The Path to Quality

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Introduction

Given the pace of change involving a variety of environmental factors affecting organizations around the globe today, successful internal auditors supporting these organizations must focus on:

• Meeting or exceeding their stakeholders’ expectations
• Delivering high-quality services resulting from disciplined processes performed by competent personnel.
• Helping their organizations seize opportunities in pursuit of strategic and operational objectives.
What is Quality?

• Quality is the essence of excellence in the business environment.
• Processes must be measured and evaluated objectively.
• Includes ongoing commitment to growth and improvements.
International Professional Practices Framework

• International Standards for the Professional Practice of Internal Auditing (Standards)
  – Mandatory Guidance
    • Attribute
    • Performance
    • Implementation
      – Assurance
      – Consulting
• Practice Advisories
• Development and Practice Aids
Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Fostering Enterprise Risk Management

Re-engaging on Internal Controls

Facilitating more effective corporate governance
International Professional Practices Framework

• Code of Ethics
  – Mandatory Guidance
• Principles /Rules of Conduct
  – Integrity
  – Objectivity
  – Confidentiality
  – Competency
Quality Standards

1300 - Quality Assurance and Improvement
1310 - Quality Program Assessments
1311 - Internal Assessments
   – Ongoing Reviews
   – Periodic Reviews
1312 - External Assessments
   – Five Year Requirement
1320 - Reporting on the Quality Program
Establish a Quality Assurance and Improvement Program (QAIP)

• Required by *Standard 1300*

• Internal audit Activity should:
  – Perform in accordance with its charter, Standards and Code of Ethics
  – Operate in an effective and efficient manner
  – Be perceived by stakeholders as adding value and improving organisation’s operations
Standard 1300
Establish a Quality Assurance and Improvement Program

- Document the components of the program:
  - Covers all aspects of the internal audit activity including a list of the features from PA 1300-1.
  - Continually monitors the internal audit activity’s effectiveness. Develop performance measures
  - Assures compliance with the Standards and Code of Ethics.
Standard 1300

Establish a Quality Assurance and Improvement Program

• Document the components of the program:
  – Help the Internal Audit activity add value and improve organisational operations.
  – Includes both periodic and ongoing internal assessments.
  – Includes an external assessment at least once every five years, the results of which are communicated to the Board of Directors (BOD) through the Audit Committee of the Board of Directors (Audit Committee)

• The omission of any of these six elements form the QA program represents non-compliance to the Standards
Quality Program Components

1. Internal Quality Assessments
   - On-going
   - Periodic

2. External Quality Assessments
   - Independent assessment with independent validation
   - Self assessment with independent validation (SAIV)
Internal Assessments

*Standard 1311*

- Key component of a quality assurance and improvement program
- Prepares IA Activity for the once every 5 years external QA or validation
- Conclusions should be developed as to the quality of ongoing performance
- Follow-up action should be taken to ensure appropriate improvements are implemented
Internal Assessments

*Standard 1311*

**Ongoing Internal Assessments**

- Ongoing quality is most effective when built into internal audit processes
  - Ensure effective engagement supervision
  - Implement checklists for work programs
  - Obtain feedback from audit customers and other stakeholders
  - Establish performance metrics
  - Monitor project budgets, timekeeping systems, audit plan completion
External Assessments

Standard 1312

External assessments must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization. The chief audit executive must discuss with the board:

• The form and frequency of external assessment; and
• The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.
Global Survey

The Value of Quality Assurance and Improvement Programs
A Global Perspective
Objective of Survey

- Using input from more than 1,000 respondents in 46 countries, this report evaluates the current state of quality assurance and improvement programs (QAIPs) around the world and offers practical information about leading practices.
Research Objectives

The IIA Research Foundation (IIARF) sponsored this project to address the following questions:

– What are the business reasons why an internal audit activity should invest in building a QAIP?
– How does developing a QAIP add value to the daily operations of an internal audit activity?
– What are the challenges confronting internal auditors around the world during establishment of a QAIP?
– What are the key characteristics of effective QAIPs?
– How does a successful QAIP enable an internal audit activity to achieve its mission of addressing stakeholder needs and adding value to the organization it supports?
Existing QAIPs

The goal of one of the key research questions was to find out how many respondents have implemented a QAIP.
Geographic Diversity

One of the survey goals was to seek out a broad cross-section of internal audit practitioners around the globe. Hearing from many different voices enhances the robustness of the research results.
Industries & Organisational Structure

- Banking, financial institutions, and insurance made up the largest single component of respondents, as illustrated in figure 1.3. Apart from the category “Services,” which includes a variety of organizations, other key industry components had lesser but adequate representation within the survey results.

