

German Institute of Internal Auditors (IIR)

IIR Audit Standard No. 3

**Quality Management
in the internal audit activity**

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P R E A M B L E

(1) Quality management in the internal audit activity is a quality assurance and quality improvement program that encompasses all aspects of auditing work and ensures the continuous monitoring of its effectiveness. The purpose of quality management is to ensure, to a sufficient degree, that the work carried out by the internal audit activity contributes to adding value, and to improving the organization's operational processes.

(2) Responsibility for quality management lies with the chief audit executive, who should ensure that a quality management system commensurate with the size and structure of the internal audit activity and of the organization is put in place. The chief audit executive should further decide in what form the quality management components described in Chapter 1 are to be implemented in the internal audit activity. These procedures should be documented in an audit manual or audit charter.

(3) Quality management should be implemented in a structured process, taking into account the size and structure of the internal audit activity, and should thereafter undergo continuous development. Chapter 2 sets out a possible procedure for establishing such a system.

(4) Quality management should encompass all areas of audit activity. The requirements relating to it are listed in detail in Chapter 3.

(5) To assist the process of quality monitoring, quality criteria are set out in Annexes 1 and 2 in the form of checklists. These criteria form the basis for assessment of the internal audit activity by the chief audit executive, by an internal assessment or by an external quality monitoring mechanism.

Quality management in the internal audit activity

Contents

- 1 The components of quality management**
 - 1.1 Definitions
 - 1.2 Principles
 - 1.3 Disseminating the quality management system
 - 1.4 Planning for quality
 - 1.5 Generating and controlling quality
 - 1.6 Monitoring quality
 - 1.6.1 Internal quality monitoring
 - 1.6.1.1 Project supervision
 - 1.6.1.2 Internal assessments
 - 1.6.1.2.1 Control by means of quantitative indicators
 - 1.6.1.2.2 Quality assurance reviews
 - 1.6.1.2.3 Client questionnaires
 - 1.6.1.2.4 Benchmarking
 - 1.6.2 External quality monitoring
 - 1.6.2.1 Certification
 - 1.6.2.2 Quality assurance and peer reviews (external assessments)
 - 1.7 Improving quality
 - 1.8 Responsibility
 - 1.9 Special circumstances

- 2 Establishing a quality management system**
 - 2.1 Initial implementation
 - 2.1.1 Defining the quality policy
 - 2.1.2 Identifying areas for action
 - 2.1.3 Creating the necessary structures
 - 2.1.4 Drawing up quality specifications and defining quality criteria
 - 2.1.5 Disseminating the implementation process
 - 2.2 Ongoing quality management

3 Fundamentals of quality assurance in the internal audit activity

- 3.1 Aims
- 3.2 Scope of operation
- 3.3 Structure
 - 3.3.1 Organizational status of the internal audit activity
 - 3.3.2 Structure of the internal audit activity
- 3.4 Budget
- 3.5 Specialist activities
 - 3.5.1 Planning an engagement
 - 3.5.2 Performing an engagement
 - 3.5.2.1 Preparation
 - 3.5.2.2 Auditing
 - 3.5.2.3 Reporting
 - 3.5.2.4 Follow-up
- 3.6 Periodic reporting
- 3.7 Staff
 - 3.7.1 Selection
 - 3.7.2 Development/professional training
 - 3.7.3 Management
- 3.8 Legislation, standards, professional guidelines

Annexes

- Annex 1 Selected quality criteria
- Annex 2 Selected extracts from client questionnaires

1. The components of quality management

1.1 Definitions

Quality comprises all the features and characteristics of a product or activity that relate to its ability to meet defined requirements.¹

Quality management in the internal audit activity is a quality assurance and quality improvement program that encompasses all aspects of auditing work and ensures the continuous monitoring of its effectiveness. The purpose of quality management is to ensure, to a sufficient degree, that the work carried out by the internal audit activity contributes to adding value and to improving the organization's operational processes.

1.2 Principles

In line with the definition of the terms "quality" and "quality management", the main principles of successful quality management are:

- a focus on the client (e.g. engagement client, activity to be audited) and a quality policy clearly defined on that basis;
- systematically structured operational procedures;
- active staff involvement;
- open communication flow regarding the quality improvement process;
- sufficient flexibility to enable adaptation of the quality management system to meet new requirements.

These principles will form integral components of an effective quality management system, which can be seen as a cycle incorporating the following phases:

- presenting the quality management system;
- planning for quality;
- generating and controlling quality;
- quality monitoring;

- improving quality.

Ensuring a high level of quality not only constitutes a sound working basis for the internal audit activity; it also provides the organization with a significant competitive advantage.

