2019 North American Pulse of Internal Audit

Defining Alignment in a Dynamic Risk Landscape
Setting the Stage
Pulse Survey Respondent Demographics

**Internal Audit Position**
- 87% CAE
- 13% Director/senior manager

**Total: 512 respondents**

**Years of CAE/Director Experience**
- 5 or fewer: 41%
- 6 to 10: 25%
- 11 to 15: 17%
- 16 to 20: 10%
- 21+: 7%
Pulse Survey Respondent Demographics

Organization Type with Financial Services Breakout

- Publicly traded: 31%
- Financial services: 30%
- Public sector: 19%
- Privately held: 10%
- Nonprofit: 10%

Internal Audit Function Size (FTEs)

- 1 to 3: 19%
- 4 to 9: 37%
- 10 to 24: 26%
- 25 to 49: 10%
- 50+: 8%
Staffing Update:
More Functions Increasing Than Decreasing

- Experienced an increase
- Experienced a decrease

<table>
<thead>
<tr>
<th>Internal audit function size</th>
<th>Experienced an increase</th>
<th>Experienced a decrease</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 to 3</td>
<td>13%</td>
<td>4%</td>
</tr>
<tr>
<td>4 to 9</td>
<td>24%</td>
<td>13%</td>
</tr>
<tr>
<td>10 to 15</td>
<td>35%</td>
<td>6%</td>
</tr>
<tr>
<td>16 to 24</td>
<td>32%</td>
<td>14%</td>
</tr>
<tr>
<td>25 to 49</td>
<td>27%</td>
<td>17%</td>
</tr>
<tr>
<td>50+</td>
<td>36%</td>
<td>17%</td>
</tr>
<tr>
<td>All</td>
<td>26%</td>
<td>11%</td>
</tr>
</tbody>
</table>
Average FTE Increase or Decrease vs. Previous Year

- Number of FTEs increased
- Number of FTEs decreased

<table>
<thead>
<tr>
<th>Internal Audit Function Size</th>
<th>1 to 3</th>
<th>4 to 9</th>
<th>10 to 24</th>
<th>25 to 49</th>
<th>50+</th>
<th>All</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of FTEs increased</td>
<td>1.0</td>
<td>1.6</td>
<td>1.9</td>
<td>3.8</td>
<td>9.8</td>
<td>2.7</td>
</tr>
<tr>
<td>Number of FTEs decreased</td>
<td>1.3</td>
<td>2.3</td>
<td>2.6</td>
<td>3.1</td>
<td>8.8</td>
<td>3.2</td>
</tr>
</tbody>
</table>
Inhouse vs. External Sourcing for Internal Audit

![Graph showing inhouse and outsourced FTEs against internal audit function size categories.]

- **Inhouse FTEs**
  - 2 FTEs in the 1 to 3 category
  - 5 FTEs in the 4 to 9 category
  - 10 FTEs in the 10 to 15 category
  - 17 FTEs in the 16 to 24 category
  - 30 FTEs in the 25 to 49 category
  - 155* FTEs in the 50+ category

- **Outsourced/cosourced/contracted FTEs**
  - 0.3 FTEs in the 1 to 3 category
  - 1.0 FTEs in the 4 to 9 category
  - 1.6 FTEs in the 10 to 15 category
  - 1.9 FTEs in the 16 to 24 category
  - 2.8 FTEs in the 25 to 49 category
  - 9.5 FTEs in the 50+ category
Where Executives See the Risks in 2019

<table>
<thead>
<tr>
<th>Top Risks for 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Existing operations meeting performance expectations (competing against “born digital firms”)</td>
</tr>
<tr>
<td>2. Succession challenges and ability to attract and retain talent</td>
</tr>
<tr>
<td>3. Regulatory change and regulatory scrutiny</td>
</tr>
<tr>
<td>4. Cyber threats</td>
</tr>
<tr>
<td>5. Resistance to change operations</td>
</tr>
<tr>
<td>6. Rapid speed of disruptive innovations</td>
</tr>
</tbody>
</table>

Source: 2019 Executive Perspectives on Top Risks: Key Issues Being Discussed in the Boardroom and C-suite; Research conducted by NC State’s ERM initiative and Protiviti; © Protiviti, Inc, 2018
On average, the four risk areas that comprise the bulk of audit plans are:

- Financial-related – 22%
- IT & Cyber – 17%
- Operational – 16%
- Compliance – 16%

The percentages vary greatly between organization types.
### Audit Plan Trends – All

