KPMG

2017 Internal Controls Survey

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Executive summary

Although Sarbanes-Oxley (SOX) is not a new regulation, it has continued to evolve over the last 15 years since it was enacted. We've seen additional focus areas from the Public Company Accounting Oversight Board (PCAOB) which increased the levels of documentation, and upcoming changes in key accounting standards may require further changes to systems, controls and documentation. Additionally, the uses of technology and data have changed significantly in this time frame – bringing about new considerations such as using intelligent automation to facilitate business processes or compliance activities. And all of this is happening while organizations strive to take costs out of their SOX programs.

> "Organizations are looking at the 'compliance exercise' associated with SOX and are trying to reduce the cost aspect. However, to truly see improvement in your SOX program, it's important to look at the controls through a value lens, rather than just a cost lens."
>
> **– Sue King**
> KPMG's SOX Solutions Lead

KPMG LLP surveyed more than 100 organizations to compile data related to current SOX trends, challenges and strategies. We are pleased to present the results of this survey to provide insights into how your organization's SOX program compares with both your industry peers and across the total population of respondents.

Key takeaways

1

A focus on cost reduction targeted specifically at control testing costs, rather than the total cost of control.

- 52% of strategies included minimizing the cost to test SOX controls vs. only 11% focused on decreasing the cost of performing controls.
- Organizations may be overlooking the cost of performing control activities, which is typically the largest contributor to the total cost of control.

2

External auditor reliance as the primary strategy used to manage compliance costs and the SOX burden on the organization.

- The SOX program strategy for 54% of the organizations is to ensure maximum reliance by the external auditor. However, only 23% of organizations are able to quantify the savings achieved as a result of external audit reliance on their organization's testing.
- Focusing less on external auditor reliance may open the door to other cost reduction strategies, such as smaller sample sizes or self-assessments in low-risk areas. External auditor reliance should be a deliberate economic decision, weighing the costs and benefits of that strategy vs. other strategies.

3

Lack of confidence in control execution and documentation.

- Less than half of the respondents (45%) are confident that their controls would pass (i.e., be effective) without testing them.
- Four out of five top areas of improvement were related to control execution — improving controls over key spreadsheets, increasing control automation, quality of control evidence and overall quality of control performance. However, the common SOX program strategies (maximize external auditor reliance and minimize testing costs) are not aligned with these areas of improvement.

Survey objectives:

- Gain valuable perspectives on how an organization's SOX program compares to that of its peers.
- Obtain insights into results across the total population of respondents and industry trends.
- Enhance understanding of SOX program maturity.

Detailed findings

Strategy

Strategy for 2017 SOX program:

Strategies related to the SOX programs were primarily related to testing aspects – ensuring maximum external auditor reliance (54%), minimizing testing costs (52%), and rationalizing controls (49%).

52% vs. 11%

52% of strategies included minimizing the cost to test SOX controls vs. only 11% focused on decreasing the cost of performing controls.
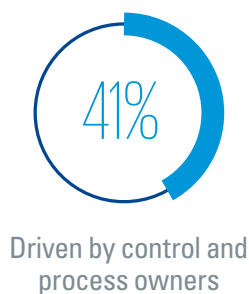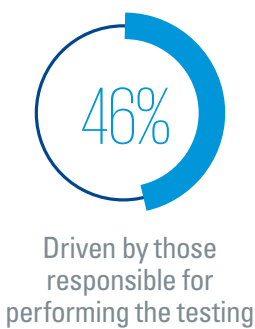
65%

Organizations in the financial sector (Banking & Capital Markets and Financial Services) were more likely (65%) to include "Change business processes so that the controls are embedded in the process, are not performed just for SOX, and are valuable to the business" as part of their strategy. This may be influenced by the large number of regulatory and compliance activities that need to be embedded within their business processes.

61%

Organizations with annual revenues of $10 billion or more were most likely to include controls rationalization (61%) and focusing efforts on the entity-level and most critical controls (57%) as part of their strategy.

Development of SOX strategy:*

46%
Driven by those responsible for performing the testing

41%
Driven by control and process owners

38%
Largely influenced by the external auditor

Although the SOX program strategy for 54% of organizations was to ensure maximum external auditor reliance, that strategy was not always driven or largely influenced by the external auditor.
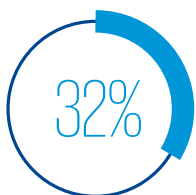
32%
Developed in conjunction with other compliance / assurance functions
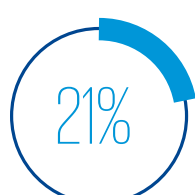
21%
Driven by the audit committee

