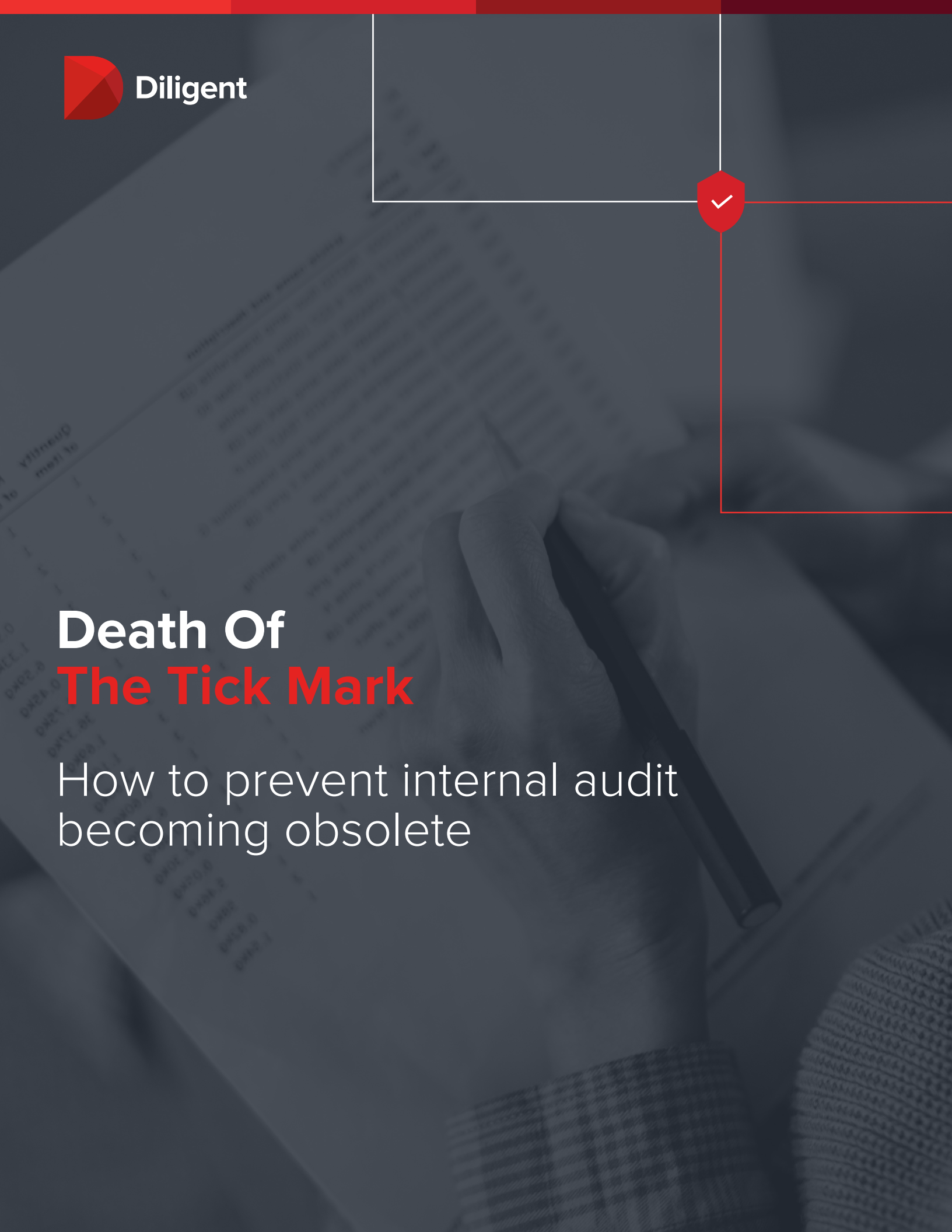


Diligent

Death Of
The Tick Mark

How to prevent internal audit becoming obsolete

Contents

It Started With A Winnebago

Well, kind of ...

Early in my career, I was in the Risk Advisory Services practice of EY. One of my biggest clients was a chain of midwestern US hospitals, and every year we developed an annual audit plan that we thought would deliver real value and important assurance for management and the board.

But when we presented our plan to the CFO, including the risk areas and which hospitals we'd cover in our reviews, he barely paid attention.

As we left the meeting, he stopped me in the doorway and joked: "You know how we could really save? Instead of flying you auditors all over the place to stay in overpriced hotels, maybe we could rent you guys a Winnebago and you could drive the audit RV across the country!"

