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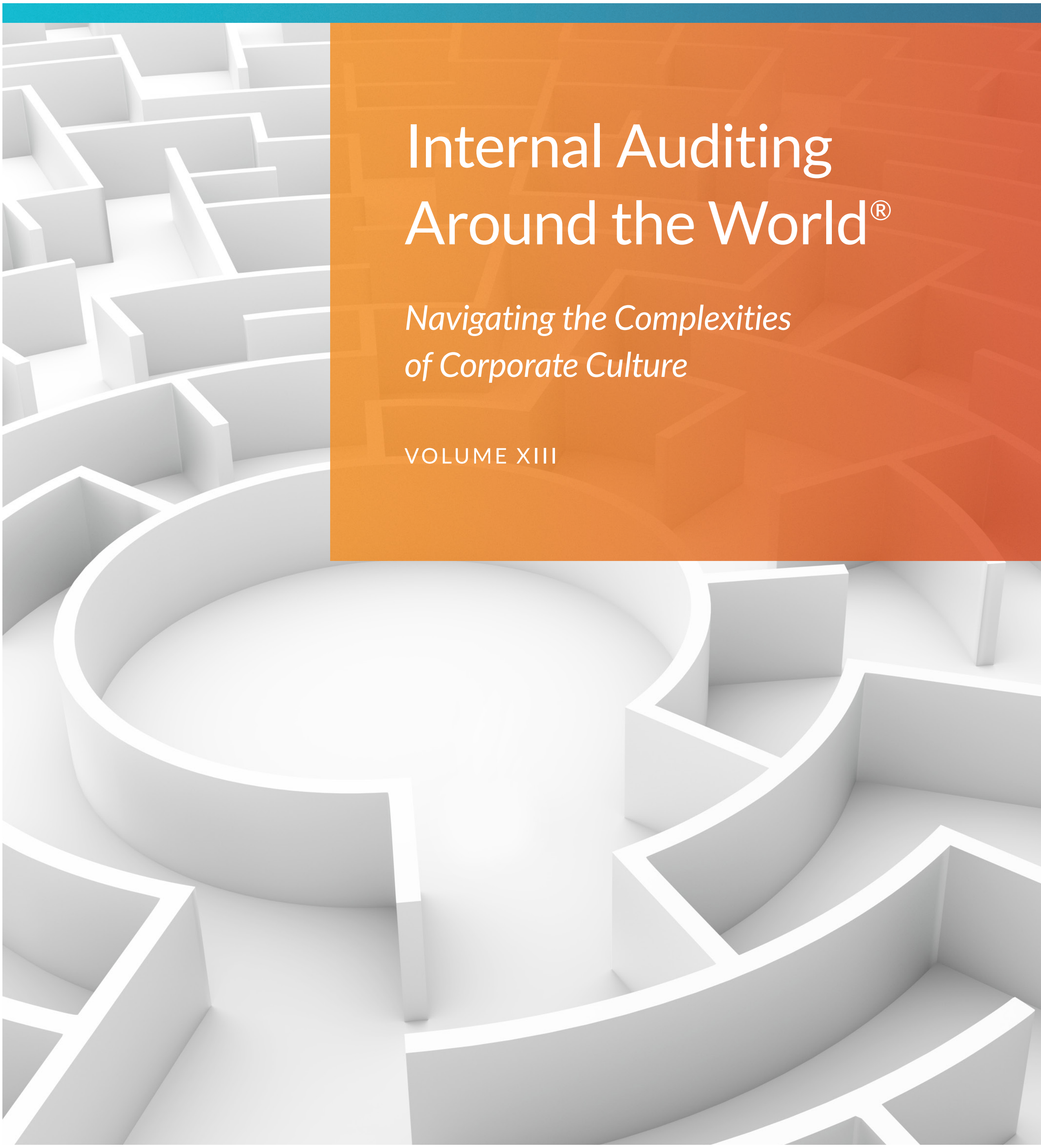


Internal Auditing Around the World®

Navigating the Complexities of Corporate Culture

VOLUME XIII

Internal Audit, Risk, Business & Technology Consulting

Foreword

Since 2005, Protiviti has been reporting on trends in the internal audit profession in our annual *Internal Auditing Around the World®* series. The internal audit leaders we've interviewed over the years have spoken candidly about the challenges that they and their teams have faced — from helping the business to navigate the financial crisis to assessing the risk of new technologies. Often, they have had to adapt their practices and rethink their roles in their organizations to meet those challenges.

During the Great Recession, as an example, we learned that many internal audit leaders were starting to recognize the importance of partnering with boards of directors and senior management to create greater transparency, establish sound corporate governance and better understand risk exposures. Today, many internal auditors serve as strategic advisers to the business — a role they fully embrace.

In the early years of the recovery, we examined how the fundamental shift toward collaborative working — with organizations eliminating cultural, operational and technological barriers to productivity — gave some internal auditors pause. They wondered if collaborative working would impact their ability to be independent and objective. But what they quickly learned is that collaborative work environments foster trust, and that trust, in turn, helps to support a more effective audit process.

Now, in 2017, we find many internal auditors staring down yet another challenge that places them into unfamiliar and somewhat uncomfortable territory: auditing risk culture. Business leadership is looking to the audit function to assess not only tone and conduct at the top of the organization, but also how and if those things are reflected throughout the business. They want to know if the company's core values and strategic vision are understood and actively practiced by employees.

For many of the organizations featured in *Internal Auditing Around the World® XIII,* risk culture audits are new endeavors that are only at the planning or pilot stage. Senior management and boards are looking to internal audit leaders to help the business develop the right approach for, and get the most value from, these types of audits. The function has a clear opportunity to play a transformative role in responding to the needs of key stakeholders, particularly boards, who want assurance that the organization is aware of and addressing all types of potential risk.

We hope that the profiles in this edition of *Internal Auditing Around the World®* provide valuable insight on how an organization can approach auditing its risk culture. It is a new frontier for many internal auditors. But just like partnering effectively across the organization and working in a collaborative environment, it is a challenge worth conquering.

Brian Christensen
Protiviti Executive Vice President
Global Internal Audit

Table of Contents

Introduction

> *Knowledge of the fact differs from knowledge of the reason for the fact.*
>
> — Aristotle (384 – 322 B.C.)
> Greek philosopher and scientist

Weak organizational cultures in entities across the world's financial system are widely considered to be one of the primary causes of the global financial crisis a decade ago. Perhaps as a result, maintaining a strong risk culture is an imperative for all major businesses today — as well as an expectation by their stakeholders, regulators and customers. Many of these organizations look squarely to their internal audit functions to provide assurance that their risk culture is indeed effective.

Fulfilling this mandate requires internal auditors to tread carefully and adhere to a well-structured approach. The definition of internal auditing from The Institute of Internal Auditors (The IIA) sheds light on why:

> *Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.*[1]

Auditing risk culture seems to fall neatly under internal audit's mandate to help the organization improve the effectiveness of its risk management and governance. However, when considering other components of The IIA's definition — namely, the word "objective" — it becomes clear why an internal auditor would view auditing any aspect of an organization's culture as potentially problematic. The core concern is that, in reviewing and measuring an intangible thing like culture, the internal auditor would be at risk of making a subjective assessment of the state of that culture.

Culture is complex and different within every organization. There are some guideposts available — for example, risk culture, as defined by the Risk Management Association (RMA) and Protiviti, is "the set of encouraged and acceptable behaviors, discussions, decisions and attitudes toward taking and managing risk within an institution."[2] But even when defined, culture remains largely abstract.

Through our research for Volume XIII of Protiviti's *Internal Auditing Around the World®*, we learned that the internal audit leaders in many of the organizations already auditing, or that intend to audit, their risk culture are taking great pains to create methodologies, frameworks and processes that can give structure to the abstract.

[1] "Definition of Internal Auditing," The IIA: www.theiia.org/guidance/standards-and-guidance/ippf/definition-of-internal-auditing/?search%C2%BCdefinition.

[2] For more details, see "Risk Culture: From Theory to Evolving Practice," *The RMA Journal*, December 2013–January 2014, RMA and Protiviti: www.rmahq.org/WorkArea/DownloadAsset.aspx?id=5452. Also see, "Strengthening Your Risk Culture," *Board Perspectives: Risk Oversight*, Issue 57, 2014, Protiviti: www.protiviti.com/US-en/insights/strengthening-your-risk-culture.

For example, at the Options Clearing Corporation in Chicago, the world's largest equity derivatives clearing organization, former chief audit executive (CAE) Adi Agrawal and his team have developed a maturity framework for risk culture audits. Agrawal says it has a "regulatory backdrop" that was framed using the "common expectations of regulators and pronouncers of standards and principles for financial market infrastructure." It also draws on pronouncements from the Federal Reserve Board and the Basel Committee on Banking Supervision, among other regulatory authorities.

Some internal audit groups are taking more incremental steps toward formalizing an approach to assessing and monitoring risk culture. Group Audit at Westpac Banking Group, for example, recently modified its quarterly enterprise risk management dashboard to include a specific line for culture. The team is also working with an outside expert to develop a formal risk audit questionnaire, reports Craig Duker, head of audit for the risk, compliance and human resources divisions at the Australian bank.

Other internal audit departments look to their company's guiding principles and core values — as well as its "tone at the top" — to help give structure to their process for auditing culture. "To me, auditing culture comes down to the tone set by leadership, and whether that tone permeates the business, flowing down through the ranks and every level of management," says Michael Rimkus, senior vice president of internal audit and risk management for U.S. wireless company T-Mobile.

Several of the leaders we interviewed said they recognized early the importance of examining and strengthening the culture within the internal audit function before moving to assess the culture elsewhere in the company. Ruurd van den Berg, executive vice president and CAE of Group Internal Audit at Aegon N.V., a multinational life insurance company headquartered in The Hague, Netherlands, explains, "We believe we should lead by example. We knew that if we didn't have a strong culture, we would lack the credibility to run culture audits."

The results of these internal audit culture assessments can be eye-opening. Richard W. Moore, inspector general for the Tennessee Valley Authority's Office of the Inspector General (OIG), says consultant-led, 360-degree surveys of his internal audit organization's culture revealed "dysfunctional attributes" like "low trust and poor communication." When he realized that he was part of the problem, it was an "aha" moment. "If you're going to instill trust in people, you need to be vulnerable and fix yourself first," Moore says. "Then, invite others to join you in your journey to improve."

For businesses that have yet to begin their risk culture audit journey, like Takeda Pharmaceutical, the process will likely add dimension to internal audit's other work. Katsuaki Kaneko, senior vice president, head of Group Internal Audit for the Japanese company, explains, "When we dig into the root cause of a compliance-related audit issue, we often find that it is related to people's behavior or a management attitude. We rarely state that explicitly in a report because it can be too subjective. However, when people read the report, they can understand what the core issue is."

And even though Corporate Audit Services (CAS) at Expedia does not conduct formal audits of the U.S. travel company's culture, CAS vice president Jeff Davis believes that his team still audits culture every day. "We interview people daily about risk and controls, interacting at all levels of the organization, starting with the brand presidents or the C-suite through to the rest of their teams," he says. "Each day, we gauge whether we believe we are getting the right level of transparency and candor we need from the individuals, teams and systems."

A company's culture may be abstract, but one thing is clear from an internal audit perspective: Developing the right approach for auditing an organization's risk culture takes time and careful planning. And for any business, the value of undertaking this process is developing a better understanding of the cultural causes that create risk — in short, human behaviors. Ironically, it is the internal audit function — the objective eye of the organization — that is uniquely qualified to bring "a systematic, disciplined approach" to a potentially subjective process.

Protiviti
July 2017

Acknowledgements

We would like to thank the organizations and internal audit leaders who contributed to this year's publication. The profiles herein would not be possible without their interest, cooperation and insights. We would also like to extend our sincere appreciation to The IIA for its commitment to advancing the internal audit profession, and for its long-standing partnership with our company.

Abu Dhabi National Oil Company (ADNOC) Transforms to a Performance Culture

We want ADNOC to be a company where the best people and ideas win, and people feel empowered to speak up and contribute to drive positive change.

— Ahmed Abujarad,
Audit and Assurance Unit Manager

EMPLOYEES IN ADNOC GROUP OF COMPANIES:
50,000

INDUSTRY:
Oil and Gas

ANNUAL REVENUES:
N/A

NUMBER IN IA FUNCTIONS ACROSS GROUP COMPANIES:
158

YEARS IA FUNCTION HAS BEEN IN PLACE:
31

IA DIRECTOR/CAE REPORTS TO:
Audit Committee; administratively to CEO

Established in 1971, Abu Dhabi National Oil Company (ADNOC) is a diversified group of energy and petrochemical companies that manages and oversees the production of around 3 million barrels of oil and 9.8 million tons of raw gas per day. The company delivers refined and processed products to six continents, employs more than 50,000 people, and is a major contributor to the gross domestic product of the United Arab Emirates (UAE). ADNOC's 16 subsidiary companies operate in the fields of exploration and production; oil refining and gas processing; chemicals and petrochemicals; refined products and distribution; maritime transportation; and support services, including sales and marketing, human capital, legal, finance, and IT.

Ahmed Abujarad has worked for ADNOC, either at the holding company or one of its group companies, for 15 years. He returned to ADNOC Group headquarters in October 2016 in the role of Audit and Assurance Unit Manager. Abujarad's unit reports functionally to the Audit Committee and administratively to the CEO. His Audit and Assurance Unit has a total headcount of 29.

The Audit and Assurance Unit provides assurance and advisory to ADNOC headquarters (HQ) and drives internal audit performance across the group. It accomplishes these key mandates through three major focus streams: (1) ADNOC Audits at ADNOC HQ operations and ADNOC Group companies; (2) Specialty Audits, including fraud and forensics, and IT Audits; and (3) Quality Assurance and Excellence, which includes activities such as providing quality assurance and technical support, driving internal audit performance at headquarters and subsidiaries across the board, handling stakeholder communications, managing transformation and change projects, and striving for excellence.

Four Pillars of Culture: 3P&E

Responding to changes in the evolving market for oil and gas, ADNOC recognized the need for a fresh vision, a new mission, and a more open and collaborative corporate culture. In early 2016, the organization launched a groupwide realignment of company strategies based on the four key pillars of Profitability, Performance, People and Efficiency (3P&E), while maintaining health, safety and environment (HSE) and plant integrity as the prime priorities.

"The new vision, mission and values define our strategic objectives, articulate who and what we are, and set out the core values that underpin all that we do, along with our key cultural attributes," Abujarad explains.

He says ADNOC defines those culture attributes (*who we are*) as:

1. Bring the energy.
2. Embrace teamwork.
3. Seek excellence.
4. Deliver results.
5. Exceed expectations.

"A strong and open culture catalyzes the energy, commitment and hard work required to ensure we retain our competitive edge in a highly competitive market," says Abujarad. "We want ADNOC to be a company where the best people and ideas win, and people feel empowered to speak up and contribute to drive positive change."

Re-Engineering Internal Audit Governance and Execution

In keeping with changes across the group and its subsidiaries, the internal audit function is also undergoing a major transformation. The key objectives of that effort include achieving alignment with the four pillars, focusing on enhancing value to the business (through assurance, insight and objectivity), and being perceived as strategic partners to the management team.

The ADNOC Group Internal Audit Transformation Project established a strategic plan based on an end-to-end diagnostic study covering all internal audit activities across ADNOC Group. The project is comprised of 10 change streams with 52 initiatives aimed at re-engineering internal audit governance and execution, as well as continuing to strive for internal audit excellence ensuring high performance across the group.

"We are re-engineering the governance and execution processes to move toward a state of continuous improvement and excellence," Abujarad says.

He explains that this effort starts with standardization of internal audit governance, planning and execution methodologies across the group. It also includes remodeling the ADNOC Group Internal Audit Operating Model to capitalize on internal infrastructure, expertise and other resources that promote consolidated planning, collaborative and efficient working models, and effective knowledge management.

"Our plan includes leveraging the best that leading processes and technology have to offer in terms of conducting internal audits, and using reporting dashboards, data analytics and continuous auditing, while making sure our most important resources — people — continue to be developed and inspired to deliver their best," Abujarad says.

A new unified, balanced scorecard approach to measuring performance, benchmarked against key performance indicators (KPIs) and international standards, has been introduced. Now, every employee will be measured against consistent and equal standards, according to Abujarad.

Learning and development frameworks, standardized grades and professional career ladders have also been implemented to nurture and embed a performance-led culture across all ADNOC's businesses. Abujarad says an open culture requires this level of transparency.

Refining Culture to Benefit People

Abujarad says that he believes an open culture, which is led from the top down and encourages people to stand up and speak — whether about new ideas and initiatives, or breaches of company values — is vital to the messages of teamwork, collaboration and shared success through shared energy.

"Here we share the success of everybody's efforts," he says. "The organization focuses on promoting employee well-being, work-life balance, skills development and a learning culture."

A large component of ADNOC's open culture is a "trust" element, where management empowers employees to take calculated risks and exposure to mistakes is expected.

"We learn from mistakes," Abujarad says. "Empowerment doesn't happen without trust. When employees feel trusted and empowered, they also feel engaged."

He says that since the company began emphasizing solutions over problems, employee satisfaction has increased. ADNOC's most recent employee engagement survey reflected that.

One ADNOC Spirit

A tangible benefit of increased employee engagement is the development of a "one spirit, one family" atmosphere at ADNOC. The company has created internal communities where employees with different specialties interact to network, form close professional relationships, and exchange views and other processes for them to report on mishaps anonymously or act as whistle-blowers regarding code of ethics violations.

"This spirit of collaboration, communication and coordination among employees has benefitted internal audit by eliminating the defensive policeman and watchdog mentality of departments being audited," says Abujarad. "They perceive internal audit as a value-adding activity."

He says internal audit is examining their internal culture for opportunities for improvement. "We realized that, as auditors, we've been more focused on process evaluation and operational systems evaluation. But to audit culture, we must move from technical skills to softer skills, and perhaps take training courses to increase our competencies. We cannot conduct cultural audits the same way we conduct traditional audits."

ADNOC has developed an integrated audit approach and methodology — "Extended Assurance" — that is implemented across the group. The model is represented as a circle of six elements that surround a core comprised of the four pillars (3P&E). The elements are:

- Strategic
- Financial
- IT
- Operational
- Standards and Regulatory
- Performance Monitoring and Reporting

The model was created to provide management with a holistic view of the audit function. Critical cultural elements are also embedded in the model. For example:

- Strategy, organization structure, governance and communication are part of the Strategy element;
- Compliance with HSE Codes of Practice (COP) and other mandatory requirements from international standards is part of the Standards and Regulatory element; and
- KPIs and the performance management framework are part of the Performance Monitoring and Reporting element.

