



Internal Auditing Around the World

Profiles of Internal Audit Functions at Leading International Companies Undergoing Significant Change

VOLUME V

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Introduction

“IN THE STRUGGLE FOR SURVIVAL, THE FITTEST WIN OUT AT THE EXPENSE OF THEIR RIVALS BECAUSE THEY SUCCEED IN ADAPTING THEMSELVES BEST TO THEIR ENVIRONMENT.”

CHARLES DARWIN*

Internal auditing, as noted in The Institute of Internal Auditors’ formal definition, is about “adding value and improving an organization’s operations.” Few would argue with the assertion that such objectives have never been more critical than in the current business environment, where virtually every organization worldwide is facing unprecedented challenges. Yet there are signs progress is being made, especially when considering the current global crisis from an internal audit (IA) perspective. During these uncertain times, IA leaders and their teams have a unique opportunity to help their management and board of directors understand their risks and build the controls necessary for their companies to run more effectively and improve their bottom line.

Without question, the risk landscape has changed dramatically since 2005, when we published the first volume of *Internal Auditing Around the World*. Four years ago, many organizations were investing more in their IA functions as they sought to comply with the internal control requirements of the Sarbanes-Oxley Act. Not surprisingly, internal auditors today find themselves in a very different place and facing challenges difficult to imagine just a short time ago.

How are IA functions helping their organizations adapt and even succeed in these unprecedented times? In this year’s guide, we feature 11 successful international companies that are undergoing significant changes, such as restructuring, mergers and acquisitions, and industry transformation. As detailed in the following pages, we learned that these organizations have not only adapted successfully, but that they also have uncovered many untapped opportunities.

For example, the need to create greater transparency, establish sound corporate governance and understand risk exposures has never been greater. To address these priorities, many of the IA leaders in these profiles have identified ways to partner more effectively with their boards and management, as well as provide accountability to external stakeholders such as investors and customers. At Prudential, for example, Marcus Adams communicates key issues to board members and presents them with a concerted risk management view. This approach has helped to make Adams and his team true partners with their board.

Also, in any difficult business climate, internal auditors often must assume greater responsibilities with fewer resources. In response, many are finding ways to work smarter. At Continental Airlines, Steve Goepfert acknowledges the challenges of being an effective leader while being in an industry hit hard by the economic downturn. Goepfert makes the most of available resources. For example, by using IT to continuously monitor key risk areas, Continental’s IA function has more time for creative problem solving and focusing on value-add activities. And at FEMSA, José Gonzalez Ornelas plans on using state-of-the-art IT tools to become adaptable to the evolving needs of his organization.

*This year is the 150th anniversary of the publication of Darwin’s *On the Origin of Species* and the 200th anniversary of Darwin’s birth.

Now, more than ever, boards, management and other stakeholders are looking to internal audit to help them navigate the uncharted course ahead. Pierre-Arnaud Cresson at Gemalto may have said it best: “In the end, internal audit is not like external audit. Internal audit focuses on the future of the company, staying ahead of change in order to guide the company for whatever is to come.” At Protiviti, we recognize that change can be difficult but also brings opportunity. We hope these profiles will provide guidance and inspiration to CEOs, CFOs, CAEs, boards of directors and IA professionals worldwide as they address the challenging times ahead.

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Acknowledgements

Protiviti is grateful to the companies and internal audit teams who freely discussed how they are adapting to change and what best practices are most effective for their organizations. We wish to acknowledge the extraordinary leadership of The Institute of Internal Auditors (The IIA). The IIA provides invaluable guidance to IA professionals worldwide. As always, Nancy Hala has done an outstanding job conducting the interviews and writing the excellent profiles in this publication.

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Company Headquarters – Indonesia
Number of Countries Operates in – 5
Number of Employees – 22,804
Industry – Financial Services
Annual Revenues – Rp29.4 Trillion
Annual IA Operating Costs/Budget – Rp60 Billion
Number in IA Function – 117
Number of Years IA Function Has Been in Place – 10
IA Director/CAE Reports to – President Director (CEO)

Note: All of the above information is accurate as of December 31, 2008.

“The internal audit group must be the catalyst for constructive changes in Bank Mandiri. As the bank has identified the challenges faced by each of its [strategic business units] in moving toward its vision, and recognized that the risks surrounding it are increasing in complexity and magnitude, the role of chief audit executive becomes all the more critical and needs to be much stronger to ensure that internal audit continues to move in step with the bank.”

– Riyani T. Bondan

Internal audit moves in step with Bank Mandiri to be the regional champion

Bank Mandiri, the result of a 1999 merger of four state-owned banks, is the largest bank in Indonesia. As of 2008, Bank Mandiri had approximately 960 branches, including overseas in Singapore, Hong Kong, Cayman Islands, Shanghai and Dili, with several subsidiaries, including Bank Syariah Mandiri, Mandiri Sekuritas, AXA Mandiri and Bank Mandiri Europe Ltd. in London.

In 2005, Bank Mandiri faced a critical business challenge with nonperforming loans representing 26 percent of its total loan portfolio. Shareholders of the bank appointed a new management team, including a new CEO. At that time, the priority for the new management team was to improve loan quality, implement strong corporate governance and distill corporate culture around five core values: trust, integrity, professionalism, customer focus and excellence (TIPCE).

A regional champion

According to Ogi Prastomiyono, the former chief audit executive of Bank Mandiri, by the end of 2005 the bank had developed a five-year business plan divided into three phases:

- 2006-2007 – *“Back on track”*
In this phase, Bank Mandiri emphasized strengthening corporate culture, the organization, human resources, the business model and management of nonperforming loans.
- 2008-2009 – *“Outperforming the market”*
In the second phase, Bank Mandiri is aspiring to be the dominant multispecialist bank; that is, to be the revenue pool market leader in each business segment.
- 2010 – *“Shaping the end game”*
Bank Mandiri envisions becoming a regional champion bank.

The initial back-on-track phase has been an important milestone in the transformation process of Bank Mandiri. Success can be seen in the significant upturn in the bank’s financial performance, with net profit rising sharply from Rp600 billion (US\$61 million) in 2005 to Rp4,300 billion (US\$458 million) in 2007. Additionally, asset quality improved significantly, as reflected by net nonperforming loans falling from 15.3 percent in 2005 to 1.5 percent in 2007.

Bank Mandiri was ranked first in customer service excellence in the annual MRI Infobank survey in 2007, moving up from sixteenth, eleventh, third and second place between 2003 and 2006. In addition, the bank's consistent efforts in good corporate governance (GCG) implementation have garnered recognition from both domestic and international institutions. The Indonesian Institute of Corporate Governance has appraised Bank Mandiri as a "highly trusted" company with the highest score and as the best publicly listed company in the financial sector. Bank Mandiri also was selected by *Asiamoney* magazine in 2007 as the "overall best managed large capitalization company in Indonesia," following the awards for "the best in disclosure and transparency" and "the best corporate governance" in 2006. Bank Mandiri followed the back-on-track phase successfully and in less time than expected.

"Bank Mandiri's objective, by the end of 2010, is to become a banking champion in the region," Prastomiyono says. The criteria for achieving this include attaining market capitalization of US\$10 billion and a share of 20 percent to 30 percent of the revenue pool of each segment. Since Bank Mandiri seeks to be a regional champion, the internal audit (IA) group intends to promote and support the necessary international standards for achieving this objective.

Bank Mandiri: Three key changes

The IA group was determined to be fully aligned with and supportive of all strategic changes prevalent in the bank's continued growth. Therefore, it established processes and programs that corresponded with each of the three key changes that Bank Mandiri initiated in 2007 – the creation of strategic business units (SBUs), the development of a performance-based culture and the implementation of risk management practices.

Strategic business units

When SBUs were established throughout the bank, the IA group also reorganized its structure to align with those of the bank. "This represented an important organizational change for Bank Mandiri," says Prastomiyono. With this change, specific auditors are now responsible for corporate banking, commercial banking, treasury and investment banking, and small and "micro" banking. Additionally, auditors are assigned to fraud investigations and provide support for quality assurance and audit development.

Performance-based culture

Performance-based culture was introduced so that key performance indicators (KPIs) for each SBU and supporting unit cascade through the organizational structure down to each individual. Based on the KPIs of each organizational unit, IA provides reasonable assurance that the unit's processes are in place and operationally effective to enable achievement of its objectives.

According to Riyani T. Bondan, the current chief audit executive of Bank Mandiri, the IA group measures its performance consistent with the rest of the bank by using a balanced scorecard approach including financial, customer, internal process and human capital development aspects. As part of the process in ensuring audit satisfaction, a survey of auditees is conducted to understand what they need and how to help them improve their processes. The results are folded into the audit plan for the year. Another survey is sent to the board of directors and the board of commissioners to ensure that they are satisfied with IA's reports and performance.

Risk management and corporate governance practices

Risk management practices throughout the organization have helped strengthen the decision-making process. Independent risk management consists of credit risk and policy, and market and operational risk. Additionally, the bank's enterprise risk management (ERM) unit comprehensively evaluates risk – including credit, market and operational – so the bank can comply with Basel II regulations by 2010. The implementation of risk-based auditing has enforced the synergy between IA and the risk management function.

Bank Mandiri has adopted a two-tier board structure consisting of a board of directors and a board of commissioners. The board of commissioners is composed of representatives of shareholders and independent commissioners and is not involved in day-to-day management of the organization or running of the bank. The audit committee is a subset of the board of commissioners, while the board of directors is composed of the senior management members or the C-level executives. One person cannot be both a commissioner (member of board of commissioners) and a director (member of board of directors) at the same time.

The chief audit executive at Bank Mandiri has a solid reporting line to the chairman of the board of directors (the CEO) and a dotted line to the board of commissioners through the audit committee. This reporting line provides independence and objectivity for the IA group and is in compliance with Indonesia Central Bank regulations.

“Since 2005, we have implemented corporate governance principles,” says Bondan. “When we conduct an audit, our team reviews both the risk management and the governance processes in every business unit. For the past three years, we have had an independent corporate governance review conducted by an independent third party. Last year, our reviewers concluded that the bank exhibited best practices in corporate governance.”

Becoming a world-class IA function

During his tenure as chief audit executive, Prastomiyono declared that his plan was to move the IA group toward becoming a world-class organization by improving three key areas: methodology, people and systems. The improved methodology is the recently enhanced risk-based audit approach, which is considered an international best practice. With regard to people, the group is in the process of developing the Internal Audit Capability Model, designed to help ensure all auditors have the competencies and training they need to be strategic partners and consultants for the SBUs. Finally, systems improvements are achieved through the development and implementation of an audit management information system called SIMA (Sistem Informasi Manajemen Audit) – the bank’s IA management information system.

Risk-based auditing

The IA group has identified at least four driving factors for the implementation of risk-based auditing at Bank Mandiri:

- Facilitating compliance with Bank Indonesia’s risk management-related regulations
- Conforming audit operations to international standards
- Fulfilling the Internal Audit Charter
- Advancing the role of IA

The group also identified at least four benefits gained from the implementation of risk-based auditing:

- Facilitating rapid adoption of risk management practices bankwide
- Hastening the risk maturity progression bankwide
- Focusing on auditing higher risk areas
- Increasing IA capacity in order to perform more value-added tasks

Risk-based auditing enables IA to prioritize its audit in a systematic and disciplined manner. While internal auditors have always focused their efforts on the riskier areas of the organization, it is usually directed by IA’s own assessment of risks. By contrast, risk-based auditing makes full use of management’s assessment of risks.

IA capability

The IA group has nine departments with about 120 internal auditors located in the head office. The bank has branches throughout the country, many at considerable distances from the head office, which makes covering them a challenge. To address this, in 2006 the IA group designed and implemented an approach using regional internal control officers. “Currently, we have about 10 regional offices, each with 30 regional internal control officers. This is a change for us,” says Bondan. “Before we established this, we only relied on the auditors in the head office to provide such coverage.”

Bondan and her team use an IA competency model to identify competency gaps among auditors. “To perform our role, we want to improve audit capability,” she explains. “For existing auditors, we send them to prepare for international certification. Currently, about 20 percent of our staff is internationally certified, a number we plan to increase by 2010.”

Recruiting auditors with expertise in the banking industry is another area of focus for Bank Mandiri’s IA group. In 2006, the chief audit executive recruited, both internally and externally, senior officers with experience in treasury, banking, loans and credit. Training programs also play an important role. “We send our auditors to other areas in the bank to promote a shared and better understanding of audit and business issues,” Prastomiyono says. “This gives our auditors in our many regions a comprehensive view of the bank. This is important for becoming a regional champion.”

Audit management information system

IA’s SIMA is used to automate audit paperwork utilizing the paperless concept to improve the efficiency and effectiveness of the audits. The system enhances audit process, reporting and the database. With SIMA, audit supervision can be conducted remotely from the head office.

