

NEW TRENDS IN INTERNAL AUDIT

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Abstract: The entity's internal audit structures are faced with increasingly complex requests from executive management, the board of directors and, ultimately, investors. Switching from conventional internal audit to risk-based internal audit takes into account the future of a business, addressing the issues of those responsible for managing risk. The trend is to identify measure and prioritize risks. This is due to the increasing requirements of risk management, information, insurance, consultation leading to the continuous adaptation of the internal audit function. On this basis, we consider important research efforts to identify new trends in internal audit that require the extension of scope to activities to add value.

Keywords: insurance, internal audit, business risk, corporate governance, management.

Introduction

In the business environment, there is a change in the frequency of occurrence of external disrupting factors, which are transformed from disrupting factors with cyclical occurrence into ones with a continuous occurrence. Thereby, the tendency of the internal audit department is to focus on business risks and to add value by identifying risks, determining their potential effects, and ways to eliminate or mitigate their effects. Also, internal audit work provides the external auditor with information processed in the internal control assessment process.¹ From our studies we noticed that many researchers and authors are currently addressing the concept of risk prevention in internal audit, presenting sustainable options for internal auditors.

As for the business environment, the internal audit activities have a continuous dynamic, evolving from the use of cyclical audit plans to assess the internal control activity in the past to the use of a risk-based audit plan in the present and the assessment of the risk management process adopted by the company in the future.

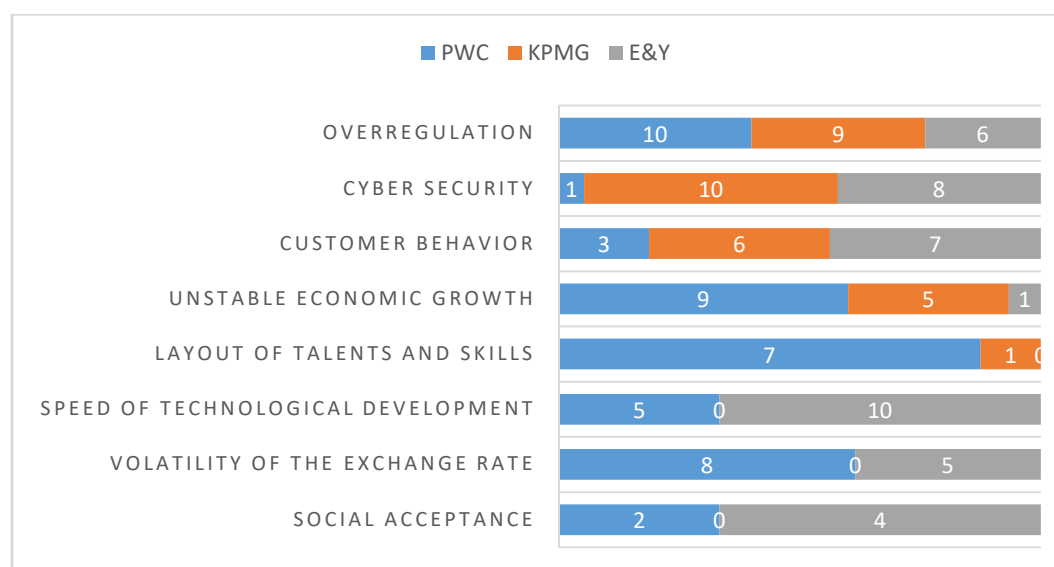
Research Methodology

The research is of a qualitative type. We want to highlight the evolution of the expectations, trends, objectives, means and techniques currently used globally, as well as the trends and directions of future development of the profession. From the investigations conducted in the literature, as well as the latest studies in the field by international bodies or practitioners, we have turned our attention to new risk factors such as cyber security, technological progress or new business models. The presented research is an integral part of a complex project, which aims at highlighting the evolution of the stakeholders' requirements regarding the internal audit function, the way in which the internal audit function meets these requirements as well as the latest risk categories and the latest technologies, and means used in the field of work.

