

Towards the development of a framework for ethics audits: an internal auditing perspective

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ABSTRACT

Ethics performance should efficiently and effectively be managed and assessed within an organisation to ensure continued stakeholder trust, and the attainment of a mutually sustainable advantage. According to the Professional Practice Framework (PPF) issued by the Institute of Internal Auditors, the internal audit function is a key role-player in assessing and making appropriate recommendations for improving the corporate governance processes within an organisation, which includes evaluating the effectiveness of the organisation's ethics-related objectives, programmes and activities. The internal audit function should proactively assess ethics within an organisation, but no formal framework for conducting ethics audits is provided. The purpose of this article is to study ethics from an internal auditing perspective and to develop a framework which can be used by internal auditors to conduct ethics audits within an organisation and ultimately measure the ethics performance or ethical health of the organisation.

Key words

Ethical culture; ethics management programmes; ethics audits; internal audit function

1 INTRODUCTION

In recent years, the management or governance of ethics within organisations has come to the fore. For several valid business reasons, organisations have been, forced to become socially responsible, to act with increased ethical sensitivity and to report on the organisation's ethics performance to all stakeholders (Kuper 2006:1; Rossouw, Prozesky, Van Heerden & Van Zyl 2006:114). A few critical driving forces for organisational concern with ethics are explained by Rossouw and Van Vuuren (2004:32-38). They argue that the strategic importance of ethics within business is emphasised by increased investors' confidence, increased trust in the organisation and increased reputation for organisations that manage ethics and report on ethics performance.

An increased awareness in the sustainability of organisations has also shifted the focus away from financial reporting only, to a more inclusive approach of triple bottom-line or sustainability reporting (KPMG 2006). For sustainable business success, organisations need to manage and report on their economic, social (including ethics performance) and environmental performance to various stakeholders.

Effectively managing ethics within an organisation is the responsibility of senior management and the board of directors, who should buy into the fact that ethics can and should be effectively managed. Critical in the ethics management process is utilising other role-players within the organisation. One such role-

player that can provide a value-adding service is the internal audit function. According to the Professional Practices Framework (PPF) issued by the Institute of Internal Auditors (IIA 2004:18), the role of the internal audit function is to evaluate the adequacy and effectiveness of risk management, internal control and governance processes within an organisation (IIA 2004:3). With regard to governance processes, the PPF emphasises that the internal audit function should assess and make appropriate recommendations for improving the governance process (IIA 2004:14). This entails promoting appropriate ethics and values within the organisation, ensuring effective organisational performance management and accountability, and evaluating the design, implementation, and effectiveness of the organisation's ethics-related objectives, programmes and activities (IIA 2004:14&166).

The PPF is the only guideline in respect of the role of the internal auditor with regard to organisational ethics issued by the IIA and was therefore used as point of departure for this article. The PPF implies that internal auditors must carry out an assessment of the ethical climate and the effectiveness of the organisation's strategies, tactics, communications, and other processes to ensure ethical compliance, but do not make the performance of an ethics audit explicit. The PPF also provides a checklist of considerations when assessing the ethical climate, without formalising the process needed to effectively assess the ethical climate or culture of an organisation. In the author's view, the internal audit

function will only be able to play a proactive role in the ethical culture of the organisation if formal ethics audits are built into the scope, strategy and overall audit plan of the internal audit function. It is argued that the internal audit function should regularly conduct ethics audits by following a holistic approach to assess organisational integrity and report on ethical performance.

In addition to the PPF, other authors have highlighted that the internal audit function has a major role to play with regard to organisational ethics. Verschoor (2007:11) states that the assessment of the ethical climate in an organisation is an area where internal auditors can add considerable value, specifically with reference to the prevention of fraudulent activity. Jackson (2006:40) supports this by stating that internal auditors who conduct ethics audits can help prevent inappropriate activities from being ignored and thus ensure the organisation's good reputation. Crowe Chizek and Company LLC (2005:7) also highlight the pivotal role internal audit plays in strengthening governance by performing a behavioural sciences ethics review to assess the understanding and perception of compliance across organisational levels. However, the question arises as to what framework the internal audit function would use to assess ethics within the organisation.

Previous research studies on ethics and the internal auditor have focused on the professional ethics of the internal auditor (Dittenhofer & Sennetti 2004; Sawyer & Dittenhofer 1996). Limited research is available in respect of the role of the internal auditor in managing and auditing ethics and on ethics audits in general. According to Boyd (cited by Jackson 2006), it will take time to build up a well-accepted common body of knowledge about ethics audits as well as an accepted ethics audit framework that can be used by internal auditors. The study on which this article is based focused on ethics audits from an internal audit perspective and aimed to develop a framework that internal auditors can use to conduct ethics audits and to report on the ethics performance of the organisation.

2 LITERATURE REVIEW

To appreciate the role of internal auditors in conducting ethics audits, it is necessary to have an understanding of the concept of an ethics management framework, as well as the internal audit process. Management implements an ethics management framework, whereas the internal auditor follows a specific audit process and applies a specific audit approach to audit the ethics management framework. For the purposes of this study, the term ethics management framework is used to refer to the entire ethics management process as well as all the interrelated systems within an organisation aiming to ensure organisational integrity. Two dimensions of an ethics management framework are discussed; firstly ethical culture (this is the only concept highlighted in the PPF) and secondly, the ethics management process. Although these elements of an ethics management framework are discussed separately, the ethical culture and ethics management process

within an organisation are inextricably linked; for example, the dimension of ethical leadership (discussed as part of the ethics management process) forms an equally important part of the ethical culture within an organisation. In the researcher's view, the internal audit function will only be able to conduct effective ethics audits if an in-depth knowledge of the organisation's integrated ethics management framework is obtained.