In addition, SIMA can generate reports instantly to help both auditors and top management make decisions. Risks and controls data are stored in SIMA for use by internal auditors, while the risk management unit also uses this data to conduct risk and control self-assessments. The IA and the risk management teams envision a single risk and control database to ensure consistent data and efficient data maintenance.

Changes, challenges and a vision

The most critical changes and biggest challenges for Bank Mandiri involve people. “Our vision is to become a trusted internal audit organization that conforms to international standards and to be the strategic partners for our business units,” says Bondan. “To achieve this vision, we have to adopt best practices. As auditors move into their roles as strategic partners, their skill sets, certifications and overall competency levels will have to continue to rise. In 2005, there was a question as to whether or not to outsource the internal audit function. I believed we could evolve our team internally, so we are committed to this, and we hired a consultant to develop a methodology to build an esprit de corps and enhance our auditors’ skill sets.”

Synergy between risk management and IA at Bank Mandiri is another focus of attention, according to Bondan. Moving forward, by applying an appropriate change management program, the alignment between IA and risk management will be stronger. “I want to grow the change agent role in risk management and internal audit,” Bondan says. “That means everyone can be a role model, a teacher, a consultant.”

She adds, “The internal audit group must be the catalyst for constructive changes in Bank Mandiri. As the bank has identified the challenges faced by each of its SBUs in moving toward its vision, and recognized that the risks surrounding it are increasing in complexity and magnitude, the role of chief audit executive becomes all the more critical and needs to be much stronger to ensure that internal audit continues to move in step with the bank.”



BARRICK

Company Headquarters – Canada

Number of Countries Operates in – 10

Number of Employees – Approximately 20,000

Industry – Gold Mining

Annual Revenues – US\$7.9 Billion

Annual IA Operating Costs/Budget – US\$4 Million

Number in IA Function – 8 Employees and 3 to 4 Co-source FTEs

Number of Years IA Function Has Been in Place – 5

IA Director/CAE Reports to – Solid Line to Chair of Audit Committee, Dotted Line to VP Risk and Assurance

Note: All of the above information is accurate as of December 31, 2008.

“We are a relatively new function within the company, and we want to be the partners to the organization’s various functions and instrumental to their success. That is why we approach our audits with the series of discussions about purpose, objectives and success factors. We view our role as partner and trusted advisor for senior management.”

– Ted Szpargala

Barrick Gold Corporation: The mining company of the future

Barrick, headquartered in Toronto, Canada, is a gold producer with a portfolio of 27 operating mines, several advanced exploration and development projects located across five continents, and large land positions on both prolific and prospective mineral trends. As of December 2008, the company’s reserves – the largest in the industry – consisted of 138.5 million ounces of proven and probable gold reserves, 6.4 billion pounds of copper reserves, and more than 1 billion ounces of contained silver within gold reserves. In that same year, Barrick produced 7.7 million ounces of gold at a cash cost of US\$443 per ounce and 370 million pounds of copper.

The company has the gold mining industry’s strongest and only “A” rated balance sheet, which positions it to fund its project pipeline and seize other exploration and acquisition opportunities as they arise.

Barrick nearly doubled in size in early 2006 when it acquired a major competitor. This has had significant implications for the company in terms of integration. Barrick’s divisions, which operate independently, are structured on a regional basis – North and South America, Africa and Australia Pacific. Each division is led by a regional president and has a corporation-like hierarchy or organizational structure with a regional CFO, head of operations, human resources leader and other key positions.

Ted Szpargala is the senior director, global internal audit (IA) at Barrick, a position he has held for more than two years. He oversees a group of eight auditors and three to four FTEs from external service providers. “We operate primarily on a co-source basis. Our department is much smaller than many in our peer group, although our team has grown recently,” Szpargala says. “It was originally entirely outsourced, with only two people in-house. When I was hired, we assessed the needs of the business in its enlarged footprint, as well as the need for specific expertise to be ‘on top,’ and changed the structure from outsource to co-source.”

When he created the co-sourced team at Barrick, Szpargala hired a senior manager responsible for the coordinated administrative aspects of running the department, such as assigning audits to individual members and monitoring progress. The team reports to both the senior manager and Szpargala, who has a solid reporting line to the audit committee chair and a dotted line to the company’s vice president of risk and assurance.

The risk and assurance function consists of six interdependent functions: enterprise risk, security, insurance, compliance, fraud prevention and IA. Compliance, fraud prevention and IA share some common subject matter, so there are similarities among those groups, and the work is coordinated to minimize duplication of effort to the greatest extent possible. Insurance is separate, but IA activities contribute to a better risk profile, which aids the insurance team. IA activities are also articulated and coordinated with the enterprise risk function. Szpargala and his group work closely with the company's security function.

Do you sleep comfortably?

At the company level, the major recent change has been acquisition integration, which involved incorporating and bringing online additional systems for Barrick to reach its vision of being the best gold mining company. For the IA team, an important change has been greater stability. As a developing function in the organization, IA literally had to be built from the ground up; processes needed to be defined, resources needed to be employed, awareness needed to be created and acceptance developed. In order to facilitate the development of the function, an external consultant was appointed to perform a QAR on the baseline, and the outcome was used to develop an action plan. Over the last year or two, those requirements have fallen into place and are working well. Another significant development for Barrick's IA function has been its transformation from a total outsourced model to a co-sourced one. "In our co-source structure, we have staffed the department with top-of-the-line people to work with resources and SMEs in delivering quality work to management and the audit committee," Szpargala says.

There has been a great improvement in the culture and environment of the company. "We have contributed to a greater recognition of blind spots," Szpargala says. "Other organizations may take an IA approach that asks, 'What keeps you up at night?' We ask instead, 'What allows you to sleep comfortably?' We include that input in our audit plan to provide assurance around that comfort, or point out blind spots. This helps us either confirm the basis for their comfort or point out why they are wrong. This approach was validated when a member of senior management called me in and told me that our findings helped him identify new opportunities for further improvement and asked us to replicate the audit at another location."

It helps Szpargala that Barrick has embraced the objective to manage change and continually improve. "For us, this has been more a case of dealing with a very dynamic, rapidly growing organization in an environment of finite resources," Szpargala says. "The auditing approach we have taken in the past two years has been *auditing for leverage*. When an area comes under audit scrutiny, we go directly to the head of that area and discuss success factors and related measurements, action steps, obstacles and all procedures that facilitate the monitoring of progress, and because we operate on a regional basis, we ask them to nominate the region that does it best. We then take our discussion to the highest level process owner in the region, as well as the local president/CFO/other stakeholders in the region, and ask them to name the location (mine site) that is performing at the highest level. That is the one we audit. We take our findings to the functional and operational head of the area, who will then communicate to the rest of his or her organization the issues we found with the best of the best." The message is clear at Barrick: IA adds value, and exists to help make things better.

Rather than doing the same audit multiple times, Szpargala says he tries to be proactive, audit the top performers, and then circulate the output to the rest of the company so they have something to aspire to. "We used to go around the world and replicate the same audits at each location, but when you look at the sheer numbers, it quickly became clear that it would consume too many resources to take a cookie-cutter approach to these audits," Szpargala says. "This helps us accelerate the coverage in terms of subject areas and rely on the management teams of these organizations to take the output and share the information."

The communication web at Barrick typically includes a corporate-level senior vice president who has a dotted reporting line to counterparts in the regions, who then communicate to counterparts at individual mine sites.

“This approach has certainly been validated over the past 18 months,” says Szpargala. “At a time, when we were migrating from outsourcing to co-sourcing, we had to prove our worth before we could significantly increase head count.”

Building the co-source team

Szpargala sets the bar very high when he hires auditors for his small IA and line management team. Some members of the current team have worked with Szpargala before, and have several years of diverse IA experience. Szpargala says he has sought out professionals who have worked for large, multinational organizations, where an auditor often crosses functional lines and earns significant hands-on experience. “We need people who have been on the other side of the fence,” he says. “We need the experience and practicality for implementing recommendations. We are not a teaching shop.”

Changes in vision and mission

The IA vision and mission statement is still in development. “We have a mandate statement, but we are working on evolving our mission and vision,” Szpargala says. “We are a relatively new function within the company, and we want to be the partners to the organization’s various functions and instrumental to their success. That is why we approach our audits with the series of discussions about purpose, objectives and success factors. We view our role as partner and trusted advisor for senior management. We want to continue to progressively improve our delivery methodology.”

When Szpargala joined Barrick he developed the infrastructure and methodology to comply with The IIA’s *Standards* to create a broader understanding and acceptance of IA’s purpose and delivery process. “Since we are a new group, there are some pockets of Barrick that do not know us. Whenever possible, we want to have up-front involvement rather than come in after the fact and perform autopsy work,” he says.

Three-year strategic plan

Beyond working in accordance with The IIA’s *Standards*, the team’s objectives are to optimize their resource mix with the correct balance of internal and external resources, continue to be viewed as trusted advisors, become better known in the company, and establish coverage that satisfies both organizational leadership and the audit committee.

The IA team’s three-year strategic plan includes the following components:

- Conduct an ongoing quality assurance program of other internal/external reviews and audit activities.
- Continuously develop staff, and introduce a university co-op program. (“Right now, our staffing model does not accommodate junior people, but it will as we grow,” Szpargala explains.)
- Facilitate an even higher level of requests from the organization.
- Create a program in which auditors rotate out of the department and into operations, in order to develop the IA team as a talent pool for Barrick.
- Develop skills in specific areas. (“For example, we are building a number of mines right now,” says Szpargala. “We are spending many years and billions of dollars to do this, and with the timeline and money involved, it is critical that IA focus on continuing to help the company protect all stakeholder interests. Right now, we are bolstering our IA skill set to address this.”)
- Raise awareness and acceptance of IA through a variety of ways, including developing a presence on Barrick’s intranet, visiting regional business units, and meeting with regional leadership to gather feedback on IA’s performance.

Szpargala is also working to establish key performance indicators; some have recently been included in his submissions to the audit committee. “Another measure is the number of times we are asked to perform special projects,” he says.

Most likely because of these improvements and initiatives, and because the IA team delivers a quality product and points out blind spots, the relationships that the team has forged with Barrick’s leadership have become strong. “We say that we are truly here to help – that is our role – and it comes out in the way we write our reports,” Szpargala says. “We are fair and balanced and accent the positive. We believe the shorter the report the better, as long as the content is accurate and delivers value.”

Changes for the future

Szpargala says he expects to see normal turnover among his audit staff, as the IA team’s efforts and skills have been recognized by other Barrick departments. This will inevitably create a void of talent that Szpargala must work hard to fill.

According to Szpargala, the next steps for IA at Barrick are to build on the good work his team has accomplished so far and continually cultivate and improve relationships in the organization.

Company Headquarters – United States
Number of Countries Operates in – 50+
Number of Employees – 42,000
Industry – Aviation
Annual Revenues – US\$15.2 Billion
Annual IA Operating Costs/Budget – US\$2.2 Million
Number in IA Function – 23
Number of Years IA Function Has Been in Place – 30+
IA Director/CAE Reports to – Executive VP and CFO

Note: All of the above information is accurate as of December 31, 2008.

“In times of change, your focus has to be on your people, who can help the company navigate through challenges and are able to keep their eyes on the strategic goals of the company. Our auditors are flexible, solutions-oriented and creative thinkers. Those are some of the attributes that make them so good at what they do.”

– Steve Goepfert

Continental Airlines: “Work Hard. Fly Right.”

Based in Houston, Texas, Continental Airlines is the fourth-largest airline in the United States, with major hubs in Houston, Newark and Cleveland. Continental recently was voted “Best Domestic Airline” by *Executive Travel Magazine*. The company’s advertising tagline – “Work Hard. Fly Right.” – speaks to its straightforward formula for ongoing success in an industry beset with changes and challenges.

Steve Goepfert, staff vice president of internal audit (IA) for Continental, oversees a recently trimmed team of 23 auditors. “We have seen so many changes this year,” he says. “Mergers, new alliances, fluctuating oil prices and overall volatility have impacted our industry.”

The three most significant changes, according to Goepfert, are a reduction in airline capacity and workforce, an increase in merger and alliance activity in the airline industry, and a renewed focus on the bottom line in a challenging economic environment.

Maintaining quality, delivering value

As with many other departments, Continental’s IA department has had to take proactive measures to be able to do more with less. Goepfert says, “During these challenging times, auditors are called upon even more to ensure key risks are managed, fundamental controls are sound and business units are operating effectively.” As Continental reduced airline capacity and – through a series of furloughs and voluntary separations – reduced its workforce by approximately 3,000, IA also reduced its team from 25 to 23 professionals by refraining from filling two open posts.

