



# 2018 NORTH AMERICAN PULSE OF INTERNAL AUDIT

Financial services focus



**Financial Services**  
AUDIT CENTER

# About the Pulse of Internal Audit

## Financial services focus

Financial Services Responses	
CAEs	164
Director/senior managers	22
<b>Total</b>	<b>186</b>

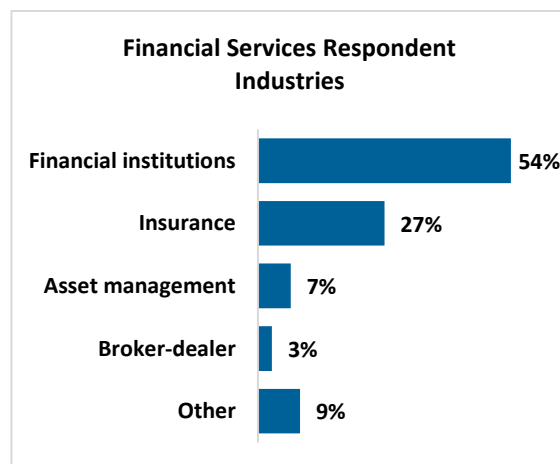
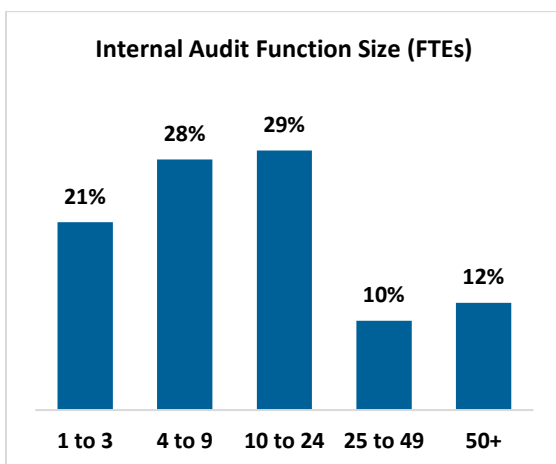
The IIA's Audit Executive Center® (AEC®) has gathered insight from leaders in the profession through the annual Pulse of Internal Audit survey since 2009. Each survey collects information about both established and emerging issues that are important to the profession as well as information about internal audit management (such as areas of focus, staff, and budget levels).

The 2018 North American Pulse of Internal Audit survey (Pulse) was conducted online from Oct. 5 to Oct. 26, 2017, with survey invitations distributed by The IIA. In Pulse reports, chief auditors and directors/senior managers are collectively referred to as chief audit executives (CAEs).

The survey results are analyzed and presented in multiple reports of which this is one, using just financial services responses. Complimentary high-level reports are made available to the public through The IIA's Pulse of Internal Audit resource page (visit [www.theiia.org/Pulse](http://www.theiia.org/Pulse)). More in-depth reports for internal audit management are available exclusively to members of the AEC. For more information about joining the AEC, visit [www.theiia.org/AEC](http://www.theiia.org/AEC).

## Financial services focus

Out of the 636 respondents to the 2017 North American Pulse of Internal Audit survey, 186 — almost 30 percent — were from financial services industries. The distribution of respondents according to internal audit function size and financial services industry are shown below.



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## Foreword

The Financial Services Audit Center (FSAC) presents this report as a supplement to the 2018 North American Pulse of Internal Audit report titled [The Internal Audit Transformation Imperative](#) (Pulse). To provide insights specifically for financial services industry CAEs, FSAC conducted a separate analysis on the responses from financial services participants and collected expert feedback from a panel of CAEs representing a variety of financial institutions and insurance companies. The primary topics explored in the financial services analysis are:

- Agility.
- Innovation.
- Talent.

This report is an exclusive benefit for members of FSAC, who are encouraged to share the report with their stakeholders to provide a better understanding of the unique needs and challenges of the internal audit function within the financial services industry.

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# AGILITY

## Embrace to confront disruption

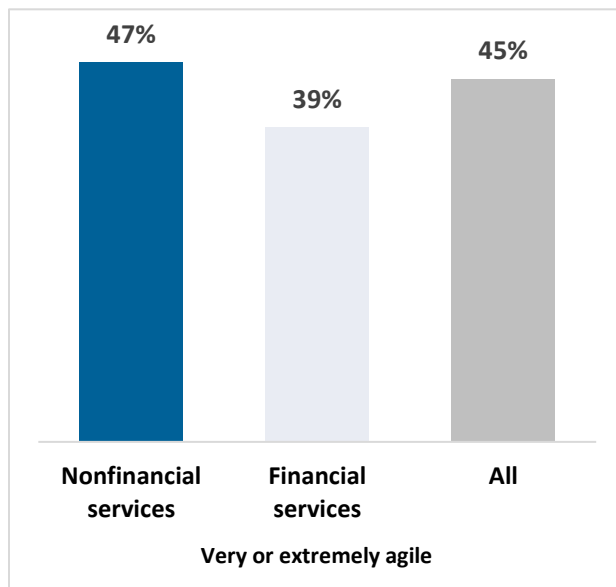
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### Expect changes in risk

**Agile auditing** was defined in the Pulse 2018 survey as "the capability of an internal audit department to rapidly change or adapt in response to the business environment."

Internal audit must quickly change direction when risks change. It is impossible to predict the future with certainty, but changes in risk should be expected. Internal audit has responded well, and with agility, to unexpected risks in the past. In the financial services industry, regulatory changes and new products and services come at a brisk pace, disrupting both day-to-day operations and business strategies. Internal audit functions in the industry must stay flexible in order to adapt to the next shift in this highly regulated and innovative environment.

### INTERNAL AUDIT AGILITY



*Note:* Pulse 2018 survey, Q27: To what degree do you consider your internal audit department to be agile? Percentages show those who chose "very agile" or "extremely agile."  $n = 439$  for nonfinancial services.  $n = 186$  for financial services.

Fewer financial services CAEs assess internal audit agility as very or extremely agile, compared to CAEs in other industries (see above). Some panel experts opined that the lag in internal audit agility

within financial services may be due to the regulatory expectations relative to audit coverage and audit process conformity. These expectations tend to make it difficult to redirect resources and adapt processes to be more agile. A large bank CAE contends that remaining nimble, however, is crucial. The industry is transforming at a pace never before seen. With the ever-changing regulatory climate and the rate in which innovation is hitting the market, internal audit must adjust and cover emerging trends in order to add more value and improve risk coverage.