20%
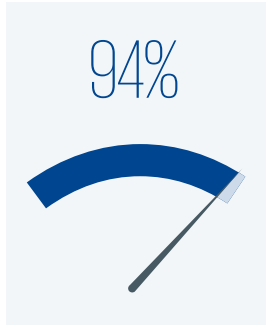Developed as a stand-alone compliance effort

2%
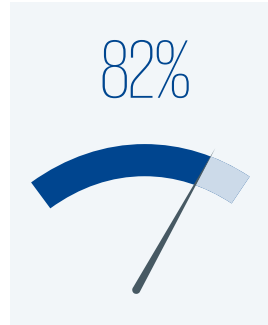Does not have a clear strategy

*Respondents could select multiple responses

4

Areas of improvement

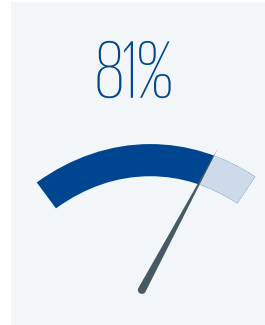## Top five areas that are "fine as is" or need only minor tweaks*:
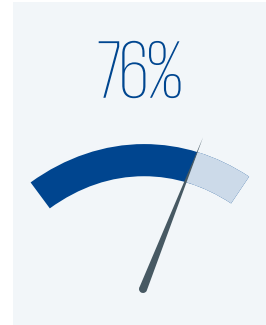
Improve communication with audit committee	Improve the SOX risk assessment process	Take control of the SOX program overall	Improve system scoping to align with key business processes	Improve risk mitigation by changing process design
94%	82%	81%	76%	75%
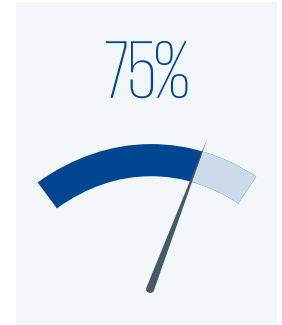
*Respondents ranked multiple statements

Top five areas with improvement or significant improvement needed*:

Increase control automation

51%

Improve controls over key spreadsheets

41%

Improve quality and consistency of control performance

37%
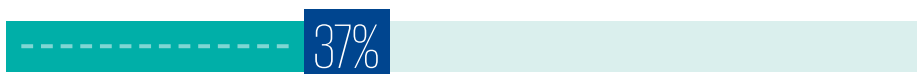
Improve quality of control evidence
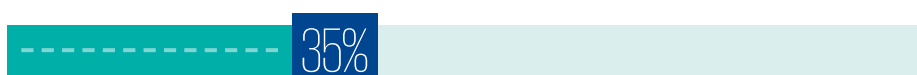
35%

Reduce control testing cost / effort

34%

The top areas with improvement needed primarily focus on how controls are performed and documented. Improving control performance and documentation may have a correlation to reducing associated testing costs; however, these responses indicate that perhaps organizations should first focus their strategy on control design and performance, before focusing efforts on reducing testing costs.

*Respondents ranked multiple statements

There were only two areas where organizations with revenue of $10 billion or more were more likely to believe that improvement or significant improvement was needed in comparison with the full respondent group:

Focus efforts on critical control areas including significant unusual transactions

36% >$10B VS. **33%** All

Reduce control testing cost / effort

36% >$10B VS. **34%** All

Industry trends were noted in industries that often have a more distributed and decentralized nature of operations, such as Industrial Manufacturing, Building, Construction & Real Estate and Consumer Goods:

21%

Only 21% of respondents indicated that expanding into non-SOX business units needed improvement or significant improvement.