1.3 Disseminating the quality management system

As an important aspect of quality management, the quality policy and associated quality objectives must first be defined and disseminated. In doing so, organizations that operate internationally must bear in mind that different cultures and value systems, different legal frameworks² and special economic circumstances³ in particular countries may have a significant influence on the way organizations are managed, and thus on the operation of the internal audit activity (see Section 1.9 "Special circumstances"). As a result, these various cultural, legal and economic factors also influence quality policy, which must strive to integrate such national differences as effectively as possible in order to achieve a high level of quality across the entire organization.

Based on the quality policy and objectives, the fundamental conditions for a viable and effective quality management system must be created. To ensure the requisite degree of transparency and commitment, both the quality policy and the quality management system, including its individual components, must be documented and communicated, for example in the form of a quality management manual.

1.4 Planning for quality

Quality planning incorporates the selection, classification and definition of quality criteria on the basis of the defined quality policy and objectives. These are taken, for

¹ *Deutsche Gesellschaft für Qualität e.V.* (German Quality Institute, DGQ), "*Begriffe zum Qualitätsmanagement*" (Quality Management Terms), 6th edition 1995, p.30, and *Deutsches Institut für Normierung e.V.* (German Standards Institute), Part 11 of DIN Standard 55350 (new) 1987

² For example, German corporate governance legislation (KonTraG), which decrees a strict separation of powers between Executive Board and Supervisory Board; EU regulations governing the organization of companies' internal control systems; alignment of the framework conditions of the EU-wide legal norms for corporation law

³ Examples include typical shareholder structures and the , structure of equity capital financing.

example, from legislation, regulations on corporate governance structures⁴ and professional standards⁵. As part of the process of continuous quality improvement, quality planning also incorporates ideas and suggestions for improvement resulting from benchmarking and ideas management. The defined quality criteria should be mandatory and measurable (see Annex 1 "Selected quality criteria").

1.5 Generating and controlling quality

Based on the results of quality planning, action should be taken to implement defined quality criteria. In the first instance this might involve, for example, the formulation of detailed guidelines and operational instructions for the various engagements and tasks of the internal audit activity, as well as the development and implementation of procedures and methods to support auditors in their work. To ensure effective, timely control, quality metrics and indicators must be developed and regularly analyzed by the chief audit executive, to enable appropriate action to be taken promptly in the event of discrepancies (see Annex 1 "Selected quality criteria").

1.6 Monitoring quality

The purpose of quality monitoring is to investigate the extent to which a unit meets the defined quality criteria. Based on the classification used by the Institute of Internal Auditors, quality monitoring activities can be broken down as follows:

- Internal quality monitoring carried out by the internal audit activity itself (internal assessments)
- External quality monitoring and peer reviews (external assessments)

In the first instance, quality monitoring is the task of the relevant managers and falls within their managerial responsibilities (see Section 1.8 "Responsibility").

By rating the individual quality components on a scale, a quality benchmark can be developed which enables neutral measurement to take place. For notes on assessment by the internal audit activity or by external parties, see Annex 1 "Selected quality criteria" and Annex 2 "Selected contents of client questionnaires".

⁴ E.g. KonTraG, or "Minimum requirements for organization of the internal audit activity in banks", issued by the German Federal Banking Regulator

⁵ E.g.: "Standards for the Professional Practice of internal Auditing" issued by the IIA and IIR

1.6.1 Internal quality monitoring

1.6.1.1 Project supervision

An important element of quality monitoring is project supervision (project here standing for an audit engagement). By means of regular quality checks, this enables compliance with quality standards to be monitored in the course of ongoing audit work. Project supervision should be carried out at various levels, in the first instance by the audit manager responsible for the engagement, who may be involved in the audit work itself. More experienced managers, such as the heads of units within the internal audit activity in whose area of responsibility the engagement falls, should then be involved, and ultimately the chief audit executive.⁶

1.6.1.2 Internal assessments

1.6.1.2.1 Control by means of quantitative indicators

Control by means of quantitative quality indicators can be achieved using metrics, e.g. by recording the effects of cost saving measures, or by measuring engagement duration.

1.6.1.2.2 Quality assurance reviews

The quality manager of the internal audit activity (chief audit executive, or quality management unit reporting directly to him/her; see Section 1.8 "Responsibility") should carry out quality assurance reviews in the form of self-assessments at regular intervals.

The main objectives of such reviews are:

- to identify shortfalls in quality and opportunities for improvement in operational processes and procedures, and
- to check and validate quality criteria in order to determine whether they are still up-to-date, adequate and valid.

⁶ Precise job titles will depend on the organization concerned.

