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## **Continuous Auditing: Wave Of The Future?**

*Current internal audit models may be too little, too late.*

by Anthony O'Reilly

# Continuous Auditing: Wave Of The Future?

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As corporate oversight and regulatory demands become stricter, boards and managers need more robust financial controls. If internal audit discovers a danger six months after the fact, the situation will have had plenty of time to grow into a disaster. Consider "continuous" auditing—an ongoing, technology-driven audit regimen that holds the promise of monitoring controls in real time.

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To address stakeholder demands for faster and better assurance, internal auditors are accelerating the frequency of their internal audit cycles. This is prompting strong interest in *continuous* auditing. Continuous auditing holds the potential to shorten audit cycle times and provide more timely risk and control assurance.

**Continuous auditing replaces the traditional audit cycle with a dynamic, more responsive set of audit-related activities.**

Precisely what *is* continuous auditing? It is the use of technology to identify changes in risk or control indicators. Continuous auditing allows internal audit to identify and report control deficiencies more rapidly, even without going through the formalities of a full audit. It also allows auditors to test entire populations of data as opposed to relying on the limited testing of data samples.

In this way, the traditional annual audit cycle of assessing risk, planning, auditing and reporting is replaced by a more dynamic, yet more responsive set of audit related activities.

In practice, very few corporations have yet achieved true continuous auditing on a "real-time" basis. Practices vary and include deploying standard computer-assisted audit programs on a regular basis, combined

with manual procedures and inquiries performed at regular intervals.

With technology-enabled continuous auditing, internal auditors can improve assurance quality, gaining the ability to audit 100 percent of transactions as opposed to just samples. In addition, by expanding the scope and frequency of the audit process, technology-enabled auditing allows internal auditors to communicate more effectively with business units, senior management, and the board's audit committee.

The concept of continuous auditing has gained momentum. Today's compressed business cycles are fueling demands from internal audit's key stakeholders for faster and better assurance. Senior executives and corporate directors must accept risks and make business decisions more quickly. To do so, they need more real-time or just-in-time assurance over risk management and related controls.

Yet despite being pressed for better and faster assurance, internal auditors are often constrained by the cycle of activities dictated by following professional norms. In particular, risk assessments are conducted annually, resources are assigned well in advance and reports are only issued after an audit has been completed and debriefed, sometimes with several layers of management.

In meeting this challenge, chief audit executives can either accelerate the components of this cycle or look for ways to change the cycle itself.

Our 2006 state of the internal auditing profession survey finds the quest for greater audit efficiency and effectiveness is prompting many companies to pursue the potential of continuous auditing and monitoring. Of the 392 companies who responded to questions about continuous auditing in this year's survey, 81 percent either have a continuous auditing or monitor-

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ing process in place or were planning to develop one. Just 19 percent said they do not have a continuous auditing process nor plans to develop one.

From 2005 to 2006, the percentage of survey respondents saying they have some form of continuous auditing or monitoring increased from 35 percent to 50 percent. Of this 50 percent, 13 percent said they have a process that is fully operational, and 37 percent have a process in place, although it is not yet fully developed. Another 31 percent have plans to add a continuous auditing or monitoring capability.

**Technology can be an essential element in continuous auditing. It is a strategic enabler, enhancing all aspects of the audit process.**

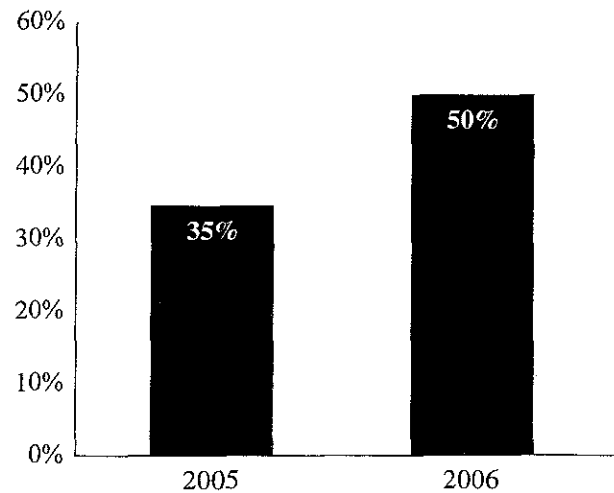
Of note was the fact that manual activities and automation alike played significant roles in continuous auditing activities. Although only three percent claimed to have a fully automated continuous auditing process, 56 percent said their continuous auditing activities include both manual and automated elements. The remaining 41 percent said their continuous auditing processes were entirely manual in nature. This statistic is sure to surprise members of the internal audit community who believe technology is an essential part of any continuous auditing activity.

Technology can be an essential element in continuous auditing. It serves as a strategic enabler, enhancing all aspects of the audit process, from strategic planning to the delivery of quality assurance. For example, the 41 percent of respondents whose continuous auditing practices lack automation could likely gain even greater productivity from wise application of technology.

