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The Institute of
Internal Auditors
Australia

Whitepaper

Balanced Scorecard Reporting

Updated 2023

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Balanced Scorecard Reporting

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Background

Purpose

This White Paper outlines a structured and practical approach for Chief Audit Executives (CAEs) to provide 'balanced' reporting to the Audit Committee and senior management on the performance of internal audit.

Background

Boards and senior management increasingly expect CAEs to report on both the value of the insights that internal audit delivers, as well as the performance metrics that facilitate effective oversight of the internal audit function. Exhibit 1 illustrates examples of common reporting practices beyond standard reporting on the results of individual audits.

The practices within the three upper boxes (themes-based reporting; collaborative reporting; and annual report on internal audit) provide insights to the Audit Committee and senior management, and facilitate collaboration with 2nd line of defence assurance functions.

This White Paper focuses on balanced scorecard reporting. Other White Papers are available for several of the additional reporting practices illustrated in the following diagram.

Exhibit 1 - Examples of high-level internal audit reporting practices

INSIGHTS DELIVERED BY INTERNAL AUDIT	Highest value	Themes-based reporting	Collaborative reporting	Annual report on internal audit
	Limited value	Standard internal audit report for each separate engagement	Internal audit staff competency profiling	Balanced scorecard reporting
		Absence of KPIs and fluent reporting	Quality assurance and improvement program, including internal and external reviews and benchmarking	Well founded KPIs with both qualitative and quantitative measures
		Limited performance visibility	Effective performance oversight	
PERFORMANCE OF THE INTERNAL AUDIT FUNCTION				

Discussion

Issue

The CAE is required under the 'International Standards for the Professional Practice of Internal Auditing' (Standard 2060 – Reporting to Senior Management and the Board) to report periodically to senior management and the board on the internal audit purpose, authority, responsibility, and performance relative to its plan and on its conformance with the Code of Ethics and the Standards.

The Global Internal Audit Common Body of Knowledge (CBOK) study in 2015 determined that 85% of internal audit functions use KPIs in one form or another to measure their performance¹. The study also encouraged CAEs to drive towards a better blend of both inward-facing and outward-facing measures, which are both qualitative and quantitative in nature. A useful way of depicting the KPIs in a structured reporting manner is to utilise a balanced scorecard reporting approach.

The CBOK study also found:

- › About 57% of CAEs report their internal audit department is fully aligned or almost fully aligned with the strategy of their organisations; the remaining 43% are somewhat, minimally, or not aligned.
- › There was a six-fold increase in the use by CAEs of balanced scorecard reporting between 2010 and 2015 (increasing from 4% to 26%). The upward trend is expected to continue.

¹ Bruce Turner, GREAT Ways to Motivate Your Staff - Shaping an Audit Team that Adds Value and Inspires Business Improvement (Lake Mary, FL: The Institute of Internal Auditors Research Foundation, 2016), p 25

Balanced Scorecard Reporting

Balanced scorecards are designed to translate internal audit strategy into action with the aim of helping to manage and measure the performance of the internal audit function, and, consequently, achieving alignment with organisational strategies. They are becoming an increasingly well-established means for reporting quantitative and qualitative KPIs to the audit committee in a balanced way.

History

Internal audit effectiveness

The mission of internal audit is to “enhance and protect organisational value by providing risk-based and objective assurance, advice and insight”²². The catalyst for achieving the mission is a capable, well-credentialled auditor cohort with a strong performance culture.

An internal audit function’s performance culture is driven by absolute clarity of the organisation’s strategies and business objectives, coupled with the steps that the CAE establishes to ensure the auditors perform in line with that. A firm foundation is established through effective goal-setting and clear KPIs that are consistently applied at both the internal audit function and auditor levels.

Effectiveness of an internal audit function is founded on three key dimensions³³:

- › Consistently meeting the needs of key stakeholders.
- › Operating in a manner that embraces leading practices.
- › Meeting professional auditing standards and related regulatory requirements.

