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## Internal Audit Key Performance Indicators

Internal audit activity has an important role to play within public sector organizations and is a core element of good governance. By providing risk-based and objective assurance, advice and insight to management they enhance and protect the organizational value, hence management is increasingly interested that the internal audit function is operating with sufficient quality, effectiveness and efficiency, and demonstrate value to the organization. This publication provides further insight on performance measurement in the internal audit context and offers examples of performance measures that can be useful for internal audit teams and the regulators.

### Why should the internal audit activity focus on, and measure its performance?

The International Standards for the Professional Practice of Internal Auditing (ISPPA) require that an ongoing monitoring of the performance is included during internal assessments as an integral part of the day-to-day supervision, review, and measurement of the internal audit activity.

In order to comply with the requirements of the Standards, it is therefore important that audit teams demonstrate a commitment to use of proper performance indicators to measure, report on, and enhance performance.

### What are the benefits of performance measurement?

There are many benefits of performance measurement for the internal audit activity, including:

- Providing objective data for improvement through self-evaluation and/or benchmarking;
- Increasing the effectiveness and efficiency of their work;
- Demonstrating the value internal audit brings to an organization and its management;
- Helps gain credibility, objectivity and accountability of the internal audit function.

# What do the Standards Require?

Standard 1300 – Quality Assurance and Improvement Program, requires from the chief audit executive to develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity, assesses the efficiency and effectiveness of the internal audit activity with a view for improvement and includes both internal and external assessments:

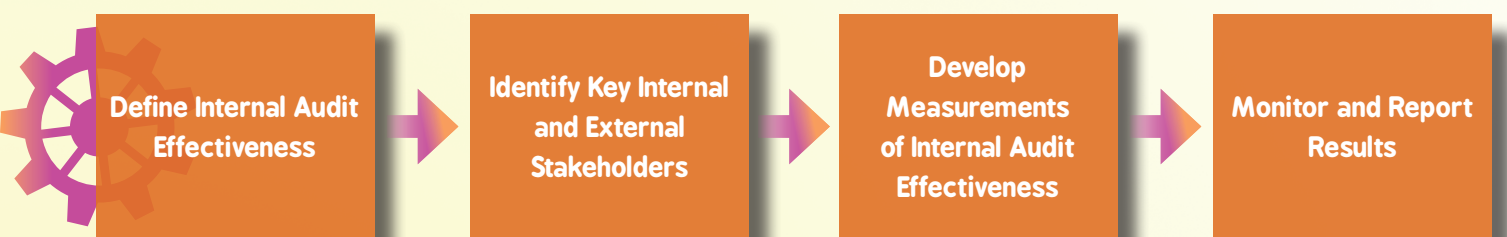
- **Internal Assessments:** Attribute standard 1311 requires that internal assessments should include an (i) ongoing monitoring of the performance of the internal audit activity which is part of the day-to-day supervision, review and measurement of the internal audit activity; and (ii) a periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices.
- **External Assessments:** Standard 1312 requires external assessments of the internal audit activity to be conducted at least once every five years by a qualified independent assessor and these can be in the form of a full external assessment, or a self-assessment with independent external validation.

The chief audit executive is required to communicate the results of the quality assurance and improvement program to senior management and the board, including any nonconformance of the internal audit activity with the standards and other requirements.

Performance Standard 2060: The chief audit executive must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan and on its conformance with the Code of Ethics and the Standards.