The relevant approaches to ethics audits as well as the audit process will also be discussed. An understanding of all these concepts is important as it will form the basis of developing the ethics audit framework for internal auditors. An overview of the literature will now be introduced.

2.1 Ethical culture

An understanding of both organisational culture and ethics is important when defining ethical culture. Schein (1992:17) describes organisational culture as "a pattern of shared basic assumptions that was learned by a group as it solved its problems of external adaptation and internal integration, that has worked well enough to be considered valid, and therefore, to be taught to new members as the correct way to perceive, think, and feel in relation to those problems." According to Gebler (2006:337), the culture of an organisation is a reflection of the collective values and behaviours of all employees, managers and leaders of an organisation, and provides the informal recognition and acceptance of any action or decision as a corporate action. Kinicki and Kreitner (2006:44) refer to three fundamental layers of organisational culture, namely observable artifacts (physical manifestation of an organisation's culture for example rituals, myths, stories), espoused values (explicitly stated values and norms preferred by an organisation and basic assumptions (unobservable values assumed to guide organisational behaviour).

When applying the concept of ethics (as defined by Rossouw and Van Vuuren (2004:3) as the balance between considering what is good for oneself and what is good for others) to organisational culture, it implies that an organisational culture in which the interests of all stakeholders are considered, rather than one group alone, could be considered to be ethical (West 2005:3). It is argued that an organisation aspiring to create an ethical organisational culture should make a concerted effort to integrate ethics into its artefacts, values and basic assumptions taking into account all stakeholders. An ethical organisational culture is therefore an alignment of an organisation's formal (systems, organisational structure, codes, rules, and policies) and informal (norms, heroes, role models, rituals, myths, stories and language) cultural systems grounded in the same core ethical values in deciding and doing what is right, good, and fair considering all stakeholders (Landman & Punt 2006b:11).

Creating and maintaining an ethical organisational culture is an important part of the ethics management framework. Top management has a responsibility to oversee the process of establishing an ethical culture.

According to Rossouw and Van Vuuren (2007a:82), a culture of ethics is characterised by amongst others, an ethical awareness, ethics leadership, ethics talk, ethical decision-making and stakeholders' satisfaction. Top management should therefore ensure that the organisation has an ethics vision, an ethics management strategy, and the necessary systems and structures in place to empower and enable ethics within the organisation (Rossouw & Van Vuuren 2007a:84; COSO 2004:22). An organisation should be given a mandate to become ethical and stay ethical, and a formal, legitimate ethics management process should also be established (Rossouw & Van Vuuren 2007b:85).

2.2 Ethics management process

As discussed earlier, the management of ethics has come to the fore and organisations are increasingly aware of the need to not only manage their financial performance, but also to actively manage ethics performance. Ethics management refers to the governance of ethics within an organisation (Rossouw & Van Vuuren 2004:197). When studying applied ethics, and specifically the application of ethics to organisational contexts, the ethics management process refers to a range of ethics-based organisational instruments, tools, or strategies for running an ethical organisation. (Rossouw & Van Vuuren 2004:43-57; Jeurissen 2004:12). Kaptein & Wempe (2002:293) use the term integrity management and describe it as a process of bringing an organisation into alignment with objectives, behavioural principles (conduct), and qualities (context). Organisations should formulate and adopt principles and standards of ethical business conduct to ensure organisational integrity (IoD 2002:104).

While it is the responsibility of management to implement an effective ethics management process within the organisation, the role of the internal auditor is to express an opinion on the effectiveness of the ethics management process and ultimately report on the ethics performance of the organisation (Sinason:2005). The internal audit function therefore needs an in-depth understanding of the organisation's ethics management process to conduct ethics audits.

An effective ethics management process should include the following key components (Federal Sentencing Guidelines 2006; Kaptein & Wempe 2002; IoD 2002; Landman & Punt 2006a; Paine 1994; Rossouw & Van Vuuren 2004):

- Demonstrating ethical leadership;
- Determining ethics risks;
- Codifying ethics;
- Institutionalising ethics; and
- Assessing, reporting and disclosing ethics performance.

Each of the components is briefly discussed below:

2.2.1 Demonstrating ethical leadership

Brown, Trevino and Harrison (2005:6) define ethical leadership as "the demonstration of normatively

appropriate conduct through personal actions and interpersonal relationships, and the promotion of such conduct to followers through two-way communication, reinforcement, and decision-making". Landman and Punt (2006b:11) state that ethical leadership is characterised by setting high standards and communicating these standards loudly and repeatedly in public and private, acting when someone violates the standards, funding and supporting ethics initiatives and holding people accountable for ethical and unethical conduct. Furthermore, ethical leadership requires more than being an ethical person and ethical leaders should shape the ethical culture, model ethical conduct, require ethical conduct from others, reinforce ethical conduct in others and sanction unethical conduct by others (Landman & Punt 2006b:2).

