COVID-19 AND INTERNAL AUDIT

Preparing for the New Normal in 2020 and Beyond

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About the Expert

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INTRODUCTION

How many of us could have foreseen the changes that have occurred since COVID-19 was first identified? Many, if not all, aspects of our lives have been impacted. As internal auditors, we think about the impact of risk every day. Going forward, COVID-19 will change how we think about and communicate many of the risks that we may not have fully contemplated before. Our experiences will also cause us to rethink our processes and the value we bring to our organizations.

The goal of this report is to provide practical direction as to what internal audit functions can do to support their organizations and meet their internal audit charter responsibilities as they work through the impacts of COVID-19 — today and in the future. It draws from discussions and recommendations gleaned from many sources, including internal audit function leaders, consultants, and The IIA’s Audit Executive Center (AEC). The contributors discuss how COVID-19 is impacting the operation of internal audit departments, the implications for Sarbanes-Oxley compliance, how the risk landscape has changed and where internal audit needs to step up, and what the future holds for internal audit.

INTERNAL AUDIT FUNCTIONS

Internal Audit Activities

It is clear that internal audit functions have been inconsistently impacted by COVID-19. The effect appears to vary by industry, geographic location, relevant government mandates, and perception of value provided by the functions. Some internal audit departments have been furloughed for the duration, while others have updated their risk assessment and risk-based audit plan based on the current environment. Many are focused on the new or updated processes with higher risk profiles such as cybersecurity, identity access management, and remote working arrangements.

On April 9, 2020, AuditBoard hosted a webinar titled Coronavirus and Internal Audit: Preparing for the New Normal in 2020 and Beyond. The 2,500+ participants were asked to identify which of the responsibilities taken on by internal audit functions have had the most significant impact on their organizations. Their responses were not surprising:

- Updating their risk assessment (45%)
- Carrying out audit projects (39%)
- Creating awareness of key controls (31%)
- Performing research and benchmarking (16%)
- Reperforming essential first- and second-line tasks and processes (16%)

Agility Amid Crisis

Increasing the frequency of the risk assessment is important to reprioritize the organization’s top risks during times of crisis. By identifying and prioritizing the emerging risks related to the pandemic that threaten the business’s top strategies, audit leaders can help executive leadership develop appropriate mitigation strategies to ensure business objectives will continue to be met. Key risks to be assessed during this time are impact to revenues, employee safety and well-being, supply chain, and cybersecurity. Updating the risk assessment is especially useful as this process can highlight the impact of similar risks if the pandemic dissipates before a second wave returns in the next four to six months.
Anecdotally, some functions have stepped into roles where their process and risk knowledge allow them to be very impactful and where their independence is a future consideration. For example, because of their process, risk, and control knowledge, some internal auditors have moved temporarily into first- and second-line positions processing and reviewing transactions. Others are assisting with the completion or review of applications for funding opportunities from federal and state government programs. Some internal audit departments are analyzing the processes that are most affected by the changes required by the COVID-19 environment and identifying the necessary changes in the key controls to minimize the risk to financial reporting, transaction processing, technology operations, and compliance.

Internal Audit Adjusting Audit Plan Due to COVID-19

A recent quick poll by the AEC confirms the anecdotal evidence. Nearly four in 10 poll respondents added new engagements because of COVID-19, and a similar percentage redirected staff to put aside their normal audit work to assist their organizations in this time of crisis by doing non-audit work.

The poll of North American chief audit executives (CAEs) and senior audit leaders, conducted April 9–13, drew more than 400 responses.

The data reflect that internal audit’s skills and flexibility are particularly valuable in times of crisis. Internal Audit Foundation Trustee, IIA President and CEO, Richard Chambers’ blog post on the poll results addressed that value.

“The current environment is offering internal audit leaders a unique opportunity to extend their value beyond traditional audit activities and help drive the future of their business.”

— Tom O’Reilly
Senior Director Solutions Advisory, AuditBoard

Source: Audit Executive Center Knowledge Brief: COVID-19 Impact on Internal Audit: Survey results about risk assessment, audit plans, staffing, and budget, Exhibit 12 pg. 11 (The Institute of Internal Auditors, April 2020)

“Overall, the quick poll paints a positive picture about internal audit’s role in response to this crisis. I believe that shows stakeholders are welcoming the input from internal audit and are looking for new ways to leverage the skills and insights it offers,” Chambers wrote.
Many Sarbanes-Oxley programs are mature and require few significant adjustments from one year to the next. With the substantial changes in the business environment and operations resulting from the pandemic, management should identify and analyze potential impacts on the components of their Sarbanes-Oxley program. The following are some areas that organizations should consider:

- Changes in the components of the materiality calculation, which may then impact the general ledger accounts, applications, and related processes and key controls that are in scope for Sarbanes-Oxley.

