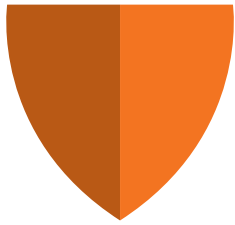




Barclay Simpson  
corporate governance recruitment

# Market Report 2008

Internal & Computer Audit



**Barclay Simpson Market Report 2008**

# Internal & Computer Audit

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## 01 Executive summary

### 18 years of market reports

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Welcome to Barclay Simpson's 2008 Market Report. This is the 18th year we have produced a report summarising and analysing recruitment trends in internal auditing, as well as making predictions for the year ahead.

We place great value on professional reaction to the Report and would appreciate your comments.

### Review of 2007

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Until the third quarter, there was little doubt that 2007 had been a successful year for the internal audit recruitment market. Corporate governance had come to an end of a period of regulatory excess and many internal audit departments, having had their activities distorted by regulatory initiatives, were able to return to more usual recruitment patterns.

Demand remained strong and the number of internal auditors employed continued to grow. Skill shortages remained in many areas of the economy and earnings growth and job prospects were robust. It was a year that in many respects was without event. Demand for internal auditors exceeded the available supply. The economy, the key market driver that underpins employment and recruitment, continued to grow above trend. Five interest rate rises designed to cool the economy and curb potentially sticky inflation were broadly seen as the appropriate remedy.

At any given time there are risks to the economy, and by mid year, with one exception, they were collectively or individually perceived to be no more elevated than usual. The exception, and like most risks, there was no shortage of commentators who foresaw potential trouble, was **US sub prime mortgage lending**. Whilst for many a far away and arcane matter, its sudden manifestation in the UK was a run on a FTSE 100 bank, Northern Rock. This was an unprecedented event, where confidence, the commodity that underpins not only the financial system, but much else, simply drained away. The benign view was that it was a one off event, where incompetent management took excessive risks. More likely, **in our view, it was the harbinger of tougher times. Northern Rock was a very public example of a risk that was not just mis-priced, it was not recognised. The management had not played the 'what if game?' with sufficient rigour.**

There appear many more such risks that come in a variety of different guises. Here are just two examples:

Until the third quarter, there was little doubt that 2007 had been a successful year for the internal audit recruitment market.

1. According to the IIA's 2007 Employment Survey, 90% of internal auditors believed that hiring in the profession would remain unaffected or only slightly decrease in the event of a recession. The problem with this is that it is simply wishful thinking. It is apparent that with £1.4 trillion of personal debt, vast tracts of the UK working population also believe their future revenue streams from employment are secure. This perception has encouraged people to gear themselves up with debt. This has no doubt brought consumption forward, increased the growth rate of the UK and allowed people to feel even more secure to go and borrow some more. Debt, however, at some point has to be repaid. It could be a rude awakening, as there are not too many areas of economic activity and employment that would be immune to the affects of a recession.
2. The UK economy, off the back of an unprecedented period of economic growth, has a ratio of government debt to GDP that is one of the highest in the OECD. Fine if you believe the never ending growth story, not so good if you perceive that there may be a risk in its delivery. At this stage of the economic cycle government finances should be robust and capable of expansion to prime a weakening economy. They are plainly not.

Against this backdrop, by the final quarter of 2007, the change in the internal audit recruitment market was more real than perhaps apparent. The number of vacancies, although marginally down from its peak, was holding up. The number of candidates registering was continuing a very gradual rise. The number of interviews taking place was broadly consistent with previous quarters. What was not consistent were the number of job offers, acceptances and therefore internal auditors starting new jobs. These seemingly had started to decline. The difference was evidence that some companies and individuals, in response to uncertainty, had started to defer decision making.

## Prospects for 2008

Any slowdown in the rate of internal auditors accepting positions can be temporary, and there are a number of instances of this in recent years. However, nobody should be under the illusion that the recruitment market is not ultimately dependent on the economy. **Whilst regulatory initiatives certainly increase demand and existing frameworks ensure that internal audit and wider governance efforts are properly resourced, a slowing economy will compromise the employment prospects of internal auditors.**

It is perhaps not surprising that we have become complacent. The lowest growth rate achieved by the UK economy in the last 15 years was 1.8%, in 2004/5. For

some sectors of the economy, and certainly those internal auditors employed in sectors dependent on discretionary consumer spending, it felt like a recession. However, at that time, government spending was increasing in real terms at over 4%, which ensured the economy continued to grow.

**Whilst you can pick your economic forecast for 2008, there is little doubt that the economy will grow more slowly than we have become accustomed to.** What is certain is that there are elevated levels of uncertainty not only regarding the UK economy but also the world economy. It is also clear that **in 2008 government and personal finances will not be what they once were. Any slowdown will further aggravate government borrowing and inflation will make it difficult to fully use interest rate cuts to stimulate economic growth.**

**Provided the economy continues to grow at anything above 1.5%, which is about as pessimistic as the current spate of economic forecasts allow, it is reasonable to assume that the vast majority of internal auditors will continue to enjoy secure employment.**

However, the number of internal auditors forced into the recruitment market would increase. The time taken for employers to fill vacancies would reduce and the time taken for internal auditors to find new positions would lengthen. Whilst some sectors would be hit harder than others it would remain a broadly familiar recruitment market.

**At growth of less than say 1%, which would be the result of a contraction in private sector economic activity, significant levels of uncertainty would develop, recruitment activity would fall and unemployment amongst internal auditors would rise.** It would also allow an updated assessment to be made of whether the shortage of internal auditors is structural or cyclical.

## 02 Key market drivers

2007 was a successful year for internal auditing and the internal audit recruitment market. Whilst any reflection on the year is likely to be dominated by the economic developments in the final months, the number of internal auditors employed in the economy continued to grow and for many internal audit departments, the availability of internal auditors in the recruitment market improved.

In 2007, and we will leave the economy to last, the following factors had the most impact on the internal audit recruitment market:

### Regulation

In recent years, the internal audit recruitment market has been distorted both directly and indirectly by regulation: directly by requiring additional resources to audit compliance with regulations; indirectly, by peeling internal auditors away from their primary responsibilities and using their skills and experience for other purposes.

It has perhaps always been this way. The natural attrition rates in internal auditing have been appreciably higher than in any other comparable disciplines. This has resulted in the internal audit profession losing a high proportion of its practitioners to other disciplines and most Chief Internal Auditors having to be familiar with and regularly using the recruitment market.

Whilst there are no prescriptive regulations in the UK for the existence or activities of internal audit departments, it is encouraging that without any regulatory stimulus, the number of internal auditors employed in the economy grew during 2007. In the past, a frequently asked question was; what is the optimum number of internal auditors a company of any particular size and in any given sector should employ? Although historically it has been highly divergent, in recent years, due to a trend to reduce headcount, there has been a convergence in the number of internal auditors employed. There are two explanations for this:

1. There is now almost universal understanding of the role and responsibilities of internal audit. Until recently, this was not always the case and the size of internal audit departments often reflected differing responsibilities.
2. There was a trade between the individual capabilities of internal auditors and the numbers employed. For example, does a company employ two experienced, capable and qualified internal auditors or three less capable individuals? In response to the almost universal increase in complexity of audit environments the former has prevailed.

It is encouraging that without any regulatory stimulus, the number of internal auditors employed in the economy grew during 2007.