People in management positions are not necessarily ethical leaders demonstrating ethical leadership. An effective ethics management process should be managed by people who have a reputation for ethical leadership. Rossouw and Van Vuuren (2004:240) identify cognitive (having analytical and decision-making skills), behavioural (commitment and courage to implement ethical decisions) and managerial (the knowledge and skills to direct, control and reward the ethical behaviour of others) competencies that are required by ethically competent managers. These ethical leaders should be change agents for organisational ethics, ethics managers, as well as be ethical in their own jobs (Rossouw & Van Vuuren 2004:240).

The determination of ethical leadership is therefore a critical part of the ethics management process. Ethical leaders or role models who have adopted praiseworthy values and are consistently guided by these values need to be employed within the organisation (Kuper 2006:160). According to Kaptein and Wempe (2002:267), leaders should set examples and should express explicit support for the norms and values for which the organisation stands. Executives should develop a reputation for ethical leadership and should set the ethical tone at the top. Even though senior management and the board remain the driving forces behind the ethics management process, it is critical that they continuously consult with stakeholders throughout the process enhancing ethical decision-making and ensuring stakeholder engagement and feedback. Once ethical leaders have been identified within the organisation, ethics risks need to be determined.

2.2.2 Determining ethics risks

An organisation must identify and manage the ethics risks associated with the organisation. Ethics risk can be defined as the potentially detrimental or, alternatively, beneficial outcomes of unethical and ethical conditions or behaviours respectively (Rossouw & Van Vuuren 2004:200). It is critical that the organisation's executives understand the opportunities and threats of ethics performance or unethical behaviour. There is for example, a crucial connection between ethical behaviour and an organisation's reputation and it is very clear that

reputation is an ethics risk factor that needs to be managed (Rossouw & Van Vuuren 2004:202).

Ethics risk identification, as part of ethics management is the responsibility of the board of directors of an organisation. It is regarded as best practice to follow a multilateral approach to risk identification through a process of stakeholder engagement (Rossouw & Van Vuuren 2004:205). Stakeholder engagement refers to the involvement of all those parties affected by the organisation. Freeman (in Goodpaster, 1993:205) defines a stakeholder in an organisation as any group or individual who can affect or is affected by the achievement of the organisation's objectives.

There are various methods that can be used to obtain information on ethics risk: conducting personal interviews, requesting specific stakeholders to complete questionnaires, analysing documents relevant to ethics and conducting focus group sessions. When identifying risks, the role-players need to examine the sources of ethics risk, namely the conditions (corporate structure, culture, policies and systems) or behaviours (lack of transparency, fairness, accountability and responsibility) that gave rise to the ethics risk.

The determination of ethics risks as part of the ethics management process provides the platform for codifying ethics and therefore reducing ethics risks to an acceptable level. The purpose, process of development, format and implementation of the code are important considerations in the codifying stage.

2.2.3 Codifying ethics

A code generally signifies a set of principles and/or rules of conduct that apply to multiple persons or groups. A business code of ethics is a document that expresses what an organisation considers as its moral norms and values (Kaptein & Wempe 2002:271). Rossouw and Van Vuuren (2004:216) define a code of ethics as a document or agreement that stipulates morally acceptable behaviour within an organisation by defining the moral standards or guidelines that need to be respected by all members thereof.

A code can serve several purposes: internally (to raise ethical awareness and expectations by establishing standards of morally acceptable behaviour within an organisation), externally (to promote the reputation of the organisation amongst its external stakeholders) and culturally (to establish agreement about shared values between members of an organisation) (Rossouw & Van Vuuren 2004:216). The process of code development will be determined by the said purpose of the code. Rossouw and Van Vuuren (2004:217) recommend applying a multilateral process involving various role-players, in stead of the development of a mere product by top management.

Various formats exist for codes of ethics, namely the aspirational format and the directional format (Rossouw & Van Vuuren 2004:219). The aspirational code focuses on the ethical values that should guide

behaviour in an organisation whereas a directional code, also referred to as a code of conduct, provides specific guidelines on behaviour and identifies consequences for behaviour in contravention with the code. Landman, Punt & Painter-Morland (2002:9) suggest that a quality code of ethics should consist of a balance of clear and relevant guiding values (values statement), operationalised by key policies, procedures and rules (code of conduct).

The effective implementation of the code is vital to the success of the ethics management process. It is critical that the code's words are put into actions and that its true meaning is adequately interpreted by its users. The code's implementation also entails its proper institutionalisation: setting down adequate procedures, structures and systems to encourage people to follow the code and monitoring them in this process (Kaptein & Wempe 2002:280). Buy-in from all the stakeholders is important; they need to continuously reinterpret and reformulate the various elements of the code to ensure that corporate integrity is maintained. The code of ethics needs to be communicated regularly and in different ways so that it is reinforced over and over again (Rossouw & Van Vuuren 2004:222).