I realized that, after all the hard work and time we'd invested, our presentation hadn't resonated at all. The CFO wasn't interested. He was more concerned about how to minimize expenses in this "cost-center-we-have-to-tolerate" function of internal audit and compliance.

Ouch! This is exactly why auditors need to change the perspective on auditing and emphasize the value they deliver.

In this eBook, I'll share my views on how the internal audit profession could be heading for extinction—and how auditors can become more proactively valuable to their organizations. I'll also outline some inspiring stories from Diligent's global customer base, and examine what separates forward-thinking teams from audit groups that remain focused on the tick mark.

Diligent

Tough Questions I Had To Ask

“Traditional auditors are barreling towards obsolescence and most don’t even realize it.”

Those were the words from an analyst at one of the world’s leading enterprise technology analysis firms. Her argument was twofold:

- Auditors are rarely focused on the problems that really matter
- Auditors are being systematically replaced by automation as big-data technologies continue to advance

It’s an aggressive stance, but it was also a wake-up call that helped me think about how I’m supporting the audit profession—and how I can help make sure it doesn’t become obsolete.

> My epiphany: eradicating the tick mark, and what it symbolizes, is our first step in making serious progress toward industry-wide transformation.

As I began to think about why we need to change our perspective on auditing, and how to drive real and quantifiable value, I wondered about two things:

1. Do we need to do what we’ve always done?

During my audit career, I spent countless hours creating detailed workpapers with vast documentation and endless tick marks. I also spent hundreds of hours writing and editing traditional audit reports.

But nobody cares about your detailed working papers— if they did, then why are auditors the only ones creating them? Why are we writing reports, when it’s metrics that management actually cares about?

2. Have we truly embraced the possibilities that technology now offers?

Are we approaching day-to-day activities in the most impactful, repeatable and efficient ways possible?

I would argue that data analytics is, by far, the most underused technology in audit—but I’m also thinking about the role of mobile and social platforms in transforming the way we work.

The Origin Of The Tick Mark

Google “audit tick marks.” Most results (and even the Auditing for Dummies book) are related to financial statement auditing—it’s no wonder we have trouble adding the deep value that stakeholders expect!

Let’s take a moment to review the official definition of internal audit from The Institute of Internal Auditors:

“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.”

This is important work and it impacts an organization’s entire operations. So why is much of our time, as a profession, spent in granular, low-impact financial areas? I’d argue that this level of granularity (and the ridiculous tick-marking and documenting that goes with it) isn’t required by our professional standards, as long as our conclusions are supported.

Much like stenography stepped aside with the arrival of the personal computer, it’s time for old-fashioned workpapers and tick marks to get out of the way of internal audit’s new future: a future that is heavily centered on automation.

Diligent

AI & Automation: Changing Audit For The Better

Emerging technologies are having an enormous and very positive impact on internal audit.

A World Economic Forum report[1] examined the future impacts of emerging technologies—such as artificial intelligence (AI), robotic process automation and machine learning—on a range of different careers. The report identifies internal audit as a profession being heavily impacted by these technologies.

But it's not the doomsday situation that's been widely portrayed. As reported by Gartner,[2] robots and automation bring many opportunities for the audit profession. To stay relevant, internal audit will have to adapt and embrace these technologies and opportunities. Basically, it comes down to this: you're either the one creating automation, or you're the one being automated.

There's not an audit team on earth that has an adequate number of people to look at all of the key aspects of risk using a manual approach—and there never will be. It's critical that we extend our reach through data and automation. Data analysis allows a single auditor to analyze billions of bits of information to gain real insights. Data automation puts the lowvalue but must-watch areas on autopilot so we can refocus our time and energy where it really matters. However, even as automation grows and is adopted in many organizations, some auditors say they're frustrated with the technology. But that's because they're approaching it differently.

An auditor who sits back and just watches new tech roll in and waits for instruction is very different from an auditor who takes an active role in developing the technology within an organization. Which one would you want on your team?

[1] **World Economic Forum,** 2018, The Future of Jobs Report
[2] **Gartner,** 2017, Gartner says by 2020, artificial intelligence will create more jobs than it eliminates

Increase Internal Audit Value...

...by spending time on what really matters.

Internal audit can use data and automation to deliver a perspective that's much broader and more objective than what other organizational areas can provide.