**The long process of substituting quality for quantity has ended and in response to factors such as new technologies, communication, globalisation, regulation and legislation, more internal audit resources are required to provide management with the assurance they can rely on.**

It may well be that the current hiatus in regulatory development is allowing internal auditors to focus exclusively on their core responsibilities. This may not last long. **Difficulties in the credit markets, particularly in the United States, are still primarily a business problem. However, if material numbers of Americans lose their homes it will become a political problem.** Politicians, post Enron, will be seen to have failed to effectively reform corporate governance. At the very least, executive compensation schemes seem to have encouraged some very poor risk taking. Further regulation will follow.

## Business investment

Business investment has always been a key driver in the internal audit recruitment market. A growth area in internal auditing is the audit of business investment and project developments. Whilst historically anchored in the development of new IT systems and applications, an increasing number of internal audit roles are either partially or exclusively devoted to projects of all types.

Not surprisingly, these types of positions and the work of internal audit departments increase on the back of any growth in business investment. **However, annual investment growth declined during the first half of 2007, having grown strongly during 2006. Recent developments in the credit markets are likely to depress business investment as the average cost of borrowing from banks increases.**

Whilst most big companies have other sources of finance to fund their investment, any impairment of the ability of banks to lend will no doubt affect corporate investment.

**It is worth remembering that recruitment is ultimately a form of investment. If companies are not making big investment decisions, it is less likely that smaller ones will be made too.**

## Financial Services

Three sectors employ the bulk of internal auditors in the UK: the public sector, the external audit providers, primarily in the guise of the Big 4, and the financial services sector.

The Big 4 and other external audit providers are by far the biggest trainers and developers of internal auditors and are net exporters of staff to the internal audit recruitment market. The public sector, if it was all added up, may well be the biggest employer. The majority of public sector auditors stay in the public sector and movement between the public and private sectors is limited. Transfers most often happen via external audit providers who recruit internal auditors from the public sector and then ultimately lose them to the private sector. Direct movements from say civil service internal audit departments into the private sector, which were once common, have become increasingly rare.

**Of the three sectors, the financial services sector has the biggest influence on the internal audit recruitment market.** By far and away the largest and possibly the majority of movements between employers in the internal audit recruitment market involve a financial services company. Any other sector in commerce could stop recruiting and it would only have a marginal impact on the total internal audit recruitment market. Should the financial services sector significantly slow, then the whole tone of the recruitment market would change.

**During the first half of 2007, the financial services sector recruited strongly across all its various sub sectors, both in London and throughout the provinces. It was apparent, however, that internal audit recruitment in the financial services sector had become more problematic by the final quarter.** Within some sectors, such as general insurance and even the building societies, there was no change. However, in other areas, such as commercial and investment banking, there were signs that recruitment activity had slowed. A classic symptom is that interviews are conducted, but decisions to recruit are not made. Whilst this may be a transitory phenomenon, there is as yet no clear indication of the total losses sustained by the credit markets and even where the losses will ultimately accrue.

One might speculate that in spite of the considerable investment in corporate governance, particularly risk management and to a lesser extent internal audit and compliance, much of the banking industry has sustained huge losses on credit instruments whose potency was not fully appreciated. It does beg the question how effective was the investment? Can an argument be made that not enough has been spent? **If what is a business problem becomes a widespread political problem, it is difficult to see how corporate governance will not ultimately return to the political agenda.**

## Migration

Much, perhaps rightly, is made of migratory flows in and out of the UK. The statistics, based on International Passenger Surveys and the allocation of National Insurance numbers to overseas nationals, suggests that there is net inward migration of approximately 200,000 people per year with perhaps 1,000 people leaving per day and 1,500 arriving.

Within internal auditing there is not much evidence of significant numbers of internal auditors leaving the UK. If they are, then it is via internal transfers within companies rather than via the recruitment market. **There are, however, significant numbers of people either with internal audit experience or aspiring to be internal auditors still migrating to the UK.**

In 2006 we reported that the flow of internal auditors from other EU countries into the UK has slowed. This continued into 2007 and the migration of large numbers of internal auditors, particularly from the EU accession countries, is now over. In fact **employment prospects for internal auditors in the EU, where significant skills shortages have emerged, are now at least as good as in the UK.** Many of those who now come to the UK, and perhaps the majority of those already here, view a period in the UK as transitory and a good opportunity to improve their English, enjoy some valuable commercial experience and then return to their home country.

The number of Antipodeans coming to the UK, usually on 2 year working visa, remains broadly constant. Their language, internal audit and commercial skills allow them to immediately find work and they continue to provide a significant portion of the internal auditors available for contract work. They are a transitory, but established part of the internal audit recruitment market.

**The number of internal auditors arriving in the UK under the Highly Skilled Migrant Programme, at least as indicated from our candidate registration data, is continuing at a high level.** Whilst historically these migrants have come from the Indian sub-continent, South East Asia and Africa (essentially Commonwealth Countries where English is often the business language), more recently migrants have been registering worldwide. Like many administrative exercises, particularly where points are awarded against set criteria, some have appropriate skills and experience to work in the UK, others plainly do not.

The effect of internal audit migration into the UK remains primarily London-centric, though this is likely to change as migrants settling long term in the UK start to move away from London.

The increasing internationalisation of the internal audit recruitment market is now an established trend. However, not unreasonably, it has developed during a period of uninterrupted economic growth. Any internal auditor entering the recruitment market with reasonable expectations has found employment. No doubt from an economic perspective migration has restrained salary inflation and has been beneficial. How the process would adapt to a shrinking employment market is not clear.

## Employment legislation

The UK has witnessed a huge increase in employment related legislation. This has primarily been driven by the European Union working to standardise employment practices and employee rights across the Community. After the Age Discrimination Regulations in 2006, 2007 saw the implementation of numerous measures in areas such as maternity, paternity and adoption leave, equality, statutory holidays and the establishment of a single Commission for Equality and Human Rights. Future developments include amendments to existing regulations in areas such as sex discrimination, obligations to consult with employees on key issues and measures affecting the rights of fixed term and agency workers.

**The introduction of employment legislation covering such a wide range of issues has had a number of effects on UK employers and employment markets.**

As with all legislation, the devil is in the detail. The scale and complexity of these regulations has made employers increasingly reliant on HR professionals and lawyers to protect them from the risks of non-compliance. The premiums to insure against claims for discriminatory or unfair practices are rising. The regulations have been given teeth through the uncapping of penalties and the burden of proof lies more heavily on the employer than the employee. Employment Law is one of fastest growing areas of the legal profession.

In recruitment, this has led to the increasing involvement of HR in formalising and standardising recruitment processes and has been a factor in the growth of the outsourcing of the management of recruitment processes.

**Whilst the growth in regulation has helped to lessen the incidence of exploitation and unfair discrimination, it has increased the costs involved in recruiting and employing staff.** It has also lessened the ability of

companies to alter their employment practices in the light of changing economic conditions. In attempting to protect the vulnerable and to promote fairness in the workforce, the legislators need to strike a balance and ensure job creation is not compromised.

Compliance with employment legislation cannot now be ignored.