2.2.4 Institutionalising ethics

Institutionalising ethical standards consists of various activities, amongst others, the formulation and implementation of an ethics strategy, the implementation of the code of ethics and the implementation of relevant systems within the organisation that will contribute to enhanced ethics performance. A proper implementation plan should be drawn up that highlights the ethical objectives to be achieved and adjustments can be made to the plan on the basis of experience gained during the implementation process (Kaptein & Wempe 2002:279). Van Vuuren (2002:21) suggests a multi-level ethics strategy for institutionalising ethics. He argues that if an organisation has chosen to make ethics a part of how it defines itself and how things are done, ethics strategies should be embraced, designed and implemented at the strategic, systems and operational levels.

• Institutionalisation at strategic level

Institutionalising ethics at the strategic level within an organisation, implies that an organisation has to develop a sustainable ethics strategy in pursuit of achieving ethical objectives. Rossouw and Van Vuuren (2004:389-402) present a Modes of Managing Morality model which explains the different ethical objectives and management strategies organisations adopt to manage ethics. They highlight five primary strategies, each of which will be discussed briefly.

The *immoral* strategy is characterised by a culture where management does not see the need to make decisions concerning ethics. There is no commitment to dealing with ethics and practically no sensitivity to ethical issues. Organisations operating in the immoral mode have no ethics management interventions and the corporate culture makes little or no provisions for

an ethical way of thinking (Rossouw & Van Vuuren 2004:47).

The *reactive* strategy is, for many organisations, a starting point in managing ethics but a defensive approach to managing ethical risk (Rossouw & Van Vuuren 2004:227). Unethical behaviour is normally ignored and remains unpunished. This strategy, also referred to as *laissez-faire* ethics management, is used by organisations who believe that a show of commitment in the form of a set of ethical values (mere words on paper), will create a sufficient context for ethical behaviour.

The *compliance* strategy is a rule-based approach to managing ethics and is selected by organisations who want to commit themselves to monitoring and managing their ethics performance (Jeurissen 2004; Paine 1994; Rossouw & Van Vuuren 2004). These organisations use their codes of ethics to prevent unethical behaviour and as a standard against which its ethical performance can be measured.

An *integrity* strategy on the other hand, is a value-based approach selected by organisations who want to “walk the ethics talk”. These organisations want to raise the level of corporate ethics performance and recognise the strategic importance of ethics. They pro-actively promote ethical behaviour and strive to obtain commitment to a set of shared values from individual members of the organisation (Jeurissen 2004; Paine 1994; Rossouw & Van Vuuren 2004).

An ethically mature organisation will choose a *totally aligned* strategy where ethical behaviour is of strategic importance to the sustained success of the business. Ethics is integrated into the corporate purpose, strategy and operations and reinforced as part of the organisational structure and culture. The totally aligned organisation (TAO) recognises ethics heroes who embody the vision, purpose and ethical commitment of the organisation. The ethics management strategies of these organisations focus on continuous stakeholder engagement as well as identifying discrepancies between behaviour and organisational values (Rossouw & Van Vuuren 2004:231).

The Modes of Managing Morality model (refer to table 1) helps business ethics scholars and practitioners make sense of the differences that exist in the ways in which different organisations manage their ethics (Rossouw & Van Vuuren 2004:56). An organisation’s ethics strategy will determine the nature and extent of its ethics management process. An organisation in the immoral mode will not be interested in managing ethics, whereas the ethics management process within a totally aligned organisation will contribute to management at all levels being empowered to integrate ethics in their activities and decision-making (Rossouw & Van Vuuren 2004:55). An effective ethics management process will therefore include a strategy for managing ethics performance.

Table 1: Summary of modes of morality model

	Immoral	Reactive	Compliance	Integrity	Totally Aligned Organisation
Nature	Bread first, morals later	Awareness of ethics risk	Prevent unethical conduct	Promote ethical conduct	Ethics integrated with corporate purpose and strategy
Purpose	Unethical practices endorsed	Create ethical standards, but do not enforce it	Rules and external enforcement	Values and internal commitment	Ethics entrenched in corporate culture

(Source: Rossouw & Van Vuuren 2007b:38)

• **Institutionalisation at systems level**

At systems level, key ethics management role-players should translate the ethics strategy into meaningful ethics management systems. The ethics function at systems level plays a vital role to ensure that systems for monitoring and evaluating ethics performance are implemented within the organisation. Various systems can be established within the organisation to make ethics real. These systems are, amongst others, a communication system, staffing system, performance management system, training system, and evaluation and monitoring system (Rossouw & Van Vuuren 2004:231 - 241).

An effective communication system will ensure proper communication of the organisation’s ethics expectations to all the stakeholders as well as communication of the stakeholders’ experiences to the organisation. Proper communication about ethics is critical in the institutionalisation process and ethics awareness programmes, an ethics help-line and ethics newsletters are some of the useful ethics

communication tools that can be used as part of the communication system within the organisation. A staffing system should be designed and implemented to ensure the recruitment, selection and promotion of staff with integrity. In addition, an induction system for new employees can be used to make them aware of the organisation’s expectations regarding ethical behaviour as well as explaining the values and guidelines provided in the code of ethics. A performance management system can also be used to appraise the ethics performance of individuals within the organisation by incorporating certain ethics requirements into the key performance areas of all jobs. An ethics training system will amongst others, assist employees to understand, interpret and apply the code of ethics and to consider the ethical dimension of their decisions. Finally, an evaluation and monitoring system is required to ensure that ethics performance is measured regularly and feedback is provided to management with regard to the effectiveness of the ethics management systems implemented. (IoD 2002:103; Rossouw *et al* 2006:139).