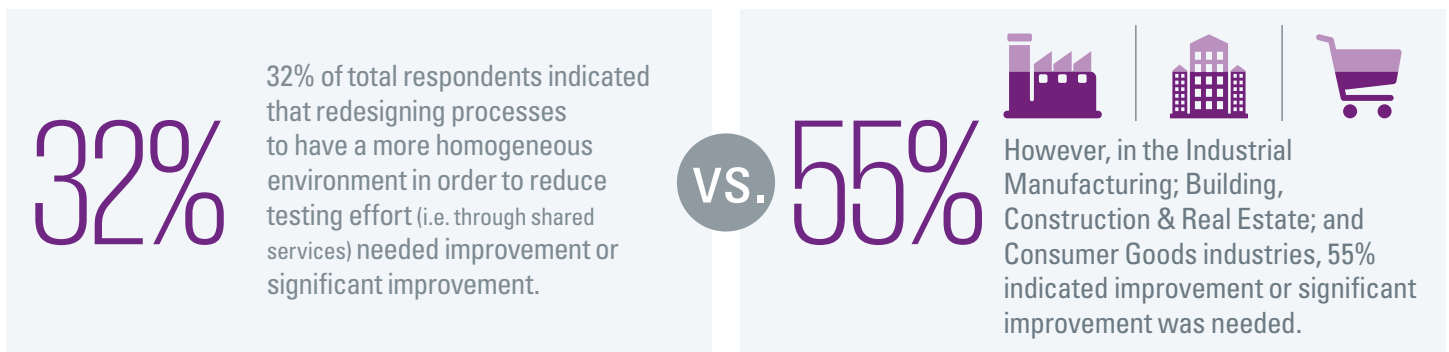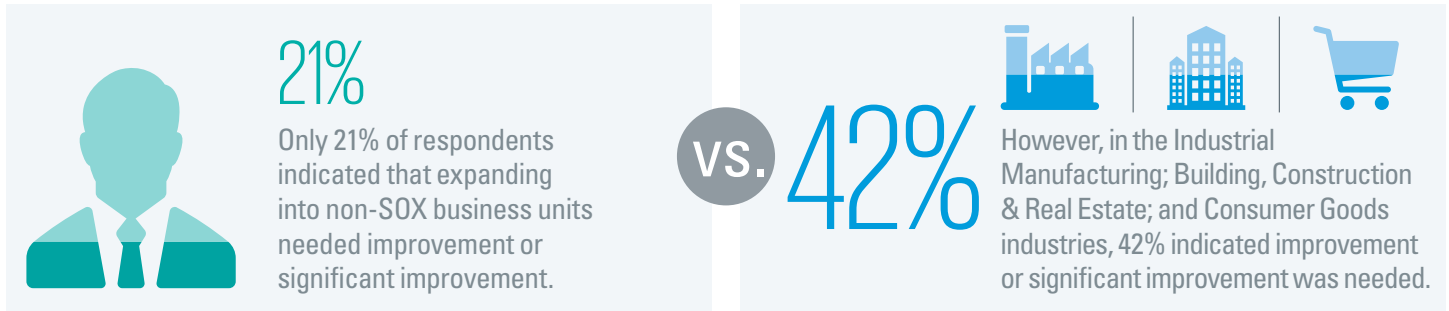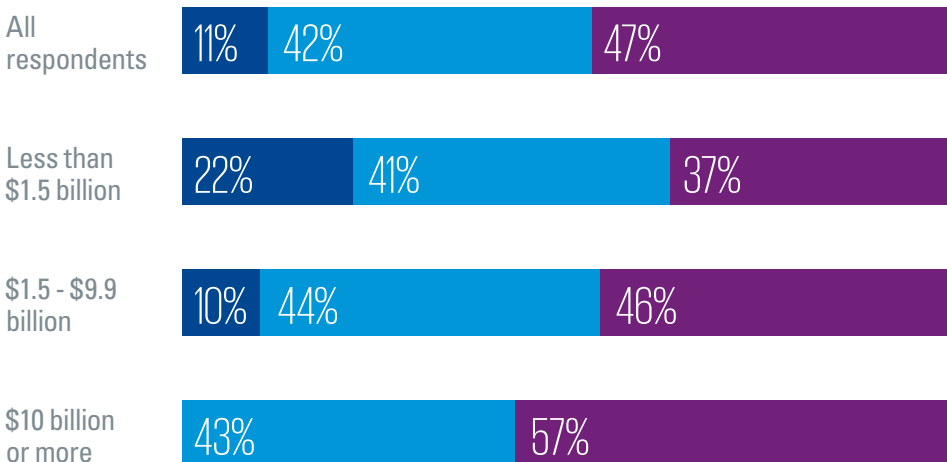VS. **42%**

However, in the Industrial Manufacturing; Building, Construction & Real Estate; and Consumer Goods industries, 42% indicated improvement or significant improvement was needed.

32%

32% of total respondents indicated that redesigning processes to have a more homogeneous environment in order to reduce testing effort (i.e. through shared services) needed improvement or significant improvement.

VS. **55%**

However, in the Industrial Manufacturing; Building, Construction & Real Estate; and Consumer Goods industries, 55% indicated improvement or significant improvement was needed.

State of the SOX program

SOX program's maturity level:

	Developing	Evolving	Maturing
All respondents	11%	42%	47%
Less than $1.5 billion	22%	41%	37%
$1.5 - $9.9 billion	10%	44%	46%
$10 billion or more		43%	57%

Developing: Controls identification and stabilization

Evolving: Improved risk assessment and scoping, and rationalized controls (optimization of current control environment)

Maturing: Improved business processes which have reduced the cost of control performance, reduced risk, and added value to the business

Smaller organizations (less than $1.5 billion in revenue) were more likely to be developing.

VS.

Larger organizations ($10 billion or more in revenue) were more likely to be at the other end of the maturity spectrum.

