PULSE OF INTERNAL AUDIT
Navigating an Increasingly Volatile Risk Environment
Overview

• Pulse of Internal Auditing:
  – Assessing Emerging and Evolving Risks is a Key Priority
  – Linking Risks and Audit Coverage Remains an Enduring Challenge
  – The Profession is Facing a Talent Shortage
  – Emphasis on Quality Assurance is Lagging

• Parting Thoughts: Internal Audit’s Journey
Surveys & Demographics

Pulse of Internal Audit
370 Completed Surveys
- October 2014
- 7th consecutive year
- 63% Public/Private companies
- 84% CAEs and Directors (311 responses)
- 92% internal audit managers or above

311 Responses From CAEs and Directors
- 28% Finance and Insurance
- 14% Manufacturing
- 10% Educational services
- 7% Healthcare and social assistance

CBOK
12,570 completed the survey
- Q1 2015
- Conducted every five years
- 32% CAEs and Directors/Sr. Managers (4,043 responses)
- 28% North American participants
- 878 CAEs and Directors/Sr. Managers from North America

878 Responses From CAEs and Directors/Sr. Managers in North America
- 30% Finance and Insurance
- 10% Healthcare and social assistance
- 10% Manufacturing
- 8% Public Administration

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There is a Lot Going On for Internal Audit!

- Rising Stakeholder Expectations
- Increased Regulatory Scrutiny
- Complex Technology Risks
- Volatile Risk Landscape
- Emerging Stature of 2nd LOD Functions
- Balancing Assurance With Other Services
- Ever-present Political Pressure
- Emerging Talent Shortage

**INTERNAL AUDIT**
Five Priorities for 2015!

• Assessing emerging and evolving risks

• Linking risks and audit coverage

• Navigating an emerging talent shortage

• Address gaps in quality assurance and improvement
ASSESSING EMERGING AND EVOLVING RISKS IS A KEY PRIORITY
• 93 percent use risk-based methodologies when planning
• But, emerging risks present a challenge
• Risks often materialize with little or no warning
• Decades of accumulated value can evaporate
• We must be able to “audit at the speed of risk”
Continuous Risk Assessment is Still Aspirational for Many

<table>
<thead>
<tr>
<th>How frequently does internal audit conduct a risk assessment?</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual assessment without formal updates</td>
<td>38%</td>
</tr>
<tr>
<td>Annual assessment with periodic formal updates</td>
<td>41%</td>
</tr>
<tr>
<td>Continuous assessment</td>
<td>13%</td>
</tr>
<tr>
<td>Never (Internal audit does not conduct a risk assessment.)</td>
<td>4%</td>
</tr>
<tr>
<td>Other</td>
<td>4%</td>
</tr>
</tbody>
</table>

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## Continuous Risk Assessment Methodologies

<table>
<thead>
<tr>
<th>The degree to which internal audit utilizes these methodologies to continuously assess risk</th>
<th>Very/Extensively Utilized</th>
</tr>
</thead>
<tbody>
<tr>
<td>Periodic manual monitoring of KRI s</td>
<td>27%</td>
</tr>
<tr>
<td>Using technology to continuously monitor KRI s</td>
<td>10%</td>
</tr>
<tr>
<td>Periodically interview management to identify changes in the organization's risk profile</td>
<td>71%</td>
</tr>
<tr>
<td>Initiate formal updates of the internal audit risk assessment &amp; audit plan</td>
<td>60%</td>
</tr>
<tr>
<td>Initiate informal or ad hoc updates of the internal audit risk assessment &amp; audit plan</td>
<td>61%</td>
</tr>
<tr>
<td>Periodically update risk assessment based on changes to risk ratings identified during ongoing audit operations</td>
<td>54%</td>
</tr>
</tbody>
</table>

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Continuously Assessing Emerging and Evolving Risk – Key Imperatives

- Assess existing risk assessment maturity
- Develop/refine processes to identify and report on emerging risks
- Assess existing processes for updating the annual audit plan
- Obtain stakeholders’ input on the need for frequent updates
- Develop/refine audit reporting to demonstrate a stronger link between changes to:
  - The organization’s risk profile
  - Associated changes to the audit plan
LINKING RISKS & AUDIT COVERAGE: THE ENDURING CHALLENGE
Linking Risks and Audit Coverage: The Paradox of “Structural Expectations”

- Stakeholders often expect base level of coverage:
  - Financial risks
  - Regulatory risks
  - Compliance risks
- Once base is addressed:
  - Operating risks
  - IT risks
- Only then, is there interest in strategic and business risks
- The paradox:
  - Base level coverage often provides the lowest perceived value

Source: The CBOK 2015 Global Internal Audit Practitioner survey: © 2015 The IIA Research Foundation
Delivering Internal Audit Value: According to Grant Thornton, CAE’s Believe

They Add Value by:

1. Identifying improvement opportunities
2. Mitigating risk
3. Increased efficiency
4. Stronger corporate governance
5. Stronger financial controls compliance

Barriers Include:

1. Budget constraints (60%)
2. Talent quality or capacity (47%)
3. Focus on financial controls and compliance (43%)
4. Perception of internal audit (40%)
5. Organizational politics (40%)