According to Goepfert, “To ensure we provide a consistent quality deliverable to our constituents, we have re-emphasized the importance of empowering our team with identifying ways to work smarter. This includes using robust technology to continuously monitor key risk areas. For instance, the IA department has processes to receive key accounting and operational data from our field locations that identify key risks, such as late deposits, late sales reporting and disbursement errors. This data allows IA to quickly identify field locations that are having problems so that we can respond to emerging issues and send resources to problem sites to get these matters fixed expeditiously.”

Sound auditor skepticism and judgment are integral parts of the team’s ability to stay abreast of the challenges. “I have been with Continental for 25 years,” Goepfert says. “My core team has more than 75 years of airline audit experience. While leadership and professionalism are always important, it is especially critical to be recognized as a credible source of information in down cycles.” The

department specifically searches for auditors capable of being future leaders for Continental; in fact, Goepfert says he is proud of having placed more than 50 auditors in key roles throughout the organization during the past 20 years.

“In times of change, your focus has to be on your people, who can help the company navigate through challenges and are able to keep their eyes on the strategic goals of the company. Our auditors are flexible, solutions-oriented and creative thinkers. Those are some of the attributes that make them so good at what they do,” Goepfert says.

Merger mania

Throughout 2008, the airline industry went through a period of several mergers, acquisitions and near deals – the most widely known being the merger of two U.S. airline giants, Northwest and Delta. In December 2008, Lufthansa acquired Austrian Airlines; British Airways announced its plans to merge with Qantas, the Australian flag carrier; and Ryanair launched a bid for Aer Lingus. In early 2008, there was talk of a merger between Continental and United Airlines, which never came to fruition.

While the department did not take a direct role in these merger activities, management did keep the staff focused on adding value to the organization’s bottom line and remaining focused on the continuing business. Goepfert says, “Too often in mergers employees get caught up in all the rumors of what is happening or might happen to people and departments. It is important for management to keep people focused on the day-to-day operation of the business, but to also be prepared to respond if an immediate merger-related project comes forward.”

While the department was not involved in the merger activity, there were other deals that did come to fruition for which IA provided support, such as assisting the corporate development group in analyzing an updated capacity purchase agreement with an airline partner that was successfully completed. “Timing was crucial to finalizing the deal, and IA was able to bring its expertise in the area to assist another department in the timely completion of this analysis,” Goepfert says. “This is a way that IA can add value that goes beyond its normal functions.”

Staying focused on the bottom line in times of change

In any economic downturn, auditors must renew their focus on the bottom line and demonstrate to the organization that the IA team can add value. “Too often, when things get difficult, auditors either stay with the tried and true, like doing the routine compliance audits, or become distracted and veer in many different directions,” Goepfert says. “We believe a key area for focus is on audits that add bottom-line value, such as third-party contract audits, benefits exams and the audits of receivables. When things get challenging, departments cut back on personnel, and they may not pay as much attention to vendor billings or ensure receivables are being collected as promptly. So, audits in these areas could be productive.”

Goepfert adds, “It’s not hard to be a leader of an organization when things are really good, but it requires a different sort of leadership when things go against you. You can’t call the same play you’ve called 20 times before. People who can lead in difficult times, who take steps systematically and logically and don’t panic, are the ones who rise to the top.”

After 9/11, many airline audit groups stopped doing field audits for a time because of the increased security concerns in the airports. “We didn’t stop,” Goepfert says. “Internal controls and protection of assets were still just as important, perhaps more so, after 9/11. We were out in the field in full force. The point is, even through challenging times of immense change, it is vital to stay focused on what must be done to add value to the company every day.”

Performance measurement

One key indicator Goepfert and his team evaluate in terms of their performance is how many dollars they have helped bring into the organization. “This is a good statistic to keep track of,” he says. “It helps to demonstrate how we are adding value to the bottom line. When we can market our services and activities as value-adding, we will get more buy-in across the organization.”

Flying right, into the future

Goepfert predicts that he and his team will continue to focus on the dollar-value proposition for Continental in the near future. “In this tough economy, auditors need to show they add value to the bottom line,” Goepfert says. “Since most organizations have reached a steady state on Sarbanes-Oxley, those who are still throwing all their resources at it likely are missing the boat. At Continental, we are using continuous monitoring to reduce Sarbanes-Oxley hours. Now, we are gearing up for International Financial Reporting Standards (IFRS) 2012.”



ENERGY IN TUNE WITH YOU.

Company Headquarters – Italy
Number of Countries Operates in – 22
Number of Employees – 75,981
Industry – Energy and Utilities
Annual Revenues – €61.2 Billion
Annual IA Operating Costs/Budget – About €1 Million
Number in IA Function – About 100
Number of Years IA Function Has Been in Place – 10+
IA Director/CAE Reports to – Executive Director, Internal Control Committee, Board of Statutory Auditors

Note: All of the above information is accurate as of December 31, 2008.

“We have organized ourselves differently. We now focus on our international portfolio, which has been a large challenge. Also, getting people accustomed to working in a matrix was important. Now, for the first time, I have people who are specialized in a specific branch of the business, who have technical expertise, and who are becoming familiar with working internationally.”

– Francesca Di Carlo

Creating an international audit team at Enel

Enel is Italy's largest power company and Europe's second listed utility by installed capacity, producing and selling electricity and gas across Europe, and North and Latin America. Following its acquisition of the Spanish utility Endesa, together with partner Acciona, Enel serves more than 50 million power and gas customers. The company operates a wide range of hydroelectric, thermoelectric, nuclear, geothermal, wind-power and photovoltaic power stations.

The company is organized by operational divisions, with a separation of its distribution and production businesses. Enel has three operating divisions in Italy: Marketing, Distribution and Generation. Internationally, Enel's Renewable Energy arm, which includes wind farms and other renewable energy sources and innovations, spans the globe. Enel was privatized in 1999, and the energy industry in Italy has also been transformed; therefore, structurally and industrywide there have been many changes. The most significant, from an organizational and an audit standpoint, is that Enel doubled its size and half of its net invested capital is now abroad.

According to Francesca Di Carlo, the director of audit for Enel since January 2008, the most important change has been the process of internationalization. The corporate audit department includes approximately 100 people in Italy and abroad. Enel has Rome-based Marketing, Distribution and Generation teams, as well as a team that covers corporate activities such as purchasing. The power company also has a unit that coordinates risk assessment methodologies used annually for its audit plan. The Renewable division is a newly created team, and one person has been appointed to oversee this area.

For Enel's recent acquisition in Russia, Di Carlo hired a Russian auditor who is stationed in Rome and helps to mingle cultures, and another auditor who was sent to Russia to help export culture and ethical standards.

“Our challenge over the past 18 months has been to create an international department,” says Di Carlo. “We are working with different cultures to create or strengthen local teams.”

The corporate audit function

The corporate audit group at Enel consists of several units:

- Audit corporate service
- Ethical and fraud audit
- IT audit
- Audit generation and energy management
- Audit infrastructure and network
- Market audit
- International audit
- Audit renewables

“We have organized ourselves differently,” says Di Carlo. “We now focus on our international portfolio, which has been a large challenge. Also, getting people accustomed to working in a matrix was important. Now, for the first time, I have people who are specialized in a specific branch of the business, who have technical expertise, and who are becoming familiar with working internationally.”

Di Carlo seeks auditors with various skills because she says Enel’s team must represent a mix of experiences, cultures, expertise and talents. “We don’t recruit and hire auditors,” she explains. “An engineer can be trained to be an auditor because he or she is a highly ordered, clear thinker. I look for individuals who are flexible and have a well-rounded mentality. We do very little financial auditing; my key auditors are those who are more process-oriented and possess advanced interpersonal skills.”

Audits conducted in other countries differ from those conducted in Italy; for many reasons, laws and regulations, control rules and maturity of governance are varied. “We typically start with implementing procedures rather than verifying procedures in countries such as Romania, Bulgaria or Slovakia. It is similar to pioneering audit and control techniques rather than going in and verifying that things are right, which is how we do it in Italy,” Di Carlo says.

Even with the substantive changes that have occurred, audit objectives have not changed for Enel. “The goals are always the same,” says Di Carlo. “In the last five to six years, the daily objectives are to ensure that people work together as a team, beyond boundaries. This makes life very exciting and satisfying because everyone is contributing. One of our missions is to make sure that the ethical code is respected. We are the custodians of the code.”

Anti-fraud and compliance

The company’s commitment in the fight against corruption is spelled out in its implementation of a “Zero Tolerance towards Corruption Plan (ZTC Plan),” which outlines the general principles of the code of ethics regarding the rejection of corruption.

The ZTC Plan incorporates anti-corruption principles, and the document is distributed within and outside the company indicating the responsibilities and actions to be taken across different company divisions. The code of ethics covers bribes, contributions to political parties and charitable organizations, sponsorships, facilitations, gifts, hospitality and expenses.

The audit approach

“To put together our audit plan, we benchmark data from large international and domestic companies and use risk assessment, which is aimed at reviewing all the business units by interviewing process owners to determine risk rankings,” Di Carlo says. “Over time, we reassess each area to make sure that process owners implement the action plans that we have identified in our audits.” The team also conducts special audits at the request of Enel management.

Overall, Enel's audit approach is based on an enterprise risk management (ERM) model, which focuses on processes and their risks. The model is shaped by the views and vision of the company's board of directors or management. ERM at Enel is designed to identify and manage those risks, events or circumstances that can influence the company's business, providing reasonable assurance that the company's objectives will be achieved. At Enel, ERM focuses on the following:

- Identifying the key risks through the mapping of corporate processes
- Assessing and prioritizing the determined risks
- Identifying the tolerance limits defined by management or by the audit assessment
- Formulating corrective plans to limit the risks and/or improve the effectiveness of controls
- Sharing the results with management

Areas of audit interest include acquisitions, governance and controls, and key operating processes. The risk assessment process allows a thorough review of all processes and the identification of those areas and activities that are more relevant and carry more risk.

The audit plan also is derived from corporate audit's participation in management meetings, input from the external auditor, results from past audits and an analysis of the budget's objectives. "We create an audit universe where all processes are analyzed together with their related risks, and then are prioritized," says Di Carlo. "The draft plan is then consolidated and taken for the approval of the audit committee, CEO and chairman to become the final version."

The final report contains a description of the issues in the scope of the audit and the audit analysis, audit findings, and the action plan, which is designed to solve the deficiencies in the control system.

The report also contains an executive summary, which is addressed to senior management and outlines:

- Activities carried out
- Results obtained
- Overall assessment of the control system of the process or area audited
- Action plan

According to Di Carlo, challenges ahead for Enel include international consolidation, primarily in Russia. "That is our real risk right now, determining how to cover that region in the optimal way," she says.



FEMSA

Company Headquarters – Mexico

Number of Countries Operates in – 9

Number of Employees – 122,000

Industry – Consumer Products and Retail

Annual Revenues – US\$12.1 Billion

Annual IA Operating Costs/Budget – US\$7.5 Million

Number in IA Function – 120

Number of Years IA Function Has Been in Place – 18

IA Director/CAE Reports to – CEO and Audit Committee

Note: All of the above information is accurate as of December 31, 2008.

“The main challenge the IA function faces in the near future is maintaining a sufficient organizational structure and state-of-the-art IT tools at a competitive market cost. This will allow us to easily adapt to the changing needs of the organization, which include our new businesses, territories, operating processes and regulations.”

– José Gonzalez Ornelas

FEMSA: A time of constant change

Headquartered in Monterrey, Mexico, FEMSA is the largest beverage company in Latin America, exporting its products to the United States and to countries in Latin America, Europe and Asia.

FEMSA is a holding company, with 215 million consumers across its market territories. Its principal activities are grouped under the following sub-holding companies and carried out by their respective operating subsidiaries:

- Coca-Cola FEMSA – Produces, distributes and markets nonalcoholic beverages. It is the second largest Coca-Cola bottler in the world, following Coca-Cola Enterprises, and the largest Coca-Cola bottler in Latin America.
- FEMSA Cerveza – Produces, distributes and markets beer and flavored alcoholic beverages. It is one of the largest brewers in the world, with operations in Mexico and Brazil.
- FEMSA Comercio – Operates OXXO, the largest chain of convenience stores in Latin America, with 6,088 in Mexico as of September 2008.

FEMSA also has packaging and logistics operations, which provide cans, glass bottles, crown caps, labels and refrigeration equipment to its core beverage operations.

A champion of corporate social responsibility

Since its inception in 1890, FEMSA has remained at the forefront of the beverage industry through innovation, performance and growth. Additionally, the company is a pioneer in Mexico in establishing policies focused on its employees, community development and environmental care.