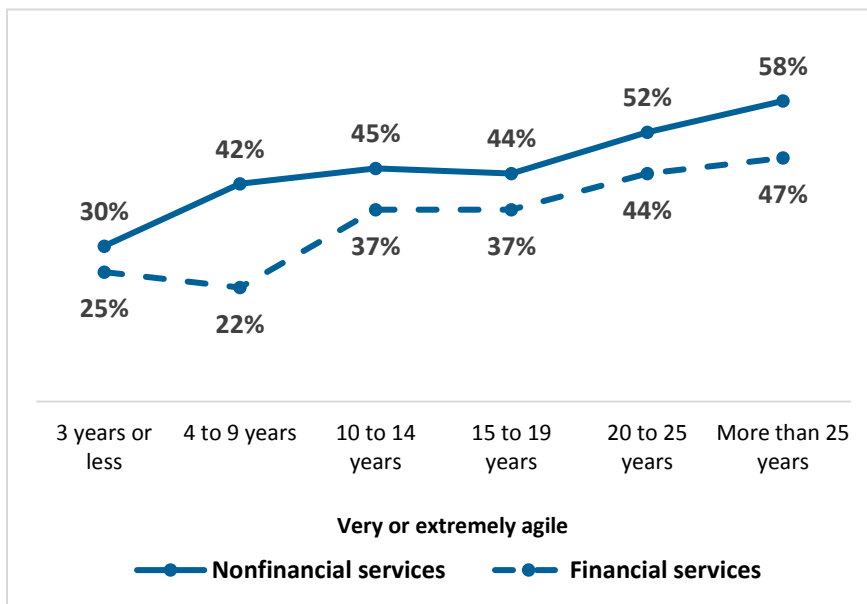
# CAE EXPERIENCE

## Experienced CAEs foster agility

### Broad perspective and diverse backgrounds matter

There is a strong relationship between agility and a CAEs' years of experience (see below). More experienced CAEs are likely to have a better understanding of the importance of agility and how to make it happen while still providing the necessary internal audit coverage. The general belief among the panelists is that the more experienced CAEs likely have been exposed to a greater variety of perspectives and ideologies, which allows them to link seemingly unrelated resources together to achieve agility when needed. One panelist adds that having a diverse background other than financial services not only contributes to outside-the-box thinking, but it also allows one "to look back into the box with a different perspective to come up with solutions."

### RELATIONSHIP BETWEEN INTERNAL AUDIT AGILITY AND CAE EXPERIENCE



Note: Pulse 2018 survey, Q27: To what degree do you consider your internal audit department to be agile? Percentages show those who chose "very agile" or "extremely agile." Compared to Q63: How many years have you been in internal auditing?  $n = 439$  for nonfinancial services.  $n = 186$  for financial services.

# STRATEGIES FOR RESPONDING TO DISRUPTION

Financial services leads in implementing approaches to disruption

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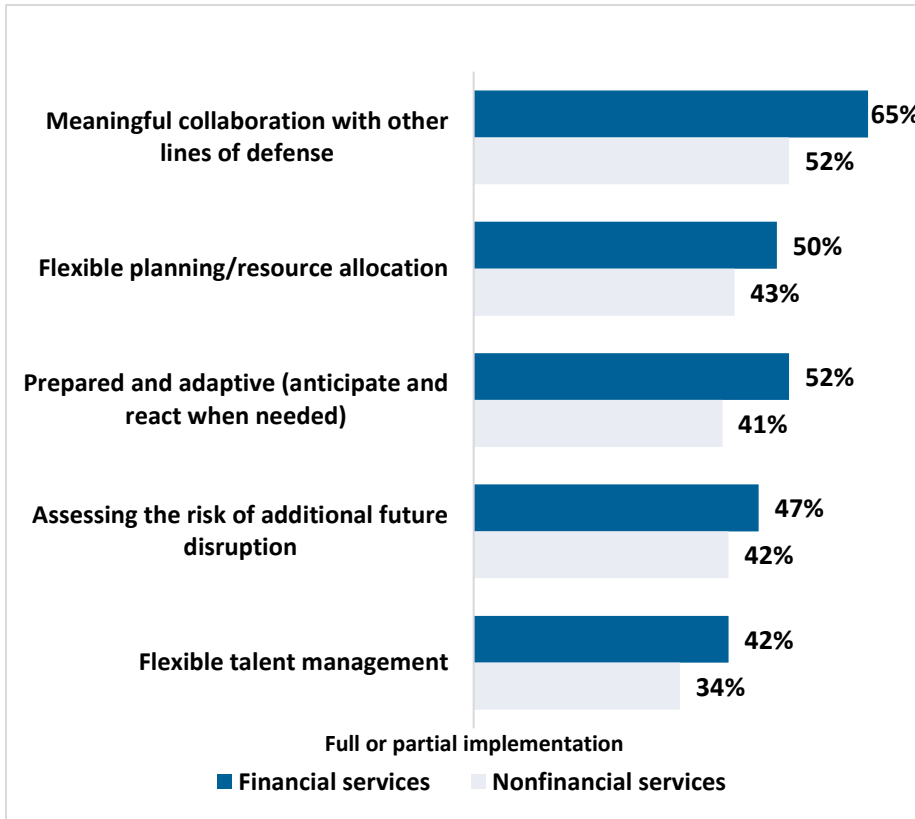
## Is talent the underlying issue?

**As stated** in Pulse, the only thing certain about an annual or quarterly audit plan, or even the audit plan for a specific audit, is that it will likely change before the work is completed. How an internal audit function *prepares* for disruption is just as important as how the function responds when disruption occurs.

A higher percentage of financial services CAEs state their internal audit functions are fully or partially prepared to anticipate and react to disruption, compared to CAEs in other industries (see next page). This presents a bit of a paradox in light of the fact that financial services CAEs assess agility lower, as shown on page 4. How can the level of agility be lower while preparedness to respond to disruption is higher? One panelist suggested that with regulatory expectations, financial market volatility, and the constant stream of innovative products, CAEs in financial services have set a higher bar for themselves. Another panelist from a large bank points out that talent may be the underlying issue. If the internal audit staff and that of their business partners cannot respond with the flexibility required, internal audit agility suffers.



