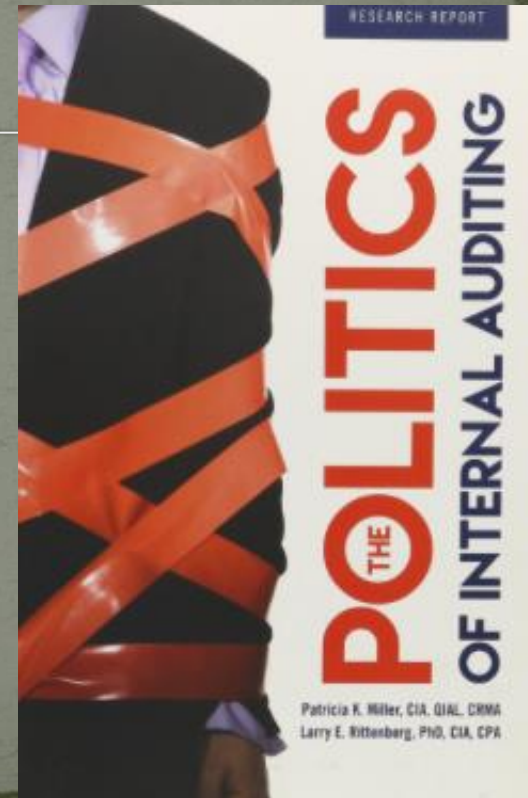


Organizational Political Pressure and the impact on Internal Audit

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Discussion Topics

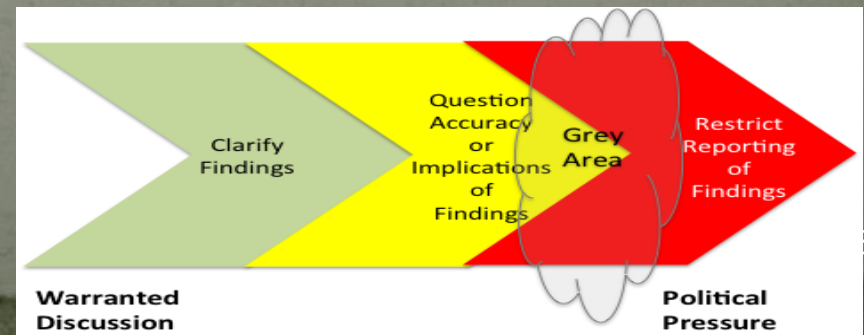
- Background
- Approach
- Results of Interviews/Survey
- Aggravating Factors for Political Pressure
- Implications for Chief Audit Executives
- Concluding Thoughts

Why This Topic?

- Why do this research?
 - Everybody must navigate political waters
 - Internal audit very susceptible
 - Minimal existing research
 - The IARF: too many cases look like political pressure

Definition of Political Pressure Related to Internal Audit

The situation in which individuals in leadership positions exercise their authority to achieve a personal benefit, or to protect an organization, by attempting to manipulate the internal audit activity or internal audit reports. Such manipulation may result in actions to restrict the scope of audit activities, suppress audit findings, or undermine the credibility of the chief audit executive or the internal audit activity.



Approach

- Review of research, articles, and reports on political situations affecting internal auditing
- Conducted 23 interviews
 - Fortune 100 Companies
 - Global Organizations
 - Governmental – federal, state and municipalities
- Focus group at General Audit Management Conference
- Flash survey of North America CAEs

Research Results

Interviews – a Few Stories

Could the events described happen to auditors?

- CAE threatened with loss of future job opportunities if they continued audit
- CAE who ignored executive and reported issue to board, subsequently excluded from key executive meetings
- Executive who shared their version of events with CEO and board before CAE could present results, swaying ultimate conclusion
- CEO who refused to meet with CAE to avoid having direct knowledge of issue at hand, on advice of legal counsel

Survey – Personal Comments

- Restructured out of company
- Negotiated package to leave company
- Eventual termination
- Personal threats
- Silent treatment
- Treated as not part of team/not a team player
- Access to information restricted
- Denied request for additional resources
- Stagnation when peers upgraded

Case – New Officer Issue

- Major publicly traded consumer service business
- Standard officer expense audit
- Newly promoted officer doctoring expense receipts and charging personal items
- Would CEO look bad if newly promoted officer was terminated? Officer had made significant contributions to organization
 - could officer be salvaged?

Case – Stay in Scope!

