



# THE TRANSFORMATION OF INTERNAL AUDIT

a whitepaper by **Grant Morgan**

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## **THE CATALYST MOMENT**

For many years, Internal Audit thought leadership has focused on the need for the profession to change, however, the reality is that very little transformation has taken place. Neither the methodologies and approaches, nor the tools and technologies Internal Audit functions utilise have had a considerable impact on Internal Audit processes. The ways of the profession are deeply entrenched and have lacked the innovation and progress to enable Internal Audit to keep pace with the change of business and business priorities.

There is no doubt that the Covid-19 pandemic and associated lockdowns, advances in cloud-based and other business technologies, and the broad adoption of flexible work arrangements have had a considerable impact on the business landscape. Indeed, these catalysts have triggered a complete metamorphosis. The world of business has undergone permanent changes, and will never again look as it did pre-Covid.

## **THE REQUIRED RESPONSE**

With all this in mind, how has the Internal Audit profession been impacted, and how is it responding? This new business landscape represents new opportunities as well as new risks for the profession.

Internal Audit functions now have the opportunity to grow, to change, to transform. In fact, it is essential that they do so in order to remain relevant as third line of defence and trusted advisor to business. Without a transformation, Internal Audit functions will become increasingly irrelevant to the businesses they serve, losing their voice at the table. They may even be replaced by Internal Audit offerings provided by other entities that have transformed, or appear to have done so.

We believe that just as the world of business has undergone a metamorphosis, so the Internal Audit profession must change in order to remain as relevant as it has been historically. Only by transforming will Internal Audit functions be able to appropriately support businesses and entrench their trusted advisor status within the organisations they serve.

## **WHAT DOES THE BUSINESS LANDSCAPE LOOK LIKE TODAY?**

The world of business is not what it used to be. Technology has advanced to such an extent that IT environments are now more pervasive in many more organisations than before. Without connectivity, apps or devices, many businesses, from small to medium enterprises to large corporations and multinational companies, would be unable to operate. Technology is integrating transactional processing between businesses throughout the supply chain, not just in

a local environment but globally. Technology has also dramatically impacted the way in which people interact, communicate and work together.

Considering the rate of change, the benefits technological advances have delivered for businesses, and the associated cost and time savings, this scenario is unlikely to reverse. Rather, it will develop further, becoming increasingly integrated, automated and mature.

Covid, lockdowns, cloud-based technologies and flexible work arrangements have all played a part in facilitating this new business landscape. Together, this unique combination of factors has brought about a fundamental shift in business systems and work arrangements that took place almost overnight.

## **Technology**

Today, IT is pervasive no matter the size of the organisation. Transaction flows through business systems are largely automated and digital, or at least capable of being digitised through Optical Character Recognition (OCR) functionality. In some cases, transactions between suppliers/ customers are even processed directly between the entities' accounting systems, with no human interaction whatsoever.

This has dramatically enhanced the completeness, accuracy, and speed of transaction processing, saving vast amounts of time and expense.

In addition, businesses can interact with markets anywhere on the globe in a way that was previously unimaginable, further increasing the number and complexity of transactions being processed across the business.

## **Process**

Automation of processes is driving substantial improvements in the efficiency and control throughout these business processes. Bank accounts now integrate directly with accounting systems for bank transaction recording. Customers interacting through the business' online portals are capturing the sales order information that is used to create the invoice (picking slips, GRN etc.) automatically through the process of performing the service or delivery. Warehouse management, picking and packing of goods ordered are being performed by sophisticated sets of robots and algorithms. The physical delivery of goods is even confirmed through the use of geolocation data when customers receive goods. Almost every area of business you can think of is being impacted through some form of automation.

With the increase in Electronic Data Interchange (EDI), manual input is quickly becoming an exception when processing transactions. This is true even of conversions of manual documentation into digital transactions using OCR functionality, which is becoming more and

more accurate through machine learning algorithms. At some point in the future, manual input and processing may disappear completely.

## Change in nature and complexity of risk

With the rise of automation, automated processes and automated controls, which offer huge benefits to business, the nature and complexity of risks has also evolved. For example, over the past 5 years the majority of boards have come to consider cyber risk as a serious business risk. Many professionals are now employed in new cyber security roles that never existed previously. Connected supply chains have recently been tested by the global pandemic, wars and shipping channels being blocked, with harbours desperately trying to clear the backlog of cargo ships. This has dramatically impacted inventory levels globally, leaving many businesses unable to sell simply due to lack of available stock, and causing significant business interruption.

