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KNOWLEDGE REPORT

MEASURING INTERNAL AUDIT PERFORMANCE

September 2009

The Institute of Internal Auditors

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ABOUT THIS REPORT

As part of its services, The Institute of Internal Auditors (IIA) will publish a series of reports on topics of appeal to chief audit executives (CAEs) and other internal auditors that provide leading practices based on survey results and recommendations from audit professionals in the field.

Please note that The IIA surveys referenced in this report are not statistically based and their results are not representative of the entire population of internal auditors. Rather, they are benchmarking surveys based on the responses of CAEs and other internal audit professionals who are members of GAIN. In addition, results from these surveys are solely intended to provide information (i.e., tools, resources, and/or other knowledge) that is based on the responses of survey participants only.

EXECUTIVE SUMMARY

A point of discussion in many, if not all, senior management meetings is how best to capture and evaluate group performance. As part of the organization's senior management team, CAEs are no exception. Throughout the internal audit profession, CAEs in different organizations use a variety of performance tools and quality assurance techniques, including satisfaction surveys and benchmarking metrics. While no single tool or technique is best, it is important that CAEs and internal audit managers choose a performance management methodology that best fits their internal audit activity's and organization's needs.

This *Knowledge Report* summarizes some of the key points, recommendations, and leading practices on performance management from guidance-setting organizations and internal audit practitioners, as well as information from The IIA's GAIN Flash Surveys and Annual Benchmarking Study.

Leading Practices From IIA Members

Leading practices gathered from CAEs around the world address various aspects of the performance management process, including the selection of performance metrics, the use of internal and external quality assessments (QAs), and tips on how to use a balanced scorecard.

Selecting the Right Performance Metrics. Prior to selecting the metrics that will be used to measure internal audit performance, CAEs should:

- Perform an inventory of the metrics being used.
- Consider existing organizational performance reporting processes, stakeholder expectations, professional requirements, and the internal audit activity's maturity level.
- Review the internal audit activity's mission and vision statements.

Once these steps are performed, CAEs can select the metrics that will best capture their internal audit activity's performance based on the organization's needs. During the selection process, CAEs and audit managers should:

- Brainstorm and identify new metrics.
- Identify links between selected metrics and the department's mission and values.
- Categorize metrics into logical groups (i.e., staff development metrics, audit plan management metrics, client satisfaction and coverage metrics, and value creation metrics).
- Rank and prioritize metrics within each group.
- Select the top two or three metrics by category.
- Accumulate data from the top two or three metrics and establish a performance baseline.
- Report the data to the internal audit activity, senior management team, board, and audit committee.
- Solicit feedback from stakeholders and implement continuous improvement techniques.

Using a Balanced Scorecard. A balanced scorecard can help CAEs determine whether **an** internal audit activity is adding value to the organization and contributing to its overall performance. Before using a balanced scorecard CAEs need to:

- Identify and document balanced scorecard performance measures or categories.
- Identify objectives for each category with their respective measurement metrics.
- Ensure management, the board, and audit committee understand the entire balanced scorecard methodology.
- Obtain the audit committee's endorsement of the project to ensure its success.
- Determine if tools will be used to automate the performance management process and select the tool that best fits the internal audit activity's needs and budget.
- Use technology to ease the implementation process. Tools used by IIA members include dashboard applications, which give CAEs a better view of their internal audit activity's performance.

Internal QAs. CAEs use internal QAs to ensure the quality of internal audit services. According to the latest statistics from The IIA's Annual Benchmarking Study, 63 percent of the organizations represented in the study (288 companies from 15 industry groups) perform the internal QA on an ongoing basis compared to 37 percent that perform it on a periodic basis.

The main tool used to perform ongoing internal QAs is engagement supervision (93 percent), while the number one tool used to perform periodic internal assessments is self-assessments of the internal audit activity (78 percent). Recipients of internal QA results include the audit committee (75 percent), senior management team (64 percent), and the organization's external auditors (35 percent).

External QAs. Fifty-nine percent of the internal audit activities represented in the study have performed an external QA. Leading external QA practices identified by the Annual Benchmarking Study participants include:

- Type of external QA: 25 percent of all participants perform a self-assessment with independent validation and 75 percent perform an independent, external assessment.
- Frequency: 72 percent of all participants perform the external QA every five years as recommended by the *International Standards for the Professional Practice of Internal Auditing (Standards).*
- Key external QA elements: Elements examined during the external QA include the audit charter (97 percent), compliance with the *Standards* (96 percent), and knowledge and expertise of internal audit staff (90 percent).
- Sharing of results: The majority of respondents share the results with the audit committee (98 percent), senior management team (88 percent), and external auditors (61 percent).

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WHAT IS PERFORMANCE MANAGEMENT?