# What guidance is available for internal audit teams?

In December 2010, the Institute of Internal Auditors published its Practice Guide on "Measuring Internal Audit Effectiveness and Efficiency" which highlights the importance of establishing performance measures sufficient to determine if internal audit is meeting its goals. The guide emphasizes the need for the internal audit function to effectively demonstrate value to an organization and for it to lead from the front by establishing robust performance measures related to its function. The guide outlines an illustrative high-level four step process in this regard:



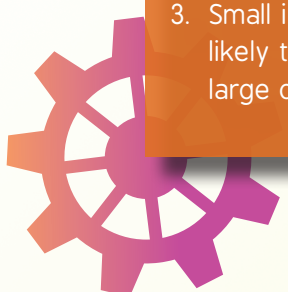
It also highlights that it is imperative that performance measures include both quantitative and qualitative criteria. Quantitative criteria include those based upon existing data which is understandable. Examples include actual versus planned costs, training hours per auditor, percentage of audits completed versus audits planned, etc. Qualitative data is usually obtained through additional information collection methods such as surveys, questionnaires or interviews. Qualitative metrics may include measures like staff member satisfaction, head of budget organization or audit committee feedback, etc. The Guide recommends a balanced scorecard approach to performance measurement and provides illustrative examples of metrics related to internal audit *effectiveness* and *efficiency* along categories like:

- |  |                         |
|--|-------------------------|
| • Basic measures   | • Technical development |
| • Service to stakeholders                                | • Innovation            |
| • Knowledge of budget organization and the public sector | • People development    |



## Performance Measures for Internal Audit Functions: A Research Project by IIA

In 2009, the IIA Research Foundation published survey of over fifty internal auditors in Austin, Texas, USA and sought to provide insights into how internal audit practitioners used performance measures along five categories. These categories included (i) environment (ii) output (iii) quality (iv) efficiency; and (v) impact. The report concluded that:

1. Many internal audit departments (30%) are failing to use performance measures
  2. Performance measures are being reported to management although the internal audit departments do not directly report to them
  3. Small internal audit departments are less likely to use performance measures than large ones
  4. Quality measures are the most likely type of performance measure used
  5. Although efficiency measures are used very few of them are measures of financial efficiency
  6. Very few internal audit departments are using any form of performance measure related to impact.
- 

## Key Performance Indicators: Examples

There are many performance measures and indicators that public sector internal audit teams could decide to use and the following list provides indicative examples grouped in various categories:



### External indicators

This category measures factors which impact the works of the internal audit function indirectly and are not necessarily under the control of the internal audit department. Examples may include setting specific targets such as:

- Time spend on management requested reviews relative to the overall internal audit plan
- Management satisfaction survey results
- Number of meetings between Head of Internal audit and senior management / Audit Committee, if established





## Planning indicators

These indicators measure factors which impact the work of the internal auditors related to planning the audit processes, or which are expressed relative to the overall internal audit plan. Possible indicators include:

- Total number of engagements completed by the internal audit function
- Number of assurance engagements performed by the internal audit function as a proportion of the overall internal audit plan
- Time spent on compliance audits, operational / performance audits, IT audits and consulting engagements
- Percentage of key risks audited per annum
- Proportion of audit universe addressed in the audit plan



## Budget indicators

Under this group of performance measures items such as output relative to resourcing of the internal audit function are measured. Indicators may include:

- Resources allocated to the internal audit department relative to benchmarks
- Various comparisons including: cost per audit hour, budget versus actual, comparisons with previous year, internal audit costs relative to overall payroll costs, costs of internal audit relative to total operating costs



## Staffing indicators

These indicators measure the performance and quality of the staffing resources within the internal audit department. Examples include:

- Number of internal auditors relative to total staff
- Average years of internal audit staff relevant experience
- Proportion of internal auditors with professional qualification/certification including those required by the regulator (usually the Ministry of Finance)
- Internal audit staff turnover
- New internal audit hires versus total internal audit staff
- Number of hours spent by internal audit staff in Continuing Professional Development
- Number of hours of training per staff
- Proportion of internal audit budget allocated to professional development
- Levels of internal audit staff satisfaction



## Impact and Quality indicators

These indicators measure the ultimate impact and effectiveness of and internal audit function. Possible indicators under this category include:

- Time from completion of field work to issue the draft / final internal audit report
- Number of recommendation issued (overall or per audit report)
- Percentage of recommendations issued (per audit report)
- Percentage of recommendations implemented
- Number of repeat findings relative to overall findings
- Number and frequency of periodic / health checks
- External assessment score