¹ Marcel Ghiță, *Auditul Intern*, 2009, Editura Economică, București, pp.44-46

Disruption factors identified for companies today

Technological developments, scientific research, and the extent to which innovations and scientific discoveries are used, are experiencing unprecedented progress. Technological development, widespread use of the internet and new inventions are not just business opportunities but also risks for companies. Considering the above mentioned, we appreciated that in the vision of those in the executive management of corporations the challenges presented by the new era of digitization are ranked first among the disruption factors. Analyzing the data presented by three well-known companies for their contribution in the audit field, PriceWaterhouseCooper, KPMG and Ernest & Young, we have done, according to Graphic 1, a classification of the disruptive factors according to their importance in the vision of the persons with roles in executive management of corporations, in 2017.



Graphic 1. Classification of disruptive factors according to the level of importance
 Sours: Based on information found in bibliographic sources.²³⁴

In order to have a relevant result of the analysis, we made a rating grid according to the importance of each factor presented in the survey charts, by the three companies and presented the results simultaneously so that they can be analyzed concurrently and comparatively.

According to the analysis, we identified eight disruption factors that were present in the classifications of at least two of the three companies that conducted the studies. The first and most important for executive leadership among disruptive factors, according to our scoring grid, is over-regulation, and therefore inconsistent with our expectations, the speed of technological development is considered the main disruptive factor. The speed of technological development is considered only in two of the three studies, with a very high importance for the sample studied by Ernest & Young and an average importance for the one studied by the PWC.

According to our analysis, three other factors common to the three studies were presented: cyber security, customer behavior and unstable economic growth. In addition to the factors presented in Graphic 1, there were others which did not present any common points between the

²PriceWaterhouseCoopers, „21st Annual Global CEO Survey”, 2018 - <https://www.pwc.com>

³ KPMG, „Key Risks for internal audit”, 2017 - <https://assets.kpmg.com>

⁴ Ernest&Yong, „Top Business risks facing mining and metals 2017-2018”, 2017 - <http://www.ey.com>

three studies but consider relevant to be mentioned: Data Analysis and Big Data, Management and Monitoring, Tax Austerity, Operational Efficiency.

The factor mentioned as Social Acceptance refers to the Corporate Social Responsibility (CSR) function that has recently begun to present a new area for internal audit, especially since 2005, when Japan first began reporting in formations on social responsibility activity.⁵

Internal Audit: Features and Expectations

We note that, in the past, the most important achievements in the field of internal audit highlighted the shift to a risk-based approach as well as increasing the reputation of this function by helping companies achieve their goals. At the time of 2012, the main risks capturing the attention of the Audit Committees were: compliance risks, operational risks, IT risks, financial risks and strategic risks, and in the opinion of CEOs: strategic risks / business risks, operational risks, compliance risks, financial risks and IT risks in general.⁶

According to previous studies⁷, in the opinion of the majority of stakeholders, the key factor in organizing the internal audit activity is the management of the organizations. The leaders of the internal audit compartments face a changing (economic, political, legislative) environment, but also a rising risk. According to the above-mentioned study, in 2016, 54% of respondents were of the opinion that the internal audit function adds significant added value and 62% of them expect a more significant contribution to this function. As far as the 2017 statistical data is concerned, there is a decrease, with only 44% of the stakeholders saying that the internal audit function contributes added value to companies' efforts to achieve the objectives.⁸ Although 55% of managers and board members interviewed in 2015 said they were planning to have an internal audit department that would become a trusted consultant by 2020, 2017 only 9% of them considered this function fulfills the status of a trusted consultant.⁹

Through Chart 2, we compared the stakeholders' opinion with internal audit. Thereby, it can be noticed how during the period analyzed in the public opinion of the stakeholders the appreciation that the internal audit function brings added value to the entity is decreasing as compared to the view that the internal audit function offers added safety in managing risks, which is growing.

