Internal Audit in the age of fast pace, rapidly changing risk environments

February 24, 2017
Topics

• Tech company disruptor mindset
• Objectivity and Independence
• Eight attributes of internal audit excellence
• Risk landscape
• Key takeaways
Tech company disruptor mindset

**Technology**
- Pervasive use of Technology

**Culture of empowerment**
- Distributed authority structure bakes empowerment into the organization’s core
- Preference for collaboration over control

**Common characteristics of successful disruptor companies**

**Consumer focused**
- Customers input in product development/features & direction
- Consumers roles - advisory council, early adopters etc.
- Emphasis on consumer experience
- Push innovation to the outer part of the organization

**Innovation**
- Constant innovation and relentless product iteration
- Willing to compete against their own products and services

**Speed/agility**
- Tolerance to risks and failures
- Speed to market
- Biased towards actions
- Resilience

**Focus on core competence**
- Laser focus on core competency and outsource everything else to ‘best provider’
Objectivity and Independence

Objectivity

• Unbiased view on risk and controls
• Collaborate during consulting phase

Independence

• No ownership of controls
• Direct reporting and access to Audit Committee
Keeping pace with stakeholder expectations

Discussions with stakeholders, CAEs and experienced internal audit leaders have consistently pointed to the importance of eight core attributes shared by effective internal audit functions, regardless of their mandate, scope of work or size.

- Business alignment
- Quality and innovation
- Service culture
- Risk focus
- Technology
- Talent model
- Cost optimization
- Stakeholder management
**Attribute 1 – Business alignment**

**Definition**

The alignment of scope and the resulting audit plan with the business direction.

Internal Audit incorporates stakeholder expectations into its mission and vision and clearly defines the value it will deliver to the organization.

**How to capture unrealized value?**

Remain cognizant of the organization’s business goals, objectives and decisions while keeping a pulse on the company through its regulatory filings, competitor and industry information, and insights gained through participation in strategic discussions.

**How internal audit is performing**

<table>
<thead>
<tr>
<th>Year</th>
<th>Trusted advisor</th>
<th>Assurance provider</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>65%</td>
<td></td>
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<tr>
<td>2015</td>
<td>68%</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>67%</td>
<td>89%</td>
</tr>
</tbody>
</table>

**Attribute 2 – Risk focus**

**Definition**
Holistic view of risks that considers internal, external and emerging risk factors.

Internal Audit invests the appropriate time to perform a dynamic risk assessment that encompasses top-down, strategic perspectives focused on identifying the most critical risks facing the business today and in the future.

**How to capture unrealized value?**

- Gather internal and external points of view by researching industry trends and leveraging subject matter expertise.
- Incorporate these factors into the audit plan and share the insight gained with the business, enabling the business to more proactively manage or take advantage of the risks.

**How internal audit is performing**

<table>
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<tr>
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<tbody>
<tr>
<td>2016</td>
<td>53%</td>
<td>92%</td>
</tr>
<tr>
<td>2015</td>
<td>69%</td>
<td>93%</td>
</tr>
<tr>
<td>2014</td>
<td>66%</td>
<td>84%</td>
</tr>
</tbody>
</table>

**Attribute 3 – Stakeholder management**

**Definition**
Understanding and managing relationships with a broad set of stakeholders.

The internal audit strategic plan is calibrated to align with stakeholder expectations.

**How to capture unrealized value?**
Drive accountability across your teams by structurally aligning individual team members to specific stakeholders, providing clear expectations to expand interaction beyond the audit, routinely measuring results, and driving actions to improve performance.

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<th>Year</th>
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</thead>
<tbody>
<tr>
<td>2016</td>
<td>56%</td>
<td>86%</td>
</tr>
<tr>
<td>2015</td>
<td>51%</td>
<td>82%</td>
</tr>
<tr>
<td>2014</td>
<td>52%</td>
<td>78%</td>
</tr>
</tbody>
</table>

% of companies where Internal Audit is performing well at stakeholder management

Attribute 4 – Cost optimization

**Definition**
Delivering efficient and value-added services through robust, well communicated audit methodology and processes.