Mean responses for agreement with the following statements regarding SOX programs:

(1 = strongly disagree and 5 = strongly agree)

Our organization's culture and tone at the top support our SOX program
4.3

Investors care about material weaknesses
4.2

Our management, executive management, and Board find our SOX program to be valuable
4.1

Changes required to remediate control issues are not only performed to make it through the SOX process, but are also taken seriously going forward
4.0

Our SOX program effectively improves transparency in our organization
3.8

The new revenue recognition and/or lease accounting standards will increase our control performance efforts
3.8

Our organization considers SOX when planning significant business initiatives, such as new information systems, process reengineering, or outsourcing
3.7

We often add key controls based on external auditor requests
3.5

I am confident our controls would pass (i.e., be effective), even without testing them
3.3

45%

Only 45% of respondents agreed or strongly agreed with this statement. This indicates a potential problem with the control culture and that perhaps more effort and strategic focus needs to be placed on the effective and efficient performance of control activities.

Frequency with which issues identified through SOX testing are used to make changes to the process:
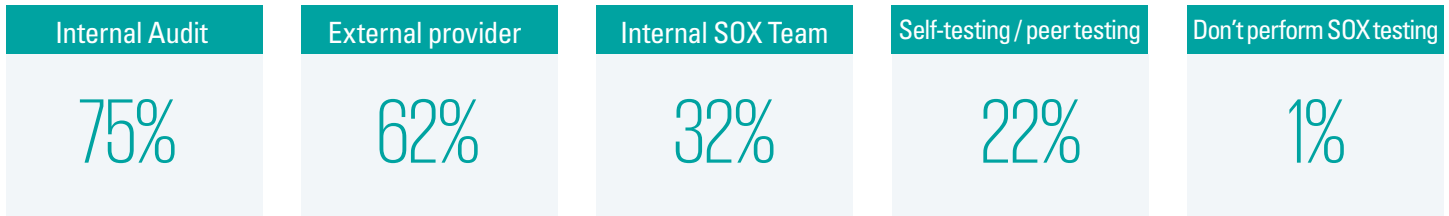
To enhance the control environment and reduce risk

To change the process so controls are more meaningful to the business (not just performed for SOX)

To make a process more efficient regarding control performance (i.e., increase automated controls)

Never | **Rarely** | **Often** | **Always** | **Don't know**
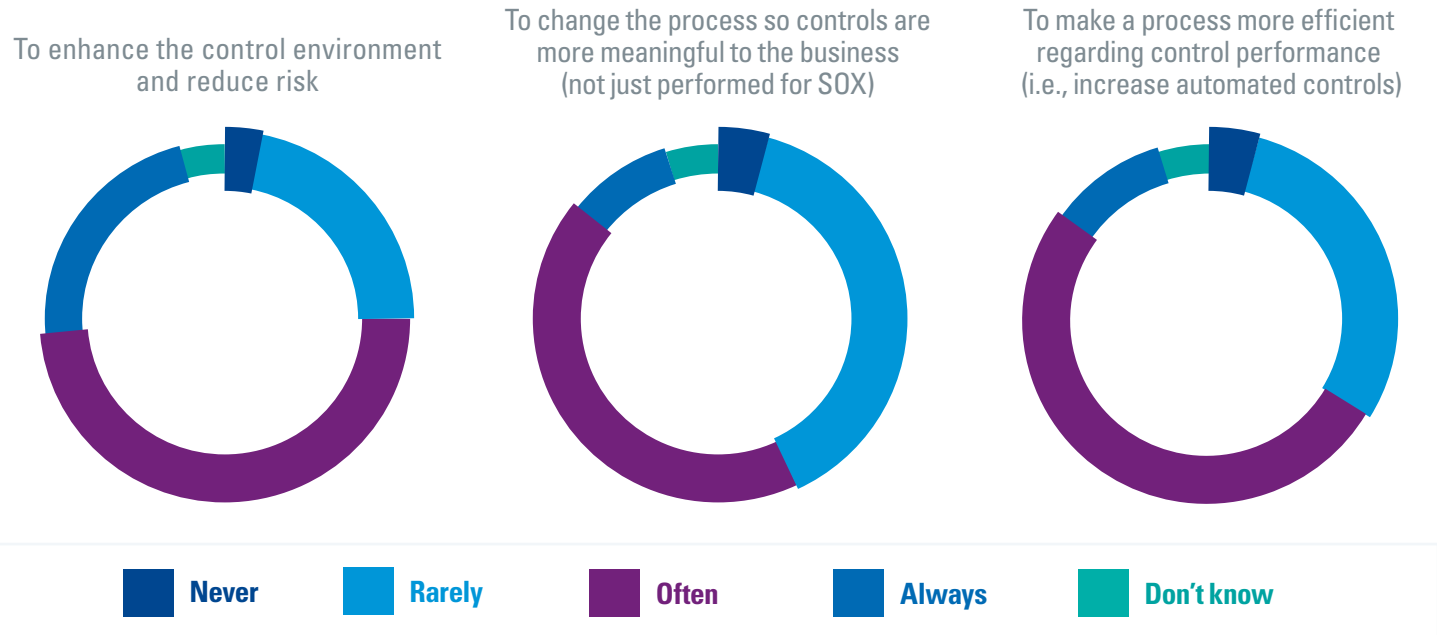
SOX program execution