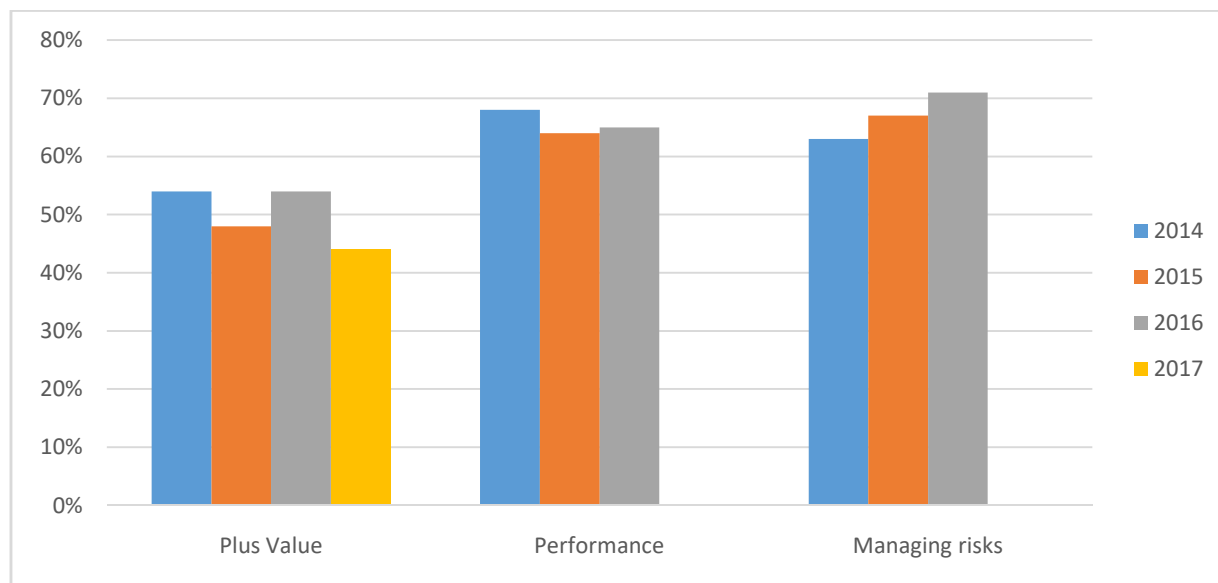
⁵ Tiffany Daykin, "The Role of Internal Auditing in Sustainable Development and Corporate Social Reporting", 2006, The Institute of Internal Auditors, pp. 3-5

⁶ The Institute of Internal Auditors, Sharpening our Focus on the Road Ahead: Internal Audit in 2020, 2013 - <http://www.dallasiaa.org>

⁷ PriceWaterhouseCoopers, „2016 State of the Internal Audit Profession Study”, 2016 - <https://www.pwc.com>

⁸ PriceWaterhouseCoopers, „2017 State of the Internal Audit Profession Study”, 2017 - <https://www.pwc.ru>

⁹ PriceWaterhouseCoopers, „2017 State of the Internal Audit Profession Study”, 2017 - <https://www.pwc.ru>



Graphic 2. Representation of stakeholders' opinion on the added value of internal audit
Sours: Based on information found in bibliographic sources ¹⁰

Among the expectations of the stakeholders addressed to the services of the internal audit function, the following can be listed:

- Orientation of the internal assurance audit objectives to strategic risks, where this component is considered as a priority and benefits from stakeholders' appreciation;
- good knowledge of the mission, strategy, risks and objectives of the organization;
- increased input in terms of risk advisory capacity;
- efficient relationship with the management and the members of the Board of Directors, communicating more often and not only in writing;
- good coordination with the second line of defense in order to meet the objectives of insurance work.¹¹

As far as internal auditors are concerned, it is advisable that they pay attention to:

- acquiring a good knowledge of the mission, strategy, objectives and risks of the organization;
- taking into account both current and future risks when planning audit work;
- using the unique position in the organization to increase risk understanding and risk management throughout the organization.¹²

With regard to the relationship between the internal audit department and the management structures, 45% of the internal audit departments are subordinated to the executive management and 73% report to the Audit Committee or the Board of Directors, 35% of the respondents expecting a budget increase (only 9% % decrease) and 26% increase in the number of members of the internal audit department (only 6% decrease).¹³

¹⁰ PriceWaterhouseCoopers, „2016 State of the Internal Audit Profession Study”, 2016 - <https://www.pwc.com>

¹¹ Chambers Richard, "Internal Auditing: Poised to the Future: Global Outlook, 2017, The Institute of Internal Auditors, <https://www.iaa.nl>

¹² Chambers Richard, "Internal Auditing: Poised to the Future: Global Outlook, 2017, The Institute of Internal Auditors, <https://www.iaa.nl>

¹³ Chambers Richard, "Internal Auditing: Poised to the Future: Global Outlook, 2017, The Institute of Internal Auditors, <https://www.iaa.nl>