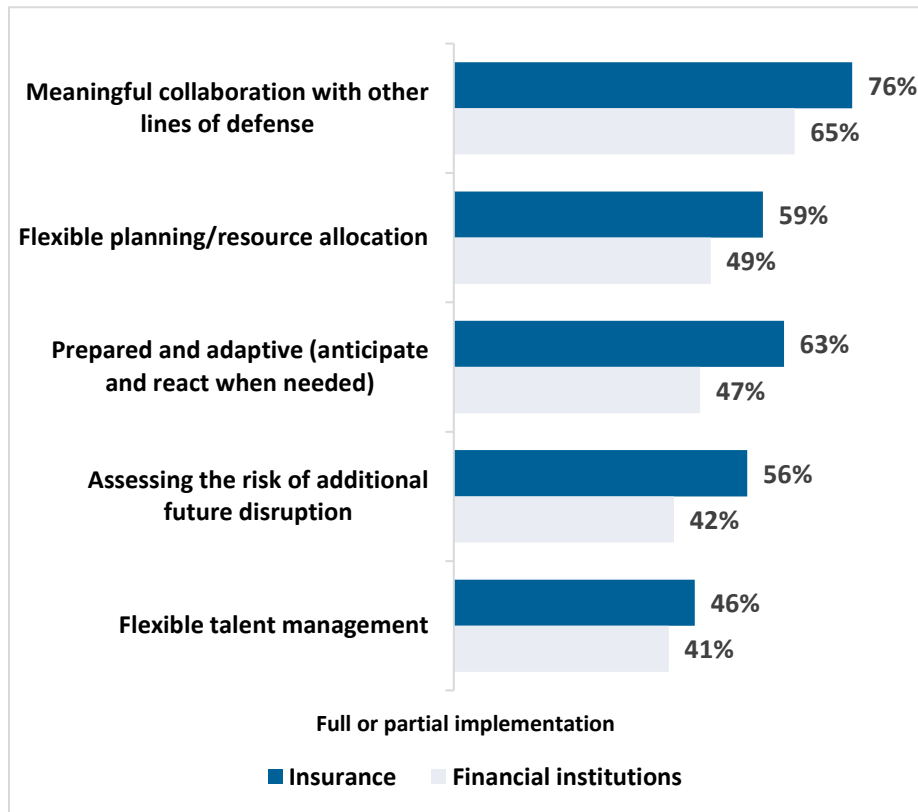
## INTERNAL AUDIT STRATEGIES FOR RESPONDING TO DISRUPTION



Note: Pulse 2018 survey, Q26: For each of the following potential approaches your audit team could use in responding to your organization's disruption, please indicate the degree to which your internal audit department has implemented each of the following:  $n = 148$  for financial services.  $n = 338$  for nonfinancial services.

Within financial services, a higher percentage of insurance industry CAEs state that their internal audit functions are fully or partially prepared to anticipate and react to disruption, compared to the financial institutions. One panelist from the insurance sector explains, “Dealing with disruption is what the insurance world is all about.” Another insurance CAE offers the following explanation: In the United States, insurance companies are regulated by the states and territories, which means they are subject to regulation by up to 54 different jurisdictions — each with unique nuances to consider. Those with international operations face an even greater degree of regulation. Internal audit’s ability to respond to this high level of potential disruption is vital.

### INTERNAL AUDIT STRATEGIES FOR RESPONDING TO DISRUPTION (INSURANCE COMPARED TO FINANCIAL INSTITUTIONS)



Note: Pulse 2018, Q26: For each of the following potential approaches your audit team could use in responding to your organization’s disruption, please indicate the degree to which your internal audit department has implemented each of the following: *n* = 41 for insurance. *n* = 83 for financial institutions.

# ROADBLOCKS

## Perceived roadblocks can be managed

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### Use existing resources more effectively

**Internal audit** will inevitably encounter roadblocks along the path to agility. Perceived roadblocks differ by internal audit function size (see next page). For the financial services industry as a whole, the two highest perceived roadblocks to internal audit agility are inadequate quantity of internal audit resources (42 percent) and executive management’s traditional expectations of internal audit (39 percent). This implies that it would help internal audit to be more transparent with key stakeholders when it comes to staffing needs and the value that internal audit can bring outside of traditional audit services. Clear communication and properly managing expectations with executive management may reduce the size of these roadblocks. However, as stated in the Pulse, internal audit will never get all the resources it could deploy. The CAE’s approach should be to use existing resources more effectively, and to justify additional resources with internal audit’s proven ability to be effective and agile.

Two interesting correlations are revealed regarding internal audit function size:

1. As audit function size increases, the perception of inadequate quantity of internal audit resources as a roadblock decreases. Smaller audit functions lack the capacity to cover everything — especially in an industry with numerous regulatory requirements. CAEs from larger organizations express less concern over resource quantity.
2. When it comes to a high degree of organizational complexity, however, the opposite is true. Sixty-four percent of larger organizations perceive this as a roadblock as opposed to only 10 percent of the smallest organizations. Large institutions, with their myriad of products, services, and facilities obviously have a much higher level of complexity. It is much more difficult to be agile when the organization has many moving parts to coordinate.

## PERCENTAGE OF CAEs THAT PERCEIVE FACTORS AS ROADBLOCKS TO AGILITY

Internal audit function size	1 to 3	4 to 9	10 to 24	25 to 49	50+	All
Inadequate quantity of internal audit resources.	63%	38%	39%	33%	27%	42%
Executive management has overly traditional expectations of internal audit.	35%	50%	43%	17%	32%	39%
There is a high degree of organizational complexity.	10%	33%	37%	33%	64%	33%
There is a low level of reliance on the first and second lines of defense.	28%	25%	37%	22%	41%	31%
Inadequate capabilities of current internal audit personnel.	23%	19%	39%	28%	41%	29%
Stakeholders cannot clearly state business needs and objectives.	28%	37%	19%	17%	14%	25%
Audit committee has overly traditional expectations of internal audit.	28%	23%	26%	6%	0%	20%
Stakeholders are generally not available for collaboration.	13%	19%	19%	6%	5%	15%
None of the above	10%	6%	7%	17%	5%	8%
<b>Number of respondents per group</b>	<b>40</b>	<b>52</b>	<b>54</b>	<b>18</b>	<b>22</b>	<b>186</b>

Note: Pulse 2018, Q30: Which of the following do you perceive as roadblocks to your internal audit team being agile? Select all that apply. Compared to Q38.a: Number of internal audit department employees plus number of outsourced/cosourced internal audit employees. *n* = 186 for financial services.

## The path forward: agility

The Pulse report recommends the following pathways to becoming an agile audit organization:

1. Start with a change in mindset.
2. Prepare to quickly refocus on disruptive risks and opportunities.
3. Prioritize work according to what matters most.
4. Break the mold and create teams with the right blend of skills.
5. Coordinate with other resources in the organization.

