

Internal audit and audit committee

Effectively managing the expectations of the audit committee from an internal audit perspective

The recent study of KPMG¹ offers insights into what members of Executive Management and the Board of Directors including the audit committees are expecting from the internal audit function and to what extent these expectations are met.



¹ [Seeking Value through Internal Audit, KPMG Study 2016](#)

By conducting more than 400 interviews with audit committee chairs (AC head) and Chief Financial Officers (CFO), the findings of the KPMG study "Seeking Value through internal audit" call attention to a general "value gap" between what the AC heads and CFOs identify as priorities and what they are receiving from their internal audit functions (IA) in the form of IA reports and additional insights. This gap predominantly exists in the following areas:

- assessing and managing key risks of the firm;
- providing insights into emerging risks that can threaten operations in the future; and
- providing insights into how the organization is focusing on generating sustainable profits.

In general, the interviewed stakeholders consider the ground-level risk assessment of IA to be, at best, adequate. In other words "the job gets done". However if it comes to more comprehensive detection and response to emerging risks, only one in ten respondents believes that this is addressed satisfactorily by their IA function. Particularly, the respondents mention that IA functions do not provide enough of a "surprise" effect; that being things which are new to the stakeholders and which they have not considered to be of relevance so far.

Look beyond existing risk paths

This leaves a great opportunity for additional value to be provided by the IA function as part of its assurance assignment. IA needs to become more proactive in identifying and mitigating the current key risks of the organization. It should also more prominently outline possible opportunities and dangers that might not yet be

very transparent and clear to the firm but will matter in the near future.

As a result, the assurance provided by IA should not only focus on assessing the design and effectiveness of the current corporate governance frameworks and control-portfolios, such as Internal Control Systems (ICS) or SOX-404, but also talk about additional considerations that can be important to stakeholders when reflecting on the future success and development of the organization.

Such reflections and insights can for example include the following matters:

- Effectiveness on how the firm's strategy is being rolled-out by the auditees and if they are on track.
- How goals are being met in relation to generating sustainable revenue streams.
- How processes are aligned within the organization in terms of efficiency and effectiveness.
- Efficiency and effectiveness of the alignment to the functionalities of the IT-systems.
- How potentials for cost-saving are identified, followed-up and put into practice.
- To what extent modern tools such as mass-data-analysis are being used to gather better insights and provide a more comprehensive view on relevant topics, e.g. workflows that require a lot of manual intervention.
- How key projects are progressing and to what extent they are meeting the desired objectives.
- What the auditee's performance is compared to similar functions within the organization.
- What type of risks are being bottom-up fed into the organization and could become key risks in the future.



More effective coordination between assurance functions

In this context the survey shows that nearly half of the companies currently track risk through a compliance function, half as many through their legal function and only nine percent through an Enterprise Risk Management Function. Stakeholder responses also indicated that they care more about how IA was responding to risk, especially emerging risk, than about what function was accountable for risk tracking.

This suggests that a stronger alignment of IA with other assurance functions within the organization, as for example Compliance, Legal or Risk Management, is needed when it comes down to developing the strategic audit plan and preparing the scope of specific audits.

Although remaining independent from the organization, by not taking on managerial ownership for managing risk, IA should seek to get more preliminary insights and intelligence from the other risk tracking and facilitating functions.

In other words, a combined assurance view should be emphasized by the assurance functions. This would allow the stakeholders to have a more comprehensive, overall view on the current corporate governance state of the organization and to understand if key risks are adequately addressed in terms of monitoring and auditing.

To facilitate this collaboration, greater efficiency and effectiveness is required. This is where technology comes into play.

