PEMPAL

IACOP

Internal Audit
Community of
Practice

KEY PERFORMANCE INDICATORS FOR INTERNAL AUDIT FUNCTION

July 2020

PEM⊕PAL

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Acknowledgements

PEMPAL and IACOP

Public Expenditure Management Peer Assisted Learning (PEMPAL) is a network to facilitate exchange of professional experience and knowledge transfer among public financial management practitioners in countries across the Europe and Central Asia region. The network, launched in 2006, aims to contribute to strengthening public financial management practices in the member countries through developing and disseminating information on good practices and their application.

The network is organized around three thematic communities of practice:

- Budget Community of Practice,
- Treasury Community of Practice, and
- Internal Audit Community of Practice.

The main overall objective of the IACOP is to support its member countries in establishing modern and effective internal audit systems that meet international standards and good practices; key for good governance and accountability in the public sector.

The key donors and development partners to the program are the Swiss State Secretariat for Economic Affairs, the Ministry of Finance of the Russian Federation, and the World Bank. The Dutch National Academy for Finance and Economy provides non-financial support.

Knowledge products developed by the IACOP include "Good Practice Internal Audit Manual Template"; "Good Practice Continuing Professional Development Manual Template"; "Internal Audit Body of Knowledge"; "Risk Assessment in Audit Planning"; "Cooperation Among Public Sector Audit and Financial Inspection Entities"; "Quality Assessment and Improvement Guide"; "PEMPAL Guidance on Internal Audit: Demonstrating and Measuring Added Value"; and "Impact of COVID-19 on the Role and Activities of Internal Audit". All are available from **www.pempal.org**.

Preface

This paper is based on materials and discussions at a Smart Interactive Talk among members of the IACOP and relevant global experts on June 2, 2020. The aim was to identify good practice for heads of internal audit units on the key performance indicators to measure performance of the internal audit function and how they can best be used.

Representatives from Austria, the United Kingdom, and the European Commission gave presentations and joined a question and answer session with IACOP members. More information, including the agenda and presentation materials, are available on PEMPAL website.[1]

Glossary

COVID-19	Corona Virus Disease 2019
CHU	Central Harmonization Unit
GIAA	Government Internal Audit Agency of the United Kingdom
KPI	Key Performance Indicator
IAD	Internal Audit Department of the Ministry of Finance of Austria
IIA	The Institute of Internal Auditors
IAS	Internal Audit Service of the European Commission
IACOP	PEMPAL Internal Audit Community of Practice
IPPF	International Standards for the Professional Practice of Internal Auditing on Quality Assurance and Improvement
MOU	Memorandum of Understanding
PEMPAL	Public Expenditure Management Peer Assisted Learning network

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[1] https://www.pempal.org/events/smart-interactive-talk-key-performance-indicators-internal-audit-activity

Part 1. Background
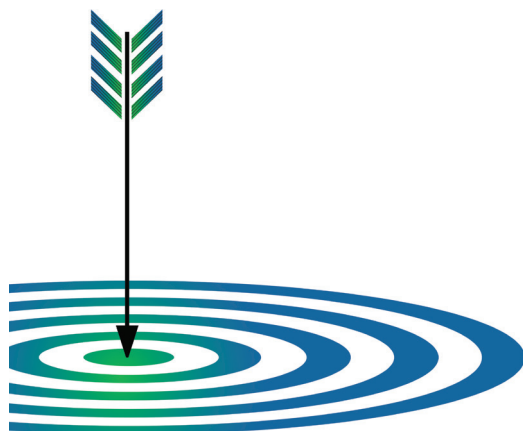
"What gets measured gets done!" is a favorite saying in many management textbooks. There is much evidence to support this saying and good reasons to assume that it can be applied to the work of internal auditors. Demonstrating and measuring the value of public sector internal audit was a priority area in the IACOP 2018 – 2019 Action Plan. Good practices were identified through an extensive collaborative process, involving practitioners and policymakers from PEMPAL member countries and other partners.

In October 2019, PEMPAL issued guidance for internal audit on demonstrating and measuring added value in the public sector.[2] Its focus is on how internal audit can demonstrate that it adds value in the different circumstances that exist in PEMPAL member countries; and how to measure this in terms of value for money (economy, efficiency, and effectiveness).

This paper builds on that guidance by providing more detail on key performance indicators (KPIs) that can support internal audit in measuring its performance. The following sections address:

- What are KPIs? What do the standards require of internal audit and what are the main elements to be considered in developing strong indicators. **(Part 2)**

- Which KPIs should be included in a balanced scorecard for internal audit that focuses on both internal and external stakeholders. **(Part 3)**

- Three practical examples: how the United Kingdom, Austria, and the European Commission have developed KPIs for internal audit. **(Part 4)**

- Four key areas for consideration in the use of KPIs. **(Part 5)**

- The central harmonization unit (CHU) component of the internal audit function. **(Part 6)**

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[2] Available at https://www.pempal.org/knowledge-product/pempal-guidance-internal-audit-demonstrating-and-measuring-added-value. See also "Internal Audit Key Performance Indicators" by the World Bank Centre for Financial Reporting Reform https://cfrr.worldbank.org/publications/internal-audit-key-performance-indicators

Part 2. What are key performance indicators?
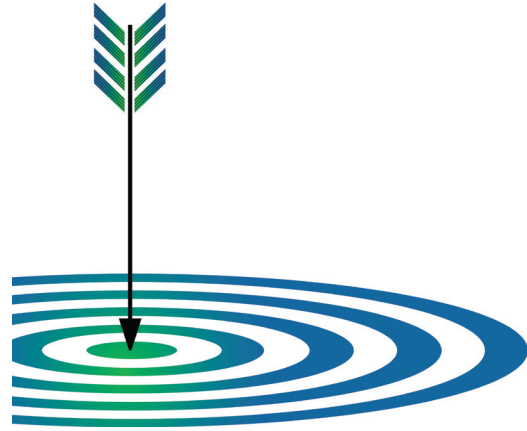
A performance indicator is a means of measuring the extent to which an individual, group, or entity is meeting its objectives. Initially a key performance indicator was a way of denoting the most relevant performance indicators for a particular organization. However, the terms performance indicators and KPIs are now often used interchangeably.

Internal audit standards

The Institute of Internal Auditors (IIA) International Standards for the Professional Practice of Internal Auditing on Quality Assurance and Improvement (IPPF 1300) require that internal audit units carry out internal assessments including "*ongoing monitoring of the performance of the internal audit activity*". In 2010, the IIA issued a Practice Guide on Measuring Internal Audit Effectiveness and Efficiency. This explains that a critical element of this monitoring is for internal audit units to establish, measure, and report on a range of KPIs. The IIA consider that the essential first step is to identify KPIs for activities that stakeholders believe add value and improve the organization's operations.

