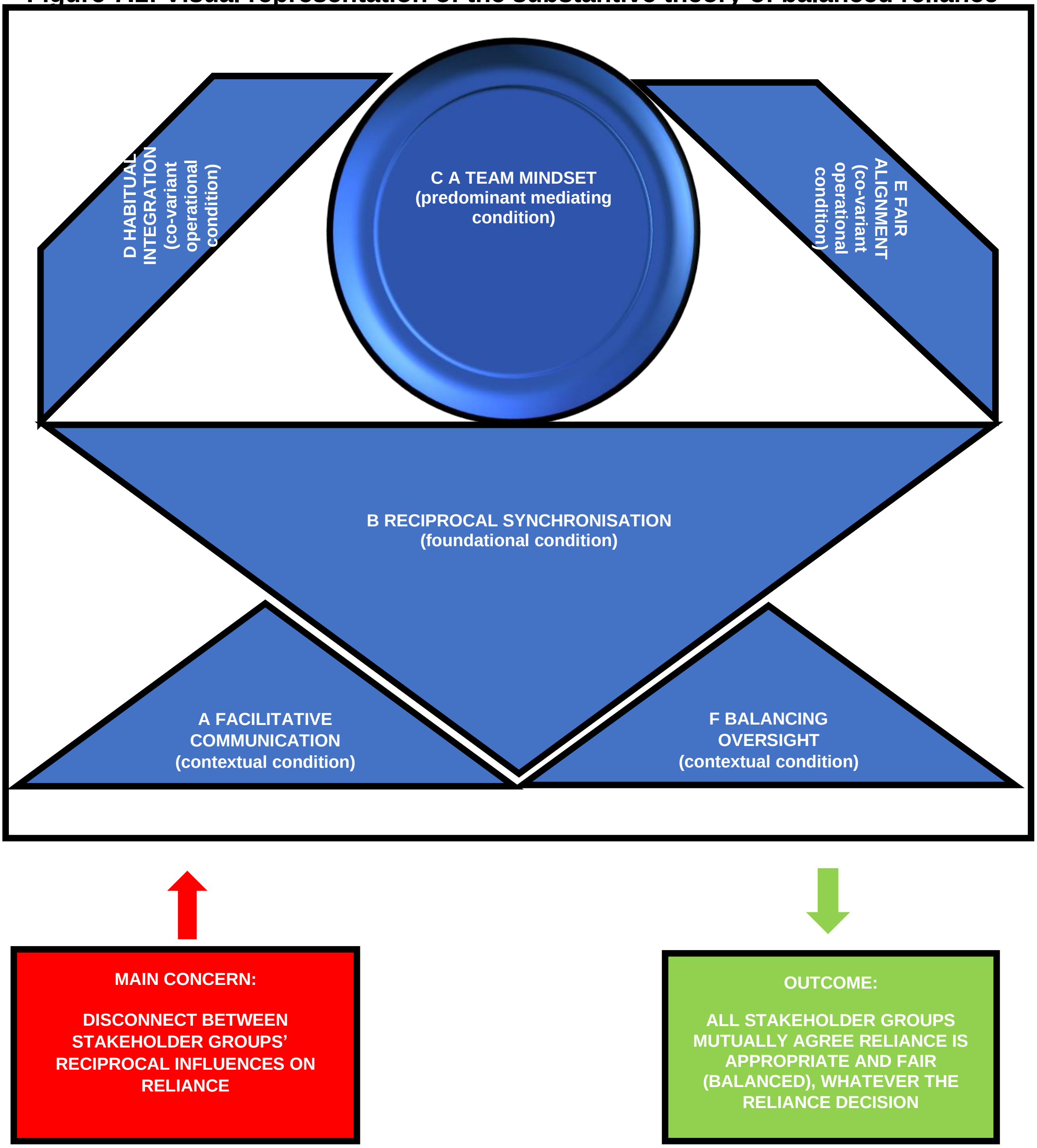
		- Reflection on lessons learned and ways to improve assurance effectiveness and efficiency
Balancing oversight	Audit committee oversight of assurance effectiveness and efficiency	A strong audit committee mitigates the external auditors' engagement risk by: - Overseeing implementation of a formalised combined approach to assurance as a means for synchronising stakeholder groups' assurance needs and responsibilities and achieving assurance effectiveness, including minimising assurance gaps and improved coverage - Balancing the influence of managements' general focus on profit margins on having strong governance in the form of: o Strong internal financial controls o A strong internal audit function, including by approving the internal audit budget o A competent independent chief audit executive - Although the audit committee may also exert some pressure on external auditors to increase reliance, balancing management's pressure to increase reliance against the effect of reliance on external audit quality and the external auditor's liability, including when it: o Is reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance - Balancing management's influence on the relevance of internal audit work for statutory audit purposes, including when it: o Approves changes to the scope and focus of internal audit's mandate and plans which threaten internal audit's risk-based focus, for example special investigations and *ad hoc* work for management - Balancing management's influence on the credibility of internal audit work for statutory audit purposes, including when it: o Evaluates the competence of the internal audit team annually o Gives the chief audit executive direct access to the audit committee o Reviews the outcomes of external assessments of internal audit quality o Monitors whether internal audit meets their plans
	Audit committee's inherent strength and closeness to the business	A strong audit committee: - Shares members with the risk committee or engage about risks and controls in joint meetings with internal audit and risk management prior to quarterly audit committee meetings - Knows and understands the trustworthiness of the management of the organisation - Has the support of the strong head of internal audit - Asks the right questions of management, internal and external audit - Engages in 'focused conversation' during robust audit committee meetings where there are extensive discussions about areas of concern, for example as highlighted in internal audit reports A strong audit committee is empowered by: - A 'business sense' - Knowledge of governance requirements - A mix of appropriate financial and operational training and experience - A strong risk view grounded in business, financial and industry insights - An uncompromising emphasis on sound governance - Strong upfront succession-planning of audit committee members A strong audit committee is supported by internal audit who provides it with:

		- Internal audit reports detailing risk and control problems, their impact and who should take responsibility for addressing them
		- Updates in documentation ‘packs’ and during ‘closed sessions’ without management present on:
		  o The state of risks and controls
		  o Whether management take internal audit findings seriously
		  o Questions to raise with management

***Source**: Own compilation*

The propositions of the substantive theory of balanced reliance are represented visually in Figure 7.1 below.

Figure 7.1: Visual representation of the substantive theory of balanced reliance



7.5 METHODOLOGICAL CONTRIBUTION OF THE STUDY

This study applied the classic grounded theory methodology to construct a conceptual explanation of reliance, considering the reciprocal influences of the roles, interpretations, interests and practices of management, the audit committee and internal and external auditors.

The methodology used in this study is innovative for three reasons, thus extends extant knowledge. First, most prior reliance studies have used deductive methods, typically experiments, for testing relationships between *a priori* determined variables influencing reliance. These were mainly derived from external auditing professional standards. Examples include the studies referenced in the synthesis of Bame-Aldred *et al.* (2013) and Gramling *et al.* (2004). Using an inductive qualitative grounded theory methodology, without a preselected or *a priori* theory, allowed the empirical identification of novel influences on reliance.

Second, most prior studies on reliance sourced empirical data from external auditors only, for example, most studies referenced in the synthesis of Bame-Aldred *et al.* (2013) and Gramling *et al.* (2004). In contrast, this study adds novel explanations of reliance based on empirical data collected from all stakeholder groups involved in the statutory financial reporting and external audit processes. These include management, the audit committee and internal and external auditors. This methodological approach also contributes to the quality of the study, as data was not randomly collected but sourced from the individual with the highest level of accountability in each stakeholder group at each data site, namely, the chief financial officer, the external audit engagement partner, the head of internal audit (commonly known as the chief audit executive) and the audit committee chair.

Third, no prior empirical study has developed a comprehensive holistic explanation of reliance or proposed a substantive theory, as each considered relationships between two or a few influences on reliance. This study contributes a substantive theory, providing a comprehensive explanation of reliance. The theory explains how stakeholder groups make *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* viable and practicable.

Fourth, given the limited use of grounded theory studies in auditing, specifically when studying the audit process, the step-by-step explanation (Chapters 3 to 6) add to the quality of the findings. It also contributes to the literature on research methodology within a classic grounded theory research process. The explanation could be useful for other novice researchers contemplating grounded theory studies.