**How to capture unrealized value?**
Hone in on residual risk by gaining a deeper understanding of second line of defense activities, embedding data analytics to monitor the more traditional risks and creating more cost-effective approaches to audit more complicated risk areas by employing flexible staffing models that more effectively match the supply of specialized skills against demand.

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<th>Year</th>
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<tbody>
<tr>
<td>2014</td>
<td>44%</td>
<td>79%</td>
</tr>
<tr>
<td>2015</td>
<td>54%</td>
<td>79%</td>
</tr>
<tr>
<td>2016</td>
<td>52%</td>
<td>85%</td>
</tr>
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</table>

Attribute 5 – Talent model

**Definition**
Possesses the appropriate mix of core internal audit talent, subject matter expertise, business acumen and position parity to align to its mandate and meet expectations of stakeholders.

Talent is managed to include the appropriate balance of technical skills and softer skills such as conflict management, intellectual curiosity, critical thinking, relationship development, and overall leadership.

**How to capture unrealized value?**
Proactively adapt the talent model to address the increasing complexity of risk profiles of companies beyond controls over financial reporting and general IT.

### How internal audit is performing

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<th>Year</th>
<th>Trusted advisor</th>
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<tbody>
<tr>
<td>2016</td>
<td>40%</td>
<td>72%</td>
</tr>
<tr>
<td>2015</td>
<td>45%</td>
<td>68%</td>
</tr>
<tr>
<td>2014</td>
<td>36%</td>
<td>65%</td>
</tr>
</tbody>
</table>

**Attribute 6 – Quality and Innovation**

**Definition**
Using well-defined standards that align to overall IIA standards to promote a culture that rewards innovation and continuous improvement of core processes.

- Focus on the strategic imperatives of the business.
- Data analytics, reporting and visualization tools used to deliver on the core mandate and innovate.

**How to capture unrealized value?**
- Embed innovation in the culture of the function.
- Provide benchmarking and points of view on the maturity of business processes and visually present audit findings in ways that enable them to assess the business impact of a process/control breakdown.

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<tr>
<td>2016</td>
<td>83%</td>
<td>43%</td>
</tr>
<tr>
<td>2015</td>
<td>78%</td>
<td>46%</td>
</tr>
<tr>
<td>2014</td>
<td>73%</td>
<td>30%</td>
</tr>
</tbody>
</table>

Attribute 7 – Technology

Definition
The ability to leverage analytics and technology effectively in the execution of the entire lifecycle of the audit process.

• Data analytics is used to focus on the right risk areas and business issues.
• Analytics and visualization tools are used to enhance the understanding and evaluation of risks.
• Continuous auditing techniques are leveraged to increase coverage or provide early warning of risk indicators to the business.

How to capture unrealized value?
Understand the complexities of the company’s systems architecture and innovate by using technology to drive audit efficiency.

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</tr>
<tr>
<td>2015</td>
<td>58%</td>
<td>34%</td>
</tr>
<tr>
<td>2014</td>
<td>51%</td>
<td>29%</td>
</tr>
</tbody>
</table>

% of companies where Internal Audit is performing well at leveraging analytics and technology

Attribute 8 – Service culture

**Definition**

Serving stakeholders while maintaining objectivity, having a well-defined mandate (mission, vision and scope) and clear reporting lines.

**How to capture unrealized value?**

- Anticipate stakeholder needs and exhibit broad business awareness and unrelenting focus on getting to the root cause of issues.
- Become an active contributor in executive sessions and board meetings on matters beyond your immediate mandate.

**The core of service culture**

- **Invest in relationships**
- **Share & collaborate**
- **Put yourself in their shoes**
- **Enhance value**

**How internal audit is performing**

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<tr>
<th>Year</th>
<th>Trusted advisor</th>
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</tr>
</thead>
<tbody>
<tr>
<td>2016</td>
<td>87%</td>
<td>55%</td>
</tr>
<tr>
<td>2015</td>
<td>83%</td>
<td>54%</td>
</tr>
<tr>
<td>2014</td>
<td>75%</td>
<td>51%</td>
</tr>
</tbody>
</table>

% of companies where Internal Audit is performing well at demonstrating a service culture

Become a trusted advisor

Providing value-added services and proactive strategic advice to the business well beyond the effective and efficient execution of the audit plan.