- **Institutionalisation at operational level**

At operational level, the focus is to manage ethics in such a way that ethical principles are applied in the daily activities of each member of the organisation. Ethical behaviour should manifest itself in all jobs and interpersonal interactions (Rossouw & Van Vuuren 2004:242). The key role-players in the process of institutionalising ethics at the operational level, should be identified and specific roles and responsibilities allocated to each of the role-players. These role-players within an organisation are, amongst others, the chief executive officer (CEO), the ethics committee and an ethics manager. As ethics role models, these individuals should be used to mentor, coach and train employees to have an ethical awareness, identify ethical issues and make ethically sound decisions (Van Vuuren 2002:26).

Applying a multi-level strategy to the institutionalisation of ethics is an attempt to ensure that ethics is embedded at all levels in the organisation. Ethics is made real by embedding ethics at a strategic, systems and operational level followed by the assessment, reporting and disclosure of ethics performance.

2.2.5 Assessing, reporting and disclosure of ethics performance

The assessment process is an important stage in the ethics management process to ensure that the organisation's ethics performance is measured and evaluated. The King Report on Corporate Governance recommends that an independent verification of conformance to established principles and standards of ethical behaviour is conducted (IoD 2002:103). The Federal Sentencing Guidelines (FSG 2006) highlight the importance of evaluating the effectiveness of the ethics and compliance programme. It is argued that an independent party (independent to the ethics management team) should assess the adequacy and effectiveness of the ethics management process of the organisation. Senior management is responsible for reporting ethics performance internally and externally to all the relevant stakeholders.

Reporting on ethics performance is a critical part of the ethics management process. Communicating the results of the ethics management process in an integrity or corporate sustainability report to the various internal and external stakeholders on a regular basis, has several advantages. An integrity

report or corporate sustainability report provides feedback and enhances the accountability of the organisation. The report highlights, amongst others, the corporate efforts, conduct and outcomes, the corporate dilemmas addressed by the organisation and the values and norms that have been developed in stakeholder dilemma discussions (Kaptein & Wempe 2002:289). Kaptein & Wempe (2002:289) suggests an integrated reporting structure which addresses the triple bottom-line, namely the financial, environmental and socio-economic (which includes ethics performance) spheres. Painter-Morland (2006:363) argues that triple bottom-line reporting could prove to be a vital source of moral resuscitation in business life if it is not approached as another tick-the-box exercise but seen as a process of stakeholder engagement where organisational integrity is built into the organisation's system and where stakeholder activism is promoted.

Empirical evidence (studies by Verschoor (1998) and Webley & More (2002) as cited in Rossouw & Van Vuuren 2004) indicates that there is a positive link between social and financial performance. Social performance, which includes ethics performance and reporting, leads to enhanced stakeholder relationships, improved risk management and improved investor relations (Rossouw & Van Vuuren 2004:255).

To ensure some consistency into the process of sustainability reporting, international standards are available that can be used by organisations to assist them in the reporting process. These include, amongst others, the AA1000 Framework (a management framework that focuses on the quality of the accounting process), the Federal Sentencing Guidelines issued by the United States Federal Sentencing Commission and the Sustainability Reporting Guidelines of the Global Reporting Initiative (GRI) (McIntosh, Thomas, Leipzinger & Coleman 2003:87). The GRI developed a set of performance indicators that can be used by organisations to measure economic, environmental and social performance. Although the social performance indicators highlight aspects such as human rights, impact on society and health and safety (GRI 2002:55), the challenge is to develop a set of indicators which could be used to effectively measure the ethics performance of an organisation and report accordingly.

Table 2: Summary of the components of an ethics management process (Plant 2007:24)

	COSO	Federal Sentencing Guidelines	Kaptein & Wempe	King II Report	Rossouw & Van Vuuren
Ethical leadership	- Tone at the top - Senior management should exhibit ethical values and integrity	- High-level personnel should have overall responsibility	- Senior management should make a visible and lasting commitment to corporate integrity	- Commitment to organisational integrity - Determine ethics direction and strategy	n/a
Risk assessment	Risks identified are measured in terms of likelihood and impact	- Periodically assess the risk of criminal conduct	n/a	- Regular and formal identification of ethical risk areas	- Multilateral approach to ethics risk identification - Stakeholder engagement
Codifying ethics	Policies and procedures are established to address risks	- Establish standards and procedures to prevent and detect criminal conduct	- Develop a Code of Integrity by considering dilemmas employees are confronted with	- Ethical principles should be codified and communicated to stakeholders	- Develop an effective Code of Ethics
Institutionalising ethics	Adequate information, communication and monitoring of entire risk management process	- Incentives to perform in accordance with the compliance and ethics process - Disciplinary measures for those engaging in criminal conduct	- Draw up an implementation plan - Establish procedures and measures to implement integrity	- Structural measures such as training on ethical principles, standards and decision-making; regular monitoring of compliance with ethical principles	- Institutionalise ethics at the strategic, systems and operational levels
Assessing ethics	n/a	- Monitoring and auditing to detect criminal conduct - Evaluate effectiveness of the ethics and compliance program	- Draw up an audit plan - Use key integrity indicators for measuring performance	- Independent verification of conformance to established principles and standards	- Measurement of ethics performance - Reporting on ethics performance

2.2.6 Summary

The components of an effective ethics management process are summarised in table 2. The table indicates the importance of using a formal framework to manage ethics within organisations. The code development process should be an outflow of an ethics risk assessment, followed by an institutionalisation process and assessment process. It is clear that a code of ethics or code of conduct used in isolation will not be effective; the aim should be to pro-actively embed the code's rules, principles and standards within the organisation by applying a multi-level approach (Van Vuuren:2002).