Auditing for culture, Abujarad says, involves instilling a sense of inclusiveness, empowerment and ownership by providing all employees with the space to provide suggestions on how to improve their businesses and processes.

The Interrelationship Between Overall Culture and Risk Culture

"A strong overall culture is evidenced by open and transparent communication at all levels, synergy and collaboration between business units, and a sense of ownership," Abujarad says. "Culture helps to ensure that the effects of risk are considered in decision-making." Risk culture, he adds, helps to shape the overall culture of the organization by setting the parameters for strategic decision-making.

Abujarad says the biggest challenge in cultural change lies in overcoming people's natural resistance and skepticism, and that driving cultural change is neither an easy nor quick thing to do.

"ADNOC is evolving into a smarter and more agile organization. It is important for everyone to understand why it is necessary to become a truly commercially focused and performance-driven organization, and what their individual role is in achieving those goals," Abujarad says. "A strong corporate culture starts with a clear definition of attributes from the top — who we are and how we do business — and an understanding of this culture that is consistent across people and situations."

Directors and senior management bear much of the responsibility for ensuring the culture permeates throughout the organization, he says, so they must "walk the talk" and ensure that the transformative message reaches all employees.

Ultimately, however, Abujarad says promoting a strong culture is the responsibility of everyone at ADNOC: "While this effort is led by H.E. Dr. Sultan Ahmed Al Jaber, Group CEO, and his executive team, and supported by the business heads, it is a united effort aimed at transforming ADNOC Group into a company that is fit for the future."

Global Internal Audit Team Carefully Builds a Culture Audit Program for Aegon, One Phase at a Time

I think once we reach the final phase of our program, where we are assessing attitudes and behavior, it will become even more challenging to document our observations. We must be very careful about what we say, and we need people who have the credibility to do it. Those people are not traditional auditors.

— Ruurd van den Berg, Executive Vice President and Chief Audit Executive, Group Internal Audit

EMPLOYEES IN COMPANY:
29,380

INDUSTRY:
Insurance

ANNUAL REVENUES:
€1.9 billion
(in earnings as of December 31, 2016)

NUMBER IN IA FUNCTION:
120

YEARS IA FUNCTION HAS BEEN IN PLACE:
7 (locally organized prior to 2010)

IA DIRECTOR/CAE REPORTS TO:
Chief Executive Officer

Aegon N.V. is a multinational life insurance, pensions and asset management company headquartered in The Hague, Netherlands, that employs 29,000 people and serves more than 30 million customers around the globe. It is one of the world's top 20 insurance firms and has offices and joint venture operations in more than 20 countries, including the United States, United Kingdom, Spain, Hungary, Turkey, India, Japan and China. But at its core, this complex global business has one simple purpose: helping people achieve financial security.

Aegon began in 1844 as Algemeene Friesche, founded by two civil servants in the northern Dutch province of Friesland. The company provided funds for people to arrange burials for their loved ones. Over time, Algemeene Friesche merged with other small companies and associations in the Netherlands that were providing widows' funds, life insurance, health insurance and other services to form what would become today's Aegon. The company has seen rapid global expansion since the 1990s. That includes its acquisition of San Francisco-based Transamerica in 1999, one of the best-known insurers in the United States; Transamerica operates under its own brand name in North America.

Ruurd van den Berg, executive vice president and chief audit executive (CAE) of Group Internal Audit at Aegon, oversees a "lean and mean" team of 120 auditors worldwide who are focused on operational auditing and providing strategic advice. (An external auditor conducts Aegon's financial audits.) Van den Berg has been with the company for 25 years, and since 2010, building and operating "a truly global internal audit function within a global governance structure."

Taking a New Position With the Board

The strategic goals for Global Internal Audit align with Aegon's strategic objectives: loyal customers (or clients, in the case of internal audit); operational excellence; empowered employees; and optimized portfolio. Three "driving principles" also guide Global Internal Audit:

- **Positioning:** "This relates to how internal audit collaborates with Aegon's board of directors," Van den Berg explains. "In the past, the function was more traditional, interacting mostly with senior management. But now we have truly qualified leaders in audit who can engage at the board level and be trusted advisers. That helps give us credibility with the board, and to be recognized as an independent function."
- **People:** Since 2010, when he began building the Global Internal Audit function for Aegon, Van den Berg has been working to hire highly skilled business professionals for his team — and not just career auditors.

  "We've been recruiting people who have a good balance between audit expertise and business acumen and expertise," he explains. "We find that our clients greatly appreciate it if the person across from them understands their business." This balance is especially important for the audit leaders who interact with the board to possess, he adds.
- **Processes:** "This principle is about the way we work — and achieving operational excellence," says Van den Berg. "We align with international audit standards, and The Institute of Internal Auditors is obviously very important to us. We have global charters, reporting lines, methodology, quality assurance programs and consistent key performance indicators (KPIs)."

As part of establishing the global function, Van den Berg appointed, in addition to the chief audit executives for Aegon's country units, two CAEs for the following global business lines: Aegon Asset Management (AAM), the company's investment management arm, and the Global IT Office. He also developed a "matrix" that outlines the reporting structure for the audit directors at Aegon's strategic business units.

"They all have dual reporting lines to the CEOs of the strategic business units and also to me. That helps to underpin their independent positions," says Van den Berg. "You can have a ton of charters, but what is truly important is to have a team that supports the structure of the function. Everyone needs to support the model wholeheartedly if the function is to operate successfully."

Leaving the Comfort Zone to Build a Strong Culture

Under Van den Berg's guidance, Global Internal Audit has started to take thoughtful steps toward developing a formal global program for auditing culture at Aegon. "Auditing culture is sensitive because you are auditing people's attitudes and behavior," he says. "You must do it well — and not everyone can."

When Van den Berg first started to think about conducting culture audits and the value the process might provide to Aegon, he says he immediately recognized that it was essential to build a strong culture in Global Internal Audit first. "We believe we should lead by example," he explains. "We knew that if we didn't have a strong culture, we would lack the credibility to run culture audits."

Among the steps taken to strengthen the internal audit culture at Aegon is a culture program that was launched within the U.S. Transamerica audit team. Van den Berg says the program "internalizes cultural beliefs, like trust, as well as acting as one team, embracing change, being accountable and speaking up." He says, "We share stories about our experiences and provide appreciative and constructive feedback to each other."

Van den Berg also points to the work that Rinus de Hooge, CAE for AAM, has been doing to foster a strong culture with his global team. He says it represents the next step of what the Global Internal Audit function is striving to achieve on a broader scale within the company.

Soon after joining Aegon in 2015, de Hooge started recruiting auditors for his team who would work at the company's locations in the Netherlands; Cedar Rapids, Iowa; and Edinburgh, Scotland. He says he quickly realized that his auditors, due to their geographical separation, could easily face communication problems. They also would have little or no opportunity for personal interaction. And both conditions could lead to culture problems that could undermine the team's success.

So, de Hooge took the initiative to meet these potential obstacles head on. He arranged for his newly assembled team of 12 to meet in the Netherlands for three days. But they didn't go to Aegon's headquarters right away. Instead, they spent two days at an archaeological theme park built on the site of an ancient Roman settlement and located near de Hooge's home.

We believe we should lead by example. We knew that if we didn't have a strong culture, we would lack the credibility to run culture audits.

"This got everyone out of their comfort zone," says de Hooge. "Our first objective was to get to know each other. We also talked about values and mission statements during those two days. I strongly believe that if people share common values, they can work more effectively toward the same goal."

This exercise, according to de Hooge, also helped to lay the foundation for trust throughout his internal audit team. His next goal is to extend the collaborative culture in AAM even further by building a "team of teams" with auditors from different countries working together on the same assignments or helping each other to perform audits in their locations.

Maintaining a cohesive global team is a full-time job for de Hooge, who says he reads books on anthropology and team-building to deepen his understanding of how to build and maintain a strong culture and assess soft controls. He also shares knowledge and insights about culture with his team through newsletters and frequent discussions by phone. He regularly travels to his team members' offices so he can engage with them in person, too.

He says, "It's a different way of working. It requires a lot of time and communication and talking about the softer side of working together. I also make sure everyone knows that they can reach out to me when they have an issue, and I will back them up. That is very important for people to know when they work far away from the head office."

Looking for a Special Set of Skills

The "team of teams" concept de Hooge is instituting at AAM has Van den Berg thinking about how to implement the same practice at the global level. He has already established "centers of excellence," like the global professional practices group. Van den Berg now envisions creating dedicated audit teams with global resources focused on thematic audits on one area of expertise, like actuarial or risk management. These specialized teams could be deployed to perform thematic audits at any Aegon location, anywhere in the world.

As for auditing culture at Aegon, Van den Berg says Global Internal Audit is now at what he considers "a halfway mark" toward developing a formal program. The first step, which Global Internal Audit completed with help from an outside consultant, was to determine what criteria to use when auditing culture. They found that basic criteria in Aegon's own values: working together, bringing clarity and exceeding expectations.

"We linked our audit findings and observations to those company's values," says Van den Berg. "We did not provide ratings because we were not mature enough in our skills to do that. But we did provide our observations in the management summary of our audit reports."

Cultural aspects are also now being included in more traditional audits; for example, auditors review incentive programs and the KPIs tied to them.

While this was a good starting point for building a culture audit program, Van den Berg says the process didn't have enough impact. So, Global Internal Audit took another step: developing a "Risk and Control Culture Toolkit" based on the Financial Stability Board's (FSB) guidance for assessing risk culture.[1] The four elements in the FSB's framework are tone from the top, clear incentives, accountability, and communication and challenge.

Global Internal Audit is applying the framework elements by first conducting tone from the top interviews to establish what senior management thinks the risk and control culture is. Then, using surveys, they are testing whether the company's values are "being lived throughout the organization," says Van den Berg.

The team is currently piloting this "target culture audit" process in Aegon's U.K. operations. According to Van den Berg, cultural aspects are also now being included in more traditional audits; for example, auditors review incentive programs and the KPIs tied to them.

[1] "FSB releases *A Framework for Assessing Risk Culture and Progress Report on Enhanced Supervision,*" media release, FSB, April 7, 2014: www.fsb.org/2014/04/pr_140407/.

However, Van den Berg says he does not view surveys as the most reliable approach to auditing culture because the answers are prepared. Auditors interviewing staff in person and getting a firsthand look at the culture in place in an area of the company is a better approach, he says. So, the surveys serve only as a next step toward achieving Van den Berg's ultimate vision for Aegon's culture audit program.

"The final part of our journey will be truly being able to observe the attitudes and behavior of people," he says. "Again, it's a very sensitive area, and you need to have credibility with the auditees. Saying something about people's behavior is very different from saying something about hard controls. The skills you need to do that are more like those of a psychologist than an auditor."

To obtain those skills, Van den Berg says he plans to hire people for the Global Internal Audit team who have these specific capabilities — for example, professionals with a background in psychology. Those skills will be especially important for reporting findings from audits of culture, he says.

"I think once we reach the final phase of our program, where we are assessing attitudes and behavior, it will become even more challenging to document our observations," Van den Berg explains. "We must be very careful about what we say, and we need people who have the credibility to do it. Those people are not traditional auditors."

Eagle Warrior: Aeromexico's "Atmosphere Project" Connects Company and Culture

When employees believe that the organization is serious about embracing its core values, they are willing to invest more of their discretionary effort into things that can't be mandated, such as innovation, initiative and teamwork.

— Mario Torres Rangel,
Audit Senior Vice President

EMPLOYEES IN COMPANY:
14,084

INDUSTRY:
Aviation

ANNUAL REVENUES:
US$2.7 billion
(as of March 31, 2017)

NUMBER IN IA FUNCTION:
29

YEARS IA FUNCTION HAS BEEN IN PLACE:
5

IA DIRECTOR/CAE REPORTS TO:
Audit Committee

Aeromexico, founded in 1934, is the flag-carrier airline of Mexico. It operates scheduled services to more than 80 destinations in Mexico; North, South and Central America; and the Caribbean, Europe and Asia. Officially known as Aerovías de México, S.A. de C.V., it is one of six companies owned by Aeromexico Group, which also owns Aeromexico Connect (for regional flights), Aeromexico Cargo, Aeromexico Servicios (for maintenance and repairs), Aeromexico Training and PLM (a loyalty program).

From the Aztec *Cuāuhtli* eagle warrior in its corporate logo to its landmark headquarters on Paseo de la Reforma in Mexico City, overlooking the famous "Diana the Huntress" fountain, Aeromexico is a company steeped in national culture. A founder of the SkyTeam global airline alliance, along with Air France, Delta Air Lines and Korean Air, the company has also played a significant role in shaping global connectivity and the codesharing culture within the airline industry. (Codesharing refers to a business arrangement where two or more airlines share the same flight.)

Aeromexico is now in the process of reinforcing its own corporate culture with a formal initiative focused on leadership, effectiveness, commitment and service. *Proyecto Atmósfera*, the "Atmosphere Project," launched in 2016, is based on the premise that organizational culture affects all aspects of performance, from finances to operations to reputation. Within that context, the internal audit function at Aeromexico is working to do its part by strengthening control structures and regulatory frameworks.

A Culture of Accountability

Mario Torres Rangel, Audit Senior Vice President at Aeromexico, joined the company in 2011. In his current role, Torres Rangel oversees a team of 24 auditors, with help from an assistant and two deputy directors — one for IT audit and the other for operational audit. His team is currently focused on a full slate of transformative initiatives, from real-time audits and continuous monitoring to strengthened fraud prevention and cybersecurity risk assurance.

These short-term initiatives are part of a culture of accountability driving internal audit toward its long-term goal of serving in a consultative capacity to other divisions and companies within Aeromexico Group. "To do this, we must use state-of-the-art technology and integrated analysis to orient our work to strategic risks and help adapt controls to changes in the company," Torres Rangel says.

The internal audit department also makes recommendations on cultural risks and plans to begin conducting specialized corporate culture audits in the second half of 2017, according to Torres Rangel.

Risk Culture Integration With Organizational Culture

Risk appetite is a subset of organizational culture that includes tolerance for, and management of, risk. The internal audit function at Aeromexico evaluates the general working environment to identify any formal or unwritten "rules" governing employee interactions and practices that are inconsistent with Aeromexico's core values.

Clear assignment of responsibilities ensures that each risk and control group understands the limits of their duties and how they fit into the overall risk position of the organization and the control structure.

There is a tendency, says Torres Rangel, for risk culture to promulgate controls at the department or operating unit level that may be redundant of controls in other departments or divisions. Similarly, a siloed organizational culture could create gaps in risk management, if controls and practices are not aligned across all lines of risk defense with a clear understanding of how individual and group efforts combine for the greater good.

"The challenge is to coordinate roles among various work groups, using The Institute of Internal Auditors' 'Three Lines of Defense' risk management model, so that there are no gaps or redundancies created by unnecessary controls or duplication of effort in some risk areas to the detriment of others," Torres Rangel explains. "Clear assignment of responsibilities ensures that each risk and control group understands the limits of their duties and how they fit into the overall risk position of the organization and the control structure."

The Atmosphere Project

Recognizing that the organizational culture can positively (or negatively) affect the finances, operations and prestige of the enterprise, Aeromexico's board launched the Atmosphere Project in 2016. The enterprisewide cultural initiative encourages employees and third-party vendors to work together across departmental and divisional lines to help the company succeed in the ultracompetitive airline industry. Torres Rangel says the project kickoff was a key event that demonstrated a shared commitment by the company, partners and employees to achieve a balanced life, passion for work and optimal performance.

The program employs four pillars to promote a positive environment, strengthen control structures and create an adequate regulatory framework:

1. **Leadership:** *Inspire by example.*
2. **Effectiveness:** *Focus on results.*
3. **Commitment:** *Do your best.*
4. **Service:** *Demonstrate human warmth.*

"The chairman of the board, the CEO, senior management and all stakeholders are fully engaged with the Atmosphere Project," says Torres Rangel. "We believe it will improve our organizational culture by obtaining improvements in financial, operational and organizational matters."

Indicators of a Strong or Weak Corporate Culture

At Aeromexico, a strong corporate culture is considered one in which core values are strongly held and widely shared. Torres Rangel says, "When employees believe that the organization is serious about embracing its core values, they are willing to invest more of their discretionary effort into things that can't be mandated, such as innovation, initiative and teamwork."

Following are some indicators that Aeromexico looks for as evidence of a healthy culture under the Atmosphere Project:

- **Innovation** — the extent to which employees are encouraged to be innovative and take risks
- **Attention to detail** — the expectation that employees will demonstrate accuracy, analysis and attention to detail
- **Results orientation** — the degree to which management focuses on results or consequences, rather than on the techniques and processes used to achieve them
- **People orientation** — how often management takes into account the effect of their results on people within the organization
- **Team orientation** — the level to which work activities are organized around teams, rather than around individuals
- **Energy** — the degree to which workers are energetic and competitive, rather than apathetic
- **Stability** — the extent to which organizations prefer maintaining the status quo rather than insisting on growth
- **Initiative** — the degree of responsibility, freedom and independence that individuals have
- **Control** — the number of rules and amount of direct supervision used to control employee behavior
- **Identity integration** — the degree to which employees identify with the organization as a whole, rather than with their particular work group or professional field, and organizational units are encouraged to collaborate
- **Incentive system** — the degree to which incentives such as salaries and promotions are based on criteria of employee performance rather than criteria such as seniority or favoritism
- **Conflict tolerance** — the degree to which employees are encouraged to air conflicts and criticisms openly

- **Communication model** — the degree to which organizational communications are restricted to the formal hierarchy of authority

Meanwhile, in a weak corporate culture, there is little alignment with the values of the organization; thus, control must be exercised through exhaustive procedures, says Torres Rangel. In his view, some red flag characteristics of weak cultures are:

- Close supervision
- Narrow freedom in staff performance
- Standardized jobs
- Formalized rules and procedures
- Production-focused rather than people-focused management
- Unclear productivity levels
- Minimal levels of constructive conflict
- Dysfunctional or destructive conflicts
- Low risk propensity
- Discouragement of innovation
- Lack of appreciation or reward for loyalty, effort or cooperation

The board of directors establishes the desired corporate culture, says Torres Rangel. The culture is then disseminated throughout the organization, by everyone, through adherence to central values and a code of ethics that details acceptable versus unacceptable behaviors.