## External audit providers

As we acknowledged in last year's report, whilst the Big 4 make up probably over 80% of this sector, there are a number of top 10 firms and smaller consultancies which are active. The sector always has the potential to be a key market driver. **As the largest reservoir of internal audit resource and particularly as a source of recently trained internal auditors, this sector casts a long shadow over the internal audit recruitment market. It has the potential to quickly exacerbate either shortages or surpluses in the recruitment market.**

The boom years of section 404 Sarbanes Oxley and International Financial Reporting Standards work are over. The market for the provision of externally sourced internal audit services is now more competitive and it is clear that some of the smaller providers have recruited against the anticipation of work that has not been forthcoming.

However, the external audit providers had a benign effect on the recruitment market during 2007. They broadly, and perhaps against expectation, retained their staff and undertook limited sector specific internal audit recruitment.

Should economic growth stall during 2008 it is reasonable to assume that the sector as a whole, with varying degrees of coercion, would encourage internal auditors into the recruitment market.

## The economy

It is worth reiterating that the economy underpins the recruitment market. In 2007, taken as a whole, the UK economy grew slightly above trend against another highly favourable year of world growth. If nothing else we usually cover ourselves by referring to the myriad of threats that exist at any given time. Whilst these are usually speculative, the last quarter of 2007 seemed to confirm that the effects

of a 'credit crunch', could be painful. **The high point of the current cycle is over and a soft landing is less likely than thought earlier in the year. The squeeze on credit will certainly reduce business investment, investment in housing will fall and the growth in household spending will most likely be below trend.**

The risks to growth all appear on the downside and it is reasonable to conclude that the economic outlook is more uncertain than it has been since 2002/3. Then, the war in Iraq and the consequences of a mini recession in the United States resulted in a problematic recruitment market that lasted for almost a year. The UK economy and the internal audit recruitment market was assisted by the public sector embarking on an unprecedented recruitment drive, a cut in interest rates to their lowest levels in 40 years and the emergence of Sarbanes Oxley, the biggest jamboree the auditing profession had ever known. As we pointed out last year, in the event of economic trouble, none of these stimulants is going to be available this time.

## 03 Detailed analysis

### Overall market

As a standard part of the information gathering process used to compile the Barclay Simpson annual market reports, we conduct a quarterly survey of internal audit departments.

The survey consists of 50 private sector internal audit departments and provides an indication of the number of internal auditors employed and vacancy levels in the UK economy.

### Key observations

#### Employment and vacancies both up

The statistics would seem to indicate that the budgeted number of internal auditors, the total number employed and the number of vacancies are all up on last year. The immediate conclusion is of a robust recruitment market. However, bald statistics can be misleading. For example, a rise in the number of vacancies could readily be interpreted as a sign of buoyancy when in fact internal audit departments can have vacancies that they choose not to fill. They are either subject to a recruitment freeze or are sufficiently uncertain about the future that they choose to delay recruitment.

#### Conflicting pressures

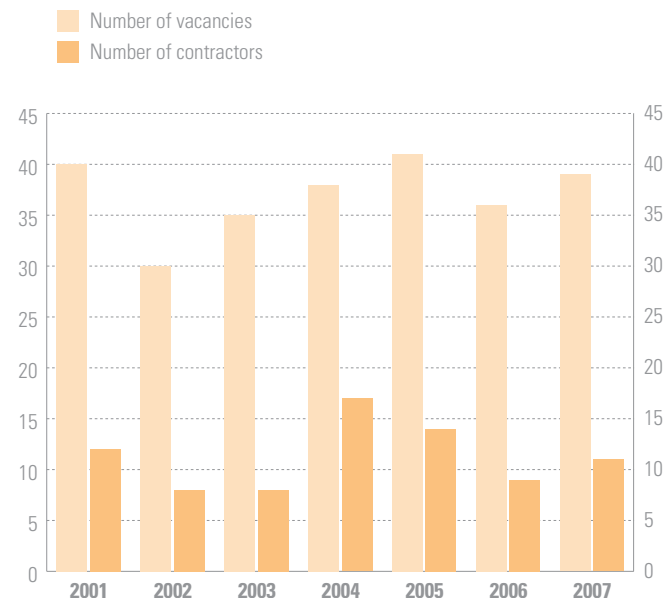
The current internal audit recruitment market is subject to conflicting pressures.

The increase in both the budgeted number of internal auditors and the actual number employed indicates that companies have been prepared to increase the resources available to their internal audit departments. We discussed the likely causes of this in our interim report during 2007:

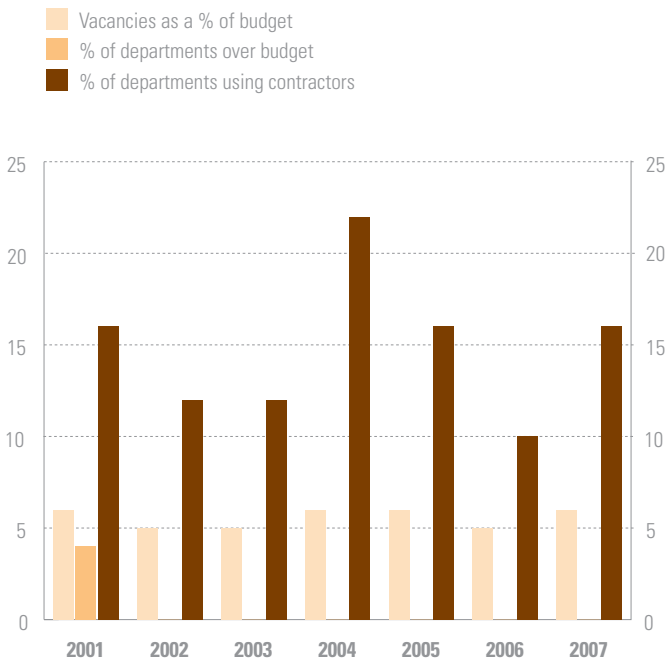
1. Even though internal audit is becoming more efficient, the demands made upon it are increasing. This is not only in response to the increased complexity of the audit environment, but internal audit is becoming increasingly integrated into a more comprehensive control environment which ultimately leads to more responsibility and the need for more resources.
2. Whilst companies continually make decisions between in-sourcing and out-sourcing, there has recently been a bias towards building up in-house teams.
3. Finally, and the effect is now complete, resources that had been diverted away from internal auditing to achieve compliance with Sarbanes-Oxley have flowed back.



Over the course of 2007 the budgeted number of internal auditors increased from 664 to 683 in Q2 and up to 684 by the year end. The total number of internal auditors employed rose from 628 to 645.



At the year end the number of vacancies stood at 39, up from 36 at the start of the year.



Vacancies as a percentage of budgeted number was 6% against 5% at the start of the year.



Naturally, when companies are looking to increase the number of internal auditors they employ, in what remains a candidate scarce recruitment market, the number of vacancies increase. Without doubt, **the increased resources companies were prepared to make available during 2007, constitute a vote of confidence in corporate governance generally and internal auditing specifically.**

There is no doubt that internal audit departments are more secure in their existence and funding than they have been in the 18 years that this report has been produced. This should be accepted, whilst also appreciating that if there is a material down turn in the growth of the economy, the whole tone of the recruitment market will change.

**The flow of candidates into the market**

The internal audit recruitment market is finely balanced. Without any redundancies or forced entries into the recruitment market (which incidentally ran at a historically low number in 2007), internal auditors, for both professional and personal reasons, are continually entering the recruitment market. Those with marketable skills and experience, who are appropriately priced, secure employment and leave the market. Others who have specific skills that are in less demand or those with less marketable skills and experience remain in the market for longer.