7.6 CONTRIBUTION OF THE STUDY TO PRACTICE

The new theory of balanced reliance fits the data and is workable and relevant insofar as it explains what is happening in practice. The theory thus adds pragmatic knowledge for making all stakeholder groups' *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* viable and practicable (Glaser, 1978:4, 38, 134; Glaser & Strauss, 1967:2). Thus, theory and practice are brought together, allowing stakeholder groups to 'chang[e], reshap[e] and improv[e]' reliance (Corley & Gioia, 2011:12 in Brennan & Kirwan, 2015:481). Ahrens, Filatotchev and Thomsen (2011:321) urge researchers not to overlook the value of seemingly simple or minor changes for improving governance.

Given that a number of the conceptualised dimensions and theoretical constructs of the theory are not currently addressed in internal and external auditing standards or in literature (Chapter 6), the theory could prove useful when reviewing reliance in a practice context. First, professional bodies of internal and external auditors and regulators of external auditors could use the theory to review current requirements and guidance on reliance and related professional development courses. In this regard, Bame-Aldred *et al.* (2013:280) indicate regulators could use research findings to 'draft regulations and oversee the profession in such a way that reflects an understanding of the complex environment in which practitioners make reliance decisions'.

Second, audit firms could use the theory to review their audit methodologies and training offered to professional staff. Such training could be useful as the PCAOB urged external auditors to consider additional training for auditing personnel on practising reliance in an appropriate manner (PCAOB, 2013:35).

Third, the Institute of Directors in Southern Africa (IoDSA) could refer to the theory when training directors, including audit committee members, on the reliance aspect of combined assurance.

Fourth, boards of directors could use the governance related conceptualisations in the theory, for example about a strong internal audit function and audit committee, when reviewing and revising the strength of governance in their organisations.

Fifth, financial heads in companies could use the theory as a basis for discussing reliance with audit committees and internal and external auditors.

Sixth, each stakeholder group could use the theory when contemplating and practising reliance. Below, each stakeholder group's major practical contributions to reliance are described.

7.6.1 Management's contribution to reliance

Management have an indirect effect on reliance, through their influence on the reliance environment, the relevance and credibility of internal audit work for statutory audit purposes and participation in combined assurance. Two related illustrative quotations from the further data set of other knowledgeable senior internal and external audit professionals include:

Quotation 5: The influence of the reliance environment created by management on reliance – the status of internal audit:

> 'What happens to their [internal audit] reports? Are someone [management] seriously looking at it and trying to change the way people do things, or are they just trying to window dress and so we have internal audit … That's the kind of things that I would look at [when making the reliance decision]' (Mid-tier 1).

Quotation 6: The influence of the reliance environment created by management on reliance – the strength of internal controls:

> '[To] determine whether external audit can in fact place reliance … it's not just about the quality of the work, it's about the quality of the result of what comes out of the [internal audit] findings that will determine whether the external auditor would actually [rely]… whether they can in fact place reliance on the controls. As much as they can place reliance on the internal audit work, what may happen is that the controls are either inadequate or inadequate and ineffective which means that they [external audit] may need to go with a totally substantive audit approach' (Mid-tier 1).

Table 7.6 details what management could do to contribute to appropriate and fair (balanced) reliance.

Table 7.6: Management's contribution to appropriate and fair (balanced) reliance

Management should:	
Facilitative communication	Engage in extensive open discussions with internal and external auditors, as well as the audit committee, about planned and achieved reliance, displaying a mindset favouring assurance effectiveness over efficiency
Reciprocal synchronisation: Stakeholder groups' assurance needs and responsibilities	Participate in regular combined assurance meetings to develop a combined assurance mapping, clearly reflecting stakeholder groups' shared goals and an integrated risk and assurance view Manage expectations about internal audit's role, especially when the function is also required to perform work specifically for external audit purposes Incorporate balanced reliance expectations, cognisant of assurance effectiveness and efficiency, in internal audit's mandate and plans, if desired (as approved by the audit committee)
Reciprocal synchronisation: The reliance environment	Follow a strategy that balances profitability with good governance Implement a strong risk management function with senior management collaboration Implement strong internal financial controls which function effectively for the entire financial period Implement a strong in-house internal audit function that uses technology to overcome resourcing constraints Provide realistic resourcing in line with internal audit's mutually agreed realistic mandate and plans, cognisant of implications when internal audit performs work specifically for external audit purposes and special investigations and *ad hoc* work for management Formalise internal audit's role as provider of assurance on combined assurance Openly acknowledge and support the value of internal audit to the business (particularly the chief executive officer) Support the appointment of a very strong head of internal audit with direct access to the audit committee, the chief executive officer and the chairperson of the board A very strong head of internal audit should be a senior independent influential leader, who has: - Business and industry insights - A commercial orientation - Hands-on assurance experience and qualifications - The ability to communicate at all levels - The ability to accept and drive change Obtain the audit committee's approval for the appointment of the chief audit executive Provide the chief audit executive with minutes of all executive committee meetings

Reciprocal synchronisation: The relevance of internal audit work for statutory audit purposes	Mutually agree with the audit committee and internal audit on a realistic mandate and plans for internal audit, and refrain from overloading internal audit with conflicting demands, for example, special investigations and *ad hoc* work for management If they decide to prioritise reliance in favour of (in addition to) internal audit's wider assurance role, they must: - Provide resources allowing internal audit to (also) edit a large proportion of direct assistance work (including controls assurance work and extensive substantive procedures) for statutory audit purposes into internal audit plans during alignment planning - Agree that internal audits should (also) have a strong financial focus, with or without a strong operational focus - Ensure internal audit's realistic mandate allows a focus on risk-based audits - Ensure internal audit resourcing allows annual assurance work on key risks and controls - Understand that most reliance is possible at subsidiary level rather than at group level of larger listed companies, as internal audits at subsidiary level usually incorporate a large volume of audit work, in accordance with a transactional, end-to-end integrated business process approach - Provide structures and opportunities for risk management and internal audit to work closely together, enabling an integrated risk view - Understand external audit's combined audit approach is conditional on strong internal financial controls and does not mean external audit performs no substantive procedures

Reciprocal synchronisation: The credibility of internal audit work for statutory audit purposes	Ensure realistic internal audit resourcing allows the appointment of a sufficient number of internal auditors with unquestionable competence, consisting of:
	
	- The right mix of skills to fulfil internal audit's risk-focused mandate
	- A smaller, stable team consisting of:
	    o Mostly senior level internal auditors
	    o Sufficient management level internal auditors
	    o A majority of professional career internal auditors
	    o Some internal auditors with specialist operational skills
	    o Some business staff on a rotational basis
	
	Allow the unimpeded scope of internal audit's mandate, plans and reports
	
	Ensure realistic internal audit resourcing allow credible internal audit work by a stable internal audit team managed by a very strong head of internal audit, including the use of technology, for example data analytics
	
	Support and monitor internal audit's well-developed stable risk-based internal audit processes, in compliance with the Standards, including the requirements for quality audit documentation and quality control procedures
	
	Consider internal audit reports and implement recommendations, as appropriate
	
	Ensure that the mutually agreed realistic internal audit mandate and realistic resourcing of internal audit make it possible for internal audit to meet their flexible internal audit plans
	
	Recommend and support the use of the 80 / 20 principle to allow for internal audit's responses to changing and emerging risks, including any special

	investigations and *ad hoc* work for management which could impact on the normal assurance work
Reciprocal synchronisation: External audit quality and the external auditor's liability	Allow the external auditor to independently select reliance work Be cognisant of the requirement of sufficient external auditor involvement in the audit as a whole, taking into account: - Sufficient external audit coverage - Reperformance levels - The risk of material misstatement at the assertion level associated with the reliance environment - The effect of significant risks on reliance
Team mindset	Understand that internal and external auditors have distinct roles Understand the influence of engagement risk on the external auditor's decision to adopt a team mindset Support, participate in and monitor a combined approach to assurance Discuss increasing assurance requirements and demands with the audit committee and internal and external auditors to come up with a joint plan that address them Enquire about and encourage internal audit to make use of continuous development opportunities offered by external auditors to their clients
Habitual integration	Understand the influence of the external auditor's engagement risk when habitual integration of internal and external audit work is encouraged Promote assurance coming from the most effective and efficient provider, taking into account: The combined cost of internal and external audits The level of assurance required Whether internal audit's focus is operational or financial The geographical location of audit sites Planned visits by internal audit to sites of third-party service providers of the organisation Ensure a balance between efficiency-driven reliance expectations and assurance effectiveness in strategic and other plans, keeping in mind: - The distinct roles of internal and external audit, in particular the effect of reliance work on internal audit's business-wide risk focus, concentrating on controls assurance work with mostly an operational focus - The need to duplicate or extend some internal audit work to ensure sufficient external auditor involvement in the audit of key risks - Internal audit's implicit contribution to external audit effectiveness, considering what work external auditors are doing and what work they would have done if no internal audit was present
Fair alignment	Understand and support fair alignment of internal and external audit work, remaining cognisant of the external auditor's engagement risk, including by: - Encouraging early engagement by internal and external auditors in alignment planning - Encouraging liaison between internal and external auditors about changing, reshuffling their plans when aligning their work and

	professional requirements - - Reviewing and discussing the reshuffled aligned plans in a meeting with internal and external auditors
Balancing oversight	Understand and support the role of the strong audit committee, including its role in overseeing reliance