"Unacceptable and unethical behaviors put the organization at risk and contribute to a toxic culture associated with misconduct, fraud and corruption," Torres Rangel explains. "Any example of unacceptable or unethical behavior should be a wake-up call for internal audit to perform a culture audit to ensure that the organizational culture is consistent with core values, ethical conduct, and compliance with laws and regulations."

Auditing Corporate Culture

Torres Rangel's research in preparing for the launch of corporate culture audits determined that an effective corporate culture audit describes the overall work environment. He says it also identifies written and unwritten rules governing employee interactions and practices in the workplace, determines potential barriers to work practices and communication, and allows auditors to make recommendations to address identified issues to strengthen corporate culture.

Some examples of the questions Aeromexico's internal audit team plans to start asking include:

1. Are you being compensated fairly?
2. Are your profits comparable to those of the company's competitors?
3. Does the company value your work?
4. Are you receiving the training you need?
5. Is there open communication in the company?
6. Do you feel challenged?
7. Do your values match those of the company?

"Those questions are routinely asked in exit interviews," Torres Rangel says. "Why wait for the answers until after the company has already lost its investment in an employee?"

Any example of unacceptable or unethical behavior should be a wake-up call for internal audit to perform a culture audit to ensure that the organizational culture is consistent with core values, ethical conduct, and compliance with laws and regulations.

Torres Rangel expects cultural audits to reveal potential friction points and create possibilities for internal process improvements, as well as sources of synergy that can be replicated across the organization. Aeromexico's current general audits include a review of adherence to the company's code of ethics and code of conduct, as well as an assessment of how behavioral expectations are disseminated and promoted throughout the organization.

The company has also created an ethics committee to define issues that strengthen organizational culture. Many of the topics covered by the committee originate over the complaint hotline, which is externally administered to provide anonymity to its users.

Keys to Successful Cultural Audit Programs

Auditing for culture is a complex undertaking that draws on a wide range of "soft," as well as technical, skills. In preparation for Aeromexico's first culture audit, Torres Rangel trained his audit team to evaluate key cultural indicators such as leadership, feedback, anti-corruption, bribery, workplace satisfaction and management skills.

A culture audit, in itself, is a cultural change. So, Torres Rangel has had to hone his own communication skills so he can build strong relationships at all levels of the organization and pave the way for his auditors.

"Tone at the top, middle and bottom are critical to getting buy-in for this kind of cultural change," he explains. "Executive leadership from top management, human resources and the audit committee will be key to making our cultural audit program a success."

Building a Sustainable Risk Culture at Bpifrance SA

The reason the [Bpifrance risk culture] is so strong is that our risk policy is built on the fact that we want to develop an ecosystem that helps companies and supports entrepreneurship for generations to come. To accomplish this, we need to be sustainable today, tomorrow and into the future.

— Michel Cadelano, Inspecteur Général

EMPLOYEES IN COMPANY:
2,500+

INDUSTRY:
Finance (Banking)

ANNUAL REVENUES:
N/A

NUMBER IN IA FUNCTION:
21

YEARS IA FUNCTION HAS BEEN IN PLACE:
5

IA DIRECTOR/CAE REPORTS TO:
CEO

Banque Publique d'Investissement SA (Bpifrance), founded in 2012 and headquartered in Paris, offers financing, private equity and venture capital, and export assurance services through three primary subsidiaries. Those businesses are Bpifrance Financement, with a network in France comprised of 2,000 employees; Bpifrance Participations, which employs 400; and, as of January 2017, Bpifrance Assurance Export, with 250 employees. Functional departments such as Finance, Technology, Compliance, Legal, Human Resources, Communications, General Resources, and Audit provide support to these businesses.

Michel Cadelano is the Inspecteur Général of Bpifrance. He oversees a team of 21 in the company's Inspection Général — Audit (IGA) department. He reports hierarchically to CEO Nicolas Dufourcq, and functionally to the board.

"Audit's primary mission is to be the third line of defense," says Cadelano, referring to the three lines of defense in risk management and control. The first line is Operational

Management, the second line is the Risk Management and Compliance functions, and the third line is Internal Audit.

"Since last year, we have been using cartography, or risk mapping, of residual risk for key activities, such as asset liabilities management or equipment finance," says Cadelano. "Before that, we had a cartography of risks for each organization unit, which was more focused on the organizational matter. This new risk map helps the Audit department shape our three-year audit plan, identifying the risk level of activities to audit. It is updated once a year."

Our motto is 'Serving the Future' and our corporate culture is the basis for all our actions and vital to all our activities.

The IGA team's central short-term goal is to design an audit plan that can cover all the major risks of the activities of the Group within three years. According to Cadelano, each "audit mission" is risk-oriented, meaning it should be more a strategic audit and less an audit of compliance. Each mission should align to the risk map and contribute to the next upcoming audit plan. Key performance indicators in the business are systematically assessed during each mission to make sure that the approach is executed and on target with the strategic business plan. The secondary short-term goal of the audit mission is to identify risks before they happen, or before they are assessed by external supervisory bodies.

In the longer term, Cadelano says, "First, we want to have a fully automatic system wherein risks that are identified can immediately update the risk cartography and the global schedule system, including budgeted workload dedicated to each mission, leading to an ongoing risk assessment process."

An additional long-term goal is to be able to better evaluate the added value of an audit mission, by determining how often or to what extent it prevents a negative event. "For example, we should be in a position to evaluate potential costs for the organization if a risk evolves into an incident," Cadelano says. "We could also measure the probability of that happening. We want to be as strategic as possible, contributing to building new businesses and new devices."

Serving the Future

"Bpifrance is a trusted partner for entrepreneurs, financing businesses from the seed phase to transfer to stock exchange listing, through loans, guarantees and equity," says Cadelano. "Our motto is 'Serving the Future' and our corporate culture is the basis for all our actions and vital to all our activities. Monitoring and shoring up our culture starts with the CEO and extends to the Communications, Institutional and Media Relations departments; of course, the Executive Committee as a whole, and also each executive director, is accountable for the risk culture. It is part of their responsibility to develop and explain a measurable risk culture for the company, first for healthy management, but also because boards and regulators are assessing the way this risk culture is managed, measured and improved."

"I would add that everyone here is an owner of the Bpifrance culture," Cadelano says. "The reason the risk culture here is so strong is that our risk policy is built on the fact that we want to develop an ecosystem that helps companies and supports entrepreneurship for generations to come. To accomplish this, we need to be sustainable today, tomorrow and into the future."

He says the risk culture of Bpifrance shapes the company's corporate culture, "which is symbolized in our four institutional values: *Proximity, Simplicity, Optimism, and Drive*."

For Cadelano, strong corporate culture is represented by both a robust team spirit throughout the organization and high levels of customer satisfaction. "Weak culture is when there is a lack of consistency or coherence between actions and decisions," he says. "It is easy to be compliant with rules but more complex to truly integrate culture and consistency as a way of life in the organization."

Adapting to New Environments

IGA's audit plan includes standard missions focusing on credit, compliance and operational risks, but also incorporates a forward-thinking, strategic element that is centered on an assessment of the direction of the audited activity. That forward-thinking element asks where the activity or entity will be in the next two years.

It is easy to be compliant with rules but more complex to truly integrate culture and consistency as a way of life in the organization.

"This assessment helps us evaluate whether the activity or entity deviates from our cultural standards and institutional values," Cadelano says. "Then, at the end of each year, an executive summary of our findings helps us measure new possible 'positive' deviation from the culture. We call this adaptation, or versatility, to the new environment."

One example of such adaptability is the bank's willingness to co-finance. "We never finance or invest alone," Cadelano says. "We always do it with another partner."

BARCLAYS

Agile Auditing: Barclays Embraces Focus and Conversation in Return to Values

Habit trumps logic every time. If you want to replace an old cultural mantra with a new one, it takes a while for people to hear it, interpret it, understand it, accept it and then act on it with confidence.

— Sally Clark, Chief Internal Auditor

EMPLOYEES IN COMPANY:
129,000

INDUSTRY:
Financial Services

ANNUAL REVENUES:
GB£1.7 billion
(group profit before taxes; as of March 31, 2017)

NUMBER IN IA FUNCTION:
650

YEARS IA FUNCTION HAS BEEN IN PLACE:
N/A

IA DIRECTOR/CAE REPORTS TO:
Chair of the Board Audit Committee and the Group CEO

Barclays was formed in 1896 when several banks in London and nearby English provinces united. But the multinational banking and financial services company can trace its roots back to a London goldsmith banking business established in 1690. Today, Barclays is divided into two core businesses: Barclays International, housing Barclays investment banking, multinational corporate and overseas Barclaycard operations; and Barclays UK, its UK retail and SME banking, and Barclaycard's operations in the UK. Barclays' total assets top £1.1 trillion, and the global company employs more than 129,000 people.

Sally Clark joined Barclays in 2012 and was appointed Chief Internal Auditor (CIA) in 2014. A career auditor, she previously worked for nine years at the Royal Bank of Scotland after almost two decades at JP Morgan Chase. She reports directly to the Chair of the audit committee, and administratively to the CEO.

In her capacity as CIA, Sally heads the global audit functions across the company:

1. The retail, card, wealth and small business banking business within Barclays UK
2. The investment banking, corporate banking, capital markets, international card and private banking businesses in Barclays International

3. The operations and technology in the Corporate Operating Office — soon to be Service Company
4. Group functions — Risk, Finance, Compliance, HR and Legal

In addition, the management team comprises a central office to look at learning and development, quality assurance, strategy, change and operations with approximately 50 people. The internal audit team at Barclays comprises 650 people located across four continents.

The Art of Conversation and a Focus on Agile Auditing

The enduring mandate of the internal audit department at Barclays, according to Sally, is to provide independent, objective assurance to the audit committee that risks are managed in accordance with the risk appetite and the values of the firm. At present, the audit function is engaged in a transformation program looking at its organizational design, its methodology and its overall approach to completing its work. This includes a new approach, which is termed "Agile Auditing," which borrows as its basis the Agile project management approach in vogue within technology projects. When applied to audit, one of the key elements is a return to the "art of conversation" with teams engaging each other daily and working collaboratively together.

"Our teams stand together at a whiteboard each morning for 15 minutes and discuss the audit that they have in progress," Sally says. "The audit work underway is represented on the board and items are moved physically from left to right across the whiteboard. Because everyone is involved with the planning, fieldwork and reporting, there is huge efficiency in people talking together every day about what they need to do."

This "agile auditing" approach is also predicated on *not* multitasking. Auditors are engaged on one audit at a time, from start to finish, instead of trying to juggle multiple audits simultaneously. "It turns out that multitasking is the enemy of productivity in the agile methodology," Sally says.

Sally believes the adoption of the daily discussion at the whiteboard removes blockages and keeps work scopes tight. "It should stop people from going off and doing unnecessary testing," she says. At present, her audit team has resisted the urge to develop an automated electronic version of the whiteboard because they find the face-to-face conversations more efficient and motivating. Sally says the adoption of agile in a number of pilots has reduced audit duration by up to 30 percent. In addition, the team tried out an approach to writing an agile audit report and managed to get it finalized within two hours.

LIBOR Scandal a Catalyst for Cultural Transformation Journey

The London Interbank Offered Rate (LIBOR) fraud controversy of 2012 was a wake-up call for British banks to examine what drove the issues underlying the scandal. And it caused Barclays to embark on a cultural transformation journey. The firm asked Sir Anthony Salz to examine what had happened within the bank and make recommendations to prevent similar occurrences in the future. Sir David Walker, Chairman of Barclays, said at the time, "Mistrust and the perception of inadequate standards have led to a crisis of confidence, and it is severe. … We must not recoil from the shock waves, rather embrace the current reality and deliver the cultural change."

In his landmark report, which would form the basis of Barclays' cultural reformation, as well as provide broader insights applicable to the entire British banking system, Salz wrote about culture and values: "Culture is experienced socially and intellectually. … Values are the foundation of culture. They represent the core of what is important — the shared principles by which individuals and groups in organizations make choices. They help people to determine that which is right and wrong. Business practices are shaped by values."

Salz concluded that although Barclays had written ethics policies and a code of conduct, performance evaluation parameters tied to integrity were ill-defined, which led to confusion over what "good" looked like. Importantly, Salz wrote that a majority of Barclays' employees wanted to act with integrity, restore public trust, and rebuild an organization in which they and their customers could feel pride, but he indicated that could only be achieved if the Group, throughout all levels of leadership, consistently strengthened its efforts to define, embed and reinforce a sustainable culture suited to a modern, major financial institution.

Sally credits the 244-page "Salz Report" with providing a wake-up call that enabled the firm to create the cultural roadmap that Barclays has followed over the past four years. Embedding values takes time and needs the combination of determining what "good" looks like, weaving that picture into day-to-day processes, ensuring that people are recognized for living the values and are held to account when they don't.

Barclays rose to the challenges exposed in Salz's report by developing and implementing the corporate values of Respect, Integrity, Service, Excellence and Stewardship. And in terms of how these are embedded, one example is, Sally says, that Barclays now turns down business if it does not fit with the cultural aspiration of the firm.

Board Reputation Committee and Dashboards

Following the Salz Report, Barclays set up the Board Reputation Committee, an official structure under the Group Board. The Board Reputation Committee has oversight of how Barclays manages its conduct and reputation risks and focuses on the development and embedment of culture.

The Group Executive Committee also monitors key cultural risk factors through the use of dashboards that are utilized by each of the businesses and functions. "The dashboards show positive and negative trends and any hot spots related to certain elements from employee opinion surveys, complaint data, breaches, mandatory training, grievances, external measures and the like," Sally says.

The dashboard, which measures cultural risk across the whole firm, is organized by the five core values and uses RAG ratings to indicate where focus is needed.

The dashboards are created within the learning, talent and leadership teams within Barclays' HR department.

Cultural Change: "Like Moving a Tanker Rather Than a Speed Boat"

Even when change is highly desirable, such as a return to agreed-upon positive core values, implementation is sometimes difficult. "You'll have early adopters versus people who simply don't like change," Sally says. "Habit trumps logic every time. If you want to replace an old cultural mantra with a new one, it takes a while for people to hear it, interpret it, understand it, accept it and then act on it with confidence. Only then do the new habits replace the old ones."

Audit functions are now involved in auditing culture — as a result of The IIA Code (guidance issued by Chartered Institute of Internal Auditors) used within financial services. This is a very new field for internal audit to approach and is very different from the traditional areas that are audited, such as processes, systems and products. Looking at how to do this sometimes involves trying things that may not work out. That can be difficult when many audit functions are either risk-averse or are not of sufficient size to be able to experiment. Sally gives the example of a culture questionnaire they tried to use at the beginning of every audit. "We found in the end that it wasn't that helpful. It added massive amounts of time to the audit, but did not give us meaningful information to inform our audit conclusions."

The takeaway from this exercise is that not everything works and it's okay to fail. Internal audit at Barclays has continued to test different mechanisms to study corporate culture and are currently looking to use an approach based on Ethnography — a system of personal observation — something that auditors are naturally good at, says Sally.

"However, it's a challenge to audit intangibles such as culture," she notes. "We need to remember that auditors are not professional psychologists, and start from the perspective of having their own lens through which they make these observations. They do not start from a completely neutral point."

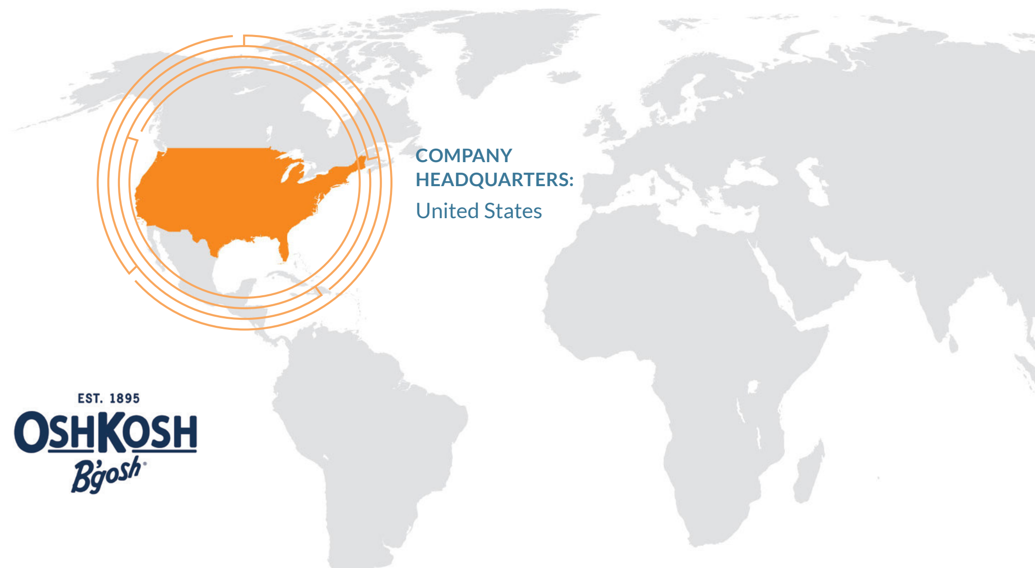
Although Sally has not, to date, hired any professional psychologists, she and her team have been working with the UK Banking Standards Board and have attended some of their training courses.

According to Sally, changing corporate culture is more like moving a tanker than driving a speed boat. Some people will embrace and make change quickly but for many this is a long journey that takes time. She says a starting point is to be able to see visible signs of the tone from the top permeating through middle management and then bouncing back up from the bottom of the firm.

Surprises: A Sign of Weak Culture

Sally says a strong corporate culture is one where problems and challenges are regularly surfaced and resolved through communication and a commitment to integrity and continuous improvement. Where a business finds its own issues, raises them and fixes them within a reasonable time period and where it encourages open dialogue among colleagues to ensure best practice — this is a sign of a good culture.

If issues arise during an audit and they are a big surprise, she says, it's an indicator that people may have hidden issues — or, at least, they haven't escalated them through the proper channels. "If internal audit is finding a lot of things that the business hasn't found out for itself, that's also an indication that the business doesn't understand its own vital role in discovering and managing risk," Sally says.



Carter's, Inc.: Collaboration Keeps the Culture Strong

Our executive leadership team has a good understanding of what a strong culture means to the organization, and that we can't meet our objectives unless people are willing to stand up and tell us what's right and what's wrong with the company.