# Internal Audit Capability Model for the Public Sector and Performance Measures

The Institute of Internal Auditors, USA has developed a capability model for the public sector<sup>1</sup> which provides an illustration of the various stages through which an internal audit function can evolve over time. The model can be useful for planning internal audit improvements as the function evolves over time and includes five capability levels for an internal audit function through a continuum which includes<sup>2</sup>:

- **Initial:** No sustainable repeatable capabilities and the function is dependent on individual efforts
- **Infrastructure:** Sustainable and repeatable internal audit practices and procedures
- **Integrated:** internal audit management and professional practices uniformly applied
- **Managed:** internal audit integrates information from across the organization to improve governance and risk management
- **Optimizing:** internal audit function is learning from inside and outside the organization for continuous improvement.

Further, the model delineates Internal Audit Activity along six elements including

1. Services and role of IA,
2. People management,
3. Professional practices,
4. Performance management and accountability,
5. Organizational relationships and culture, and
6. Governance structure.

The element related to performance management and accountability “refers to the information needed to manage, conduct, and control the operations of the internal audit activity and account for its performance and results”<sup>3</sup>. The spectrum in this domain is outlined as follows:

- **Level 1:** Absence of any formal structure for performance measurement.
- **Level 2:** Presence of an operating budget and plan.
- **Level 3:** Cost information on the internal audit activity has been developed, cost information is used in decision making, [performance measures developed which are primarily input based with a few output measures.
- **Level 4:** Balanced qualitative and quantitative performance measures are developed, input from key stakeholders is obtained on a regular basis, results from the Quality Assurance and Improvement Plan are used to enhance performance
- **Level 5:** Impact measures developed, public reporting of internal audit activities

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<sup>1</sup> <https://na.theiia.org/iia/f/Pages/Internal-Audit-Capability-Model-for-the-Public-Sector.aspx>

<sup>2</sup> Source: IIA

<sup>3</sup> Source: IIA



# Performance Measures In Practice: A View from the Asian Development Bank

## Measures that Matter

In 2011, the Asian Development Bank (ADB)'s Office of the Auditor General (OAG), ADB's internal audit office, developed and implemented its Quality Assurance and Improvement Program. Performance and productivity measures deemed most relevant for OAG were defined as part of OAG's internal assessment through ongoing monitoring. Actual metrics against targets are monitored throughout the year, analyzed by OAG's Quality Assurance Working Group (QAG), and reported bi-annually to the audit committee.

OAG has defined performance measures in these areas: (i) OAG staffing and training; (ii) annual work program deliverables; (iii) implementation of audit recommendations; (iv) client feedback; and (v) productivity measures. In determining which performance indicators to include in its ongoing monitoring, QAG did not have a specific number in mind, but simply focused on: i) which measures were currently being used by OAG management, ii) practices and procedures already in place in terms of how the audits / advisory engagements are expected to be conducted, and (iii) other measures already being reported to the audit committee. Targets were based on the level of quality and efficiency OAG wished to achieve as set out in OAG's strategy paper. Some targets were also based on benchmarking against other similar organizations.

It is important to note that the performance measures and targets are evolving. OAG, on a regular basis, evaluates whether the current performance measures are still relevant, or whether the target needs to be raised to ensure more efficiency in operations or adjusted to a more realistic one.