According to the U.S. Office of Personnel Management, performance management is the systematic process by which an organization involves employees as individuals and members of a group in improving business effectiveness in the accomplishment of mission and goals.[1] Employee performance management activities include:

- Planning work and setting expectations.
- Continually monitoring performance.
- Developing the organization's capacity to perform.
- Periodically rating performance in a summary fashion.
- Rewarding good performance.[2]

As evident in many organizations, performance management activities are not limited to individual employees only. The process also is used to measure an organization's or department's success rate in accomplishing strategic goals and objectives and in determining a business process' or service's effectiveness, efficiency, and quality. The Free Management Library's Web site describes a number of steps senior managers can follow prior to developing a performance management plan for their business unit, department, or process.[3] These steps include:

1. Reviewing organizational goals, which are established during the strategic planning process, to associate preferred results in terms of units of performance (i.e., quantity, quality, cost, or timeliness).
2. Specifying desired results for the domain (i.e., the business unit, department, or process).
3. Ensuring the domain's desired results directly contribute to the organization's results.
4. Weighting or prioritizing the domain's desired results. A weight is often expressed in the form of a percentage of time spent performing an activity or as a numeric ranking (e.g., ranking an activity's effectiveness from 1 to 5 using 5 as the highest ranking).
5. Identifying first-level measures to evaluate if and how well the domain's desired results are achieved.
6. Identifying more specific measures for each first-level measure if necessary.
7. Identifying standards for evaluating how well the domain's desired results are achieved.
8. Documenting a performance plan that includes desired results, measures, and standards.

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[1] U.S. Office of Personnel Management's Web Site, www.opm.gov/perform/overview.asp

[2] U.S. Office of Personnel Management's Web Site, www.opm.gov/perform/overview.asp

[3] The Free Management Library provides online resources on the topics of leadership and management as they pertain to individuals, groups, and organizations.

Besides its immediate benefits, such as determining the success rate of business initiatives and their impact on the organization's bottom line, performance management activities enable senior managers to:[4]

- Focus on results rather than behaviors and activities.
- Align organizational activities and processes to the goals of the organization.
- Cultivate a systemwide and long-term view of the organization.
- Produce meaningful measurements to help ensure equitable and fair treatment to employees based on performance.

While collecting benchmarks and other performance measures might seem easy to many CAEs, first time audit managers might have a harder time determining the right approach to use based on the size of their internal audit activity and main responsibilities within the organization. In addition, summarizing the wealth of data collected during the performance review process might seem daunting or time consuming. The following sections summarize the performance management and quality assurance and improvement efforts, recommendations, and leading practices from CAEs and other internal audit professionals who are members of GAIN.

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[4] The Free Management Library, Performance Management: Benefits and Concerns Web page, www.managementhelp.org/perf_mng/benefits.htm

MEASURING INTERNAL AUDIT PERFORMANCE

The October 2006 issue of *Internal Auditor* magazine[5] published an article that discusses different ways CAEs can go about measuring and making sense of their internal audit activity's performance reports. According to the article, a CAE at a financial services institution needed an effective methodology for reporting key performance information to audit staff, senior management, and the audit committee, as well as for implementing a formal quality assurance and improvement program within the department, which consisted of an audit manager and five staff auditors. The CAE also struggled to summarize the information in his GAIN annual internal audit benchmarking report.

Selecting the Right Performance Metrics

The CAE was given a number of recommendations by two internal audit executives that can be used by audit leaders in any industry or organization type, and regardless of audit

Steps for Selecting the Right Performance Metrics

Prior to the selection process:

1. Perform an inventory of the metrics being used and ensure they reflect industry and organizational trends as well as changes in the scope of internal audit responsibilities.
2. Consider existing organizational performance reporting processes, stakeholder expectations, professional requirements, and the internal audit staff's maturity level.
3. Review the internal audit activity's mission and vision statements.

During the selection process:

1. Brainstorm and identify new metrics.
2. Identify links between selected metrics and the department's mission and values.
3. Categorize metrics into logical groups (i.e., staff development metrics, audit plan management metrics, client satisfaction and coverage metrics, and value creation metrics).
4. Rank and prioritize metrics within each group.
5. Select the top two or three metrics by category.
6. Accumulate data from the top two or three metrics and establish a performance baseline.
7. Report the data to the internal audit activity, senior management team, and board and audit committee.
8. Solicit feedback from stakeholders and implement continuous improvement techniques.

staff size. A key recommendation provided pertains to what to do prior to developing, measuring, and reporting on performance metrics. As the article explains, performance metrics or benchmarks need to reflect any changes in the industry, organization, and the scope of the internal audit activity's responsibilities. As a result, CAEs might need to update the metrics being used to measure internal audit performance.

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[5] *Internal Auditor* (October 2006), Ask the Experts: "Collecting Performance Data," http://theiia.texterity.com/ia/200610/

Besides updating performance metrics, the article recommends that CAEs consider:

- **Existing performance reporting processes.** Choosing an existing performance reporting process (e.g., one used by other business units) can help bridge the gap that sometimes develops between management and internal audit groups by using a proven venue to explain metrics to management and the board.
- **Stakeholder expectations.** CAEs should interview members of the board and management team to clarify desired internal audit outcomes and market the audit department's added value to the organization.
- **Professional requirements.** Understanding different professional requirements can help CAEs support the selection of performance metrics. These include, but are not limited to, the professional requirements listed in the *International Standards for the Professional Practice of Internal Auditing* (*Standards*).[6]
- **Staff and department maturity level.** Involving staff in the benchmarking process can help ensure their buy-in and provide professional development opportunities. In terms of staff, CAEs need to consider the size of the department and how long the department has been in existence as some of the metrics that are appropriate for large departments might be inappropriate for a small department. Also, the maturity level of the internal audit activity is important in considering what metrics to measure.