Here at Diligent, we choose which areas we want to spend time on, based on what our data tells us. We developed a research project to examine the top risk factors disclosed in Form 10-K reports from the Fortune 500.

We wanted to answer the question "What does management disclose to the investing public as the most impactful, most relevant risks within their organizations?"

Not one of the organizations we researched referenced the inability to accurately report financial results.

In contrast, we see the following top three risk disclosures in nearly all Form 10-K reports:

- The ability to attract and/or retain top talent
- Pressure from the competition
- Product quality and customer satisfaction

I wondered: "How many audits did I conduct in any of those three areas, given that they're the key risk areas for the world's largest organizations?"

The answer is a gut-wrenching zero.

Vanderbilt University

How real risk assurance made a big difference.

A few years ago, I heard about a physician at Vanderbilt University Medical Center whose wife was a patient. During his wife's time in hospital, the physician noticed that many employees caring for her weren't consistently washing their hands. He observed 60 instances where a lack of hand-washing could have spread communicable diseases and threatened the quality of patient care.

He took the problem back to the staff and worked with many different stakeholders to explore how handwashing could become an area of compliance. The team developed a way to observe, monitor and capture handwashing data. They learned that staff were only following the medical policy 58% of the time. So they created training and communication initiatives, and developed accountability assessments for individual departments.

Three years after this program began, hand-washing compliance at Vanderbilt increased from 58% to 97%. That's a fantastic improvement, but the outcomes were even more impressive.

Hospital-contracted diseases such as urinary tract infections from catheters and pneumonia acquired from ventilators had dropped by 33% and 61%, respectively. In this case, risk assurance had a material positive impact on the organization.

I love this Vanderbilt story, because it opens a new world of thinking (and opportunity) for internal audit—it challenges us to find and target the real risk areas.

Real-Life Examples

Here are some inspiring stories from the worldwide Diligent customer base. They show us the incredible impacts that real risk assurance can have.

MITIGATING BANK ROBBERY RISK

A major bank examined their data for indicators of past and potential branch robberies. They ran analytics to determine where future robberies were likely to occur, and then changed their policies to reduce those risks. As a result, they've built an additional risk management program into any branches that are statistically more likely to experience robberies.

STOPPING CHILD LABOR & AVOIDING CONFLICT MINERALS

Another customer used supply chain data to remove vendors who were engaging subvendors who were using child labor. Not only does this work have great social impact, but it also eliminates the organizational risk of a child labor disclosure in the supply chain. They also found indicators in their supply chain of raw materials coming from war-torn regions in Africa. Knowing this, they were able to remove the risk of acquiring conflict minerals that might be supporting war and atrocity.

FREEZING TERRORIST FUNDING

In the financial sector, our customers have identified suspicious patterns and behaviors. They were then able to freeze funds that would have supported terrorist sympathizers, drug dealers and other organized crime.

ASSESSING ARMED FORCES DEPLOYMENT READINESS

A national government defense department's internal audit team considered the process for determining operational readiness for soldier deployment. The audit analyzed key data on equipment condition, spare parts inventories, training statistics and other points to build a risk profile that measures whether teams are truly ready for deployment.

Diligent

In The Past Year...

...have you done an audit that mattered?

I love this analogy from a marine biologist: "Why spend precious limited time counting how many individual fish have expired, when you can focus on finding out what's killing the fish in the first place?"

Progressive auditors use data to look forward.

The next generation of audit techniques and technologies that drive real value include:

- Data analytics
- Mobile devices as core audit tools
- Continuous auditing/monitoring
- Real time, automated, assurance-related reporting and dashboards

Why would we continue to pick samples of 25 and make 10 tick marks at a time when we can do billions all at once?

That's the power of technology and automation!

DATA PAYS DIVIDENDS (DIRECTLY INTO YOUR BANK ACCOUNT)

If nothing else motivates you to think about broad data applications, consider the salary advantages. According to a major US recruiter, an analytics expert or data scientist commands almost 50% more pay than an auditor with average experience.

The same patterns apply on a leadership level. If you compare your typical audit leader salary to those who lead teams of analytics and data science experts, the pay difference has completely outpaced traditional audit—a clear referendum from executive management on the value of those skill sets.

Diligent

How We Use Data For Business Impact...

...and to get a seat at the executive table.