Figure 1.3. Industries
Maturity of Internal Audit Activities

Above figure demonstrates the dynamic nature of the practice of internal auditing, as nearly half the respondents work in internal audit activities that have been in place for less than 10 years. Establishing an effective QAIP is a key step in developing a new internal audit activity.
Organisational Size

Above figure demonstrates another interesting characteristic of the survey responses: nearly half came from internal audit activities with five or fewer employees.
Reasons for Investing in QAIPs

Survey respondents cited the following primary reasons for investing in QAIPs:

• To identify areas for improvement
• To be in conformance with the mandatory guidance of the IPPF
• To increase the credibility of the internal audit activity within the organization
• To anticipate, meet, or exceed stakeholder expectations
• To bring a systematic, disciplined approach to the internal audit activity
Focus on Continuous Improvement

**Figure 2.1. Reasons for Investing in a QAIP**

- To identify areas in need of improvement: 68%
- To be in full conformance with IIA Standards: 57%
- To bring a systematic, disciplined internal audit approach: 46%
- To increase the weight/credibility of the internal audit activity within the organization: 46%
- To anticipate, meet, or exceed stakeholders’ expectations: 42%
- To be in greater support of the strategy: 11%
- To increase the reputation of the organization: 9%
- To contribute to the effectiveness of the financial reporting process: 7%
Alignment of Value Added with Reasons to Invest in QAIPs

A key overall finding from the research is that internal audit activities with a QAIP in place (or planning to implement one within 12 months) confirmed that an effective QAIP adds value to their internal audit activity consistent with their primary reasons to invest in one. These results demonstrate a clear alignment of value added from an effective QAIP with the most important reasons why an internal audit activity should invest in one.
## Added Value from an Effective QAIP

<table>
<thead>
<tr>
<th>Survey Question</th>
<th>Disagree (1–3)</th>
<th>Neutral (4)</th>
<th>Agree (5–7)</th>
</tr>
</thead>
<tbody>
<tr>
<td>19a. Better use of resources</td>
<td>22%</td>
<td>21%</td>
<td>57%</td>
</tr>
<tr>
<td>19b. Attention paid to customers’/stakeholders’ perception and satisfaction</td>
<td>18%</td>
<td>17%</td>
<td>65%</td>
</tr>
<tr>
<td>19c. Enhanced internal auditors’ professionalism and specialized skills</td>
<td>11%</td>
<td>14%</td>
<td>75%</td>
</tr>
<tr>
<td>19d. A sense of accomplishment and satisfaction for internal auditors</td>
<td>16%</td>
<td>20%</td>
<td>64%</td>
</tr>
<tr>
<td>19e. Systematic documentation and evaluation of the performance of critical processes</td>
<td>12%</td>
<td>15%</td>
<td>73%</td>
</tr>
<tr>
<td>19f. Identification of critical areas and points for improvement</td>
<td>9%</td>
<td>10%</td>
<td>81%</td>
</tr>
<tr>
<td>19g. Improving the organization’s reputation</td>
<td>22%</td>
<td>22%</td>
<td>56%</td>
</tr>
</tbody>
</table>
Added Value from an Effective QAIP

• As illustrated, the results of survey question 19 indicate that the top three contributors of value added to the internal audit activity resulting from an effective QAIP are identification of critical areas for improvement, enhanced internal auditors’ professionalism and specialized skills, and systematic documentation and evaluation of the performance of critical processes.
Implications For Practitioners

Internal audit activities that have not yet established a QAIP should consider the value added from an effective QAIP, as outlined in the survey results. These benefits form the basis for a decision to initiate investment in a QAIP and provide offsets to perceived costs associated with establishing one.
Implications For Practitioners

CAEs should promote their QAIP as a source of value added in support of organizational objectives—strategic and operational. A high-performing internal audit activity contributes to achieving organizational objectives through its systematic, disciplined internal audit processes and the competencies of its staff.