# INNOVATION

Pursue quantum leaps

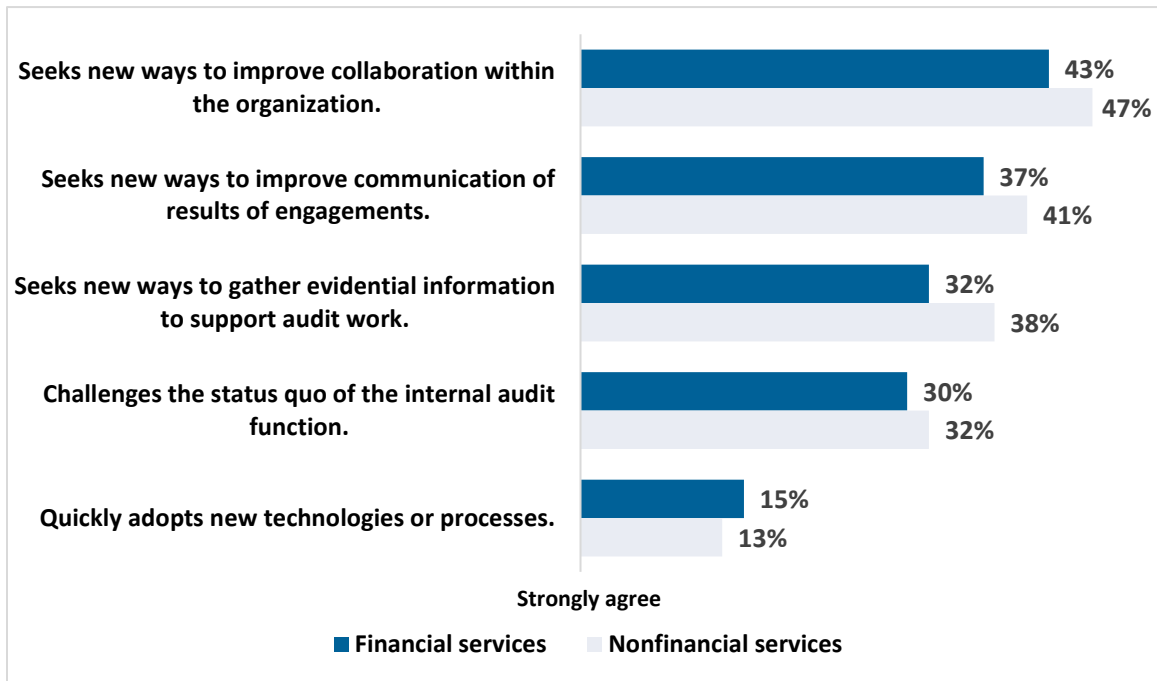
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## Financial services internal audit departments lag in innovation

**Disruption often forces** internal audit to embrace innovation in order to enhance the function's capabilities to fill an increasingly important role in an organization. The Pulse describes this type of innovation as "a path to challenge what is done, how it is done, and how well objectives are being accomplished."

Compared to CAEs in other industries, fewer financial services CAEs strongly agree that their functions are involved in innovative activities (see next page). As mentioned in reference to agility previously, this may be related to the regulatory burden on the industry.

## INNOVATION ACTIVITIES IN THE INTERNAL AUDIT FUNCTION



*Note:* Pulse 2018, Q31: To what level do you disagree or agree with the following statements: Response options were: strongly agree, somewhat agree, somewhat disagree, strongly disagree.  $n = 186$  for financial services.  $n = 439$  for nonfinancial services.

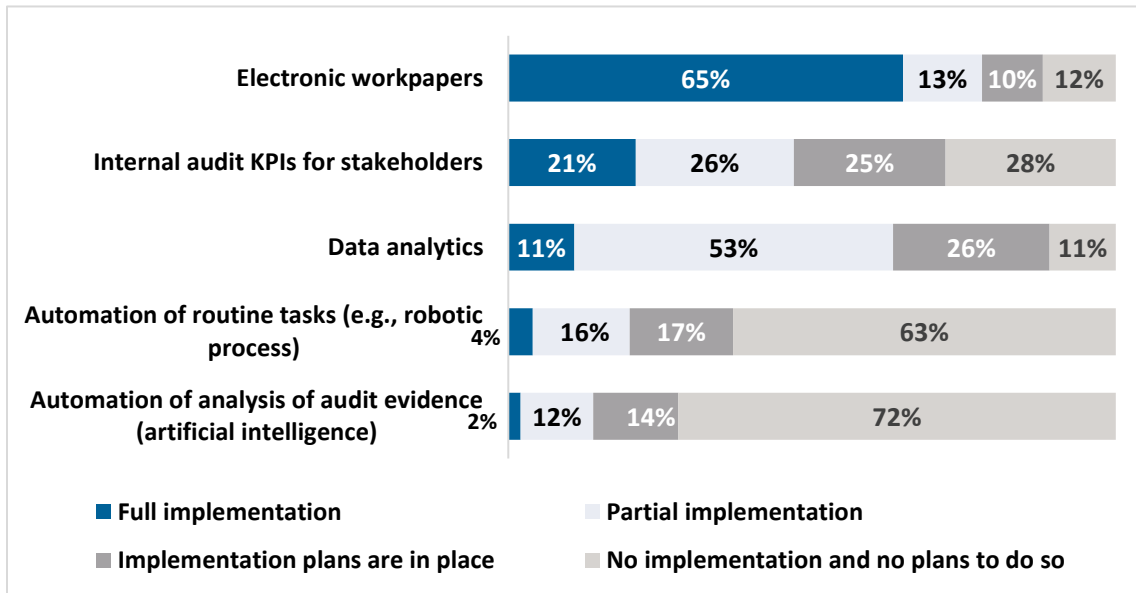
# INNOVATIVE TECHNOLOGIES

Many have yet to implement even decades-old technologies

## Time and resource constraints are no excuse

Most internal audit departments have not fully implemented innovative technologies (see below).

### IMPLEMENTATION OF TECHNOLOGY AND DATA INNOVATION

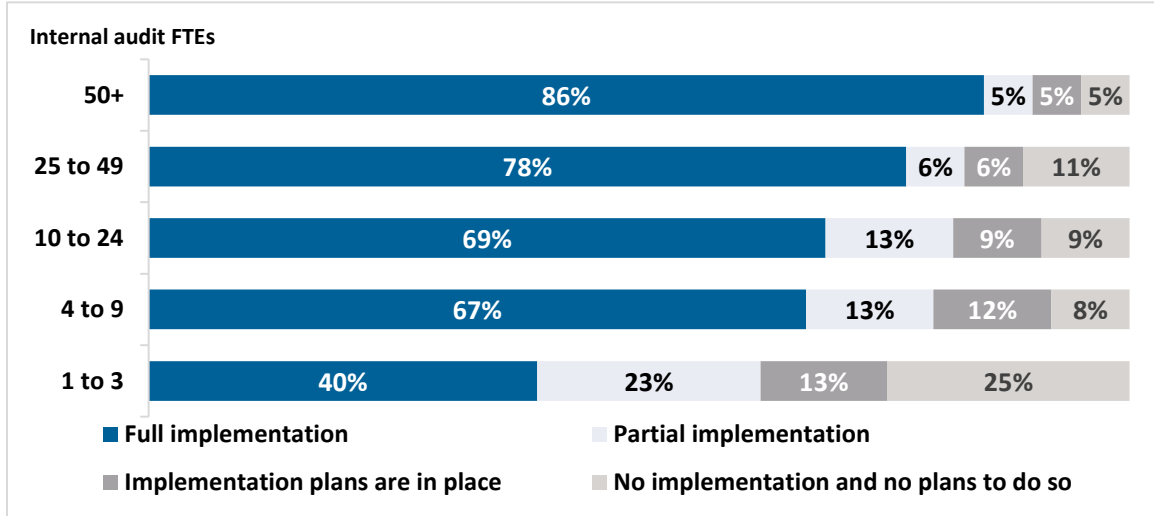


Note: Pulse 2018, Q32: What best describes the degree to which your internal audit department has implemented each of the following? n = 186 for financial services.

