The Global Profession of Internal Auditing

Dallas Chapter of the IIA
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Patty Miller
Chairman of the Board - IIA
Partner, Deloitte & Touche LLP
pkmiller@deloitte.com
510-287-2805
Topics

• The Global IIA
• The IIA’s New Strategic Plan
• Current Environment and Emerging Trends
• Closing Thoughts
## The IIA

<table>
<thead>
<tr>
<th>Region</th>
<th>Members</th>
<th>Institutes/Chapters</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global</td>
<td>159,500</td>
<td>251</td>
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<tr>
<td>Asia Pacific</td>
<td>31,300</td>
<td>20</td>
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<tr>
<td>Europe</td>
<td>34,250</td>
<td>32</td>
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<tr>
<td>Middle East</td>
<td>2,450</td>
<td>6</td>
</tr>
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<td>Africa</td>
<td>11,100</td>
<td>20</td>
</tr>
<tr>
<td>Latin America</td>
<td>9,550</td>
<td>19</td>
</tr>
<tr>
<td>North America</td>
<td>70,850</td>
<td>154</td>
</tr>
</tbody>
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Membership has increased over 100% since 2000!

Approximately 75,000 Certified Internal Auditors
New Strategic Plan for the IIA
IIA Strategic Planning – 2008-2013

Preferred Future Milestones

By 2013:

1. Internal Auditing is universally recognized as a profession

To Accomplish this The IIA:

2. Defines the principles of the profession and assures that the principles are available seamlessly worldwide
3. Assures adherence to professional requirements
4. Is the preferred provider in the research, development and dissemination of knowledge to advance the profession
5. Is seen by its members and operates as one global organization
Near Term SP Initiatives

- **2008**
  - Global Governance
  - Value Proposition & Professionalism
  - IAEP
  - Advocacy
  - IPPF
  - Global Research Process
  - Emerging Issues

- **2009**
  - Global Committee Participation
  - Revisit Principles of Profession
  - Competency Model

- **2010**
  - Knowledge Management

Proposed Owners:
- ARC
- IIARF
- Professional Practices Council
- Advocacy
- NAB

New Initiative

Existing Initiative

Proposed Owner
Theme for 2009

Internal Auditing....
Recognized.
Trusted.
Valued.
Recognition

- Our profession, our organization, each professional
  - Roles understood
  - Expectation of due care, objectivity, fair and accurate reports
  - Appreciation of professional behaviors and attitudes
  - High integrity and ethics

Recognized.
Trust

- High integrity and ethics
- Respect those audited
- Understand the business; management’s strategies and objectives
- Focus on the right areas and the right risks
- Provide practical, relevant and persuasive recommendations
Value

• Contributions to your organization and assurance to stakeholders
  – ‘Seat at the table’
  – Proactive catalyst for positive change
  – An objective and informed reporter on business risk, control and governance
  – Trusted advisor on risk, control and governance issues
  – Balance of consultative and assurance services
  – Help protect AND grow the business
Current Environment and Emerging Trends
Corporate Governance Failures - Then

Andrew Fastow
Enron
*pleaded guilty to fraud and conspiracy*

Scott Sullivan
Worldcom
*pleaded guilty to fraud*

Martha Stewart
Omnimedia
*convicted of lying, conspiracy, and obstruction of justice*
Corporate Governance Failures - Now

- Bear Sterns (US) – Trading practices
- Societe Generale (Europe) – Management competence; trader fraud
- Citigroup – Lending practices
- UBS (Europe) – Tax advisory services
- Fisher Price (US/China) – Lead paint in toys
- GlaxoSmithKline (US) – Paxil side effects
- Oji Paper and Nippon Paper (Japan) – False claims on recycled paper content
- IndyMac Bank (US) – Lending practices
- Samsung (Korea) – Tax evasion
- Satyam (India) – Fraudulent financial reporting
Definition of Internal Audit (IA)

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”*

* The International Standards for the Professional Practice of Internal Auditing promulgated by the Institute of Internal Auditors

Did Internal Audit fail in organizations with governance failures?