As far back as 1918, FEMSA incorporated a social entity known today as SCyF, which promoted the development of its workers and their families. The original objective was to improve the standard of living of its people by providing them with food, medical services, a savings bank, discounts, sports, courses and scholarships. In 1945, the SCyF clinic was established to provide free medical care for the company’s employees at a time when the Mexican Social Security Institute did not exist.

During the 1950s, then President of Mexico, Adolfo Ruiz Cortines, inaugurated the Cuauhtémoc neighborhood in Monterrey with 1,318 houses for FEMSA employees and workers – another social initiative ahead of its time, before the creation of the Mexican Federal Housing Development Institute (Infonavit).

One of FEMSA's core educational contributions is the creation and ongoing sponsorship of the Instituto Tecnológico y de Estudios Superiores de Monterrey (Monterrey Tech), founded under the leadership of Don Eugenio Garza Sada, former CEO of Cerveceria Cuahutemoc, a brewery company where FEMSA's history began. At present, Monterrey Tech has 32 campuses throughout the country and academic centers in Mexico and other Latin American countries, as well as international offices in Asia, Europe and North America.

For the third consecutive year, the Mexican Industrial Chamber Confederation honored FEMSA with the Ethics and Values in Industry Award. This award is given to corporations that conduct business guided by ethical principles and values centered on human dignity, transparency and environmental conservation. Moreover, the Mexican Center for Philanthropy recognized all of FEMSA's businesses for their dedication to corporate social responsibility.

FEMSA's internal audit team

FEMSA's internal audit (IA) function has a matrix-process-oriented structure supported by offices in Argentina, Brazil, Colombia, Costa Rica, Mexico and Venezuela. It has a staff of approximately 120 auditors; about 25 positions are outsourced. The IA function charges its services to business units based on hours applied at a cost per hour authorized by the audit committee.

To maintain IA independence, all audit staff reports to José Gonzalez Ornelas, the chief audit executive. He reports administratively to the company's CEO and functionally to the board's audit committee. Ornelas is responsible for:

- Providing annual evaluations of the sufficiency and effectiveness of company processes with regard to controls and risk management, set forth under the mission and scope of work established
- Reporting significant issues related to the processes intended to control company and affiliate activities, including potential improvements for such processes, up to resolution
- Submitting periodic information on the status and outcomes of the annual audit plan and the sufficiency of human and material resources in the area
- Coordinating with and overseeing other control and monitoring areas in the company and external auditors

The IA team uses new technological tools to facilitate and increase effectiveness and efficiency of the risk assessment process, audit planning, corrective action follow-up and report generation work. Additionally, during the execution of fieldwork, analytical tools are used to identify risks, select samples, conduct control testing, and develop programs for fraud detection.

Among the tools used for such purposes are Direct Link and Server Edition for direct access to ERP databases; ACL Windows for data extraction and analysis; and SAP Auditing modules and tools such as Auditing Information System, Management of Internal Control, and Segregation of Duties Auditing. FEMSA also uses Oracle Auditing tools such as Oracle International Controls Manager.

"The use of new IT tools has been a strategic element in the recent transformation of the IA approach based on a business risk assessment," says Ornelas.

A period of tremendous growth

While FEMSA's core businesses are centered on soft drinks and beer, during the past three years its fast-growing chain of OXXO convenience stores and its packaging and logistics operations have accelerated the strategic growth of its core beverage businesses by enabling FEMSA to increase the availability of its products and achieve greater operational efficiencies.

Building on its leadership position as Mexico's largest and fastest growing modern convenience store chain, OXXO opened 716 new stores in 2007, for a total of 5,563 stores nationwide, and made plans to initiate operations in Colombia. As a leading vendor of beer, bread, snacks and soft drinks in

Mexico, the company remains on track to further expand its market penetration and deepen its integrated beverage coverage. By 2015, OXXO is planning to operate 12,000 stores.

At the same time, FEMSA has made significant investments in information gathering and processing systems that enable it to improve the efficiency and efficacy of its production, marketing and distribution processes. In November 2007, through a new joint venture company, Coca-Cola FEMSA and The Coca-Cola Company acquired in equal proportion 100 percent of the shares of Jugos del Valle, one of the leading juice producers in Mexico and Brazil. Both companies invited the rest of the Coca-Cola bottlers in Mexico and Brazil to participate in this joint venture.

Also during 2007, FEMSA announced the construction of two new plants – a brewery and a glass bottle facility – in Meoqui, in Mexico’s northern state of Chihuahua. In its first stage, the new brewery is expected to increase annual production 15 percent over FEMSA Cerveza’s current capacity in Mexico. The first stage of the glass bottle plant will have installed capacity of 700 million bottles per year, an increase of 54 percent over current levels. “Expected to begin operations in 2010, these investments will ensure that FEMSA’s growth in Mexico and in the United States is supported by adequate production capacity,” says Ornelas.

In June 2008, Coca-Cola FEMSA announced that it closed the transaction with The Coca-Cola Company to acquire its “Remil” franchise territory in Brazil. This territory includes the third-largest city in Brazil, Belo Horizonte, expanding the company’s position in this growing market by more than a third.

Key changes within the IA function

Recently, due to the complex technological environment prevailing at FEMSA, a new strategy was established to strengthen IT audits by creating a specialized IT audit staff. With this new team, the IT audit plan includes reviews covering the following areas:

- General controls
- COBIT domains
- Automatic controls and information integrity
- Security issues, such as system vulnerability and segregation of duties
- Fraud prevention and detection

“Since 2007, the IA function started reviewing main operating business processes at the company,” says Ornelas. “One aspect under review is a new audit approach based on a risk assessment using the COSO framework. Such reviews incorporate, as part of their regular scope, the control effectiveness testing related to the internal control certification process required by Sarbanes-Oxley 404.

“In addition, the IA function created a specialized area in charge of updating and developing its internal human resources,” Ornelas says. “Also, using a permanent task force, this area conducts periodic quality reviews in every IA location for the adherence to approved processes and quality standards for the function. It updates innovative processes for the IA activity. Furthermore, this particular department also practices quality assurance audits to the internal control areas of every business unit of FEMSA.”

A new practice – a centralized Shared Center Service – was also created to identify audit universes, test samples for the operating units, identify red flags exceptions and opportunities for further examination, and create aggregated reports.

“The objective of this specialized service is to reduce the amount of repetitive planning and reporting activities in every regional office so that the audit staff can dedicate most of its time to its core activity,” Ornelas says.

A new audit approach

To support these strategic changes, the IA team created a new “matrix-process-oriented organizational structure” in which audit regional managers and supervisors were assigned to specific operating processes in every geographic region and for every one of FEMSA’s business units. The managers and supervisors were grouped according to specialization of processes, such as manufacturing, commercial, distribution, retail and central processes such as procurement, marketing and human resources.

This new audit approach included a training program and a continuous professional development plan to reinforce the knowledge and skills required to conduct risk-based process audits and to interact in a multicultural environment.

“In times of constant change, such as the ones we are experiencing at FEMSA, a broad range of skills and expertise is critical to maintaining an effective internal audit function,” says Ornelas. Essential elements include in-depth knowledge of the organization’s industry and main business processes, technical understanding and expertise on risk-based audits, accounting academic background, intercultural skills, persuasion capability, and strong oral and written communication skills.

A new vision and mission

A new regulatory environment and recent changes in the company and the IA function have spurred a revision of IA’s vision and mission, which is now more holistic and broader in scope.

IA’s new mission is to evaluate, independently and objectively, the integrity, effectiveness and efficiency of FEMSA’s corporate governance system, mainly on those elements related to risk management and internal control, to detect opportunities for improvement, recommend and implement the necessary actions, and validate follow-up by management. “The central idea of the new vision is to transform our IA function as the benchmark in Latin America,” says Ornelas. “This was requested by the audit committee.”

Under its new mission, IA’s scope of work includes the following objectives:

- Company programs, strategic plans and objectives are achieved and risks are appropriately identified and managed.
- Various governance groups interact as needed.
- Significant financial, operative and managerial information is accurate, reliable and timely.
- All actions taken by owners, board members, managers and employees are in compliance with applicable policies, standards, procedures, laws and regulations, and the business ethics code.
- Communications received through the whistle-blowing system are subject to follow-up and resolution.
- Production and financial resources are acquired at the lowest possible cost, used efficiently and adequately protected.
- The organizational control process encourages quality and ongoing improvement.
- Significant legal or regulatory issues affecting the organization are recognized and addressed properly.
- As a benefit, opportunities to improve profitability and/or company image may be identified in the course of audits.

Corporate governance changes

FEMSA’s shares are listed on the Mexican Stock Exchange and the New York Stock Exchange; therefore, the company complies with the corporate governance standards established in the Mexican Securities Market Law and with the applicable provisions for foreign issuers contained in the Sarbanes-Oxley Act of the United States.

Under this new regulatory environment, an important part of FEMSA's mandatory audit committee duties are now supported by the IA function in issues such as:

- Coordinating its activities with external audit
- Overseeing the internal control activities
- Checking compliance with the business code of ethics and corporate policies
- Following up on the comments received in the whistle-blowing system
- Checking related parties and unusual transactions

To make this possible, FEMSA's audit committee regularly ascertains that the function's organizational structure is appropriate, that auditors have the necessary professional education and experience to perform their functions, and that the audit activity is carried out objectively and independent of management by complying with the professional standards that govern it.

Measuring performance

To measure and monitor its performance, for the past 12 years FEMSA's IA function has participated in GAIN, an international information exchange network managed by The Institute of Internal Auditors (IIA). FEMSA receives an annual report with benchmarking against the universe of participants in more than 35 countries, with those that belong to the beverages specialty group, as well as with a set of IA departments with a similar staff size. Additionally, in 2007, an external firm completed a quality assurance review for the IA team, providing feedback based on IIA standards.

As part of FEMSA's One Page System (its planning and performance system), Ornelas has established critical success factors, or annual objectives, for all IA personnel. These include performance indicators such as audit scope results, recommended actions implemented, savings generated, internal quality assurance results, audit committee evaluation, auditee evaluations, improvement projects advances, and more. All results are reviewed monthly. Based on these indicators, an annual performance assessment is made for promotions, salary increases and special incentives purposes.

FEMSA's audit committee also performs an annual evaluation of the IA function, providing feedback on a long list of issues, including:

- Understanding the audit committee and its chairman's expectations
- Understanding the organization's business and risk environment
- Adequacy of roles and responsibilities regarding the current organizational needs
- Quality of services
- Understanding the company's business issues
- Appropriate geographical coverage
- Competitive service cost vs. market price
- Delivery of value to the organization
- Skills and experience
- Independence from operations
- Timely and appropriate reports on significant business issues and fraud investigations
- Effectiveness and efficiency indicators
- Effective coordination with the external auditors
- Use of international best practices

Also, as an international best practice for the IA function, individuals responsible for audited business units must evaluate the IA service provided to them during the year. These assessments are sent directly to Ornelas for review. Content is strictly confidential and feedback of the aggregated results, along with recommendations raised, are provided to the audit staff to promote improvement projects. More than 500 evaluations are generated every year.

“At FEMSA there is a marked culture of orientation towards internal control within the organization, and users are aware that the responsibility for control is theirs, up to the point that it is considered an important part of their annual performance assessment and corresponding incentives plans,” says Ornelas. “This has created a more collaborative relationship with the IA function. Communication and quick response to all levels of the organization have raised our visibility and our image. In the latest quality assurance review, our IT team was described as ‘a high-credibility, respected team that contributes value to the organization.’ There is no doubt that the recent changes in the organization and in IA activity have reshaped the function, closing gaps of communication between parties and breaking former relational paradigms.”

Looking to the future

“In a long-term perspective, FEMSA’s goal is to deliver consistently profitable growth and strengthen its position as Latin America’s largest integrated beverage company,” Ornelas says.

With this in mind, he says the company’s strategy is to:

- Leverage its soft drink business’ diverse geographic footprint and unique distribution network.
- Spearhead positive change in the Mexican beer industry and turn around its newly acquired Brazilian beer business.
- Expand its beverage platform through its fast-growing OXXO convenience store chain, and create synergies and accelerate innovation.

“The main challenge the IA function faces in the near future is maintaining a sufficient organizational structure and state-of-the-art IT tools at a competitive market cost,” says Ornelas. “This will allow us to easily adapt to the changing needs of the organization, which include our new businesses, territories, operating processes and regulations. We also must enhance our risk-oriented activity, provide adequate geographic coverage, stay close to business management, and deliver consistency and quality in our service.”

Company Headquarters – France

Number of Countries Operates in – 120+ (many via agents)

Number of Employees – 10,000

Industry – Electronics and Communications

Annual Revenues – €\$1.6 Billion

Annual IA Operating Costs/Budget – Prefer Not to Disclose

Number in IA Function – 8

Number of Years IA Function Has Been in Place – 3

(since merger of Axalto and Gemplus)

*IA Director/CAE Reports to – Audit Committee Chairman,
Administratively to CFO*

Note: All of the above information is accurate as of December 31, 2008.