In periods of uncertainty, and the economy is now operating in far more uncertain conditions, companies defer recruitment in the same way they cut back or defer investment.

There does not have to be a recruitment freeze for a Head of Audit to take the view that they would rather run a person short and cover themselves for any future budget cuts. Internal candidates are more likely to be available and there may be more pressure to accommodate them. They may also take the view that with more candidates becoming available in the recruitment market they can afford to wait and not to compromise on who they consider to be their ideal candidate.

Should companies slow down or hold off recruiting then the market backs up surprisingly quickly. What was a market with candidate shortages can rapidly change.

**Forced redundancies**

If economic uncertainty was to crystallise into something more tangible and, in response, companies scale back their employment, close or sell off operating divisions or ultimately fail, then their resident internal audit departments would be adversely affected and internal auditors made redundant. There were modest redundancies in areas of

the economy dependant on discretionary spending during 2004/5 and more significant redundancies in 2002/3 in the run up to the war in Iraq. Not surprisingly, forced redundancies directly impact the recruitment market. At the start of 2008 redundancy levels remain low.

However, there appears to be growing levels of uncertainty in the economy. Many share prices in sectors such as house building, banking, retail and even the recruitment industry have tumbled in the last six months. Investors appear to be betting on a hard rather than a soft economic landing, particularly in the discretionary areas of the economy.

**The recruitment industry is perhaps the more interesting and pertinent. Whilst there is currently no significant deterioration in trading conditions, investors in the sector are pricing in a lot of potential bad news.**

### Contractors

After a number of years of unprecedented demand for contract and temporary internal audit staff, Sarbanes-Oxley projects, the great provider, tailed off in 2006 and throughout 2007. Projects were concluded and **Sarbanes-Oxley compliance became a business-as-usual function. As a result, the number of contract roles available for temporary internal auditors was significantly reduced and, after a low point achieved during the first half of 2007, only started to recover towards the end of 2007.**

Sarbanes-Oxley distorted the market rates for contract internal auditors and the down turn in demand had a number of effects. The main two are as follows:

1. Contractors have in many cases experienced longer than average periods of unemployment between contracts and have had to lower their rate expectations.
2. Many Sarbanes-Oxley contractors originally came from the public sector and have looked to move back. However, many parts of the public sector, having been priced out of the contract market by Sarbanes-Oxley, entered partnering arrangements with audit providers. This trend was largely hidden from the contractor base until 2007 when contractors coming out of Sarbanes-Oxley projects have found far less contract work available in the public sector.

### Employment growth

Current best estimates for 2008 are that unemployment in the UK, currently at 5.4%, will rise modestly. In recent years, increasing numbers of jobs have been met with an increasing number of available workers. This has resulted in a low and broadly constant rate of unemployment. However, job growth in the UK economy is likely to be flat in 2008.

Most of the recent increase in employment has been in the public sector. That growth is now over and whilst job growth in the private sector rose modestly during 2007, it is unlikely to compensate during 2008. Areas such as retail, leisure

and distribution are likely to be weak, as is the biggest area of growth in recent years, the financial services industry.

**If there is to be any growth in employment in the UK during 2008 it is currently difficult to know where it will come from.**

## Computer Audit

The demand for experienced computer audit staff caused by initial Sarbanes-Oxley compliance work subsided during 2007. In fact, **the demand for computer audit staff was noticeably less than it has been in recent years. However, for those companies looking to recruit computer auditors, the number actively looking for new positions was correspondingly lower and skill shortages remained widespread.** Subject to developments in the wider economy, we expect these shortages to continue into 2008.

We would make the following observations regarding the skill sets that are currently or are likely to be in demand during 2008:

**Network security** remains a priority. Good network security skills, particularly those concerned with firewalls such as Checkpoint Firewall-1, Nokia and Cisco PIX are in demand, as are those for network routers, such as Cisco. Security fears over the use of wireless networks now seem to be easing, but familiarity with the security and control issues is becoming increasingly important for IT audit personnel, together with a good understanding of intrusion detection and prevention systems. Penetration testing (ethical hacking) is also being used by many groups to ensure the security of their network perimeter and a good appreciation of this area is generally considered useful.

The technical IT platform skills most widely sought remains consistent with recent years. Specifically, a sound knowledge and experience of **Microsoft Windows XP/2003** and the various flavours of **UNIX, specifically Linux. Technical IBM mainframe and AS/400** skills remain in demand, as do those for **HP Non-Stop (Tandem)**, although on a smaller scale than other platforms. Demand for technical database security skills, specifically **Oracle, Sybase, and SQL Server** remains strong.

We noted in last year's market report that there is **greater focus on core IT audit reviews such as business continuity, resiliency and physical security**, particularly in relation to pandemic flu and terrorist threats. Climate change, as evidenced by the severe flooding experienced in many parts of the country in 2007 has reinforced this key area of IT audit activity.

Any significant economic slowdown during 2008 will most likely impact IT investment and therefore project and systems development work. However, experience in enterprise systems such as SAP and Peoplesoft remains in demand. Further, the need to make greater use of

technology is likely to ensure continued demand for IT audit skills as companies make extensive use of Blackberry devices, for example, and remote working via VPN to facilitate more flexible working.

## Market sectors – review and predictions

Here is a review of how the key market sectors fared in 2007, along with predictions as to likely recruitment activity in 2008.

### Banking – demand currently uncertain

Up to the fourth quarter of 2007, demand in banking remained robust. Candidates, particularly those with investment banking and specialist capital markets knowledge were scarce. Salary inflation was particularly noticeable for newly qualified candidates and those with up to three years experience. Candidate shortages in the City were eased in some instances by applicants with Highly Skilled Migrant Visas, but exacerbated by the Big 4 who broadly retained their staff with higher salaries and the prospect of management opportunities.

The shortage of candidates resulted in many banks taking good generic auditors without banking experience who they considered worth training and developing.

**In Q4, the banking sector was dominated by the global credit crunch and it was clear that some recruitment was postponed.**

However, recruitment in the banking sector is always problematic in the final quarter. It is currently still difficult to judge how much relates to the usual seasonal fourth quarter downturn and how much to changed market conditions.

The large City based banks that are responsible for the vast majority of recruitment are highly diverse in the range of activities they undertake, many of which have remained profitable. Whilst it is reasonable to assume that sentiment in the banking sector will remain depressed into 2008, plans for staffing levels appear to remain positive and many of the vacancies seemingly shelved in Q4 will be reactivated.

Although the shortage of candidates is likely to remain, the credit crunch may make internal audit a more popular option with, for example, newly qualified ACAs, who may perceive it as being more secure than roles in corporate finance or product control. We would also expect the trend to source candidates internally with banking product and risk skills from such areas as modelling, credit and front office activities to continue.

### Insurance – steady demand

Demand for internal auditors was stronger from the general rather than the life insurance sector during 2007. Overall, total demand was broadly consistent with 2006.

Demand from the general insurance sector remained robust. There was a steady stream of vacancies from the numerous Lloyds managing agents and other insurance, reinsurance and broking groups based in the City. As in 2006, there were fewer start-ups, but no shortage of movements by internal auditors between companies. Candidates with relevant industry sector experience remained in short supply and there was no evidence in Q4 that credit market problems were impacting business.