— Julie Schoen Hower, Vice President of Internal Audit and ERM

EMPLOYEES IN COMPANY:
18,300

INDUSTRY:
Retail

ANNUAL REVENUES:
US$3.2 billion
(as of December 31, 2016)

NUMBER IN IA FUNCTION:
8

YEARS IA FUNCTION HAS BEEN IN PLACE:
14

IA DIRECTOR/CAE REPORTS TO:
Audit Committee; administratively to General Counsel

William Carter, a British immigrant, knitted cardigans in his kitchen in Needham, Mass., during the Civil War. The Carter family sold the business in 1990, and it passed through a handful of owners before an initial public offering in 2003. Today, Carter's, Inc., based in Atlanta, Ga., is North America's largest branded marketer of baby and children's apparel and accessories.

The company is best known for its flagship brands, the eponymous Carter's and OshKosh B'gosh, both of which have been household names for more than a century. Leading department stores, national chains and specialty retailers in 100 countries sell Carter's products. The company also sells them through its website and in nearly 1,000 company-operated stores in the United States and Canada. In 2016, Carter's, which trades under the symbol CRI on the New York Stock Exchange, reported annual revenues of US$3.2 billion.

Julie Schoen Hower, vice president of internal audit and enterprise risk management (ERM), joined the company in 2012 after more than a decade as an auditor with a leading audit consulting firm. She oversees an internal audit group of eight people with a mission of enhancing and protecting organizational value by providing risk-based and objective assurance, innovative solutions, and strategic insights. Hower reports to the audit committee, and administratively to the general counsel.

The Cultural Imperative

Hower cites the need to live up to customer, consumer and shareholder expectations as drivers of a strong and transparent corporate culture at the company. "There has always been an emphasis on culture at Carter's, perhaps stemming from the fact that moms and dads trust our company with clothing their young children," she says.

Carter's deep roots as an iconic American brand, its fiduciary responsibilities as a publicly held enterprise and its evolving global business landscape — which includes international sourcing and expanding points of distribution — require that the company make culture training and monitoring top priorities, Hower says.

"As we expand our employee and vendor base and acquire new companies, it is critical to assimilate them into our culture from day one," she explains.

The Carter's culture begins with a personal commitment to the company's core values:

- Act with integrity
- Exceed expectations
- Succeed together
- Inspire innovation
- Invest in people

Carter's also sets up workshops and provides multimedia training materials to help employees understand, from their first day on the job, their specific role in risk and compliance — the obligation to behave ethically and to report unethical behavior — and how to escalate issues they might encounter.

Hower says employees, at all levels, are encouraged to "raise their hand" and stand up for what's right when they observe activities or behaviors that raise risk or compliance concerns, and that managers are trained to take such concerns seriously and act on them promptly.

"There is an expectation that all leaders — not just 'leadership' — model our values," she says. "Strong leadership promotes a strong culture, and a strong culture is critical to the achievement of our strategic objectives."

Integrating Culture, Risk Culture and Compliance

Culture is so central to Carter's strategy that it is audited as part of the overall ERM strategy. Hower says internal audit includes 12 risk culture questions in an annual ERM survey. The human resources (HR) function also incorporates culture questions in its employee surveys. Both surveys are anonymous. Results of the annual surveys are analyzed and shared with all participants, including the board. Action plans are also developed to address opportunities and demonstrate leadership's commitment to a continuously strengthened culture.

Hower says internal audit also embeds culture questions in its audits. Results are consolidated and shared with the CEO and audit committee quarterly.

"Protecting our brands is a tremendous responsibility, and it is critical that we act with integrity in everything we do," explains Hower. The CEO and entire leadership team at Carter's echo this belief, she says, and that has helped to evolve the ERM program and survey process from a paper exercise to a valued program.

"Our executive leadership team has a good understanding of what a strong culture means to the organization, and that we can't meet our objectives unless people are willing to stand up and tell us what's right and what's wrong with the company," Hower says.

Cascading Expectations

Executive support is key to getting momentum behind the program and having "risk" and "culture" as part of the daily dialogue, according to Hower.

But executive support only goes so far. Studies have shown that direct supervisors have the greatest impact on employee behavior.[1] Hower says the internal audit function at Carter's looks beyond the tone at the top to the tone at the middle and bottom to determine whether expectations are cascading to all levels within the organization.

"Engagement at all levels improves internal audit's ability to identify root causes and recommend impactful remediation," she says.

Follow-through is also important. Hower says, "Our culture survey is valued because we don't just take the survey results and say, 'I wish we did better.' We come up with action plans to say how we're going to continuously improve results or understand why we have certain perceptions. Action owners are assigned. There's substantial follow-up, and it has the visibility of the full board. Our survey respondents realize the results are reviewed at the highest levels of the organization, and it helps us achieve 100 percent participation."

Relying on Relationships

The internal audit team at Carter's has not attended any specific training for auditing culture, but Hower says they have conducted extensive research on the subject. She adds that internal audit is also well-suited to assess culture because of the extensive network of relationships auditors have developed with employees and management in every department of the company over the years.

Our culture survey is valued because we don't just take the survey results and say, 'I wish we did better.' We come up with action plans to say how we're going to continuously improve results or understand why we have certain perceptions.

"They are trusted by other employees as ethical watchdogs who genuinely care about risk management and ethical concerns," she says.

Ongoing collaboration among the internal audit, legal and HR functions helps to ensure that surveys are focusing on the right risks and that questions are designed for optimal response. One outcome from this collaboration has been the addition of an open-ended response opportunity for each question, and a mandatory explanation of any specific concerns.

Additionally, Carter's CEO sends out the internal audit risk survey, along with a call for 100 percent participation. This demonstration of support helps response rates tremendously, says Hower.

Going forward, Hower says she plans to add more culture questions into company surveys, which go to all levels of the company. She also plans to expand the scope of the internal audit survey to include middle management, so her team can measure how well cultural leadership is communicated.

[1] "Sustaining an Ethical Culture," *Tone at the Top*, Issue 68, The Institute of Internal Auditors, June 2014, https://global.theiia.org/knowledge/Public%20Documents/TaT_June_2014.pdf.

"The tone at the top is very strong," she says, "But if those ideas aren't cascading down, we have a problem."

Other examples of cultural collaboration include a new "Risk and Compliance Guide" for new hires. HR, legal, finance and internal audit created the publication to help acculturate new employees with key information, including:

- Compliance expectations
- Department-specific strategic priorities
- Risks to achieving those priorities

Legal and internal audit have also teamed on in-person, global presentations to communicate the company's "raise your hand" ethics violation reporting policy. "Hotlines are important," Hower says. "But you need more than that. Employees need to know who they can trust with an ethics complaint. They need to know that we are tracking complaints and we are going to act on them."

Proof of a healthy culture is observed in employee behavior — at the top, in the middle and at the bottom of the organization.

Engaging Employees

Focusing on culture can pay dividends, Hower says, even at a company like Carter's, where the increased audit and risk management attention has led to a greater awareness and improved employee perception of corporate culture, as measured by the annual survey.

For example, survey results have shown an increase in employee-reported awareness of risk and compliance roles from the day of hire. And employees in international locations have expressed a clear understanding of travel and expense policies as well as policies on "facilitation payments" — such as bribes paid to foreign officials to gain a business advantage. Facilitation payments are prohibited under the Foreign Corrupt Practices Act (FCPA).

"One thing I love about our training is that it's very interactive," Hower says. "Our associate general counsel will quiz people to remind them that our values and code of conduct are not just things that we read, but characteristics we should be living."

Having spent much of her career as a consultant, Hower says she has had the opportunity to observe a variety of corporate cultures. Based on that experience, and the success she has seen at Carter's, she offers the following tips for auditing culture:

- Collaborate with other functions, such as compliance and HR, that may already be conducting culture surveys to determine how internal audit can best align their independent evaluation.
- Develop a series of questions that auditors can embed within each audit. Topics might include whether employees understand their compliance responsibilities from day one and whether they fear retaliation for reporting activities and behaviors that are in violation of the company's core values and code of conduct.
- Communicate trends, and root causes, to the CEO and the board.
- Collect limited demographic information, such as an employee's location (by country, and level of the company), to facilitate data analytics without compromising confidentiality.
- "Slice and dice" data using visualization tools to help identify truths and trends that might be hard to glean from raw data.

Hower says the proof of a healthy culture is observed in employee behavior — at the top, in the middle and at the bottom of the organization.

"With compliance, it's a little more black and white," she says. "You know when something is wrong or unethical. When it comes to risk, sometimes people are hesitant to raise their hand and say they think we're taking too much risk or we're not taking enough risk because they don't want to be the naysayer in the room."

Next Steps

Carter's implemented an SAP enterprise resource planning (ERP) system in July 2016, and internal audit is looking for ways to leverage data analytics for risk monitoring and reporting. In conjunction with the SAP ERP rollout, the company recently implemented Riskonnect, an automated ERM tool that allows the business to track not only high-level risks, but also sub-risks and risk events, such as a strengthening dollar's impact on sales from international customers. Over the next several months, Hower's group will be working to raise awareness regarding the availability of the tool and its capabilities.

Over the long term, Hower says her team's efforts will be largely data-driven, focused on using the ERM tool to provide actionable information to help the company achieve strategic priorities. That, in itself, is a cultural change — one that is already underway.

This data-driven culture is part of a bigger strategy to position the internal audit function at Carter's as a strategic adviser to both senior management and the board of directors. Hower says her team spends no more than 40 percent of their time on more traditional internal audit activities like Sarbanes-Oxley compliance testing. They focus the rest of their time offering objective advice to management on ways the company can meet its growth objectives.

"We typically get very high marks on that, and we're seen as a trusted adviser," she says.

CDKGlobal

CDK Global Seizes Opportunity to Build New Culture from Scratch

We are designing our own "corporate uniform" — custom fit to our industry — to grow our employees, and best serve our customers. Audit has the opportunity to ensure the organization has the culture it wants and that we're making the right progress.

— Katie Shellabarger, Vice President, Chief Audit Executive

EMPLOYEES IN COMPANY:
8,700

INDUSTRY:
Technology Solutions

ANNUAL REVENUES:
US$2.1 billion
(as of June 30, 2016)

NUMBER IN IA FUNCTION:
7

YEARS IA FUNCTION HAS BEEN IN PLACE:
3

IA DIRECTOR/CAE REPORTS TO:
Audit Committee (functionally) and CFO

Cultural challenges related to risk issues and resistance to change consistently rank among top executives' concerns.[1] It was a different cultural challenge — the opportunity to build a new culture — that faced the executive team at CDK Global, LLC (CDK) as they left the corporate umbrella of ADP in October 2014 and became a stand-alone publicly traded company.

Based in Hoffman Estates, Ill., CDK is a global provider of information technology and digital marketing to the automotive retail industry and adjacent industries. It serves clients in more than 27,000 retail dealer locations, and most of the original equipment manufacturers, in more than 100 countries. CDK's systems automate and integrate all parts of the buying process, from digital advertising and marketing campaigns to the sale, financing, insuring, repair and maintenance of vehicles.

CDK was hardly a startup when it became a separate corporate entity with a new executive team and board of directors. CDK was started

[1] *Executive Perspectives on Top Risks for 2017*, Protiviti and North Carolina State University's ERM Initiative, December 2016, www.protiviti.com/toprisks.

in 1972 as a division of ADP and grew to have almost 9,000 employees and more than US$2 billion in revenue before the 2014 spin-off. Independence put CDK at a crossroads, however; it had to decide how much of the old culture to keep, and what its new culture would look like.

Katie Shellabarger, Vice President and Chief Audit Executive for CDK, explains, "The spin-off provided an opportunity for CDK to build on the cultural legacy of ADP, while at the same time energizing itself with new people, who bring new ideas and practices."

Building Relationships, Setting Expectations

Shellabarger joined CDK just before the spin-off to establish and build out the audit and enterprise risk management functions. Before that, she worked in a variety of senior audit positions at large corporations and global consulting firms. Her internal audit department has seven full-time employees, with a co-source model that allows her team to flex according to project resource needs and to scale as the company grows. Internal audit reports functionally to CDK's audit committee of the board and administratively to the CFO.

"Our long-term goal in internal audit is to be a strategic partner to the business and to add value to the organization through our audits and consulting projects. But since we're a relatively new shop, we're starting small — building our internal audit brand and our credibility with our audit clients," she says.

To date, internal audit has focused on:

- Educating the business on the role of internal audit;
- Building relationships and trust across the organization;
- Executing audit plans timely;
- Communicating trends and issues to senior management and the audit committee clearly; and
- Monitoring company culture on an ongoing basis to determine whether core values are upheld.

"Since we're new, every audit we execute is being performed for the first time, and it requires extensive education of the audit client," Shellabarger says. "This also gives our department the opportunity to create our brand."

Shellabarger says the internal audit function is building a foundation based on understanding, trust and valued insight.

"What this means is that we need to understand the business," she says. "Our audit clients need to understand our role. We need to have a basis of mutual trust. Lastly, internal audit has to deliver valued insight. Without these, we will never achieve the objectives we've set for our team."

Everything Is New, So Everything Is Change

Since spinning off from ADP, the company's people, processes and technology have undergone significant change. First, there was the spin-off itself. "The biggest change was going from being *part* of a public company to *being* a public company," says Shellabarger.

CDK also initiated a three-year business transformation plan (BTP) shortly after going public to streamline operations, maximize capital allocation and improve the customers' experience with CDK products and services. These two events introduced unprecedented change to the organization, says Shellabarger: "The spin-off and the BTP have touched every aspect of our business, changing people, processes and technology."

Internal audit must be sensitive to these changes when considering the annual audit plan. There are scores of projects in process, so internal audit tries to give management the time it needs to complete projects. But some projects have a long tail. "It's a balancing act, for sure," Shellabarger says. "We want to give management the time it needs, but we also want to ensure the organization is properly managing risk."

With so much in flux, internal audit is seeing an opportunity to understand and evaluate the evolving culture of CDK. To Shellabarger, the key questions are, "To what is the culture evolving? Is this the culture the company wants? Does the entire organization 'buy in' to the CDK culture?"

Providing Education and Instilling Accountability

"One of my first jobs out of college was at a global professional services firm," Shellabarger says. "The culture was given to me very early on. We were told the culture standards, and we were expected to live and represent the firm's brand. There was no flexibility. You either accepted the culture, in which case you thrived, or you didn't, in which case you were not likely to stay long with the firm."

CDK refuses to accept historical practices as dogma. "We are encouraged to challenge and change these practices to be more efficient and effective," says Shellabarger. "This has created an opportunity for the cross-pollination of ideas."

What draws Shellabarger to evaluate culture at CDK is the fact that the culture is new and evolving, she says. "We are designing our own 'corporate uniform' — custom fit to our industry — to grow our employees and best serve our customers. Audit has the opportunity to ensure the organization has the culture it wants and that we're making the right progress."

For her part, Shellabarger says that working as a consultant gave her a broad survey of best practices and a sense of what worked and what didn't.

"As a consultant, I often parachuted into companies for long periods of time," she says. "I needed to acclimate to and understand the culture to make the project successful. I got to see a variety of cultures and evaluate in my own mind their effectiveness. It has made me adaptable and able to benchmark against some best practices based on my personal experiences. My management team brings that experience, as well."

The perspective on culture is enhanced, she says, by internal audit's "hall pass," which grants the function broad access and visibility into people, processes and technology throughout the organization. That access has allowed Shellabarger and her team to see trends that might not have been obvious at the departmental level.

"As an example, we identified an issue during an audit, and because of our ability to view the organization more broadly, we confirmed that it was an issue throughout the company," she says. "So, we're hosting a workshop with all the relevant parties. We educate about the problem and the control expectations, but the risk owners are empowered to solve the problem. It helps to instill accountability while educating our audit clients."

Building on their foundation of understanding, trust and valued insight, internal audit is beginning to evaluate culture in all audits. Actual outcomes and audit issues are weighed against the company's core values of integrity, simplicity, partnership, innovation and results, and against its leadership competencies — customer focus, strategic orientation, business acumen, people focus, collaboration, dealing with ambiguity, accountability and drive for results.

The scope is limited for now, but Shellabarger expects that focus to broaden over time. She maintains that when processes fail, or ethical issues arise, they can usually be tracked back to a people issue: lack of resources, lack of understanding, and lack of expectations or accountability.

Rather than look for these things in a "culture audit," Shellabarger says her team has opted for a more organic approach, in which internal auditors embed themselves within project teams in an advisory role and frequently meet with management to deepen internal audit's understanding of issues and trends. "It's less about auditing and more about being part of the process," she says.

Shellabarger also feels the people element cannot be understated. When a risk issue arises, she recommends asking: How does this affect our people? "It is people who create, deliver and service products to our customers, so the people element is really important," she explains.

Measuring Culture by Its Absence

Most audit leaders can tell you what elements of a strong corporate culture look like: being viewed as an employer of choice, people speaking up when they see something is wrong, a proactive approach to risk management and compliance, and a "practice what you preach" mentality throughout the organization. Quantifying culture, however, is a different matter. Shellabarger says culture is a little more complicated than "the way we do things." It is also asking, "Do we do the things we say we're going to do?" From an internal audit perspective, she says, that entails tracking issues back to their root causes and determining whether the company is living up to the values and principles it has on paper.

Shellabarger says she believes that good culture is just as much about the tone in the middle and bottom as it is the tone at the top. The culture must be shared among senior management, middle managers and individual contributors.

Shellabarger adds that her team's active engagement process provides internal audit with clearer real-time insights into corporate culture as it exists. It also allows auditors to observe root causes and audit issues as they arise, and recommend timely remediation, instead of waiting a year or more for issues to arrive in a scheduled audit.

Building an effective culture takes time, Shellabarger says: "It's something people have to live and believe in, not something that can be mandated or turned on like a light."

As a new organization, CDK has moved deliberately, beginning with principles and values and working iteratively to educate employees and vendors and ensure that management is modeling the desired behavior.

"We are tailoring the approach to the maturity of the organization," says Shellabarger. "We're taking things slowly and focusing on small wins. 'Crawl, walk, run' is our mantra."

Deutsche Bank

Reconstructing Culture at Deutsche Bank

It's about managing an organisation within the norms of the society you are living in. Good, transparent governance, the right tone from the top, and the right levels of consequences from management.