“In the end, internal audit is not like external audit. Internal audit focuses on the future of the company, staying ahead of change in order to guide the company for whatever is to come.”

– Pierre-Arnaud Cresson

Widening the audit scope at Gemalto

Gemalto is the worldwide leader in digital security, with a focus on smart cards and secure personal devices. The company is registered in the Netherlands and is listed on the Paris stock exchange, and operates in approximately 120 countries, with 24 factories and 10,000 employees worldwide. In 2007, Gemalto produced and personalized more than one billion microprocessor cards. Gemalto is a result of the merger of Gemplus and Axalto in 2006, two companies of the same size with the same worldwide activities and competitors.

The internal audit (IA) team at Gemalto has undergone significant change in recent years. Since 2006, it has increased in size from two to eight professionals, and has been coping with the merger and the resulting reorganization of IA departments. Pierre-Arnaud Cresson has been the director of IA at the company since February 2007. At the request of the audit committee, Cresson oversaw expansion of the audit team and is now in charge of a two-person team responsible for financial internal control.

Gemalto has several business units, including telecom; operations, such as research and development and manufacturing; and corporate functions, such as human resources and finance. The IA team focuses on internal control over financial reporting (ICFR), an emphasis formally established as an ongoing initiative in April 2008. In addition to the IA team, one IA manager and one ICFR manager report directly to Cresson, who, in turn, reports directly to the chairman of the audit committee.

“We operate as an external audit firm would,” says Cresson. “We use tools and technology, such as our own IA software from Paisley and a web-based tool for ICFR. We want to perform and be evaluated as a third party, so we measure our hours and the money we spend. Our aim is to obtain the certification of The Institute of Internal Auditors (IIA) in 2009, so that we can fully guarantee both the independence and the objectivity of our auditors.”

Key changes

When the IA team grew from two to eight people, its charter was rewritten on the basis of IIA standards and included an anti-fraud and an ICFR component. “Another change is that we are not only covering IA matters, but internal controls as well. I now also oversee all activities relating to fraud, ERM and risk-mapping,” adds Cresson.

Gemalto’s internal control steering committee meets every three months and oversees all aspects of control; the anti-fraud committee meets every two months. The internal control steering committee

consists of the CFO, the CAO, the group controller, a senior vice president in charge of a division within one of Gemalto's three business units, a high-level human resources representative, the legal counsel and Cresson. The anti-fraud committee for Gemalto consists of the heads of human resources, legal, security, IT and IA. "There is much more focus on internal control and anti-fraud today than ever before," Cresson says.

Adaptability and initiative

When he was building his team, Cresson says he was "looking for professionals who demonstrated adaptability and initiative." He recruited junior auditors with a financial background, senior auditors with accounting experience from big international firms, and managers with the same qualifications but with more experience. Training is targeted toward the most useful skills for the individual; for example, anti-fraud auditors participate in anti-fraud courses and training.

In Cresson's previous job, where he was the head of IA for a large organization, he dealt with all types of audits. However, at Gemalto he is currently concentrating on finance. "I have already started expanding our efforts," he says. "For example, we are now auditing the efficiency of some functions."

Cresson adds, "In the short term, we want to complete the implementation of all that we have started and become certified by The IIA in late 2009. In the long term, we will move away from our finance-only approach and perform more organizational audits, quality audits and projects audits."

IA methodologies

The primary audit methodology the IA team employs is risk-based scoping for the audit plan. "During an engagement, we develop a list of the inherent risks involved in any particular business area, and we speak with business owners who have a comprehensive knowledge of the entity to understand what they say are their top priorities," he says. "For every audited site, we define a materiality level and adapt ourselves to the site's size. Depending on the risks, we reduce our materiality level, which means we will audit more toward the lower level. This is exactly the approach an external audit firm would adopt."

IA also led a risk-mapping exercise – called enterprise risk assessment (ERA) – for the company, creating an inventory for every risk Gemalto faces and all related actions taken to manage the risk. This information leads to the development of the annual audit plan. "Every big site needs to be audited every three years, and a follow-up takes place one year later," Cresson says. "In cases where we may have riskier areas to audit, such as obsolete inventories or treasury problems, we audit on an as-needed basis. We present this information to our external auditors and to the audit committee."

One significant differentiator with Gemalto's audit group is that it systematically performs a balance sheet review. "Usually, people audit the process and stop there," he says. "We audit the process and analyze the balance sheet as well (giving the balance sheet a rating – A is perfect, then the rating decreases to B, C and D), and this completes the audit loop."

To measure IA performance, key indicators are monitored and reported monthly, including:

- Time spent per mission and time not spent on mission
- Number of days to issue a draft report
- Number of days to issue a final report

"We use rigid metrics. We can, ourselves, be audited at any time, and if you outsource your IA department certain criteria will be measured, and it will reveal how much time is spent per mission, as well as time spent on vacations, training and more," says Cresson. "We have to determine whether we spend too much or not enough time, and we can begin to understand that by measuring and benchmarking our efforts. We also measure the quality of our audit reports to ensure that management or the audit committee will not send it back for questions or disagreements."

Marketing the function

The IA team and its reports are widely recognized for their quality and reliability. “Our challenge now is to convince management to use our team more frequently than on imposed internal audits,” says Cresson. “I try to market our team; however, one lingering problem is that our team is very finance-oriented and not enough operations-oriented. I wish I had more discussion with nonfinance top management on a regular basis, so that I could see the risks and issues we are facing more clearly. We have to continue to market ourselves more aggressively, and one way to achieve this is to conduct one-on-one visits. We are hoping to widen our audit scope. To do this, things will have to change.”

Increasing the scope and effectiveness of audit

Increasing the size of the audit department, improving the skills and talents of the auditors, choosing audit missions more strategically, conducting ERA and focusing on anti-fraud activities have all drastically changed the scope and effectiveness of Gemalto’s IA team. “We were able to cut the fees of our external auditor by a significant percentage in just one year,” says Cresson.

He adds, “I also see myself as a recruiter for new talent and quality for the group – like an ‘agency’ for recruiting, training and helping auditors transfer out to the business after two years or so. I am against having auditors remain within the audit profession indefinitely. We want a mix of professionals, so that we never lose our focus on the business and we continue to stay abreast of business changes. We also value auditor diversity, with regard to nationalities, genders and more. We recruit business professionals, and train them on how to perform audits, and be rigorous, pragmatic and listeners, and then put them back into the business.

“In the end, internal audit is not like external audit,” Cresson says. “Internal audit focuses on the future of the company, staying ahead of change in order to guide the company for whatever is to come.”

The Microsoft logo is displayed in a bold, black, sans-serif font. It is positioned in the upper left quadrant of the page, partially overlapping a light beige silhouette of the United States map that serves as a background for the introductory text.

Company Headquarters – United States
Number of Countries Operates in – 100
Number of Employees – 91,000
Industry – Computer Technology
Annual Revenues – US\$60 Billion
Annual IA Operating Costs/Budget – US\$12.5 Million
Number in IA Function – 69
Number of Years IA Function Has Been in Place – 18
*IA Director/CAE Reports to – Functionally to CFO,
Administratively to the Audit Committee of the Board
of Directors*

Note: All of the above information is accurate as of June 30, 2008.

“We are becoming a more service-oriented business. This change in focus presents different risks to the business, and we are adjusting our function and capabilities in order to respond. Trust from our customers is critical to our company’s success, as our customers depend on us to reliably deliver high-quality, secure, uninterrupted services. As an audit department, we are anticipating the shifting risk landscape and transforming our strategies to help our business partners successfully execute their project plans.”

– Melvin Flowers

The integrated auditor at Microsoft

Microsoft’s 55 auditors and 14 fraud investigators report to Melvin Flowers, the company’s vice president of audit and chief audit executive. Flowers directs the Internal Audit (IA), Financial Integrity Unit (FIU) and Enterprise Risk Management Project Management Office functions. The IA team is headquartered at the company’s Redmond, Washington campus, with two regional IA teams located in Dublin and Singapore.

Like every other company in the technology industry, Microsoft has evolved over time. “We are becoming a more service-oriented business,” Flowers says. “This change in focus presents different risks to the business, and we are adjusting our function and capabilities in order to respond. Trust from our customers is critical to our company’s success, as our customers depend on us to reliably deliver high-quality, secure, uninterrupted services. As an audit department, we are anticipating the shifting risk landscape and transforming our strategies to help our business partners successfully execute their project plans.”

Strategic planning

To respond to the changing risk landscape, in 2008 the IA group developed a long-term strategic plan to guide the department’s annual investments and activities, linked with Microsoft’s key imperatives and strategies. The IA strategic plan defines a set of strategic initiatives that will enable the department to achieve its vision to be universally recognized as a driving force behind a culture of governance, accountability and execution excellence at Microsoft.

Because these strategic initiatives span several years, the IA team defined a series of annual initiatives, some of which are discussed below. The leadership team also defined a governance model for tracking progress and driving accountability through a dashboard and regular updates to a strategic plan steering committee.

Leveraging technology

Technology Enabled Continuous Assurance (TECA) is one of two major technology initiatives deployed by Microsoft’s IA team. TECA increases risk coverage through data analysis and enhances audit staff data analysis skills. Leveraging Access, Excel and SQL software, the TECA program has developed a rich set of data analysis queries that broaden audit and risk coverage and improve the company’s continuous assurance capabilities. Many areas are currently under TECA development, including expense account accruals analysis, logical user access review and audit issue resolution.

“Our TECA program will significantly change the way we perform audits, helping us to increase our reach and achieve more coverage. By using this technology, we are freeing our auditors to spend more time and effort on building relationships and expanding their advisory roles throughout the company,” says Julie Kwon, who occupies the newly formed position of professional practice group manager. Kwon reports to Flowers, and in this role she manages key department processes and programs, such as audit committee reporting, annual planning and risk assessment, quality assurance, learning, performance management and technology platforms.

“Auditweb is the other major technology initiative and is used for information management and workflow. Using Microsoft Office SharePoint technology, we developed a common portal to efficiently link auditors to workflow, documents and data. Auditweb is used to facilitate audit committee reporting, performance evaluations, view the audit plan and share common documents,” she says.

The integrated auditor

Another key initiative is the Integrated Auditor Program, designed to increase and optimize the audit team’s technical and functional competencies. This program defines common levels of experiences and proficiency. Every auditor self-assesses his or her level of competency in areas such as technology, privacy, data analytics, finance and sales channel operations. Minimum required proficiency levels are defined, and opportunities to build further expertise are identified based on individual preferences and departmental needs. Employees then build a development plan to increase their proficiency in a collection of areas.

The program is designed to increase auditors’ competencies, anticipate the skills needed to serve the business and ensure those competencies are appropriately developed in the team, thereby increasing IA’s value to the business.

The Integrated Auditor Program is connected with IA’s learning program and becomes the road map for “Learning Weeks,” which are held twice a year. Learning Week is a time for this geographically diverse organization to come together for training. During the week, several learning tracks take place. They are designed to increase the understanding of Microsoft and develop technical and functional competence aligned with the Integrated Auditor Program, as well as core audit skills.

“Because of the Integrated Auditor Program, we are able to target our training to specifically increase competencies in areas we know will make the greatest impact to our staff development,” says Kwon.

Performance measurement

Performance is measured against a balanced scorecard for which the IA team is accountable. The scorecard focuses on three areas: program excellence, talent management and strategic plan execution. From these three areas stem specific, detailed targets. “These metrics hold us accountable to the audit committee for performing at the highest standards,” says Kwon. “Each year, we discuss our scorecard with the audit committee and CFO and determine the right definitions for green, yellow and red. As a result, we know mutually what the expectations of us are, and we hold ourselves accountable to meeting those expectations.”

Challenges ahead

Implementing the long-term strategic plan is top of mind for Flowers, Kwon and Microsoft’s IA management team. “The strategic plan is all about enabling us to have a greater impact on our business,” Flowers says. “Achieving the strategic plan will enable the IA team to partner with the company in successfully executing their strategies.”



PRUDENTIAL

Company Headquarters – United Kingdom
Number of Countries Operates in – 15
Number of Employees – 15,000 and 410,000+ Agents
Industry – Financial Services
Annual Revenues – GBP£20.1 Billion
Annual IA Operating Costs/Budget – GBP£16 Million
Number in IA Function – Approximately 130
Number of Years IA Function Has Been in Place – Not Certain
IA Director/CAE Reports to – Functionally to Group Audit Committee, Administratively to Group CFO

Note: All of the above information is accurate as of December 31, 2008.