KPIs for internal audit

KPIs should provide management with a clear indication of the performance and quality of the internal audit function and should be an integral part of the internal audit system. They should focus on the added value generated by internal audit activity for both internal and external stakeholders. The performance measures captured in KPIs can be quantitative and qualitative.

- **Quantitative performance measures** are often based on existing or easily obtainable data and are easily understood (for example percentage of completed vs. planned audits). They often require less effort to collect and are readily comparable to the same metrics in other organizations.

Figure 1. KPIs for internal audit should be

1. Part of the management systems of the internal audit function	
Performance measurement process	Quality assurance process
2. Indicators of the value internal audit delivers	
Internal measures	External measures
Quantitative measures	Qualitative measures
3. Focused on what internal and external stakeholders want from IA	
External: Audit Committee, CHU	Internal: Management, Clients, IA
4. Directly linked to the maturity level of the IA function.	
Expand as the internal audit unit increases in maturity	

- **Qualitative performance measures** are often based on data that needs to be collected or derived, for example through survey research or interviews. They offer a broader view of performance on a range of topics that can provide depth to quantitative metrics.[3]

There is much evidence to suggest that KPIs should expand in content and depth as the internal audit function matures (see Figure 1).

Creating strong and effective KPIs

The IACOP considers that there are five distinct steps or elements involved in creating a strong and effective KPI. These elements are outlined in Figure 2.

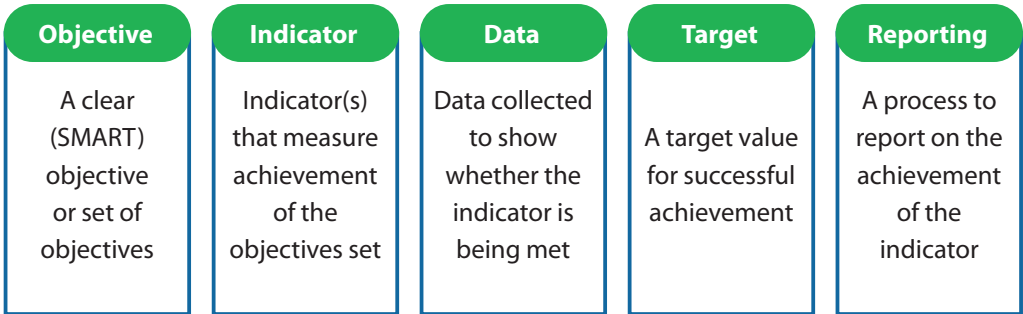[3] IIA practice guide on Measuring Internal Audit Effectiveness and Efficiency, 2010

Figure 2. Five elements of a strong KPI

Objective	Indicator	Data	Target	Reporting
A clear (SMART) objective or set of objectives	Indicator(s) that measure achievement of the objectives set	Data collected to show whether the indicator is being met	A target value for successful achievement	A process to report on the achievement of the indicator

The first element/step for all performance measurement systems is to establish objectives that specify what the organizational entity – in this case internal audit - is trying to achieve. These **objectives** must be SMART (**S**pecific, **M**easurable, **A**chievable, **R**elevant, and **T**ime-bound).

The second element/step is to identify **indicators** which measure whether those objectives are in fact being met. The European Commission Internal Audit Service (IAS) uses the mnemonic RACER to measure the effectiveness of an indicator:

- **R**elevant (capable of measuring the objective),
- **A**ccepted (by those being measured and those who receive reports of the measure),
- **C**redible (unambiguous and not overly technical),
- **E**asy (to monitor), and
- **R**obust (must monitor actual change).

The third element/ step is to collect **data** to show the extent to which the indicator is being met. Ideally, the data for quantitative indicators will be generated as a by-product of the planning, operational, and financial systems relating to the audit process. For qualitative indicators, however, additional process to generate this data may be needed - for example, the development, issue, and review of survey questionnaires.

In all cases it is important to guard against the manipulation of the data collected – for example, splitting one recommendation into its constituent parts to better meet a KPI on the proportion of recommendations accepted.

The fourth element is to set **baselines and target** achievement levels. A baseline is a reference point against which to measure achievement or progress towards objectives and assess if performance has improved. A KPI without a target, the ultimate desired situation that is both quantified and timed, will do little to influence future performance.

Milestones should be set for longer-term targets. Internal audit should avoid the trap of setting targets that are too easy to meet. Targets should be updated in accordance with the maturity of the internal audit function.

The final element is to ensure that there is a process to collect and **report** on data that shows whether the indicator has been achieved or not:

- **The type of reporting** should vary to meet the needs of different stakeholders – what a senior manager needs to know will be different from an audit committee.

- **The frequency of reports** should also reflect stakeholder needs. For example: senior managers may need a report once a year, audit committees may want a report for each meeting, the CHU may expect a report in accordance with the frequency of the reporting requirements by the internal audit function (but at least once a year), and internal audit managers may be monitoring KPIs every month.

- **The format of the report** should meet readers' expectations. Dashboards may be used to summarize data across a number of indicators. A traffic light coding to identify the most critical information should also be considered.

Part 3.
A balanced scorecard for internal audit
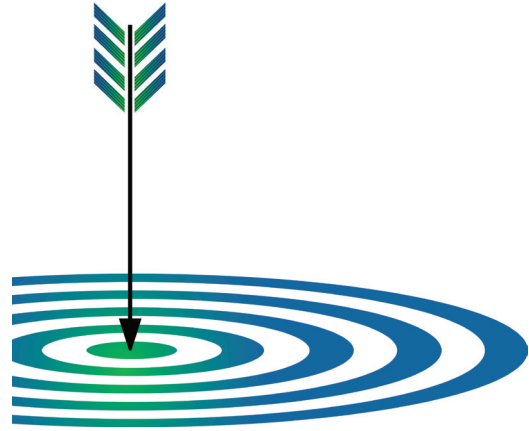
Setting and measuring KPIs is intended to influence the performance of internal auditors. However, if too few indicators are used they may have unintended consequences. Good practice is therefore to develop a number or "basket" of indicators that measure different aspects of internal audit performance and also reflect the needs of different stakeholders. This is usually referred to as a "balanced scorecard".

A balanced scorecard for internal audit could include the four dimensions as shown in Figure 3.

The four dimensions represented in the model above are:

- **Internal stakeholders.** These are the senior and/or supervisory managers of the entity where internal audit operates – normally the head of the institution in which internal audit operates.