What can Internal Audit learn from these governance failures?
Responsibilities TODAY

Are each of us ....

- Hiring the **best and brightest**
  - and providing a learning and career pathway
- Seeking to understand **stakeholder** expectations and evaluating effectiveness in meeting those expectations
- Embracing and executing a **risk-based approach** with a balanced plan
- Providing **leadership on issues of corporate governance**, fraud, risk management, internal control and financial reporting
- Willing to **challenge status quo**, and operating as change agents
- Staying informed on **emerging trends in our profession**?
- Keeping **abreast of new developments** in our businesses, industries and regions, considering risks and taking a proactive role:
  - Economic downturn
  - Currency destabilization
  - Extended enterprise
  - IFRS adoption worldwide
  - Corporate responsibility and sustainability
  - Etc.
New IA Risk Assessment Approach

The Fallibility of Probability

- Little or no predictive value
- Major value losses are often high impact / low likelihood
  
  9/11 1997 Asian Financial crisis
  Dot com bubble Financial scandals
  Oil / commodity price spikes Natural disasters
  Danish cartoons ???

- Biases management to direct resources to high impact / high likelihood events
- Typically focuses on single events rather than a series of events or domino effects
- Audit activities are often misdirected to the “red zone”
New IA Risk Assessment Approach

**M = High Impact/High Vulnerability**
- Provide assistance in design of controls where impact and vulnerability are high
- Track progress on remediation plans

**A = High Impact/Low Vulnerability**
- Obtain assurance confidence in preparedness is justified

**R = Low Impact/Low Vulnerability**
- Obtain assurance on effectiveness
- Identify ways to improve efficiency

**CI = Low Impact/High Vulnerability**
- Assess cumulative impacts and frequency
Economic Downturn/Financial Crisis

- **Illustrative risks:**
  - Increased incentives for financial fraud
  - Disgruntled ex-employees who sabotage, pilfer assets
  - Short term cost-cutting with destructive operational or control implications
  - Reliance on a third party supplier, distributor, or joint venture partner with financial difficulties; what contingency plan is in place
  - Potential liquidity issue due to the tightening of credit

**Internal Audit Role**

*Help management identify risks, design risk management strategies, assess and monitor effectiveness of applicable controls*
Potential Internal Audit Involvement

- Participate in cross functional ‘what if’ discussions to reconsider risks and identify action plans
- Help design risk management / monitoring processes (i.e., controls!) to address risks
- Redirect audit resources to re-assessed highest risk areas
  - Risk assessment and risk management/monitoring practices
  - Complex decision models – such as risk monitoring and valuation
  - Physical and system security in the aftermath of layoffs
  - Operational reviews in processes that MUST continue to work
  - Investment diversification policy
  - Consumer loan, credit policy
  - Governance roles, responsibilities, practices
    - Financial and nonfinancial metrics used to measure performance
  - Extended enterprise reviews
## Extended Business Relationships

<table>
<thead>
<tr>
<th>Supply-Side Partners</th>
<th>Demand-Side Partners</th>
<th>Licensees</th>
<th>Infrastructure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vendors</td>
<td>Franchisees</td>
<td>Co-brand partners</td>
<td>IT outsourcing</td>
</tr>
<tr>
<td>Suppliers</td>
<td>Distributors</td>
<td>Joint developers</td>
<td>HR services</td>
</tr>
<tr>
<td>Manufacturers</td>
<td>Advertising agencies</td>
<td>Patent licensees</td>
<td>Travel agencies</td>
</tr>
<tr>
<td>Replicators</td>
<td>Retailers</td>
<td>OEMs</td>
<td>Legal services</td>
</tr>
<tr>
<td>Integrators</td>
<td>Warranty providers</td>
<td></td>
<td>Transaction processing</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Call centers</td>
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</tbody>
</table>

- IT outsourcing
- HR services
- Travel agencies
- Legal services
- Transaction processing
- Call centers
Internal Audit: Turn Trust into Value