## THE MOUNTING CHALLENGES ON INTERNAL AUDIT

Internal Audit has various challenges in transforming the function. These include:

- **Strategy:** Resistance to change has been a key limiting factor to the Internal Audit industry
- **Access to appropriate data:** Internal Audit teams frequently have difficulties in accessing the data required to conduct their work
- **Skills & knowledge:** Internal Audit functions require specialist skills that are not widely available and carry a high cost
- **Capacity:** executing swift responses to problems that are large in scope is a challenge for many Internal Audit teams
- **Insufficient budget:** Internal Audit teams are expected to do more with less, and must often operate on limited budgets
- **Leveraging analytics and advances in technology:** effective integration of analytics into Internal Audit processes is difficult and sometimes requires major upfront investment
- **Data privacy:** Legislation has added complexity to Internal Audit processes and increased the costs involved

Analytics has been a key focus area of Internal Audit for many years, but this has not brought about a fundamental change in the way the overall process is conducted. It is often seen as just a bolt-on to the existing approaches and methodologies.

While many organisations include core analytics, data skills and toolsets, the outcomes of analytics testing are not optimally integrated into their Internal Audit processes. Internal Audit teams that leverage traditional analytics are reliant on IT support and often must copy or move data from one location to another before they are able to use it. They must also deal with the access control, security and privacy risks associated with storing of data themselves.

This is not an efficient approach. The steady rise in catastrophic events around the world has increased the frequency and intensity of risk that businesses face. This, along with other factors, has added complexity to Internal Audit functions, and exposed the limitations of the current approach. It's evident that just as the business landscape has undergone a metamorphosis, the time has come for Internal Audit to execute a complete transformation of its own.

## TRANSFORMING INTERNAL AUDIT

So how does the Internal Audit profession respond? What is clear is that a radical response is required, a response that keeps pace with, or catches up to, the transformation of business and the risk business faces. So where do we look, and how do we start to move from being a caterpillar to becoming a butterfly? Current audit technologies, processes and methodologies, and development of auditors do not deliver on this requirement.

So where does one start? We should go back to the basics and reassess the building blocks of the Internal Audit function. Things that need to be considered:

- **Strategy** – how do we become a data-led and data-driven function?
- **Technology** – how has audit technology transformed to support this new Internal Audit function?
- **People** – how do our people need to grow, change, and/or be reskilled?
- **Process** – how can we automate our audit processes for optimal efficiency?
- **Budgets and allocations** – how do our budgets need to be reprioritised to deliver on the new strategy?

### Strategy

From a strategic perspective, the three lines of defence model remains intact in terms of the role that Internal Audit plays. Internal Audit is a specialist function in the world of process, risk and controls, and in addition to assurance, can provide significant consulting value to businesses.

In this digital world, data is king. How can Internal Audit become a truly data-driven, and more importantly, data-led function that provides the assurance and value-add to the business? It stands to reason that in order to transform its processes and assurance effectiveness, while considering the changing nature of risks to the business, Internal Audit must take advantage of technological advances and automation - not simply digitising old methodologies, but rather transforming them. In addition, the roles and responsibilities of audit staff must be reshaped, and staff must be trained and upskilled to be able to perform these new roles.

There is much debate over the topics of continuous control auditing and continuous control monitoring. Who is responsible for this? Is it a function of management or a function of Internal

Audit? Is it appropriate that third line of defence performs this? What is important is that technological improvements have enabled the performance of control and/or the review of controls to be completed in near real time. This provides either management with the opportunity to intervene, detect and correct, or Internal Audit with the ability to report and quickly escalate important matters to management. Certainly, Internal Audit could play a key role in establishing this activity and subsequently transferring it to management, however, where responsibility for this type of activity ultimately resides may largely be determined on a case-by-case or company-by-company basis.

Being a data-driven and data-led function means that Internal Audit has the ability to:

- understand the data landscape,
- connect to business systems and data environments,
- analyse and assess the risk as identified through the data, utilising the entire dataset and not just samples,
- complete significant portions of this risk analysis during the planning phase of the audit,
- perform audit procedures on the entire dataset that demonstrate the lineage between the input data and how it was transformed to get to the results, and ultimately,
- perform additional audit procedures on exceptions identified,
- quantify audit outcomes,
- transform this into valuable audit evidence and business insights, and
- perform all this in near real time.

## **Technology**

Internal Audit is often at the tail end when it comes to access to business systems and data. Traditional thinking gives Internal Audit access to data extracts or a standalone data warehouse at best and does not allow access to core systems. This presents the audit process with additional challenges and compromises the reliability of audit results as data may be manipulated intentionally or in error during this transfer process.

### ***Connect not Collect***

Controlled and secure access to the relevant systems and data is essential. Implementing the audit solutions that can take advantage of this is critical. This is a fundamental building block to transform the function and represents a complete move away from data extracts and standalone data warehouses.