Taking a more proactive role - suggesting meaningful improvements and risk assurance.

Bringing analysis and perspective on root cause of audit findings to support the corrective action of the business.

Delivering objective assurance of the effectiveness of an organization's internal controls.
## Leadership – Advancing toward true north

<table>
<thead>
<tr>
<th>Trait</th>
<th>Very effective leaders*</th>
<th>Chief audit executives: Lead</th>
<th>Stakeholders: Enable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vision</td>
<td>89%</td>
<td>Build a vision aligned to strategic objectives.</td>
<td>Hold internal audit leader accountable for aligning with business strategy.</td>
</tr>
<tr>
<td>Talent</td>
<td>76%</td>
<td>Mentor and develop talent and supplement with outside resources.</td>
<td>Communicate your expectations around internal audit talent.</td>
</tr>
<tr>
<td>Position</td>
<td>82%</td>
<td>Take action to build stature in the organization.</td>
<td>Empower internal audit through tone of controls and proactive risk management.</td>
</tr>
<tr>
<td>Communication</td>
<td>91%</td>
<td>Communicate with impact to get attention and influence results.</td>
<td>Provide feedback to help internal audit optimize your time and decision-making.</td>
</tr>
<tr>
<td>Business alignment</td>
<td>95%</td>
<td>Built trusting relationships to raise level of engagement.</td>
<td>Work in a consultative way and let internal audit know when you expect more.</td>
</tr>
</tbody>
</table>

* Percent of leaders considered strong in each trait

2016 State of the Internal Audit Profession
Current risk and compliance landscape at many organizations

Fragmented functions, lacking clear ownership, accountability and integration

Current state

Challenges

Future state

- Gaps and overlaps in risks/compliance areas
- Potentially an “us” vs. “them” culture
- Compliance and audit fatigue in the business
- Significant cost of compliance
- Difficulty in coordinating overall responses
- Challenge growing/developing organizations

Obtaining an efficient risk management ecosystem is a common challenge in large, global organizations
### Business drivers for risk management ecosystem

<table>
<thead>
<tr>
<th>Drivers</th>
<th>Strategy &amp; Structure</th>
<th>People</th>
<th>Processes</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Built in redundancies</td>
<td>• Built in redundancies</td>
<td>• Primarily in-house functions</td>
<td>• Tailored risk appetite &amp; tolerance</td>
</tr>
<tr>
<td>• Central and market structure</td>
<td>• 2nd and 3rd line coverage over critical risks</td>
<td>• Incremental co-sourcing</td>
<td>• Robust processes across all functions</td>
</tr>
<tr>
<td>• Central and market structure</td>
<td>• Presence in high-risk areas</td>
<td>• Co-sourced model</td>
<td>• Standard risk appetite, with variable tolerances</td>
</tr>
<tr>
<td>• Primarily in-house functions</td>
<td>• Lean operating structure</td>
<td>• Balance of institutional knowledge and leading practice</td>
<td>• Stratified processes</td>
</tr>
<tr>
<td>• Incremental co-sourcing</td>
<td>• Primarily outsourced model</td>
<td>• Balance of institutional knowledge and leading practice</td>
<td>• Standard risk appetite &amp; tolerance</td>
</tr>
<tr>
<td>• Standard risk appetite, with variable tolerances</td>
<td></td>
<td>• Standard risk appetite, with variable tolerances</td>
<td>• Stratified processes</td>
</tr>
</tbody>
</table>

#### Overarching business strategy

- **Level of Centralization**
- **Level of Business Homogeneity**
- **Level of Industry Regulation**
- **Global Complexity**
- **Risk Tolerance**
- **Cost Sensitivity**

#### Appetite

- **Lower**
- **Higher**

#### Global Complexity

- Overarching business strategy
- Drivers
- Appetite
## Areas of IA focus by tech companies