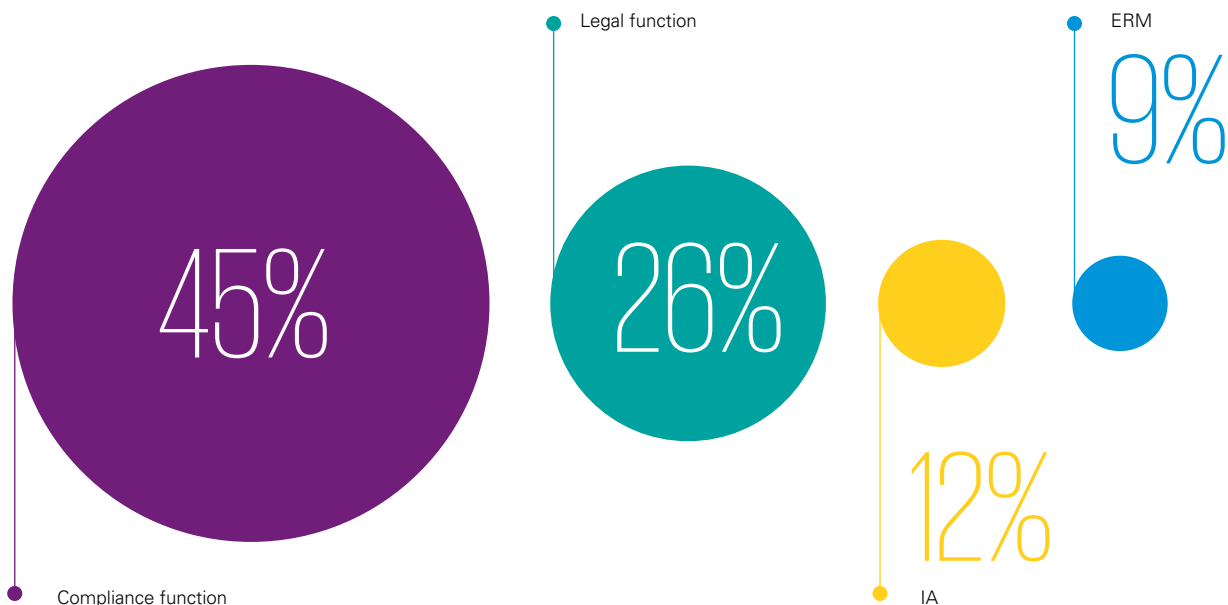
Use of technology to enable fresh perspectives

It's no longer useful to use phrases like "technology is the future." If companies are not fully integrating technological advancements in every aspect of the business, no degree of strategic prowess is going to make a measurable impact. How IA is conducting its audits is no exception to this matter. The full potential of data analytics has been recently outlined in a 2015 KPMG study.²

The study points out how interpreting data patterns will be an effective key differentiator for organizations in the future and how a good Data & Analytics (D&A) strategy has the potential to improve the financial performance. This is done by creating value through tapping on the unused growth potential, controlling key risks and optimizing performance. Currently, more than 63 percent of companies actually use some sort of D&A technology. However, the approach is mostly isolated or specifically focusing on ad-hoc instances only. This rather statistic method in using data analytics will drop to less than 50 percent in the next three years, while the use of enterprise-wide risk-focused D&A capabilities will

² [Clarity on Data Analytics, KPMG Publication 2015](#)

Where do companies address their enterprise-wide risk?



Source: Seeking value through Internal Audit, KPMG International, 2016

jump from 35 percent to 47 percent. This enterprise-wide risk-focused D&A promises to have a more holistic perspective on risks and allows for a common understanding across the various assurance functions regarding, for example, the magnitude of a specific risk or issue.

KPMG believes that if the IA function gave way to operating through an integrated, organization-wide technology platform, then the incorporation of risk assessment, D&A, knowledge and experience would advance the potential of IA to deliver significant benefits and added-value not only for the stakeholders, but for the whole organization.

The potential for making value real through technology is enormous, especially if IA were able to integrate a higher percentage of data analytics procedures into its audit approach. An integrated approach to using D&A throughout the audit process (for example, analytics-driven continuous auditing, dynamic audit planning, audit scoping and planning, audit execution and reporting) would provide greater insights and value.

Particular examples of such benefits would be a more effective monitoring of risk indicators that could lead to the identification of emerging risks, assessing adequate risk coverage and facilitating data-driven decisions that provide actionable insights into the strategic drivers of the business. All in all, a holistically integrated technology platform would optimize both business performance and the risk mitigation process of the organization.

IA profile demands wider skill sets

As for the existing desire to move toward such a technology-enabled approach, when asked about the key skills needed in IA, the respondents concluded that technology (62 percent) is second only to communication (67 percent) in importance, while critical thinking and judgment ranked third (52 percent).

This confirms the trends already outlined in a study by the Institute of Internal Audit (IIA)³ in 2013 when analytical and critical thinking combined with good communication skills and strong data mining skills were captured as the top skills desired from internal auditors.⁴

Conclusion

With the global economy being in a decade of challenges and uncertainties, the key stakeholders of organizations are seeking an approach to IA that goes beyond reviewing past activities. They want an IA function that is insightful, forward-looking, and which is not afraid to go beyond preserving current assets, instead focuses on creating value on a departmental, divisional, or organizational level.

To meet these expectations, IA leaders must strive to migrate to more advanced stages of maturity. This includes evolving the basic auditing processes and skills towards an approach of creating value and bringing insights for an organization. At the same time, IA leaders should implement stronger use of company-wide data mining and analysis tools and a more effective and efficient coordination and cooperation with other assurance functions within the organization. The skill sets and competencies of the IA team may have to be adapted to enable the IA function to deliver the expected value to its stakeholders.

³ Pulse of the Profession Survey, The Institute of Internal Auditors (IIA) 2013

⁴ [Transforming Internal Audit Through Critical Thinking, KPMG Publication 2014](#)



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