Once CAEs understand the different performance reporting options available to them, their stakeholder expectations, professional requirements, and staff and departmental resources, they can select the right performance metrics for their internal audit activity by following a series of steps. These include:

1. Brainstorming and identifying new metrics.
2. Identifying links between selected metrics and the internal audit activity's mission and values.
3. Categorizing metrics into logical groups.
4. Ranking and prioritizing metrics within each group.
5. Selecting the top two or three metrics by category.
6. Accumulating data from the top two or three metrics and establishing a performance baseline.
7. Reporting the data to the internal audit activity, senior management team, and audit committee.
8. Soliciting feedback from stakeholders and implementing continuous improvement techniques.

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[6] For a complete list of *Standards* and Practice Advisories related to performance management visit The IIA's Web site, www.theiia.org/guidance/standards-and-guidance/ippf/standards/.

While brainstorming and identifying the metrics that will be incorporated into the internal audit activity's performance management plan, CAEs can refer to those outlined in The GAIN Annual Benchmarking Study[7] for additional guidance. These metrics can enable CAEs to understand what similar organizations are doing to measure internal audit performance and provide a basis to report the internal audit activity's accomplishments to senior management and audit committee.

Depending on the performance metrics chosen, CAEs might categorize each into one of four main categories. These are:

- **Staff development metrics** (e.g., number of staff credentials compared to similar organizations and staffing activity, such as promotions, auditor rotation into management positions, transfers to other departments, number of staff brought into the internal audit activity from other business units, and terminations).
- **Audit plan management metrics** (e.g., audit deliverables by month, audit reports per full-time equivalent, number of completed projects and reports issued, time use by individual staff members and type of activity, corrective action status to identify past due corrective actions, cycle times for the audit and reporting process, and planned versus actual hours worked by audit project).
- **Client satisfaction and coverage metrics** (e.g., quantification of post-audit client satisfaction scores and audit resources by area and topic).
- **Value creation metrics** (e.g., quantifiable audit results and number of audits requested by management).

Data on these metrics should be reported periodically to senior management and the audit committee. Although performance status reports must be provided annually at a minimum, it is best to consult with the audit committee and senior management team regarding the appropriate or preferred distribution frequency.

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[7] For information on the Annual Benchmarking Study, visit www.theiia.org/guidance/benchmarking/gain/.

BALANCED SCORECARD APPROACH TO PERFORMANCE MANAGEMENT

A common tool used by many CAEs to measure internal audit performance is a balanced scorecard. Developed by Robert Kaplan and David Norton, a balanced scorecard is an approach to corporate performance measurement that is designed to identify success by breaking down the overall vision and strategy of an organization into specific objectives, targets, measures, and initiatives.[8] Many CAEs have adapted this approach to their internal audit activities, considering its use a leading practice.

Using a balanced scorecard to measure performance can answer the following questions about an internal audit activity:

- Is it adding value?
- Is it contributing to the organization's overall performance?
- Is it achieving its vision, mission, and overall objectives?

Steps to Using a Balanced Scorecard

A balanced scorecard can help CAEs determine whether an internal audit activity is adding value to the organization and contributing to its overall performance. Before using a balanced scorecard CAEs need to:

1. Identify and document balanced scorecard performance measures or categories.
   a. Keep categories simple.
   b. Involve all stakeholders in the categorization process.
2. Identify key objectives for each category with their respective measurement metrics.
   a. Limit the number of metrics used to keep the process efficient.
   b. Determine what metrics the audit committee, board, and management are interested in.
   c. Ensure metrics relate directly to the goals of the internal audit activity.
3. Obtain the audit committee's endorsement of the project to ensure its success.
4. Ensure management, the board, and audit committee understand the entire balanced scorecard methodology.
5. Use technology to ease the implementation process. Tools used by IIA members include dashboard applications that give CAEs a better view of their internal audit activity's performance.

While it is up to each organization to determine whether the benefits associated with using a balanced scorecard outweigh its costs, some of the benefits of using this performance management approach include:

- Aligning an internal audit activity's strategy, operations, and stakeholder needs.
- Providing a comprehensive snapshot of performance.
- Allowing benchmarking against other peers.
- Improving the bottom line through cost recoveries and process efficiencies.