In the light of quality assurance reviews the chief audit executive, together with the staff of the internal audit activity, should define specific, mandatory action to improve quality.

1.6.1.2.3 Client questionnaires

To assist quality monitoring, the client (e.g. engagement client, activity being audited) may be asked to respond to a questionnaire on completion of the engagement. This will involve rating, on a given scale, aspects of the engagement itself, or of the work carried out by the internal audit activity in general. Annex 2, "Selected contents of client questionnaires", contains a list of possible questions.

1.6.1.2.4 Benchmarking

Finally, performance comparisons can be used for quality monitoring purposes. For example, the internal audit activity may perform its own targeted benchmarking with comparable units in other organizations, either within the same sector or on a cross-sector basis. The objective is to develop better processes and methods through comparison with other units, for example through the IIR's own working groups⁷.

1.6.2 External quality monitoring

External quality monitoring is an important component of quality management.⁸ It provides the board, and other groups that rely on the work of the internal audit activity, with independent confirmation of the quality of work carried out.

External quality monitoring should be performed by qualified persons who are independent of the organization, who have no conflict of interest, and to whom no such conflict could be imputed.

⁷ An analysis of the IIR "Internal Audit 96" survey also provides useful information: German Institute of Internal Auditors (IIR), Frankfurt am Main, Internal Audit Association, Vienna, Swiss Institute of Internal Auditing, Zürich, "Internal Audit 96 – Survey Results"

⁸ Cf. IIA Practice Advisory No. 1312-1

1.6.2.1 Certification

Certification of the internal audit activity under ISO 9000 ff. constitutes a form of external quality monitoring. Approximately one quarter of the organizations who responded to a survey carried out among IIA members worldwide in 1994/95 were considering such certification. Some 15% were already certified.⁹

As motives for this step they cited the following advantages of certification:

- Clear formulation of a quality policy and quality assurance
- Description of the principles of effective audit work
- Written documentation of operational instructions and procedures
- Description of quality assurance action, as proposed in the IIA standards¹⁰
(supervision, internal assessments, external assessments)

1.6.2.2 Quality assurance and peer reviews (external assessments)

A part of the quality assurance review may be constituted by the statutorily required annual audit of financial statements.¹¹ For organizations not covered by the requirements of corporation law to this effect, external quality assurance reviews may take the following forms:

- a quantitative operational comparison in which the review is carried out by an organization in accordance with the relevant procedure, e.g. of the IIA in the USA,
or
- a qualitative approach in which the review is carried out by the internal audit activity of another organization, by external institutions or by external service providers¹² (peer review).

It is intended in the future to offer suggested frameworks and sectoral comparisons for use in such reviews via the German Institute of Internal Auditors (IIR).

⁹ Cf. Ridley, J.: The worldwide implications of ISO 9000 on the Internal Auditing, ISO 9000-News 1/1997

¹⁰ IIA Standards for the Professional Practice of Internal Auditing

¹¹ Obligation of joint-stock corporations listed on the stock exchange in accordance with § 317 of the German Commercial Code and obligation of banks in accordance with the "Minimum requirements for internal audit organization in banks" issued by the German Federal Banks Regulator

¹² See also the external auditors' peer review, IDW (German Institute of External Auditors), draft audit standard: Implementing quality monitoring in external auditing practice (IDW EPS 140, status: June 28, 2000)

1.7 Quality improvement

The overall objective here is to optimise audit work through a process of continuous improvement. Specific initiatives may be triggered by the internal audit activity's own staff and by audit clients, as well as by inter-organization and cross-sector benchmarking.

1.8 Responsibility

Responsibility for quality management lies with the chief audit executive. Where the internal audit activity is sufficiently large, it may be appropriate to create a quality management unit which reports directly to the him/her and works independently of the audit units themselves. In the following, the generic term "quality manager" is used to describe both these options.

As a superordinate and independent authority, the quality manager should initiate, facilitate and coordinate the requisite change processes, and support the specialist units within the internal audit activity in implementing the defined action.

Nonetheless, a separate quality management unit should have no authority over the audit units in the course of their normal work. Responsibility for conducting engagements (ex post and ex ante), including all specialist aspects such as the assessment of the activities being audited and the formulation of audit programs and audit processes, should remain with the relevant audit units.

1.9 Special circumstances

For organizations that operate across national borders, internationally accepted standards and checklists can be used to achieve a uniform level of quality in the internal audit activity that takes account of national differences to a large extent.

However, it must be noted that, for various reasons organizations in different countries may be managed in radically different ways. Such variation will be reflected in the operations of internal audit activities. The factors involved may be cultural, legal or economic in nature.