— Mark Cullen, Managing Director and Global Head of Group Audit

EMPLOYEES IN COMPANY:
100,000

INDUSTRY:
Banking

ANNUAL REVENUES:
US$33.6 billion
(as of February 2, 2017)

NUMBER IN IA FUNCTION:
N/A

YEARS IA FUNCTION HAS BEEN IN PLACE:
N/A

IA DIRECTOR/CAE REPORTS TO:
Chief Executive Officer

Deutsche Bank AG is a German global banking and financial services company with headquarters in Frankfurt, Germany. It is the country's largest commercial bank, with around 100,000 full-time employees, a global footprint spanning 70 countries and over US$30 billion in net revenues.

Deutsche Bank is in a period of restructuring and recent years have featured a number of legal settlements. The bank is now seeking to reduce its global footprint and recently reorganised into three business divisions: the Corporate & Investment Bank, Private and Commercial Bank, and Deutsche Asset Management.

Mark Cullen, who currently heads up the bank's Group Audit team, has been at Deutsche Bank since 1990 and was asked to become the Global Head of Group Audit in 2015. When he took on his current role, the number of auditors on his team totaled 470; today that number has swelled to 700.

An Evolving Audit Function

"There has been significant growth in the Group Audit function over the last two years," Cullen says. "Deutsche Bank is a very complex organisation. In my experience with the bank for most of the past 27 years, I have

Note: This profile is written in British English.

been in the first line of defence." (Cullen is referring to the three lines of defence in risk management and control: the first line is operational management, the second line is risk management and compliance functions, and the third line is internal audit.)

"My current role, running Group Audit, is to manage and build out an effective and impactful function," Cullen says. "I'm not an auditor by training."

German banks are organised along a two-tier structure — with both a management and a supervisory tier. From an external perspective, the responsibility of the Group Audit function is supervisory, identifying weakness in the organisation's design and operating effectiveness of controls and compliance with relevant regulations.

Auditing conduct comes down to auditing behavior, which is a very challenging proposition.

"We need to create transparency around the control environment," Cullen says. "The third line of defence should look into how the bank operates and raise findings where the bank is exposed to risk. The goal is a safer, better functioning and controlled bank."

The Culture Carriers

Cullen believes that "culture" can be one of the most abused words in the banking industry — often used as a potential solution to a problem when there may not be any real meaning behind it. "You must have strong cultural carriers from the top, and throughout the organisation. You also must make sure that you reward them all for their positive contributions."

He adds, "Internal audit's job is to raise findings and identify weaknesses. Our role is reporting control issues. It is management's role to ascertain the severity of the breach, determine the consequences and remediate the risk."

"This is a complex business," he explains. "To audit our culture, where would we start? For example, regulations say we must cover conduct risk. But conduct takes many different forms. Auditing conduct comes down to auditing behavior, which is a very challenging proposition."

He continues, "For me, the word 'culture' embodies how the bank functions."

Cullen says he also believes organisations that swiftly and appropriately punish errant behaviour have stronger cultures. "Historically in the banking industry, some have turned a blind eye to this type of behaviour," he says. "The industry has paid the price for that approach — culturally and financially."

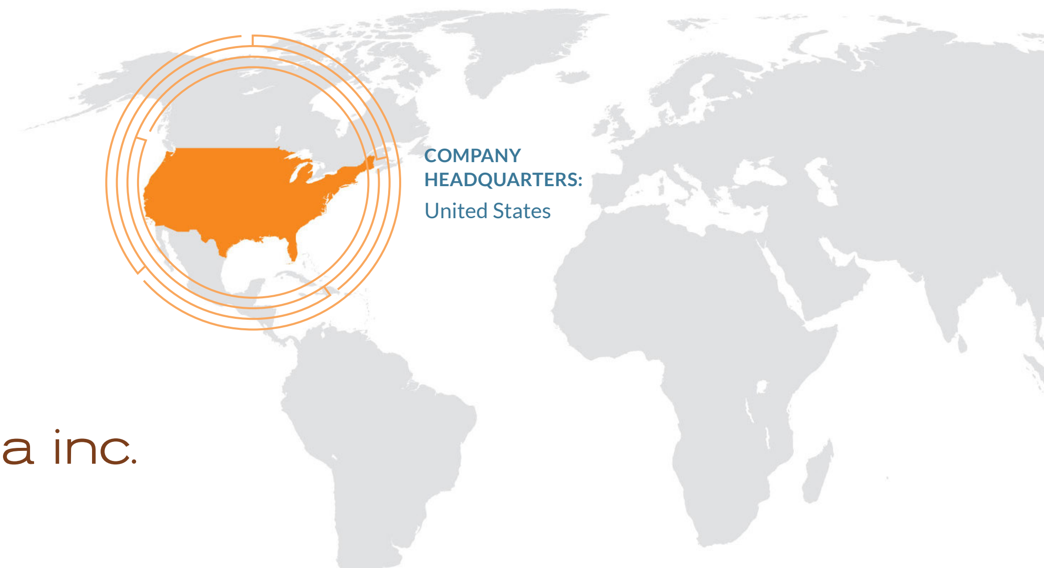
It’s About Doing What’s Right

According to Cullen, an effective management team is one that is open to constructive criticism, that encourages self-identification of control weaknesses and delivers sustainable remediation. “Control has to be a priority — it is as important as revenue,” he says. “In fact, I wished I’d done this job before any of my other jobs here, because I now understand how the control environment actually drives equity value.”

Tone at the top is, for Cullen, where the restoration begins. “It’s about managing an organisation within the norms of the society you are living in,” he says. “Good, transparent governance, the right tone from the top, and the right levels of consequences from management.”

He explains, “If a management team thinks control is something they *have* to do because they are told to do it, that’s an issue. It’s important that management believes control is something they need to do, from a moral and financial standpoint.”

Perhaps it is because of his unique non-audit point of view that Cullen can speak openly about these issues. He has the benefit of nearly three decades in the banking industry, most of that time spent running businesses within the bank.



expedia inc.

Expedia Revolutionizes Global Travel With a Clear Eye on Cultural Accountability

To me, that is culture: a partnership in the truest sense of the word. I believe I can talk to any level of management, put my cards on the table, state the facts and then work together with the teams to get to the right answer.

— Jeff Davis, Vice President of Corporate Audit Services

EMPLOYEES IN COMPANY:
20,075

INDUSTRY:
Technology/Travel

ANNUAL REVENUES:
US$8.8 billion
(as of December 31, 2016)

NUMBER IN IA FUNCTION:
25

YEARS IA FUNCTION HAS BEEN IN PLACE:
12

IA DIRECTOR/CAE REPORTS TO:
Audit Committee Chair; administratively to the CFO

Expedia, Inc., which debuted in 1996 as Microsoft Expedia Travel Services, sprang from an idea at Microsoft that researching and booking travel online would be nifty. Turning this concept into reality led to a major transformation in the way people plan and book travel. Expedia has grown rapidly over the past 20 years and is now the world's largest online travel organization, offering a full suite of online travel services. As one of the world's largest e-commerce companies, its mission is to revolutionize travel with the power of technology.

Over the past two decades, Expedia has acquired many well-known brands, creating a powerful and highly diversified supply base. These brands include the flagship Expedia brand, Hotels.com, trivago, HomeAway, Orbitz, Travelocity and Hotwire, to name a few. The company serves a US$1.4 trillion worldwide market and has a global footprint that spans 75 countries.

Jeff Davis is vice president of Corporate Audit Services (CAS) for Expedia. He joined the company in May 2005, three months before Expedia became an independent public entity, and during a time when the company's management team recognized the need to establish a corporate governance model, including an internal audit function. Today, Davis oversees a team of 25 auditors, which manages audit and compliance projects for all the company's worldwide brands. Three team members report directly to Davis, and all work from a centralized location at the company's headquarters in Bellevue, Wash. "Even though we are in 75 countries, the power of the technology allows us to create a significant amount of leverage by performing our work centrally," Davis says.

Davis' three direct reports include the director of Enterprise Risk Management (ERM), who oversees ERM and Sarbanes-Oxley (SOX) compliance; the director of Internal Investigations, who covers global internal investigations in addition to compliance and policy management; and the internal audit director, who oversees the operational internal audit function. The ERM and internal audit director duo are responsible for audit scoping and high-level design of controls, while the internal audit team spends most of their time on operational audits, SOX design and operational effectiveness testing based on the results of ongoing risk assessments with leaders across the company. Additionally, internal audit takes on large consulting projects or audit tasks stemming from new initiatives or the changing Expedia landscape.

Davis and his team cover risk, compliance and operational audits with an ever-present focus on developing people. He says the internal auditors first seek to understand and identify strategic risks that affect the organization, then assess those risks, and finally recommend controls to mitigate those risks to an acceptable level. Second, they help to ensure regulatory and Sarbanes-Oxley compliance — what Davis describes as "table stakes for most audit teams at this point."

Third, according to Davis, the internal audit team makes sure operational audits "shine a light in the right places" within the organization, including those that represent the highest strategic, operational and compliance risks. And finally, he says, CAS is committed to growing its people and placing them throughout the company. Davis explains, "This helps our individual team members develop in their professional careers. It also enables us to share our risk and controls mindset with the rest of the organization. Having former internal auditors sitting in key financial or technology positions within the organization helps strengthen our overall control environment."

We Audit Culture Every Day

Even though the CAS team does not conduct formal audits of the company's culture, Davis says he believes that they audit culture every day. He explains that an active awareness of culture is imbued in all his team's audit activities, from conducting scoping and process interviews to strengthening the relationship between organizational culture and the internal control environment.

"We interview people daily about risk and controls, interacting at all levels of the organization, starting with the brand presidents or the C-suite through to the rest of their teams," Davis says. "Each day, we gauge whether we believe we are getting the right level of transparency and candor we need from the individuals, teams and systems."

Davis says he is happy to report that Expedia's culture lends itself to exactly that transparency and candor. In fact, it is one of their six cultural norms. "I think that culture is always a hot topic, and it should be — for anyone in an organization or looking to join one," he says. "A job can have the greatest description in the world and come with significant compensation. But if you don't personally believe you can align with the company's culture and leadership, then it won't work. If you think about culture at the highest level, the question is: Are you comfortable bringing your whole self to work every day, or do you act differently with your team than you do with company leadership?"

Davis says establishing and monitoring culture starts at the top at Expedia. "The CEO and executive team live and breathe the culture," he says. "And we are all expected to adhere to our 'Cultural Norms.' They were identified several years ago when Expedia redefined its mission and strategy to really crystallize the idea of who we are as an organization."

The Cultural Norms at Expedia are:

- **We Believe in Being Different.** Diverse Expedia teams seek out new ideas and different ways of thinking.
- **We Lead Humbly.** Leaders serve their teams with curiosity, humility and a genuine desire to find answers.
- **We Are Transparent.** Open, honest communication is a cornerstone at Expedia. Issues are surfaced and acted on quickly.
- **We Organize for Speed.** Gathering data as quickly as possible leads to rapid learning and improvement.
- **We Believe in the Scientific Method.** Hard data leads the way, guiding action for all levels of the organization.
- **We Act as One Team.** The goal is to optimize the greater good. Each team member is actively interested in the success of others.

Have Your "Boarding Pass" Ready

Using the Cultural Norms as a foundation, CAS created a travel-themed "Employee Code of Conduct — The Boarding Pass" for all employees. "The Boarding Pass is a clear reminder of what is expected of every person in the organization. It is a framework for accountability," says Davis. "The Boarding Pass is anchored in integrity and describes in simple terms how Expedia expects employees to interact with each other, our customers, our suppliers and our technology."

A job can have the greatest description in the world and come with significant compensation. But if you don't personally believe you can align with the company's culture and leadership, then it won't work.

The Boarding Pass has a direct impact on the risk landscape at Expedia. With Boarding Passes in hand, employees understand what Expedia believes in, and the standards they are expected to follow. Davis explains, "For example, as the scientific method is part of our core values, we conduct A/B testing as we constantly refine our operational audits, SOX design work and testing, consulting projects, and risk assessments."

He adds, "We know we are going to take on risk — there is not a business in the world that doesn't — but we take on measured, data-vetted risk. In Expedia, Inc. chairman Barry Diller's own words, 'Risk is the way good things happen.' In that instance, culture very much helped shape and formalize our approach to risk and controls."

Leading humbly is another guidepost that impacts culture. "In some corporate cultures, the attitude is, if you make one wrong step, you're in trouble," Davis says. "In those environments, people tend to deliver only the messages leadership wants to hear. In Expedia's culture, I stand behind the conclusions of the audit team, which are supported by facts and data, whether the news is favorable or not."

He continues, "Anything less is a slippery slope and breeds a different outcome. We focus on what's tangible and real. Our job is to help the organization identify, understand and mitigate the risks that need to be mitigated."

We don't really talk to people about controls. We talk to them about doing the right things for the business and what could go wrong.

Addressing Culture With an Auditor's Eye

A key tenet for the CAS team at Expedia is to be well-informed before interacting with brands and leadership. The second is to consider the intangible nature of culture when auditing more tangible metrics.

"We make sure that our culture is flowing down through the organization," Davis says. "For example, if our CEO and leaders are talking about transparency, but the team we approach tells us they can't talk to us, then we know the message about transparency has not permeated the environment the way it should."

Davis points to Expedia's CEO, Dara Khosrowshahi, as a representation of their culture. "His management style and his approach to people are very down to earth," he says. "He strikes a collegial and transparent tone, and that is true across the executive team. To me, that is culture: a partnership in the truest sense of the word. I believe I can talk to any level of management, put my cards on the table, state the facts and then work together with the teams to get to the right answer."

Davis adds, "We don't really talk to people about controls. We talk to them about doing the right things for the business and what could go wrong. We ask, 'If this were your business, what would you do?'"

COMPANY HEADQUARTERS:
Australia

Group Internal Audit at IAG Adds Structure to Risk Culture Audits With a "Triage Approach"

Internal audit is independent and can objectively assess risk behaviors and attitudes that impact the company's ability to operate within the group's risk appetite. We use risk culture as a basis for informing outcomes for every internal audit review.

— Lee Sullivan, Group General Manager of Internal Audit

EMPLOYEES IN COMPANY:
15,000

INDUSTRY:
General Insurance

ANNUAL REVENUES:
US$8.5 billion
(as of June 30, 2016)

NUMBER IN IA FUNCTION:
23

YEARS IA FUNCTION HAS BEEN IN PLACE:
15

IA DIRECTOR/CAE REPORTS TO:
Chief Risk Officer

Insurance Australia Group Limited (IAG), headquartered in Sydney, Australia, is a multinational company that provides auto, home and other types of non-life insurance. Auto insurance represents the largest percentage of its portfolio, which is not surprising given that IAG originated from a roads and motor services mutual serving the Australian state of New South Wales.

In 2000, the company's insurance arm demutualized from the motoring and road services group. Since then, IAG has gone public (it's listed on the Australian Securities Exchange), grown its employee base to 15,000, and acquired several insurance brands in Australia and New Zealand. The company is the largest non-life insurer in both those countries; it also has joint venture investments in Asia.

IAG's chief audit executive Lee Sullivan joined the company's internal audit department about a decade ago. Today, as the group general manager of internal audit, Sullivan reports functionally to the chair of IAG's group audit committee and administratively to the group's chief risk officer. He oversees 23 staff in Group Internal Audit (GIA). Most of the internal audit team is based in Sydney; other members work in the company's Melbourne and Auckland offices.

GIA's strategic goals include providing assurance to IAG's board of directors that the financial and operational controls designed to manage the company's risks and achieve its objectives are operating in an efficient, effective and ethical manner. "We also assist management in improving IAG's business performance," says Sullivan, adding that company leadership is "keen" to have internal audit serve as a strategic partner.

"They want us to add more value beyond performing simple compliance audits," he explains. "It's a direct request, requirement and desire by management and the board that internal audit is a strategic partner to the business. It is something that I strive for, as well."

A Renewed Focus on Culture

Culture, in general, has been an important topic for IAG for many years, according to Sullivan. "We are proud of our culture and passionate about how it guides the way we operate. We believe we have a responsibility to help people be safer and more confident. For us, it's not just about paying claims, but also raising risk awareness and helping communities reduce and prevent risks."

Understanding risk culture is intrinsic to changing, monitoring and managing behavior, which are all essential elements for maintaining a successful business.

Since risk culture became a specific measure incorporated into IAG's annual organizational staff survey, culture has become a more focused topic at the company — and for GIA.

"In recent years, organization-wide culture has been subject to increasing regulatory focus," says Sullivan. "Regulators in Australia have had a dual focus on 'conduct risk' — or how we treat our customers or other stakeholders — and 'risk culture,' which relates to how our employees behave and respond to the risks they face. All financial services companies in Australia, and not just IAG, have a renewed focus on culture."

GIA is in a good position to help the company's senior leadership to monitor and strengthen the culture of IAG, says Sullivan. "Internal audit is independent and can objectively assess risk behaviors and attitudes that impact the company's ability to operate within the group's risk appetite," he explains. "We use risk culture as a basis for informing outcomes for every internal audit review."

Sullivan adds, "Risk culture plays a vital role in ensuring effective risk governance is maintained through changing environments. Understanding risk culture is intrinsic to changing, monitoring and managing behavior, which are all essential elements for maintaining a successful business."

Focusing on Root Causes, Not Just Symptoms

Sullivan says measuring culture is something his team has always done in every audit — in an intuitive way. "What we didn't have until recently was a structured approach for reporting on risk culture or applying our learnings to what we were finding from a formal audit perspective," he says.

To develop the right approach to auditing IAG's risk culture, Sullivan sought advice from experts outside of the company and weighed several ideas before settling on what he calls a "triage approach." This process, which is now incorporated into every internal audit review, involves completing a maturity assessment on key behavioral enablers so that auditors can form a view of the risk culture within the area being reviewed. This view may be used to identify opportunities for improvement or weaknesses that require a deeper risk culture assessment by the first or second line.

The key behavioral enablers used in the maturity assessment include tone from the top, behaviors, roles and responsibilities, governance, risk appetite, risk transparency, relationship, responsiveness, motivation, and capabilities. The ratings the internal audit team assigns to an area's risk culture are "basic," "evolving" or "established."

"The goal of the risk culture audits is to provide a cultural reason for control issues and other findings documented as part of our reporting," says Sullivan. "Risk culture insights often help us to identify the true root causes of failures and issues, thus providing an improved chance of properly fixing those root causes and not just the symptoms."

Sullivan cites the following three elements as evidence of a strong risk culture:

- The tone from the top is clear and consistent, and messaging reaches all levels of the business.
- Employees feel they can speak up and have honest conversations about issues.
- Risks are clearly articulated through risk appetite, and consequences for going outside of that appetite are well-understood.