- Updates made to the design of the key controls due to changes in processes.

- Impact of changes in key control ownership and performance, with special consideration given to competence and the ongoing monitoring of control effectiveness.

- Verification that evidence collection and storage are appropriately controlled.

- Whether and how often to update the risk assessment over financial reporting as the control environment undergoes changes. Identify significant transactions and key controls that should be in scope for Sarbanes-Oxley.

- Impact on financial reporting, including changes in judgmental processes and the assessment of impairments, investment valuation, goodwill, and employee stock option programs.

- Whether internal audit should serve as a resource to the external auditors. Show how the organization is being thoughtful regarding the impact to the Sarbanes-Oxley program and serve as a liaison to ensure the needs of the external audit firm are met.
THE CHANGING RISK LANDSCAPE

Most Impactful Risks

**COVID-19 is having a profound impact** on most industries and geographic locations around the world. When asked which risk will have the most significant impact on their organizations now and in the next two to four months, webinar participants responded as follows:

- Revenue (61%)
- Human resources (34%)
- Supply chain (28%)
- Another pandemic (13%)

These results are not surprising — we would expect these areas to have the most visible impacts. Revenue risk may include revenue recognition, collections and liquidity, delay in the launch of new products, and changes to the costs of manufacturing, if retooling and other employee protection processes are necessary. The impact on the human capital that our organizations rely on is yet to be fully determined. Attention has been focused on the short-term perspectives of employee well-being and safety, but the long-term impacts are not yet known, as this type of situation has not occurred in at least a generation. In the long term, we may see organizations adjusting their workforce planning — determining who works (FTE vs. contractor) where and how they work. Supply chain risk has been very impactful as we have moved to just-in-time processing over the last 20 years, and the ripple effect of China being the initial point of infection resulted in disruption ahead of COVID-19 appearing in most other locations.

Underrepresented Risks Highlighted Amid Pandemic

As time goes by, it is likely that the results of the pandemic will also highlight other areas of risk. The IIA’s 2020 North American Pulse of Internal Audit report, *Bridging Critical Gaps*, provided an annual snapshot of the internal audit profession. Completed pre-COVID-19, the report identified the following risks recognized by internal audit leaders, executive management, and boards as being among the top concerns for organizations but underrepresented in the annual internal audit plans:

- **Cybersecurity.** “More than three-quarters of Pulse respondents said that cybersecurity is a high or very high risk. Yet, the number of functions that report no audit plan resources related to this risk remains surprisingly high. Nearly one-third of respondents report they devote no portion of the audit plan to this ubiquitous and dynamic risk.” This is critical as organizations have moved to a remote...
workforce and operational workstreams in response to COVID-19, placing reliance on processes and controls over cyber risks that may not be adequately assessed.

- **Information technology.** “For information technology — defined as the use of technology for communications and information gathering and storage — size largely dictates audit plan coverage. Overall, 69% of Pulse survey respondents report they include IT in their audit plans.” During March 19–23, 2020, the AEC conducted a survey of CAEs and internal audit directors in North America. Of the 170 responses, 59% said their organizations added new technology and data security in response to changes in their working arrangements. Again, as organizations have shifted to rely even more heavily on technology capabilities, processes, and controls, it is clear for about 30% of the organizations surveyed that internal audit has not given assurance over the design and operating effectiveness of the implementation of this technology and its operation.

- **Third-party relationships.** “Less than half (48%) of respondents say their functions devote any portion of the audit plan to third-party relationships. This finding should raise concern because most organizations rely to some extent on third-party providers in key risk areas.” This reliance has not decreased in the current pandemic environment. However, a significant number of organizations have not reviewed the governance of or design and operating effectiveness of the controls over third-party relationships.

Clearly, the pandemic increases the need for internal audit functions to provide assurance over these risks and others that have increased in the current environment.

The AEC poll noted increases in internal audit focus in all three areas. Respondents reported significant or slight increases in cybersecurity (43%) and IT (38%). Third-party relationships were not broken out in the poll, but the overall focus on enterprise risk management (ERM) increased by 42%.

“Risk assessments completed before the current crisis should be assumed to be obsolete. Internal audit leaders should be focusing audit efforts on highest risk areas in light of the current environment.”

—Harold Silverman
Managing Director,
The IIA’s Audit Executive Center
Our organizations are in a state of flux and will be for some time. There is a high likelihood that internal audit functions are also far from going back to business as usual. We should view this situation as an opportunity to improve our understanding of the risks our organizations are facing and may face in the future and update processes to incorporate these changes.