2. Establishing a quality management system

When establishing a quality management system in the internal audit activity the differing natures of the tasks to be carried out during initial implementation and in the course of ongoing audit work must be taken into consideration.

During both these phases, however, communication with the staff of the internal audit activity is of paramount importance. Thus audit units must be provided with up-to-date information about quality requirements and criteria, the future development of these, and the action to be taken. Conversely, the feedback and ideas provided by staff are crucial elements of the continuous improvement process.

2.1 Initial implementation

The first task during the implementation phase is to itemise existing operational procedures and instructions, in order to determine what quality rules and quality assurance tools are already in place. Based on this information, and in cooperation with the audit units, areas for action should be identified. These should then be used to develop quality criteria and minimum quality assurance requirements, to be set down in the form of quality specifications. Together with the audit units, the necessary action should then be initiated and incorporated in the internal audit activity's documentation, e.g. in the form of process descriptors or operational

instructions. Another task to be carried out in the implementation phase is to develop methods for ongoing (self-) monitoring, such as quality metrics or self-assessments.

In line with the above description, the following stages can be identified in implementation of a quality management system:

- Defining a quality policy
- Identifying areas for action
- Creating the necessary structures
- Drawing up quality specifications and defining quality criteria
- Disseminating the implementation process

2.1.1 Defining a quality policy

As a prerequisite for establishing an effective quality management system, it is first necessary to define a quality policy for the internal audit activity. This should be derived from the remit of the internal audit activity, as set out in its charter. It should include a clear statement of the nature and scope of the services to be provided (e.g. auditing, internal consultancy), and of the target client groups (e.g. board and/or senior management, subordinate reporting levels) and the approach to be adopted towards each of these.

2.1.2 Identifying areas for action

The areas where action is required in order to establish a quality management system should be identified on the basis of the defined quality policy. This task involves creating the necessary structures, defining quality criteria, and itemising the existing quality rules and quality assurance tools as a basis for formulating specific action.

2.1.3 Creating the necessary structures

The first task under this heading is to nominate a quality manager within the internal audit activity (as described in Section 1.8).

In view of the need to involve all audit staff in quality management, it is advisable to form quality teams whose membership covers the whole range of audit work. During the implementation phase, these teams should provide the driving force behind the quality and change process. They should be actively involved in all aspects of the implementation process, in which they should act as both participants and catalysts. Subsequently, once the quality management system is in place, they can act as "interface managers" between the operational audit units and the quality management unit within the internal audit activity, thus ensuring the necessary communication between all parties involved. As part of the continuous improvement process, they can act as critical and objective observers of audit work, and make timely immediate recommendations for improvement and act as (lead) reviewers in quality assurance reviews.

2.1.4 Drawing up quality specifications and defining quality criteria

During the implementation phase, an important task of quality teams is to define the minimum requirements for high-quality audit work and to draw up corresponding quality specifications. As set out in Section 1.4 above, a minimum basis for these latter is provided by statutory requirements, in particular those relating to corporate governance arrangements, such as the German legislation on transparency and control in corporations (KonTraG) or the "Minimum requirements for organization of the internal audit activity in banks" issued by the German Federal Banking Regulator. However, specifications should also incorporate the suggestions and requirements of other parties, both internal and external.

On the basis of the specifications, specific quality criteria should be defined. Corresponding mandatory and measurable quality and time standards should be applied to create a standardized framework that will enable the internal audit activity to carry out its tasks effectively and efficiently (see *Annex 1 "Selected quality*

criteria"). These standards should be documented in writing, for example in an audit manual.

Quality assurance tools should also be developed at this early stage. These include, for example: quality metrics, reviews of the internal audit activity's own projects, quality assurance reviews, self-assessments, interviews with the audit units and client questionnaires. Here, too, quality teams can provide valuable contributions.

2.1.5 Disseminating the implementation process

To ensure that quality management is transparent, measurable and mandatory, a corresponding project plan, incorporating responsibilities and a schedule, should be drawn up and disseminated. This is a crucial prerequisite for a common understanding of quality management and, consequently, for the successful implementation and consolidation of a quality management system.

2.2 Ongoing quality management

Once implementation is complete the primary objective is to consolidate the quality management system and to promote a process of continuous improvement. The first task in this regard is to put into practice the measures previously identified. Regular reporting on the defined quality metrics should provide information about the status of these measures and any deviation from the standards set, thus allowing timely corrective action to be taken if required.

At the same time, the quality manager should check whether the measures adopted are generating quality as planned, e.g. by carrying out quality assurance reviews. These should assess existing processes, and investigate the extent to which audit units are complying with set standards as well as the possible existence of quality shortfalls. As during the implementation phase, any action identified as a result requirements should be planned and executed jointly with the audit units.

