How The Recession Has Changed Internal Auditing

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Agenda

- Who am I?
- The Recession: 2008-Present
- The Recession's Affect on Internal Audit
- How Can We Help?
- Recovery Strategies
- How Can Auditors Help Themselves?

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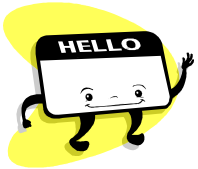
I. Introduction



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- Founding Partner, SOFT GRC (www.thesoftaudit.com)
- Former Director of Corporate Audit/SOX at Dr Pepper Snapple Group & Tyler Technologies
- Texas A&M University – 97/98
- Served on the Audit Committee of the Dallas Independent School District
- Published Author
  - *Internal Auditor* Articles (April 2007, December 2007, October 2010)
  - *ISACA Online* Article – December 2009
  - June 2010 – *Audit Report* – Cover Article – "How the Recession is Changing is Internal Audit"
  - December 2010 *New Perspectives - Sell Your Work:* How to Deliver Best Practice Audit Reports
  - November 2010 – *Bureau of National Affairs* - Internal Audit: Fundamental Principles and Best Practices
  - January 2011 – *Dallas Business Journal* – The Yes Man Phenomenon

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The Recession: 2008 - Present

Since 2008, How has the Economy Affected Us?

- How many in attendance:
  - Are currently in transition?
  - Know someone that is currently in transition?
  - Personally been affected by the economic downturn?
- Job Market for Internal Auditors
  - Weaker than previous years HOWEVER
  - Consistently Stronger than other professions
  - Everyone still needs auditors!

Economic Lifestyle Changes

- Have your spending habits changed?
- Have your Company's spending habits changed?
- Have you been asked to cut your budget?
- What has changed around you?

March 2011

- Jobless Rates Dip to 8.9%, lowest in Nearly 2 years
- When factoring in the number of part-time workers who would rather be working full time and those who have given up looking for work, the percentage of "underemployed" people dropped to 15.9 percent in February.
- Lowest in nearly two years.

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National Unemployment Rates, 2008 - 2011													Annual Average
	Jan.	Feb.	Mar.	April	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	
2011	9.0	8.9											9.0
2010	9.7	9.7	9.7	9.9	9.7	9.5	9.5	9.6	9.6	9.6	9.8	9.4	9.6
2009	7.6	8.1	8.5	8.9	9.4	9.5	9.4	9.7	9.8	**10.2**	**10.0**	**10.0**	9.3
2008	4.9	4.8	5.1	5.0	5.5	5.6	5.8	6.2	6.2	6.6	6.8	7.2	5.8
2007	4.6	4.5	4.4	4.5	4.4	4.6	4.7	4.6	4.7	4.7	4.7	5.0	4.6
2006	4.7	4.8	4.7	4.7	4.6	4.6	4.7	4.7	4.5	**4.4**	**4.5**	**4.4**	4.6
2005	5.3	5.4	5.2	5.2	5.1	5.0	5.0	4.9	5.0	5.0	5.9	4.9	5.2
2004	5.7	5.6	5.8	5.6	5.6	5.6	5.5	5.4	5.4	5.5	5.4	5.4	5.5
2003	5.8	5.9	5.9	6.0	6.1	6.3	6.2	6.1	6.1	6.0	5.8	5.7	6.0
2002	5.7	5.7	5.7	5.9	5.8	5.8	5.8	5.7	5.7	5.7	5.9	6.0	5.8
2001	4.2	4.2	4.3	4.4	4.3	4.5	4.6	4.9	5.0	5.3	5.5	5.7	4.7
2000	4.0	4.1	4.0	3.8	4.0	4.0	4.0	4.1	**3.9**	**3.9**	**3.9**	**3.9**	4.0
1995	5.6	5.4	5.4	5.8	5.6	5.6	5.7	5.7	5.6	5.5	5.6	5.6	5.6
1990	5.4	5.3	5.2	5.4	5.4	5.2	5.5	5.7	5.9	5.9	6.2	6.3	5.6
1985	7.3	7.2	7.2	7.3	7.2	7.4	7.4	7.1	7.1	**7.1**	**7.0**	**7.0**	7.2
1980	6.3	6.3	6.3	6.9	7.5	7.6	7.8	7.7	7.5	**7.5**	**7.5**	**7.2**	7.2

Recession's Affect on IA

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Ramifications of Actions

- Economic downturn = Increased risk
- People Cuts = Control Cuts = Increased Risk
- Cost cutting becomes a main priority ➡ Certain risks areas might lack focus necessary during normal economic times.