**Competition remains particularly fierce in the general insurance market. Premium income is growing, as is investment in new systems and technology. We expect demand for internal auditors to remain strong and the shortage of candidates with relevant experience to continue.**

The life sector enjoyed an increase in new business during 2007. However, the outlook for growth is now flat, which is perhaps not surprising given recent market turmoil. The sector enjoyed good profit growth during 2007, which was partially achieved by lower costs and associated staffing levels. During 2007, merger and takeover speculation surrounded a number of major companies within the sector.

During 2007, the number of vacancies was lower than usual. Internal audit departments appeared to be retaining their staff and not losing them internally to other functions. At present **there is little evidence that the uncertainty caused by the credit crunch in the banking sector has spilled over into recruitment patterns in the life market. However, given current uncertainties, the demand for internal auditors is likely to remain subdued during the first half of 2008.**

### Mortgage banks, building societies and credit companies – uncertainty prevails

We reported last year that the expansion of personal credit has spurred the growth of an industry that employs a significant number of internal auditors. We anticipated that the mortgage providers would enjoy steady internal audit recruitment during 2007, but that other credit providers would suffer from the increased credit risks that rising interest rates and a potentially slowing economy would create.

**Although 2008 could potentially be a different story, during 2007, credit providers were not undermined by bad debts. The problem within this sector was the availability of financing.** Northern Rock was simply an extreme example of the problem of using short term

financing to fund long term lending. At the end of 2007, the sector was embroiled in a high degree of uncertainty and there is little doubt that any material deterioration in the quality of the sector's loan portfolios could further destabilise it and make funding both more expensive and problematic.

In the final quarter of 2007, whilst there were a limited number of redundancies in the sector, overall employment remained stable. Many groups continued to recruit.

The outlook for 2008 is subdued recruitment. Mortgage advances both in number and volume have begun what looks like a sharp decline. Credit is less available. Consolidation rather than expansion in the sector looks likely, with the traditional building society model, where funding is substantially based on retail deposits, prevailing. At the very least there will be fewer internal auditors leaving departments internally and therefore fewer vacancies.

Should the sector's problems not remain contained, then the implications for the wider economy could potentially be severe. Rightly or wrongly, the provision of credit has become a big business and potentially a big problem.

### **Manufacturing, energy, construction and contracting – steady demand**

Demand from the manufacturing sector remained steady during 2007. The vast majority of demand was from US and other multinational groups who base their international internal audit departments in the UK. The UK remains an attractive base because of the availability of English speaking internal auditors. Demand from local groups, in spite of the upsurge in manufacturing activity during 2007, remains limited and reflects the relative decline in the UK manufacturing base. Much of the demand during 2007 was, as is usually the case, for recently qualified accountants. Their availability, as in other sectors, was limited and many groups struggled to recruit. Prospects for 2008 are particularly dependent on world growth and, given the uncertainty in the US and Europe, we should expect lower demand during 2008.

It is perhaps worth noting the **increase in demand for internal auditors during 2007 from the energy sector and particularly oil related companies**. There was demand not only from the major multinational groups, but also from the smaller exploration and service groups. High energy prices are stimulating investment and, after many years of only limited recruitment, the oil and wider energy

related sector is now actively recruiting internal auditors. This is likely to continue throughout 2008.

After many years of decline, internal auditing within construction and contracting companies has recently grown. Whilst internal audit departments remain generally small, internal audit has become embedded in the sector. Not surprisingly, growth and record profitability together with the demands of PPP and PFI initiatives have helped. It is likely that demand during 2008 will be more subdued. Whilst spending on infrastructure projects and such things as the Olympics should support the sector, it is slowing along with more speculative property development.

### **Technology, telecoms and media – mixed demand**

Although technology does not account for a big part of the overall demand for internal auditors in the UK, demand was buoyant during 2007.

Heavy worldwide investment in IT has resulted in strong revenue growth for the sector and this has been reflected in the demand for internal auditors.

Many of the opportunities require international travel and, once again, a preference for recently qualified accountants is common. Any significant decrease in demand does not appear imminent.

The UK telecoms market is now relatively mature and international expansion is driving growth. In spite of pricing pressures and fierce competition, demand from the sector was surprisingly strong during 2007, with the majority of the larger groups having regular vacancies. We expect this demand to continue into 2008.

Demand from the media sector was subdued during 2007. Many of the larger groups faced challenges that were either unique to them or common in terms of the competition for advertising and the rapid changes that are sweeping through the sector. A number of smaller niche groups are developing market share, but have yet to reach a point in their development where in house internal audit departments are required. We expect demand in the sector to remain depressed during 2008.

### **Retail and leisure – tough times ahead**

Demand from the retail sector was subdued during 2007. It is becoming clear that employment opportunities for multi-site retail auditors have declined and are unlikely to improve. Technological developments are continuing to make these

positions redundant. The retail sector is currently highly competitive both in its traditional format and the challenges faced by on-line shopping. Demand for corporate auditors was patchy during 2007. The strongest demand came from the major supermarket chains. The rest of the sector ranged from modest recruitment from traditional high street retailers to redundancies and at least two audit department closures. **2008 is likely to be a particularly tough year for the retail sector.**

Leisure follows the same trend as retail and much of the sector is even more dependent on discretionary consumer spending. Recruitment in the sector held up during 2007. However, **based on the redundancies that occurred in the sector during 2004/5 when growth in consumer spending fell back sharply, the outlook for 2008 does not look promising.** It is a large and diverse sector that is likely to have real pockets of weakness during the course of 2008.

### **Transport and distribution – steady recruitment**

The transportation sector has benefited from strong passenger growth. This has resulted in improved profitability and investment. The sector is not a large employer of internal auditors and many that might otherwise be considered large groups have relatively small internal audit departments. Recruitment in the sector was steady during 2007 and, unlike distribution, it is not quite so dependent on the economic cycle. With investment likely to hold up and continued pressure to expand and improve services, **the transport sector is likely to continue to recruit throughout 2008.**

The distribution sector has undergone significant consolidation in recent years, with a number of takeovers and mergers. The sector recruited steadily during 2007, but its prospects for 2008 are likely to be closely tied to developments in the retail sector. **Prospects therefore do not look encouraging.**

### **Public sector – partnering more widely used**

The large real increase in spending that the public sector has enjoyed in recent years is now coming to an end. Whilst the Gershon and Lyons reviews have come and gone, there always appears to be ongoing reforms and modernisations which tend to create uncertainty. What is clear is that partnering, co-sourcing and the use of consortium based audit resourcing are becoming more widely used.

In many parts of local government there were frustrations during 2007 at their inability to recruit. They rely heavily on traditional advertising, which in some parts of the country did not work. Many departments have relied on partnering and co-sourcing arrangements and have extensively

employed temporary internal auditors. On an ongoing basis this rarely represents good value.

Central government actively recruited during 2007, with many departments running advertising campaigns, a number driven by major restructuring exercises. Within the public sector, civil service departments remain the most popular to work for and are therefore better able to fill their vacancies. The work is perceived to be more interesting with a commitment to working with modern methodologies and technologies, and is seen to have better career prospects. There are likely to be further campaigns during 2008.