Figure 3. The Balanced Scorecard for Internal Audit
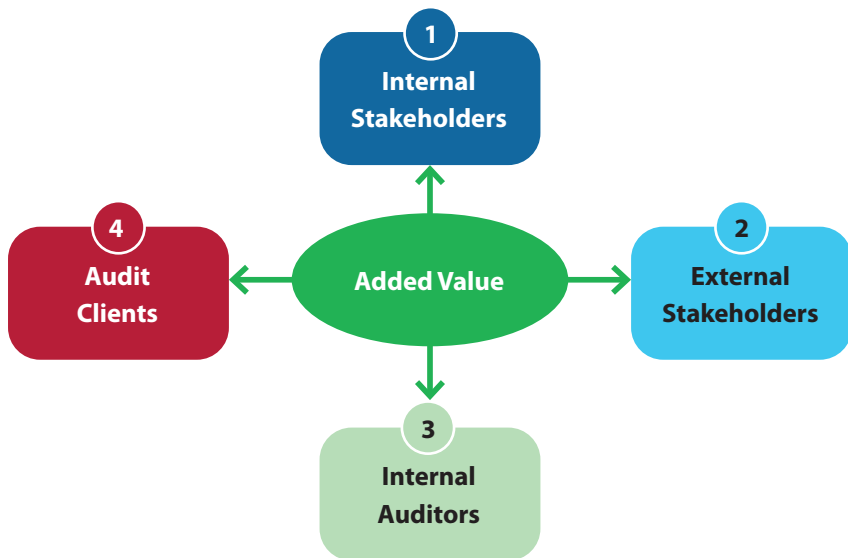
- **External stakeholders.** These would include an audit committee (if one exists) and a body such as a CHU that has a role in supporting/overseeing internal audit functions. The supreme audit institution is also an external stakeholder in most PEMPAL countries.

- **Internal auditors.** The auditors and managers who work inside the internal audit function. This is another subset of internal stakeholders who have specific needs in terms of more detailed KPIs related to internal productivity (that may appear less relevant in the eyes of other stakeholders).

- **Audit clients** are a subset of internal stakeholders who have specific interactions with internal audit in relation to audit engagements.

Each of these stakeholder groups have different requirements and/or interests in terms of the performance and perceived value of internal audit and may therefore require different KPIs. Some indicators may also be of relevance to more than one stakeholder.

The possible performance indicators of interest to each stakeholder group in the balanced scorecard are shown in tables 1 to 4 below.

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Table 1. Internal Stakeholders

Possible Performance Indicators	Comment
Materiality of audit findings.	Helps managers understand whether internal audit has identified serious issues.
Percentage of unsatisfactory ratings.	Measures how many audits result in poor or unsatisfactory ratings. This may be an indicator of the control maturity of the organization.
Percentage of the audit plan delivered during the year.	A low percentage may indicate that internal audit is taking on too many unplanned assignments. But it could also indicate that internal audit is being agile in responding to requests for assistance.

Possible Performance Indicators	Comment
Percentage of recommendations implemented by taking corrective action.	An indicator of the relevance, credibility, and quality of internal audit work.
Number of complaints from regulatory bodies.	Provides an indication of areas that may have been overlooked by internal audit. Plus the control maturity/ culture of the organization.
Number of frauds per annum and the value of frauds.	The quantity of frauds and the total value of fraud measure different aspects of fraud risks within the organization.
Percentage of high-risk audit universe covered each year.	How far is internal audit covering the major areas of risk within the organization.
Percentage of internal auditors being promoted elsewhere in the organization.	May indicate that internal audit is developing high quality staff that are valued elsewhere in the organization.
Results of client satisfaction survey questionnaire at the end of audit assignments.	Provides senior managers with an indicator of how well internal audit is performing its individual audit assignments.
Cost savings generated by implementing internal audit recommendations.	Senior managers are interested in knowing to what extent internal audit recommendations result in cost savings across the organization.
Changes to processes resulting from implementing internal audit recommendations.	Measures the level of process improvement generated by internal audit.

Table 2. External Stakeholders

| Possible Performance Indicators	Comment
Audit committee rating.	An overall rating of the internal audit function provided by the audit committee – this may be descriptive rather than a rating within a scale.
Percentage of recommendations accepted or not.	The proportion of recommendations accepted is a measure of the success of internal audit work.
Number of frauds per annum and value of frauds.	The quantity of frauds and the total value of fraud measure different aspects of fraud risks within the organization.
Indicators of the independence of internal audit.	These may be qualitative rather than quantitative for example the results of external quality assessments or CHU reviews, plus annual declaration by internal audit.
Percentage of high-risk audit universe covered each year.	How far is internal audit covering the major areas of risk within the organization.
Percentage of audit assignments that respond directly to concerns raised by the audit committee.	Measures whether internal audit is responding to the needs of the audit committee.
Results of client satisfaction survey questionnaire at the end of audit assignments. Results of annual client satisfaction survey of senior managers.	Helps the audit committee to assess the level of satisfaction from senior management.
Results of internal quality assessments.	A critical indicator of the quality of audit work undertaken by the internal audit function.
Results of periodic external quality assessments.	The highest value indicator of the quality of internal audit work.

Table 3. Internal Audit Function

Possible Performance Indicators	Comment
Percentage of audits completed versus those planned.	May indicate there is too much unplanned work.
The elapsed time for completing an audit from start to finish.	A general indicator of the overall efficiency of the audit.
The mean or average time from a closing meeting to issuing the audit report.	A good measure of efficiency in the report writing process which in turn indicates that the audit was well planned to generate the evidence needed.
Percentage of annual audit costs versus annual budget.	Looks at how good an audit unit is at managing costs.
Number of years of relevant business experience across all staff.	A useful indicator of the level of required business expertise.
Number of years of audit experience across all staff.	A useful indicator of the level of direct audit experience.
The percentage of certified auditors.	A good indicator of the level of trained auditors.
Percentage of planned and unplanned staff turnover during the year.	High levels of turnover may be an indication of staffing problems in the unit.
Number of training hours per auditor per year.	Measures the extent to which auditors are meeting continuing professional development expectations. This is also an indicator of the priority internal audit gives to training.
Number of innovative improvements.	An indicator of whether the internal audit unit is regularly reviewing its own processes.

Table 4. Audit Clients

Possible Performance Indicators	Comment
Satisfaction survey rating.	May indicate satisfaction or problems with individual assignments or managers.
Percentage of issues that are open, closed, or past due.	May indicate that managers are not taking sufficient action to address recommendations raised by internal audit.
Percentage of recommendations accepted or not.	May indicate that internal audit is not selling their findings to clients well.
Number of repeat findings.	May indicate that systemic weaknesses are not being addressed.
Number of requests by local management for audit support.	May indicate that clients are seeking out internal audit help and value their services.