"It is not time to decrease controls; its time to strengthen the control environment"

The Ever-Changing Field of Internal Audit

- 50% of the respondents feel that budget cuts across their organization would damage its control environment and its ability to achieve business outcomes this year.
- The survey said auditors should be reviewing what the organization is doing to maintain its control coverage, but the majority (58 percent) have no plans to do any work on this risk.

SOURCE: IIA Gain Knowledge Report: 2009 Hot Topics for the Internal Audit Profession, January 2009

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The Ever-Changing Field of Internal Audit

- The two main areas gaining increased attention are strategic/business risk and operational risk.*
- Many companies still heavily rooted in SOX testing.
- 33% of organizations in the survey say the downturn is affecting the focus of their work, with the risk of fraud representing the main area receiving extra attention.**

* SOURCE: IIA Gain Knowledge Report: 2009 Hot Topics for the Internal Audit Profession

**SOURCE: PwC, "Business Upheaval: Internal Audit weighs its role and the recession and evolving enterprise risks"

The Recession's Effect on Internal Audit

- The Institute of Internal Auditors polled 817 of its members
- 23% of internal audit activities experienced staff reductions during 2009
  - percentage is projected to drop to 12% in 2010
- Internal audit departments have experienced staff reductions since 2008, with 2009 showing the greatest impact
- The cuts didn't go as deep in Fortune 500 companies
  - average reduction was only 12% of the staff, compared to an average cut of 21 percent of the staff in the overall survey population
  - 34% of the Fortune 500 companies reported reductions in 2009, whereas only 23 percent of the total survey population experienced reductions

SOURCE: IIA Survey 10/2009

The Recession's Effect on Internal Audit

- 17% of the survey respondents actually increased their internal audit staffing during 2009
- 60% maintained their staffing level
- Projected to trend slightly upward, with 18 percent projecting a staffing increase next year, and 70% saying they will maintain the same number of staff

SOURCE: IIA Survey 10/2009

- 31% of the respondents indicated they have rotational models in place, but this number jumps to 64% among Fortune 500 companies

Direct Economic Impact on IA

- Internal auditors in the United States and Canada appear to be holding their own during these challenging economic times.
  - The study, which polled more than 1,200 companies, finds that internal auditors with the Certified Internal Auditor (CIA) designation are cashing in earning significantly more than their counterparts without an internal audit certification.
  - Internal auditors on average will continue to receive raises over the next year, despite the looming recession.
    - The study found that a staggering 91% of employers surveyed indicated they are likely to increase internal auditor salaries next year.
    - 69% are planning to provide increases to 100% of their audit staff in the next 12 months, versus 34% for their entire workforce.

SOURCE: IIA Compensation Study, 10/08

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2010 Results

- A peak to trough economic contraction of 6% has seemingly resulted in a 1% loss in the number of people working in internal auditing
- Very little evidence that in response to the recession companies have resorted to general cuts in the numbers of internal auditors they employ
- Recession has actually increased the demands on many internal audit departments as they have become involved in risk and cost reduction programs
  - Due to the increasingly specialist nature of internal audit work, many companies lack the ability to recruit internally

SOURCE: Barclays Simpson – Winter 2010

Increased Role and Value of IA

- The IA role has expanded beyond internal controls assessment to achieve strategic and operational windfalls
- Internal auditors have been enjoying a surge in demand for their services.

SOURCE - http://blog.aefeldman.com/2009/04/06/internal-audit-departments-staff-up-as-focus-shifts-toward-value-creation/

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Corporate Role and Value of IA

- Corporate management is asking internal audit to find new ways to help achieve strategic objectives.
- Internal auditors are expected to extend their role and use quantitative skills and risk knowledge to help improve risk management and processes, and reduce complexity and costs.
  - Increased role of IA in the ERM process?