Signs of a weak culture, meanwhile, include risk behaviors that are not role-modeled by leadership and lack of alignment between incentives and adherence to the company's risk appetite. "In a weak culture, you also find that staff don't understand the role they play in risk management, and their capabilities aren't being developed," says Sullivan.

The Importance of Applying a Consistent Approach

Developing his own team's capabilities is a high and ongoing priority for Sullivan. "One of my challenges as a chief audit executive is making sure that my staff, who are ambitious and highly talented, always feel that they are being invested in. One aspect of that investment is learning and development. I want my staff to have the skills not only to perform better, but also to really enjoy their jobs."

Ensuring all audits, including risk culture audits, are high quality is another motivation for Sullivan to make sure his auditors are equipped with the right skills — particularly, soft skills. When developing the triage approach for risk culture audits, Sullivan says he recruited organizational psychologists to train his staff on how to ask questions about culture and categorize the information they learned appropriately. He says the outcome of the training is a more consistent approach for all of GIA's audits.

"In softer areas, like auditing risk culture, you must be consistent," says Sullivan. "If your approach is unstructured or untrained, there is a danger you might call out things for the wrong reasons. So, there's a sense of corporate responsibility to all our staff to ensure that we get to the underlying issues using what we learned from the psychologists — and not just point out what we *think* the issues are. It's all about finding the root cause and the right treatment."

Making the Intangible Tangible

Sullivan says auditors must work through three layers of interviews, according to the risk culture audit methodology at IAG — the processing layer, middle management layer and senior management/expectation layer. "We need to work through those layers and then build our observations. That helps to make our risk culture audits more tangible to the business — and less of a dark art," he says.

He adds, "The challenge is breaking down what is essentially an intangible concept into practical applications and using language that can be associated with a business concept. We need to demonstrate how we have validated impressions gained through time spent in the business. We overcome this by using tangible mechanisms to support our views.

"I never intended to industrialize our process for risk culture audits, but simply use the outputs to provide deeper insights into adverse control findings. So, I'm now working on building a risk culture dashboard tool with a real-time reporting layer at the request of the audit committee. It's going to take some time, though, to build the requisite data library so that we can start identifying and analyzing any risk culture trends at IAG. It's a journey."

While Sullivan is tasked with creating a new tool for reporting on risk culture audits, he says existing reporting capabilities and frameworks are still very valuable for internal teams to use in building a library of tangible mechanisms for measuring culture. "Validation is integral to being able to support your results and views," he says.

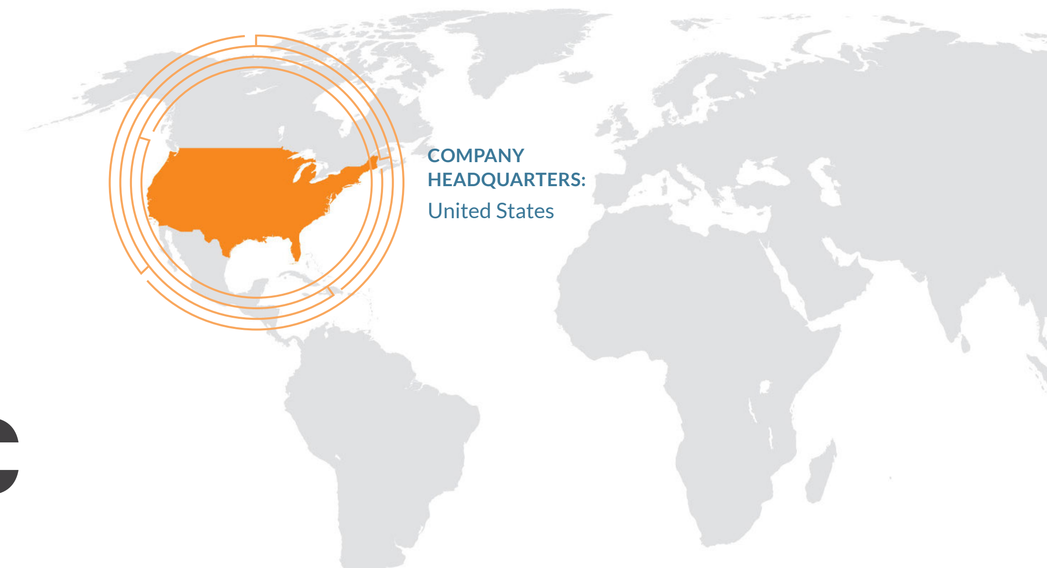
Starting Point for Success: The Pilot Program

An important step to formalizing the risk culture auditing process in any organization is conducting a pilot program, according to Sullivan. The internal audit team at IAG conducted their pilot in an area of the business that was "very self-contained" and had evidence of "good control efficiencies," he says.

"There was very little interlock with other parts of the company through servicing or transactions. So, it would have been difficult for anyone in that unit to say, 'The culture's not about us, it's about those people in the next room.' It allowed us to have a constructive discussion."

He adds, "It was important to start our process in a safe environment where we wouldn't find any big surprises — and where we couldn't fail. I knew if the first experience were negative, we probably wouldn't be able to do it again. So, it's important to be careful when selecting where to conduct a pilot."

Sullivan suggests internal audit teams be prepared to refine their methodology continually as their risk culture program evolves. "You need to keep learning from your experiences," he says.



OCC

A "Regulatory Backdrop" for OCC's Risk Culture Internal Audit

Culture is the component that has the highest leverage within our risk management capabilities. If we encourage the kind of culture that supports good risk management, then we are more likely to succeed. This formulation is accepted and supported by our board and leadership.

— Adi Agrawal, Senior Vice President and Chief Business Transformation Officer, and former Chief Audit Executive

EMPLOYEES IN COMPANY:
560

INDUSTRY:
Financial Services/Exchange-Listed Options Clearing House

ANNUAL REVENUES:
US$283 million
(as of December 31, 2016)

NUMBER IN IA FUNCTION:
20

YEARS IA FUNCTION HAS BEEN IN PLACE:
N/A

IA DIRECTOR/CAE REPORTS TO:
Audit Committee Chair, administratively to Executive Chairman and CEO

The Options Clearing Corporation (OCC), founded in 1973, is the world's largest equity derivatives clearing organization. Like all clearing houses, OCC acts as a guarantor between clearing parties, ensuring that the obligations of the contracts they clear are fulfilled. Headquartered in Chicago, OCC specializes in equity derivatives clearing and provides central counterparty (CCP) clearing and settlement services to 15 exchanges.

In 2012, OCC was designated a systemically important financial management utility (SIFMU) by the Financial Stability Oversight Council as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act. It is one of eight U.S. entities that have this designation.[1]

Its status as a CCP clearing house and a SIFMU means that OCC must meet, in addition to tough regulatory requirements, "a heightened set of expectations for internal audit and business

[1] "Designated Financial Market Utilities," Board of Governors of the Federal Reserve System, January 29, 2015: www.federalreserve.gov/paymentsystems/designated_fmu_about.htm.

assurance capabilities as well as good risk management practices," says Adi Agrawal, the firm's Senior Vice President and Chief Business Transformation Officer, and former Chief Audit Executive (CAE).

Agrawal says, "At the core of OCC's business is the ability to manage complex financial risk. Every U.S. exchange-traded option that trades is cleared by us. It is therefore terribly important for OCC to have very high-quality financial risk management in place to manage liquidity, market, credit and customer performance risk." Electronification of trading over the past decade, which has exponentially increased trading volume, has only amplified the expectations for OCC and other financial market infrastructure firms, he adds.

Developing One Team With Two Broad Areas of Skill

Agrawal was CAE for 16 months before he was appointed in April 2017 to his current and newly created position of chief business transformation officer at OCC. During his time as CAE, Agrawal says he was responsible for transforming OCC's internal audit function into "the kind of a department a SIFMU should be operating."

Internal audit at OCC reports functionally to the audit committee of the board of directors, and administratively to Executive Chairman and CEO Craig S. Donohue. The department has 20 full-time employees, all of whom work at OCC's headquarters in Chicago.

The team also includes a quality assurance manager. "She's trained as an internal auditor, but also has a very good understanding of standards and controls that should apply to the internal audit profession," says Agrawal. "She helps to keep our department honest and provides ongoing assurance that the work product and underlying capabilities continue to meet and exceed the baseline expectation established within our quality assurance and improvement program (QAIP)."

Under Agrawal, OCC's Internal Audit Department developed into "one team with two broad areas of skill" — risk and clearing, and technology and operations. The risk and clearing team has specialists who study OCC's operations by applying financial risk management, regulatory knowledge, and process design and engineering capabilities. "They understand the basic components of running a clearing house, including financial risk management, clearing, settlement and asset management," says Agrawal. The latter group is comprised of auditors with a solid information technology and process background, including information security expertise.

One of Agrawal's first tasks as CAE was to develop a 12-month rapid maturation plan with several short-term goals for the internal audit function; these goals were approved by OCC's Audit Committee and shared with OCC's regulators, he says. By the time that Agrawal moved into his new role as chief business transformation officer at OCC, the internal audit team had met, or had nearly achieved, all those goals. The short-term plan had four facets:

1. **Investing in human capital.** Agrawal says, "Our primary focus had to be on our talent — creating a robust leadership team supported by technical and assurance expertise and solidifying our co-sourcing arrangement with one strategic partner, Protiviti."
2. **Building out a process infrastructure.** "We had good policies, but our process was not right-sized or grounded in relevant professional standards and guidance," Agrawal explains. "So, we had to re-engineer our entire audit life cycle from

the ground up." After that, the QAIP was introduced to "study our processes, extract metrics and provide the audit committee with insights into what internal audit produces in terms of quality and efficiency, and how we use those metrics to sustain capabilities or drive necessary change," he says.

3. **Interacting with stakeholders.** "We had to become deliberate about our engagement with stakeholders," Agrawal says. "This is about internal audit regularly interacting with leaders across the firm and board members, as well as meeting with regulators, so that we can keep our finger on the pulse of the organization's risk and stakeholder priorities and expectations."
4. **Meeting regulatory expectations.** This aspect of the plan was a two-part exercise, according to Agrawal. "Internal audit had a backlog of capability issues, so we cleaned those up," he says. The second part of the exercise, he explains, was re-engineering internal audit's reporting to OCC's Board of Directors and regulators so that the reporting "has quality and consistency and tells them what they need to know with complete transparency." The CAE has an obligation to help the audit committee discharge its oversight responsibilities effectively, he adds.

Agrawal also set up a comprehensive, risk-aware, three-year plan for internal audit, which the team began executing in January 2016. A risk culture audit was one of the audits planned for the first year.

"The idea to do a risk culture audit stemmed from our risk assessment process as well as from our discussions with management," says Agrawal. "The firm was undergoing a great deal of change at the time. For example, our management team had experienced significant changes. Regulatory expectations were pronounced. A lot of training was going on, and a new set of cultural biases were being developed. So, we decided that we needed to assess how we were doing and help formulate a more deliberate and measurable risk culture plan."

Engaging in Conversations About Culture

Agrawal and his team worked with Protiviti to develop a maturity framework for the risk culture audit. He says the framework utilizes a "regulatory backdrop" based on the "common expectations of regulators and pronouncers of standards and principles for financial market infrastructure." It also draws on pronouncements from entities such as the Federal Reserve Board and the Basel Committee on Banking Supervision.

The idea to do a risk culture audit stemmed from our risk assessment process as well as from our discussions with management.

After setting up the framework, the internal audit team deployed a methodology for the audit to gather input from people in the organization, including leadership, about how they perceive OCC's risk culture.

"We wanted to put all that information against the framework to determine a maturity score that could indicate how we are doing relative to our expectations," Agrawal says. Once they knew where OCC sat on the curve, he explains, they could create a road map to help guide the organization to where it wanted to be. They could also determine what steps, such as staff training, would help OCC to reach that goal.

The methodology was executed using a series of "meetings, surveys and conversations," according to Agrawal. He emphasizes the importance of the latter component, "We are not a large firm, so I did not want the methodology to be entirely survey-based. I wanted to include an element of conversation in the process."

OCC's internal audit team engaged in several in-person meetings with almost every member of OCC's Management Committee. Agrawal also attended conversations with a cross-section of board members. "We wanted the board to be involved in the process, but we had to be careful in our approach," he says. "Logistically, we couldn't talk to the entire board, so we spoke to the chairs and some independent board members of key committees — risk, technology and audit."

If culture, or a particular type of culture, is important to the business, you need to be able to measure it.

About 100 risk culture surveys were sent to a curated list of recipients in the organization, as well. "We wanted to include viewpoints that covered all our process families," Agrawal explains. "The survey response rate was about 82 percent, so we definitely ended up with a statistically relevant response."

After the meetings and surveys had been completed, the internal audit team wrote up their findings and then had several meetings with OCC's Management Committee and the Office of the Chairman to review them. Through those discussions, it was decided that OCC's chief risk officer (CRO) would be accountable for managing the execution of several of the top-priority items on the list.

"That is the CRO's committed accountability to the risk committee of the board as well as to our CEO," says Agrawal.

Preparing for the Next "Health Check"

In about 18 months, the internal audit team at OCC plans to run another comprehensive risk culture audit — which Agrawal says he views as more of a "risk culture assessment or a health check" than a formal audit. "We'll run the methodology again and refine the process, and see how the baseline changes from that initial maturity read," he says.

"I know that, over time, we will adjust some of the components and areas we want to focus on," he continues. "However, I think we have established a repeatable methodology that the firm can employ. Eventually, we can embed it into other survey-taking around engagements and other practices."

Meanwhile, Agrawal says the internal audit team is receiving training to help them identify and assess "local" cultural issues while conducting audits. "We've gone over the framework with them, shared the results of the first audit, and helped them thematically tie the results back to observing similar issues within individual process families," he says.

Measuring the "Cultural Underpinnings"

Agrawal says he believes it is important for all organizations to have an objective, repeatable way to measure outcomes that are important. "If culture, or a particular type of culture, is important to the business, you need to be able to measure it," he explains. "I also think it is valuable to have these audits and formulations in place because it allows internal audit to take subjective formulation and line it up to objectively observable behaviors or outcomes."

Financial utilities and institutions should be having conversations about culture anyway, Agrawal says — and if they are not already contemplating a risk culture audit, they should be.

"Culture is a good business conversation, in general. But it's important for other reasons, too," Agrawal says. "For example, culture is the component that has the highest leverage within our risk management capabilities. If we encourage the kind of culture that supports good risk management, then we are more likely to succeed. This formulation is accepted and supported by our board and leadership."

Agrawal says the risk culture audit process can also help organizations to measure their "cultural underpinnings." For OCC, these include transparency, clarity, completeness and collaboration.

"As an organization, we say, 'We are going to be honest and clear about how we communicate issues, and we are going to be honest and clear about how we deal with them.' Well, how do we measure that if we don't audit it?" asks Agrawal. "And if we don't measure it, then how can we have assurance that our organization is consistently delivering those behaviors?"

"Every audit is about positive assurance," he adds. "There's a belief system about expected outcomes, and you want to have an objective way to assure against it. I think culture is no different."

For organizations that want to audit their risk culture, Agrawal offers this advice: "Be sure to establish a measurement framework that fits your business. It will help you to avoid taking a 'black or white' or 'yes or no' approach to assessing culture. And once you've put some specific guidance into the framework, you'll be set up to measure against the things that are important to you."

COMPANY HEADQUARTERS:
Japan

Internal Audit Keeps Takeda's Deeply Rooted Culture in Focus When Assessing Risk

> *Corporate culture is the key to business success and to how employees view the corporate strategy. That's why it's important for internal audit to engage in this area.*
>
> — Katsuaki Kaneko, Senior Vice President, Head of Group Internal Audit

EMPLOYEES IN COMPANY:
30,000

INDUSTRY:
Pharmaceuticals

ANNUAL REVENUES:
US$15.4 billion
(as of March 31, 2017)

NUMBER IN IA FUNCTION:
40+

YEARS IA FUNCTION HAS BEEN IN PLACE:
65

IA DIRECTOR/CAE REPORTS TO:
CEO and Audit and Supervisory Committee

Takeda Pharmaceutical Company Limited began in 1781 as a small shop in Doshomachi, the medicine district of Osaka, Japan. Chobei Takeda I was a purveyor of traditional Japanese and Chinese herbal medicines, buying them wholesale and then selling smaller batches to local medicine merchants and doctors. The founder's reputation for business integrity and quality products and services has proven to be a strong foundation for a company that is now more than two centuries old, traded on the Tokyo Stock Exchange and doing business in 70 countries around the globe.

Takeda is also the largest pharmaceutical company in Japan and Asia, and one of the leading companies in the industry worldwide. One of its most well-known drug brands is the heartburn medication, Prevacid (generic name: lansoprazole). Takeda has more than 30,000 employees and operates two main offices in Osaka and Tokyo. Its U.S. subsidiary, Takeda Pharmaceuticals U.S.A., Inc., is in Deerfield, Ill.; its global operations outside of Japan and the United States are based in Zurich, Switzerland. The company also maintains research and development (R&D) operations in several countries, including Singapore and the United Kingdom.

Katsuaki Kaneko joined Takeda in October 2015 to lead the company's Group Internal Audit (GIA) function. He reports to Takeda's president and CEO, Christophe Weber — the first non-Japanese person to head a Japan-based pharmaceutical company — and to the audit and supervisory committee of the board of directors. Kaneko oversees a team of nearly 50 auditors. About 20 team members work in Japan, and the others are in Chicago, Zurich and Copenhagen. Takeda also maintains co-sourcing and outsourcing relationships with global professional services firms.

Meeting Goals on a Path to Transformation

Kaneko has outlined several long-term, midterm and short-term strategic goals for GIA at Takeda. Among the long-term objectives, he says, is developing a "highly motivated team of risk and control experts with deep domain expertise through robust training and dynamic performance management and by providing best-in-class tools to allow auditors to perform their jobs productively and efficiently on a consistent global basis."

Another long-term goal is to "exceed the expectations of key stakeholders by raising awareness of control risk, providing advice to management in developing control solutions and monitoring the implementation of management control measures."

Kaneko emphasizes that achieving these goals will result in GIA building a diverse workforce, industry-leading audit practice, and value-adding assurance and advisory activities, and will help to separate the organization distinctly from its competitors.