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[8] GAIN Benchmarking Compilation, *Balanced Scorecard Approach to Internal Auditing* (Sept. 10, 2007), www.theiia.org/download.cfm?file=3974

Four main categories are typically used to identify balanced scorecard performance measures: financial, customer, internal business process, and learning and growth. However, these categories might vary based on the organization and the key factors to be measured. According to a 2007 GAIN Benchmarking Compilation of balanced scorecard approaches to internal auditing from 50 CAEs, some of the key categories used when adapting this methodology to an internal audit activity have included:

- Stakeholders.
- Employee satisfaction.
- Audit planning.
- Added value.
- Operations.
- Execution of audit plan.
- Audit process.
- Quality.
- Service and effectiveness.
- Risk coverage.

Once the main categories are documented, key objectives need to be identified for each category with their measurement metrics. Metrics used by CAEs have included cost recovery data; external auditor, customer, stakeholder, and employee satisfaction survey information; and retention/turnover of audit staff rates.

Tips for Implementation

When implementing a balanced scorecard for their internal audit activity, CAEs should keep in mind the following tips:

- Keep it simple.
- Limit the number of metrics used to keep the process efficient.
- Determine what metrics the audit committee, board, and management are most interested in.
- Ensure metrics relate directly to the goals of the internal audit activity.
- Involve all stakeholders in the categorization process.
- The CEO or audit committee must endorse the project for it to be successful.
- Ensure management, the board, and audit committee understand the entire balanced scorecard methodology.

Many CAEs employ different technology tools to assist in the implementation process. The overall consensus among CAEs who provided information for the GAIN Benchmarking Compilation is that no tool is particularly better than another; it is just a matter of finding the right tool given the organization's needs and financial resources. Tools listed include:

- Microsoft's Balanced Scorecard Manager.
- Cognos.
- Microsoft Excel.
- Performancesoft Views.

- ActiveStrategy Enterprise Software.
- Business Objects' Enterprise Performance Management.
- Hyperion's Performance Scorecard.
- SAP's Strategic Enterprise Management.

Besides using a tool to help in the balanced scorecard's implementation process, CAEs need to ensure the technology used is reviewed for its effectiveness and accuracy in providing performance data. For instance, a June 2005 article published in *Internal Auditor* magazine[9] describes how to review the dashboard's architecture and security controls to ensure control strength.

According to the article, a good starting point for auditing the dashboard application and balanced scorecard is to review the reporting system's architecture and security. Application security reviews should start with management's security policy and its realization in the software application. The review should determine the structure and level of refinement of the system, as well as ongoing or current plans for modification and refinement. During the review, dashboard users should be interviewed to identify potential concerns and confirm that the basic functions of the system are working.

Next, auditors need to evaluate the dashboard's contents (i.e., the metrics or indicators that form part of the balanced scorecard system) and the application's accuracy in reporting the data. Doing so can reveal potential issues, such as misrepresentation of the underlying process, manipulation of indicators, and failure to achieve desired outcomes. A balanced scorecard application typically includes metrics on:

- Sales performance and customer satisfaction.
- Cost-of-goods-sold efficiency and finished goods quality.
- Procurement and logistics effectiveness.
- General and administrative expenses.
- Employee morale and development.
- Environmental and community impact.

Finally, CAEs need to consider the integration of process controls into the dashboard to strengthen the application, unintended negative behaviors due to the use of a particular dashboard metric and indicator, and the application's use as part of the audit risk assessment and continuous monitoring process.

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[9] *Internal Auditor* (June 2005)*,* Computers and Auditing (now Tech Forum): "The Driver's View," http://theiia.texterity.com/ia/200506

QUALITY AND IMPROVEMENT AS A PART OF AUDIT PERFORMANCE

To ensure consistent quality in the services provided by their internal audit activity, CAEs need to establish a quality assurance and improvement program that consists of ongoing and periodic internal QAs, external QAs, internal monitoring, and assurance that the internal audit activity is conforming with the definition of internal auditing, the *Standards,* and Code of Ethics. While the internal QA program should include ongoing monitoring through the use of metrics and periodic assessments of conformance with the *Standards* (refer to table 1 for a list of IIA Standards pertaining to quality assurance)*,* the external QA should be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization.

Table 1: IIA Standards on Quality Assurance and Improvement

IIA Standard	Description
IIA Standard 1300: Quality Assurance and Improvement Program	The CAE should develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity and continuously monitors its effectiveness. This program includes periodic internal and external QAs and ongoing internal monitoring. Each part of the program should be designed to help the internal audit activity add value and improve the organization's operations and to provide assurance that the internal audit activity is in conformity with the *Standards* and the Code of Ethics.
IIA Standard 1310: Requirements of the Quality Assurance and Improvement Program	The quality assurance and improvement program must include both internal and external assessments.
IIA Standard 1311: Internal Assessments	Internal assessments must include: • Ongoing monitoring of the internal audit activity's performance. • Periodic reviews performed through self-assessments or by other persons within the organization with sufficient knowledge of internal audit practices.
IIA Standard 1312: External Assessments	External assessments must be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization. The CAE must discuss with the board: • The need for more frequent external assessments. • The qualifications and independence of the external reviewer or review team, including any potential conflict of interest.
IIA Standard 1320: Reporting on the Quality Assurance and Improvement Program	The CAE must communicate the results of the quality assurance and improvement program to senior management and the board.