In addition, the defined quality criteria should be reviewed in terms of their appropriateness and continuing validity, and undergo further development. During

this process, use should be made of the knowledge and ideas of staff, whose suggestions for improvement should be actively sought. Suggestions and requests made by audit clients, or comparisons with the audit units of other organizations, can also be utilized here. Possible means of generating such input include ideas management, client questionnaires, service level agreements and benchmarking.

The objective of ideas management is to make the best possible use of staff's knowledge and creative potential, in order to bring about a continuous and effective improvement in the quality of audit work. Ideas management provides a sound basis for driving the continuous improvement process and obtaining new ideas for further quality standards. All staff should be consulted and involved, to ensure that quality management is accepted and put into practice. Staff should be able to communicate directly with the quality manager, so that every auditor is genuinely in a position to put forward suggestions for improvement. Moreover, a mechanism to record the input of all auditors should be established, to prevent ideas from being lost.

Various methods can be used to determine the requirements of audit clients. Thus questionnaires can be used, e.g. when presenting the audit program, to identify additional priority audit areas for inclusion in the annual audit plan. In addition, both the parameters of agreed service provision and the corresponding quality expectations can be defined in contracts between a service provider and its client (service level agreements). For auditing purposes, service level agreements are required at a minimum in cases where audit tasks are either outsourced to third parties or insourced, e.g. carried out on behalf of subsidiary organizations.

3. Fundamentals of quality assurance within the internal audit activity

3.1 Aims

The internal audit activity performs independent and objective auditing (assurance) and consulting services, which are aimed at adding value and improving the organization's operational processes.

It supports the organization in achieving its objectives by evaluating in a systematic and targeted manner the effectiveness of risk management, control, and of management and governance processes, and by helping to increase such effectiveness.¹³

3.2 Scope of operation

The internal audit activity's field of operation should comprise the full range of the organization's activities, and can be broken down as follows:¹⁴

Audits of the organizations financial position and net worth, the reliability of accounting systems and information derived from them (financial auditing)

Audits of the quality, security, compliance with proper procedures, cost-effectiveness and functionality of the organization's structures, processes and systems, including the ICS (operational auditing)

Audits of management performance with regard to the organization's strategy and objectives, and with regard to implementation of the measures adopted in the light of these (management auditing)

Assessment of projects, structures and processes and, associated with this, provision of consulting to the organization (internal consulting)

3.3 Structure

3.3.1 Organizational status of the internal audit activity

The principle of independence and objectivity requires the internal audit activity to report directly to the board.¹⁵

Staff of the internal audit activity must not have any decision-making powers or responsibilities in relation to the activities that they audit.

¹³ German Institute of Internal Auditors (IIR), according to a resolution of the IIR Executive Board dated June 7, 2002

¹⁴ See also the "Minimum requirements for internal audit organization in banks" (Circular 01/2000 issued by the German Federal Banks Regulator) and BIZ Internal Audit in Banking Organisations and the relationship of the supervisory authorities with internal and external auditors (July 2000)

Like the internal control system (incorporating organizational security measures and internal controls), the internal audit activity is a basic component of the organization's internal monitoring system.

In order to perform its tasks effectively, the internal audit activity must have unrestricted active and passive information rights.

The purpose, authority and responsibility of the internal audit activity should be set out in a charter, which must be adopted by the board and disseminated throughout the organization.

3.3.2 Structure of the internal audit activity

The internal audit activity must have an organizational structure commensurate with its size and function. This will be influenced by the following factors:

Organization size

Economic sector or field of activity

National or global operations

The organization's complexity, and its managerial and governance structure

Security requirements of the organization

Statutory requirements, in particular those relating to corporate governance

The structure and operational procedures should ensure that auditors build up a deeper and more detailed knowledge of the activities to be audited.

The structure should be documented, e.g. on the basis of functional descriptors.

Staff should be required to sign a written undertaking to respect secrecy and confidentiality.¹⁶

3.4 Budget

The internal audit activity's budget must be adequate to ensure that its staffing level is commensurate with its tasks, in both quantitative and qualitative terms. Two developments are of especial importance in this regard. On the one hand, the introduction of new statutory requirements, in particular those relating to corporate governance (e.g. KonTraG), represent a new challenge to a high-quality internal audit activity as a component of an internal control system. On the other, account must be taken of increased staffing requirements resulting from the organization's

¹⁵ Based on the "Standards for the Professional Practice of Internal Auditing" issued by the Institute of Internal Auditors (IIA)

¹⁶ The principles underlying this issue are set out in the IIA Standards and Code of Ethics

strategic direction (e.g. globalization, rapid development in the area of IT).
Quantitative benchmarks can provide useful guidance for budget allocation.¹⁷

With regard to material costs, too, the budget must enable the chief audit executive activity to react to new developments.