Many panelists agree that electronic workpapers have been available and a necessity for years and should not be considered an innovation. That argument adds to the alarming fact that 22 percent of financial services CAEs state they have not implemented electronic workpapers in their internal audit function. Implementation is lowest among the smallest internal audit functions (1 to 3 FTEs), with 38 percent saying they have not implemented electronic workpapers (see next page). One panelist from a small insurance company offered that some smaller internal audit functions are not using electronic workpapers because they may not have the time or resources for the

implementation. Ironically, implementation of electronic workpapers could actually help CAEs address time and resource constraints.

## ELECTRONIC WORKPAPER IMPLEMENTATION

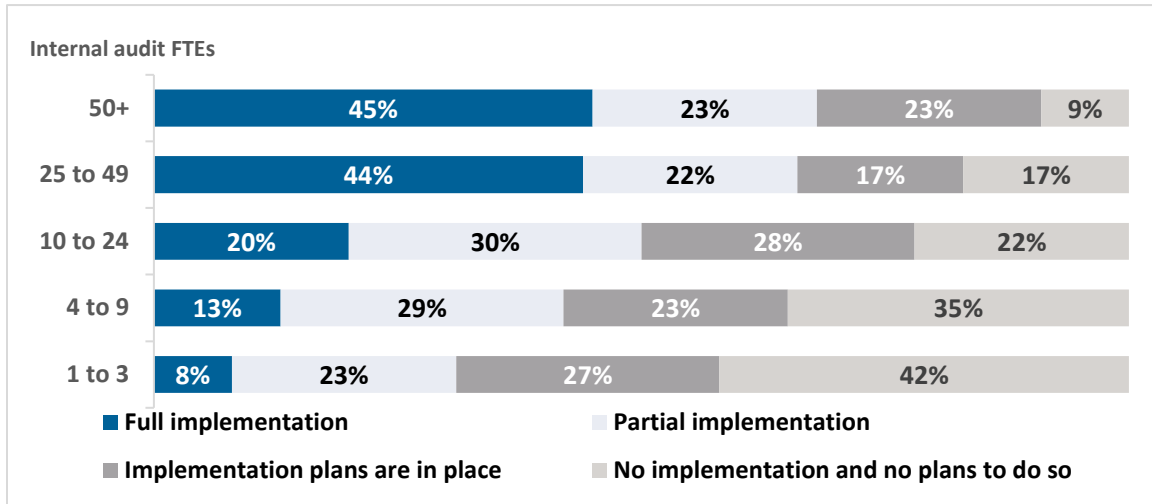


Note: Pulse 2018, Q32\_1: Use of electronic workpapers compared to Q38.a: Number of internal audit department employees. *n* = 186 for financial services.

**Internal audit KPIs** for stakeholders have been implemented by surprisingly few in financial services, on average, only 21 percent. The degree of implementation is related to the size of the internal audit function. Only 8 percent of the smallest organizations report KPIs, increasing to 45 percent among the largest functions (see next page). One panelist makes this observation: “As auditors we tend to hold ourselves less accountable than we hold those whom we audit. We should have metrics demonstrating our performance to management and the audit committee. We should follow the IIA’s International Professional Practices Framework (IPPF) and implement a Quality Assurance and Improvement Program, and we should be having an independent, outside validation performed at least every five years. That is how we will improve, and that is how we will garner and maintain respect from those we audit and those to whom we report.”



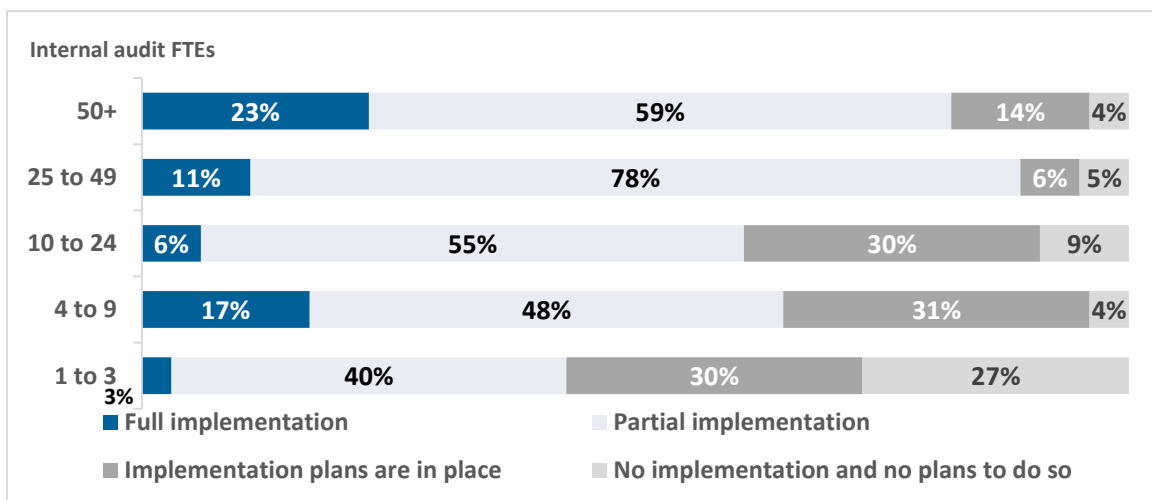
## INTERNAL AUDIT KPIs FOR STAKEHOLDERS



Note: Pulse 2018, Q32\_5: KPIs facilitating understanding of internal audit by stakeholders (e.g., scorecard for audit committee or management) compared to Q38.a: Number of internal audit department employees.  $n = 186$  for financial services.

Full implementation of data analytics in internal audit is rare, but most internal audit functions have achieved at least partial implementation. The exception is for the smallest internal audit functions (1 to 3 FTEs) where less than half of CAEs say they have at least partial implementation (see below). According to the panel, these results reflect the ability of larger audit functions to devote more resources to data analytics. However, although smaller functions are more resource constrained, they are also more in need of continuously improving their efficiencies. Reflecting the data analytics expectations of big banks, one expert panelist comments: “Audit teams need to leverage analytics in every audit — and throughout the audit — from planning to reporting.”