At Diligent, our CEO is consistently surprised by the chasm between how the world views CEOs (and the C-suite in general) and how the world views audit and risk professionals. Yet, both of those groups:

- Set objectives
- Identify what could go wrong
- Add controls
- Evaluate their effectiveness with data
- Change behaviors

Maintaining independent oversight doesn't mean that agendas shouldn't overlap. Both CEOs and risk professionals need to be pointed at the critical, strategic risks and opportunities.

SO WHAT WOULD HAPPEN IF WE APPLIED AN AUDIT & RISK APPROACH TO THE PROBLEMS OF A CEO?

To find the answers, we needed to go well beyond the basic financial analysis that would be done primarily with enterprise resource planning (ERP) system data. We used our HighBond platform to join our financial (ERP), customer relationship management (CRM) and product usage data for analysis.

This helped us get a full data picture that we could use to monitor our most important business conditions.

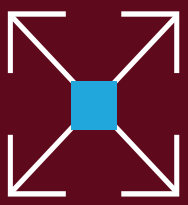
As an example of what we can do with data, let's consider the single most important thing at Diligent: that customers like and actually use our software. But how do we make sure it stays that way? By monitoring the data, of course!

We built data analytics that we call the Index of Customer Engagement, which audits and monitors customer experiences. The index was based on product usage, support levels, and training. We evaluated how deeply customers were engaging with our product and how much value they were getting.

We then correlated this engagement measurement to the contract value and other relevant financial measures for each customer to risk-score them. We added risk triggers to notify Diligent staff to get in touch immediately to make sure each customer receives full value from the software.

We developed an overall storyboard that explains customer engagement levels to executive management. That storyboard completely replaced the need for an audit report and helped us by being up to date—in real time—at all times.

We did all of this with the same technology that every HighBond user has at their fingertips.



Unleashing audit and risk management power on strategic corporate challenges has earned us a seat at the executive table. We're able to answer our CEO's questions that can only be answered with our data analysis. Fully automated key risk and performance metrics have also made it possible to shift Diligent's focus (and time) with the board to more strategic conversations.

Diligent

Where Is Audit Technology Headed?

And what does it mean for you?

At Diligent, we're creating a world where governance, risk and compliance (GRC) professionals are the most sought-after people in their organizations. We believe that audit technology is always evolving to help auditors better serve their organizations.

Here are some technology trends that are providing huge opportunities to increase audit value:

01 Standardized analytic apps. These are apps that are pre-configured with the knowledge to extract and analyze data for specific risks. They can easily be added if you have a standardized data source like a major ERP system in place.

02 More powerful analytics that can make use of less structured data, and dirtier data.

03 Textual analysis that uses linguistic sentiment knowledge to identify discussions of interest and find other meaning in large bodies of text.

04 Easier-to-implement statistical tools that make analytics more predictive and forward-looking.

Technology is getting increasingly sophisticated in these areas—but next-generation tools aren't the only things that can create billions of dollars in impact.

We need to create value by reimagining how we approach audit resource challenges.

REFRAMING THE PROBLEM

When I lived in New York City, I heard the story of an office building where tenants often complained about the slow elevator. Management decided to look into the problem and found that a full fix would cost over $10 million—and that wasn't in the budget. So, they hired an independent, objective professional who asked, "If I could solve the problem, would you pay 10% of that $10 million?" Management said yes.

A week later, the consultant brought in $10,000 worth of materials and quickly solved the problem. How? The consultant's team installed mirrors in the elevator. Soon, everyone was so busy straightening their ties and fixing their hair that they stopped worrying about the slow elevator ride.

That's a great example of reframing the problem.

Diligent

Think Differently

Reconsider your approach to workpapers, tick marks and audit findings.

I'll leave you with IIA president and CEO Richard Chambers' five imperatives for enhancing internal audit's perceived value (as outlined during an IIA General Audit Management Conference).

I thought these were well articulated and that they serve as great guidance in developing big-picture goals for your internal audit team:

01 Assess and address the gaps in stakeholder expectations of internal audit's focus and capabilities.

02 Develop and implement robust talent acquisition and knowledge-sharing.

03 Implement or enhance methodologies for assessing risk continuously.

04 Assume a leadership role in coordinating and aligning activities in the organization's second line of defense.

05 Find innovative ways to enhance audit efficiency.

Spending more time on those imperatives and less time on menial work like tick marks and detailed workpapers will help all of us change our profession for the better.