Internal Audit: Strategies and Directions to Follow

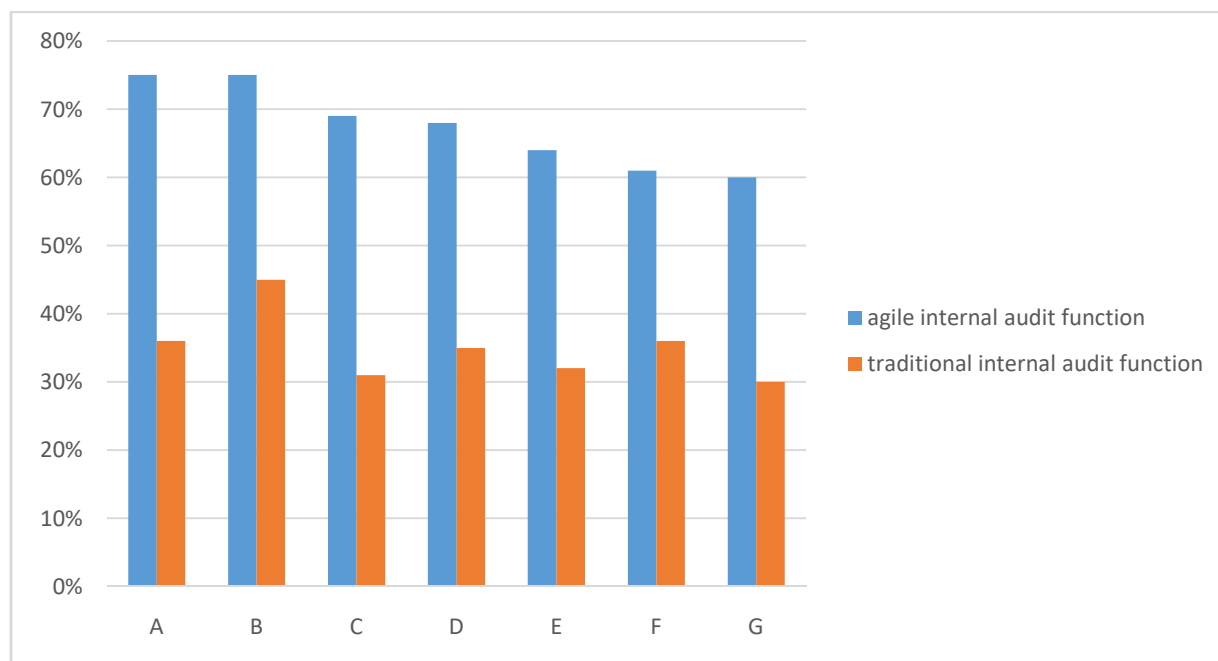
In order to improve internal audit work and to increase the prestige of the profession, Richard F. Chambers, President of the Institute of Internal Auditors, proposes five strategies to follow:

- satisfying the client's desire;
- achieving an internal audit function with increased agility;
- transforming the talent of the internal audit function;
- revolutionizing the processes specific to the internal audit function;
- increasing the prestige of the internal audit function.¹⁴

By satisfying the customer's desire, in the present context, it is meant to achieve the expected performance by the stakeholders. They generally have different expectations or attach different importance to the objectives, depending on the position held in the organization chart or their interests. Meeting stakeholder expectations may involve summing up the other four strategies to follow.

An agile internal audit function means a significant contribution to the company's effort to meet the challenges and about which the company's management has stated that it has done more than an effective implementation of the audit plan.¹⁵ The difference between a traditional internal audit function and an agile internal audit function is due to the fact that the agile internal audit function addresses a larger number of disruptive factors at the company.

By depicting graph 4, we highlight the difference identified by the PWC between the performance of an agile and traditional audit function, taking into account the level of involvement of the two on the following factors: A - operational disrupters; B- new regulations; C- Changes in business or strategy model; D - technological advances; E-brand or reputation incidents; F- financial challenges; G-Innovations in the Digital Sphere.