Within the NHS, most of the recruitment is now done indirectly through consortiums and external service providers. They actively recruited during 2007 and will continue to do so during 2008. A consequence of this process is that fewer internal auditors are gaining direct experience and training within the NHS. As internal auditors leave the external audit providers for the private sector, there is less scope to replace them with NHS trained staff.

The Charities and NFP sector recruited steadily during 2007. The Education and Housing sectors are now heavily dependent on consortia and external audit providers who recruited during 2007 and will continue to do so during 2008.

## **The years of significant real increases in public spending are coming to an end.**

As improvements in services must become more efficiency based, it might be that greater resources will be allocated to internal auditing. In 2008 this is possible but unlikely. The most likely outcome is that the various external audit providers that are coming to dominate public sector internal audit recruitment will, under intense competition and cost pressures, feel obliged to promise to deliver more for even less.

### **The Big 4 and other external audit providers – limited recruitment**

Internal audit recruitment, specifically amongst the Big 4, was limited during 2007. Demand was primarily for manager grade staff with financial services and banking experience. Within IT audit, candidates with project assurance and more broadly based skills in business processing, risk and control advice were sought. However, in total, there was little active recruitment.

The decline in Sarbanes-Oxley work that was particularly evident during the first half of 2007 resulted in a number of redundancies. These were not internal auditors but principally contractors who had benefited from the boom in Sarbanes-Oxley related work.

A number of the top 10 firms sought internal auditors with private sector experience, as they attempted to expand their services beyond the public sector. Candidate shortages resulted in only limited success. A major development during the year was the merger of Grant Thornton and Robson Rhodes which resulted in the formation of a sizable internal audit group.

The Big 4 were largely successful in retaining their staff during 2007 and, against expectations, there was no exodus into the recruitment market. In fact, at the end of 2007 there were tentative signs that the Big 4 were looking to undertake more general recruitment.

However, should growth in the economy in any way fall below what is currently expected, more Big 4 staff will be entering the recruitment market in 2008 than in 2007.

## 04 Salaries

### Overview

#### Salaries

Barclay Simpson analyse the salary data that accumulates from the placements we make in the UK. This provides a useful guide to the trend in salaries for internal auditors.

In the first table, base salary is the average accepted by internal auditors securing employment through Barclay Simpson. No allowance is made for any benefits other than company cars, which are valued at £5,000. The numbers are averages for the UK and reflect salaries ranging from £18,000 to in excess of £100,000.

The percentage salary increase represents the average salary increase achieved by internal auditors who have changed position and is based on the same data as base salary. The averages are weighted by the percentage increase achieved by individual internal auditors rather than total salaries. The average hides substantial variances and should not be viewed as typical.

#### Salary increases down

The average salary accepted by internal auditors during 2007 was £51,584, a 4.3% increase on 2006. This compares with an increase in average earnings of 3.9% in the wider economy and is the lowest it has been both in absolute terms and relative to average earnings for four years.

The percentage salary achieved by internal auditors changing job was 12.6%, again the lowest since 2003.

#### Banking market subdued

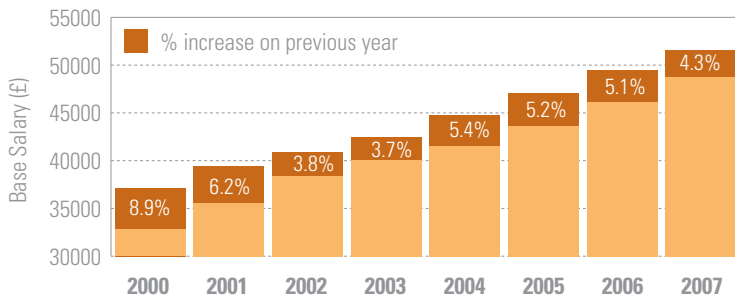
These statistics might seem surprising given how buoyant the first three quarters of 2007 were. However, during Q4, the banking sector was particularly subdued and, historically, placements in this sector have often flattered the overall average.

Anecdotally internal auditors remain in a strong bargaining position with few employers having the luxury of a choice of appropriate candidates from which to select. Against that, salary costs in the wider economy remain well controlled and, whilst surveys suggest that people have higher expectations of future inflation, it does not appear to be translating into salary demands in internal auditing.

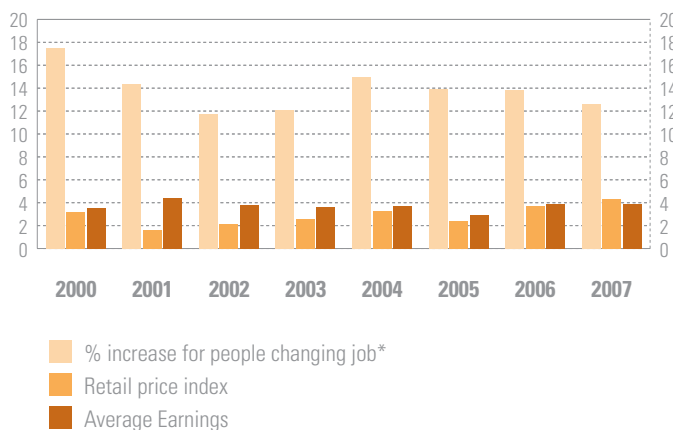
#### Increase in non-financial incentives

Companies are increasingly using non-financial incentives such as flexible / home working, additional holiday, training and career development opportunities to recruit and retain staff. Home working is more often offered to established rather than prospective staff. Given the problems of commuting and the increasing capability of remote communication, the prospect of at least limited home working will become a significant element in the overall employment packages offered to internal auditors.

#### Average salaries



#### Salary increases when changing job



\* Whilst the high percentage increase in base salary achieved by changing job might be more than expected, the increase in total package in the year immediately following a move, is significantly lower. The reason is the qualifying period in many companies to be eligible for both annual bonuses and salary reviews. Many internal auditors give up the possibility of impending bonuses and salary increases and may have to wait over a year to merit them with a new employer. We would estimate that this accounts for approximately 5% of the increase that internal auditors receive as a result of changing position.

## Salary prospects for 2008

It is clear from the tone of this report that we are expecting the internal audit recruitment market to soften in 2008 and for some sectors to experience weakness. Given that price is a function of supply and demand, we believe that the salary increases achieved by internal auditors via the recruitment market will be subdued in 2008.

## Salary survey

Our salary survey is in three parts:

1. Regional analysis with a survey covering salaries for newly and recently qualified MIAs, ACCAs and ACAs.
2. A wider perspective on the salaries paid to internal auditors who are not simply newly or recently qualified. We provide a number of different candidate profiles and the salary ranges they fall into.
3. Salaries for Chief Internal Auditors.

## 1. Regional analysis

### London

- Banking is by far the biggest employer of internal auditors in London.
- In recent years, the high salaries and benefit packages offered in banking have not only attracted large numbers of internal auditors into London, but have also distorted the recruitment market. Many non-banking internal audit departments based in London have, in salary terms, not been able to compete.
- Outside of banking, London tends to be the base for the audit departments of British commercial companies such as leisure, retail and other trading groups, and the international and UK audit departments of non-UK multinationals.
- Salaries remain higher in London, primarily to compensate people for the cost of commuting in and around London in terms of time and money.

### South East

- Outside of London, the South East has the largest and most diversified concentration of audit departments. To an extent it has benefited most from the migration away from Central London.
- The main geographic areas where internal audit departments tend to be based are the M25 corridor to the west and south of London and the M3 and M4 corridors.
- A drawback to the South East is the relative difficulty in commuting around it. Many companies are forced to pay almost as much as London salaries because the supply of staff within reasonable commuting time can be relatively low. In many respects Central London is a more logical location to base an internal audit department.