Who performs SOX testing:*

Smaller organizations ($1.5B or less in revenue) were more likely to use external providers (72%)

VS.

Larger organizations ($10B or more in revenue) were more likely to have an internal SOX team (54%) and to incorporate self-testing or peer testing as a component of their SOX program (39%)

Internal Audit	External provider	Internal SOX Team	Self-testing / peer testing	Don't perform SOX testing
75%	62%	32%	22%	1%

* Respondents could select multiple responses

For organizations where SOX testing is performed by Internal Audit, the proportion of total Internal Audit hours related to SOX:

- **1-25%**
- **26-50%**
- **51-75%**
- **76-100%**

In organizations where Internal Audit performs SOX testing, 34% of those organizations spend more than 50% of their total Internal Audit hours on SOX. This is largely the case for organizations with less than $10B in revenue (44%). In organizations with $10B or more in revenue, the burden of SOX testing was often distributed across various parties (Internal Audit, SOX team, other departments, etc.), allowing a larger proportion of Internal Audit hours to be focused on other value-add activities.

How use of an external provider for support with SOX program has changed from 2016 to 2017:

Frequency of control training for control / process owners (or control performers):

Using external providers more in 2017

Using external providers less in 2017

Using external providers about the same

Less than annually

More than annually

Annually

Don't know

SOX program costs

How costs are expected to change from 2016 to 2017 in regards to:

Cost and effort for management to perform the control activities

4%   66%   27%   3%

Control performance costs are largely staying the same or increasing in 2017; however, only 11% of organizations included focusing on decreasing such costs as part of their SOX program strategy.

SOX compliance activities (costs related to control documentation, control testing, and SOX program governance; not including the cost of control performance)
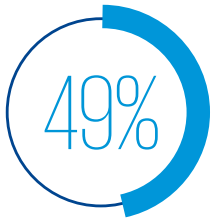
16%   46%   36%   2%
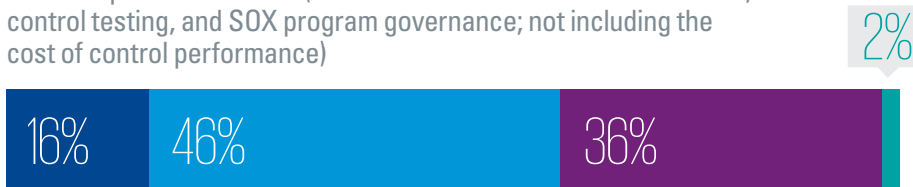
Cost will decrease

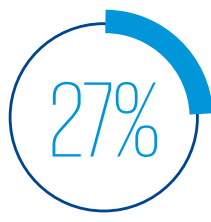**Costs will stay the same**

Costs will increase

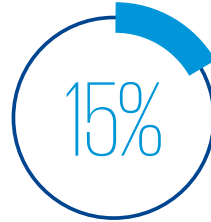**Don't know**

External auditor coordination

Differences in SOX controls for testing in comparison to the external auditor:
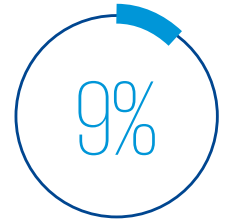
49%

Our organization has more controls in scope for testing than our external auditor

27%

Our organization and our external auditor have the same number of controls in scope for testing and the controls are the same

15%

Our organization and our external auditor have approximately the same number of controls in scope for testing; however, the controls vary

9%

Our external auditor has more controls in scope for testing than our organization