Strategically, this will have an appreciable impact on the responsiveness and effectiveness of the transformed Internal Audit function. Today, technology exists that allows Internal Audit to connect directly to business systems or operational data warehouses without impacting the performance or security of those systems. These technology solutions leverage caching to facilitate a near real-time view of the data, with no disruption to business activities.

Internal Audit can now perform audit procedures at source, rather than on extracted/second-hand data provided by IT. This significantly enhances the reliability of the audit results achieved, without taking on the risks and responsibilities of securing and managing the auditee's data.

### ***Speed to Value***

Being able to quickly test and build new audit procedures in response to new scope or risks will considerably improve the value, both in time and cost savings, to produce audit assessment, as well as the quality of the outputs produced. This further enhances Internal Audit's reputation of being able to provide quality and timely outputs for both assurance and consulting engagements.

### ***Advanced Automation***

Scheduling of audit procedures and alerting the audit team to exceptions on a predetermined timeline will assist in the focusing of audit efforts on the most important issues and exceptions.

### **Process**

Identifying and implementing opportunities to transform Internal Audit processes, including approach and methodology, is possible and will be critical moving forward. Some considerations include:

- interaction and communication with own staff and the business
- implementing Agile methodology at coverage plan level as well as within individual audit engagements
- transforming methodologies, moving from sample-based auditing to the evaluation of full transaction populations, identification and follow-up of exceptions and quantification of exceptions
- real-time responsive to risk and changing business conditions, even if this means replanning, rescheduling, or cancelling engagements
- team and individual performance management and promotion
- training activities of audit team being facilitated by AI digital twins

### **People**

There is no question that Internal Auditors will require new and more advanced skills, as a result of basic audit procedures and conclusions becoming automatable. Many Internal Audit functions should also consider the diversity of skills they need to perform their work with professional competence and due care, and offer increased training with respect to:

- skills relevant for the audit technologies implemented – low-code technologies enable auditors to negotiate this hurdle without having to become data scientists in the process
- evaluation and judgement of exceptions identified

- empathy and ethics
- interpersonal and communication skills

## **Budgets and Allocation**

Many Internal Audit functions are under pressure to do more with less. A change is needed. By redirecting budgets and resources into the correct audit and supporting technologies, not only will functions be able to improve the reliability, timing, volume, and quality of the assurance provided, they will also be able to offer staff more engaging, interesting, important, and enjoyable work.

## **Next Steps**

It's time to perform some critical self-review, time to consider:

- **Strategy**
  - Does your strategy provide a platform for your function to transform?
  - How does your strategy need to change to transform your function?
  - How can a data-driven and data-led approach change your methodologies and be more effective?
- **Technology**
  - What technologies are you currently using?
  - Do these technologies support the strategy of a data-driven and data-led function?
- **Process**
  - What processes can you automate for your function and create time and cost efficiencies that can be redeployed?
- **People**
  - What skills and expertise do you require to deliver on your strategy?
  - What is the gap between this and your existing staff?
  - What additional training requirements and development is needed for your staff?
- **Budget**
  - How can you most effectively use the budget allocated for Internal Audit?

This transformation may not be easy on your own. Are you ready for a change, looking for a guide, or someone to open the world of possibilities for Internal Audit for your organisation? Reach out and contact us to start the conversation.

**Grant Morgan:**

Grant Morgan has over 24 years' experience working across the domains of internal and external audit, risk management, compliance and governance, as well as financial management. During this time, he has fulfilled corporate and consulting roles across multiple industries for a diverse range of clients. His previous key roles include Director of Audit Services at Naspers, and Senior Manager at Deloitte Risk Advisory.

Grant is passionate about making a positive impact and adding value to his clients. His current role at Intenda includes the development of technology solutions that are designed to transform the audit and GRC industries into data-led functions.

**Intenda:**

Intenda is a multinational software company with offices in the UK, EU, USA and South Africa. Its flagship product is the big data management platform, Fraxses. The company also offers consulting services and specialises in platform technology and bespoke product development. Intenda's customer base includes clients across multiple sectors, including Audit & Assurance (Big 4), Banking, Healthcare, Insurance, Logistics, Petrochemical, Professional Services, Retail, Security and Government.

Fraxses is utilised by customers in 14 countries around the world. It is recognised as one of the most powerful and versatile data management solutions on the market, and has a proven track record in enabling businesses to elevate their performance to new levels. As a low-code/no-code platform that advances a distributed architecture and serves data to users direct from the source, Fraxses addresses the challenges Internal Audit functions face and presents a compelling solution to support the transformation of the profession. To find out more about Fraxses, email [info@intenda.tech](mailto:info@intenda.tech) or visit [www.intenda.tech](http://www.intenda.tech).