Part 4. Examples of the use of KPIs by internal audit
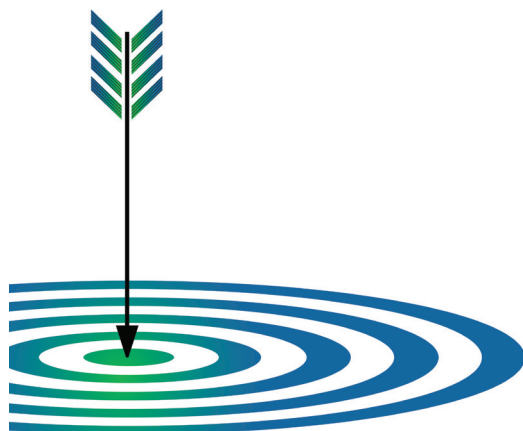
This part of the report provides three examples of the way that KPIs have been developed and used by internal audit in two countries (the United Kingdom and Austria) and the European Commission.

United Kingdom

The KPIs of the UK's centralized Government Internal Audit Agency (GIAA) must be directly related to its mission to provide objective insight so that central government can achieve better outcomes and value for money for the public. Its vision focusses on having firm foundations; being demanding on customer impact, uncompromising on quality, and ambitious on innovation; and unleashing its people's talent and confidence.

For each of its clients, the GIAA establishes a detailed memorandum of understanding (MOU) which specifies the work that will be carried out and includes key targets, for example:

- The annual audit plan will be agreed with the accounting officer[4] and audit & risk committee by 31 March and 30 April respectively.

- The GIAA will keep the client updated on changes to the annual audit plan.

- The GIAA will assign competent auditors to deliver the agreed audit plan.

- Planning meetings will be held with the engagement sponsor to kick-off all audit scoping exercises.

- Terms of reference will be issued for all audits at least 5 days before the start of audit unless the client has asked for assurance to be provided at short notice.

- Fieldwork will be completed in accordance with the terms of reference during the agreed timeframe for this work.

- The GIAA will conduct an audit close-out meeting on the agreed date (at end of fieldwork period) usually within 10 days of the completion of audit fieldwork.

- The GIAA will submit its draft report to

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[4] The accounting officer is usually the senior civil servant in the department or agency concerned.

key contacts within 15 days of fieldwork completion and the final report within 5 days of receipt of management response.

- The annual opinion by the head of internal audit will be delivered in accordance with the customer's year-end audit & risk assurance committee and governance statement timetable.

The MOU in effect drives the KPIs of most relevance for the GIAA's internal and external stakeholders. Many of these measures are generated automatically as a by-product of the audit software used. There are also two types of customer survey:

- A client survey questionnaire sent to all clients at the end of each audit assignment (Figure 4).

- A high level survey of all clients once a year which tries to establish the quality of the relationship between internal audit and senior management and the extent to which internal audit contributes to the strategic direction of the agency (Figure 5).

When the GIAA issued the assignment questionnaire and the annual questionnaire only electronically they experienced a low return rate (35%). Since introducing follow up face to face interviews where possible, using the questions as a structure for the interview, they are able to obtain an 85% response rate.

Figure 4. Extract from GIAA annual client survey questionnaire: Assignment/operational level

1. How satisfactory was the engagement process? (Please consider how you feel about: planning of the engagement; the engagement process itself; reporting; usefulness of recommendations; and professionalism of those undertaking the work)?

   - Planning

   - Engagement procedures

   - Reporting

   - Outcomes and Recommendations

   - Professionalism

2. On a scale from 1 to 10, where "1" represents Extremely Dissatisfied and "10" Extremely Satisfied, please rate how satisfied you are with the service provided by GIAA.

Figure 5. Example of GIAA annual questionnaire to the senior management of a government department

1. Management trusts and values the advice of the Head of Internal Audit and the internal audit service?

2. The internal audit service is seen as a key strategic partner throughout the Department?

3. Internal audit is valued throughout the Department?

4. The internal audit service is delivered with professionalism at all times?

5. The internal audit service responds quickly to changes within the Department?

6. The internal audit service is adept at communicating the results of its findings and securing agreed outcomes?

7. The internal audit service ensures that agreed management actions are appropriate and practicable in relation to the risks identified?

8. There have not been any significant control breakdowns or surprises in areas that have been positively assured by the internal audit service?

9. The internal audit service includes consideration of all key risk areas in its audit plan?

10. Internal audit advice has a positive impact on the governance, risk, and the system of control of the Department?

11. The internal audit service asks challenging and incisive questions that stimulate debate and improvements in key risk areas?

12. The internal audit service raises significant control issues at an appropriate level in the Department?

13. The Department recognizes and uses the business knowledge of internal auditors to help improve business processes and meet strategic objectives?

14. Delivery of the Department's objectives has improved as a result of the internal audit work performed?

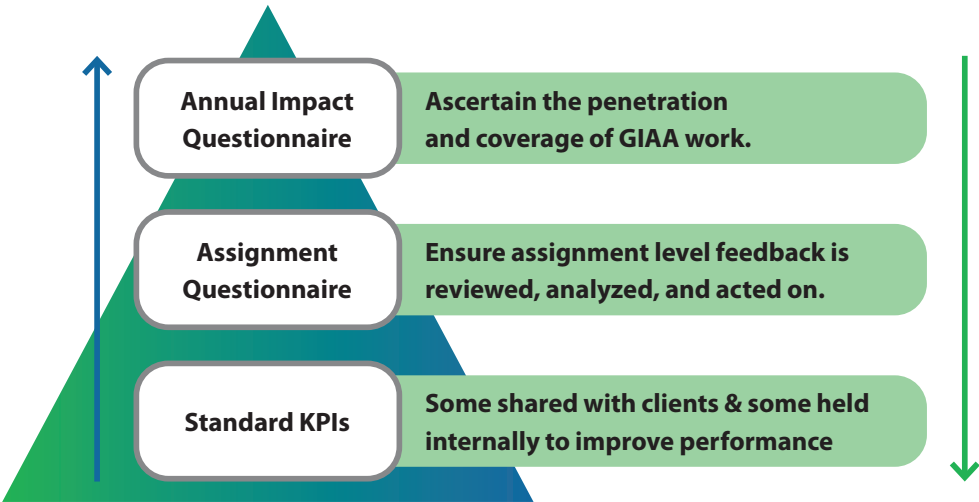15. Overall, internal audit has fulfilled its remit for the Department?

The GIAA has a range of KPIs that are directed internally on the efficiency and effectiveness of the audit process itself. All the KPIs have related targets.

In summary, the GIAA view their performance indicators as a pyramid where each level in the pyramid influences another (Figure 6).