<table>
<thead>
<tr>
<th>Finance</th>
<th>Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue automation</strong>: controls using data analytics, new standard</td>
<td><strong>Global compliance requirements</strong>: inventory of requirements and related compliance</td>
</tr>
<tr>
<td><strong>Shared service center</strong>: impact on processes and controls</td>
<td>Review of <strong>specific compliance areas</strong> such as Trade Compliance</td>
</tr>
<tr>
<td><strong>Finance Effectiveness review</strong>: assessment of finance organization’s people, processes and systems; including benchmarking to align with leading practices / expected growth</td>
<td><strong>Operational Controls</strong> Compliance</td>
</tr>
<tr>
<td></td>
<td><strong>Monitoring of Operational Controls</strong></td>
</tr>
</tbody>
</table>
Areas of IA focus by tech companies

<table>
<thead>
<tr>
<th>Engineering/ Product Development</th>
<th>Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Change management</strong>: assessment of internal IT development and operational processes, compliance controls in an agile software development environment</td>
<td><strong>Customer service</strong> operational review</td>
</tr>
<tr>
<td><strong>Data Privacy and Security</strong> (including cyber security)</td>
<td><strong>Refunds and rebates</strong>: programs, processes and systems</td>
</tr>
<tr>
<td></td>
<td><strong>Pricing</strong>: strategy, compliance, processes and systems</td>
</tr>
<tr>
<td><strong>Real Estate</strong></td>
<td><strong>People Ops / HR</strong></td>
</tr>
<tr>
<td>----------------</td>
<td>---------------------</td>
</tr>
<tr>
<td><strong>Data Center related projects:</strong> sustainability, 3rd party projects</td>
<td><strong>Talent management process review</strong> - start to finish prior to onboarding an employee</td>
</tr>
<tr>
<td><strong>Construction</strong> - cost and completion reviews</td>
<td><strong>Benefits reviews</strong>: review of intake process, taxability of perks to employees, effectiveness of such perks</td>
</tr>
<tr>
<td><strong>Facilities</strong> - capacity planning, optimization, lease audits</td>
<td>Use of <em>contingent labor</em>/ contractors in the company (cost and compliance)</td>
</tr>
</tbody>
</table>
# Areas of IA focus by tech companies

<table>
<thead>
<tr>
<th>Treasury</th>
<th>Other Areas</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Review of policy</strong> robustness, exposure in areas of investments and derivatives</td>
<td><strong>Large program reviews</strong> (Changes in business model and related impact)</td>
</tr>
<tr>
<td><strong>Cash disbursement</strong> review (all sources of in’s and out’s for fraud/error)</td>
<td><strong>Mergers &amp; Acquisition</strong> (integration, SOX readiness)</td>
</tr>
<tr>
<td></td>
<td><strong>Spend governance</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Country Audits</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Channel Distributor Audits</strong></td>
</tr>
</tbody>
</table>
Key takeaways

- **Collaborate with business**: In lock step with the business strategy, risks, compliance and controls
- **Ease of doing business with IA**: Make it seamless to work with IA both culture and skills to support the business
- **Balance between Forward Looking and Look Back auditing**: Define audit plan based on organization needs of assurance and consulting
- **Real Time support instead of Point in Time**: Provide support as needed instead after the fact
- **Protect and build on "trust" in internal audit**
Key takeaways (continued)

10 steps to take for sustained success and growth

01  Align risk management to strategic planning
02  Appoint a CRO, or similar role, if you don’t already have one
03  Define your risk appetite
04  Invest in data analytics to take a forward-looking view of risk
05  Establish a set of KRIIs that are relevant for your business, and then align them to your company’s KPIs
06  Hold the business units accountable for managing & monitoring their risks
07  Develop flexible GRC technology platforms and automated security processes across your IT infrastructure
08  Learn how to effectively partner with and leverage third parties
09  Ensure strong triangulation between strategy, risk management and business continuity management
10  Develop flexible GRC technology platforms and automated security processes across your IT infrastructure
Thank you

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