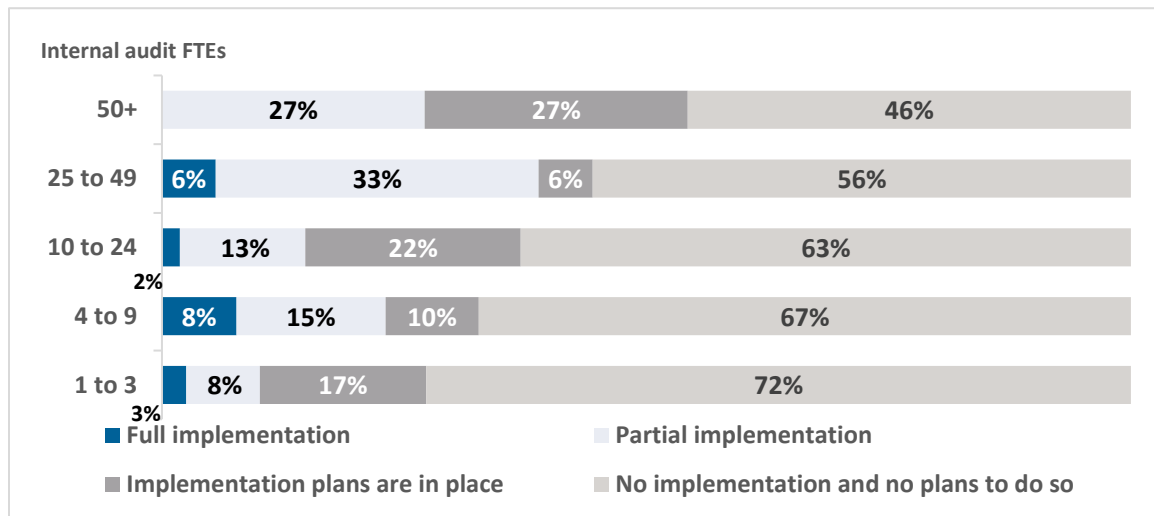
## INTERNAL AUDIT USE OF DATA ANALYTICS



Note: Pulse 2018, Q32\_2: Internal audit use of data analytics compared to Q38.a: Number of internal audit department employees.  $n = 186$  for financial services.

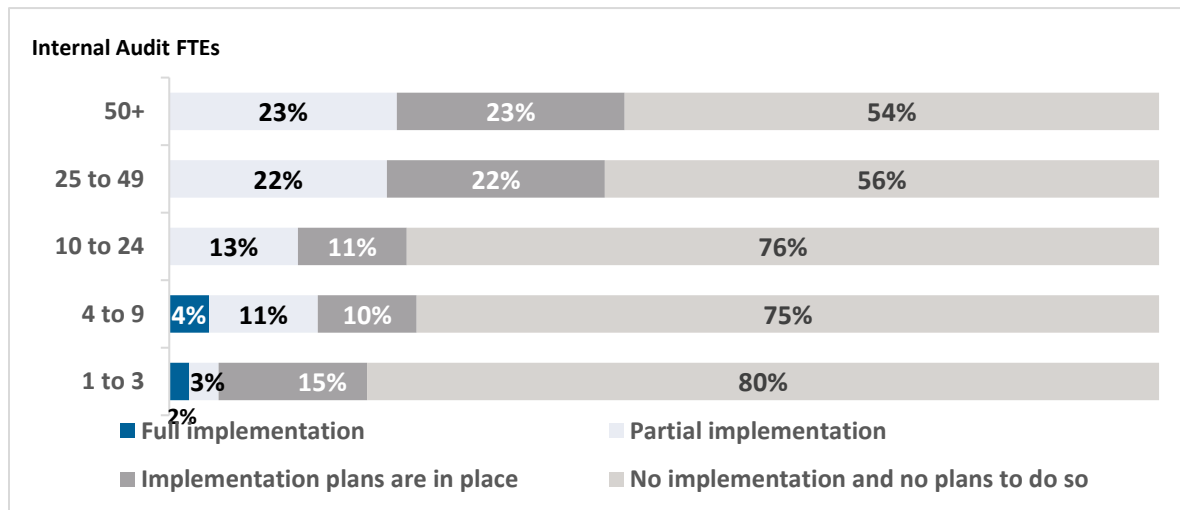
**Automation of routine audit tasks and automated analysis** of audit evidence are rare. For both activities, on average less than 10 percent of financial services CAEs report full implementation, and 33 percent or fewer have partial implementation or implementation plans in place. When broken down by internal audit function size, it was surprising to see that audit organizations with between 4 to 9 FTEs have the highest percentage of full implementation. What is not surprising is that none of the largest institutions with more than 50 FTEs claim to be fully implemented likely due to complexities from years of legacy systems and middleware, and intermingled customer accounts from mergers and acquisitions.

## AUTOMATION OF ROUTINE INTERNAL AUDIT TASKS



Note: Pulse 2018, Q32\_3: Automation of routine internal audit tasks (e.g., robotic process automation) compared to Q38.a: Number of internal audit department employees. *n* = 186 for financial services.

## AUTOMATION OF ANALYSIS OF AUDIT EVIDENCE (ARTIFICIAL INTELLIGENCE)



Note: Pulse 2018, Q32\_4: Automation of analysis of audit evidence (artificial intelligence) compared to Q38.a: Number of internal audit department employees. *n* = 186 for financial services.

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## The path forward: innovation

The Pulse report recommends the following pathways to embrace innovation:

1. Recognize the need for self-assessment and challenge how objectives are being accomplished.
  2. Embrace technological advances.
  3. Do not blame the failure to innovate on the lack of resources.
  4. Develop and communicate the case for internal audit to actively pursue innovation.
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# TALENT

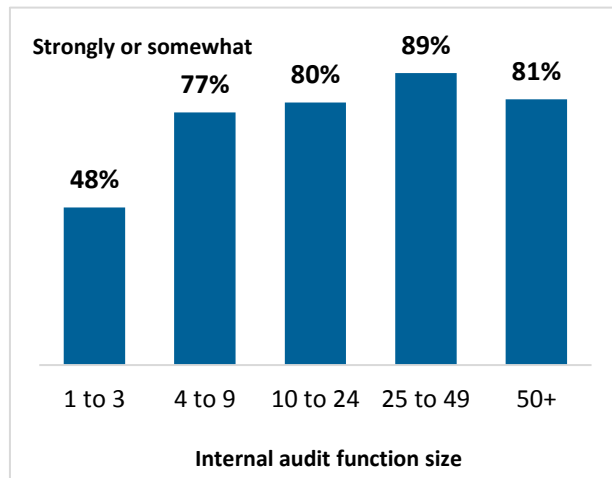
## Focus on tomorrow's risks

### Commit to finding the right talent

CAEs can have all the right intentions and work diligently to increase internal audit's agility and innovation, but without the right talent, these efforts cannot succeed. The Pulse survey explored the challenges and priorities related to recruiting internal audit talent. It also included questions about the collective competency of the internal audit function and what steps are taken to respond to competency gaps.