Table 5. Internal KPIs in the GIAA

Objective	KPI	Target
Maximizing the amount of time spent directly on audit work.	The proportion of total working hours spent on direct audit activity.	Direct hours should be in excess of 80% of total hours available.
Individual assignments are completed on time and within budget.	Actual versus budgeted time and resources.	Audits to be completed to time and within the budget set.
The annual audit plan is substantially completed during the financial year.	Planned audits that have reached the draft report stage within the financial year.	Delivery of 90% of audit work to the draft report stage by the end of the financial year (31 March).
Clients have a high level of satisfaction with the conduct of the audit and the output of the audit process	Responses to standard questionnaire on a scale of 1 to 10, where 1 is poor and 10 is excellent.	Client survey questionnaire feedback should score an average of 80%.

Figure 6. A layered approach to KPIs in the UK

Annual Impact Questionnaire — Ascertain the penetration and coverage of GIAA work.

Assignment Questionnaire — Ensure assignment level feedback is reviewed, analyzed, and acted on.

Standard KPIs — Some shared with clients & some held internally to improve performance

Austria

Being part of an organization, the Internal Audit Department of the Ministry of Finance of Austria (IAD) aligns with the strategies, objectives, and risks of the organization and is insightful, proactive, and future-focused. It sees the audit universe very broadly: "What could be managed can be audited."

Performance indicators of an internal audit department are seen as means of measuring the extent to which it meets its objectives. These objectives are focused on audit specific (i.e. internal) issues but also linked to organization wide (i.e. external) issues. The following clear principles apply to internal audit department KPIs:

a. Only what is performed by the internal audit department can be subject to a performance indicator or KPI.

b. Performance indicators are linked to internal audit department objectives.

c. Objectives are shown on the internal audit department's balanced scorecard, which must also include all KPIs (none should be outside the balanced scorecard).

The KPIS developed by the IAD focus on 3Es – economy, efficiency and effectiveness (Figure 7) – derived from the standard management framework for meeting objectives by using inputs (resources) to carry out activities that create outputs, outcomes, and effects/impacts (Figure 8).

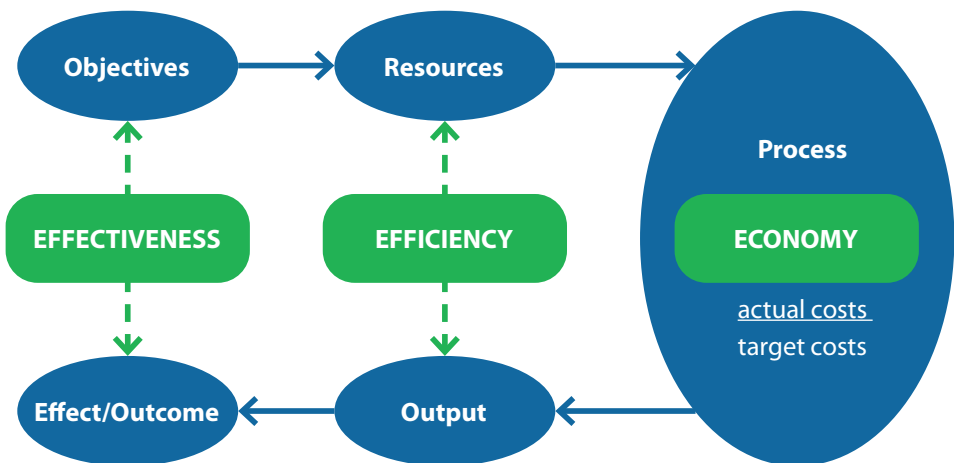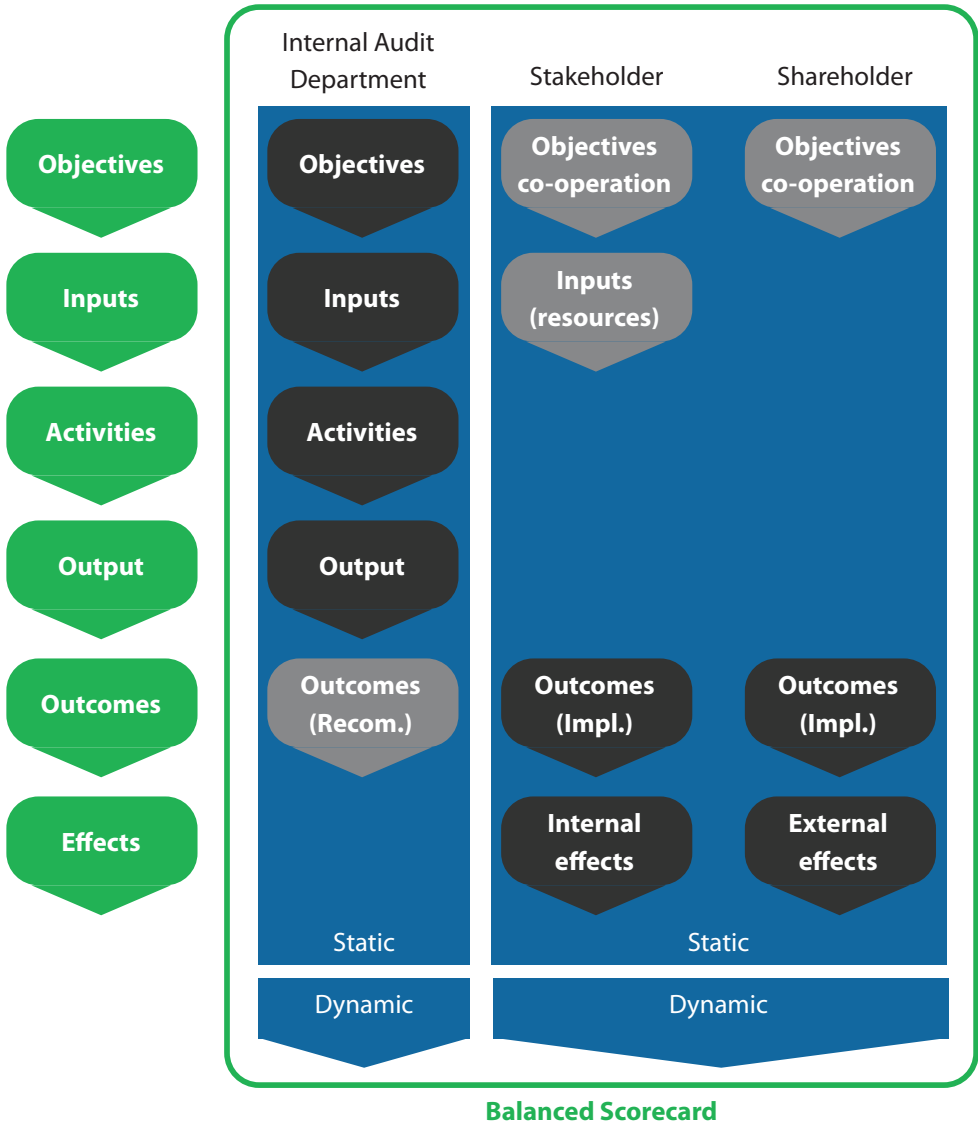**Figure 7. Measuring Economy, Efficiency, and Effectiveness**