The KPIs included in a balanced scorecard need to measure these key dimensions to be truly meaningful.

The audit committee and chief executive officer should be consulted on the KPIs for their organisation, so they are tailored to align with organisational priorities, and the vision, mission and mandate reflected in the Internal Audit Charter.

Discussion

Definition of a Balanced Scorecard for Internal Audit⁴⁴

The balanced scorecard performance management system is widely used by organisations and has become a leading management framework for strategy execution throughout the world.

Balanced scorecards in internal auditing help to translate strategy into action, and to manage and measure internal audit performance through Key Performance Indicators (KPIs) used to evaluate success of the internal audit function. They can also help to connect the internal audit strategy with that of the organisation.

Balanced Scorecards often flow into the ‘Annual Report on Internal Audit’ that showcases the contribution and achievements of internal audit, demonstrates its value, and delivers consolidated insights to the audit committee and senior management.

Demonstrating value

The most visible part of an internal audit function is characteristically the final audit reports (and / or executive summaries) on respective audit engagements. But internal auditors are typically measured on more than the outcomes of individual audits, with key stakeholders interested in having a well-considered set of KPIs that help them evaluate the overall success of the internal audit function.

By helping to translate the internal audit strategy into action, balanced scorecards measure and report on internal audit performance through the KPIs used. They also help to connect the internal audit strategy with that of the organisation.

Structuring the balanced scorecard

While internal audit functions will often have some measures focused on quality and performance, they do not always have measures addressing the full range of key stakeholder expectations.

² International Professional Practices Framework, (Lake Mary, FL: The Institute of Internal Auditors, 2017), p 21

³ Mark L Frigo, The Balanced Scorecard – Applications in Internal Auditing and Risk Management (Altamonte Springs FL: The Institute of Internal Auditors Research Foundation, 2014), pp 88-89

⁴ Bruce R Turner, New Auditor’s Guide to Internal Audit: with Insights, Stories, and Tips from Expert Practitioners from Across the World, (Lake Mary, FL: Internal Audit Foundation, to be published mid-2019), chapter 19

Balanced Scorecard Reporting

Exhibit 2 - Examples of KPIs included in balanced scorecard reports⁵

Balanced Scorecard Element	Examples of Internal Audit Function Key Performance Indicators (KPIs)	Measure Type	Inward or Outward Facing Measure
Partnering with the audit committee	Board (or audit committee) expectations met	Qualitative	Outward (delivers value for critical stakeholders)
	Percentage of audit plan complete	Quantitative	Inward
Supporting senior management	Client satisfaction goals—value added	Qualitative	Outward (delivers value for critical stakeholders)
	Client satisfaction goals—usefulness of recommendations	Qualitative	Outward (delivers value through useful recommendations for critical stakeholders)
	Cycle times (duration period of audits)	Quantitative	Outward (drives timely reporting for stakeholders)
Managing internal audit processes	Performance against the internal audit financial budget	Quantitative	Inward
	Availability of current and relevant internal audit charter, intranet, audit manual	Qualitative	Outward (provides useful resources for stakeholders)
	Budget to actual audit times	Quantitative	Inward
	Conformance with quality assurance and improvement standards (based on internal and external quality assessments)	Qualitative	Outward (adds to credibility of work for stakeholders)
Managing Innovation and capabilities	Internal auditor workforce satisfaction	Qualitative	Inward
	Completion of initiatives in professional development plan	Quantitative	Inward
	Optimising innovative practices and utilisation of internal audit resources (to conduct audits while minimising 'administration')	Quantitative	Inward

Source: Sawyer's Internal Auditing: Enhancing and Protecting Organizational Value, 7th ed

Exhibit 2 illustrates a possible structure for internal audit balanced scorecard reporting, and reflects key stakeholder groups in two of the four perspectives (i.e. audit committee and senior management). Specific examples of KPIs are also illustrated in this exhibit (these KPIs are the basis of further expansion in Exhibits 3, 4 and 5).