## OAG Performance Measurements and Targets



| Description of Indicators                               | Targets  |
|---|--|
| <b>A. External Indicator</b>                            |  |
| i. Audit and Advisory Services Feedback Surveys         | 70% satisfaction   |
| <b>B. Planning Indicators</b>                           |  |
| i. New audits for the year                              | 80%  |
| ii. Carryover audits from previous year                 | 100%   |
| iii. Average response time to perform advisory requests | Within year of request   |
| <b>C. Budget Indicators</b>                             |  |
| i. Direct vs. indirect time of staff per audit          | 90% direct time to total time  |
| ii. Budgeted hours vs. Actual hours                     | <ul style="list-style-type: none"><li>Audit / Bi-Annual Reports - 75%</li><li>Advisory - 15 %</li><li>Continuous Professional Education - 5%</li><li>Continuous Improvemen<sup>4</sup> - 5% target</li></ul> |

<sup>4</sup> Refers to involvement of internal audit staff in different working groups within OAG such as: Quality Assurance Working Group, Data Analytics Working Group, Report Writing Working Group, Audit Risk Working Group, Professional Development Working Group, etc.

| Description of Indicators   | Targets   |
|---|---|
| <b>D. Staffing Indicators</b>   |   |
| i. Audit staff per ADB staff (excluding vacancies)                            | 1 per 100   |
| ii. Average years of audit experience   | At least 5 years' experience in auditing  |
| iii. Percentage of audit staff with professional designation                  | 90%   |
| iv. Percentage of audit staff time spent on continuing professional education | 5%  |
| <b>E. Impact and Quality Indicators</b>                                       |   |
| i. Bi-Annual Reports (issued twice a year)                                    | Circulated to Management 2 months after the end of the reporting period   |
| ii. Average time to complete an audit   | <ul style="list-style-type: none"> <li>Audit Report finalized within 2 months from last day of field work</li> <li>Working papers completed and signed-off in Audit Management System 2 weeks after issuance of Final Audit Report</li> </ul> |
| iii. Timeliness of audit recommendations implemented                          | <ul style="list-style-type: none"> <li>60% High within 12 months</li> <li>60% Medium within 24 months</li> </ul>  |

## Translating Metrics into Meaning

Setting out performance measures and assessing through ongoing monitoring were not only a reporting mechanism for OAG. These have benefited OAG in the following ways:

- Ensuring conformance with the Standards (Attribute Standard 1311) and consistent application of the Core Principles for the Professional Practice of Internal Auditing;
- As internal audit staff are aware of OAG's performance targets, this has set the tone for the level of quality and efficiency expected from staff when conducting audit or advisory engagements;
- Review of actual results against targets allows the QAG to narrow the gaps and assess why targets are not being met.
- Optimizing OAG's resources; and
- Developing a culture of continuous improvement among staff.

# Key Highlights – Community of Practice Survey

Further to the discussions at the advanced workshop for the Community of Practice, which took place in Vienna at the Joint Vienna Institute on 5-8 June 2018, the topic of performance measurement for internal audit emerged as one area of considerable interest for participants. In this respect, a survey was administered to gauge current practices in this area. Key highlights from the survey are reproduced below:

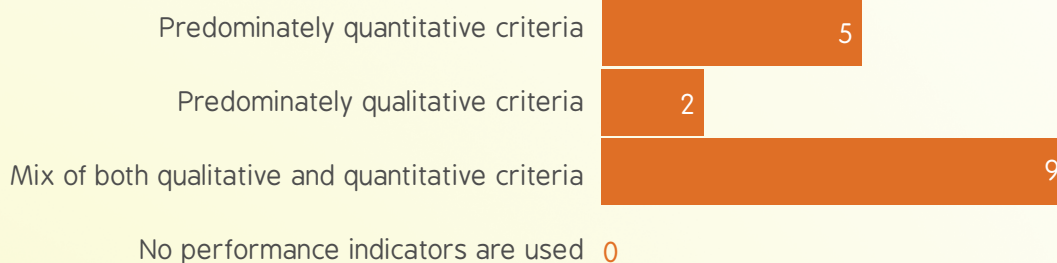
## Question 1

Do you use performance indicators to measure the performance of the internal audit unit?