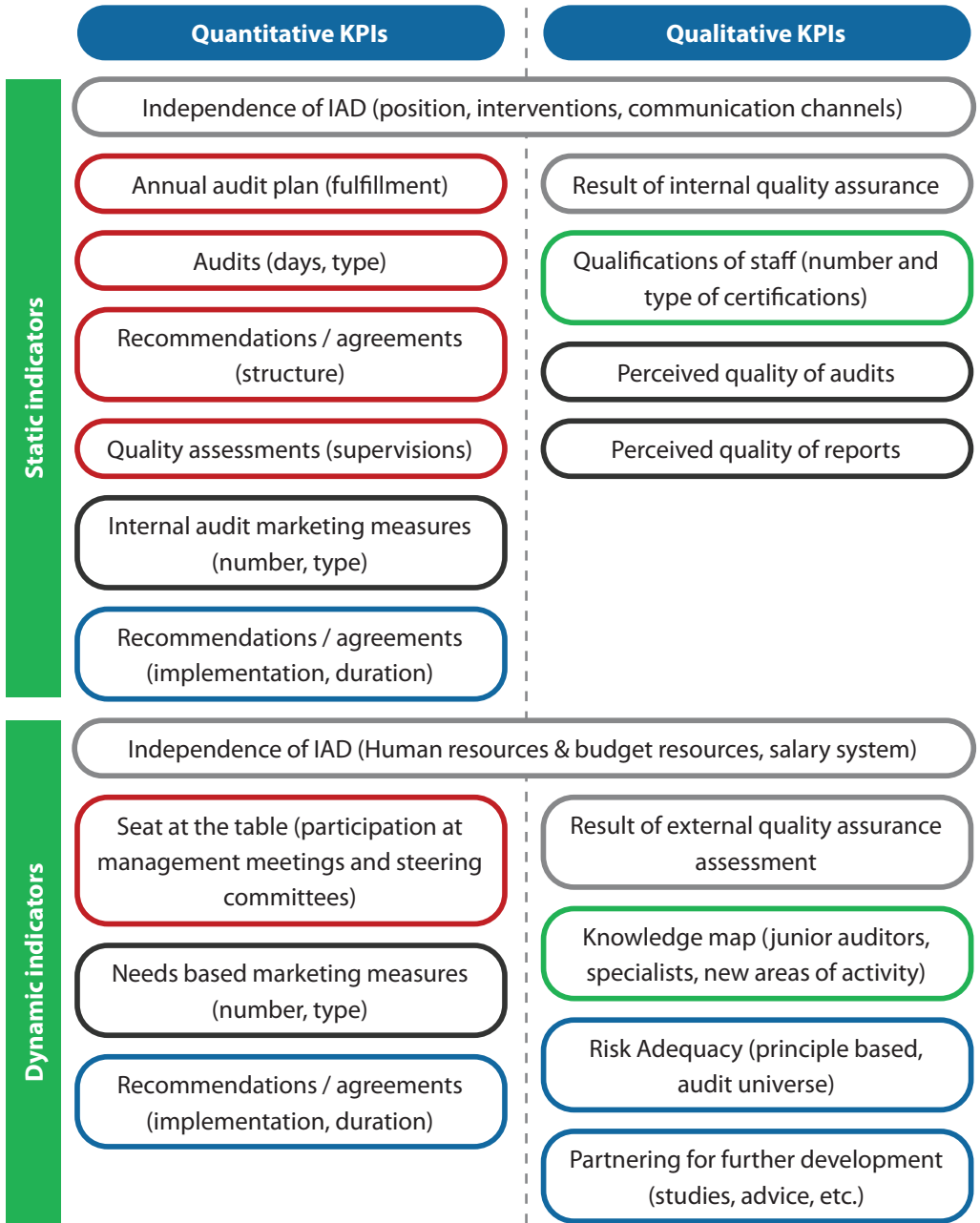## Figure 8. The balanced scorecard used by IAD, Austria

The IAD seeks to address different strategic perspectives and goals when developing their KPIs (see Table 6).

The IAD also seeks to distinguish static KPIs, that are measured annually, from dynamic KPIs, that are measured over a period of 4 years (see Figure 9). KPIs themselves can be grouped in quantitative and qualitative measures.

Table 6. IAD Strategic Perspectives and Goals

Strategic Perspectives	Strategic Goals	Focus on
1. Strategic Alignment – IAD strategy is aligned with its clients.	IAD focusses on the effectiveness of client activity.	Effectiveness
2. Learning & Growth - IAD staff are prepared to do their work.	IAD seeks continuous improvement in its maturity.	Inputs
3. Processes - IAD processes are standardized and result-oriented.	IAD has strong reputation for the quality of its audit work.	Activity (auditing, consultancy)
4. Customers - IAD takes care of its administrative environment.	IAD cooperates with management to make the public administration "fit for the future".	Activity (Cooperation)
5. Fiduciary & Value - IAD activities lead to improvements in the work of the public administration.	IAD creates value added for the public administration it audits.	Output & Outcomes

Figure 9. Static and Dynamic KPIs for IAD

Quantitative KPIs	Qualitative KPIs

Static indicators

Independence of IAD (position, interventions, communication channels)

Quantitative KPIs	Qualitative KPIs
Annual audit plan (fulfillment)	Result of internal quality assurance
Audits (days, type)	Qualifications of staff (number and type of certifications)
Recommendations / agreements (structure)	Perceived quality of audits
Quality assessments (supervisions)	Perceived quality of reports
Internal audit marketing measures (number, type)	
Recommendations / agreements (implementation, duration)	

Dynamic indicators

Independence of IAD (Human resources & budget resources, salary system)

Quantitative KPIs	Qualitative KPIs
Seat at the table (participation at management meetings and steering committees)	Result of external quality assurance assessment
Needs based marketing measures (number, type)	Knowledge map (junior auditors, specialists, new areas of activity)
Recommendations / agreements (implementation, duration)	Risk Adequacy (principle based, audit universe)
	Partnering for further development (studies, advice, etc.)

Legend

Processes   Learn & Grow   Customer

Strategic Alignment   Fiduciary & Value

The IAD takes account of the following in developing KPIs:

- That the right things are being measured: what is done may not be what has to be done.

- The number of indicators needed to provide an accurate and balanced summary of the effectiveness of an internal audit unit. The reliability of the data used to generate performance indicators.