**Identify Relationships**
- Identify all contractual relationships

**Identify Relationship Objectives**
- Identify the objectives of key relationships

**Assess Risk**
- Determine the key control points and dependencies of relationships
- Develop processes to identify risks
- Target relationships that pose significant risks
- Identify the risk of not achieving key objectives

**Evaluate Compliance**
- Determine key controls/processes at external business partners that impact your business
- Evaluate data/records against contract terms
- Identify process improvement opportunities

**Mitigate Risk**
- Improve policies and procedures
- Improve relationships and performance
- Enhance compliance
- Incorporate learnings
- Train contract writers & negotiators
- Avoid relationships that pose greater than normal risk

Inform the partner selection and contracting process
## IFRS – Are You Informed?

### Illustrative Adoption Timeline

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
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<tbody>
<tr>
<td>2009 – 2011</td>
<td>Option to use IFRS</td>
</tr>
<tr>
<td></td>
<td>Last US GAAP Financial Statements</td>
</tr>
<tr>
<td>2012 – 2013</td>
<td>IFRS Opening Balance Sheet</td>
</tr>
<tr>
<td></td>
<td>First IFRS Financial Statements</td>
</tr>
<tr>
<td>2014</td>
<td>Mandatory Use of IFRS Begins</td>
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### Plan & Transition
- US companies launch **internal holistic assessments** and start mapping their paths to adoption
- SEC proposes IFRS road map
- Many US companies have the option to use IFRS
- Early adopters and large complex companies shift into **high gear**

### Convert & Compare
- Comparison of **US GAAP and IFRS** Financial Statements
- **Process and systems** changes are taking place as a result of IFRS transition
- Companies are executing on **communication** and **training** plans

### Sustain & Improve
- All large accelerated filers are reporting under IFRS
- Continued focus on efficiencies and benefits to drive sustainability
IFRS – Have You Started?

Illustrative Adoption Strategy

- Alignment with other initiatives and training for appropriate personnel
- Rationalization and standardization of statutory reporting

2009
- Awareness
- Assessment
- Planning
- Initial Training
- Roadmap

2009-2010
- Targeted Statutory Implementation
- System & Process redesign

2010-2011
- Statutory Implementation
- Select Exemptions
- Prepare IFRS Opening BS
- “Dry Runs”

2012-2013
- U.S. GAAP & IFRS opening balance
- Investor Communications
- Audit Procedures
- Change Standards

2014
- Transition to IFRS
- Investor Communications

Reporting Date

Transition Date
Corporate Social Responsibility

• Significant and growing worldwide trend and stakeholder expectation
• Both a threat and an opportunity
  – Can you meet the expanding expectations?
  – Have you anticipated your competitors’ actions?
  – Have you anticipated your regulators’ actions?
  – Can you leverage the trend to an economic and societal advantage?
• Improve operations, attract talent, promote positive relations, enhance transparency and accountability, streamline regulatory compliance, heighten competitiveness, draw investors
Corporate Social Responsibility

• Consider .... Is your organization ready?
  – To pay for what was formerly free?
  – To take advantage of shifting demographics?
  – To respond to activists?
  – To anticipate your stakeholder’s changing needs and expectations?

• IA as catalyst
  – Understand your organization’s approach and attitude
  – Educate on breadth of risk and opportunity
  – Assist in collecting data and benchmarking
  – Assist in planning approach with appropriate measurements to monitor progress and risk management
  – Ultimately, assist in designing new processes and supporting controls
Closing Thoughts
Final Thoughts

• Risks facing our organizations are unprecedented and stakeholders’ expectations continue to increase
• Internal audit profession has an opportunity to step forward
• Individual practitioners and organizations must ‘raise the bar’ to most effectively represent and advocate for our profession
• Our new challenges will bring new opportunities for our organizations, internal auditing as a profession, and each of us as professionals
My Challenge

Challenge yourself
Challenge your team
Challenge and support the IIA

to be not just recognized
not just trusted
but a valued member of the organization, our profession, and our Institute