The percentage of CAEs who strongly or somewhat agree that their internal audit function has sufficient staff differs by internal audit function size (see above). Only about half of CAEs with 1 to 3 FTEs say that they have sufficient staff. These CAEs may consider communicating with executive management and the audit committee that internal audit will do its best with the resources provided, and that internal audit will collaborate with the other assurance providers to constantly seek more efficiencies. One panelist from a small bank encourages identifying champions of internal audit and developing relationships with business units so they have a good understanding of the value internal audit brings to the whole organization. These relationships may take a couple years to develop, but they are well worth the time and effort when the result is a strong audit function.

### STAFF IS SUFFICIENT



Note: Pulse 2018, Q44: Please indicate your level of agreement with the following statement: The internal audit activity at my organization is sufficiently resourced with competent and objective professionals able to carry out the internal audit plan. *n* = 185 for financial services.

# RECRUITING CHALLENGES

## Difficulty in recruiting more experienced staff

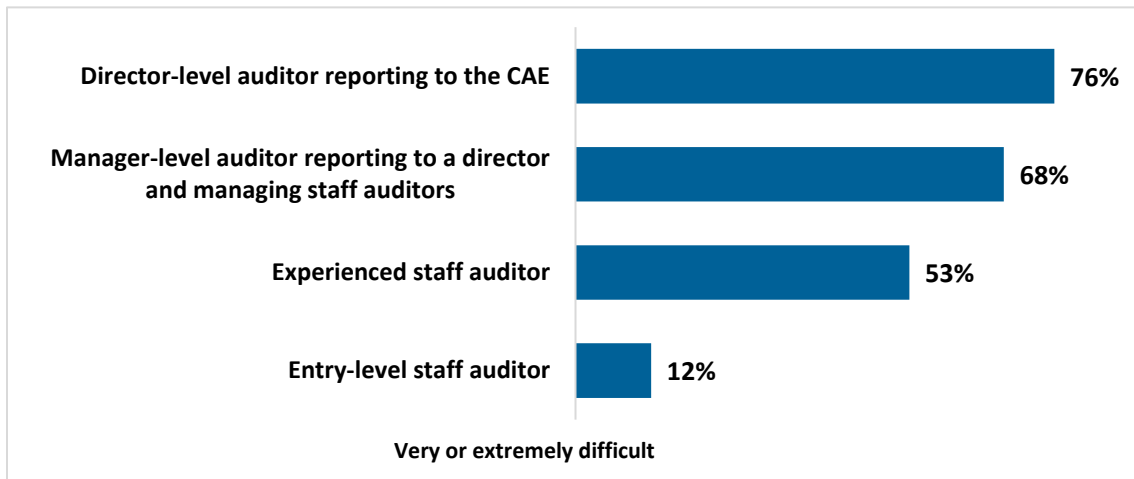
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### Develop a talent strategy

**Finding** experienced, skilled personnel is difficult for any profession. The higher the staff level needed, the greater difficulty in recruitment (see below).

The panel agrees that they are all seeking experienced talent from the same pool. The large institutions tend to attract the best talent from the smaller ones. Some believe in developing talent from within the organization as a means to address the recruiting difficulties, and others also suggest looking for talent outside of audit. Even with the perceived talent shortage, many of the CAEs agree that when internal auditors have opportunities in other business areas, internal audit benefits because the knowledge of internal controls and the value of internal audit are spread throughout the organization.

### RECRUITING DIFFICULTY FOR DIFFERENT STAFF LEVELS



*Note:* Pulse 2018, Q13: Please indicate the level of difficulty in recruiting talent at each level. Response options: extremely, very, somewhat, not difficult. Financial services only.  $n = 168$  for financial services.

CAEs identified the competencies most in need collectively by their internal audit functions as:

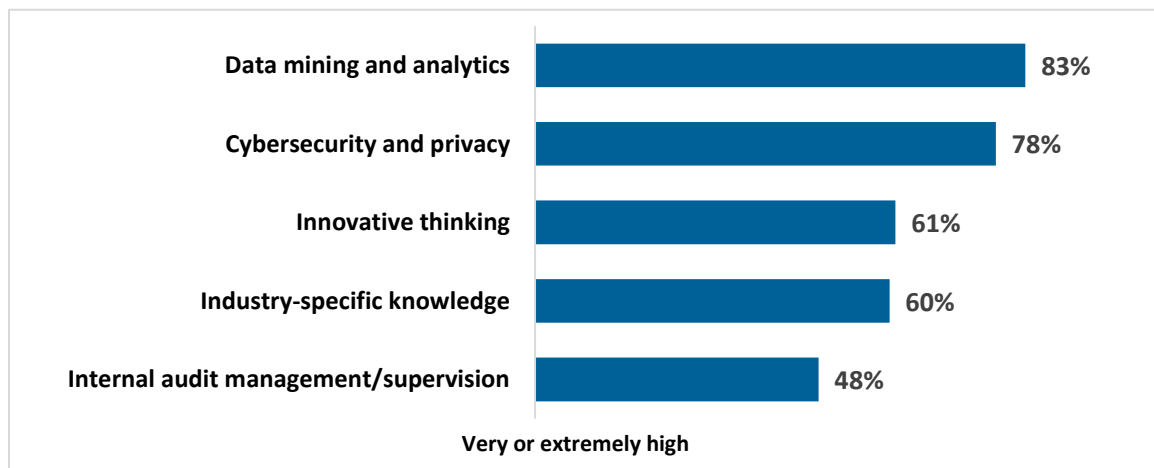
- Data mining and analytics.
- Cybersecurity and privacy.
- Innovative thinking.

According to the experts, this list of competencies is an accurate reflection of reality and highlights areas to improve. In addition, one large bank panelist contends that data proficiency will soon become a standard competency. He expects that the list of valued competencies in the near future will include navigating ambiguity, learning agility, and the ability to contextualize risks not historically experienced (e.g., artificial intelligence and cloud computing).

Candidates with these competencies are not easy to find.

Technology talent is most difficult to recruit. Eight in 10 CAEs have very or extremely high difficulty in recruiting talent with competencies in data mining and analytics, and cybersecurity and privacy.