***Source**: Own compilation*

7.6.2 Internal audit's (particularly the chief audit executive) contribution to reliance

Internal audit has a direct influence on reliance, through the relevance and quality of internal audit work performed for statutory audit purposes (including the quality of direct assistance work) and alignment planning with external auditors. Two related illustrative quotations from the further data set of other knowledgeable senior internal and external audit professionals include:

Quotation 7: The important influence of the chief audit executive on internal audit effectiveness and reliance:

> 'I think that [the status of internal audit] is actually critical, if you ask me and whether this is about chief auditor executive or whether it is an outsourced function, let's call it the account leader or the account partner, I think that actually really determines … my view of the internal function function. You can do wonderful, detailed internal audits, but if your chief audit executive doesn't know they have the respect of the organisation or the person is unable to influence the thinking of the executives, in my view then, then it is not going to work. So that role for me is very critical and it is actually very important, that that person is at the right stature and able to communicate at the right level and have the respect of the organisation because … a [wrong] chief audit executive will negatively impact an internal audit function. Where there is a strong chief audit executive, that will certainly uplift internal audit or make sure that there is the right respect for the internal audit function… [The chief audit executive should be] robust … not afraid … of the right calibre … [not] somebody that will just tell [management] the good news. I don't want somebody that just wants to have the easy conversations. I actually want somebody that … will not be afraid to challenge [management], will not be afraid to give his or her own views, based on the work that they had performed. That for me is crucial' (IAS 1).

Quotation 8: Reliance on work performed by a well-resourced competent internal audit function:

> 'Where [external audit] does work with sophisticated internal audit departments where they have lots of resources, is to also assist with … general IT controls environment where they evaluate and they document and they test it. We come in and we look at the work that they have done, but also obviously when you do [rely] … [external auditors consider if they have] assessed the skills of internal audit and [determined that] they do

have sufficient skills on the [quality] review levels, to be able to do that kind of work. Because we find that's an area that internal audit very much sometimes cover as a normal part of their procedures, and when you have an IT environment where it is critical for the business that they do look at the general IT controls, more application controls for the system, and when we can come in and we can look at detailed work that they've done and that does create an area we can be more … where you can pick up efficiencies' (Mid-tier 2).

Table 7.7 details what internal audit could do to contribute to appropriate and fair (balanced) reliance.

Table 7.7: Internal audit's contribution to appropriate and fair (balanced) reliance

Internal audit (particularly the chief audit executive) should:	
Facilitative communication	Engage in extensive open discussions with management and external auditors, as well as the audit committee, about planned and achieved reliance, displaying a mindset favouring effectiveness over efficiency Engage with external auditors to coordinate internal and external audit work, by means of: - Unrestricted, confident, easy and open (formal and informal) communication - Frequent conversations and regular meetings throughout the year - Knowledge-sharing on areas of concern - Reflection on lessons learned and ways to improve assurance effectiveness and efficiency
Reciprocal synchronisation: Stakeholder groups' assurance needs and responsibilities	Participate in regular combined assurance meetings with management and external auditors to develop a combined assurance mapping, clearly reflecting the stakeholder groups' shared goals and an integrated risk and assurance view Ensure internal audit's mandate and plans accommodate its distinct role and provide for performing work, especially for external audit purposes (if desired by management and the audit committee) Incorporate balanced reliance expectations, cognisant of assurance effectiveness and efficiency, in internal audit's mandate and plans (if desired by management and the audit committee)
Reciprocal synchronisation: The reliance environment	Obtain and display a superior understanding of the business, including key risks Display qualities of a very strong head of internal audit, including: - Strong leadership qualities (particularly being independent of management and an influential leader) - Business and industry insights - A commercial orientation - Hands-on assurance experience and qualifications - Communication skills (supporting communication and a contribution at all levels in the business)

	- Qualities to function within and drive change With audit committee support, balance internal audit's resourcing and work by: - Negotiating sufficient budget and appointing a sufficient number of competent internal auditors - Using technology, including data analytics - Carefully considering opposing demands on internal audit resources, including by special investigations and *ad hoc* work for management and reliance work Use opportunities for direct access to the audit committee, the chief executive officer and the chairperson of the board Request minutes of all executive committee meetings from management – review these for new and evolving risks which should be addressed by internal audits and guide the audit committee about questioning management during meetings
Reciprocal synchronisation: The relevance of internal audit work for statutory audit purposes	Mutually agree with management and the audit committee on a realistic mandate and plans for internal audit, balancing internal audit's mandate against conflicting demands on internal audit (for example, by special investigations or *ad hoc* work for management) – this agreement can be formalised in a memorandum of agreement between internal audit and auditees to prevent expectation gaps If management and the audit committee decide to prioritise reliance in favour of (in addition to) internal audit's wider assurance role: - Include a large proportion of direct assistance work (including controls assurance work and extensive substantive procedures) for statutory audit purposes in internal audit plans during alignment planning - Ensure internal audits (also) have a strong financial focus, with or without a strong operational focus - Ensure internal audit focuses on risk-based audits - Ensure internal audits' annual assurance work focuses on key risks - At subsidiary level, follow a transactional, end-to-end integrated business process approach Work closely with risk management, enabling an integrated risk view Understand that external audit's combined audit approach depends on strong internal financial controls and does not mean external audit performs no substantive procedures

Reciprocal synchronisation: The credibility of internal audit work for statutory audit purposes	Taking into account internal audit's scope and plans, appoint an internal audit team consisting of a sufficient number of internal auditors who possess unquestionable competence, consisting of:
	
	- The right mix of skills to fulfil internal audit's risk-focused mandate,
	- A smaller, stable team comprising:
	    o Mostly senior level internal auditors
	    o Sufficient management level internal auditors
	    o A majority of professional career internal auditors
	    o Some internal auditors with specialist operational skills
	    o Some business staff on a rotational basis
	
	Ensure the unimpeded scope of internal audit's mandate, plans and reports by actively managing relationships between internal auditors and business staff, including by:
	
	- Rotating internal audit teams, areas and auditees

	- Continuous actions to raise awareness of and provide training on the importance of independence - The internal quality assurance programme - Not isolating internal audit from business realities - Reporting even uncomfortable findings, verbally and in writing Oversee the performance of credible internal audit work, in line with: - Well-developed, stable, risk-based internal audit processes - A focus on key risks and controls (assisted by technology) - The Standards - Requirements for quality audit documentation - Requirements for quality control procedures - Use the 80 / 20 principle to allow for internal audit's responses to changing and emerging risks When required, seek audit committee support for keeping internal audits focused on risk-based audits and meeting the internal audit plan amidst too many special investigations and *ad hoc* work for management which could impact on the normal assurance work Ensure internal audit reports contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems Discuss the draft internal audit report with external auditors to determine that all conclusions anticipated by the external auditor are included Discuss the draft internal audit report with management to get their input and feedback on findings and recommendations Ensure the wording in internal audit reports emphasise that the adequacy and design of organisational processes are not internal audit's responsibility Ensure that the mutually agreed, realistic internal audit mandate and realistic resourcing of internal audit allow internal audit to meet their flexible internal audit plans
Reciprocal synchronisation: External audit quality and the external auditor's liability	Accommodate the independent selection of reliance work by the external auditor Remain cognisant of the requirement of sufficient external auditor involvement in the audit as a whole, taking into account: - Sufficient external audit coverage - Reperformance levels - The risk of material misstatement at the assertion level associated with the reliance environment - The effect of significant risks on reliance
Team mindset	Understand the influence of engagement risk on the external auditor's decision to adopt a team mindset With the support of the audit committee and management, discuss with external auditors and implement a formalised combined approach to assurance focusing on: - Synchronising stakeholder groups' assurance needs and responsibilities in the context of their integrated risk and assurance view - Obtaining a very clear and detailed shared knowledge of internal compared to external audit's work - Aligning reliance work on key risks of interest to both internal and