Additional recommendations for measuring quality assurance and identifying improvement areas are outlined in The IIA's *The Internal Audit Activity: Current Trends, Issues, and Practices*. The report provides recommendations from audit professionals in eight difficulty areas identified in external QAs performed by The IIA and provides supporting data from The GAIN Annual Benchmarking Study. According to the report, the number one method for measuring an internal audit activity's quality assurance and identifying audit improvement areas is the use of an internal QA.[10]

Tools or methods cited in the report to collect internal QA information include:

1. Using satisfaction surveys at the end of each audit.
2. Using an engagement letter that compiles information from each auditee.
3. Talking to auditees and senior managers directly during the year to obtain feedback on audit performance.
4. Reviewing a sample of workpapers from each auditor every quarter with the help of senior managers outside the internal audit activity.
5. Obtaining metrics from similar internal audit activities and comparing these benchmarks with their own internal audit activity's performance.
6. Using automated audit tools to obtain information on key performance metrics, such as budgeted versus actual audit time, the internal audit's life cycle, and automated distribution of online survey links to auditees.

Two other studies also describe the different practices in the area of quality assurance and improvement program activities from audit practitioners around the world. According to The IIA Research Foundation's 2006 Common Body of Knowledge report,[11] respondents listed engagement supervision (43 percent), checklists/manuals to provide assurance that proper audit processes are followed (41 percent), and feedback from audit customers at the end of an audit (39 percent) as the top three practices performed as part of their internal audit quality assurance and improvement program.[12] Other practices performed include:

- Ensuring internal auditors are in compliance with The IIA's Code of Ethics (31 percent).
- Performing reviews by other members of the internal audit activity (30 percent).
- Verifying that the internal audit activity complies with the *Standards* (28 percent).
- Conducting reviews by an external party (20 percent).
- Complying with non-IIA standards or codes (19 percent).

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[10] Sixty-nine percent of Annual Benchmarking Study participants (288 CAEs) have a formal quality assurance and improvement program. Data was collected from Jan. 1, 2008 to June 30, 2009.

[11] *A Global Summary of the Common Body of Knowledge 2006*, www.theiia.org/research/common-body-of-knowledge/

[12] A total of 9,366 internal auditors of all organizational levels from 91 countries participated in the 2006 CBOK study.

The second study is a GAIN Flash Survey of 145 CAEs and other audit managers conducted in November 2008 on performance monitoring and quality assurance program activities.[13] Of all the respondents, 77 percent have a formal or informal performance monitoring and quality assurance program. The top five tools used by survey participants are (refer to figure 1 for a detailed list of all responses):

- Compliance with the audit plan (i.e., number of audits planned versus executed; 93 percent).
- Compliance with a budget (81 percent).
- Satisfaction surveys from auditees (77 percent).
- Audit time management (i.e., planned versus actual planning, fieldwork, and report writing; 59 percent).
- Reporting time management (i.e., planned versus actual reporting time; 59 percent).

As evident by the different activities described in each report, performance management and quality assurance practices vary somewhat in their importance, although the key elements remain the same (i.e., use of satisfaction surveys at the end of each audit engagement, planned versus actual audits completed, and conformance with The IIA's *Standards* and Code of Ethics). However, a more definitive answer can be found in the GAIN Annual Benchmarking Study, which summarizes the responses through different filters, including company type. Leading practices obtained from the Study will be discussed later in this report.

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[13] "Performance Monitoring/Quality Assurance Programs in the Internal Audit Activity" (Nov. 2008), www.theiia.org/download.cfm?file=82004; a total of 145 CAEs responded to the initial survey request out of which 112 were eligible to participate. Those of were ineligible to participate worked in internal audit activities lacking either a formal or informal performance monitoring/quality assurance program.

Figure 1: Tools Used to Monitor Performance and Assurance Quality[14]

Response	Chart	Frequency
Compliance with a budget		81.4%
Compliance with the audit plan (number of audits planned vs. executed)		**92.9%**
Audit time management: planning, field-work, closing (plan vs. real)		59.3%
Reporting time management (plan vs. real)		59.3%
Efficiency in the use of resources (e.g. tests per day, man-days per audit, etc)		15.9%
Number of recommendations offered		16.8%
Number (or percent) of recommendations implemented		32.7%
Number of key findings detected		10.6%
Cost recovery (audit savings)		14.2%
Auditor training metrics		53.1%
Satisfaction surveys from auditees		77.0%
Satisfaction surveys from audit committee		14.2%
Audit complaint records		8.8%
Number of management requests		26.5%
Role of internal auditing viewed by the audit committee		36.3%
Role of internal auditing viewed by the auditee		16.8%
Travel time		9.7%
Balanced scorecard		20.4%
GAIN's top performance measures		10.6%
Identification of best practices		22.1%

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[14] Percentages are based on the responses of 112 participants who stated their internal audit activity has a formal (41 percent) or informal (37 percent) performance monitoring and quality assurance program.