The three midterm goals for Takeda's GIA function, which Kaneko says his team intends to achieve by fiscal year 2019, are:

1. **Successfully complete an external quality assurance assessment.** "This is required by The Institute of Internal Auditors, but we want to have this assessment anyway to make sure that our audit practice is best-in-class in terms of quality," says Kaneko.
2. **Roll out a "rotation/exchange program."** Takeda currently devotes a large portion of its auditing budget to co-sourcing and outsourcing. The downside of these arrangements, Kaneko explains, is that it is "sometimes difficult to ensure quality of service and to retain knowledge and experience from external partners."

   He says, "We want to develop and utilize our own people more, including people from other functions — and especially younger, high-potential people inside Takeda." Kaneko's vision for the program, which is aligned with Takeda's Accelerator Program, is for participants to receive extensive risk and control training and experience, including exposure to interacting with senior management. Participants then go back into the business to be "ambassadors" for internal audit, who can support educating the first and second lines of defense about risk management and governance.
3. **Move toward a "loan staff model."** The purpose of this objective, which relates to the second goal, according to Kaneko, is to shift away from more costly co-sourcing and outsourcing arrangements. "This model will give us more control over quality and help us to retain knowledge and experience within our team," he explains. Kaneko expects that Takeda will continue to co-source or outsource, as needed, in regions that require language skills his team lacks and/or in areas where leveraging external expertise is feasible and cost-efficient.

GIA's short-term goals are intended to help move the function closer to achieving its longer-range plans and relate to an 18-month "transformation program" for internal audit that is currently underway. Takeda itself has been in a period of transformation since making several global acquisitions in the last decade. And Weber, who was promoted from chief operating officer to CEO in 2015, has been driving the company to become a truly global organization.

Kaneko says the fact that Takeda's "global footprint and presence have changed completely" in recent years means that internal audit must change, too, so it can serve the new business effectively. "Our transformation program is changing the way we audit — from how we interact with people throughout the organization to how we develop our own people," Kaneko explains.

Objectives for the transformation program include providing more training to internal audit staff, including in soft skills, and expanding the use of technology tools, like data analytics. The latter is especially important for engaging key stakeholders such as senior management, the audit and supervisory committee, and the board. "They want more analysis," Kaneko says. "These tools will help us provide the additional insight that stakeholders seek and give them strategic advice."

Changing the Mindset, and Culture, in Internal Audit

Another aspect of GIA's transformation program is teaching the internal audit team to consider culture when auditing, and to talk with stakeholders about the importance of culture and its role in helping Takeda manage risk effectively and achieve its business strategy. Changing the mindset of staff who are more conditioned to "old school" auditing approaches has been challenging, though, according to Kaneko. It also has required the internal audit function to evolve its own culture.

"Japan is still behind in terms of internal audit practices," says Kaneko. "In many Japanese companies, internal audit is the place for people to go at the end of their career. Management thinks, 'This person has worked here a long time and knows many people in the organization. Let's put him in internal audit because people will listen to him. That will help our internal audit function to catch up.' However, that's not an effective approach."

He continues, "Fortunately, Takeda's senior management team has given me a mandate — and the funding — to change my function's culture and audit practice so that we can provide strategic advice and align our goals with the company's strategy and goals. We are in a unique position that enables us to help management deliver messages about culture and risk to people throughout the global organization."

[An] aspect of GIA's transformation program is teaching the internal audit team to consider culture when auditing, and to talk with stakeholders about the importance of culture and its role in helping Takeda manage risk effectively and achieve its business strategy.

However, Kaneko says his team is not yet ready to conduct audits that focus solely on Takeda's culture. One reason is that senior management is very focused on operational compliance issues since Takeda is in the highly regulated pharmaceutical industry. "Our audits are heavily focused on compliance risk right now, but our coverage is expanding to other areas like technology risk and even strategic risk, including a review of key initiatives," Kaneko says.

He adds, “Of course, culture has an impact on compliance risk. When we dig into the root cause of a compliance-related audit issue, we often find that it is related to people’s behavior or a management attitude. We rarely state that explicitly in a report because it can be too subjective. However, when people read the report, they can understand what the core issue is.”

In the future, Kaneko says he would like his team to conduct stand-alone thematic audits of Takeda’s culture. “We have been discussing this with the CEO and other executives — for example, what the objective of the audit would be and the potential impact of this type of audit on our people. But again, my team isn’t ready for this process yet. The company needs to be ready for it, too.”

The Four “Takeda-isms” and “Vision 2025”

When GIA and Takeda are prepared to undertake culture audits, they will have a strong corporate culture foundation to use as a guide. The company’s mission — “to strive towards better health and a brighter future for people worldwide through leading innovation in medicine” — is driven by four “Takeda-isms”: integrity, fairness, honesty and perseverance.[1] Kaneko says these elements have shaped Takeda’s culture over the past 236 years and are critical to the company achieving its “Vision 2025,” which includes a goal for Takeda to be recognized as best-in-class for agility and innovation.[2]

Despite having a well-defined culture with deep roots, Kaneko says there is always, inevitably, a “gap” between the messages senior management is communicating about the culture and what people in the organization hear, absorb and put into practice. “The message from the top is very clear,” he says, “but it doesn’t always cascade throughout the organization effectively. So, we see that as something we can raise as a corporate culture audit issue: the gap between what we know in our heads and what we end up doing.”

In a strong culture, there is always transparency.

Kaneko says a key characteristic of a strong corporate culture in any organization is people feeling comfortable about bringing up and discussing matters openly. “I’m not just talking about small things, but real issues,” he explains. “In a strong culture, there is always transparency.”

That transparency should extend to promotions and performance assessments, too, he says: “Employees need to know that they are being treated fairly.”

A Message of Discipline for All Employees

Kaneko says he hopes GIA will be able to start performing culture audits in the next three to five years. He is also thinking about how GIA could conduct these audits across a diverse, global organization like Takeda. A standard approach applied to all business units in all countries might be one option, he says. But Kaneko also concedes that ramping up any program will be difficult due to regional differences, which he says can even impact standard audits.

1 “Corporate Philosophy,” Takeda website: www.takeda.com/who-we-are/corporate-philosophy/.

2 Ibid.

"We respect these differences, of course, but if Takeda wants to be best-in-class and a front-runner in corporate ethics and integrity, everyone must have discipline," Kaneko explains. "It's easy for management to accept that one area has a different way of doing things, but it's also sometimes very risky. If something were to happen in one country where we operate, it wouldn't be that country's issue. It could be Takeda's global issue."

Kaneko adds, "We ask any country where we do business for discipline. It doesn't matter how other companies in that country do things, or what the social practice is. If you work at Takeda, you must follow the company's rules rooted in its philosophy. There is no exception."

Kaneko has some advice for audit leaders who are unsure about the value of conducting culture audits — or where they should start: "Corporate culture is the key to business success and to how employees view the corporate strategy. That's why it's important for internal audit to engage in this area. As a starting point, I suggest building cultural elements into regular audits and analyzing findings. Then, have informal discussions with stakeholders so that they feel like they are part of the process. From there, you can educate management, help support the business and accelerate cultural change where needed."

Fix Yourself First: Tennessee Valley Authority OIG Leads by Example

If you're going to instill trust in people, you need to be vulnerable and fix yourself first. Then, invite others to join you in your journey to improve.

— Richard W. Moore, Inspector General, TVA OIG

EMPLOYEES IN COMPANY:
10,691

INDUSTRY:
Quasi-government Agency/Utility

ANNUAL REVENUES:
US$10.6 billion
(as of September 30, 2016)

NUMBER IN IA FUNCTION:
57

YEARS IA FUNCTION HAS BEEN IN PLACE:
31

IA DIRECTOR/CAE REPORTS TO:
TVA Inspector General reports to Congress

Headquartered in Knoxville, Tenn., the Tennessee Valley Authority (TVA) provides electrical service to more than 9 million customers across portions of seven states in the southeastern United States. It employs about 10,000 people and manages land, navigation and flood control for the Tennessee River system. TVA is a federally owned corporation but receives no taxpayer funding. It derives all its revenues from electricity sales.

TVA's Office of the Inspector General (OIG) is independent of the organization and conducts audits and evaluations similar to traditional internal audit. Richard W. Moore was sworn in as TVA's first presidentially appointed inspector general on May 9, 2003. Only the U.S. president has the authority to remove Moore from his position. TVA has no control over what the OIG reviews or reports. Moore says there are some natural tensions built into that framework by design. For example, he says the knowledge that the OIG has autonomy to investigate and audit and report "at will" precludes any closer-than-optimal relationships from forming that might hamper independent, objective results.

The TVA's OIG employs about 100 staff, including investigation, audit and evaluation groups, and administrative personnel.

Director Lisa Hammer heads a six-person evaluations team focused on Organizational Effectiveness (OE). Moore established the team in October 2015, after researching the topic and field-testing the methodology at one of the TVA's power plants.

Environmental Disaster Leads to Organizational Culture Review

On December 22, 2008, a dike failed at TVA's Kingston Fossil Plant, spilling millions of tons of coal ash into the Emory and Clinch rivers. It stood as the largest U.S. environmental disaster until the Deepwater Horizon oil spill in the Gulf of Mexico two years later. The Kingston spill resulted in years of litigation, congressional hearings (at which Moore testified) and a US$11.5 million fine imposed on TVA.

In its report to Congress and TVA's board of directors, the OIG made an observational finding that the culture of TVA and the organization's mishandling of coal ash had contributed to the spill. Until that point, corporate culture was not on the OIG's internal audit radar, according to Moore. "We measured culture informally, in ways that were never labeled 'culture,'" he says. "When we performed audits, the topic of culture would come up. But we didn't have a box to put it in, so we didn't know how to talk about it."

A Hard Look in the Mirror

The Kingston spill pointed out the need for a culture change at TVA. The question, according to Moore, became "how to accomplish that." As Moore began to research corporate culture and accountability, he became aware of a serious cultural challenge within his own organization.

"I realized that I, as a leader, did not know enough about culture," Moore says. "So, I brought in a consultant to conduct an employee engagement survey and 360-degree reviews for us individually. Through that process, we learned we had some of the same dysfunctional attributes we'd identified at TVA, such as low trust and poor communication."

The results of the first employee engagement survey placed the OIG in the lower quartile for metrics on elements such as trust, communication, teamwork and respect for leadership. Moore said that through this process he realized that *he* was a primary cause for culture problems in the OIG.

"Unfortunately, I had approached my people with the attitude of 'I'm the inspector general appointed by the president. I'm going to fix you now.' And whether I ever said that directly or not, that's what people heard — that somehow the problems we were experiencing, either culturally or operationally, were because they were not quite measuring up."

Moore says he received a great deal of stinging criticism from his staff in his first 360-degree report. So, he told them, "OK, here's what I have to fix. And I need you all to hold me accountable because you said that I don't really listen. I want to be a better leader by being a better listener."

And so, in a remarkable convergence, TVA's culture challenge also became Moore's "aha" moment. "If you're going to instill trust in people, you need to be vulnerable and fix yourself first," he says. "Then, invite others to join you in your journey to improve."

Moore and his employees participated in third-party training to learn how to communicate difficult information effectively. They also studied the book, *The Speed of Trust,*[1] which Moore calls "the how-to on trust

[1] *The Speed of Trust — The One Thing That Changes Everything,* by Stephen M. R. Covey, Free Press, 2006: www.speedoftrust.com/How-The-Speed-of-Trust-works/book.

for every leader." The strategy worked. In their next employee engagement survey five months later, the OIG group scored near the upper quartile. Six months later, they finally reached the upper quartile, where they've remained ever since. And in 2015 and 2016, TVA's OIG was named by the Partnership for Public Service as one of "The Best Places to Work in the Federal Government." (The Partnership for Public Service is a nonprofit, nonpartisan organization committed to improving the effectiveness of government.)

It's OK to mix in a little psychology with our accounting. I think we need to be able to listen and really hear people. Not listening for transactional items, but listening for intent. It tells you so much about what's really going on in your company.

Moore says the OIG's employees drove this transformation. "They realized, as TVA's auditors, that they couldn't go to TVA and analyze their culture with advice for improvement if their office's culture wasn't any better," he explains. "They knew they'd have little credibility, even if their model for evaluating culture — and their intentions — were good."

The Importance of Listening

After the hard work of transforming the OIG's culture, Hammer says she was ready to work with the management of TVA to help change theirs. "It made it a bit easier knowing we were coming from a good place. They couldn't look at us and say, 'But look at *your* culture!' TVA's management let us know that they were aware that the OIG culture had improved dramatically and for the better," she says. "Having that credibility at the beginning of the process was essential."

Nevertheless, Hammer says the OIG still faced some resistance from TVA's management, who were not accustomed to having their culture questioned by auditors. Drawing on the work they had done to improve the culture at OIG through better communication, Hammer, Moore and other OIG personnel met with TVA's operating officers, the vice president of human resources, and the CEO several times, listening to their concerns and working with them on process development. They tested their methodology at Cumberland Fossil Plant, which TVA's management had recommended as a place to start because they were confident that location already had a good culture.

Auditing TVA's culture was a change for the OIG, as well. Hammer says auditors traditionally are more conditioned to talking about things like internal controls, procedures and programs. "We're not used to asking, 'How well do you trust your manager?' or 'Do you feel comfortable expressing an opinion different from your manager without fear of retaliation?' Those are things that management can lose sight of — the importance of the people on the line and how they really feel."

She adds that the OIG enlisted help from an industrial organizational psychologist from the University of Tennessee at Chattanooga to help develop their cultural questionnaire topics. "We were moving into areas where it was important to have credibility, and so we wanted to be sure that our questionnaire was valid if challenged by TVA," she says.

This front-end work paid off later. Hammer says working with a behavioral consultant was a "transformative experience" for the auditors, adding, "I think it's OK to mix in a little psychology with our accounting. I think we need to be able to listen and really hear people. Not listening for transactional items, but listening for intent. It tells you so much about what's really going on in your company. That is something that we've not thought a lot about before — the human element and how much that impacts everything."

Hammer says she believes that auditors too often overlook the need to dig deeper when listening to the people they're auditing. When interviewing someone about a process, auditors may ask about the steps, and how a specific internal control might not be working well. Or, they may ask if there's been a breakdown in the process that has become a recurring issue. But they don't usually think about the human element driving these issues.

Hammer recommends that internal auditors look and listen for certain behaviors, lack of expectations and bad communication that may have led to internal controls breaking down. "If there has been a management override, ask, 'Why?'" she says. "Perhaps someone's bonus is based on it? Management overrides are a significant area of concern because there is a control system in place and, for whatever reason, they've done an end run. Lack of trust is one of the biggest cultural risks. If there isn't trust in the people or the system, you'll end up with manual workarounds that create problems and unintended consequences."

Red Flags for Cultural Audits

Moore concurs with Hammer's advice. "You don't have an auditing 'hot spot' unless you have a leadership problem," he says. "TVA has pockets where leadership is fantastic, so the culture is fantastic. But in hot spots, the leader isn't trusted and doesn't know how to build trust with people."

When people say that they don't feel safe to raise their hands and offer a differing opinion to management, that's a big red flag, Moore says. Other red flags include a significant dip in production, or operations running late in meeting performance metrics. Process problems, leadership problems or culture problems could be reasons for these issues. Another type of red flag, according to Moore, is a problem documented in a prior audit that is found again in a subsequent audit. Employee grievances or other concerns can also help to shed light on potential red flags, he says.

Lack of trust is one of the biggest cultural risks. If there isn't trust in the people or the system, you'll end up with manual workarounds that create problems and unintended consequences.

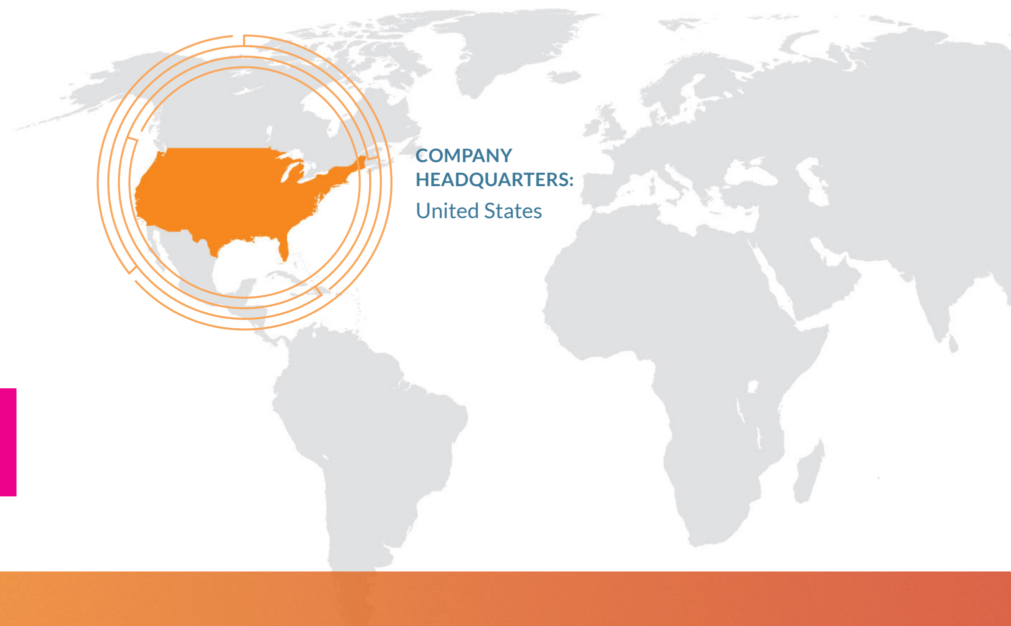
Hammer's OE group risk-assesses business groups at TVA based on red flags and determines where their audit plan will take them in the coming year. When they have audit findings, Hammer's team doesn't simply make recommendations to fix procedural, behavioral or performance issues. They are also very committed to doing follow-up 'pulse' reviews after six months, which target the issues identified in the first review. "We see if the business unit is moving in the right direction and if they are taking the actions that they said they would take," Hammer says.

Identifying Strengths

The OE team has a key goal of not only finding risks but also identifying strengths that could be replicated in other business units at TVA, according to Hammer. But effectiveness is not the only goal: Alignment with the business unit's mission, and ultimately, with TVA's mission, are also objectives for the team, she says.

With their new approach to audits and focus on organizational effectiveness, Hammer and Moore say they see the OIG's influence at TVA growing. They recently audited a very effective group that had strong leadership, good processes and performance, and an appreciative workforce. Hammer and Moore told the manager that they usually schedule a follow-up audit for six months out, but since there were no actionable items, they would not be back so soon.