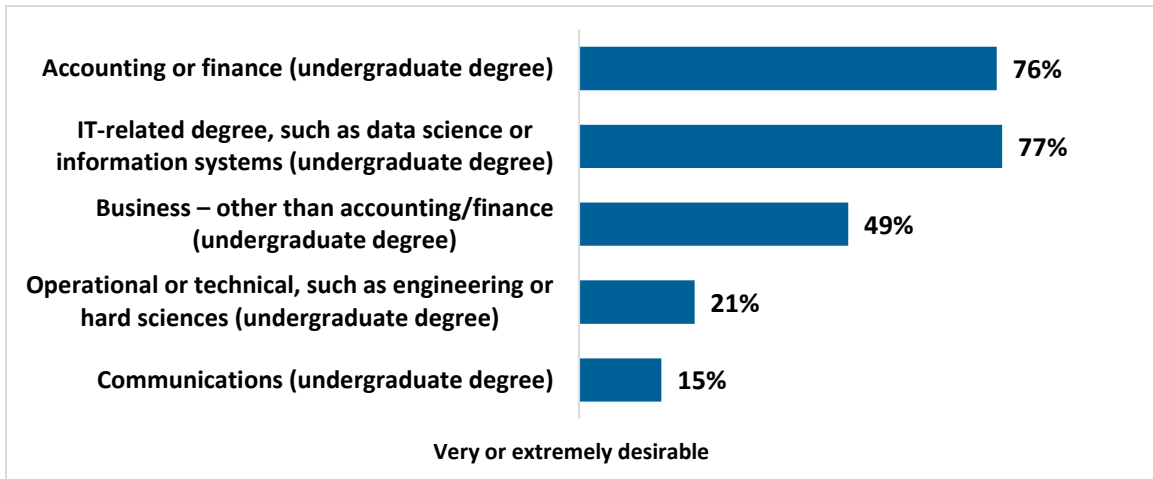
### COMPETENCIES MOST DIFFICULT TO RECRUIT



*Note:* Pulse 2018, Q15: Please indicate the degree to which you have difficulty recruiting individuals with the following competencies. *n* = 166 for financial services.

CAEs say that the academic degrees that they most actively recruit are accounting/finance and IT-related degrees. Considering the high level of difficulty recruiting talent with data mining and cybersecurity competencies, the emphasis on IT-related degrees is well-warranted.

## ACADEMIC DEGREES MOST DESIRED IN RECRUITING

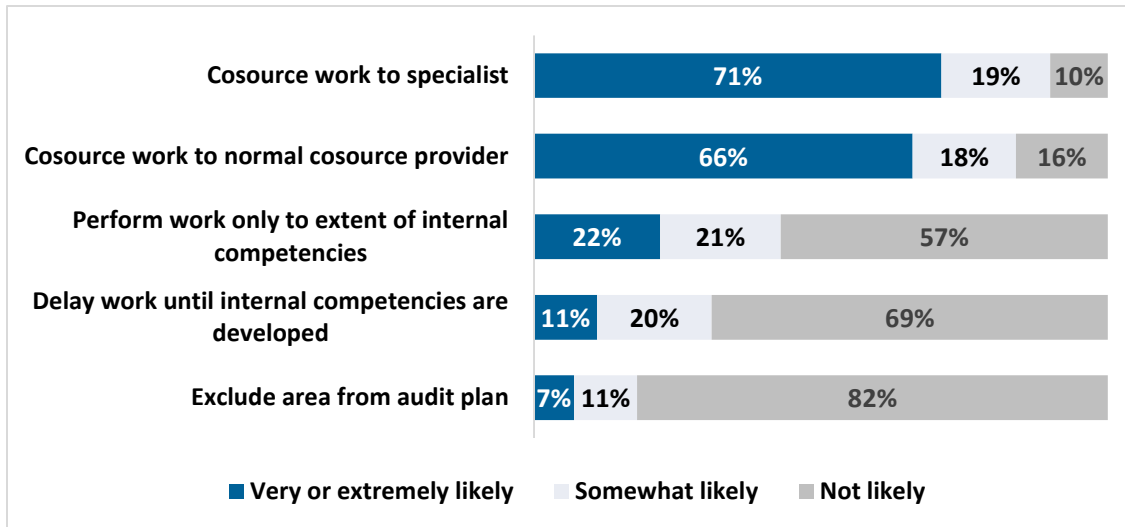


Note: Pulse 2018, Q17: Please rate the desirability of different types of professional degrees when recruiting. *n* = 171 for financial services.

The Pulse report states, “Data analytics can be used as a key enabler for innovation, and cybersecurity is a top risk. Innovative thinking, communication, technology, and other skills that support innovation and agility are in short supply. CAEs need to focus on building these skills among existing staff.” Panelists agree with this perspective. CAEs need to recruit those with fundamental skills while at the same time developing the competencies within the internal audit function. If development is not feasible or practical, then CAEs must consider other means of bridging those competency gaps.

The most common approach to fill a talent gap is to cosource (see next page). What is alarming, though, is that there are a number of CAEs who use other approaches that all involve scope limitations to avoid audit work that requires skills that lie in the skills gap. According to the Pulse report, while internal auditors should not perform work for which they are not competent, altering scope to avoid risk areas cannot be a long-term strategy.

## RESPONDING TO COMPETENCY GAPS IN THE INTERNAL AUDIT FUNCTION



*Note:* Pulse 2018, Q20: If your audit team does not collectively possess the knowledge, skills, and other competencies needed to perform in each a specific area, how likely are you to respond in the following ways? *n* = 177 for financial services.

### The path forward: talent

The Pulse report recommends the following pathways to attract and develop top talent:

1. Make sure the risks that drive internal audit's scope drive staff competencies and not the reverse.
2. Develop a talent strategy to ensure the right pipeline of qualified personnel.
3. Engage stakeholders and obtain their support for internal audit's talent management strategy.
4. Start looking for candidates with different backgrounds.
5. Reconsider which skills are most essential for success.
6. Include future-focused training and development programs geared toward specific levels of staff.



# CONCLUSION

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Both the Pulse report and expert panelists agree that internal audit must continue to innovate in order to add value to the organization. Innovation not only lies within technology, but also in internal audit's ability to be more agile in order to respond to disruptions. It most certainly lies within the way internal audit develops talent to meet key competencies and prepare for the next disruption. The complete 2018 North American Pulse of Internal Audit report can be found on the [Audit Executive Center](http://www.theiia.org/Pulse) website at [www.theiia.org/Pulse](http://www.theiia.org/Pulse).

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#### ABOUT THE FINANCIAL SERVICES AUDIT CENTER

The Financial Services Audit Center (FSAC) is a specialty offering of The IIA for financial services auditors. FSAC was established to provide financial services auditors with targeted, high-quality professional development; networking opportunities for knowledge sharing among financial services stakeholders; and ongoing, timely, and relevant reporting on trends, benchmarking, and thought leadership in the internal audit profession. For more information, visit [www.theiia.org/FSAC](http://www.theiia.org/FSAC).

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