Its processes and personnel enable the internal audit activity to build credibility within the organization, which results in an enhanced ability to meet or exceed stakeholder expectations. QAIPs empower the internal audit activity to add value by contributing to the achievement of strategic objectives (see the new Practice Advisory 2120–3: Internal Audit Coverage of Risks to Achieving Strategic Objectives).
Implications For Practitioners

CAEs are encouraged to promote their QAIP and communicate with senior management and the audit committee regarding the achievement of strategic objectives and the value added. This interaction between the internal audit activity and its key stakeholders is supported by IIA Practice Guide, Measuring Internal Audit Effectiveness and Efficiency, which notes:

“Organizations that effectively use internal auditing are better able to identify business risks and process and system inefficiencies, take appropriate corrective action, and ultimately support continuous improvement.”
Challenges Of Implementing QAIPs

The main reasons for non conformance to Standard 1300 noted in CBOK 2010 were:

• Small size of the organization or internal audit activity
• Cost of using the *Standards*
• Amount of time required for compliance
• Lack of management/board support
Challenges Of Implementing QAIPs

Practitioners continue to confront resource constraints in trying to establish QAIPs.

**Figure 3.1. Obstacles to Establishing QAIPs**

- **Financial cost**: 54%
- **Lack of staff to supervise engagements effectively**: 51%
- **Increase of bureaucratization**: 44%
- **Increase of paper workload**: 41%
- **Too theoretical**: 21%
- **Waste of time**: 9%
Resource-related Barriers

• Resource constraints dominate the obstacles identified by respondents, led by financial cost and lack of staff to supervise engagements effectively.

• Time and staffing constraints are also included in other comments gathered during the survey. Some respondents mentioned competing priorities for staff responsible for coordinating QAIP activities that make improving the QAIP program more challenging. Some small audit shops must choose between investing in their QAIP, providing staff training, or implementing a new audit tool.
Implications for Practitioners

Addressing resource constraints in establishing their QAIP will require CAEs to consider the approach outlined in IIA Practice Guide, Quality Assurance and Improvement Program, which states,

“Quality should be built in to, and not on to, the way the activity conducts its business—through its internal audit methodology, policies and procedures, and human resource practices”
Implications for Practitioners

• The benefits described earlier provide a basis for CAEs to justify the allocation of resources to building and sustaining a successful QAIP.

• To further address the issue of time and staff constraints, CAEs should consult The IIA’s Quality Assessment Manual for the Internal Audit Activity for tools that enable the integration of ongoing assessments into the daily operation of internal audit activities. Integrating quality into day-to-day audit activities reduces the need for “extra” staff time devoted to QAIP and supports development of a systematic, disciplined internal audit process.
Global Characteristics Of Successful QAIPs: Internal Assessments

• As described in the IPPF, the internal assessment portion of a QAIP is comprised of two elements:
  – ongoing monitoring and
  – periodic self-assessment

• The research found that practitioners have integrated their ongoing monitoring activities within their internal audit activity’s normal operations. This approach is consistent with IIA Practice Guide, Quality Assurance and Improvement Program, which states that “Ongoing monitoring provides assurance that the processes in place are working effectively to ensure quality is achieved on an audit by audit basis
Ongoing Monitoring

Results displayed demonstrate that practitioners have integrated their ongoing monitoring activities within their internal audit activity’s normal operations. Specifically, CAE approval of final reports, supervisory review of engagements, use of relevant audit policies and procedures, and regular review of engagement working papers comprise many day-to-day actions taken by internal audit staff and management.
Ongoing Monitoring

Figure 4.1. Components Implemented in an Ongoing Internal Assessment

- All final reports and recommendations are reviewed and approved by the chief audit executive (CAE) - 89%
- Supervision of engagements - 88%
- Audit policies and procedures used for each engagement to ensure conformance with applicable planning, fieldwork, and reporting standards - 86%
- Regular, documented review of working papers during engagements by appropriate internal audit staff - 85%
- Feedback from customer survey on individual engagements - 61%
- Analyses of performance metrics established to improve the internal audit activity’s effectiveness and efficiency - 54%
Periodic Internal Assessment