The nature and extent of the organisation's ethics management framework (ethical culture and ethics management process) will have a direct impact on the internal audit process followed by the internal audit function when conducting ethics audits. The internal audit process is subsequently discussed.

2.3 The internal audit process

According to the PPF, the internal audit process consists of four steps, namely planning the engagement, performing the engagement, communicating the results and monitoring progress. An engagement (*hereafter referred to as an audit*) is

defined as a specific internal audit assignment, task or review activity designed to accomplish a specific set of objectives (IIA 2004:205).

Planning the audit entails developing an audit plan which includes determining the audit objectives (statements of what needs to be accomplished with the audit), scope (work to be done), timing (when to conduct the audit) and resource allocations (staffing and monetary budgets). During the planning stage, the internal auditor also meets with the audit client, obtain background information of the activity or process to be audited and conduct a risk assessment to identify the high risk areas (Coetzee *et al* 2007:81).

Performing the audit entails the process of gathering information with regard to the audit objectives set. Various techniques are applied by internal auditors to ensure that sufficient, relevant, reliable and useful information is gathered. When performing the audit, the auditor compares the evidence of the reality of what is in place (condition) with the acceptable standards of what should be in place (criteria) for a specific activity, process or task as determined by management (Coetzee *et al* 2007:82).

Communicating the results of the audit entails disseminating the findings of the audit in the form of an audit report to all the relevant parties. Internal

auditors should document the significant audit observations or findings in the report and make recommendations for improvement to the process or activity to senior management and the board (IIA 2004:16).

Monitoring progress or follow-up is the final stage of the internal audit process. The internal audit function should follow-up after conducting an audit to ensure that management has implemented the necessary recommendations made by the internal audit function or has accepted the risk of not taking action (IIA 2004:17).

2.4 Summary

The literature review aimed to identify all possible aspects of the role of the internal auditor, as implicated by the PPF, as assessor of organisational ethics; namely ethical culture, the ethics management framework, and the internal audit process. Based on the literature review, a framework for ethics audits from an internal auditing perspective will subsequently be presented.

3 A PROPOSED FRAMEWORK FOR ETHICS AUDITS

The recommended framework aims to provide internal auditors with a tool that can be used to conduct ethics audits within the framework of the internal audit process identified by the PPF (Standards 2200–2500)(IIA 2004). The proposed framework is summarised in Table 3. The framework proposed in Table 3 includes the following steps:

3.1 Planning the ethics audit

The internal audit function (*hereafter referred to as the ethics audit team*) should develop an ethics audit plan, which includes the audit objectives, scope of the ethics audit, resource allocation and audit work programme (IIA 2004).

Planning considerations

The ethics audit team should identify the organisation's ethics strategy or mode of managing morality. The organisation's ethics strategy and related objectives will have a direct influence on the ethics audit team's audit approach. The ethics audit team will be inclined to follow for example, a compliance-based audit approach for an organisation in the compliance mode (as discussed earlier), but it is imperative that an integrated approach is followed to assess organisational ethics.

Furthermore, the ethics audit team should determine the ethical risks attached to the ethics strategy of the organisation. A proper risk-evaluation or risk assessment should be conducted to identify all the events that will have an impact on the achievement of the organisation's ethical objectives. The ethics audit team should also consider the adequacy and the effectiveness of the organisation's ethics management framework compared to a relevant framework or model (for example the framework discussed in section 2). In addition, the ethics audit team should consider the opportunities for making significant improvements to the organisation's ethics

management framework by identifying the ethics interventions that will add value to or improve the organisation's ethics performance.

Ethics criteria

During the planning stage of the ethics audit, the ethics audit team considers the ethics criteria for the ethics management framework. These criteria are standards of what should be in place and are determined by management based on amongst others, best practices, industry standards and historical information. The criteria or standards set by management will depend on the organisation's ethics strategy as well as the organisation's ethical culture. The ethics criteria for the desired ethical culture include the ethics qualities that the organisation aspires to embed into the organisation as well as the principles of conduct that the organisation prescribes to ensure a sustainable advantage. An organisation with a re-active ethics strategy, will have no or limited ethics criteria, compared to an organisation with an integrity ethics strategy where all stakeholders are expected to walk the ethics talk. The ethics audit team should ascertain the extent to which management has identified adequate ethics criteria to ensure ethics performance.

Audit objectives

The ethics audit team should determine the ethics audit objectives. The objectives of an ethics audit are the broad statements made by the ethics audit team to define the intended audit objectives and may for example, include:

- to assess the existence of an ethical culture within the organisation; and
- to assess the effectiveness of the organisation's ethics management process.