	external audit, considering: o Key risks included in internal audit's rotational internal audit plans o The need for external audit to cover these controls in years in-between Work closely with external audit: - Through alignment planning, enable internal and external audit to substitute and not simply complement each other's work - When appropriate, make slight changes to the scope of internal audit work for enhancing reliance - When appropriate, use external audit work for supplementing internal audit work - Foster a voluntary, closer, professional working relationship with external auditors, to the point where internal and external auditors view themselves as: o A joint team o Speaking the same language o Providing a combined assurance o Often issueing a single report to management and the audit committee on specific areas of the audit, although the external auditor signs the statutory auditor's report o Although they recognise their distinct roles - Engage in regular meetings and constructive debates with external auditors - Share insights, gained from daily involvement in the business, with external auditors - Learn from external auditors - Discuss increasing assurance requirements and demands with external auditors to come up with a joint plan that address them - Enquire about and make use of continuous development opportunities offered by external auditors to their clients
Habitual integration	Understand the influence of engagement risk on the external auditor's decision to adopt habitual integration If approved by management and the audit committee, adapt internal audit's mandate and plans to include a proportion of direct assistance work for statutory audit purposes, including: - Controls assurance work with a financial focus - Extensive substantive procedures Ensure that assurance comes from the most effective and efficient provider, taking into account: - The combined cost of internal and external audits - The level of assurance required - Whether internal audit's focus is operational or financial - The geographical location of audit sites - Planned visits by internal audit to sites of third-party service providers of the organisation Engage with external auditors in alignment planning to identify overlapping work in internal and external audit plans, and ensure aligned individual audit plans minimise duplication of internal audit work and audit queries for management's attention, while ensuring as much cross-coverage as possible Suggest external auditors should focus on more complicated or riskier work while internal auditors perform work of a routine nature

	With audit committee support, ensure a balance between efficiency-driven reliance expectations and assurance effectiveness in internal audit's mandate and plans Discuss with management, the audit committee and external audit the need using technology (for example) data analytics
Fair alignment	Understand the influence of engagement risk on the external auditor's decision to adopt fair alignment Engage early, well before the start of the financial year, with external auditors in structured, upfront alignment planning discussions and workshops for internal audit to: - Develop a shared understanding of the two professions' requirements influencing reliance - Willingly reshuffle and align individual internal audit plans as agreed with external auditors and in accordance with the approved internal audit mandate and plans - When appropriate, slightly change internal audit work for increasing reliance - Focus internal audit's reshuffled plans on key financial risks, considering internal audit findings - Focus internal audit's reshuffled plans on control assurance work - Ensure internal audit's reshuffled plans reflect an audit methodology in line with external audit requirements on reliance areas, by: o Ensuring internal audit covers the majority of the financial year, including by moving internal audit work earmarked for reliance to the latter part of the year o Aligning sampling and selection of the extent of tests, sample sizes and selection of audit items with external audit requirements, considering the audit teams' integrated view of key risks and inputs provided by external auditors o Aligning internal audit's responses to audit exceptions on reliance work to those required for external audit purposes o Remaining cognisant that reliance requires credible work, completed in time to meet external audit's reporting deadlines - Present internal audit's reshuffled plans simultaneously with external auditors' plans for review by management and approval by the audit committee
Balancing oversight	Taking into account the audit committee's role in mitigating engagement risk (including through a formalised combined approach to assurance), engage with the audit committee and trust it to resolve issues with management, including any reliance issues Support the audit committee by providing it with: - Internal audit reports detailing risk and control problems, their impact and who should take responsibility for addressing them - Updates in documentation 'packs' and during 'closed sessions' without management present on: o The state of risks and controls o Whether management take internal audit findings seriously o Questions to raise with management

***Source**: Own compilation*

7.6.3 External audit's (particularly the external audit engagement partner or audit manager) contribution to reliance

The external auditor has a direct influence on reliance as he makes the reliance decision and remains responsible for the audit opinion, irrespective of reliance. Two related illustrative quotations from the further data set of other knowledgeable senior internal and external audit professionals include:

Quotation 9: The external auditor's influence on reliance:

> 'I don't have a problem with using the work that, that they [internal audit] are doing. This is now not including them as part of the team, just rely on the work that they have done. As long as we can properly test it, and as long as their objectives are the same as mine, because quite often there is some pressure from management or the audit committee that you use the work of internal audit, but they had a different objective. I need to address my audit plans and my objectives of my audit so that needs to be the same, so I don't have a problem with using them, as long as I am happy with them. We consider all these kinds of things but we … their tests need to address my issues as well, otherwise it's worthless … And if they are a well-established company with, with a well-established internal audit team that's been there for a while, and there's at least some discussion because that happens as well, discussion between the [external] auditor and the internal auditor way before the audit starts, let's say at the beginning of the year, about what you would like to achieve out of the audit, then you can rely on the objectives and you can actually rely on a big percentage … but I think it's important then that internal audit and external audit at least talk about the work that's going to be performed during the year by internal audit' (Mid-tier 1).

Quotation 10: The external auditor's influence on reliance:

> 'You see from an external audit point of view, if you are going to rely on the work done by somebody else you must be comfortable that due process was followed. That the people who are doing the work had the knowledge of what they were doing. And so on and so forth. So specifically, with respect to internal audit, you want to make sure that the internal audit function has a methodology, they've kept their working papers well, you can look at how they have arrived at their conclusions and agree or disagree with them. So external auditors have got a process of evaluating the work of an internal audit, before they place reliance. And this is in the course of evaluating … if they come across certain discrepancies then they can say, we are not going to rely, because of A B C. It could be a coverage issue, you did not cover enough in the year or because your work was lousy or whatever … In certain cases, I have also encountered situations where the external auditor does not have a problem with the quality of the work done by internal audit, but where they say it is more efficient to do a substantive test rather than a test of controls. So, for purposes of efficiency, they may choose not to rely on the work of an internal audit' (IAS 4).

Table 7.8 details what external audit could do to contribute to appropriate and fair (balanced) reliance.

Table 7.8: External audit's contribution to appropriate and fair (balanced) reliance

External audit (particularly the external audit engagement partner) should:	
Facilitative communication	Engage in extensive and open discussions about planned and achieved reliance with management, the audit committee and internal auditors, displaying a mindset favouring effectiveness over efficiency Engage with internal auditors to coordinate internal and external audit work, by means of: - Unrestricted, confident and easy, open (formal and informal) communication - Frequent conversations and regular meetings throughout the year - Knowledge-sharing on areas of concern - Reflection on lessons learned and ways to improve assurance effectiveness and efficiency
Reciprocal synchronisation: Stakeholder groups' assurance needs and responsibilities	Participate in regular combined assurance meetings with management and internal auditors to develop a combined assurance mapping, clearly reflecting the stakeholder groups' shared goals and an integrated risk and assurance view Taking cognisance of internal audit's distinct role, plan their involvement in the external audit (in conjunction with management and the audit committee) Promote and practise a fair balance between assurance effectiveness and efficiency when considering reliance expectations
Reciprocal synchronisation: The reliance environment	Fairly assess the influence of the reliance environment on reliance, specifically considering the pervasive influence of the profile and role of the chief audit executive Fairly assess the efficient balancing of internal audit's resourcing and work, by for example considering: - The sufficiency of the budget and staffing compared to the mandate and plans - Whether technology, including data analytics, is used - Whether management and the chief audit executive is careful about opposing demands on internal audit resources, including by special investigations and *ad hoc* work for management
Reciprocal synchronisation: The relevance of internal audit work for statutory audit purposes	When appropriate, incorporate controls assurance work on key risks and controls in a combined audit approach Carefully yet fairly assess the relevance of internal audit work for statutory audit purposes
Reciprocal synchronisation: The credibility of internal audit work for statutory audit purposes	Carefully yet fairly assess the credibility of internal audit work for statutory audit purposes
Reciprocal synchronisation: External audit quality and the external auditor's liability	Carefully yet fairly select reliance work independently of external influences, considering: - Whether the combined approach to assurance and support by the audit committee mitigate undue reliance and minimise assurance gaps - The fair assessment of the relevance of internal audit work for statutory audit purposes

	- The fair assessment of the credibility of internal audit work for statutory audit purposes Carefully yet fairly ensure sufficient external auditor involvement in the audit as a whole, taking into account: - Audit coverage - Reperformance levels - The risk of material misstatement at the assertion level associated with the reliance environment - External audit should cover very significant areas themselves, usually by means of extensive substantive procedures - When a significant risk is present, external audit should not use internal audit on the complete area - Rotating assurance work on key risks between internal and external audit avoid unnecessary duplication of audit work while ensuring sufficient external auditor involvement in the audit