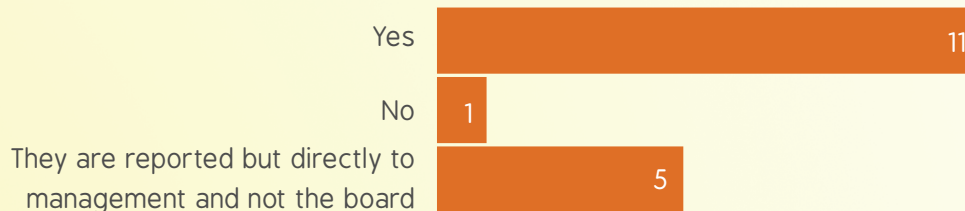
## Question 2

Are the Performance indicators based on predominantly quantitative or qualitative criteria or both?



## Question 3

Does the Head of Internal Audit report periodically to the board or management on the performance of the internal audit activity?







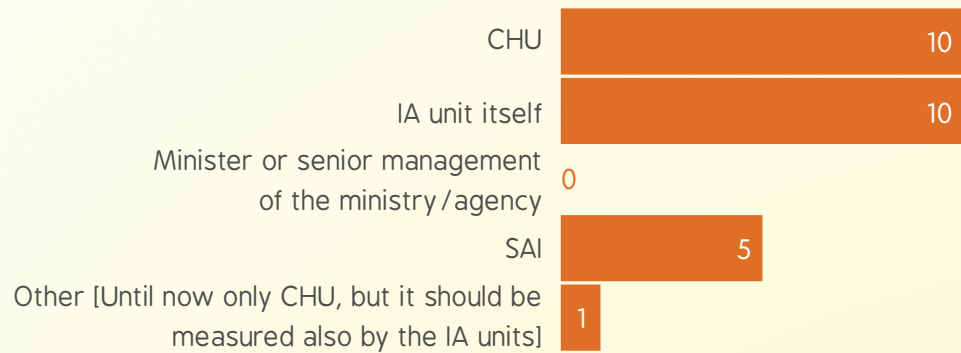
## Question 6

Do you used a balanced scorecard approach for performance measurement of the internal audit function?



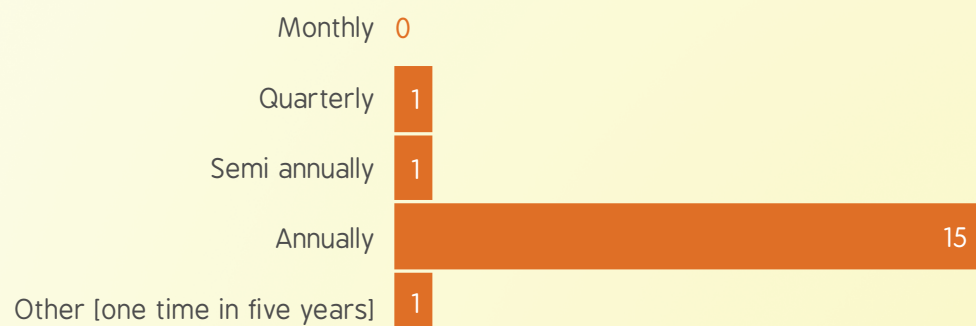
## Question 7

Who conducts the performance measurement (select all that applies)?



## Question 8

How often are performance measures reported?



# Suggested Reading

1. PEMPAL IACOP "Quality Assessment Guide for Public Sector Internal Audit"
2. IIA, IPPF Practice Guide "Measuring Internal Audit Effectiveness and Efficiency"
3. PwC "Metrics by design A practical approach to measuring internal audit performance"
4. IIA Research Foundation "Performance Measures for Internal Audit Functions: A Research Project"
5. International Standards for the Professional Practice of Internal Auditing (1110, 1300, 2600)
6. IIA IPPF Practice Guide 'Quality Assurance and Improvement Program'
7. IIA Netherlands "Measuring the Effectiveness of the Internal Audit Function"



## Internal Audit Training of Trainers Webpage

<http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/ECAEXT/EXTCENFINREPREF/0,,contentMDK:23748830~pagePK:64168445~piPK:64168309~theSitePK:4152118,00.html>



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