Figure 4.2. Components Implemented in a Periodic Internal Assessment

- Annual risk assessments for purposes of annual audit planning: 89%
- Periodic activity and performance reporting to governing bodies: 84%
- Annual review of findings: 68%
- Review of internal audit performance metrics and benchmarking of best practices, prepared and analysed in accordance with audit policies and procedures: 52%
- Semi-annual workpaper reviews for performance in accordance with internal audit policies and The IIA’s International Standards for the Professional Practice of Internal Auditing (Standards): 44%
- Internal assessment by other individuals in the organization: 31%
- Biannual customer survey: 27%
Periodic Internal Assessment

Survey results for periodic internal assessments are similar to those reported for ongoing monitoring; that is, practitioners generally implement a *Standards*-based assessment.

The annual risk assessment (Standard 2010: Planning) and periodic reporting to governing bodies (Standard 2060: Reporting to Senior Management and the Board) are the two most common elements of the periodic internal assessment.
Implications for Practitioners

To embed internal assessments in daily tasks, outputs should be visible and discussed with staff to reinforce their involvement. QAIP initiatives should be linked with staff training programs and established as part of normal job routines. CAEs should develop quality key performance indicators at the engagement level.

For an efficient use of resources, CAEs should seek to coordinate ongoing monitoring activities with periodic internal assessments. The IIA’s *Quality Assessment Manual for the Internal Audit Activity* contains tools that facilitate this coordination of ongoing monitoring with periodic internal assessments.
Implications for Practitioners

In seeking synergy between ongoing assessments and periodic initiatives, CAEs should focus on audit activities that extend beyond conformance with the Standards. Practices such as annual review of findings and analysis of performance metrics could be used to support the development of continuous improvement initiatives. Benchmarking of performance metrics could serve as a basis for discussion with the internal audit team.
Global Characteristics Of Successful QAIPs: External Assessments

The three most important reasons to invest in an external assessment are:

• Benchmarking internal audit practices
• Assuring conformance with IIA Standards
• Increasing the perceived value of the internal audit activity within the organization
An external quality assessment can be configured as:

- An assessment performed by a person or a team independent from the organization,
- A peer review involving three or more organizations, or
- A self-assessment with independent external validation conducted by a person or team external to the organization.
Investing In External Assessments

Figure 5.3. Reasons for Conducting External Quality Assessments

- To benchmark our internal audit practices: 49%
- To be in full conformance with IIA Standards: 47%
- To increase the perceived value of the internal audit activity within the organization: 43%
- To set an example: “The internal audit activity is also audited”: 34%
- To meet or exceed stakeholders’ expectations: 32%
- To raise the awareness among management of internal audit professional standards: 21%
- To increase the reputation of the organization: 13%
As figure illustrates, the three most important reasons to invest in an external assessment are:

• Benchmarking internal audit practices
• Assuring conformance with IIA *Standards*
• Increasing the perceived value of the internal audit activity within the organization
Implications For Practitioners

An external assessment is clearly an essential element of a successful QAIP. CAEs should ensure that the goals and objectives for conducting an external assessment are aligned with overall QAIP objectives and the value to be derived by the internal audit activity.

The choice of external assessment—full external or self-assessment with independent external validation—should also be consistent with overall goals for the QAIP.
External Assessment

• The full external assessment process involves the chief audit executive (CAE) acquiring a suitable independent, qualified provider of external assessment services, as guided by the Standards (Practice Advisory 1312-1).

• The CAE should provide input into the requested scope of the full external assessment and its specific objectives. This process should also ensure full consideration regarding expectations of executive management and the audit committee.

• The following illustrates an approach to the full external assessment process.
Full External Assessment Process

**Planning**
- Set scope and objectives
- Select and prepare team
- Request planning docs
- Preliminary visit
- Distribute surveys

**Off-site work**
- Review planning docs
- Review all other docs received as per docs request list
- Summarize survey responses

**Onsite work**
- Interviews with clients, IA staff, and stakeholders
- Workpaper reviews
- Review all other documents only available onsite
- Determine staffing knowledge
- Team discussions

**Evaluate and report**
- Evaluate against IPPF resources for conformance and areas for improvement
- Summarize issues
- Recommendations
- Closing meeting
- Issue draft report for comment
- Issue final report to CAE

**Key Inputs**
- QAIP
- Interviews & Surveys
- Review of process, reports, and risk assessment
- Review of workpapers, reports, and technology plan
- Report files

**Process**
- Enterprise objectives for the IA activity
- Leading industry successful practices (for example GAIN)
- The IPPF
QUALITY ASSESSMENT PROCESS MAP
Full External Assessment

Completed by the IA Activity

Background Information on the internal audit (IA) activity.