SOURCE: KPMG Audit Committee Institute

Changing Focus of IA

- Deteriorating economic conditions have led to a shift in the focus of internal auditors, with 47% telling a new survey that the downturn has led to more work on issues of operational risk.
  - Same figure have also seen an increase in cost reduction work as companies tighten their belts in the face of the recession.
- Furthermore, the IIA found that the economic crisis is fueling increased integration between risk management, compliance and internal audit. 35% of auditors said they had increased their oversight of risk controls.

SOURCE: www.barclaysimpson.com, "Recession has put focus on risk for internal auditors, March 30, 2009

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The Recession's Effect on Internal Audit

- "Fortune 500 companies reduced their internal audit staff by a lower percentage than did the overall population of internal audit departments we surveyed," said IIA president and CEO Richard Chambers in a statement. "This may indicate that Fortune 500 companies are looking to their internal audit functions as a source of insight and assurance during the current economic crisis while they right-size their overall workforce."

SOURCE: IIA Survey 10/2009

A/C Re-Examines Risk Mgmt Governance

- 82% of A/C in a KPMG Institute UK Study (summer 2009) say the recession has let them to reappraise the adequacy and effectiveness of the company's governance processes for managing risk.
- 85% report the downturn has resulted in the A/C having more involvement with management.

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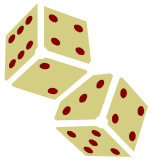
2011 Update – The IA Agenda

- Richard Chambers, president of the Institute of Internal Auditors
- "Internal auditors have almost an inherent understanding of key risks to the company," IIA Chambers says. "As companies, boards and managers are under greater pressure to demonstrate their acumen in managing risk, a lot of them are turning to internal audit."
- Key Areas:
  - Staffing and budgeting trends;
  - How auditors can better align with senior management's priorities;
  - Internal audit's biggest opportunity to add value to the organization.

Risk Tolerance of Audit Committee's

- With budget cuts, how do IAD's adjust?
  - Less Audits?
  - Same Audits but not as deep?
  - Is not completing the audit plan an alternative?
- What are the A/C's expectations?
  - Mature organization?
- Categorize Audits between required vs. nice to have?



How Can we Help?

What Can We do to Help?

- Refresh the Audit Risk Assessment
- Increased Focus on Fraud
- Increase Value-Added Services
- Decrease IA Costs – How?
- Integrate Audit Approaches/Focus on Operational Auditing

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Refresh the Audit/IT Risk Assessment

- Audit Risk Assessment should be refreshed annually and reviewed periodically
- Changing economic times = changing risks
- Audit Risk should be constantly monitored and assessed with increased scrutiny
- Continuous Audit Risk Assessment
  - Assessed in conjunction with IT

Increased Focus on Fraud

- Desperate times can call for desperate measures
  - Increase in fraud
  - Increase in time spent on frauds
- Cost/Benefit to all investigations
  - More Investigations but less staff?

Focus on Fraud - Fraud Guidance

- IIA published a new guide: "Internal Auditing and Fraud" that gives auditors general guidance to help internal auditors comply with professional standards
- Discusses how IA should be aware of the risk of fraud, including fraud indicators and explains who in an organization has what roles with respect to preventing and detecting fraud
- Explains auditor's role during audit engagements & addresses fraud risk assessment, prevention, detection & investigation
- Provides reference materials, questions to be considered and a fraud risk assessment template

Decrease IA Costs

- Decrease Travel
  - Remote testing
- Training Costs
  - Bring Training In-house
- Outsourcing

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Cost of CPE Training

- Reasons to maintain your CPA certificate
- Opportunity cost – what is your time worth?
- Options to consider
  - Live training (i.e. monthly association meetings)
  - Online training
  - Live webinars

Increase Value-Added Services

- Study of 2,000 IA in late 2009 (still relevant and growing currently) by PwC revealed assessing risk for the BoD is common but more involvement is wanted and needed at a strategic level
- 20% stated IA helps assess the company's risk appetite and tolerance & 43% assess emerging risks
- > half assess the effectiveness of risk mitigation initiatives & 65% assess key enterprise risks

Increase Value-Added Services

- How can we add value to the business?
- Lean Six Sigma
- Process Improvement
- Focus on Cost/Benefit
- Justify your budget
- Continuous Auditing/Monitoring
- Operational Auditing
  - Revenue Enhancer, not just Overhead!