Team mindset	*Depending on the engagement risk (evident from reciprocal synchronisation):*
	
	With the support of the audit committee and management, discuss with internal audit and willingly adopt a formalised combined approach to assurance focusing on:
	
	- Synchronising stakeholder groups' assurance needs and responsibilities in the context of their integrated risk and assurance view
	- Obtaining a very clear and detailed shared knowledge of internal compared to external audit's work
	- Aligning reliance work on key risks of interest to both internal and external audit, considering:
	    o Key risks included in internal audit's rotational internal audit plans
	    o The need for external audit to cover these controls in years in-between
	- Working closely with internal auditors
	- When appropriate, using internal audit work for supplementing external audit work
	
	Foster a voluntary, closer, professional working relationship with internal auditors, to the point where:
	
	- Internal and external auditors view themselves as:
	    o A joint team
	    o Speaking the same language
	    o Providing combined assurance
	- Often issue a single report to management and the audit committee on specific areas of the audit, although the external auditor signs the statutory auditor's report
	- They recognise their distinct roles
	
	Engage in regular meetings and constructive debates with internal auditors throughout the year
	
	Learn from internal audit, by encouraging them to share their deep insights, gained from daily involvement in the business, with external audit
	
	Discuss a joint approach to meet increasing assurance requirements and demands on internal and external audit with the audit committee, management and internal audit
	
	Offer continuous development opportunities to the internal auditors of clients

Habitual integration	*Depending on the engagement risk (evident from reciprocal synchronisation) and the quality of the team mindset:* Make internal audit work an integral part of evidence on the statutory audit Habitually practise optimal integration of internal and external audit work, focusing on relying on internal audit work as much as possible in line with the external audit firm’s audit approach and methodology Request internal audit to include a large proportion of direct assistance work for statutory audit purposes in internal audit plans, including controls assurance work with a financial focus and extensive substantive procedures Ensure external auditors concentrate on more complicated or riskier work while internal auditors perform work of a routine nature When a stable internal audit team performs well-developed stable internal audit processes in larger organisations, be open to assessing internal audit and its work for reliance Ensure that assurance comes from the most effective and efficient provider, taking into account the combined cost of internal and external audits, the level of assurance required, whether internal audit’s focus is operational or financial, the geographical location of audit sites and planned visits by internal audit to sites of third party service providers of the organisation Align plans with internal auditors to identify overlapping work in internal and external audit plans and minimise duplication of audit work and audit queries for management’s attention Consider the use of data analytics by either audit team Ensure a balance between efficiency-driven reliance expectations and assurance effectiveness in external audit plans, supported by the audit committee when needed
Fair alignment	*Depending on the engagement risk (evident from reciprocal synchronisation) and the quality of the team mindset:* Move external audit planning earlier, to well before the beginning of the financial year to accommodate alignment planning with internal auditors, without external audit prescribing to internal audit what to do Engage with internal auditors in structured, upfront alignment planning discussions and workshops to discuss and agree on: - A reshuffle of the individual internal and external audit plans, considering internal audit’s findings on the effectiveness of internal financial controls - Adherence to internal and external auditing professional standards and the influence on reliance Liaise with internal auditors about changes in audit plans that would increase reliance Ensure internal and external audit’s aligned individual audit plans reflect an aligned focus on key financial risks Ensure internal and external audit’s reshuffled plans reflect aligned objectives and approaches focused on control assurance work

	Ensure internal and external audit' reshuffled plans reflect aligned audit methodologies meeting external audit requirements on reliance areas, including by: - Requesting internal audit to cover the majority of the financial year, including by moving internal audit work earmarked for reliance to the latter part of the year - Aligning sampling and selection of the extent of tests, sample sizes and selection of audit items, based on an integrated view of key risks, including by giving feedback on internal audit plans in accordance with external audit's minimum sample size requirements - Aligning internal and external audit's responses to audit exceptions - Constantly engaging with internal auditors to ensure the continued credibility of reliance work and that reliance does not influence meeting external audit's reporting deadlines Reduce total sample sizes per test in external audit plans in line with the number of items for testing indicated in internal audit plans Present the reshuffled individual audit plans simultaneously with internal auditors to the audit committee for approval
Balancing oversight	Engage with and trust the audit committee as needed for resolving issues with management, including about reliance Take into account the audit committee's: - Involvement and support in mitigating the external auditor's engagement risk, including through a formalised combined approach to assurance - Profile - Strength - Support received from internal audit

***Source**: Own compilation*

7.6.4 The audit committee's contribution to reliance

The audit committee has a duty to oversee governance, risk management, internal financial controls and financial reporting, including assurance by internal and external auditors and the combined approach to assurance. The audit committee has an indirect influence on reliance, through its oversight role of the reliance environment, the relevance and credibility of internal audit work for statutory audit purposes and combined assurance. Two related illustrative quotations from the further data set of other knowledgeable senior internal and external audit professionals include:

Quotation 11: The audit committee's oversight role:

> 'As long as audit committees are not independent and well represented by specialist people, they will force the [external audit] fee down, but the moment you have a strong audit committee that understands their role, they might bring in audit quality factors and they might understand that there's these risks that they need to be balancing' (IRBA TEAM).

Quotation 12: The audit committee's oversight role:

> 'I have dealt with two kinds of audit committees … on the one hand, very competent people [who are] truly independent, know what they are doing, they are knowledgeable … Some of the people on the audit committee can do the audit just as well as you because … some of them were external audit partners somewhere in their lives … And then on the other side, where they don't even have a clue. They walk in and they argue about the fees but you question whether they are [more] concerned about the quality of the audit or the fees that they are going to save, and … there is lots in between … it's a real pleasure to work with the guys [who are] really serious about what they are doing and what they are there for … it's hard to work with the other guys [who] don't have a clue what they are doing. There is an audit committee just because we are ticking the box, we have to have this committee' (Mid-tier 1).

Table 7.9 details what the audit committee (particularly the audit committee chair) could do to contribute to appropriate and fair (balanced) reliance.

Table 7.9: The audit committee's contribution to appropriate and fair (balanced) reliance

The audit committee (particularly the audit committee chair) should:	
Facilitative communication	Engage in extensive and open discussions about planned and achieved reliance with management and internal and external auditors, displaying a mindset favouring effectiveness over efficiency
Reciprocal synchronisation: Stakeholder groups' assurance needs and responsibilities	Incorporate the distinct roles of internal and external audit into discussions about reliance Promote and practise a fair balance between assurance effectiveness and efficiency when considering reliance expectations
Reciprocal synchronisation: The reliance environment	Oversee that management balance profitability and good governance Oversee that management implement a strong risk management function with senior management collaboration Oversee that management implement strong internal financial controls which function effectively for the entire financial period Oversee that management implement a strong in-house internal audit function with a superior understanding of the business, including key risks Oversee that management provide realistic resourcing, in line with internal audit's mutually agreed realistic mandate and plans Oversee that internal audit is effective, including by ensuring that: - Internal audit's role as provider of assurance on combined assurance is formalised - Internal audit reports contain risk-focused findings and pragmatic recommendations, addressing the real root causes of control problems - The chief executive officer and management openly acknowledge and support the value of internal audit to the business - A very strong head of internal audit is appointed, characterised by: o Senior independent influential leadership

	o Business and industry insights o A commercial orientation o Hands-on assurance experience and qualifications o The ability to communicate at all levels o The ability to accept and drive change - The chief audit executive has direct access to the audit committee, the chief executive officer and the chairperson of the board Support the chief audit executive's efforts to balance internal audit's resourcing and work by, for example by considering: - The sufficiency of the budget and staffing compared to the mandate and plans - Whether technology, including data analytics, is available for use - Whether management and the chief audit executive are careful about the influence of opposing demands on internal audit resources, including by special investigations and *ad hoc* work for management Oversee that the chief audit executive receives minutes of all executive committee meetings and incorporate work on new and evolving risks in audit plans
Reciprocal synchronisation: The relevance of internal audit work for statutory audit purposes	Oversee and approve management's and internal audit's mutually agreed realistic mandate and plans for internal audit, particularly when they decide to prioritise reliance in favour of (in addition to) internal audit's wider assurance role by: - Including a large proportion of direct assistance work (including controls assurance work and extensive substantive procedures) for statutory audit purposes in internal audit plans during alignment planning - Focusing on internal audits that (also) have a strong financial focus, with or without a strong operational focus - Focusing on risk-based audits, including key risks and controls Oversee that internal audit works closely with risk management, enabling an integrated risk view Liaise with external auditors about the external audit approach
Reciprocal synchronisation: The credibility of internal audit work for statutory audit purposes	Oversee the appointment of sufficient internal auditors who possess unquestionable competence, taking into account if the team: - Has the right mix of skills to fulfil internal audit's risk-focused mandate - Is smaller and stable, consisting of: o Mostly senior level internal auditors o Sufficient management level internal auditors o A majority of professional career internal auditors o Some internal auditors with specialist operational skills o Some business staff on a rotational basis Oversee that internal audit's mandate, plans and reports are of unimpeded scope by: - Discussing the independence of internal audit with management - Reviewing that the chief audit executive effectively balances the relevance and unimpeded scope of internal audit's mandate, plans and reports without isolating internal audit from business realities - Reviewing that the chief audit executive refrains from accepting operational and / or managerial activities - Providing the chief audit executive with a direct reporting line and direct access to the audit committee chair