As operations begin to stabilize, it is important that organizations not lose sight of core activities as other priorities creep in. The following is a suggested list of priorities for internal audit functions to consider as they respond to the current environment and plan ahead.

**Business Continuity**

1. Actively engage in the organization’s lessons learned postmortem.
2. Validate that the organization has completed sufficient end-of-crisis preparation to maximize revenue when operations return to normal. Ensure that where new processes are implemented, governance is in place.
3. Verify that business reliance processes and documentation are updated based on the lessons learned postmortem, if needed.
4. Leverage resources, including business benchmarks and internal audit networks, to understand key lessons learned and best practices from other audit leaders.
5. Consider what critical technologies should have been or should be in place in the future to help executive leadership efficiently create and execute effective response plans to future crises with a similar impact on business operations. Examples: remote-working capabilities for employees, cloud-based audit, risk, and compliance collaboration solutions.

**Risk Management**

1. Verify that our risk assessment process includes all risks that may have a significant impact on the organization in the next four to 12 months, even if the likelihood is low.
2. Assess the frequency, scope of people involved, and the type of reporting of the current risk management process, and adjust as necessary.
3. Leverage automation, as much as possible, to expedite key risk management processes, including risk solicitation, aggregation, assessment, and reporting. Consider cloud-based risk management solutions that allow audit, risk, and compliance functions to quickly assess new and emerging risks, easily visualize the data, and create real-time risk reports.

“Modern cloud technology is a critical enabler in today’s highly distributed working environment. For the audit team and every stakeholder they interact with, it’s what drives the collaboration, productivity, communication, and insights necessary for success.”

— Anand Bhakta
Senior Director Risk Solutions, AuditBoard
Internal Audit Operations

1. Assess the internal audit resource plan and budget to understand if or how the pandemic will impact internal audit. Consider how organizational layoffs, furloughs, and budget cuts will affect audit commitments.

2. Reassess the internal audit plan to ensure audit resources are focused on process and risk areas most important to the business during COVID-19’s impact.

3. Reassess how internal audit engages with control owners and audit customers. Will communication and interaction practices in place before COVID-19 enable audit to carry out responsibilities effectively? Are there opportunities to automate processes, such as document requests and the validation of remediated audit issues, with cloud-based, end-to-end audit workflow automation solutions?

4. Consider the mix of audit versus awareness type projects. Is it possible that remote work can negatively impact control performance? If so, can internal audit help the organization by promoting the importance of governance, risk, and control responsibilities, and act as a resource for change management?
In the face of unprecedented rapid change in the external environment and in the operations of businesses resulting from the pandemic, internal audit functions are well positioned to lead their organizations through this time. Chambers noted as much in an earlier blog post that examined the complex and dynamic risk set created by COVID-19.

“I believe the pandemic is pulling back the curtain to show us a glimpse of the future. It has put on display the amazing speed of emerging risks; the global interconnectedness of business, industry, and society; and how we react to adversity as a global community. As practitioners in a profession that is risk-centric, we should glean as many lessons as possible from this trial.”

Embracing the changes that have occurred and helping manage downside risks are roles in which internal audit functions can excel.
ABOUT THE INTERNAL AUDIT FOUNDATION
The Internal Audit Foundation strives to be an essential global resource for advancing the internal audit profession. The Foundation's research and educational products provide insight on emerging topics to internal audit practitioners and their stakeholders and promotes and advances the value of the internal audit profession globally. Through the Academic Fund, the Foundation supports the future of the profession by providing grants to students and educators who participate in The IIA's Internal Auditing Education Partnership Program. For more information, visit www.theiia.org/Foundation.

ABOUT THE AUDIT EXECUTIVE CENTER
The IIA's Audit Executive Center® (AEC®) is the essential resource to empower CAEs to be more successful. The Center’s suite of information, products, and services enables CAEs to respond to the unique challenges and emerging risks of the profession. For more information on the Center, visit www.theiia.org/AEC.

ABOUT THE IIA
The Institute of Internal Auditors (IIA) is the internal audit profession’s most widely recognized advocate, educator, and provider of standards, guidance, and certifications. Established in 1941, The IIA today serves more than 200,000 members from more than 170 countries and territories. The association’s global headquarters is in Lake Mary, FL. For more information, visit www.theiia.org.

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AuditBoard is the leading cloud-based platform transforming how enterprises manage risk. Its integrated suite of easy-to-use audit, risk, and compliance solutions streamlines internal audit, SOX compliance, controls management, risk management, and workflow management. AuditBoard’s clients range from prominent pre-IPO to Fortune 50 companies looking to modernize, simplify, and elevate their functions. AuditBoard is the top-rated audit management software on G2, and was recently ranked as the third fastest-growing technology company in North America by Deloitte. For more information: www.auditboard.com.

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