"The manager said he really appreciated that, but hoped that we would come back then anyway because he wanted to see if they were still making progress," says Hammer. "When a business unit has no audit findings and a manager with that kind of attitude, it should be held up as a model for the rest of the organization to emulate."



T-Mobile

Doing Things the Right Way at T-Mobile

As the fastest-growing company in the wireless industry, we move quickly and shake up the industry, but we always remember that we need to behave and compete ethically. Getting business done is important, but getting it done the right way is more important.

— Michael Rimkus, Senior Vice President of Internal Audit and Risk Management

EMPLOYEES IN COMPANY:
50,000

INDUSTRY:
Telecommunications

ANNUAL REVENUES:
US$37.2 billion
(as of December 31, 2016)

NUMBER IN IA FUNCTION:
25

YEARS IA FUNCTION HAS BEEN IN PLACE:
18

IA DIRECTOR/CAE REPORTS TO:
Audit Committee and CFO

T-Mobile is not only the fastest-growing company in the wireless industry, adding more than 8 million customers per year for the past three years, it is also one of the most ethical — that's the assessment of the Ethisphere Institute. For nine consecutive years, Ethisphere, an organization that defines and measures corporate ethical standards, has declared T-Mobile one of the world's most ethical companies.

"Each year, Ethisphere keeps raising the bar for this esteemed award, and each year we keep winning," says Michael Rimkus, senior vice president of internal audit and risk management at T-Mobile. "We are known as an organization with a solid value system — an ethical company dedicated to doing things the right way."

For T-Mobile, Rimkus explains, the "right way" means solving customer pain points and making the customer experience easier, better, more flexible and less confusing. This transformative philosophy, ushered in by John Legere when he became the organization's president and CEO in 2012, helped T-Mobile evolve from a struggling entity to one of the nation's leading mobile services providers in a few short years.

"We are the 'Un-carrier' in the wireless industry," Rimkus says. "We do things differently than the other guys."

Rimkus joined T-Mobile in 2003 as the director of internal audit, so he has been around long enough to see real change at all levels in the organization. In January 2017, he was promoted to his current position, where he reports directly to the audit committee and administratively to CFO Braxton Carter.

The audit services team at T-Mobile, which is comprised of internal audit and retail audit, consists of 25 total auditors, including only three who are dedicated to IT audit. "The company is built on technology, so I didn't want to go an inch deep and a mile wide on IT auditors," Rimkus says. "For deep technology audits, we co-source with the leading global auditing and services firms. In addition, our retail audit function covers in-store operations. Ten auditors in the field oversee this effort. They focus primarily on policy compliance, cash management and inventory operations."

The audit team's short-term objectives center on helping management identify and implement appropriate controls and facilitate aggressive growth plans. "The longer term is all about mission, vision and values," Rimkus says. "Our mission is to be a trusted partner within the business by providing value-added services designed to assist risk management control and governance processes. The audit team represents the checks and balances, helping T-Mobile sustain these processes."

"How We Play"

Rimkus credits his longevity with the company to T-Mobile's corporate culture. "I would not have stayed here for 15 years unless I felt strongly that I could personally align with the organization's culture," he says.

When he first joined, Rimkus overheard other employees talking about T-Mobile's Value Statements. "They referred to these Value Statements in ordinary conversation," he says. "I thought they were kidding at first, but I soon found out that values are completely ingrained in the culture here."

The Value Statements were eventually rebranded into five "How We Play" statements, according to Rimkus:

1. **Frontline first, because customers are first.** This statement underscores that T-Mobile's most important human assets are the "frontline" — associates, sales representatives and care center representatives — who work with customers every day and can dramatically influence the customer experience.
2. **Results matter. Count on me to deliver.** Everyone at T-Mobile sets goals on what they want to achieve. When goals are set and aligned with management, there is an expectation of accountability. The underlying understanding is: *Ask for help if you need it, but be accountable and deliver on your objectives.*
3. **Be bold. Think big. Make a difference.** As the self-described "Un-carrier," T-Mobile strives to do things differently. The message to employees is to be creative, ask yourself how you could make things better, and make a difference in any way you can.
4. **Play to WIN and have fun.** "We want to be the best in the industry," Rimkus explains. "We have been adding more customers than our three main competitors combined. We are playing to win. We work hard, but we also have fun by celebrating our success."
5. **Do it the right way.** "Whatever we do for our business and our customers, we make sure that we do things the right way — the ethical way," he says.

Rimkus adds, "As the fastest-growing company in the wireless industry, we move quickly and shake up the industry, but we always remember that we need to behave and compete ethically. Getting business done is important, but getting it done the right way is more important."

In the finance organization at T-Mobile, quarterly meetings feature "How We Play" awards, which recognize employees who have exemplified one or more of the five statements in the previous quarter. "Their stories, told with enthusiasm, are met with applause at the meetings," says Rimkus. "This helps to strengthen and support the company's cultural guideposts."

He cites "tone at the top" for making this philosophy possible. "We have total accessibility and an open-door policy at T-Mobile," he says. "Representatives in the stores can send our CEO emails if they want to make him aware of something, and he will read them and respond. There are so many avenues available at the company for reporting questionable actions. We are not only trying to solve customer pain points. We want to solve employee pain points, too."

Listening to Customers

When a company wants to be disruptive, as T-Mobile certainly has been, how does it manage the risks inherent in that approach? For Rimkus and his team, managing these risks means constantly helping leadership find new approaches to demonstrate the company's "doing things the right way" philosophy.

"We're helping customers get the most from T-Mobile's products and services, so that means we have a personal conversation to find out what each customer needs," Rimkus says. "Just the simple act of listening to customers has caused such a shift for us culturally. So much of our culture, even from a risk point of view, is about the customer."

According to Rimkus, the industry's overall culture has not, historically, been focused on treating the customer fairly, but rather on locking them into two-year contracts, which have long been considered the industry norm. T-Mobile has shifted to unlimited, one-rate plans with no hidden fees or taxes, encouraging customers to purchase their phone and offering to migrate them to a T-Mobile plan, free of charge.

Another example of T-Mobile solving customer pain points is international roaming. The company has implemented roaming agreements in 160 countries. "Our customers can use their phones with no additional charge or configuration necessary," Rimkus says. "That really opened customers' eyes to the fact that T-Mobile is here for them, and striving to improve their experience in every way we can."

Just the simple act of listening to customers has caused such a shift for us culturally. So much of our culture, even from a risk point of view, is about the customer.

Aligning Culture With Tone at the Top

For Rimkus, a misaligned corporate culture is one where an organization has printed material about its values and ethics but does not demonstrate what those materials convey. "It's nice to have a code of business ethics, but if leadership is not setting an example by following the code, that speaks volumes," Rimkus says. "People can read through that very quickly."

T-Mobile uses a "Rock It Survey" to stay abreast of how employees perceive leadership's intentions and actions. The survey consists of eight to 10 questions that get to the heart of how employees feel about the company and management team, as well as individual job satisfaction and levels of engagement. All employees across the company take the survey twice per year.

Auditing culture comes down to the tone set by leadership, and whether that tone permeates the business, flowing down through the ranks and every level of management.

T-Mobile does not conduct specific audits of culture; however, the company embarks on several initiatives that reveal culture across the organization and within business units. "We assess culture in every audit project," Rimkus says. "Let's say we conduct an audit and find a pervasive compliance issue in a segment of our business. We dig deep and ask, 'How did this come about? By the tone set by leadership or by poor policy?'"

He cites fraud as a good example. The internal audit team looks not only at where it can occur, but also at the cultural tone and point of view around fraud, making sure that fraud controls — from policy compliance rules to hotline calls and anonymous complaints — are culturally aligned. "You can't stop collusion," Rimkus says. "But if you set a tone that everyone is an owner in the business, you go a long way toward minimizing the risk." T-Mobile's CEO made every employee a shareholder and asks that people treat the business as if it were their own.

"To me, auditing culture comes down to the tone set by leadership, and whether that tone permeates the business, flowing down through the ranks and every level of management," Rimkus says. "If I were in a different organization and trying to audit culture, I would look at the documented statements and guidelines the company lives by. Then, I would consider the tone set by the leadership team and see if they were really living by their own guidelines."

At Australia's First Bank, Westpac, Group Audit's Motto Is "Calling Out the Things That Matter"

Talk to people within your organization. Find out what HR, leadership and other groups really want from a culture audit. One of the most crucial aspects of this whole process is finding the right way to communicate about culture because the findings are subjective and not easy to summarize.

— Kevin McCabe, Chief Auditor and General Manager, Group Audit

EMPLOYEES IN COMPANY:
35,580

INDUSTRY:
Financial Services

ANNUAL REVENUES:
US$16 billion
(as of September 30, 2016)

NUMBER IN IA FUNCTION:
94

YEARS IA FUNCTION HAS BEEN IN PLACE:
N/A

IA DIRECTOR/CAE REPORTS TO:
Chair of the Board Audit Committee; administratively to the CFO

Westpac Banking Group, Australia's first company and first bank and one of the country's "big four" financial institutions, is celebrating its 200th anniversary in 2017. Cultural pillars like customer focus and community involvement have contributed to the bank's longevity and success.

Westpac is divided into five customer-facing divisions: Consumer Bank, Business Bank, Westpac Institutional Bank, BT Financial Group and Westpac New Zealand. In addition to its primary operations in Australia and New Zealand, Westpac operates branches in the United States, the United Kingdom and the Asia-Pacific region.

Kevin McCabe is Westpac's chief auditor and the general manager of Group Audit, which comprises about 100 full-time employees. Most of McCabe's staff members work at the bank's head office in Sydney, and the other 10 are in New Zealand. McCabe reports administratively to Westpac's CFO and functionally to the chair of the board audit committee. His colleague, Craig Duker, is head of audit for the risk, compliance and human resources (HR) divisions of the bank within Group Audit.

Banking Culture in Australia

Trends and events in the U.S. and U.K. banking industries, which suffered greater damage than Australia's banking industry in the wake of the global financial crisis, influence discussions on risk and culture at senior levels at Westpac.

Like the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in the United States, the Australian Prudential Regulation Authority (APRA) requires, under Prudential Standard CPS 220, that banks and other institutions have systems for identifying, measuring, monitoring, and controlling or mitigating material risks that may affect their ability to meet obligations to depositors or policyholders. The board of an APRA-regulated institution such as Westpac is responsible for the risk management framework and the oversight of its operation by management; it also must provide an annual risk management declaration to APRA. As part of this, Westpac's board must form a view of the risk culture in the institution.

"The real work began when APRA passed the rules to require the board to assert its view of the status of risk culture in the bank," McCabe says. "In Australia, there is a preference for senior-level accountability over rigid regulatory practices. There is a belief that there should be consequences for senior managers if their staff or they do the wrong thing."

McCabe says the intensified regulatory focus on financial institutions in recent years has made it increasingly important to communicate the importance of risk culture from the very top through all levels of the organization.

"At Westpac, we already have a good culture that is dedicated to providing great service and helping our customers, communities and people to prosper and grow. However, that said, we need to keep getting better to ensure we continue to focus on service and helping people. Getting the right culture is one of our biggest priorities."

[To audit culture], an organization must first articulate and identify the culture it wants, the culture it has, the tools available to maintain or improve culture, and the way in which culture can be measured and reported.

Duker adds, "While there is a clear responsibility for the board and CEO in monitoring and strengthening culture, the bank's HR and Risk divisions are also heavily involved in supporting the approach." In addition to recruiting, training and retaining top talent, the bank's HR team conducts an annual survey called *YourVoice* to gather information and insights about the cultural climate at Westpac. Additionally, the Regulatory Affairs group, which has a separate head of culture and conduct, is reviewing ways to measure and report on the culture at Westpac.

"Of course, Group Audit has a role to play in all this," Duker says. "It's our job to call out the things that matter to the board and executive team."

Steps to Auditing Culture

The Group Audit team keeps a watchful eye on inadequate ownership and resourcing of risk management across the three lines of defense, as well as customer complaint patterns, poor trends in audit report ratings, and failures in the broader management of issues that have been raised.

But to specifically audit culture, McCabe and Duker believe that an organization must first articulate and identify the culture it wants, the culture it has, the tools available to maintain or improve culture, and the way in which culture can be measured and reported. Most important, the audit function should have a clear mandate to audit all the above.

Elements of Strong and Weak Cultures

McCabe says that spotting strong corporate culture as an auditor comes down to looking at how easy it is to gather information, gain access to key stakeholders and communicate with others openly and honestly. "Understand whether people openly and honestly discuss problems or whether problems are glossed over or swept under the carpet," he says. "When audit is proactively updated as serious issues arise — such as regulator letters, lawsuits or terminations for cause — that's strong culture." He notes that his Group Audit team and peers in compliance, operational risk and HR cannot be effective if executive management decides to lock them out.

Westpac's foundations for strong risk culture are viewed through risk outcomes and the behaviors that the bank's employees and leaders demonstrate. Examples include how the bank undertakes measured risk-taking, how it rewards people and whether employees feel safe speaking up when they see wrongdoing.

"A CEO who does not like to hear bad news or only wants you to bring a solution, not a problem, is a sign of a weak culture," says McCabe. "Not being able to suggest changes to even the most successful areas in the business is also a warning sign. If ever the Group Audit team was asked to stay away from 'successful' areas — that, too, would be a clear sign of trouble."

McCabe points to CEO Brian Hartzer's unique approach for inviting people to speak up. "At every group meeting that I've attended with Brian, he has a small gift for the person who asks him the hardest question or tells him something about a problem in the business or an issue that they are facing."

Taking Steps in the Right Direction

Recently, Group Audit has taken steps to play an even more distinct role in assessing risk culture.

"We modified our quarterly dashboard on enterprise risk management to have a specific line for culture," Duker says. "We also recently engaged a consultant from a leading global consulting firm to create a more formal questionnaire and approach to assessing risk culture. The outcomes have the added benefit of helping to inform audit scopes."

He continues, "We just hired a Ph.D. candidate who is a registered psychologist to support our risk culture approach over the next two years and to help improve our understanding of culture and its drivers."

Spotting strong corporate culture as an auditor comes down to looking at how easy it is to gather information, gain access to key stakeholders and communicate with others openly and honestly.

As part of Group Audit's obligations to APRA, the team will be performing a deep dive on how the broader organization is managing risk culture this year. "Our audit of risk culture will focus on how management itself is assessing, measuring and reporting on risk culture across the bank," McCabe says. "This includes approaches to align risk culture better between the current and the desired states."

The objectives of these audit approaches, still in the pilot phase, are varied. According to McCabe and Duker, these are designed to meet regulatory obligations, help shape the scope of controls-based audits, provide broader observations to leadership and the board on how risk culture is managed and measured, and lastly, to identify where management has not sufficiently called out instances where risk culture is misaligned.

McCabe and Duker say that the challenges of these audits are equally diverse. Information obtained during any culture audit is often less tangible and more qualitative in nature. So, forming conclusions and overcoming pre-existing biases associated with findings is tricky.

Recommendations for Launching Culture Audits

For any organization about to embark on culture audits, McCabe and Duker caution auditors to be ready for the moment when management asks for a detailed articulation of how the audit team will assess risk culture.

“I think you should tell them that this is well-described in industry literature, and it is time for internal audit to start looking at it,” McCabe says. “I suggest trialing the approach first, then get buy-in for the value that it will add, before rolling it out more broadly. It is also important to clearly define the roles and responsibilities for assessing risk culture across the three lines of defense and ensure that the organization is moving in the same direction.”

“Overall, keep your options open,” Duker says. “Think about where the industry is going and what is best for your organization. Seek out what peers and networks are doing. Look to leading global accounting and services firms that specialize in this kind of work. Understand that auditing culture requires different skills than traditional auditing and that those skills might not be readily available in the audit industry talent pool.”

McCabe adds, “Talk to people within your organization. Find out what HR, leadership and other groups really want from a culture audit. One of the most crucial aspects of this whole process is finding the right way to communicate about culture because the findings are subjective and not easy to summarize.”

Often, playing the underlying results back to management is the first step in the reporting process, providing a good foundation for discussions around how the results should be interpreted and acted upon more broadly.

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Brian Christensen
Executive Vice President, Global Internal Audit
+1.602.273.8020
brian.christensen@protiviti.com

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PROTIVITI INTERNAL AUDIT AND FINANCIAL ADVISORY PRACTICE — CONTACT INFORMATION

Brian Christensen
Executive Vice President,
Global Internal Audit
+1.602.273.8020
brian.christensen@protiviti.com

Andrew Struthers-Kennedy
Managing Director
Leader, IT Audit Practice
+1.410.454.6879
andrew.struthers-kennedy@protiviti.com

AUSTRALIA

Mark Harrison
+61.2.6113.3900
mark.harrison@protiviti.com.au

BELGIUM

Jaap Gerkes
+31.6.1131.0156
jaap.gerkes@protiviti.nl

BRAZIL

Raul Silva
+55.11.2198.4200
raul.silva@protivitiglobal.com.br

CANADA

Ram Balakrishnan
+1.647.288.8525
ram.balakrishnan@protiviti.com

CHINA (HONG KONG AND MAINLAND CHINA)

Albert Lee
+852.2238.0499
albert.lee@protiviti.com

FRANCE

Bernard Drui
+33.1.42.96.22.77
b.drui@protiviti.fr

GERMANY

Michael Klinger
+49.69.963.768.155
michael.klinger@protiviti.de

INDIA

Sanjeev Agarwal
+91.99.0332.4304
sanjeev.agarwal@protivitiglobal.in

ITALY

Alberto Carnevale
+39.02.6550.6301
alberto.carnevale@protiviti.it

JAPAN

Yasumi Taniguchi
+81.3.5219.6600
yasumi.taniguchi@protiviti.jp

MEXICO

Roberto Abad
+52.55.6729.8070
roberto.abad@protivitiglobal.com.mx

MIDDLE EAST

Sanjeev Agarwal
+965.2295.7770
sanjeev.agarwal@protivitiglobal.me

THE NETHERLANDS

Jaap Gerkes
+31.6.1131.0156
jaap.gerkes@protiviti.nl

SINGAPORE

Sidney Lim
+65.6220.6066
sidney.lim@protiviti.com

SOUTH AFRICA

Peter Goss
+27.11.231.0600
peterg@sng.za.com

UNITED KINGDOM

Lindsay Dart
+44.207.389.0448
lindsay.dart@protiviti.co.uk

UNITED STATES

Brian Christensen
+1.602.273.8020
brian.christensen@protiviti.com

THE AMERICAS

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