Source: “Competing Priorities: Are CAE and audit committee priorities in sync?” © 2015 Grant Thornton LLP
Audit Plan Coverage in 2015

Source: The CBOK 2015 Global Internal Audit Practitioner survey: © 2015 The IIA Research Foundation Survey respondents were asked to estimate the distribution of their audit plan coverage. This figure reflects a summary of the data.
Reported Changes in Budgets From 2014-15:

- 28 percent report increased staffing from 2014 levels
- 26 percent expect staffing to increase again in 2015
- Yet only 38 percent believe that funding is sufficient
- Risks should drive resources – but resources often drive risk coverage

<table>
<thead>
<tr>
<th></th>
<th>Increase</th>
<th>Stable</th>
<th>Decrease</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall</td>
<td>47%</td>
<td>41%</td>
<td>12%</td>
</tr>
</tbody>
</table>

Source: The CBOK 2015 Global Internal Audit Practitioner survey: © 2015 The IIA Research Foundation
Linking Risks & Audit Coverage: Key Imperatives

- Undertake a comprehensive assessment
- Develop an audit plan based on the “real risks”
- Identify resources and expertise gaps
- Formulate strategies for addressing gaps
- Have candid conversations with management and the audit committee regarding:
  - Resource shortfalls
  - Expertise gaps
  - Risks that may fall victim to resources
  - A plan of action
- Develop a long-term strategy for addressing gaps
- Don’t let the “tail wag the dog”

“Disclosing the gaps in risk coverage and discussing the resources needed to address the gaps is essential.”

- Joe Steakley, CAE of Hospital Corporation of America
THE PROFESSION IS FACING A TALENT SHORTAGE
Top Skills Being Recruited or Built in Internal Audit Departments

<table>
<thead>
<tr>
<th>Skills Recruited or Built</th>
<th>Recruited</th>
<th>Essential</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Analytical/Critical Thinking</td>
<td>74%</td>
<td>96%</td>
</tr>
<tr>
<td>2. Communication Skills</td>
<td>57%</td>
<td>96%</td>
</tr>
<tr>
<td>3. Data Mining and Analytics</td>
<td>48%</td>
<td>44%</td>
</tr>
<tr>
<td>4. Industry-specific Knowledge</td>
<td>43%</td>
<td>69%</td>
</tr>
<tr>
<td>5. IT (general)</td>
<td>42%</td>
<td>43%</td>
</tr>
<tr>
<td>6. Business Acumen</td>
<td>40%</td>
<td>80%</td>
</tr>
<tr>
<td>7. Accounting</td>
<td>31%</td>
<td>48%</td>
</tr>
<tr>
<td>8. Risk Management Assurance</td>
<td>27%</td>
<td>40%</td>
</tr>
</tbody>
</table>

Source: The CBOK 2015 Global Internal Audit Practitioner survey: © 2015 The IIA Research Foundation
Internal audit functions providing significant value have more diversified skill sets:

<table>
<thead>
<tr>
<th>Skill Sets</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Continuity</td>
<td>84%</td>
</tr>
<tr>
<td>Data Privacy</td>
<td>80%</td>
</tr>
<tr>
<td>Specialized IT</td>
<td>77%</td>
</tr>
<tr>
<td>Data Analytics</td>
<td>72%</td>
</tr>
<tr>
<td>Supply Chain</td>
<td>69%</td>
</tr>
</tbody>
</table>

The talent gap is “fueling a poor perception of internal audit’s relevance and value: **65 percent** of stakeholders who do not find value in the internal audit functions cite talent as a top barrier.”

- PwC

Navigating an Escalating Talent Shortage

Key Imperative – 4 Step Process

Step 1: Create an organizational risk profile
Step 2: Assess team skills
Step 3: Identify skills gaps and develop strategies to close them
Step 4: Address strategic business risks and the effectiveness of risk management
EMPHASIS ON QUALITY ASSURANCE AND IMPROVEMENT IS LAGGING
Most Internal Audit Functions Embrace The IIA Standards

- 86 percent have an internal audit charter
- 92 percent use a risk-based methodology to develop the plan
- 35 percent have an internal audit department strategy
- Almost 70 percent report administratively to the CEO or CFO
- More than 80 percent report functionally to the Audit Committee (75 percent) or Board (5 percent)
- CAEs were invited to attend 98 percent of audit committee meetings

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Yet, Emphasis on Formal Quality Assurance/Improvement is Lagging

<table>
<thead>
<tr>
<th>How developed is the quality assurance and improvement program (QAIP) at your organization?</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nonexistent or ad hoc</td>
<td>26%</td>
</tr>
<tr>
<td>In the process of development</td>
<td>34%</td>
</tr>
<tr>
<td>Well-defined, including external quality review</td>
<td>26%</td>
</tr>
<tr>
<td>Well-defined, including external quality review and a formal link to continuous improvement and staff training</td>
<td>13%</td>
</tr>
</tbody>
</table>

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PARTING THOUGHTS: 
THE INTERNAL AUDIT JOURNEY

www.theiia.org/CAE
Parting Thoughts: The Journey Continues

Hindsight

Insight

Foresight
Questions?

The Institute of Internal Auditors

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