There are typically four common elements of a balanced scorecard for internal audit as illustrated in Exhibit 2, together with examples of common KPIs, notably:

1. How well the internal audit function partners with the Board and/or audit committee.
2. How well the internal audit function supports management in achieving their business objectives.

3. How well internal audit processes are managed.
4. Innovation and capabilities of the internal audit team.

Implementation

The essential features to the successful implementation of a balanced scorecard report include:

1. Making the internal audit strategy explicit in establishing the basis of the scorecard.
2. Choosing the measures aligned to the strategy, together with clearly understood relationships between the measures.
3. Defining and refining performance measures so the scorecard is well-understood and remains front-of-mind for all internal audit staff.
4. Dealing with the people so change is managed and embedded in the psyche⁶.

Balanced Scorecard Reporting

Alignment to personal performance goals for auditors

Internal auditors are more likely to help an organisation accomplish its objectives where their personal performance goals and objectives align to the mission and objectives of the internal audit function, which in turn should align with the strategic direction of the organisation.

The individual performance measures on which an auditor's performance can be assessed should ideally correspond to their agreed performance goals, and involve qualitative and quantitative factors. Where the internal audit function seeks client feedback after each audit in the form of a client satisfaction survey, the 'scores' for the value added from the audit and the usefulness of audit recommendations are qualitative measures directly influenced by how well the auditors have completed their work.

Auditors need to have visibility between their personal goals and those of the internal audit function. A good way to achieve this is a direct line-of-sight through a balanced scorecard report.

Establishing the information capture and reporting arrangements

It is important to determine upfront the mechanism to be used to capture and report information in the balanced scorecard, and to ensure clarity of the counting rules. The process should ensure the integrity of reporting, will ideally form part of the quality assurance and improvement program, and should be included in the internal audit manual. Exhibit 3 uses the KPIs contained in Exhibit 2 to illustrate key elements of the reporting arrangements.

Exhibit 3 – Documenting key elements of the reporting arrangements

Measure	Mechanism	Target
Partnering with the audit committee		
Board (or audit committee) expectations met	Annual satisfaction survey to all members of the audit committee. The survey will indicate the level of satisfaction with quality, type and volume of information presented and reported. It will cover the audit mandate, audit coverage, adequacy of reporting, an overall level of satisfaction, and their perception of internal audit trending (better, same, declining).	Improved trend for 'overall level of satisfaction' (or sustained positive ratings) year on year. Satisfaction rating for each part of the survey to be scored on average as 3.5 or higher on a scale of 1 (lowest) to 5 (highest).
Percentage of audit plan complete	Number of audits completed and reported to the audit committee as per the approved plan.	90%
Supporting senior management		
Client satisfaction goals—value added	Customer satisfaction survey distributed to a number of relevant stakeholders after each audit.	Average rating of 3.5 or higher on a scale of 1 (lowest) to 5 (highest) for the two key questions on the survey concerning 'value add' and 'usefulness of recommendations' (each other question on the survey points to the possible causes).
Client satisfaction goals—usefulness of recommendations	Customer satisfaction survey distributed to a number of relevant stakeholders after each audit.	
Cycle times (duration period of audits)	Number of audits completed and taken to draft report stage in 12 weeks or less (measured from the start date of fieldwork, to the date of issue of the final audit report).	80%
Managing internal audit processes		
Performance against the internal audit financial budget	Actual expenditure against the approved financial operating budget.	Variance of no more than 5% (over or under)
Availability of current and relevant internal audit charter, intranet information, internal audit manual	Periodic review of internal audit reference materials to ensure the most up-to-date versions are available for stakeholders.	100% of internal audit reference materials are kept up-to-date.
Budget to actual audit times	Number of audits completed in line with planned budget as per the ratified audit plan.	90%
Conformance with quality assurance and improvement standards (based on internal and external quality assessments)	Availability and execution of Quality Assurance and Improvement Program annually, notably: - Self-assessment, complemented by periodic peer review and external assessment at least every five years. - Annual assertion on compliance with standards to be provided by the CAE to audit committee.	100% compliance with IIA Standards (no standards are rated 'partially conforms' or 'does not conform')