3.5 Audit work

3.5.1 Planning an engagement

The following considerations form the basis for planning the engagements (over one year or several years):

Statutory requirements¹⁸

Systematic analysis of all operational processes, taking into account in particular risks and opportunities

Special requests from the board or senior management

Suggestions from inside and outside the internal audit activity

Steps must be taken to ensure that special audits not included in the plan that are required as a result of identified deficiencies or specific information needs can be carried out at short notice, and at any time.

The planning documents should be submitted to the board for approval.

The chief audit executive should monitor fulfilment of the plan of engagements. Where deviations are identified, these should be analyzed. Planning can be an effective control tool only if it is monitored consistently.

¹⁷ Cf. German Institute of Internal Auditors (IIR), Frankfurt am Main, Internal Audit Association, Vienna, Swiss Institute of Internal Auditing, Zurich, "Internal Audit 96 – Survey Results"

¹⁸ Including the "Minimum requirements for internal audit organization in banks" issued by the German Federal Banks Regulator

3.5.2 Performing an engagement

3.5.2.1 Preparation

Based on the plan of engagements, the schedule and sequence of the individual engagements can be developed.

During the preparation phase, it is essential for auditors to analyze the activity to be audited, familiarize themselves with the subject matter of the audit, carry out detailed planning of the audit procedures and obtain the relevant information.

Depending on the nature of the engagement, preparation may also involve providing advance notice of the audit.

3.5.2.2 Auditing

The audit methods and tools to be used will depend primarily on:

the nature and objectives of the engagement;

organizational factors;

the quality of the internal control system;

the importance of the activity to be audited;

potential risks.

Each engagement should be documented in accordance with proper procedures.

Documentation provides evidence that the engagement has been carried out properly and forms the basis for reporting.

3.5.2.3 Reporting

The content, language and format of reports are important aspects of quality in the internal audit activity.

The content and language must comply with the principles of completeness, truth and clarity, 'truth' being understood to encompass 'objectivity'.

As a minimum, all reports must contain statements relating to:

the scope and objectives of the engagement;

the performance of the engagement;

the activity audited;

the audit results;

action/recommendations (including responsibilities, deadline and prioritization)

All reports issued by the internal audit activity should have a standardized format to facilitate their understanding by recipients. Reporting should be concise and timely.

3.5.2.4 Follow-up

The internal audit activity should monitor whether the activities audited rectify any identified non-compliance, and implement the agreed action and recommendations by the agreed deadlines. Where necessary, follow-up audits should be carried out.

3.6 Periodic reporting

Reports should be issued periodically to the board and/or senior management, providing information on the internal audit activity's operations, on developments and on significant risks.

3.7 Staff

3.7.1 Selection

A suitable requirements profile should be drawn up to ensure that staff's technical and social competence, and training, are consistent with the internal audit activity's tasks.

Staff of the internal audit activity should work autonomously, and display a high level of responsibility, technical qualifications and trustworthiness. As a rule they should also possess professional experience and the potential for further development.

3.7.2 Development/professional training

Steps should be taken to ensure appropriate internal and external professional training for the internal audit activity's staff, who should be encouraged to improve their level of social competence and management qualifications.

At the same time – based on the organization's own human resources policy – a personnel development plan should be drawn up to map the career development of qualified staff inside or outside the internal audit activity.

3.7.3 Management

Standards and principles such as integrity, objectivity, confidentiality and competence are important not only for the internal audit activity's relations with the outside world; they apply also, and especially, to management practice within the internal audit activity itself. Such management practice must be based on the twin pillars of social and professional competence.

3.8 Legislation, standards, professional guidelines

Both knowledge of the relevant statutory requirements, in particular those relating to corporate governance, and compliance with the IIA and IIR standards are essential prerequisites for a consistently high level of quality.

Annex 1

Selected quality criteria

The following quality criteria constitute specific requirements to be met by a high-quality internal audit activity, and should be evaluated. Different rating systems may be used for this purpose (e.g. percentage values, marks on a 1-5 scale, or a positive / neutral / negative assessment).

These criteria form the basis for an assessment of the internal audit activity by the chief audit executive, by an internal assessment or by an external quality monitoring mechanism.