If I Could Do It All Again...

Thinking back to when the CFO could barely bring himself to pay attention to the audit plans we had spent so much time developing, I realize:

We were uninteresting because we only talked about audit stuff and failed to put it in the context of what the organization actually cared about.

If I could redo that day all over again, here's what I would do now:

01 Reposition the whole discussion to be based on what was laid out in the key corporate objectives.

02 Arrive equipped with a visual map of corporate strategy, mapped to major risk areas.

03 Back up every risk area with key risk indicators (KRIs) that the CFO didn't yet have. So, rather than saying, "We think IT outage might be a major risk," instead we could say, "We aggregated all system uptime logs and we batted 98.7% last year on clinical systems, but we see leading indicators that it could slide. Let's discuss our risk appetite."

04 Run through each KRI, and point out which areas are being audited, and which areas are currently exposed—so we could determine where to add coverage.

05 Rather than delivering a static, one-off annual audit report, I'd instead give them a real-time assurance dashboard to provide a single, interactive view of everything that needs attention throughout the year.

06 Finish the agenda with a conversation about how proactive they want to be—so we could go back to the office and build a notification system when thresholds are crossed.

The most important thing I learned—which underpins how I approach auditing and audit technology—is that continuing a traditional approach to auditing makes audit choices seem like an academic "we do this because we have to" activity, without a strong grounding in the reality of running an organization. Meaningful, impactful KRIs would have changed the conversation.

Diligent

Put Down The Pencil!

Stop detail-documenting your workpapers.

Pick up any kind of data analysis tool, and automate the higher-level review of whatever you were working on in that workpaper.

For example, are you reviewing payments? Skip the samples and analyze all payments to profile wasteful payments. Look at the full data population and create a meaningful statistic about what would indicate risk in those payments. Create a KRI to monitor going forward and drill down a level within the risky payments to profile further. If there isn't material value, put the pencil down and move on to a more risky business area.

Developing those risk profiles across multiple processes is far more meaningful than handing in a testing lead sheet of 50 payments and the associated invoices—full of tick marks—so you can find one or two payments where someone bypassed a control.

Are you afraid of what might happen without tick marks? I know, I know—it's the best guide to how you should be doing your job, right? The easy choice in getting guidance is to look at workpapers from the last time an audit was done. This is really a broken approach to auditing, as it only perpetuates outdated thinking.

If you missed a big risk because you only looked at 50 payments, how do you explain that? You're not doing your job. Sure, you may have been doing the job when everything was on paper. But today, every major enterprise is digital. Nor do electronic workpapers necessarily mean you're doing an audit for the digital age. The digital age means you've audited all the data. If there are 20 risks around payments and one is huge and the rest are small, it's better to know about the one risk for the process, versus each individual activity. It's not about whether one purchase order wasn't approved correctly—it's about the risky areas in the process.

For audit to cement its place as a strategic advisor to executive management, it must think bigger, and get on board with strategic goals. And the first powerful, game-changing step is bidding farewell to the tick mark—and the overly detailed, nit-picky approach to analyzing risk that it represents.

Ready to find out how Audit Management can help you add value, better manage your audit workflow & deliver strategic insights?

About The Author

Dan Zitting, Managing Director & CEO

Dan is responsible for Diligent's Galvanize brand, including the success of its customers, the evolution of its products and the overall growth of its business. He is also responsible for ensuring the successful integration of Galvanize and Diligent, creating incremental benefit for both the customers and employees of the combined organization. With more than 18 years' experience in the technology industry, Dan has garnered extensive knowledge in enterprise software, entrepreneurship and growth, and corporate risk management and compliance. Prior to Galvanize, Dan spent most of 10 years in professional services before founding SaaS platform and New York City tech startup Workpapers.com, the first enterprise cloud software for audit and compliance management. The company was later acquired by ACL (now Diligent), combining the power of cloud collaboration and big data analytics into one industry-leading platform and brand.

About Diligent Corporation

Diligent is the leading governance, risk and compliance (GRC) SaaS provider, serving more than one million users from over 25,000 organizations around the globe. Our modern GRC platform ensures boards, executives and other leaders have a holistic, integrated view of audit, risk, information security, ethics and compliance across the organization. Diligent brings technology, insights and confidence to leaders so they can build more effective, equitable and successful organizations.

For more information or to request a demo:

Email: info@diligent.com | Visit: diligent.com