

External Quality Assessment or “who audits the auditor”

The internal audit function is one of the fundamental checks and balances for sound corporate governance. Additionally, it bridges the gap between the board and management, and assesses the internal environment as well as the effectiveness and efficiency of operations. Last but not least, internal auditing safeguards and enhances the organization’s compliance with rules, regulations, and best business practices. Nowadays, leading organizations throughout the world universally recognize that a robust and objective internal audit function lies at the heart of their lasting success.

However, how robust and objective does the internal audit function have to be and who defines these qualities?

To give a definite, substantiated and unbiased answer to the above questions, organizations have gone to great lengths to ensure that their internal audit activities are conducted in accordance with the International Standards for the Professional Practice of Internal Auditing (the “Standards”). Adherence to the Standards brings about improved corporate governance, transparency, and public image, thereby boosting greatly the stakeholder’s confidence in the organization.

In order to determine compliance with the Standards, organizations must go through the external quality assessment process or Standard 1312- External Assessments.

“External assessments should be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization. The potential need for more frequent external assessments as well as the qualifications and independence of the external reviewer or review team, including any potential conflict of interest, should be discussed by the chief audit executive (CAE) with the Board. Such discussions should also consider the size, complexity and industry of the organization in relation to the experience of the reviewer or review team.” Standard 1312-External Assessments; enacted January 1st, 2002.

As a rule, external assessment covers the entire range of audit and consulting work performed by the internal audit function. The external assessment scope of work includes but is not limited to benchmarking, identifying and reporting of leading practices that could facilitate the internal audit function in becoming more efficient and effective.

The purpose of the external quality assessment is to:

- Assess the efficiency and effectiveness of the internal audit activity taking into consideration its charter, board expectations, management and the CAE.
- Evaluate the current needs and objectives of the internal audit function in conjunction with the future goals of the organization.
- Appraise the risk to the organization if the internal audit function is performing below satisfactory levels or is not in conformity to one or more of the *Standards*.
- Provide an opinion on the internal audit function’s conformity to the *Standards*.

The objectives outlined above can be accomplished by either an independent review by a qualified, independent reviewer/review team or a self-assessment with independent validation.

- *Independent review by a qualified, independent reviewer or review team – achieves maximum benefit for the internal audit function.*

Qualified individuals are persons with the technical proficiency, business experience, judgment, skills, and educational background appropriate for the audit activities to be reviewed. This could include internal auditors from outside the organization, outside consultants, or independent outside auditors, but preferably not the external audit firm that audits the organization's financial statements. Independence means not a part of, or under the control of, the corporate entity or other organizations to which the internal audit activity is related. Hence, the individuals should be free from any obligation to or interest in the organization subject to quality assessment.

- *Self-assessment with independent validation – a less costly alternative to comply with Standard 1312.*

The self-assessment follows a quality assessment process similar to the one for the independent review; however it is performed in house under the supervision of the CAE. The results of the self-assessment have to be validated by an independent review team. The independent review team has to meet the same qualifications as the ones for the external independent review.

Under either alternative, the quality assessments can be conducted through peer reviews instead of utilizing external service providers. Internal auditors from three or more different organizations come together to form a pool of professionals, all of whom must be qualified to conduct external quality assessments. However, administration of this process can be quite challenging because assuring appropriate composition and assignments of the teams is essential. Ensuring the necessary independence and objectivity can also be challenging. Reciprocal peer reviews between two organizations does not pass the independence test.

Besides Standard 1312, six new quality assurance standards were implemented by the IIA on January 1st, 2002. They are as follow:

1300 – Quality Assurance and Improvement Program – “The Chief Audit Executive (CAE) should develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit (IA) activity and continuously monitors its effectiveness. This program includes periodic internal and external quality assessments and ongoing internal monitoring. Each part of the program should be designed to help the IA activity add value and improve the organization's operations and to provide assurance that the IA activity is in conformity with the Standards and the Code of Ethics.”

1310 – Quality Program Assessments – “The IA activity should adopt a process to monitor and assess the overall effectiveness of the quality program. The process should include both internal and external assessments.”

1311 – Internal Assessments – “Internal assessments should include:

- *Ongoing reviews of the performance of the IA activity; and*
- *Periodic reviews performed through self-assessment or by other persons within the organization, with knowledge of IA practices and the Standards.”*

1320 – Reporting on the Quality Program – “The CAE should communicate the results of external assessments to the board.”

1330 – Use of "Conducted in Accordance with the Standards" - Internal auditors are encouraged to report that their activities are "conducted in accordance with the Standards." However, internal auditors may use the statement only if assessments of the quality improvement program demonstrate that the IA activity is in compliance with the Standards.”

1340 – Disclosure of Noncompliance – “Although the IA activity should achieve full compliance with the Standards, and internal auditors with the Code of Ethics there may be instances in which full compliance is not achieved. When noncompliance impacts the overall scope or operation of the IA activity, disclosure should be made to senior management and the board.”

Is your organization ready to meet the requirements of the new quality assurance standards as well as undergo external quality assessment? - If not, Global Atlantic Partners LLC can help. We know that your company and your needs are unique. For this reason, we will take the time to understand the nature of your business and the environment in which you operate so that we can tailor our skills and knowledge specifically to your situation. If you need assistance with the development and maintenance of the Quality Assurance and Improvement Program, we will be there for you from the outset. Alternatively, if you are ready for your External quality assessment and you want it to be performed quickly and proficiently, GAP will execute it in a timely fashion with professional care.

The GAP team is comprised of CPAs and CIAs who have extensive experience working with financial service companies, public companies, private companies and non-profit companies. In addition to possessing current, in-depth knowledge of the Standards, our consultants are well-versed in the best practices of the audit profession and stay abreast of the latest developments and innovations. Last but not least, each of our lead consultants has more than 20 years experience in the internal audit management capacity.

In conclusion, if it is important for you to know “who audits the auditor” as well as whether your internal audit function adds value and improves your operations, call us. You will know the answer right away.