“Traditionally, internal auditors have given assurance to the board, line management and regulators. In the future, having a visibly effective assurance function will be important to other external stakeholders, notably investors and customers. I think boards will want a single view – not bits of information from disparate sources about the control environment and the governance structure of the organization and how well risk is managed. The board will want someone pulling it all together. I want to be on the forefront of that movement.”

– Marcus Adams

Group-wide Internal Audit team gives Prudential a bird's-eye view of risk

Prudential plc is an international financial services company specializing in insurance, pensions, retail investments, institutional fund management and property investment.

The company is structured around four main business units: Prudential UK; Prudential Corporation Asia, the leading European-based life insurer in Asia; Jackson National Life Insurance Company, one of the largest life insurance companies in the United States; and M&G, the company's global asset fund manager. These four business units are supported by central functions responsible for strategy, cash and capital management, leadership development and succession, reputation management, and others. Worldwide, Prudential has more than 21 million customers, policyholders and unit holders.

Group-wide Internal Audit

Prudential established its Group-wide Internal Audit function in 2006 to help the company achieve a big picture, rather than a per-process, view of the risk and control environment throughout the organization. Marcus Adams took on the role of Group-wide Internal Audit director – the only global or group-wide function in Prudential – after leaving British Telecom in 2006. He has more than 25 years of experience in auditing and risk management and has worked in a wide range of industries.

The Group-wide Internal Audit department currently has 117 staff; that number has remained constant since the department's inception two years ago. Audit directors lead teams based in each of the major business units, reporting directly to Adams, who reports administratively to the group chief financial officer and functionally to the group audit committee. In addition, a team of 16 is based at the head office and leads specialist technical areas such as IT audit and program assurance. This team also undertakes quality assurance reviews and develops best practice tools and methodologies.

Prudential has embraced significant change in recent months. Notably, the company entered a strategic relationship with Capita, the market leader in the life and pensions outsource market in the United Kingdom. “This was a mammoth exercise,” says Adams. “We moved many people into Capita. Group-wide Internal Audit was closely involved in the whole process and, in particular, how we manage those relationships and how to establish governance.”

Additionally, Prudential established PGDS, the company's global data center and information technology (IT) team that supports its international businesses. "Prudential had hardware scattered around the world," Adams says. "The company decided to consolidate into a single data center, with a backup site. To do this, we had to determine how to migrate the hardware and all the applications from London to Michigan. We used a technology called *Thin Client* that provides flexibility, portability and ease of use for all our employees. I open my desktop in London, a full suite of Windows programs appears, my key strokes are recorded, and that information goes to Michigan. We can share screenshot information of what is happening in the United States and around the world. All applications reside in a single location, not in individual desktops. The development of shared data centers in the United States and deployment of *Thin Client* IT architecture has been a major development for us."

Group-wide Internal Audit has been involved throughout the Capita and PGDS change programs, providing ongoing assurance to management on all program stages. "We have advised on the overall program management, assessed the risks to and likelihood of successful delivery, and undertaken detailed post-delivery reviews," he says.

In addition to *Thin Client*, the IA team uses common systems in all locations: *AutoAudit* for work paper management and *IssueTrack* for action management, *Retain* for staff scheduling, and *SharePoint* for the team intranet. *AutoAudit*, in particular, has been fundamentally important in moving the established teams to a common audit methodology and enabling quality assurance and consistency throughout all of the audit work performed. Internal auditors have also produced several webcasts available over the company intranet to communicate key messages.

According to Adams, "Before the establishment of Group-wide Internal Audit, each business unit had its own IA function and reported to that unit's CEO, each using different methodologies, including planning, execution and reporting. Our regulator was uncomfortable with this model and wanted to help us evolve our IA function to an appropriate standard so that we could get a comprehensive view of our function and the organization, including its controls and governance effectiveness." Group-wide Internal Audit now manages Sarbanes-Oxley Section 404 testing at the company's headquarters and coordinates the delivery of all Section 404 programs.

To assess the effectiveness of the new function, Adams and his team asked an independent consultancy firm to undertake reviews. The first review took place in the fourth quarter of 2006, with a follow-up review in the fourth quarter of 2007. The review included visits and file evaluations at each location and an assessment of every aspect of the operations against international standards and Prudential's financial services peer group.

"It has been a two-year journey to achieve a single standard," Adams says. "Some of it was about audit methodology, some of it was about audit technology. Most of it was about people and reporting structures."

Team training and development was an important initiative. During its review, the consultants determined that Prudential was adequate, but not best practice. "We needed to re-examine how we planned and executed audits, reported findings, managed relationships with key stakeholders, developed staff and measured our performance," Adams says.

One of the first changes implemented was in the reporting structure. "Now we have an audit director, who reports to me, assigned to each business unit," he says. "This emphasizes that we are group-wide and cross-functional, and that we are all working toward the same standards. For the first time, I am able to get a view of the control environment across the whole organization."

According to Adams, audit clients within Prudential began looking very carefully at the service they were getting from the Group-wide Internal Audit function the first year. "We have been able to demonstrate excellent service, a dedication to understanding key business risks, and now, access to a far greater pool of resources," he says.

Developing the team

To develop his team, Adams targets three skill sets:

- Audit technical knowledge
- Soft skills, such as report writing, communication and negotiation
- An understanding of the business

“The last point is critical,” he says. “For auditors to be effective, they must understand not just the mechanics of the audit process but the business itself, including industry pressures coming from regulators and competitors, and the entire business environment in which Prudential operates. We must be business-savvy. We take risks, but we should take measured and known risks. I want our auditors to be true business partners. If one of our auditors is hired by another business unit, I want him or her to run it as we run an audit.”

A structured development program with rigorous appraisals facilitates the development process. Every auditor has a personal development plan that focuses on key elements for success and areas for improvement. “Group-wide Internal Audit is seen as a ‘best practice’ example within Prudential for fast-track development of high achievers, community building, and secondments and networking across business areas,” Adams says. “A recent review of every area that reports to the CFO concluded that we should carry on ‘as is.’”

The “transformation program” for Group-wide Internal Audit ran from 2006 to the summer of 2007. It was managed by an experienced program manager seconded to the team. These efforts were recognized by the external review; the conclusion being that the function had attained at least a “good practice” rating in every area assessed and “best practice” in many areas.

Goals and objectives

A key objective for Adams is the delivery of the agreed-upon risk-based IA plan for 2008. “We aim to provide reliable, objective assurance to the group audit committee and to our other key stakeholders on areas of key risk and Prudential’s ability to deliver strategic goals,” he says. “We are actively working to improve our reporting to key stakeholders – moving away from progress reports and individual audit findings. We want to identify the real underlying issues, so instead of focusing on processes, controls and symptoms, we will identify the causes, outcomes and cultural issues that underlie the former.”

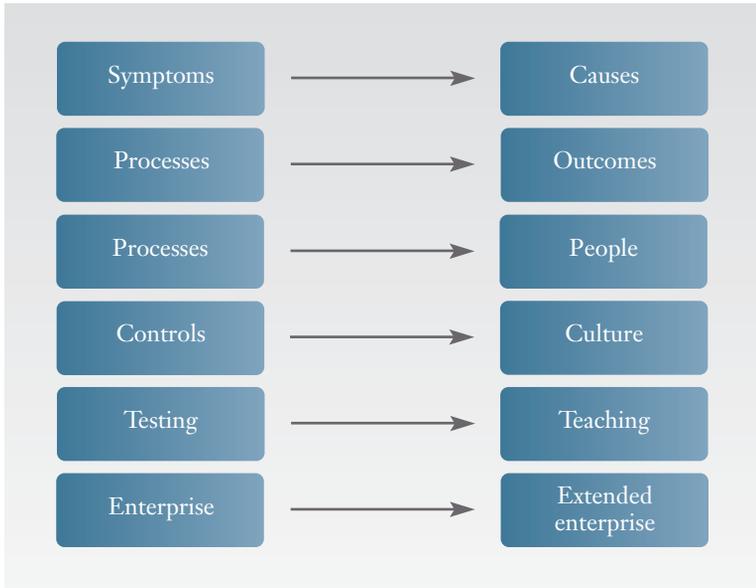
All of these changes have given the Group-wide Internal Audit team a much clearer definition and idea of its mission. “We have worked hard to get the message across,” Adams says. “We are jointly liable for the delivery of our product. We don’t operate in silos anymore. For example, we recognize that if we don’t have the right amount of resources in Asia, we need to work jointly to solve the problem.”

More important, Adams says, the focus has changed. The team is now more capable of identifying the significant risks in the organization and in key strategic initiatives. “Members of our board want one view of how well this organization manages major risks. Previously, the board had been receiving information from multiple sources – audit, compliance, risk management. Now we are able to achieve a single, comprehensive viewpoint and track the deep cultural aspects that we are finding, such as, do we have the right people in places? Communicating key issues to the board of directors is critical.”

As a result, the team’s relationship with leadership is strong; internal auditors are viewed as business partners. “Our increased focus on ensuring that our auditors are suitably knowledgeable about the business has enhanced our reputation. We have seen a significant number of our people move into senior line management positions over the past two years,” Adams says.

On the forefront of audit evolution

What will assurance look like in the future? For Adams, the movement is along these lines:



Source: Prudential

According to Adams, the main challenge for the IA industry will be to develop and evolve the nature of assurance provided to internal and external stakeholders. “Traditionally, internal auditors have given assurance to the board, line management and regulators. In the future, having a visibly effective assurance function will be important to other external stakeholders, notably investors and customers. I think boards will want a single view – not bits of information from disparate sources about the control environment and the governance structure of the organization and how well risk is managed. The board will want someone pulling it all together. I want to be on the forefront of that movement.”

TATA MOTORS

Company Headquarters – India

Number of Countries Operates in – 7

Number of Employees – 23,000

Industry – Automotive

Annual Revenues – US\$8.9 Billion

Annual IA Operating Costs/Budget – US\$2.5 Million

Number in IA Function – 45

Number of Years IA Function Has Been in Place – 35

IA Director/CAE Reports to – Functionally to the Chairman of the Audit Committee, Administratively to the Managing Director

Note: All of the above information is accurate as of March 31, 2008.

“One major upcoming challenge is developing the ability to manage the geographic spread of the company both in India and overseas. Within India, we had three large plants, and in the last two years we have added three more plants in addition to plants abroad, so our work is now spread out. This is a challenge from an auditing and assurance standpoint.”

– Abhijit Gajendragadkar

Managing global audits at Tata Motors

Founded in 1868, India-based Tata Group is a rapidly growing business group with significant international operations and approximately 350,000 employees worldwide. Estimated revenues in 2007-2008 are US\$62.5 billion (approximately Rs 251,543 crore), of which 61 percent is from business outside India. The Tata name has been respected in India for 140 years for its adherence to strong values and business ethics.

The business operations of the Tata Group currently encompass seven business sectors: communications and information technology (IT), engineering, materials, services, energy, consumer products and chemicals. The group's 27 publicly listed enterprises have a combined market capitalization of some US\$60 billion – one of the highest among Indian business houses – and a shareholder base of 3.2 million. The major companies in the group include Tata Steel, Tata Motors, Tata Consultancy Services (TCS), Tata Power, Tata Chemicals, Tata Tea, Indian Hotels and Tata Communications.

Established in 1945, Tata Motors Limited is India's largest automobile company. It is the leader in commercial vehicles in each segment and among the top three in passenger vehicles, with winning products in the compact, midsize car and utility vehicle segments. The company is the world's fourth-largest truck manufacturer and the world's second-largest bus manufacturer.

Tata Motors has more than 4 million vehicles on Indian roads. The company and its 23,000 employees are guided by the vision to be “best in the manner in which we operate, best in the products we deliver and best in our value system and ethics.” Through subsidiaries and associate companies, Tata Motors is engaged in engineering and automotive solutions, construction equipment manufacturing, machine tools and factory automation, computer applications and automotive retailing. It has a strategic alliance with Fiat, and the company's commercial and passenger vehicles are already being marketed in several countries in Africa, Europe, the Middle East, South America, South Asia and Southeast Asia, with a franchisee and joint venture assembly operations in Bangladesh, Kenya, Russia, Senegal and Ukraine.

Internal audit at Tata Motors

Abhijit Gajendragadkar has been the chief internal auditor for Tata Motors for almost five years, a role that includes internal audit (IA) and enterprise risk management (ERM) oversight. Additionally, he is the chief ethics counselor of the company. Gajendragadkar reports to the managing director and chairman of the audit committee, and manages a group of 45 internal auditors who audit Tata Motors and its nine subsidiaries.