Audit scope

The ethics audit team should determine the scope of the ethics audit. The scope of an ethics audit refers to the work to be carried out by the ethics audit team to satisfy the objectives of the audit. Consideration should be given to the relevant systems (for example, the human resources system, the communication system, performance measurement system), records (the ethics policy, code of ethics), personnel (the ethics officer, ethics manager, stakeholders), and physical properties (the ethics office), including those under the control of third parties (ethics helpline managed by a third party).

Resources allocation

The chief audit executive (CAE) should identify the appropriate ethics audit team. An ethics audit team should consist of internal auditors who have the necessary competencies to perform ethics audits. These competencies include an in-depth knowledge and a clear understanding of the organisation's ethics management framework (including the ethical culture and ethics management process), the relevant skills to conduct ethics audits, as well as experience in the field of organisational ethics. It is argued that an adequate and effective ethics audit team will consist of members with a diverse knowledge and skills base including organisational behaviour specialists, philosophers, auditors, lawyers and environmentalists.

Ethics audit approach

The nature and extent of the organisation's ethics management framework will have a direct impact on the audit approach applied by the ethics audit team when conducting ethics audits. It is recommended that the ethics audit approach should be an integration of a risk-based, compliance, culture and performance audit approach that is followed to audit the entire ethics management framework within the organisation. The purpose of the risk-based audit approach would be to assess the ethics risks attached to the organisation. The compliance audit approach is necessary to evaluate compliance to ethics policies and standards (McDonald 1999; Navran 1998; Trevino, Weaver & Gibson 1999). The culture audit is conducted to gather information regarding stakeholders' perceptions whereas the purpose of a performance audit is to evaluate the effectiveness and the outcomes of the organisation's overall ethics management framework.

When conducting an integrated ethics audit, the ethics audit team should carefully plan the audit approach. The nature of the audit procedures should be a balance of compliance procedures (rules-driven) and integrity tests (values-driven) conducted by the auditor to evaluate the ethics performance of the organisation. It is argued that a compliance audit approach is a mere tickbox exercise to provide assurance on the existence of an ethics management process. An ethics audit from an internal auditing perspective should expand beyond the rules to a more holistic approach in assessing organisational integrity. The ethics audit team should thus broaden the scope of the ethics audit to include both compliance and integrity testing to provide evidence with regard to:

- the adequacy and effectiveness of the ethics risk management framework; (risk-based audit);
- the existence of a formal ethics management process (compliance audit);
- the perceptions of stakeholders (culture audit);
- the effectiveness of the ethics management framework (performance audit); and
- the outcomes/impact of the ethics management framework (performance audit).

Audit work programme

The ethics audit team should prepare the ethics audit work programme. The work programme is the list of audit procedures to be conducted by the ethics audit team when performing the ethics audit. These audit procedures are carried out to achieve the audit objectives. The ethics audit team will therefore conduct the relevant tests to provide reasonable assurance that ethics objectives are achieved. As mentioned earlier, the ethics audit team should design the audit work programme in such a manner that the audit procedures include compliance and integrity tests that will provide assurance not only on the existence of an ethics management framework, but also on the effectiveness thereof.

3.2 Performing the ethics audit

When performing the ethics audit, the ethics audit team determines the current ethical condition (refers to *what is in place?*) within the organisation and identifies reasons for differences between set ethical standards for ethics performance and actual performance identified.

Sufficient, relevant, reliable and useful information should be gathered by the ethics audit team to enable them to express an opinion on the effectiveness of the organisation's ethics management framework. It is suggested that the ethics auditor follows amongst others, a process of stakeholder engagement when gathering audit evidence. The ethics audit team should consider the use of surveys, focus groups and interviews to gather information from all stakeholders when performing the ethics audit.

With regard to the ethics management framework, the ethics audit team should gather information in respect of the adequacy and effectiveness of the organisation's ethical culture and ethics management process. In assessing the ethical culture and ethics management process, the ethics audit team should focus on the following:

Ethical culture

The ethics audit team should obtain an in-depth understanding of all the dimensions of an ethical culture and should be able to assist management by making recommendations for enhancing the ethical culture within the organisation. The internal audit function should act as a partner to senior management, in a consulting capacity, providing advice on a regular basis with regard to fostering a culture of ethics within the organisation. The internal audit function should also provide an assurance service with regard to the adequacy and effectiveness of the ethical culture as part of the ethics management framework.

Determining ethical leadership

The ethics audit team should assess the ethical competency of senior management and determine the extent of ethical leadership at various levels within the organisation. The Committee of Sponsoring Organisations of the Treadway Commission (COSO) report on enterprise risk management highlights the important role of top management in setting the tone of an organisation. The ethics audit team will, as part of the evaluation of the organisation's risk management and internal control processes, assess management's integrity and commitment to ethical values (COSO 2004:22) and therefore management's ability to demonstrate ethical leadership.

Determining ethics risks

The ethics audit team should be a key role-player in providing assurance to management that ethics risks are effectively assessed and managed. A useful tool available to internal auditors to facilitate discussion on the ethics-related objectives of the organisation and the processes in place to achieve the objectives, is control self-assessment (CSA). CSA is a methodology encompassing facilitated meetings and surveys that will enable internal auditors and other

stakeholders to collaborate in assessing ethics risks (Reding, Sobel, Anderson, Head, Ramamoorti & Salamasick 2007:427). The ethics audit team should ensure that management followed a process of stakeholder engagement to identify and assess ethics risks, providing the platform for determining ethical standards and developing a useful organisational code of ethics.