- The range of data that may be available to measure these key elements of internal audit performance. If appropriate, a small combination of parameters is preferred, especially regarding quality indicators.

- The overlapping areas of the indicators of the economy, efficiency, and effectiveness of internal audit work are preferred instead of an isolated view.

- How internal auditors can best capture data on the level of client satisfaction with the results of internal audit examinations. Relevance of internal audit clients' views.

- Data to show the further development of the IAD.

One of the main challenges for the IAD is to ensure that quality is maintained throughout the process of defining, collecting, and reporting on KPIs. The indicators must be resilient and the IAD needs to be agile in using the indicators that are most relevant as the maturity level increases.

The problem of data manipulation is most severe when only one indicator is reported – this is because data of a single parameter can always be manipulated (directly or indirectly). However, it will rarely be possible to manipulate data that addresses the whole picture by including a mixture of (a) quantitative & qualitative data; (b) annual and longer-term data; and (c) internal and external data.

European Commission

The European Commission has an organization-wide strategic planning and programming cycle with a standardized performance management framework. Its purpose is to help ensure that the European Commission achieves its objectives in an efficient and effective manner. Data on performance is publicly available. This applies equally to the IAS, who must also comply with the International Standards for the Professional Practice of Internal Auditing on Quality Assurance and Improvement. The IAS develops and reports on KPIs against three objectives, as set out in table 7.

Main data sources

The main sources of data used by the IAS are:

- Annual stakeholder survey;

- Auditee satisfaction survey after each engagement;

- Regular internal monitoring of key data related to the audit process (for example: elapsed time for different stages of the audit, budgetary plans and results, hours spent on direct audit work);

- Report of the internal quality assessment carried out by the quality assurance cell;

- Report of the independent external quality assessor.

Table 7. Objective and KPIs for the IAS

Objective /KPI	Comments
Objective 1: To ensure that the work of the IAS adds value to its stakeholders	
KPI 1.1 - Level of satisfaction of stakeholders (audit committee/management boards and senior management of directorates).	Measured through an annual stakeholder survey.
KPI 1.2 - Level of auditee satisfaction.	Measured after every audit engagement.
KPI 1.3 - Timely delivery of IAS overall opinion on financial management in the Commission.	Provided for the Commission only.
KPI 1.4 - Timely delivery of IAS conclusion on the state of internal control (contribution to Commission services' annual reports).	Provided for the Commission only.
Objective 2: To ensure that the work of the IAS is of high quality	
KPI 2.1 - General conformance with the internal methodology and guidelines of the IAS and with international internal auditing standards as assessed through internal quality assessment.	An internal quality assurance team reviews the quality of work undertaken. There is an external quality assessment of IAS every five years in line with the standards.
KPI 2.2 - General conformance with the internal methodology and guidelines of the IAS and with international internal auditing standards as assessed through external quality assessment.	
Objective 3: To ensure that the IAS is efficient and effective in delivering its audit plans	
KPI 3.1 - Completion rate of the annual audit plan.	Measures the efficiency of the overall audit process.
KPI 3.2 - Percentage of time spent on direct audit work and audit support work by auditors.	A similar metric to that used in the UK (see Part 4, section "United Kingdom")

Objective /KPI	Comments
KPI 3.3 - Timeliness of the completion and the delivery of audit reports (time elapsed in working days between the findings validation meeting and the final report).	Many internal audit units track these KPIs as they are important indicators of internal efficiency and how effectively audit work was carried out.
KPI 3.4 -Difference between actual time and budgeted time for each audit engagement.	

Requirements and challenges

Performance measures will only be as good as the quality of the objectives set for an internal audit activity. All objectives should therefore be SMART (see page 8).

The internal audit unit should measure achievement or progress towards the objectives against key points of reference or "baselines". Performance should itself be tracked against set targets. Where these targets are long-term, milestones should be set to measure short-term gains. There must be reliable data underlying KPIs. The IAS uses the RACER mnemonic to assess the veracity of its KPIs (see page 8).

Like the UK GIAA, the IAS makes extensive use of surveys at the end of assignments and once a year at the overall client level. As with all surveys, getting response rates above 35% can be a challenge without active follow-up.

The European Commission example shows how internal audit units are able to meet international standards while also complying with the performance measurement system established for the organization as a whole.

Part 5.
Four key areas for consideration in the use of KPIs
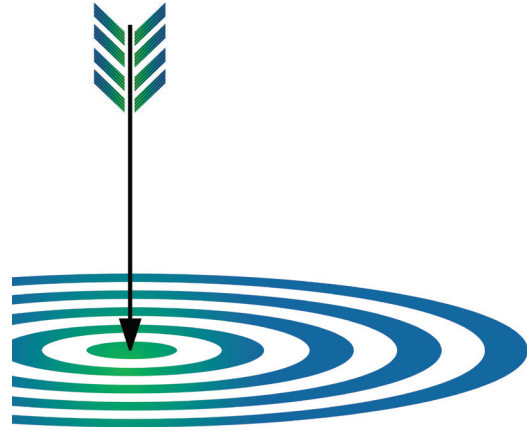
This part of the report considers four important questions identified by the IACOP as particularly relevant for internal audit units seeking to further develop the use of KPIs:

1. How should management be involved in developing KPIs?

2. Should personal performance rewards be directly linked to KPIs?

3. How long is the transition process to develop good KPIs?

4. How will the COVID-19 pandemic impact the use of KPIs?

1. How should management be involved in developing KPIs?

The quality required of internal audit is largely determined by recipients of the service or stakeholders. This represents in some respects a negotiation between internal audit and its clients. Auditors rarely ask their auditees about the questions in the client satisfaction surveys, for example. Internal audit should sit down with management and discuss the kind of survey questions they should be asking.

The perception of what is added value will vary between auditors and management. It is therefore important to understand what management consider to be activities that are adding value. In the UK, GIAA actively engage to understand what management see as the value coming from internal audit and to capture this in the audit activity MOU. They therefore report back on the KPIs as indicated/suggested in the MOU.

KPIs are totally different from compliance. Compliance is a minimum value - not added value. Compliance with components of the IPPF is a basic requirement of an internal audit function and should not be considered a key performance indicator.

2. Should personal performance rewards be directly linked to KPIs?

The IACOP are not aware of many (if any) cases in the public sector where pay is directly linked to performance measured through KPIs. Different jurisdictions approach performance rewards differently, some examples include:

- Austria has a performance related pay system which amounts to about one month's salary. This is linked to the balanced scorecard but not to any one KPI. This reward system also takes into account feedback from auditees.