LEADING PRACTICES FROM IIA MEMBERS

The GAIN Annual Benchmarking Study enables CAEs to measure their internal audit activity's performance easily and transparently by letting them compare their audit department's performance against similar organizations and peer groups. The information discussed in this section is a summary of data collected from the Annual Benchmarking Study from Jan. 1, 2007 to June 30, 2009 from 288 CAEs. Study participants represent a total of 15 industries, including finance/banking/insurance, manufacturing, services, government, utilities, and wholesale.

Leading Internal QA Practices

CAEs use internal QAs to ensure the quality of internal audit services. According to the latest statistics from The IIA's Annual Benchmarking Study, 63 percent of the organizations represented in the study (288 companies from 15 industry groups) perform the internal QA on an ongoing basis compared to 37 percent that perform it on a periodic basis.

The main tool used to perform ongoing internal QAs is engagement supervision (93 percent), while the number one tool used to perform periodic internal assessments includes self-assessments of the internal audit activity (78 percent).

Recipients of internal QA results include the audit committee (75 percent), senior management team (64 percent), and the organization's external auditors (35 percent).

Performance management information compiled from CAEs includes internal and external QA practices and performance measures. Following is a summary of all three.

Internal QAs

According to the latest Annual Benchmarking Study data, 69 percent of the organizations represented in the study have a formal quality assurance and improvement program. When broken down by organization type, percentages increase to 80 percent in nonprofit organizations and 70 percent in public companies but decrease to 67 percent in private companies. In terms of their frequency, 63 percent of internal audit activities perform the internal QA on an ongoing basis compared to 37 percent who perform it on a periodic basis. Figure 2 provides a breakdown by company type.

Figure 2: Performance of Internal QAs

	Ongoing Reviews	Periodic Reviews
Private	62%	38%
Public	61%	39%
Non-Profit Organizations	56%	44%
Universe	63%	37%

Tools used to perform the internal QA differ based on its frequency (i.e., ongoing or periodic) and by company type. For instance, the top three tools used to perform ongoing internal QAs are engagement supervision (93 percent), audit plan completion and summary reports (89 percent), and feedback from auditees (86 percent). On the other hand, the top three tools used to perform periodic internal assessments include self-assessments of the internal audit activity (78 percent), benchmarking against peers (66 percent), and in-depth interviews with stakeholders (39 percent). Figures 3 and 4 provide a detailed summary of these results by company type.

Figure 3: Tools Used for Ongoing Internal QAs

	Engagement supervision	Checklists	Feedback	Project budgets	Timekeeping systems	Audit plan completion and summary reports	Cost recoveries	Other performance metrics
Private	85%	76%	80%	55%	69%	89%	9%	42%
Public	95%	83%	88%	65%	73%	91%	14%	59%
Non-Profit Organizations	100%	100%	100%	100%	89%	89%		44%
Universe	93%	81%	86%	65%	73%	89%	14%	54%

Figure 4: Tools Used for Periodic Internal QAs

	In-depth interviews	Self-assessment	Certified Internal Auditors	Combination of self-assessment and preparation	Benchmarking
Private	40%	69%	11%	27%	64%
Public	36%	78%	10%	26%	74%
Non-Profit Organizations	33%	89%	11%	56%	78%
Universe	39%	78%	11%	27%	66%

Participants also identified the recipients of internal QA results. The audit committee (75 percent) followed by senior management (64 percent) and the organization's external auditors (35 percent) were identified as the top three recipients of internal QA results. Other recipients identified include other appropriate stakeholders (20 percent) and the organization's board of directors (18 percent). Only 13 percent of all participants stated they do not share the results with anyone.

External QAs

Another way to obtain performance management information is through the completion of an external QA. According to Annual Benchmarking Study data, 59 percent of the internal audit activities complete an external QA. This number increases to 70 percent in nonprofit organizations and remains pretty constant in the other two categories — 57 percent and 60 percent in private and public companies, respectively.

Types of external quality assessments include a self-assessment with independent validation (25 percent of all respondents) and an independent and external assessment (75 percent of all respondents). These percentages remain pretty constant in public and private companies but differ significantly in nonprofit organizations: 57 percent of nonprofit organizations perform a self-assessment with independent validation while 43 percent perform an independent and external assessment.

In terms of frequency, 72 percent of CAEs perform an external QA every five years while nearly 30 percent perform them more frequently: every 3–4 years (24 percent) and every 1–2 years (2 percent). These percentages differ somewhat in nonprofit organizations, where 86 percent perform an external QA every five years.

Key elements examined during the external QA according to all participants include:

- The internal audit activity's charter (97 percent).
- Conformance with The IIA's *Standards* (96 percent).
- The mix of knowledge and expertise in internal audit staff (90 percent).
- Tools and techniques employed by internal auditors (89 percent).
- Management expectations (87 percent).
- The internal audit activity's added value (79 percent).
- The audit integration with the governance process (69 percent).
- Compliance with legislation and regulations (54 percent).