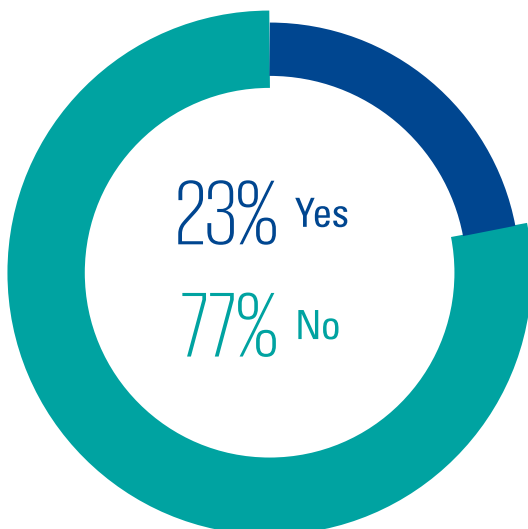## Extent to which the external auditor relies on SOX activities:
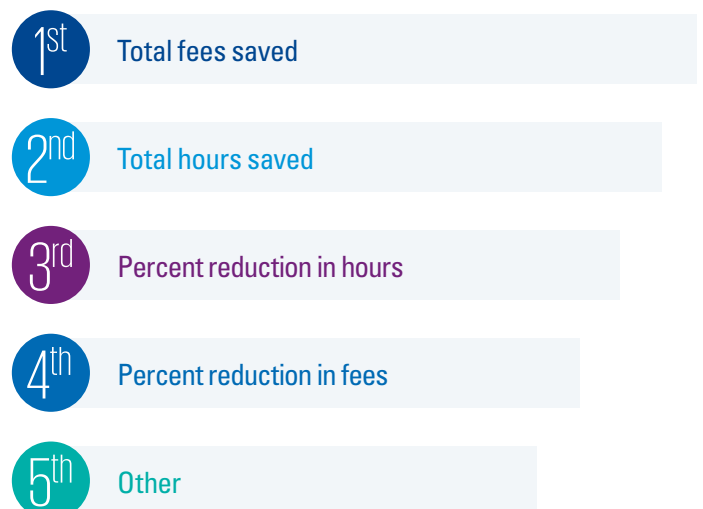
Test of design (i.e., a walkthrough)

| 28% | 13% | 31% | 25% | 3% |

Test of effectiveness (i.e., control testing)

| 12% | 11% | 33% | 41% | 3% |

Legend:
- No reliance
- Minimal
- Moderate
- Fully, to the extent possible
- Not applicable/ not performed

Able to quantify savings achieved as a result of external auditor reliance, if applicable:

23% Yes
77% No

Most common metrics used to quantify and/or monitor savings from external auditor reliance:*

1st — Total fees saved

2nd — Total hours saved

3rd — Percent reduction in hours

4th — Percent reduction in fees

5th — Other

*Respondents could select multiple responses

Approach modifications based on external auditor's reliance model:*

33% — We use templates (or nearly similar formats) from external audit in areas of reliance

26% — We modify sample sizes

18% — We modify our rollforward approach

11% — We decrease the level of documentation in areas of non-reliance

7% — We self-assess (no independent testing) in areas of non-reliance

6% — Other

48% — We do not change our approach based on our external auditor's reliance model
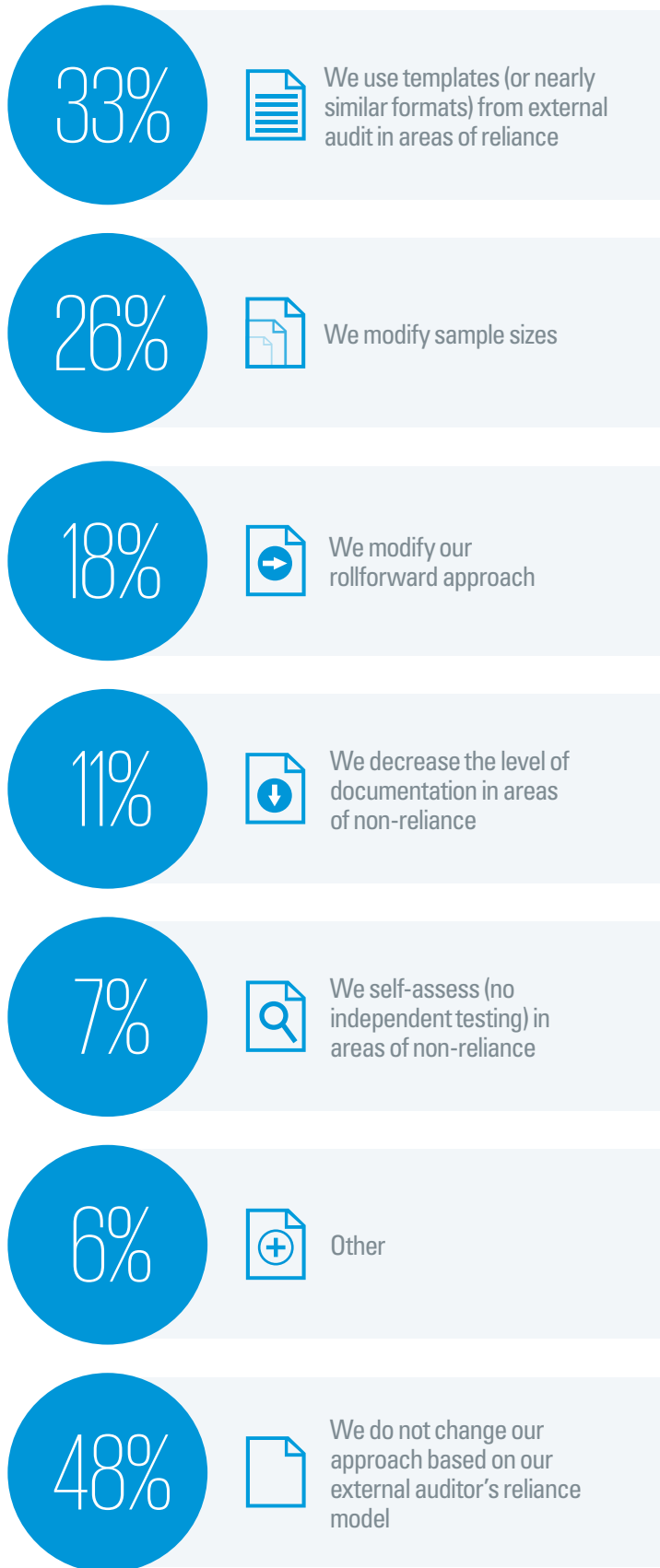
*Respondents could select multiple responses