- The UK does not have a reward system directly linked to KPIs. A previous system of this type was found not to promote the right behaviors, for example there were situations where people held back on reporting critical findings to ensure they got a good score in their client feedback survey. The pay system is instead linked to assessment of individual performance.

- There is no system of direct links to KPIs for the reward system in the European Commission.

3. How long is the transition process to develop good KPIs?

It is difficult to predict the timeframe for developing a robust set of KPIs. The main consideration is that they are relevant to the organization and are able to develop over time in line with stakeholders' needs. It makes more sense to establish a logical sequence of developing KPIs rather than impose a specific target time frame by when it should be done.

4. How will the COVID-19 pandemic impact the use of KPIs?

The COVID-19 pandemic is likely to have three impacts on the KPIs in use by internal auditors.

- While the indicators themselves will not change, the absolute number of assignments might change. For example, there could be a significant shift from assurance to consultancy assignments.

- Some units have added indicators related to the well-being of their staff, for example: how are they feeling about their work and how are they feeling about returning to work?

- This is an obvious situation where internal audit may be unable to achieve the results expected because of the pandemic. Some KPIs may need to be changed for next year.

Part 6. The central harmonization component of the internal audit function
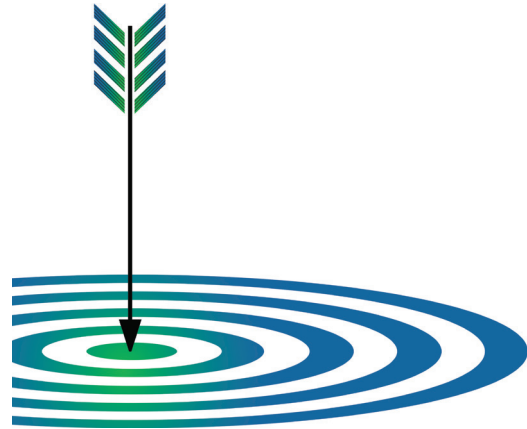
Most PEMPAL countries have an organizational unit (usually located in the Ministry of Finance) with specific responsibility to develop policies, laws, manuals, and guidelines relating to internal audit and internal control. The European Union has captured this concept of "central harmonization" by referring to such units as CHUs.

Some PEMPAL countries have one CHU for financial management and control and another one for internal audit. Other countries have one single CHU that covers both areas.

The main roles of the CHU are:

- To develops the laws, regulations, standards, norms, and guidance needed to implement effective internal control and internal audit.

- To monitor the implementation of the application of these norms and guidance over time.

- To update norms and guidance as necessary.

- To develop and implement training and capacity development activities as this is a crucial element of successful transformation.

Helping internal audit units establish KPIs

The CHU has an important role in helping internal audit units to establish KPIs that reflect the maturity of internal audit in the country and the different needs and expectations of the stakeholders of each unit. This means the CHU should take a tailored approach to the requirements of each unit and not simply develop a standardized list of KPIs and distribute this for implementation.

The CHU should also avoid falling into the trap of developing too many indicators. KPIs should reflect the information most important for management to review. The Central Audit Service (CAS) of the Netherlands, which supports a number of bilateral projects with

CHUs, points to examples of monitoring and tracking a huge number of indicators. This can lead to bureaucracy, frustration, lack of focus, lack of engagement, and thick reports which management is unlikely to read. The CAS reminds CHUs that the 'K' in KPI stands for 'key' and to be modest in their number. By way of example, the CAS currently has approximately 15 KPIs. While additional relevant information is gathered, much of it is more appropriate to internal governance (e.g. sick leave percentages, education costs, etc.) and does not need to routinely appear on the main dashboard of senior management unless they turn orange or red.

One of the best ways that the CHU can support internal audit units is to help improve the technical skills related to different techniques and methods for developing and reporting on KPIs. Most internal audit units would welcome advice on what to do and more importantly what not to do.

CHUs can also encourage the development of progressive indicators – for example, where does the internal audit unit want to be in year +1 or in year +2. KPIs should not be static but a dynamic ongoing process and the CHU can be a great help here.

CHUs should lead by example and establish KPIs for their support role

In addition to supporting and helping internal audit units to implement KPIs, CHUs should design their own KPIs based on the main responsibilities and the objectives established for the CHU. Typical areas of focus could be quality assurance missions and the training of internal audit staff as shown in Table 8.

The CHU will also want to establish KPIs for monitoring the development of internal audit activity at the national level (see table 9). For example, whether internal audit units are providing the CHU with annual activity reports so that the CHU can make a collated report to government on the national situation relating to the development of internal audit.

Table 8. KPIs for CHU Activity

Area	Indicator	Comments
Assessing the quality of internal audit work.	The percentage of all internal audit units that receive a CHU quality assurance mission each year.	In some countries quality assurance is realized once every 5 years, i.e. each year the audit universe is 20% of the total number of eligible entities. This indicator can measure the level of development of CHU. The target can go up to 100%, depending on the resources available at the CHU and maturity of the internal audit function.
	Percentage of quality assistance missions undertaken by the CHU in one year against the number of missions planned.	This is an indicator for planned activities taking into account the resources that exist at the level of CHU. The target should be 100%.
Training of individual auditors.	The percentage of auditors trained each year.	This indicator provides information about CHU general capacity to train auditors.
Extent to which CHU annual training plan is completed.	The percentage of planned training sessions delivered by the CHU each year.	The target should be 100% (including virtual training provided during pandemics or for more efficient training delivery).

Table 9. KPIs for monitoring internal audit activity at the national level

KPI	Comments	Possible CHU actions
Internal audit units created nationally		
Percentage of internal audit units created in entities which are required to have one.	This indicator measures the extent of the internal audit function at the national level.	To promote the creation of internal audit units, CHU should mount campaigns to raise awareness amongst departmental managers of the benefits and value-added of internal audit; CHU should consider imposing some sanctions for entities without an internal audit function in place.
The functioning of internal audit units nationally		
Percentage of internal audit units which are created and <u>functioning</u> in required entities.	This indicator measures at the national level whether internal audit units are capable of functioning. A functioning internal audit unit must have a sufficient number of auditors taking into account the audit universe and the skills necessary to audit certain areas (for example, IT). This indicator can provide information regarding the maturity of the internal audit function.	CHU should develop guidelines on the sizing of audit units taking into account the audit universe. The CHU can hold meetings with auditors to test out methods to identify the correct size of internal audit departments.

KPI	Comments	Possible CHU actions
Activities of internal audit units nationally		
Percentage of internal audit units who transmit an annual report on their activities to the CHU.	The annual report is an important input for CHU to develop a summary of the activities of the internal audit function at the national level.	CHU should provide clear guidance on the elements that need to be reported and support for the elaboration of the annual report. CHU should provide feedback on the quality of each report received.