Balanced Scorecard Reporting

Managing innovation and capabilities		
Internal auditor workforce satisfaction	Internal audit staff satisfaction survey distributed to all internal audit staff annually.	Average rating of 3.5 or higher on a scale of 1 (lowest) to 5 (highest) for 'overall effectiveness' question.
Completion of initiatives in internal audit's Professional Development Plan	CAE to develop a Professional Development Plan (based on input from audit committee and chief executive officer, plus emerging practices), and then track progress against priorities.	CAE to achieve 85% of priorities in Professional Development Plan (agreed with audit committee) and have demonstrated reasonable progress with others.
Optimising innovative practices and utilisation of internal audit resources (to conduct audits while minimising 'administration')	Time recording for all internal auditors, to determine time spent on undertaking audit work rather than administrative overheads.	Average result between 75% -90% overall. (90% is intended as a stretch target)

Reporting

Exhibit 4 provides an illustrative example of how several of the KPIs depicted in Exhibit 3 might be reported⁷. The structure and style of reporting will be influenced by the needs and expectations of the audit committee and senior management. By reporting on the KPIs in a structured and concise manner, CAEs can streamline other audit committee reporting to remove unnecessary detail and narrative.

Once balanced scorecard reporting has been in place for a couple of years or more, the information can be expanded to include graphs; this is best done in landscape layout. Exhibit 5 includes an example, which uses one of the measures from Exhibit 3.

Scalability

Balanced scorecard reporting is a powerful means of performance reporting that can be developed for all sizes of internal audit functions, from small (one-person or two-person internal audit functions), through to medium and large functions.

The approach has been successfully embraced by CAEs in the corporate sector and public sector (across the three levels of government – federal, state and local government). It can also be applied to both in-house or outsourced internal audit functions.

Exhibit 4 – Example of Balanced Scorecard Report Content




KPI	Target	Prior Result	Current Result	Trend	Comments
Partnering with the audit committee					
Audit committee expectations met	Average rating ≥ 3.5				Average rating of 3.9, up from 3.4 last year
Percentage of audit plan complete	90%				Currently tracking at 92% of plan completed YTD
Supporting senior management					
Client satisfaction goals—value added	Average rating ≥ 3.5				Average rating dropped to 3.2, from 3.4 last quarter. Driven by unacceptable performance of old service provider for co-sourced audits. Better results now being received for newly engaged service provider.

Legend			
Rating	Definition	Trend	Definition
	Neither KPI achieved nor positive trend.		Worse
	Trending well although KPI not yet fully achieved.		Stable
	KPI achieved and currently trending well.		Better
N/A	Not applicable.		

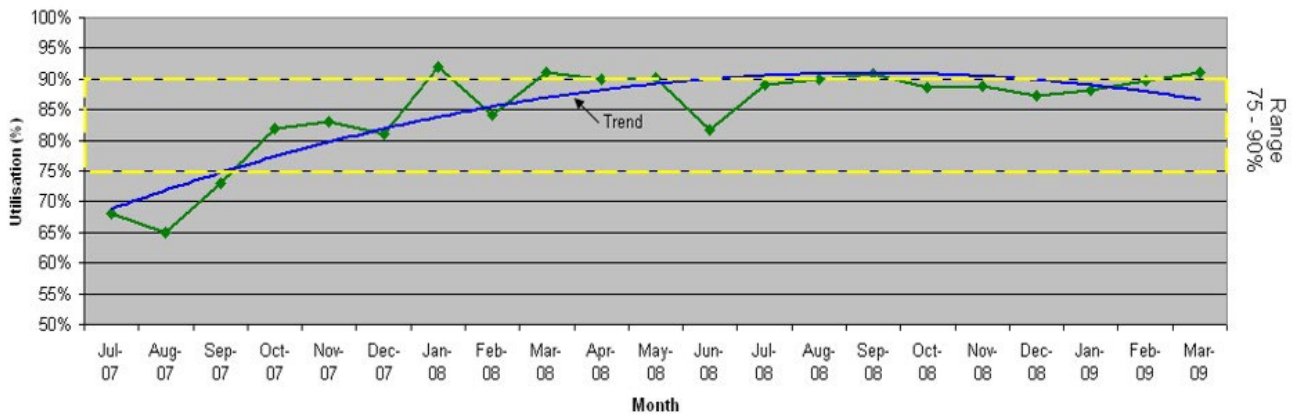
⁷ Developed based on "Governance, Risk Management and Control: Internal Audit Leading Practices Case Studies from Asia", Case study 2 - Stepping up to deliver superior performance – Implementing a balanced scorecard at the Australian Taxation Office, (Asian Development Bank, September 2010), pages 37 to 59