Document Request Checklist cross-referenced to planning/program process flow: IA Governance, IA Staff, IA Management, and IA Process.

Planning Guides designed for each segment.

Surveys containing elements from each segment.

B-1 Executive Leadership & Operating Management
B-2 IA Staff

Interview Guides containing elements from each segment.

C-1 Chief Audit Executive
C-2 Board Members, Senior & Operating Management
C-3 IA Staff
C-4 External Auditors & Other Assurance Providers

Programs designed for each segment. Assessors document their conclusions regarding conformance with mandatory guidance here.

Evaluation Summary provides a record of ratings determined within the programs by assessors.

Quality Assessment Report formatted to meet the needs of key stakeholders.

Completed by the Independent External Assessment Team
Evaluating Standards
Conformance

• GC – “Generally Conforms” means the evaluator has concluded that the relevant structures, policies, and procedures of the activity, as well as the processes by which they are applied, comply with the requirements of the individual Standard or element of the Code of Ethics in all material respects. For the sections and major categories, this means that there is general conformity to a majority of the individual Standards or elements of the Code of Ethics, and partial conformity to the others, within the section/category. There may be significant opportunities for improvement, but these should not represent situations where the activity has not implemented the Standards or the Code of Ethics, is not applying them effectively, or is not achieving their stated objectives.
Evaluating Standards Conformance

- **PC** – “Partially Conforms” means the evaluator has concluded that the activity is making good-faith efforts to comply with the requirements of the individual *Standard* or element of the Code of Ethics, section, or major category, but falls short of achieving some major objectives. These will usually represent significant opportunities for improvement in effectively applying the *Standards* or Code of Ethics and/or achieving their objectives. Some deficiencies may be beyond the control of the activity and may result in recommendations to senior management or the board of the organization.
Evaluating Standards
Conformance

• **DNC** – “**Does Not Conform**” means the evaluator has concluded that the activity is not aware of, is not making good-faith efforts to comply with, or is failing to achieve many/all of the objectives of the individual *Standard* or element of the Code of Ethics, *section*, or *major category*. These deficiencies will usually have a significant negative impact on the activity’s effectiveness and its potential to add value to the organization. They may also represent significant opportunities for improvement, including actions by senior management or the board.
Conformance to Standards

• **Standards or Code of Ethics Nonconformance**
  – Most serious category of finding
  – Requires a recommendation

• **Practice Advisories Nonconformance**
  – Opportunity for improvement
  – Not a basis for Standards nonconformance

• **Successful Practices**
QAR - Key Deliverables

Assessment
  ↓
Gap Analysis
  ↓
Results
  ↓

Stakeholder Needs & Expectations
  ↓
Professional Standards
  ↓
Internal Audit Best Practices
  ↓
Current State of Operations

Recognition of Strengths
  ↓
Practical Recommendations for Improvement
  ↓
Desired Future State

High-Level Action & Implementation Plan
  ↓
Internal Audit Desired Future State
Common Issues Observed in Quality Assurance Reviews

• Inappropriate CAE reporting relationships.
• Out-of-date charters for internal audit activity.
• Lack of board approved policy on internal control responsibility.
• Client perception of inadequate audit staff knowledge.
• Lack of a formalized risk assessment process.
• Lack of understanding regarding:
  – *Internal audit activity’s consulting responsibilities*
  – *Reflection of consulting in the mission and charter*
• Inadequate IT coverage or technical skills.
• Lack of ongoing and periodic internal quality assessment process program.
Quality Assessment Resources

• Frequently Asked Questions about Quality
• Sample request for a quality assessment proposal
• Audit customer (client) survey
• Internal audit staff survey
• Models
  – Model Audit Committee Charter
  – Model Internal Audit Activity Charter
Questions?
Thank You