	- Fostering the trust of the chief audit executive by ensuring that the audit committee chair addresses internal audit's challenges while honouring the confidentiality of information shared Oversee the credibility of internal audit work, as evident from: - The profile of the chief audit executive - The stability of the internal audit team - A review of the outcome of the independently performed quality assurance assessments of internal audit - Internal audit reports containing all anticipated conclusions - Management's response to internal audit reports and recommendations - Internal audit mostly meeting their flexible internal audit plans Recommend and support the use of the 80 / 20 principle to allow for internal audit's responses to changing and emerging risks Provide the balance for keeping internal audits focused on risk-based audits and meeting the internal audit plan amidst changes to internal audit plans, for example to accommodate special investigations and *ad hoc* work for management which could impact on the normal assurance work
Reciprocal synchronisation: External audit quality and the external auditor's liability	Allow and ensure that the external auditor independently selects reliance work Support the combined approach to assurance in a way that mitigates undue reliance and minimise assurance gaps Be cognisant of the requirement of sufficient external auditor involvement in the audit as a whole, taking into account: The risk of material misstatement at the assertion level associated with the reliance environment
Team mindset	Understand internal and external audit's distinct roles Understand the influence of engagement risk on the external auditor's decision to adopt *a team mindset* Oversee the implementation of a combined approach to assurance When appropriate, suggest to and encourage internal auditors to: - Make slight changes to the scope of their work for enhancing reliance - Use external audit work for supplementing internal audit work Discuss increasing assurance requirements and demands with management and internal and external auditors to come up with a joint plan that address them Enquire about and encourage internal audit to make use of continuous development opportunities offered by external auditors to their clients
Habitual integration	Understand the influence of engagement risk on the external auditor's decision to adopt *habitual integration* Ensure that assurance comes from the most effective and efficient provider, taking into account: - The combined cost of internal and external audits - The level of assurance required - Whether internal audit's focus is operational or financial - The geographical location of audit sites

	- Planned visits by internal audit to sites of third-party service providers of the organisation Suggest external auditors should focus on more complicated or riskier work while internal auditors perform work of a routine nature Oversee and enforce, when needed, a balance between efficiency-driven reliance expectations and assurance effectiveness in line with the audit committee's mandate. Use as benchmarks for this oversight: - The distinct roles of internal and external audit, in particular the effect of reliance work on internal audit's business-wide risk focus, concentrating on controls assurance work with mostly an operational focus - The need to duplicate or extend some internal audit work to ensure sufficient external auditor involvement in the audit of key risks - Internal audit's implicit contribution to external audit effectiveness, considering what work external auditors are doing and what work they would have done if no internal audit was present - Whether either audit team uses data analytics
Fair alignment	Understand the influence of engagement risk on the external auditor's decision to adopt *fair alignment*, including by internal audit's findings on the effectiveness of internal financial controls Support and oversee fair alignment of internal and external audit work during early planning meetings and simultaneous approval of internal and external audit's reshuffled and aligned individual audit plans

Balancing oversight	Mitigate the external auditor's engagement risk as described under the other constructs, including by the audit committee:
	
	- Overseeing implementation of a formalised, combined approach to assurance, focused on:
	  o Synchronising stakeholder groups' assurance needs and responsibilities
	  o Achieving assurance effectiveness, including minimising assurance gaps and improving coverage
	- Balancing the influence of managements' general focus on profit margins on having:
	  o Strong internal financial controls
	  o A strong internal audit function
	  o A competent independent chief audit executive
	- Obtaining insights needed to balance management's influence on the relevance and credibility of internal audit work from information shared by the strong head of internal audit
	- Although the audit committee may also exert pressure on external auditors to increase reliance, balancing management's pressure to increase reliance against the effect of reliance on external audit quality and the external auditor's liability, by being reasonable, accepting and understanding of external auditors' motivations provided for planned and achieved reliance
	- Balancing management's influence on the relevance of internal audit work for statutory audit purposes, including by approving changes to the scope and focus of internal audit's mandate and plans which threaten internal audit's risk-based focus, for example special investigations and *ad hoc* work for management
	- Balancing management's influence on the credibility of internal audit work for statutory audit purposes, including by:
	  o Evaluating the competence of the internal audit team annually

	- o Giving the chief audit executive direct access to the audit committee - o Reviewing the outcomes of external assessments of internal audit quality - o Monitoring whether internal audit meets their plans A strong audit committee should: - Request the board to appoint individuals who are members of the risk committee on the audit committee or the audit committee should engage about risks and controls in joint meetings with internal audit and risk management prior to quarterly audit committee meetings - Get to know and understand the trustworthiness of the management of the organisation - Obtain the support of the strong head of internal audit, including sharing of: o Internal audit reports detailing risk and control problems, their impact and who should take responsibility for addressing them o Updates in documentation 'packs' and during 'closed sessions' without management present on: ▪ The state of risks and controls ▪ Whether management take internal audit findings seriously ▪ Questions to raise with management - Ask probing and clarifying questions of management, internal and external audit about areas of concern - Actively pursue 'focused conversation' during robust audit committee meetings where there are extensive discussions about areas of concern, for example as highlighted in intern audit reports The board should ensure: - Audit committee members collectively have: o A 'business sense' o Knowledge of governance requirements o A mix of appropriate financial and operational training and experience o A strong risk view grounded in business, financial and industry insights o An uncompromising emphasis on sound governance - A strong, upfront succession-plan of audit committee members is in place

***Source**: Own compilation*

7.7 QUALITY OF THE STUDY

Chapter 3 justified the choice of an interpretivist paradigm and a qualitative grounded theory methodology for this study. The chapter explicated how methodological and analytical processes applied in the study ensured the fit (credibility), workability and relevance as well as the modifiability of the emergent theory. In this section, the trustworthiness of the study, considering its qualitative approach, is considered. As recommended by Babbie and Mouton (2001:276-278), this section applies credibility, transferability, dependability and confirmability as measures of trustworthiness. Trustworthiness is important in qualitative research as it ensures the findings have 'instrumental value' (De Vos *et al.*, 2011:421). This means that the contribution of the study is likely to be of value to those practising and doing research in the area studied.

7.7.1 Credibility

'Credibility' or 'authenticity' is considered the most important measure of trustworthiness in qualitative research (De Vos *et al.*, 2011:419). Credibility refers to the degree to which the method and the findings of a study can be trusted (De Vos *et al.*, 2011:419, 428; Babbie & Mouton, 2001:276). When the researcher provides a detailed account of the procedures followed, readers are able to assess the plausibility of the findings (De Vos *et al.*, 2011:419, 428; Babbie & Mouton, 2001:276). Providing such detail allows the reader to evaluate the validity of the findings in the specific context of specific participants (De Vos *et al.*, 2011:420). The reader is also able to assess the credibility of the findings, which should indicate that the researcher's interpretations and conceptualisations are compatible with participants' constructions of their realities (De Vos *et al.*, 2011:420; Babbie & Mouton, 2001:276).

Triangulation, reference materials, member checks and formalised research methodologies are recognised means of assessing the credibility of qualitative research (De Vos *et al.*, 2011:420; Babbie & Mouton, 2001:276). Triangulation implies collecting and comparing data from different points of view (Babbie & Mouton, 2001:277). In this study, triangulation was applied by matching interview data across five key data sets (from four stakeholder groups – management, the audit committee, internal and external auditors – representing five diverse South African listed companies). The latter data set included 22 initial interviews conducted in 2014 and a further three interviews conducted in 2019 (two interviews with the same participants who were interviewed initially, and one with a new incumbent in the role of external audit engagement partner). In addition, a further data set, comprising interview data from a further seven interviews conducted in 2014 and 2015 involving knowledgeable senior internal and external audit professionals, were matched to the first data set. The matched data sets enhance the credibility of the findings. Thus, although participants' statements were accepted at face value, triangulation by matched data sets supported the credibility of the findings of this study.