Contents

- 1 Structure; Organizational status of the internal audit activity
- 2 Budget
- 3 Planning
- 4 Performance
 - 4.1 Preparation
 - 4.2 Auditing
 - 4.3 Reporting
 - 4.4 Post-audit activities
 - 4.5 Follow-up
- 5 Staff
 - 5.1 Selection
 - 5.2 Professional development/ training
- 6 Management of the internal audit activity

1. Structure; Organizational status of the internal audit activity

- The purpose, authority and responsibility of the internal audit activity are documented in a charter.
- The charter includes, for example, statements on the internal audit activity's own structure, priority areas, the audit cycle, audit performance, reporting, and staff development and support.
- The charter is adopted by the board.
- The charter is disseminated within the organization.
- The charter indicates clearly that heads of operational units, plants or subsidiaries, and affiliated organizations can use the services provided by the internal audit activity (auditing and/or consulting).
- The internal audit activity's scope of operation comprises the full range of the organization's activities.
- The internal audit activity reports directly to the board, thereby ensuring its neutrality, independence, and freedom from restrictions in its auditing and consulting work.
- The internal audit activity's structure, composition and operational procedures ensures that staff can acquire a sound basis of knowledge, and apply this in audit engagements.
- The internal audit activity operates independently of all other functions.

2. Budget

- Staffing is commensurate with the tasks of, and requirements on, the internal audit activity, in both quantitative and qualitative terms.

Rating

- The budget is also adequate to meet requirements in the area of material costs (e.g. IT equipment, travel costs, training and professional development).

3. Planning

- A standardized, risk-oriented planning process is in place.
- All engagements for a particular planning period are grouped together systematically and submitted to the responsible member of the board or senior management for approval.
- Planning takes into account statutory requirements, specific requests from the board and/or senior management, and suggestions received from inside and outside the internal audit activity.
- Resource planning (human resources and material budgets) is carried out on the basis of an itemized work program agreed with the responsible member of the board or senior management.
- A standardized methodology is developed for the systematic analysis of the potential risk associated with the activities to be audited.
- All activities to be audited are mapped fully in order to establish an outline plan, or a plan covering several years.
- The range of activities to be audited is checked regularly to ensure complete coverage is maintained.
- Authorizations are established for changing the risk scoring method and the activities to be audited.
- Capacity planning provides adequately for any ad hoc special investigations and follow-up audits which are not included in the initial plan but may prove necessary.

Rating

4. Performance

4.1 Preparation

- Based on the engagement program (plan), the schedule and sequence of activities to be audited is drawn up, and the corresponding resource allocation and responsibilities established.
- Before the start of each engagement, a timetable – and thus the engagement duration – is established.
- The activity to be audited is analyzed and the requisite information obtained.
- The audit methods to be employed are identified.
- Advance notice is provided to the activity to be audited (with the exception of audits that become necessary as a result of illegal acts).
- Broad audit objectives are defined .
- The engagement work program (engagement plan) is approved by the chief audit executive or a person nominated by him/her.

4.2 Audit

- The engagement is carried out at the client site in accordance with the audit program.
- Engagements are carried out in compliance with statutory requirements, organization-specific regulations, the organization's aims, etc.
- Engagements also take into account criteria such as cost-effectiveness, profitability and effectiveness.
- Engagements are e carried out with the aim of identifying opportunities for improvement.
- The audit results are agreed on an ongoing basis with the audited activity and the audit manager.
- If, during an engagement, it becomes necessary to adjust the audit schedule, this is done at the client site and with the agreement of the chief audit executive.

Rating

- The progress of the engagement is checked regularly against the engagement work program.
- A final meeting is held with the head of the audited activity, in which the main audit results are presented and agreed.
- At the final meeting, action and deadlines for its implementation are agreed. It is confirmed that all parties are in agreement with the audit results; any objections are raised at this point.
- The engagement procedure and audit results are documented in a standardized way in accordance with proper procedures.
- Audit results are evaluated consistently using standardized rating methods (common principles for all engagement types and activities to be audited).
- Working documents are maintained in accordance with proper procedures.

4.3 Reporting

- The content and language of reports respects the principles of completeness, truth, clarity and objectivity.
- All reports contain statements relating to
 - scope and objectives of the engagement;
 - performance of the engagement;
 - activity audited;
 - audit results;
 - action/recommendations, with deadlines
 - allocation of responsibilities and priorities
- A standardized reporting format is used for all engagements and activities to be audited.
- Draft reports are submitted to the head of the audited activity in good time prior to the final meeting, and position statements obtained from all parties.
- Reporting, and the issuing of reports and lists of action to be taken, is done in a timely manner.
- The distribution list for reports is applied in accordance with standard procedures.