<table>
<thead>
<tr>
<th>Category</th>
<th>2017</th>
<th>2018</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operational</td>
<td>18.7%</td>
<td>16.4%</td>
<td>16%</td>
</tr>
<tr>
<td>Compliance/regulatory (excluding ICFR)</td>
<td>14.6%</td>
<td>14.5%</td>
<td>14.5%</td>
</tr>
<tr>
<td>Financial reporting (including ICFR)</td>
<td>9.2%</td>
<td>8.7%</td>
<td>8.3%</td>
</tr>
<tr>
<td>IT (not covered in other choices)</td>
<td>9.0%</td>
<td>8.3%</td>
<td>7.9%</td>
</tr>
<tr>
<td>Cyber</td>
<td>6.3%</td>
<td>6.1%</td>
<td>6.1%</td>
</tr>
<tr>
<td>Financial (excluding ICFR)</td>
<td>5.9%</td>
<td>5.2%</td>
<td>5.2%</td>
</tr>
<tr>
<td>ERM and related processes</td>
<td>5.6%</td>
<td>4.1%</td>
<td>3.8%</td>
</tr>
<tr>
<td>Fraud</td>
<td>4.8%</td>
<td>3.8%</td>
<td>3.8%</td>
</tr>
<tr>
<td>Support for external audit</td>
<td>4.1%</td>
<td>3.6%</td>
<td>3.6%</td>
</tr>
<tr>
<td>Governance and culture</td>
<td>3.6%</td>
<td>3.6%</td>
<td>3.6%</td>
</tr>
<tr>
<td>Third-party relationships</td>
<td>3.3%</td>
<td>3.3%</td>
<td>3.3%</td>
</tr>
<tr>
<td>Sustainability/nonfinancial reporting</td>
<td>0.8%</td>
<td>0.7%</td>
<td>0.7%</td>
</tr>
</tbody>
</table>

- **Increase**
- **Decrease**
- **Stay the same**
Breakout 1 - Internal Audit Trends

1. What are the biggest changes you’ve been making with your own audit plan? What adjustments are you making with your team to enable the changes?

2. What is driving your growth (or reduction) in staff? What changes are you making to your approach to talent management?

3. Does your reporting relationship affect your audit coverage? What strategies do you use to effectively manage these relationships?
Emerging and Atypical Risks
Definitions

Emerging Risks

• New risks or those that were of no consequence in the past.

Atypical Risks

• Risks that are difficult to define and assess, or those very infrequent in occurrence.
Emerging and Atypical Risks

87% of CAEs are extremely or moderately confident in their organization’s ability to identify and assess emerging risks.

47% of CAEs say that it is fairly common that an emerging or atypical risk will surprise management more than once a year.
Internal Audit Use of Key Risk Indicators (KRI) for Growing or Emerging Risks

- Not at all utilized: 23%
- Slightly utilized: 29%
- Moderately utilized: 34%
- Highly utilized: 14%
Board’s Sources of Information About Emerging and Atypical Risks

- **Executive management**: 78% Very likely, 15% Likely, 6% Somewhat likely, 1% Unlikely
- **Internal audit**: 49% Very likely, 35% Likely, 14% Somewhat likely, 2% Unlikely
- **Risk management function**: 48% Very likely, 29% Likely, 15% Somewhat likely, 8% Unlikely
Top Areas Rated as High/Very High Risk

Cyber (prevention and/or recovery) 68%
IT (not covered in other choices) 53%
Compliance/regulatory (not related to financial reporting) 46%
Management of third-party relationships 38%
Operational (not covered in other choices) 36%

Cyber and IT are the top 2 areas CAEs rated as high/very high risk.
Breakout 2 – Emerging and Atypical Risks

1. What best practices have you developed for your team to identify and assess emerging and atypical risks?

2. How does your internal audit function remain agile to emerging and atypical risks?

3. How do you communicate and get buy in from stakeholders over the need to modify your internal audit plan due to emerging and/or atypical risks?
Third-party Risks
Third-party Risks

- 21% of CAEs say third-party selection processes are ad hoc, weak, or non-existent.
- 48% of CAEs say third-party monitoring processes are ad hoc, weak, or non-existent.
Organizational Use of Third Parties

Eight out of ten CAEs say their organizations use third parties for IT services.

- Providers of IT services: 84%
- Vendors of business services: 68%
- Equipment or other vendors: 58%
- Marketing, sales, or distribution-channel partners: 31%
- Providers of transportation and logistics services: 29%
CAE’s Satisfaction with Organization’s Third-party Risk Management

- Extremely satisfied: 2%
- Mostly satisfied: 28%
- Somewhat satisfied: 32%
- Slightly satisfied: 25%
- Not at all satisfied: 13%
Wrap Up
Pulse 2019 Areas of Focus – Summary

• Emerging and Atypical Risks
• Cybersecurity and Data Protection
• Third-party Risks
• Board and Management Activity
Thank You

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2017-18 Global Chairman of The IIA
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