Codifying ethics

The ethics audit team should assess the content of the code of ethics and determine its consistency with other documentation generated within the organisation, for example management reports, annual reports and sustainability reports. The ethics audit team should also evaluate whether the code is sufficient for addressing all ethical dilemmas experienced by the organisation and whether the code is an effective tool for promoting ethical behaviour in the organisation as well as measuring the organisation's ethics performance. The relevance of the format and tone of the code as well as the process of code development should also be evaluated by the ethics audit team.

Institutionalising ethics

The ethics audit team should continuously gather sufficient and appropriate evidence with regard to the effectiveness of the institutionalisation process and should make recommendations for improving the process, where necessary. The ethics audit team should evaluate whether the ethics vision, strategy, structures and systems implemented by management are adequate and effective in making ethics real and improving ethics performance within the organisation. The ethics audit team can, in an assurance capacity, also make a valuable contribution to continuously monitoring and evaluating the ethics management process.

Assessing, reporting and disclosing ethics performance

It is recommended that the ethics audit team, as an independent assurance service within the organisation, provide assurance with regard to the

adequacy and effectiveness of the ethics management process and make recommendations to top management for the improvement thereof. Once the ethics management process has been assessed, the ethics audit team will report internally to senior management and the board. The external reporting and disclosure of ethics performance is the responsibility of senior management. This responsibility might be delegated to an ethics manager or alternative role-player responsible for the ethics management process. These ethics role-players should ensure continuous assessment, reporting and disclosure of ethics performance.

3.3 Communicating the results

The ethics audit team should report on the results of the ethics audit to senior management and the board of directors. The findings or engagement observations of the ethics audit should be included in the ethics audit report. These findings should highlight the weaknesses in the organisation's ethics management framework, the ethics risks attached to these weaknesses, as well as recommendations made by the ethics audit team for the improvement of the organisation's ethics management process as well as ethical culture.

It is suggested that the results of the ethics audit should be used as a basis for sustainability reporting. The ethics report will provide all stakeholders with valuable information regarding the organisation's ethics performance or ethical health.

3.4 Monitoring progress

The ethics audit team should monitor progress by considering corrective action taken by management with regard to the weaknesses identified in the ethics management framework and should follow-up on the extent to which management implemented the recommendations made by the ethics audit team to improve the ethics management framework of the organisation and to ensure organisational integrity.

Table 3: A proposed framework for an ethics audit

Audit process	Actions
Planning considerations	<ul style="list-style-type: none"> - Consider the organisation's ethics strategy or mode of morality - Consider the ethics risks attached to the ethics strategy - Consider the adequacy and effectiveness of the organisation's ethics management framework - Consider the ethics interventions that will add value or improve the organisation's ethics performance
Planning the ethics audit	<ul style="list-style-type: none"> - Determine the ethics criteria - Determine the audit objectives and scope - Determine the competencies of the ethics audit team - Determine the ethics audit approach - Prepare the ethics audit work programme
Performing the ethics audit	<ul style="list-style-type: none"> - Gather sufficient, relevant, reliable and useful evidence through stakeholder engagement - (Surveys, interviews, analysis of information are relevant ethics audit techniques) - Assess ethical culture and ethics management process
Communicating results	<ul style="list-style-type: none"> - Report on the weaknesses in the organisation's ethics management framework, the ethics risks attached to these weaknesses and make recommendations for the improvement of the organisation's ethics management framework (including the ethical culture and the ethics management process) - Report on the organisation's ethics performance and ethical health - Incorporate the ethics report into the sustainability report (if applicable)
Monitor progress	<ul style="list-style-type: none"> - Follow-up on the extent to which management implemented the recommendations to improve the ethics management framework to ensure organisational integrity

4 CONCLUSION

This study examined ethics audits from an internal audit perspective using the Professional Practices Framework issued by the Institute of Internal Auditors as a point of departure. The ethics management framework within an organisation was researched, focusing on its ethical culture component and ethics management process component. The internal audit process was subsequently discussed.

As has been indicated by this study, internal auditors should conduct formal ethics audits to enable them to express an opinion on the adequacy and effectiveness of an organisation's ethics management framework and ultimately to report on its ethics performance. Internal auditors should have a detailed understanding of the organisation's ethics management framework to enable them to provide a value-adding service to management. Internal auditors should be actively involved in an assurance capacity, to measure the effectiveness of the ethics management framework and in a consulting capacity,

making recommendations for an enhanced ethical culture and improved ethics performance for sustainable organisational success. The ethics audit approach should be an integrated, holistic approach to assessing organisational integrity.

This study concludes that a formal framework should be used by internal auditors to conduct ethics audits assisting them in their duty regarding assessing the ethical culture as prescribed by the PPF. It is recommended that more formal guidelines for ethics audits be developed by the Institute of Internal Auditors with the help of internal auditors who are actively involved in the issue of organisational ethics, as well as of experts from areas such as organisational behaviour and philosophy. In addition, the effective application of the framework will require a competent ethics audit team. The success and usefulness of the proposed framework as well as the competencies required by an ethics audit team, however, fall beyond the scope of this study and may be areas for further research.

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