Under the Indian accounting system, each subsidiary's accounts are presented separately. Tata Motors is a NYSE-listed company, and the subsidiary accounts are consolidated as one entity under U.S. generally accepted accounting principles (GAAP). "A major change for us after the NYSE listing is that we have expanded our audit work to these subsidiaries," says Gajendragadkar. "We audit a broad mix of businesses – commercial vehicles, passenger vehicles, construction equipment, IT and auto financing. Our 45 auditors are currently working from three Indian locations."

Auditing in a time of change

Tata Motors' IA team is divided into four groups: One performs audits of projects of capital spend, new product development processes and risk management. Another looks at supply chain and IT audit issues. A third group explores finance-related audits, while a fourth specializes in sales and marketing.

Aside from the global economic downturn that clearly has had an impact on the world's automobile industry, the most recent significant challenges for Tata Motors include:

- Large capital investments for revitalizing product and manufacturing capabilities
- Continued introduction of new products covering both commercial vehicles and passenger cars
- Global spread
- Development of the "Nano" small car
- Acquisition of Jaguar Land Rover

In response to these challenges, IA has introduced many changes, such as:

- Expanding the coverage of audit to business processes such as new products, capital spend and human resources.
- Standardizing the audit approach across locations through a formalized "Eight-Step Audit Process." (Gajendragadkar says, "This process describes the steps to be taken, as well as the deliverables. An important aspect of standardization is the development of checklists for all the processes we are auditing; checklists that include controls as part of Sarbanes-Oxley that are related to both finances and general effectiveness. All auditors across locations use these checklists.")
- Creating a common database of audit checklists.
- Monitoring audit recommendations. The company has implemented a self-assessment process to confirm that audit recommendations are implemented.
- Implementing an anti-fraud program.
- Sharpening the focus on technology skills. ("To sharpen this skill, we have encouraged the use of ACL, which helps us download huge amounts of data and find exceptions," says Gajendragadkar. "As a company in the engineering business, we recognize that the volume of our transactions is quite large. A tool such as ACL helps us in sifting through the data.")
- Implementing control self-assessment methodology for audits, which is now an integral part of the company's assurance process.

Gajendragadkar says the first qualities he looks for in an auditor in these times of change are integrity and a willingness to take a stand for what is right. He also seeks skills and abilities like creative thinking, communication, analytics and business knowledge. Gajendragadkar uses a balanced scorecard approach to measure audit work, focusing on the following:

- IA outcomes and output, such as audit reports
- Process improvements and innovation within IA
- Customer feedback
- Productivity of people, managing employees and guiding them on their career path

Managing audit globally

“One major upcoming challenge is developing the ability to manage the geographic spread of the company both in India and overseas,” Gajendragadkar says. “Within India, we had three large plants, and in the last two years we have added three more plants in addition to plants abroad, so our work is now spread out. This is a challenge from an auditing and assurance standpoint.”

He continues, “The second challenge is the pressure most companies around the world recognize today – doing more with less. Productivity improvements will need to be enhanced in the next one or two years.

“One positive aspect of our department is that we enjoy the solid support of the audit committee and senior management,” says Gajendragadkar. “That is a very big differentiator for us. The quality of work that we are able to do and the kind of support we get during our very difficult audits say a lot about the way senior management views the IA team. Our senior management team looks at any audit finding as an improvement opportunity. The focus of internal audit is therefore on overall improvement in the quality of corporate governance to meet the challenges posed by the continued growth and geographic spread of Tata Motors.”



Unilever

Company Headquarters – United Kingdom/the Netherlands

Number of Countries Operates in – 100

Number of Employees – 174,000

Industry – Consumer Products and Retail

Annual Revenues – US\$59.5 Billion (€40.5 Billion)

Annual IA Operating Costs/Budget – US\$29.4 Million (€20 Million)

Number in IA Function – 82

Number of Years IA Function Has Been in Place – 78

IA Director/CAE Reports to – CEO and Chairman of the Audit Committee (double reporting line)

Note: All of the above information is accurate as of December 31, 2008.

“Our biggest challenge is, of course, the change in the risk profile of our business. We have robust processes in terms of audit methodology, and accessing, retaining and returning resources to the business. At the moment, the global economic environment is going to be a challenge for all businesses, and we need to make sure we remain aware of and stay closely in touch with emerging changes in our risk profile.”

– Alan Johnson

Corporate audit at Unilever: Responding to change

Unilever is a global consumer goods giant with hundreds of consumer brands spanning 14 categories of home, personal care and food products. Unilever’s well-known brands include Lipton, Knorr, Dove and Omo, as well as local brands such as Blue Band and Suave.

In 2005, Unilever restructured its business model to align more closely with its three regions – Europe, Asia/Africa and the Americas – and it also created global categories. This change prompted the corporate audit group, led by Alan Johnson, to include global categories as part of its unit universe, taking a broad look at risks and controls across the business. Within Unilever, countries have their own control functions, which are part of the line management’s responsibility for monitoring operational controls; they are the “first line of defense,” and the corporate audit function is independent of these business operations. The regional and category leadership teams, together with the Unilever executive leadership team, represent the second line of defense, while corporate audit and the external auditors can be considered a “third line of defense.”

“In 2002, we had 132 internal auditors,” says Johnson. “The number has been reduced significantly, mainly because we now take a risk-based approach to what we audit. The reduced number also reflects the fact that within the business we have improved the company’s internal control frameworks – including the management self-assessment and positive assurance processes, and the Sarbanes-Oxley work. With robust self-assessment processes in place, we take a view regarding the amount of work we need to do in the financial reporting areas.”

Johnson reports to Unilever’s chief executive and to the audit committee, which consists of four independent nonexecutive directors. The 82 professionals in the corporate audit group are located in Europe, Asia and the Americas, and all report to Johnson. “Our people do not operate out of any one of those three centers. Our auditors are all professional managers from the business who can, if they choose, remain in their home base and travel extensively, probably up to 70 percent of the time.”

The group represents more than 25 nationalities, speaks more than 30 languages and comes from a wide range of business functions, including finance, supply chain, human resources, information technology (IT), legal, marketing and customer management. “We are a very diverse group, and we span every function of the business,” Johnson says.

Responding to change

The 2005 change in Unilever's corporate structure to a three-region approach, combined with the creation of global categories, led to an increase in the audits of the marketing and customer development processes. However, the most significant change for corporate audit was a shift from single function resourcing, primarily in finance, to a multifunctional resourcing structure, attracting managers from every part of the newly structured business.

“When I came to this role in early 2005, more than 90 percent of our resources came from finance,” says Johnson. “Unilever changed significantly in 2005, which required us to revise the mix of functional expertise within the corporate audit group. We needed to mirror the new global structure and scale up our capabilities, particularly in brand management, marketing and customer management.”

Another important change has been evolutionary: a gradual improvement in risk assessment throughout the worldwide business areas. “We are using better tools and processes, and using them more consistently across the Unilever audit world,” says Johnson. “We scope out audit work before dedicating time in the field, which results in less, but more focused and effective, field time. Our audit process involves in-depth unit risk assessments, which are completed two months from the time we conduct the fieldwork. This allows us to scope and define the work more sharply. We found this was necessary to provide the same or even a higher level of assurance with fewer people.”

Additionally, a corporate audit alumni club was introduced two years ago. It is a network of all the professionals who have worked in the corporate audit group in recent years, including former Unilever colleagues. “What we have today was built by those who came before us,” Johnson says. “We are here to manage their legacy, and we realized that there are many ambassadors in the business, and we should access that great talent.”

Audit leadership and well-being

The six-person audit leadership group, led by Johnson, is on the forefront of managing audit- and business-related change at Unilever. Audit leadership members are responsible for audit methodology and processes, including audit reporting, and the global audit resources. “We challenge ourselves,” Johnson says. “We regularly benchmark with other audit departments and are pleased with our progress. We assessed our effectiveness using an external independent body last year, and we were very satisfied with how we are performing. The findings were presented to both the Unilever executive leadership team and the audit committee.”

Corporate audit has also introduced a “Well-Being Program” for audit managers to make sure they strike the right level of work-life balance and avoid burnout or excessive disruption to their family life. “We help them manage travel, recovery [from travel], nutrition and exercise to make sure that our people are able to be effective at work and have a balanced home life as well,” Johnson says. Everyone who has joined the corporate audit group in the past 15 months has participated in a three-day program, run by a group called TIGNUM, which offers specific training and ongoing support. “The program is comprehensive, physical and psychological,” he says.

“We started this program in September 2007 with our extended leadership team – a group of about 20. We then asked our regional vice presidents to run the same program for their regions. TIGNUM shaped this program for us, and has also crafted a two-day program for the global travelers. We are committed to providing it to everyone who joins our department.”

According to Johnson, the Well-Being Program has “absolutely transformed” the team in terms of quality of work and commitment from each auditor. “I am much more careful about what I eat, I make time for exercise, and allow myself adequate recovery time when I travel,” he says. “Quality people are scarce. It's important to really care about them. We need highly motivated people who

enjoy what they do. With our resourcing model, 90 percent of our people come from the business and go back to the business after two to four years. We want them to go back enriched by the experience they gain in audit and view it as part of their future leadership development.”

Audit skills and mission

Since the corporate audit group hires functional, rather than audit, professionals, it is imperative that they have a clear understanding of risk management and a strong analytical competency. Self-confidence, integrity and the ability to draw conclusions and make decisions when presented with complex information are also high on Johnson’s list of priorities for his auditors. At the audit manager level, he looks for individuals with six to eight years of business experience. “We are part of talent and leadership development, grooming future leaders for the company,” he says.

While its secondary objective is to develop talent, the primary mission of corporate audit is to provide independent assurance to the executive team and board of directors that all major risks in the business are managed and that an appropriate control framework is in place to minimize adverse risk or the impact of risk. Three years ago, the corporate audit group examined its core activities and the rationale behind them to articulate the group’s core mission. “We did some brainstorming and came up with ‘protecting the corporate reputation of Unilever.’ We want to make sure our company has the highest reputation so that it has the freedom to operate without the burden of excessive regulation. We only achieve that when we demonstrate that we are a responsible corporate citizen. We provide an independent view of the business, identify and share best practices, develop future leaders, and champion principles and standards of corporate behavior,” Johnson says.

Knowledge networks

The corporate audit group uses a balanced scorecard approach, including quarterly updates and leadership meeting discussions, to measure the performance of its audit plan. Additionally, a “knowledge network” exists in audit for each function: finance, supply chain, human resources, IT, marketing and customer management. These knowledge networks consist of auditors who meet, either in person or virtually, several times each year. They discuss developments within each of the functional areas to engender the highest level of understanding, develop up-to-date audit guides, provide support, and offer guidance regarding the suitability of audit opinions.

“Our audit managers churn every two to three years, so we need robust guides to help auditors in the field,” Johnson says. “We achieve this through our functional knowledge networks, each of which is led by an audit director in the functional area. It is our way of professionally coordinating knowledge management.”

Audit relationships

The relationship between the corporate audit team and Unilever executive leadership is strong in the sense that auditors come from and return to the business. At the same time, corporate audit maintains its independence, so the relationship is respectful, but effective. “One of the things we measure is the success in placing our people back into the business,” says Johnson. “It’s a virtuous circle. If we can get good people in – which we can – and develop them – which we must – and place them back in the business – which we should – that generates more interest in our team, resulting in more people who want to join us. Therefore, we look at placement, as well as resource losses, and we continuously measure whether we are meeting our objectives. Our surveys and assessments tell us how our auditors feel about working in corporate audit. These assessments are web-based and managed by a third party to ensure total independence.”

Challenges ahead

One of the most significant challenges facing internal audit departments around the world is finding and retaining adequate audit resources; Johnson's team is fully staffed, and he believes it will remain so for the foreseeable future.

“Our biggest challenge is, of course, the change in the risk profile of our business,” he says. “We have robust processes in terms of audit methodology, and accessing, retaining and returning resources to the business. At the moment, the global economic environment is going to be a challenge for all businesses, and we need to make sure we remain aware of and stay closely in touch with emerging changes in our risk profile. Other than that, we have outstanding support from the audit committee and good relationships with management. Our audit strategy is sound, and leadership is good.”

Currently, Unilever's corporate audit alumni club has about 100 members worldwide. This “family” of ex-auditors provides ideas and support, scouts potential resources and counsels those seeking to return to the business from corporate audit. According to Johnson, when they return to the business, they liken it to coming out of the army. He says corporate audit is seen as a highly intense period in their lives – a time of shared experiences. To help with their transition, Johnson is developing an off-boarding program.

“I have a passion for the development of our auditor colleagues, both whilst in audit and after they have returned to the business,” Johnson says. “The most important brand in Unilever Corporate Audit is our people.”