Continuous auditing can make the audit process faster, cheaper, more efficient, and more effective. Using continuous auditing, risk assessment can be updated on a daily, monthly or quarterly basis. Companies can also improve assurance quality because they can rapidly audit 100 percent of transactions as opposed to being restricted to data samples alone.

As these benefits strongly suggest, continuous

### Continuous Auditing Increase Fifty Percent Of Companies Now Use Some Form Of Continuous Auditing



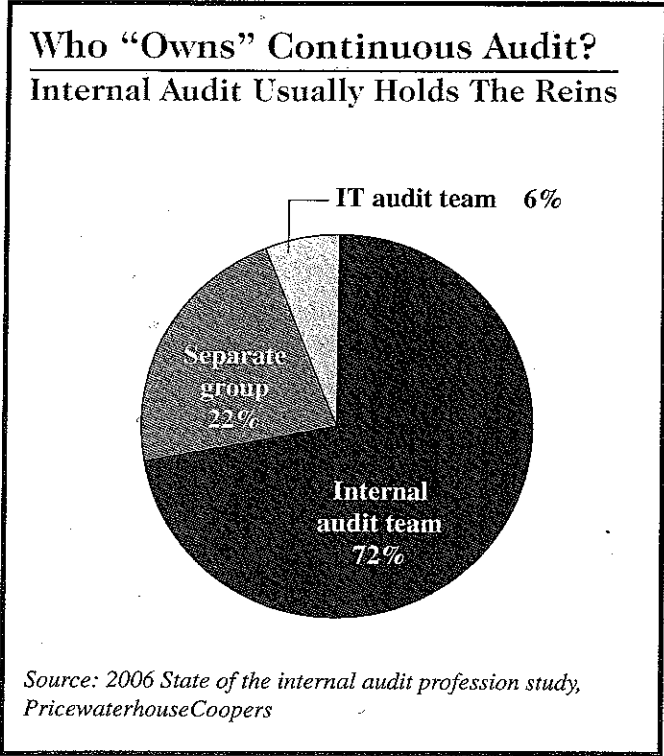
Source: 2006 State of the internal audit profession study, PricewaterhouseCoopers

auditing is far more than just another way to perform traditional internal audit activities more effectively and at a lower cost. By expanding the scope and frequency of the audit process, technology-enabled continuous auditing provides the means for internal audit to strengthen reporting to and communication with senior management and the audit committee.

By far the biggest benefit of technology-enabled continuous auditing, however, is how it strengthens the ability of internal audit to communicate more effectively with business units. Auditors can provide more timely analysis of risk factors and control assessments.

When asked to describe the primary focus of their continuous auditing processes, 27 percent seek to identify changes in risk profiles, 26 percent concentrate on audit tests to verify control effectiveness, and 20 percent focus on testing for unusual or fraudulent activities. In addition, 17 percent focus on monitoring individual controls to identify deficiencies, while 10 percent focus on monitoring key performance indicators.

It is a leading practice in internal audit circles for



those who audit a particular business unit to also be responsible for continuous auditing activities in that unit. Therefore, it was good to note that 72 percent of respondents with continuous auditing operations have settled on such an operating model.

**The most common continuous auditing "cycle" is quarterly. Only nine percent focus on daily auditing, typically high-volume transaction activity in search of fraud.**

Of the other respondents active in continuous auditing, 22 percent place responsibility for these activities with a separate group within internal audit, while six percent place this responsibility with the company's information technology (IT) audit group. The relatively low number of IT groups responsible for continuous auditing suggests that this is by no means an "IT only" issue.

The most common continuous auditing "cycle" is quarterly, with 57 percent of our respondents falling into this category. Another 34 percent focus on

monthly monitoring while only nine percent focus on daily auditing. Those using a daily audit cycle are typically conducting high-volume transaction activity in the search for fraud and other anomalies.

Purchased software is the basis for automation for nearly half of all respondents whose processes include automation. Nearly a third rely upon custom-built and custom-programmed applications for their automation. Report writer/retrieval software, frequently deployed with large enterprise resource planning programs, is used for automation at 19 percent of this respondent group.

When asked to describe their principal challenges in establishing continuous auditing, 37 percent of respondents identified: defining activities to be audited, deploying technology, and obtaining internal support. For 13 percent of our respondents, the primary challenge was determining whether a business unit or internal audit should conduct the monitoring. Surprisingly, only 12 percent cited cost as their primary challenge.

Admittedly, continuous auditing is still considered an emerging phenomenon in some circles. However, our survey clearly shows that internal auditors view continuous auditing as a means to enhance their audit processes. They can better address stakeholder needs and demands for faster and higher-quality real-time assurance. With continuous auditing methodologies, you can:

- Make the audit process faster, cheaper, more efficient, and more effective.
- Shorten audit cycle times to provide more timely risk and control assurance.
- Achieve greater audit coverage without the need to expand your resource base.
- Conduct audits on a daily, monthly, or quarterly basis.
- Automate periodic audit testing and improve audit cycle times.
- Audit 100 percent of data populations instead of just data samples.
- Compare and recalculate populations of data.
- Improve assurance quality as well as speed. ■

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