### The West

- The West in internal audit terms stretches to Gloucester and Cheltenham in the North, and Bristol and Swindon to the South.
- The higher salaries that have historically been available were due to the relatively large number of financial services organisations and the possibility of commuting into London.
- However, rationalisation in financial services has reduced the number of opportunities in the area and salary differentials between the West and the Midlands have been reduced.

### The Midlands

- Historically the most industrially biased region, the Midlands is becoming increasingly diversified.
- The greatest demand for internal auditors still comes from the many engineering and manufacturing groups that have their audit departments based in this region.
- The Midlands is, however, increasingly suffering from the same problem that afflicts the South East - commuting around it.

### North West

- Probably the most diverse area outside of London and the South East, housing a large number of insurance companies and banks, together with a relatively high number of UK and foreign manufacturing and commercial organisations.
- The North West historically has been more commercially biased than the rest of the industrialised North and as a consequence is the home of some major internal audit departments.

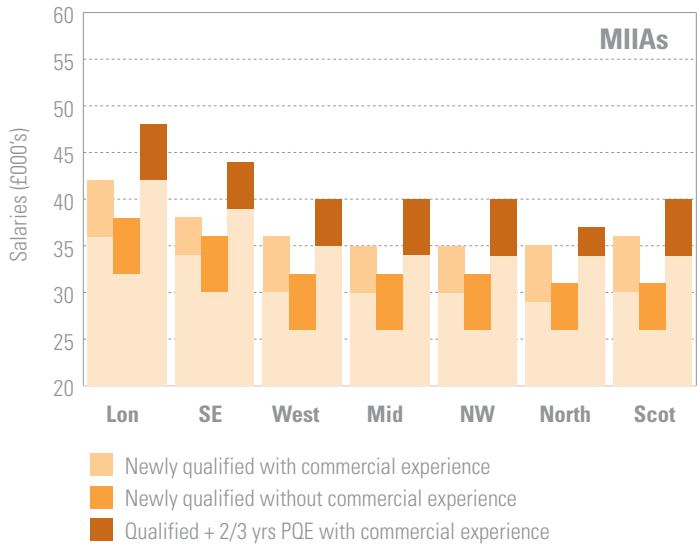
### North

- The North is split into two areas, Yorkshire and the North East.
- Neither of these areas has significant numbers of internal audit departments when compared to either the North West or Midlands.
- West Yorkshire, though, is home to a large number of financial services organisations, with Leeds in particular increasingly developing as a financial services centre.
- However, when compared to the North West, the North is a far smaller and more narrowly defined market.

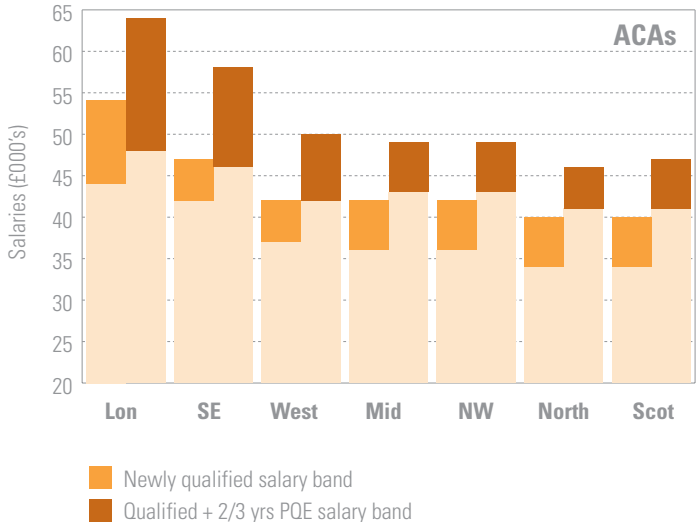
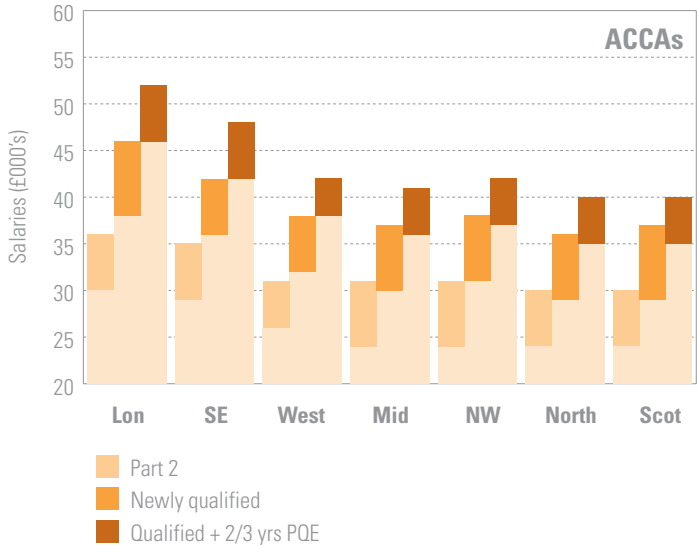
### Scotland

- Scotland is becoming an increasingly significant region for the employment of internal auditors.
- Outside of London, Edinburgh, which is also the seat of government for Scotland, has become the largest financial services centre in the UK with the consequent opportunities and salary inflation for internal auditors.
- Whilst the Strathclyde and Fife regions host a variety of companies with small teams of auditors, by far the greatest concentration of audit departments can be found in Lothian.
- Up to five years ago salaries for internal auditors in Scotland were significantly less than within the rest of the UK. This is no longer the case.

### Newly and recently qualified MIAs, ACCAs & ACAs



MIIA candidates are split between those without commercial experience; i.e. coming directly from the public sector, and those already working in the private sector.



## 2. Different levels of experience – 15 candidate profiles

To provide a wider perspective on the different types of internal auditors who may be seeking employment, this section takes 15 candidate profiles and provides an approximate salary range that they could realistically expect to achieve.

The candidate profiles are for good rather than exceptional individuals and take no account of other benefits that normally accrue to internal auditors, primarily company cars in industry and commerce, and non-contributory pensions in financial services. Nor do they take account of non-contractual bonus or profit sharing arrangements.