Graphic 3. The level of involvement of the agile internal audit function as compared to a traditional one

¹⁴ Chambers Richard, "Internal Auditing: Poised to the Future: Global Outlook, 2017, The Institute of Internal Auditors, <https://www.iaa.nl>

¹⁵ PriceWaterhouseCoopers, „2017 State of the Internal Audit Profession Study”, 2017 - <https://www.pwc.ru>

Sours: PriceWaterhouseCoopers, „2017 State of the Internal Audit Profession Study”, 2017
- <https://www.pwc.ru>

An agile internal audit function is also involved more rapidly at the time of the occurrence of the risks, in 68% of cases it is asked for a point of view regarding the risks associated with the disruption factor, as opposed to 36% for the other audit functions internal. Stakeholders with an agile audit feature reported 88% that the internal audit function contributes significantly to the company's effort to achieve its goals.¹⁶

Transforming the talent of the internal audit function can be accomplished by adapting the capabilities of the internal audit function to emerging risks through development, acquisition and outsourcing.¹⁷ In order to achieve this goal, it is necessary to act on two lines of action: to hire, recruit and train experienced auditors and to provide the internal audit department with dedicated software programs to provide auditors with a range of tools to facilitate:

- management of collected information;
- data analysis;
- data mining tools;
- carrying out a continuous audit;
- mission planning;
- tracking the implementation of recommendations;
- risk evaluation.

Revolutionizing the processes specific to the internal audit function can be achieved through the adoption of fundamental instruments, among which:

- tools for collaboration;
- data retrieval tools;
- analytical data and monitoring tools;
- predictive and automated tools.¹⁸

These studies (PWC, Deloitte, 2017) highlight the need to focus internal auditors' attention on IT risks, including:

- information security, mobile device applications, social media;
- cloud computing;
- IT tools used in the audit activity, such as data analysis or CAAT - Computer

Assisted Audit Techniques¹⁹;

- robotizing the process of automation and cognitive intelligence;
- digital risk audit;
- risks presented by collaboration with external partners.²⁰

Increasing the prestige of the internal audit function is based on an entity support that can be achieved by delivering strategic, quality and dynamic risk-oriented plans, aligning the audit function to business objectives, providing quality assurance, obtaining continuous feedback and continuous positioning to the environment in which the business operates.

In order to have the expected impact, at present, internal auditors should anticipate effectively the risks associated with technology infusion, changes in legislation, or due to changes

¹⁶ PriceWaterhouseCoopers, „2017 State of the Internal Audit Profession Study”, 2017 - <https://www.pwc.ru>

¹⁷ Chambers Richard, "Internal Auditing: Poised to the Future: Global Outlook, 2017, The Institute of Internal Auditors, <https://www.iaa.nl>

¹⁸ PriceWaterhouseCoopers, „2018 State of the Internal Audit Profession Study”, 2018 - <https://www.pwc.com>

¹⁹ PriceWaterhouseCoopers, „2018 State of the Internal Audit Profession Study”, 2018 - <https://www.pwc.com>

²⁰ Deloitte, Internal audit future trends, 2018 - <https://www2.deloitte.com>

in business or strategy, and meet stakeholder expectations. In this respect, the Classification by PriceWaterhouseCooper (2017)²¹, based on the ability to bring added value in the activity of companies, in internal audit functions, is revealed:

- evolvers, data of activities that lead to the absorption of technology and the absorption of talented auditors, their training and preparation;
- followers, activity data that succeed in attracting and adopting to a lesser extent innovations and highly skilled personnel;
- Observers, data of activities that have the worst results.²²

Conclusions

The business environment is benefiting in the present time of a continuous evolution, the economic sector being directly affected by technological progress, absorbing innovations in the activity of companies, producing competitive advantages, but also exposing the company to the associated risks. We conclude that both stakeholders and executive management expect the audit function to provide early and safe advice against the risk factors such as: Corporate Social Responsibility; Speed of technological development; Effective use of skills; Behavioral change of customers; cyber-attacks and the most important emergence of new regulations.

We also note that, in line with the increased stakeholder expectations, the internal audit function is forced to a transition and development stage redefining its capabilities and competence.

In our opinion, in order to benefit from an agile audit function, the joint effort of the members of the internal audit team is required, as well as by supporting the entity's management by providing the audit department with the necessary funds to acquire the innovative software tools needed to carry out the activity, auditors with IT experience and training, as well as continuous training. The communication between the management of the Internal Audit function and the management of the company should ensure the flow of information necessary to realign the internal audit function to the objectives of the organization as well as to the changing expectations of the stakeholders involved.

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²¹ PriceWaterhouseCoopers, „2017 State of the Internal Audit Profession Study”, 2017 - <https://www.pwc.ru>

²² PriceWaterhouseCoopers, „2018 State of the Internal Audit Profession Study”, 2018 - <https://www.pwc.com>

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