Technology use in controls

Whether key controls include continuous monitoring controls:

38% Yes

49% No

13% Don't know

Whether key controls include continuous auditing controls:

20% Yes

62% No

18% Don't know

Use of data and analytics (D&A) within SOX program:*

39%

While D&A has been somewhat of a hot topic in recent years, 39% of organizations have not incorporated it into their SOX programs.
The most common ways organizations are currently using D&A in the SOX program is to select samples or during the risk assessment process.

Sample selections — **41%**

SOX risk assessment — **32%**

As part of a control activity performed by management — **22%**

Within control testing — **7%**

*Respondents could select multiple responses

Use of digital labor/intelligent automation in regards to the SOX program:

To perform a control activity:

5% Yes

76% No

19% Don't know

To assist with compliance activities (testing or reporting on controls):

4% Yes

76% No

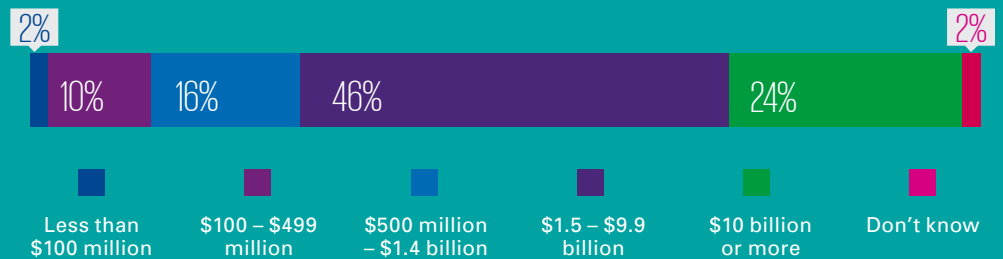20% Don't know

Survey methodology

Surveys were completed by individuals with responsibility for internal controls over financial reporting (ICOFR) / the SOX program in their organization. The survey was completed once on behalf of each participating organization (n = 114). The findings offer useful direction and provide a basis for comparison and further analysis. The results were derived from a Web-based survey that was conducted from May through June 2017.
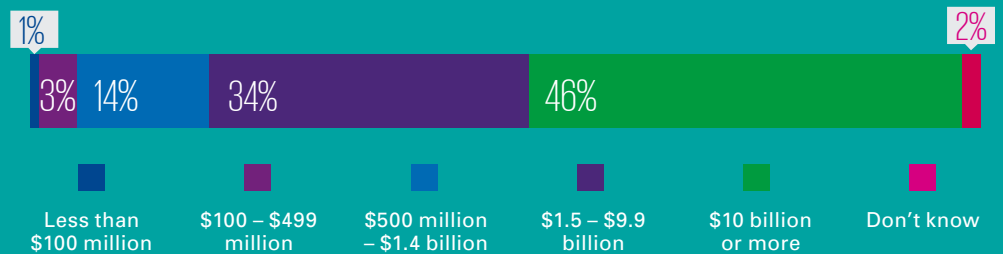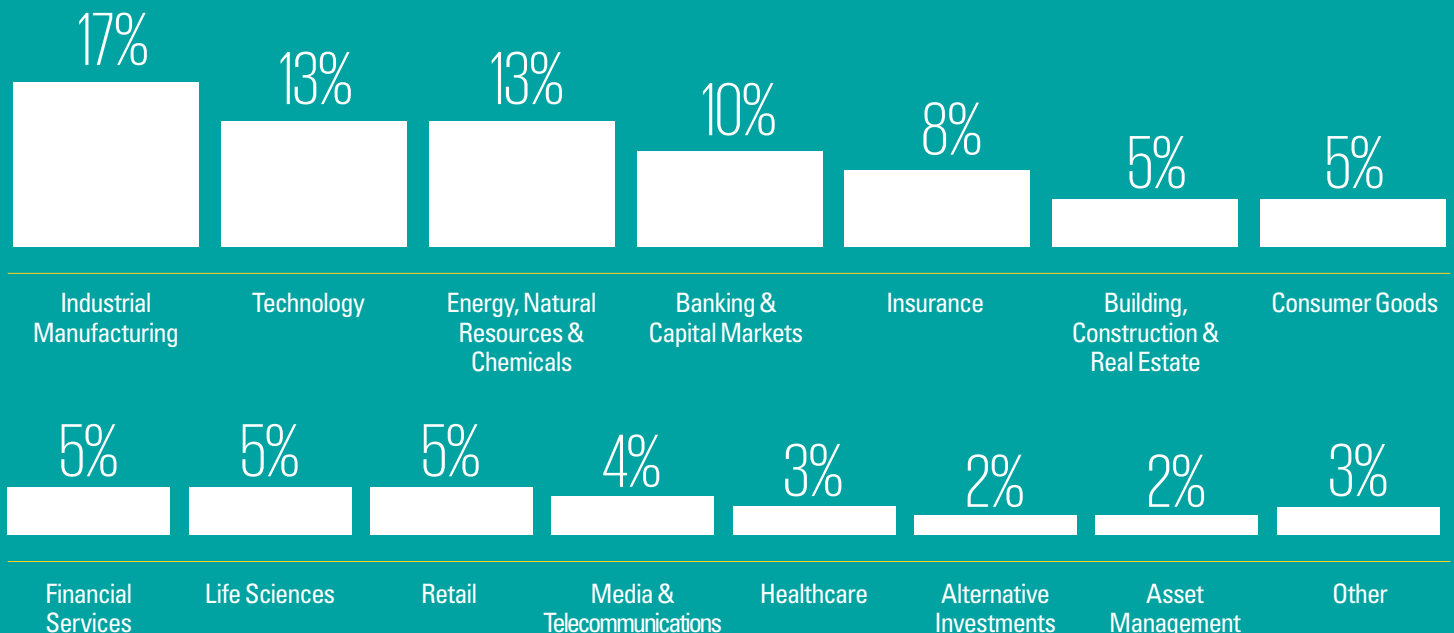
Survey demographics

Type of organization:

- 91% Public
- 5% Private
- 2% Not-for-Profit
- 2% Quasi-Governmental

Organization's total annual revenue for the most recent fiscal year:

Less than $100 million	$100 – $499 million	$500 million – $1.4 billion	$1.5 – $9.9 billion	$10 billion or more	Don't know