Rating

4.4 Post-audit activities

- Feedback meetings/project reviews are conducted by the chief audit executive, or a person nominated by him/her, with the entire audit team and, where appropriate, the quality manager, within a reasonable period of time following the audit,.
- In the light of the feedback meetings, adjustments to audit methods and processes, and to resource plans, are made where necessary.
- Risk assessments are updated shortly after each engagement; standardized criteria are available for this purpose.
- Shortly after each engagement, a comparison is made between resources planned and actually deployed, in particular the number of days spent on the engagement, and where necessary adjustments are made before the next engagement is undertaken.
- Knowledge of general interest gained in the course of the engagement is made available to all audit staff (knowledge management).
- Retention procedures and periods for audit reports and documentation are laid down.

4.5 Follow-up

- The internal audit activity monitors implementation of action documented in audit reports in accordance with the agreed deadlines.
- Where necessary, follow-up audits are be carried out.
- Any extensions to deadlines for the implementation of action are documented.
- At least once a year the board and/or senior management are informed about any failure to implement agreed action where no recognized reason exists.

Rating

- Criteria are established to enable the need for a follow-up audit to be determined, along with a maximum period within which such an audit is to be carried out. The methods to be used is clearly defined and generally applicable.

5. Staff

5.1 Selection

- For the purpose of staff selection a requirements profile is defined.
- Staff's technical and social competence, and training, is consistent with the internal audit activity's tasks.
- Staff selection takes place strictly in accordance with the predefined profile, which might include technical, personality-related, linguistic and foreign-language requirements, as well as proven practical experience.

5.2 Professional development/ training

- Steps are taken to ensure that staff receive further technical and personality-related training by means of
 - programs within the internal audit activity (e.g. seminars on internal audit),
 - organization-internal courses (e.g. on management or language skills),
 - external programs (e.g. attendance at technical courses not offered within the organization, such as those preparing candidates for the CIA examination).
- Measures are adopted to enable staff to improve their level of social competence and obtain management qualifications.
- Qualified staff of the internal audit activity are eligible for assistance under the organization's staff development schemes.
- Qualified staff of the internal audit activity are included in the organization's management selection process.

Rating

- Training toward the CIA qualification is included in the staff's personal goals and target agreements.
- For each staff member, a career development plan is drawn up, and updated within the framework of the annual appraisal dialogues/target agreement. It takes into account factors such as audit tasks, strengths/weaknesses analysis, assessment of potential, staff's own career development targets and professional training programs.
- Staff members of the internal audit activity also take personal responsibility for keeping their specialist knowledge up-to-date, e.g. through participation in the activities of the German Institute of Internal Auditors (IIR), based in Frankfurt.

6. Management of the internal audit activity

- Periodic reports are submitted to the board and/or senior management, providing information on the activities of the internal audit activity, new developments and significant risks.
- Longer-term planning is carried out for the development of the internal audit activity in line with the organization's strategic planning.
- The chief audit executive holds periodic, informal discussions with the organization's external auditor.
- The chief audit executive possesses the requisite specialist skills and personal attributes to meet the challenges of this position.
- In principle, all actions agreed with audited activities are implemented.
- There is a high degree of acceptance of the results produced by the internal audit activity among the board, senior management and the heads of audited units.

Rating

- Through the actions implemented, the results of the internal audit activity's work contributes to the improvement in the organization's performance, efficiency, effectiveness, net worth and futureproofing.
- A quality assessment is carried out once a year.
- The chief audit executive takes steps to ensure that the principles set out in the internal audit activity's charter are put into practice.
- The staff of the internal audit activity are managed in a forward-thinking way; the chief audit executive takes steps to ensure their further professional training and development.
- Statutory requirements and both IIA and IIR standards are regarded as essential prerequisites for a consistently high level of quality.

Rating

Annex 2

Selected extracts from client questionnaires

Client questionnaires may be conducted on completion of engagements for quality assurance purposes, and may include the following questions:

- Were the engagement objectives communicated clearly and in good time?
- Was the engagement carried out within an appropriate period?
- Was the disruption caused to daily activities by the engagement kept to a minimum?
- Were the organization's object and strategies considered adequately in the engagement?
- Was information provided about the progress of audit work and its results during the engagement?
- Did the internal audit activity staff concerned exhibit professionalism while carrying out their tasks in the audited units?
- Do internal audit activity staff have sufficient practical experience?
- Were the conclusions logical and well-documented?
- Were the results reported with due care?
- Was the report written clearly and logically?
- Are the recommendations for action made by internal audit activity staff constructive and capable of being implemented?
- Did internal audit activity staff prepare the final meeting properly and in good time, and did they conduct the meeting in a professional manner?
- Did internal audit activity staff make every effort to maintain effective cooperation?

Rating

- In general terms, did the engagement result in value added for the organization?