Reference material is used to document and analyse data (Babbie & Mouton, 2001:277). In this study, the reference material consisted of audio recordings, verbatim transcriptions and electronic open coding of interviews. The material allowed several rounds of recoding, reinterpretation and rewriting of the analysed material, thereby ensuring credible conceptualisations.

Member checks involve checking the data and its interpretation with the source from which it was derived (Babbie & Mouton, 2001:277). In this study, member checking was conducted in three ways. First, clarifying and probing questions raised during interviews clarified and confirmed participants' statements (Charmaz, 2014:210). Second, verbatim interview transcripts were sent to the participants for their review and confirmation. None of the participants effected any changes to the transcripts, other than superficial, cosmetic or editorial changes. Lastly, draft findings were shared and discussed with the three participants involved in further interviews conducted in 2019. These participants concurred with the findings.

Applying and explicating the use of a formalised research method such as the classic grounded theory methodology (Glaser & Strauss, 1967; Glaser, 1978) supports the credibility of a study (De Vos *et al.*, 2011:420). Chapter 3 justified and explained the use of this theory and Chapter 4 explicated an audit trail of the application of this methodology in this study.

In conclusion, triangulation, reference material, member checks and the classic grounded theory methodology contributed to the credibility of this study and its findings.

7.7.2 Transferability

In quantitative studies, the researcher is obliged to demonstrate that the findings can be generalised from the sample to the broader population (De Vos *et al.*, 2011:420; Babbie & Mouton, 2001:277). Qualitative studies use thick descriptions and purposive sampling to convince the reader that the researcher's interpretations and conceptualisations faithfully convey the participants' constructed realities in a trustworthy manner (De Vos *et al.*, 2011:420; Babbie & Mouton, 2001:277).

Thick description implies a theoretically grounded analysis and argumentation of actions and behaviours contained in empirical data (Parker & Northcott, 2016:1119). Thick descriptions of theoretical constructs rely on collecting sufficiently detailed data in context, considering the length, number and context of interviews (Babbie & Mouton, 2001:277). In this study, the sufficiency of data was ensured by collecting data from 32 interviews, comprising more than 30 hours of voice recorded data. The interviews were contextually relevant as they involved participants with the highest role accountability from all four stakeholder groups directly involved in the statutory financial reporting and external audit processes in five cases. In addition, interpretations and conceptualisations were reported in detail, with illustrative quotations and *in vivo* codes presented in Tables 4.5 to 4.15. In addition, 'short, eye-catching quotations' and 'embedded quotations' were included in thick descriptions in Chapter 5, where the data was presented as theoretically sorted substantive categories (De Vos *et al.,* 2011:426-428). The short eye-catching quotations were used to convey important points while embedded quotations were used to illustrate the researcher's interpretations and conceptualisations (De Vos *et al.,* 2011:426-428). A small number of longer quotations were included to illustrate complexity (De Vos *et al.,* 2011:426-428).

Considering sampling as a means of ensuring transferability, in qualitative studies purposive sampling implies finding knowledgeable participants able to provide significant insights about a specific phenomenon (Parker & Northcott, 2016:1115). Thus, in qualitative research, a small number of purposively sampled cases, followed by further theoretically sampled cases provide concentrated accounts allowing for 'deep contextualised articulation of phenomena and their characteristics' and theoretical generalisation (Parker & Northcott, 2016:1115). In this study, purposive sampling (as part of the process of joint collection, coding and analysis of data) ensured variety and depth of sources and data. A range of data was collected from different industries, different accounting firms and different stakeholder groups. The data was obtained from two cases where reliance was optimal and three where it was limited.

7.7.3 Dependability

Dependability refers to repeating a study with the same or similar participants in the same or similar context and arriving at similar findings (Babbie & Mouton, 2001:278). Key to dependability is a logical, well-documented and auditable research process (De Vos *et al.*, 2011:420). Due to the interrelatedness of credibility and dependability, evidence supporting the former also supports the latter (Lincoln & Guba, 1985 in Babbie & Mouton, 2001:278). Readers are able to 'audit' the dependability of the study if the researcher has provided a detailed account of the analytical process, shared excerpts from documents used in the interpretation and conceptualisation of the data and reflected on their own role and possible biases (De Vos *et al.,* 2011:427).

In this study, Chapter 4 explicated an audit trail of data analysis supporting the dependability of theoretical constructs. Furthermore, a statement on the interpretive role of the researcher and a reflection on the researcher's influence on the findings adds to the dependability of the study (Chapter 3).

7.7.4 Confirmability

Confirmability refers to the auditability of findings. In other words, can the conclusions, interpretations and recommendations be traced back to the focus of the study, as well as sources of data and results of the analysis? (Babbie & Mouton, 2001:278). This thesis incorporates extensive audit trail materials in Chapter 4. The focus of the study is confirmed in the interview guide (Annexure A), the ethical approval (Annexure B) and background of the study (Annexure D). The research process was explicated in detail while the data and its analysis were confirmed in audio recordings, verbatim transcriptions, the list of categories, the thick description of substantive categories and the thick description of the substantive theory of the study.

In conclusion, the quality measures described above, combined with the reflections on the theoretical, methodological and practical contributions of this study, support the trustworthiness of the findings, emphasising their 'instrumental value' (De Vos *et al.*, 2011:421).

7.8 LIMITATIONS OF THE STUDY AND SUGGESTIONS FOR FUTURE RESEARCH

Reflecting on the limitations and findings of this study provides ideas for future research. First, the objective of the study was the construction of a substantive theory grounded in empirical data, and not theory verification. The emergent theory is therefore untested. The theoretical propositions of this study and the variables linked to each proposition could thus be tested in future deductive studies. Also, the emergent theory proposes leads which could be tested in future studies investigating the 26 questions listed by Bame-Aldred *et al.* (2013) (Chapter 6).

Second, the focus of this study was external audit's reliance on internal audit work during statutory external audits. Future research in auditing contexts could distinguish between reliance during statutory external audits and reliance during other kinds of assurance engagements.

Third, as the study participants were chief audit executives from in-house internal audit functions with co-sourcing arrangements, future studies could consider reliance where internal audit services are fully outsourced.

Fourth, as the cases studied did not use internal audit for management training, further studies could examine reliance on work of career internal auditors compared to work done by individuals who were appointed into an internal audit function, serving as a management training ground.

Fifth, as this study was conducted in five diverse listed companies in the private sector, future studies could compare reliance in the public sector or organisations of different sizes or in a specific industry.

Sixth, inductive studies on interprofessional reliance in auditing and other contexts could modify the theory, or even develop it further into a formal theory of interprofessional reliance. Future studies could also consider influences on the theory stemming from changes in the external audit profession (for example, mandatory audit firm rotation or the use of artificial intelligence and data analytics).

7.9 A CONCLUDING REFLECTION

This chapter concluded this classic grounded theory study. An overview of the research process considering the research question was presented. Discussions considering the contributions and the quality of the study followed the overview. Then, limitations and suggestions for future research were presented. Conclusions were triangulated to illustrative quotations from the further data set.

The main contribution of this study is the substantive theory of balanced reliance. The theory, developed through the classic grounded theory methodology, explains how management, the audit committee and internal and external auditors resolve the *disconnect* between their reciprocal influences on reliance to make *mutual agreement that reliance is appropriate and fair (balanced), whatever the reliance decision* viable and practicable.

The study also makes novel methodological and practical contributions to the substantive field. The application of the qualitative classic grounded theory methodology, use of data from all stakeholder groups and construction of a substantive theory is transcending. Most prior studies used deductive methods, data obtained from external auditors only and did not aim to produce a comprehensive holistic conceptualisation of reliance. Considering the contribution to practice, a number of the conceptualised dimensions and theoretical constructs of the theory are not currently addressed in internal and external auditing standards or in literature. These could prove useful when studying, guiding, practising and regulating reliance.

In conclusion, the substantive theory is grounded in data, but was not tested. Future studies could test the theoretical propositions of this study and the variables linked to each proposition by means of deductive studies.

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ANNEXURES

ANNEXURE A: INTERVIEW GUIDE

INTERVIEW GUIDE

DISCUSSION POINT 1: What are your general views on the role of an internal audit function in an organisation?

DISCUSSION POINT 2: How do you view the changes over the past five years in the role of an internal audit function in a large listed company?

DISCUSSION POINT 3: What are your views on external auditor use of the work of internal auditors for purposes of the external audit of a large listed company?