UnitedHealth Group®

Company Headquarters – United States

Number of Countries Operates in – Prefer Not to Disclose

Number of Employees – 75,000

Industry – Healthcare

Annual Revenues – US\$81 Billion

Annual IA Operating Costs/Budget – Prefer Not to Disclose

Number in IA Function – 100+

Number of Years IA Function Has Been in Place – >15 years

IA Director/CAE Reports to – Functionally to Chairman of the Audit Committee of the Board of Directors, Administratively to EVP and CFO

Note: All of the above information is accurate as of December 31, 2008.

“Changes in the healthcare industry will continue, and UHG’s proactive response to these changes will be imperative to the company’s continued success.”

– Christopher Paulison

Internal audit transformation at UnitedHealth Group

UnitedHealth Group (UHG), ranked 21st in the 2007 FORTUNE 500, is the largest single health carrier in the United States, and a recognized leader in the health and well-being industry. The organization’s mission is to:

- Seek to enhance the performance of the health system and improve the overall health and well-being of the people UHG serves and their communities.
- Work with healthcare professionals and other key partners to expand access to high-quality healthcare so people get the care they need at an affordable price.
- Support the physician/patient relationship and empower people with the information, guidance and tools they need to make personal health choices and decisions.

Through six businesses – UnitedHealthcare, Ovations, AmeriChoice, OptumHealth, Ingenix and Prescription Solutions – UHG serves the entire spectrum of healthcare participants: individual consumers, employers, governments, commercial payers and intermediaries, healthcare providers – including hospitals, clinics, physicians and other caregivers – and pharmaceutical and medical device manufacturers. UHG serves more than 70 million individuals and operates in all 50 states and internationally.

UHG is headquartered in Minnetonka, Minnesota, where Christopher Paulison is the general auditor. He oversees a group of more than 100 third-party and in-house auditors in three areas under Business Risk and Controls (BRC): Internal Audit (IA), Business Risk Management (BRM) and Sarbanes-Oxley.

The road to transformation

UHG has been a company of dramatic growth. From 1996 to 2008, the company expanded from US\$10 billion to US\$80 billion in revenue through acquisition, diversified product mix and organic growth. Beginning in 2006, the company began making substantial improvements in a broad range of corporate controls and governance practices, including risk management.

Paulison saw this commitment to internal audit at UHG and joined the company in December 2007. Applying his extensive experience in transforming large internal audit functions, Paulison’s first step was to meet with key stakeholders to understand expectations and begin to define the path to change.

Individual meetings were held with the full senior management team of more than 30 executives (one-third of whom were new to their roles) and collectively with the full board of directors (including an audit committee composed of two-thirds new members).

These initial meetings were helpful not only to understand expectations, but also to build even greater awareness of and support for engagement in the new members in the risk assessment, internal audit planning, reporting and overall process. These meetings also formed the basis for relationship building, as the BRC team sought to become trusted business advisors to UHG's management and the board.

Creating a world-class team

Historically, the UHG IA function had been fully outsourced to a third party, atypical for a company of this size. Working with management and the audit committee, BRC set out to balance the execution workload. "There are tremendous benefits to finding the most effective balance between in-sourcing and outsourcing," Paulison explains. "The outsourced component brings hard-to-find subject-matter and industry expertise, significant institutional and audit knowledge, talented audit competency, and a self-review mechanism. The in-source component builds internal bench-strength, which is important in growing audit and risk professionals within our department, as well as acting as a feeder of talent for other departments within UHG."

Paulison adds, "With more work in-sourced, we can better manage cost and apply more audit hours where needed. The best practice audit/risk function is the one that finds this balance and applies it to its fullest benefit. We apply a one-team concept. The internal and outsourced team share a common set of goals, and the auditees see this cohesiveness and understand that we are a truly integrated team."

Risk convergence

There was a need to improve the coordination of risk-related functions – both within and outside the BRC group. Initial focus was placed on improving the coordination within BRC. The BRM team is composed primarily of top-tier MBAs who had external consulting experience prior to joining UHG.

BRM has a two-fold mission:

- Facilitate a quarterly risk assessment that involves more than 600 people throughout UHG, as well as a number of outside parties, on the topic of emerging/external risk. The emerging/external risk assessment component is actually performed daily by BRM (with weekly summaries).
- Assist management with special projects. BRM's risk assessment drives the IA plan. It indicates which areas of the company are ready for audit, and which are better suited to be a BRM "special project" until reaching a more steady state. Because the emerging/external risk assessment component is performed daily – and it involves regular contact and coordination with business management as needed, on a risk basis – there is a "real-time auditing" component in place at UHG.

The BRM team works on special projects to provide insight into changing process and functional areas. This insight not only helps process owners and executives manage risk, but also provides valuable information that UHG's IA team can use in its own audit planning. Sarbanes-Oxley work also stems from – and feeds – the risk assessment process. Entity-level, fraud risk and AS5 controls are assessed and tested in conjunction with the risk assessment activity, and certifications are made quarterly by varying levels of management in conjunction with these assessments. A shared pool of resources across the three BRC areas provides diversity in work experience. This is the basis of UHG's in-house rotational program across the three areas. Sharing talent also helps the company better manage costs.

Coordination improved between BRC and the other risk-related functions outside of BRC as well. Stakeholder needs became known and reporting responsibilities became clear. Regular coordination meetings were established at multiple levels within each of the risk-related functions. Synergies were identified, and cost savings continue to be achieved through the convergence of risk-related functions.

Back to the basics

As UHG focused on improving governance, oversight and internal control, it became important to bring a more traditional auditing approach to UHG. That approach, which aligns to the quarterly risk assessment, calls for increased substantive testing in key operational areas. The results of the team's work have been instrumental in educating process owners, management and other key stakeholders about where attention and change is needed at the process- and transaction-level.

"Producing carefully, evidence-based audit results is the best way to validate a given risk assessment," explains Paulison.

Building relationships

A high priority was placed on the need for BRC to meet with UHG's management team members on a regular and routine basis. "We make sure our calendars are always full of touch-point meetings with executives, members of line management and key process owners," Paulison says. "We make sure to attend all relevant operational meetings to understand the direction the business is moving. We also don't lose any time getting to know new members of the management team or the board."

He adds, "There is no better way to gain an understanding of the risk and control environment than to have regular discussions with management about their objectives and the status of those objectives. It is so important to build these relationships and establish and maintain credibility. It is the best way to add value as a true business advisor and provide the quality independent assessment the audit committee requires."

Looking back, looking ahead

Key stakeholders at UHG agree that the proper groundwork has been set for effectively transforming IA and its related areas, and these stakeholders look forward to seeing the organization continue its upward momentum related to effective management of the risk and control environment.

"There is still much more to come," Paulison says. "Changes in the healthcare industry will continue, and UHG's proactive response to these changes will be imperative to the company's continued success."

About Protiviti Inc.

Protiviti (www.protiviti.com) is a global business consulting and internal audit firm composed of experts specializing in risk, advisory and transaction services. We help solve problems in finance and transactions, operations, technology, litigation, governance, risk, and compliance. Our highly trained, results-oriented professionals provide a unique perspective on a wide range of critical business issues for clients in the Americas, Asia-Pacific, Europe and the Middle East.

Protiviti is proud to be a Principal Partner of The IIA. More than 1,000 Protiviti professionals are active members of The IIA, and these members are involved with local, national and international leadership to provide thought leadership, speakers, best practices, training and other resources that develop and promote the internal audit profession.



Protiviti has more than 60 locations worldwide and is a wholly owned subsidiary of Robert Half International (NYSE symbol: RHI). Founded in 1948, Robert Half International is a member of the S&P 500 index.

Internal Audit and Financial Controls

We work with audit executives, management and audit committees at companies of virtually any size, public or private, to assist them with their internal audit activities. This can include starting and running the activity for them on a fully outsourced basis or working with an existing internal audit function to supplement their team when they lack adequate staff or skills. Protiviti professionals have assisted hundreds of companies in establishing first-year Sarbanes-Oxley compliance programs as well as ongoing compliance. We help organizations transition to a process-based approach for financial control compliance, identifying effective ways to appropriately reduce effort through better risk assessment, scoping and use of technology, thus reducing the cost of compliance. Reporting directly to the board, audit committee or management, as desired, we have completed hundreds of discrete, focused financial and internal control reviews and control investigations, either as part of a formal internal audit activity or apart from it.

One of the key features about Protiviti is that we are not an audit/accounting firm; thus, there is never an independence issue in the work we do for clients. Protiviti is able to use all of our consultants to work on internal audit projects – this allows us at any time to bring in our best experts in various functional and process areas. In addition, Protiviti can conduct an independent review of a company's internal audit function – such a review is called for every five years under standards from The Institute of Internal Auditors.

Among the services we provide are:

- Internal Audit Outsourcing and Co-Sourcing
- Financial Control and Sarbanes-Oxley Compliance
- Internal Audit Quality Assurance Reviews

For more information about Protiviti's Internal Audit and Financial Controls solutions, please contact:

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KnowledgeLeaderSM

KnowledgeLeaderSM is a subscription-based website that provides information, tools, templates and resources to help internal auditors, risk managers and compliance professionals save time, stay up-to-date and manage business risk more effectively. The content is focused on business risk, technology risk and internal audit, and is updated weekly.

The tools and resources available on KnowledgeLeader include:

Audit Programs – A wide variety of sample internal auditing work programs and IT functional audit work programs are available on KnowledgeLeader. These work programs, along with the other tools listed below, are all provided in downloadable versions so they can be repurposed for use in your organization.

Checklists, Guides and Other Tools – There are more than 600 checklists, guides and other tools available on KnowledgeLeader. They include questionnaires, best practices, templates, charters and more for managing risk, conducting internal audits and leading an internal audit department.

Policies and Procedures – KnowledgeLeader provides hundreds of sample policies to help you in reviewing, updating or creating your company policies and procedures.

Articles and Other Publications – Informative articles, survey reports, newsletters and booklets produced by the KnowledgeLeader team, Protiviti professionals and other content providers (including *Compliance Week*, Auerbach, Taylor & Francis and The IIA). The content is focused on business and technology risks, internal auditing and finance.

Performer Profiles – Interviews with internal audit executives and chief risk officers from corporations around the world. These leaders share their tips, techniques and best practices for managing risk and running their internal audit function or developing and managing their enterprise risk management initiatives.

Key topics covered by KnowledgeLeader:

- Business Continuity Management
- Control Self-Assessment
- Corporate Governance
- COSO
- Enterprise Risk Management
- Financial and Credit Risk
- Fraud and Ethics
- Internal Audit
- Sarbanes-Oxley Act
- Security Risk
- Technology Risk

KnowledgeLeader has an expanding library of methodologies and models – including the robust Protiviti Risk ModelSM, a process-oriented version of the Capability Maturity Model, the Six Elements of Infrastructure Model and the Sarbanes-Oxley 404 Service Delivery Model.

With a KnowledgeLeader membership, subscribers have access to AuditNet Premium (Paid) Content; discounted certification exam preparation material from ExamMatrix; discounted MicroMash CPE Courses to maintain your professional certification requirements; audit, accounting and technology standards and organizations; certification and training organizations and information; brief review of applicable laws and regulations; and best business links.

To learn more about KnowledgeLeader, sign up for a complimentary 30-day trial by visiting our website at www.knowledgeleader.com. Protiviti clients and alumni, and members of The IIA, ISACA and AHIA, are eligible for a subscription discount. Additional discounts are provided to groups of five or more.

KnowledgeLeader members have the option of upgrading to KLplusSM (KL+). KL+ provides all of the benefits of KnowledgeLeader, plus full access to Protiviti's suite of online courses.

Protiviti's Governance Portal for Internal Audit

Protiviti's Internal Audit Portal is a web-based audit management system designed to improve the efficiency and effectiveness of your audit department. The Internal Audit Portal is an electronic work paper package that facilitates the audit process from risk assessment through issue tracking. Our advanced reporting engine will provide transparency, real-time status updates and a streamlined audit reporting experience.

Our clients are able to configure the solution to fit their approach and methodology, positioning both small and large internal audit functions to meet their objectives. When combined with our professionals and content, Protiviti will help you create a personalized response to your audit tool needs.

The Internal Audit Portal is an integrated module within the Protiviti Governance Portal that can be used independently or in conjunction with other modules to create a true governance, risk and compliance (GRC) platform. This enterprise solution allows you to leverage frameworks and build a common language and repository that brings internal audit information into a GRC context. Additional modules of the Governance Portal include:

Controls Management – A framework that supports control documentation (e.g., Sarbanes-Oxley), evaluation, documentation and testing.

Risk Management – A framework for assessing inherent, tolerable, and residual risk across defined enterprise categories.

Assessment Management – An integrated survey engine that supports a sustainable self-assessment process across multiple GRC programs and modules of the Governance Portal.

Incident Management – A system that captures actual, near-miss and potential events that can result in operational and financial losses.

For more information about Protiviti's Governance Portal for Internal Audit, please contact:

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