2%	10%	16%	46%	24%	2%

Organization's total assets for the most recent fiscal year:

Less than $100 million	$100 – $499 million	$500 million – $1.4 billion	$1.5 – $9.9 billion	$10 billion or more	Don't know
1%	3%	14%	34%	46%	2%

Primary industry:

Industrial Manufacturing	Technology	Energy, Natural Resources & Chemicals	Banking & Capital Markets	Insurance	Building, Construction & Real Estate	Consumer Goods
17%	13%	13%	10%	8%	5%	5%

Financial Services	Life Sciences	Retail	Media & Telecommunications	Healthcare	Alternative Investments	Asset Management	Other
5%	5%	5%	4%	3%	2%	2%	3%

About KPMG LLP

Our Risk Assurance Services are designed to enhance the efficiency and effectiveness of internal audit functions, enterprise risk management programs, reviews of third party relationships and risk and controls management. Our professionals can augment and enhance an organization's existing risk management capabilities through the use of experienced risk and controls professionals, supplemented by multidisciplinary skills from each of our Advisory service lines.

KPMG's Advisory professionals combine technical, market and business skills that allow them to deliver objective advice and guidance that helps the firm's clients grow their businesses, improve their performance, and manage risk more effectively.

Our professionals have extensive experience working with global companies ranging from FORTUNE 500 companies to pre-IPO start-ups. We go beyond today's challenges to anticipate the potential long- and short-term consequences of shifting business and technology. With a worldwide presence, KPMG continues to build on our member firms' successes, thanks to our clear vision, values, and our people in 152 countries. We have the knowledge and experience to help clients navigate the global landscape.

Contact us

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