Integrating Audit Approaches

- Don't work in silo's
- Integrate SOX testing with operational audits, etc
  - Don't visit a site twice
  - One round of SOX testing?
- Cross-train auditors
- Risk Management, Compliance and Audit Integration

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Operational and SOX Similarities

	Operational	SOX
Involve review of Key Procedures/Processes?	X	X
Identification of Inefficient/Ineffective Processes?	X	X
Interviews with Personnel?	X	X
Testing to Verify Current Process is in Place and Functioning as Intended?	X	X
Identification of Potential Fraud/Segregation Issues?	X	X
Identification of Efficiency/Cost Savings Initiatives?	X	

		Objectives of Operational Audit of Cash Receipts			
Example "What Can Go Wrong" Questions - Divisional SOX Compliance Review - Cash Receipts	Assertion	Review policies and procedures and determine if they are in-line with best practices and are currently in place and adhered to.	Review procedures for depositing cash and determine if process, personnel and access are appropriate.	Determine if the employees who have access to cash and related G/L accounts are appropriate.	Review the timeliness of cash received at the bank versus posted on the general ledger.
What ensures that cash receipts are recorded when received?	Completeness, Existence/Occurrence	X	X		X
What ensures that cash receipts recorded equate to amounts deposited?	Measurement/Valuation	X	X	X	X
What ensures that cash receipts/transfers are recorded in the correct period?	Completeness	X			X
What ensures that duplicate postings of cash receipts are not made to the general ledger?	Completeness, Existence	X		X	X
		X - Similar Objectives for Each Audit Process			

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Recovery Strategies

Recovery Strategies

- June 2010
  - New IIA Report, *A Glimpse Ahead: CAEs Look Beyond the Recession*, summarizes four hours of recent roundtable discussions among the CAEs of Fortune 250 enterprises.
- "Thought-leading CAEs of organizations of all sizes and types are striving to become more agile, be creative in acquiring and retaining talent, add value to their changing organization, and anticipate looming challenges— even as they maintain their focus on assessing enterprise risk," observes Roderick M. Winters, CIA, general manager of financial operations for the Microsoft Corp. and chairman of the board of The IIA.

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Recovery Strategies – Included Topics

- Evolving their risk assessment, audit planning, and audit methodologies to better address the organization's fast-changing strategic and operational risk portfolio
- Key staffing issues and ways to address them
- Steps CAEs are taking or planning to align internal audit activity with anticipated new strategic business initiatives by their organization
- Tangible benefits accruing to CAEs and the management of their organization from adopting automated auditing techniques
- Biggest potential issues for internal auditing beyond 2010

Recovery Strategies – 10 Key Takeaways

- Focus on the Best Staff
- Reassess Audit Skill Needs
- Rethink Training Needs
- Hire/Acquire New Skills
- Develop a Flexible/Agile Audit Plan

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Recovery Strategies – 10 Key Takeaways (cont.)

- Develop/Expand Strategies for automated auditing
- Get involved in new strategic business initiatives
- Ensure that internal audit is up to date on and is adding value to emerging legal, regulatory, and public policy issues
- Reassess coverage of public disclosures of all types
- Stay close to stakeholders as the organization emerges from the recession

2011 and Beyond

- "As is said about the markets--internal auditing has undergone a major 'correction,' " said Richard Chambers, IIA's president and CEO. "Given the cautious economic outlook for the coming years, it is unlikely that internal audit resources will be restored at a rate faster than the overall economic recovery
- Fifty-one percent of Fortune 500 internal audit respondents indicated their budgets were smaller in 2010 than in 2007, while 41 percent overall reported smaller staffing levels
- Thirty-four percent think their budgets will increase in 2011 and nearly one in five said they expect a higher head count

SOURCE: http://www.allbusiness.com/economy-economic-indicators/economic-conditions-recession/15479036-1.html

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Summary

- As auditors, we must continue to add value and not be an OH cost for our companies
- Explore ways to further your department's and your personal knowledge and scope
- Continue to look for new ways to cut costs
- IA must continue to evolve with our organizations and the changing dynamics of the economic environment