	London	South East	Rest of UK
<b>Auditor</b> Qualified PIIA with internal audit experience gained with an external provider of internal audit services.	£25-29,000	£23-28,000	£20-25,000
<b>Internal Auditor</b> Unqualified multi-site auditor with a high level of field audit experience.	£26-34,000	£26-34,000	£22-27,000
<b>Internal Auditor</b> Partially qualified accountant of graduate calibre, with experience in the private sector.	£29-35,000	£28-34,000	£25-31,000
<b>Senior Internal Auditor</b> MIIA qualified, with internal audit experience in the Civil Service.	£34-39,000	£32-37,000	£30-36,000
<b>Senior Internal Auditor</b> Graduate qualified CIPFA with experience gained in local government.	£38-43,000	£36-41,000	£33-39,000
<b>Internal Audit Manager</b> Unqualified multi-site audit manager with a high level of experience.	£40-45,000	£40-45,000	£28-45,000
<b>Computer Auditor</b> Qualified QiCA / CISA with 3 years computer audit experience in Big 4 risk management services.	£43-52,000	£41-48,000	£40-45,000
<b>Senior Internal Auditor</b> Qualified accountant with experience that includes some exposure to internal auditing in a Big 4 firm.	£47-52,000	£43-48,000	£37-42,000
<b>Senior Internal Auditor</b> Qualified MIIA with internal audit experience in the public sector and private sector.	£48-53,000	£45-49,000	£41-45,000
<b>Senior Internal Auditor</b> Qualified accountant, with at least 3 years internal audit experience gained in a Big 4 or commercial firm.	£50-56,000	£45-50,000	£40-46,000
<b>Internal Audit Supervisor</b> Qualified ACA with experience in either a Big 4 risk management services department or a commercial internal audit department.	£52-58,000	£50-56,000	£42-50,000

<b>Senior Computer Auditor</b> QiCA / CISA qualified, with a high level of experience in various IT positions followed by significant experience in computer auditing.	£56-64,000	£52-58,000	£47-55,000
<b>Computer Audit Supervisor / Manager</b> Qualified ACA with computer audit experience.	£60-66,000	£53-61,000	£51-57,000
<b>Computer Audit Manager</b> QiCA / CISA qualified graduate, with significant computer audit experience.	£63-75,000	£57-65,000	£53-60,000
<b>Internal Audit Manager</b> Qualified CCAB / MIIA with experience in both Big 4 risk management services and internal auditing.	£65-72,000	£60-66,000	£55-62,000

### 03 Chief Internal Auditors

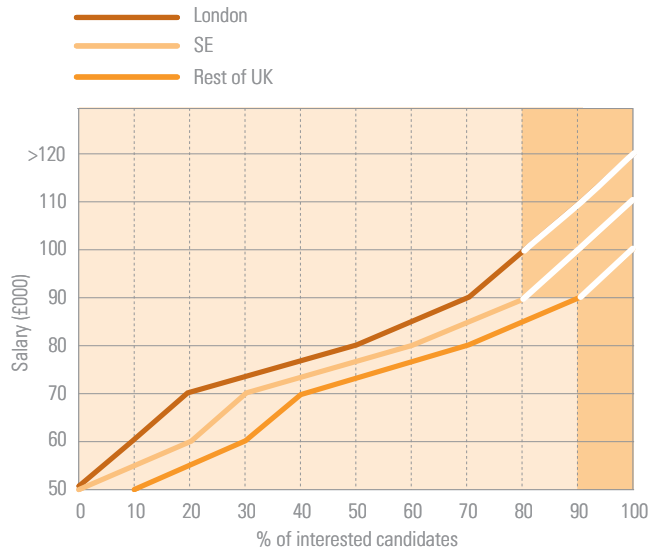
The salaries of Chief Internal Auditors are difficult to provide precise guidance on, as they vary considerably, not only between different sectors, but between similar companies in the same sector.

Consequently we have broken the data out into different sizes of company (small, medium and large) and different regions (London, the South-East and the rest of the UK) to give as good a salary indication as possible.

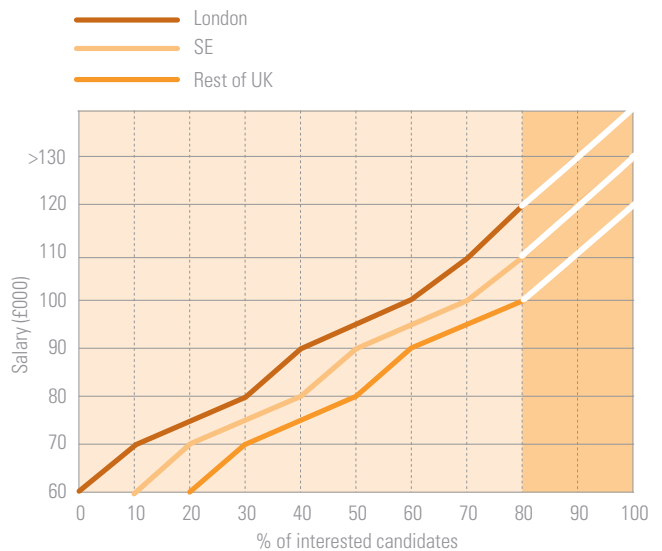
The graphs provide estimates of the proportion of internal auditors with the appropriate skills and experience, who, other things being equal, would be attracted purely on the basis of salary, not including cars, bonuses and all other benefits, which, at Chief Internal Auditor level, can be considerable. As an example, a small company in the South East, if it were to offer a salary of £90,000, could reasonably expect 80% of appropriate individuals to be interested – at £60,000 only 20%.

In our experience, if seeking to fill a role, a company should look to attract around 80% of the potential candidates and price the role accordingly.

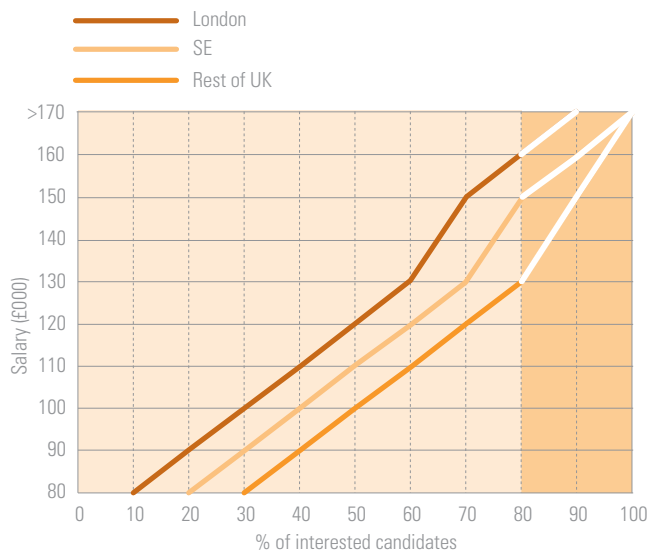
#### Small companies, i.e. Top 500 Plc or equivalent



#### Medium sized companies, i.e. Top 250 or division audit manager of Top 100 Plc or equivalent



#### Large companies, i.e. Top 100 Plc or equivalent



## 05 Outlook for 2008

At the start of 2008, there is probably more uncertainty about the prospects for the UK economy than there has been for five years. In 2003, the world was dealing with deflationary influences and the imminent prospect of war in Iraq. Now we are dealing with the prospects of falling asset prices and losses in the world's financial system that have yet to be properly identified or quantified.

**It may be that the damage is confined to the feckless areas of the financial services industry and lessons are learnt. If, however, it affects the wider economy, and recent developments in the property, leisure and retail sectors are not encouraging, then prospects for 2008 will be more problematic. The outcome is probably finely balanced.**

Structurally, and for reasons we have discussed, there is currently pressure on companies to increase the number of internal auditors they employ and they are doing so. **Recent developments in the credit markets may ultimately be interpreted as the result of too little corporate governance.** Politically in 2008 it would not be a good time to be cutting back on internal audit and related areas of governance. The question is whether cyclical pressures generated by a weakening economy are sufficiently strong to counter this.

Anyone reading this report probably has as good an insight into the future direction of the UK and world economy as we do. There is no shortage of economic forecasts.

Our experience would indicate that job prospects for internal auditors will prove to be far more closely tied to continued economic growth than many internal auditors may care to recognise.

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