DISCUSSION POINT 4: How do you view the impact of external auditors' use of internal auditors' work on the external audit?

DISCUSSION POINT 5: How do you view the changes over the past five years in external auditors' use of internal audit function work of a large listed company? How do you expect it to change in future?

DISCUSSION POINT 6: What do you perceive as important considerations for your external auditor's initial decision whether or not to use the work of your IAF for the external audit?

DISCUSSION POINT 7: What are your views on the status of your IAF and how do you contribute to that status?

DISCUSSION POINT 8: What are your views on the objectivity of your IAF and how do you contribute to that objectivity?

DISCUSSION POINT 9: What are your views on the sufficiency of your IAF's competence and resources to fulfil the required duties and how do you contribute thereto?

DISCUSSION POINT 10: What are your views on your IAF's work performance and what role do you play in this regard?

DISCUSSION POINT 11: Does your external auditor use your organisation's internal auditors as direct assistants on external audits and what motivates them to do so?

DISCUSSION POINT 12: Does your external auditor use work performed by your organisation's internal auditors for the external audit and what motivates them to do so?

DISCUSSION POINT 13: How does the management of the company influence your external auditor's use of the work of internal auditors?

DISCUSSION POINT 14: How does the audit committee of the company influence your external auditor's use of the work of internal auditors?

DISCUSSION POINT 15: How does the relationship between your company's external audit team and internal auditors influence use of internal auditors' work for the external audit?

ANNEXURE B: ETHICAL APPROVAL

UNIVERSITEIT VAN PRETORIA
UNIVERSITY OF PRETORIA
YUNIBESITHI YA PRETORIA

FACULTY OF ECONOMIC AND MANAGEMENT SCIENCES

RESEARCH ETHICS COMMITTEE

Tel: +27 12 420 4102
E-mail: berendien.lubbe@up.ac.za

12 February 2014

Strictly confidential

Prof K Barac
Department of Auditing

Dear Professor Barac

Project:	A strategy for external auditor use of the work of internal auditors
Researcher:	JM van Staden
Student No:	04326059
Promoter:	Prof K Barac
Department:	Auditing

Thank you for the application you submitted to the Committee for Research Ethics, Faculty of Economic and Management Sciences.

I have pleasure in informing you that the above study was approved on an *ad hoc* basis on 12 February 2014. The approval is subject to the candidate abiding by the principles and parameters set out in the application and research proposal in the actual execution of the research.

The approval does not imply that the researcher, student or lecturer is relieved of any accountability in terms of the Codes of Research Ethics of the University of Pretoria if action is taken beyond the approved proposal.

The Committee requests that you convey this approval to the researcher.

We wish you success with the project.

Sincerely

PROF BA LUBBE
CHAIR: COMMITTEE FOR RESEARCH ETHICS

cc: Student Administration

ANNEXURE C: LETTER OF INTRODUCTION

UNIVERSITEIT VAN PRETORIA
UNIVERSITY OF PRETORIA
YUNIBESITHI YA PRETORIA
Faculty of Economic and Management Sciences
Department of Auditing
Tel: (012) 420-4427
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3 June 2014

Dear Participant

A STRATEGY FOR EXTERNAL AUDITOR USE OF THE WORK OF INTERNAL AUDITORS
Research conducted by:
Prof JM van Staden (Student number 04326059)
Cell: 083 652 4809

Thank you for your willingness to participate in an academic research study conducted by Prof Marianne van Staden, a Doctoral student from the Department of Auditing at the University of Pretoria.

The purpose of the study is to obtain an understanding how the phenomenon of external auditor use of the work of internal auditors is practiced in South African listed companies.

You can be assured of the following:

- This is an anonymous interview based study as your name will not appear on the questionnaire. The answers you give will be treated as strictly confidential as you cannot be identified in person based on the answers you give.
- Your participation in this study is very important. You may, however, choose not to participate and you may also stop participating at any time without any negative consequences.
- Please answer the interview questions as completely and honestly as possible. This should not take more than an hour of your time.
- The results of the study will be used for academic purposes only and may be published in an academic journal. We will provide you with a summary of our findings on request.
- Please contact my study leader, Prof Karin Barac at karin.barac@up.ac.za if you have any questions or comments regarding the study.

Kind regards

JvanStaden

PHD CANDIDATE

2014/06/03
Date

KBarac

STUDY LEADER: PHD CANDIDATE

3 June 2014

ANNEXURE D: BACKGROUND TO THE STUDY

BACKGROUND TO THE STUDY

You have been approached to participate in an interview that forms part of my doctoral study.

The provisional title of my study is:

A STRATEGY FOR EXTERNAL AUDITOR USE OF THE WORK OF INTERNAL AUDITORS

Background to this study:

An in-depth understanding of the practices related to optimal external auditor use of the work of internal auditors is currently lacking. Optimum external auditor use of the work of internal auditors equates to the best possible use under the circumstances. This lack of understanding may have potentially negative implications for each of the corporate governance role players and for stakeholders. External audit quality, and thus financial reporting quality, may be negatively affected when the work of internal auditors is used in the external audit when it is not appropriate to do so. When external auditors do not use the work of internal auditors, the integrity and professional behaviour of external auditors may be questioned by management, audit committees and stakeholders, and they may also question the value added by internal auditors.

It is thus very important that external auditors, management, internal auditors and audit committees have a shared view on external auditors' use of internal auditors' work. This view should be widely communicated to stakeholders, including litigators, and endorsed by professional and regulatory bodies. As part of this shared view, all four the corporate governance role players should have a common understanding of how optimal external auditor use of the work of internal auditors is practised, and each role player should understand their own role in this regard.

The ultimate outcome of this study will be a strategy that could be used by corporate governance role players, stakeholders and professional and regulatory bodies as a benchmark for practices leading to optimal external auditor use of the work of internal auditors.

Answers to the following questions will be sought from interviewees from each of the following groups (these questions were subsumed in the interview guide in Annexure A):

1. External auditors – external audit engagement partners (EPs):
    a. How do external auditors view the practice of external auditor use of the work of internal auditors?
    b. How prevalent is the practice of external auditors using the work of internal auditors?
    c. In what ways do external auditors use the work of internal auditors?

    d. How do external auditors make judgements that relate to the appropriate and optimal use of the work of internal auditors?
2. Audit committees – chairpersons of audit committees (CACs):
    a. How do audit committees view the practice of external audit use of the work of internal auditors?
    b. How do audit committees participate in optimal external auditor use of the work of internal auditors?
3. Management – chief financial officers (CFOs):
    a. How do the management of organisations view the practice of external audit use of the work of internal auditors?
    b. How do management participate in optimal external auditor use of the work of internal auditors?
4. Internal auditors – chief audit executives (CAEs) of in-house IAFs and the heads of internal audit consulting firms:
    a. How do internal auditors view external auditor use of their work?
    b. How do internal auditors participate in optimal external auditor use of the work of internal auditors?

This study's focus is on South African listed companies in the private sector. Five large listed companies, each in a different economic sector, were selected. Interviews with these four companies' audit engagement partners, chief financial officers, chairpersons of audit committees and chief audit executives will form the basis of the strategy for external auditor use of the work of internal auditors that will be the outcome of this study.

Participation in the research study is voluntary and confidential.

ANNEXURE E: LETTER OF CONSENT

UNIVERSITY OF PRETORIA

Department of Auditing

A strategy for external auditor use of the work of internal auditors

Research conducted by:

Prof JM van Staden (Student number 04326059)

Cell: 083 652 4809

Dear Participant

You are invited to participate in an academic research study conducted by Prof Marianne van Staden, a Doctoral student from the Department of Auditing at the University of Pretoria.

The purpose of the study is to obtain an understanding how the phenomenon of optimum external auditor use of the work of internal auditors is practiced in South African listed companies.

Please note the following:

- This is an anonymous interview based study as your name will not appear on the questionnaire. The answers you give will be treated as strictly confidential as you cannot be identified in person based on the answers you give.
- Your participation in this study is very important to us. You may, however, choose not to participate and you may also stop participating at any time without any negative consequences.
- Please answer the interview questions as completely and honestly as possible. This should not take more than an hour of your time.
- The results of the study will be used for academic purposes only and may be published in an academic journal. We will provide you with a summary of our findings on request.
- Please contact my study leader, Prof Karin Barac at Karin.barac@up.ac.za if you have any questions or comments regarding the study.

Please sign the form to indicate that:

- You have read and understand the information provided above.
- You give your consent to participate in the study on a voluntary basis.

______________________________ ____________________

Participant's signature **Date**