In addition, external QA results are shared with the audit committee (98 percent), senior management team (88 percent), external auditors (61 percent), the board of directors (37 percent), and other stakeholders (28 percent).

Leading External QA Practices

According to the latest Annual Benchmarking Study findings, 59 percent of the internal audit activities represented in the study perform an external QA. Key external QA practices include:

- **Type of External QA.** 25 percent of all participants perform a self-assessment with independent validation and 75 percent perform an independent, external assessment.
- **Frequency.** 72 percent of all participants perform the external QA every five years as recommended by the *Standards.*
- **Key Elements Included.** Elements examined during the external QA include the audit charter (97 percent), compliance with the *Standards* (96 percent), and the mix of knowledge and expertise of internal audit staff (90 percent).
- **Sharing of Results.** The majority of respondents share the results with the audit committee (98 percent), senior management team (88 percent), and external auditors (61 percent).

Performance Measures

Finally, the Annual Benchmarking Study asks participants to identify the main categories used to measure internal audit activity performance. These are stakeholder satisfaction, internal audit processes, and innovation and capability. Overall, 66 percent of all CAEs stated they measure stakeholder satisfaction, 76 percent measure the quality, effectiveness, and efficiency of internal audit processes, and 46 percent measure innovation and capability. Although these numbers remain somewhat constant in private and public companies, they change considerably in nonprofit organizations. For instance:

> **Leading Performance Measures**
>
> The Annual Benchmarking Study asks participants to identify the main categories used to measure internal audit performance. The categories are stakeholder satisfaction, internal audit processes, and innovation and capability. Performance measures are defined mainly by the CAE (88 percent), internal audit management (63 percent), and audit committee or equivalent (39 percent).
>
> The main tools or techniques used to obtain stakeholder satisfaction, internal audit process, and innovation and capability information include:
>
> - **Stakeholder satisfaction.** Surveys/questionnaires, interviews/stakeholder meetings, and key performance indicators.
> - **Internal audit processes.** Presence of audit plans for each engagement, performance of audits in accordance to established methodologies and practices, and feedback from key stakeholders.
> - **Innovation and capability.** Presence of audit training, number of staff certifications, and achievement of goals and objectives.

- 50 percent of CAEs working in nonprofit organizations measure stakeholder satisfaction compared to 66 percent and 64 percent in private and public companies, respectively.
- 80 percent of CAEs working in nonprofit organizations measure internal audit process quality, effectiveness, and efficiency compared to 73 percent and 76 percent in private and public companies, respectively.
- 60 percent of CAEs working in nonprofit organizations measure innovation and capability compared to 40 percent and 47 percent in private and public companies, respectively.

Performance measures are defined by the CAE (88 percent), internal audit management (63 percent), and audit committee or equivalent (39 percent). Other parties identified include the chief financial officer (18 percent), chief executive officer (16 percent), executive management (11 percent), and board of directors or equivalent (2 percent).

In addition, study participants also were asked if they use customer satisfaction surveys and their overall response rate. Most CAEs stated they perform customer satisfaction surveys (54 percent) after each audit engagement, 18 percent do not perform them after each engagement, and 27 percent do not use them at all. CAEs who use customer satisfaction surveys stated they have a response rate of 71 percent. However, this percentage decreases significantly in nonprofit organizations to 44 percent.

Participants also were asked to identify the methods used to measure stakeholder satisfaction, internal audit processes, and innovation capability. Figures 5–7 summarize the responses of CAEs based on company type, and figure 8 describes other performance measures used, including time to issue reports after fieldwork, plan completion statistics, and audit duration.

Figure 5: Methods Used to Measure Stakeholder Satisfaction

	Interviews / Stakeholder meetings	Facilitated sessions	Surveys / Questionnaires	Performance metrics / Key performance indicators	Providing savings or cost avoidance statistics	Other
Private	65%		67%	41%	6%	7%
Public	69%	5%	81%	53%	14%	7%
Non-Profit Organizations	78%		78%	33%		11%
Universe	67%	3%	78%	45%	9%	8%

Figure 6: Methods Used to Measure Internal Audit Processes

	Feedback is obtained from key stakeholders on whether or not the audit activity has effectively addressed risk concerns	Audit activity assesses the extent that key risk areas are being addressed	Appropriate audit plans are established for each engagement including scope, objectives, timing, and resource allocation	Audits are performed in accordance with established audit methodologies and working practices	Feedback is obtained from key stakeholders on the quality, level of detail, and frequency of audit communications	Internal audit activity measures the degree that key recommendations are implemented	The internal audit activity identifies and monitors performance metrics and key performance indicators
Private	73%	73%	86%	80%	64%	63%	55%
Public	78%	73%	93%	94%	73%	78%	67%
Non-Profit Organizations	78%	78%	89%	89%	56%	78%	56%
Universe	75%	71%	91%	90%	69%	74%	63%