- Major governmental agency
- Subcontracted implementation
- Audit was selected to look at profit sharing – later expanded to fraud
- “Out of scope” audit activities
- Board support critical to completing audit and reporting issues

Survey - Extent of Pressure

Exhibit 4.13. Number of Times Asked to Suppress a Finding

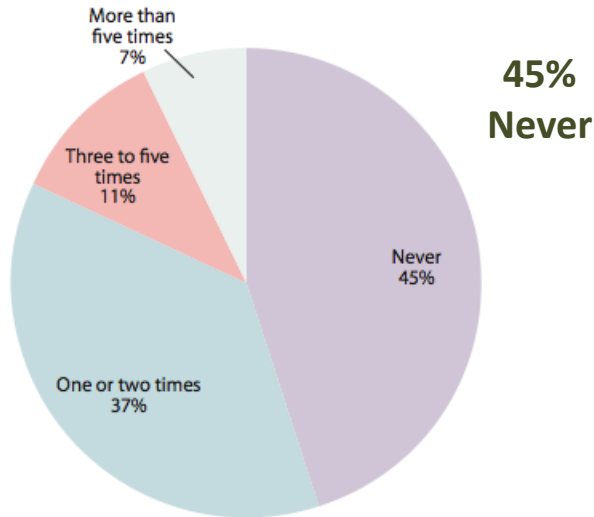


Exhibit 4.14. Number of Times Requested Not to Audit High-Risk Area

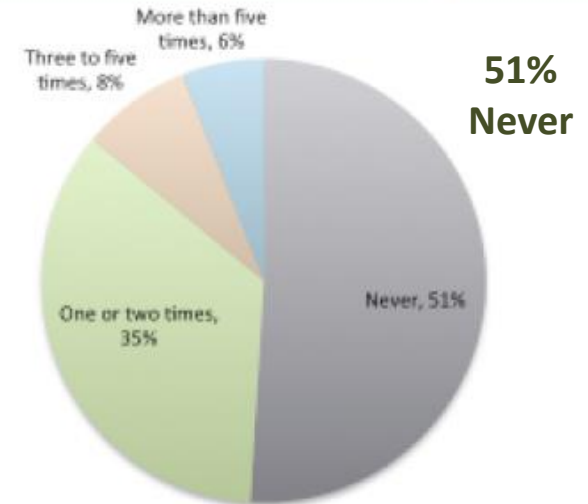


Exhibit 4.17. Strong Support Correlated with Less Political Pressure

SUPPORT OF:	% OF "NEVER" RESPONDENTS WITH STRONG SUPPORT		
	SUPPRESS FINDING	NOT AUDIT HIGHER RISK	AUDIT LOWER RISK
Audit committee	88.4%	91.7%	83.2%
Executives	79.9%	78.2%	72.6%

Aggravating Factors

- Lack of strong ethical culture from top down
- Lack of strong, independent and supportive audit committee
- Culture that embraces risk and not control, or culture that wants to put positive 'spin' on issues
- Weak relationship between CAE and AC Chair, CAE and key executives
- CAE who lacks objectivity, integrity, courage, or sound judgment
- Internal audit function that lacks competence
- Enculturation of employees – we see what we expect to see or accept what we have learned is acceptable

Implications for CAEs

Implications

- Foundational
- CAE Attributes
 - Relationship Building
- Internal Audit Function

Foundational

- Strong governance, knowledgeable board
- Strong reporting relationship and position
 - Direct reporting relationship to board/audit committee
 - CAE senior independent position
- Clear and supportive Charter
 - Documents unique role
 - Specifies authority and unrestricted scope
 - Codifies expectations
- Decision framework – when to take a stand
 - Identify alternatives, consequences, best action

CAE Attributes

- Integrity and courage
 - Know your internal 'compass'
 - Stand ground on important issues
- Objective and fair
- Relationship builder – with board, executives and management
 - “We are after the same objectives.”
- Judgment to know what IS an important issue and when to take a stand
 - Think strategically
- Anticipates and proactively addresses issues
 - Discuss protocols in advance
 - Know key parties and motivations

Relationship Building

- Meet outside of scheduled, formal meetings
- Learn about person – objectives, accomplishments, interests
- Lead outside of IA role; be visible
- Educate on emerging topics
- Find mutual areas of interest; do not take meetings casually but prepare

Internal Audit Function

- Effective communication
 - Shared understanding of scope, objectives, rationale
 - To whom and when to communicate issues
 - Fact based conclusions with clear business implications
- Staffing – rigorous selection and training
 - Competence
 - Poise
 - Reliable evidence/strong data analytics
 - “Facts are your friend.”
- Think strategically, know the business, present alternatives, jointly find solutions

Concluding Thoughts

Ongoing Challenges

- Political pressure can be managed and partially mitigated, but it is always present
- Good corporate governance critical, but can be transient
- Professional competence required, but not sufficient
- Effective communication is more than report writing
- Continuously work to align internal audit with organization

Questions and Discussion

- What techniques have you used to defuse undue pressure from internal audit clients?
- What can internal audit do if the culture of the organization doesn't support an independent and objective internal audit function?