Figure 7: Methods Used to Measure Internal Audit Capability and Innovation

	Measurements are in place to ensure that audit staff receives sufficient training	Audit staff satisfaction with training is measured	The number of staff certifications is measured	Goals have been established for staff training in the use of technology	Goals have been established for using technology to effectively support audit testing and analysis	Measures are in place to ensure that staff has sufficient knowledge of industry, business, operations, key functions	Measures are in place to ensure goals and objectives are achieved	Identification and monitoring of performance metrics and key performance indicators	Measures are in place to benchmark our internal audit activity to leading practices	Overall time percentage allocation (budget vs. actual)
Private	71%	47%	75%	35%	31%	59%	78%	63%	57%	35%
Public	84%	41%	81%	42%	49%	62%	82%	70%	65%	33%
Non-Profit Organizations	89%	56%	67%	11%	22%	56%	67%	22%	56%	22%
Universe	83%	42%	79%	35%	41%	59%	78%	66%	58%	29%

Figure 8: Other Performance Measures Used

	Plan completion statistics	Audit duration (calendar / work days)	Time to issue reports after fieldwork	Number of management requests received / accomplished	Compliance with COSO objectives	Average audits / auditor budget vs. actual	Number of recommendations offered	Percent of recommendations implemented	Percent of recommendations implemented by commitment date
Private	81%	61%	54%	28%	7%	54%	25%	39%	28%
Public	81%	69%	72%	40%	16%	49%	30%	37%	35%
Non-Profit Organizations	90%	70%	40%	30%	10%	60%	30%	30%	30%
Universe	80%	66%	65%	39%	13%	52%	31%	41%	33%

FINAL THOUGHTS

Measuring audit performance is a part of most, if not all, internal audit activities worldwide. Part of these performance management efforts is the implementation of metrics to ensure the quality of audit services and address gaps, as evidenced by the presence of internal and external QAs among IIA members.

While the particular metrics used to measure internal audit performance vary somewhat depending on the organization, different IIA surveys including the GAIN Annual Benchmarking Study have identified the use of stakeholder or customer satisfaction surveys, planned versus actual audits completed, and conformance with the definition of internal auditing, the *Standards*, and Code of Ethics as key metrics to measure performance. The use of a balanced scorecard was another leading practice identified by CAEs who are members of GAIN.

However, regardless of the tools and techniques used to measure internal audit performance, CAEs need to choose the performance management methodology that best fits the scope of audit work. In addition, CAEs need to consider the needs of different stakeholders, including the audit committee and senior management team, prior to selecting a particular performance management metric. Doing so will not only enable CAEs to measure internal audit performance effectively, but also ensure audit efforts are properly aligned with strategic goals and add value to the organization.

RESOURCES

For additional information on performance management and how to measure internal audit performance, CAEs and internal auditors can visit the following Web sites:

Balanced Scorecard

- GAIN Benchmarking Compilation, *Balanced Scorecard Approach to Internal Auditing* (Sept. 10, 2007), www.theiia.org/download.cfm?file=3974.
- KPMG's *Building a Success Model for Internal Audit: The Balanced Scorecard*, www.kpmg.com.sg/publications/ras_BuildingASuccess.pdf.

IIA Flash Surveys

- "Quality Assurance Improvement Programs"(January 2009), www.theiia.org/download.cfm?file=15227.
- "Performance Monitoring and QAIP" (November 2008), www.theiia.org/download.cfm?file=82004.
- "Ensuring Quality Assurance within the Internal Audit Activity" (October 2008) www.theiia.org/download.cfm?file=42443.
- "Internal Audit's Use of Surveys" (May 2008) www.theiia.org/download.cfm?file=66934.
- "Internal Quality Assurance Processes" (February 2008) www.theiia.org/download.cfm?file=16702.

IIA Guidance and Other Information

- *Internal Auditor* magazine:
  - o Ask the Experts: "Collecting Performance Data" (October 2006), http://theiia.texterity.com/ia/200610/.
  - o Computers and Auditing (now Tech Forum): "The Driver's View" (June 2005), http://theiia.texterity.com/ia/200506.
- The IIA's *International Standards for the Professional Practice of Internal Auditing,* www.theiia.org/guidance/standards-and-guidance/ippf/standards/full-standards/.
- The IIA's *Quality Assessment Manual for the Internal Audit Activity,* www.theiia.org/guidance/quality/qa-manual-6th-edition/.
- The IIA's Quality Web page, www.theiia.org/guidance/quality/.

Performance Metrics and Management

- U.S. Office of Personnel Management Web site, www.opm.gov/perform/overview.asp.
- Free Management Library Web site, http://managementhelp.org/perf_mng/perf_mng.htm.
- Rutgers University, National Center for Public Productivity, Performance Measure Resources Web page, http://andromeda.rutgers.edu/~ncpp/cdgp/manualref.htm.
- The University of California, Berkeley, Guide to Managing Human Resources Web site, http://hrweb.berkeley.edu/GUIDE/performance.htm.
- About.com's Performance Management Process Checklist, http://humanresources.about.com/od/performancemanagement/a/perfmgmt.htm.