Balanced Scorecard Reporting

Exhibit 5 – Example of Balanced Scorecard Report with Expanded Content

KPI	Target	Prior Result	Current Result	Trend	Comments
Managing innovation and capabilities					
Utilisation of internal audit resources	Average result between 75% - 90% overall.				Continued improvement since a low of 65% in August / September 2007. Concerted focus has resulted in a sustained improvement. The measure is currently tracking at 91%, slightly above (better than) the range.

Auditor Utilisation July 2007 - March 2009



Ten Action Steps

1. Collaborate with the audit committee and chief executive officer to agree on establishment of balanced scorecard reporting, emphasising the internal audit strategy is explicitly the basis of establishing the scorecard.
2. Establish Key Performance Indicators (KPIs) in consultation with the audit committee and chief executive officer, choosing measures aligned to the internal audit strategy, together with clearly understood relationships between the measures.
3. Incorporate KPIs and the requirement for balanced scorecard reporting in the Internal Audit Charter.
4. Modify the internal audit quality assurance and improvement program to establish a source of assurance that integrity of reporting is being maintained (refer Standard 1300 Quality Assurance and Improvement Program, particularly Standards 1310 and 1311).
5. Develop and document key elements of the reporting arrangements (Exhibit 3 provides examples), and update the internal audit manual to reflect the information capture, reporting, and quality arrangements.
6. Inform internal audit leaders and auditors (including outsourced and co-sourced service providers) of the introduction of balanced scorecard reporting, illustrating how this approach fits into high-level internal audit reporting practices (Exhibit 1 refers), and ensuring it is well-understood and remains front-of-mind for all internal audit staff and service providers.
7. Modify the personal performance goals of internal audit leaders and auditors so there is a direct and clearly understood relationship between personal goals and those of the internal audit function (eg the KPI in Exhibit 4 covering 'Client satisfaction goals—value added' is directly influenced by auditors and service providers in the outcomes of their audits).
8. Provide visibility to internal audit leaders and auditors on how their personal goals align to the KPIs of the internal audit function as reported through the balanced scorecard report, so change is managed and embedded in their psyche.
9. Design and introduce balanced scorecard reporting that suits the needs and expectations of the audit committee; streamline other existing performance-related reporting to the audit committee to avoid duplication of reporting.
10. Periodically refine the performance measures (KPIs) so the scorecard remains relevant; balanced scorecards should inspire continuous improvement and innovation, so KPIs should be tightened occasionally to maintain an element of 'stretch', rather than easily achieved measures.

Balanced Scorecard Reporting

Conclusion

Balanced scorecard report is a well-established approach to structuring qualitative and quantitative KPI measures, and reporting results to the audit committee in a balanced way. It also provides a direct line-of-sight between the overall performance of the internal audit function and performance of auditors; KPIs in the balanced scorecard will almost always align to individual performance measures.

Bibliography and References

- › Mark L Frigo, The Balanced Scorecard – Applications in Internal Auditing and Risk Management (Altamonte Springs FL: The Institute of Internal Auditors Research Foundation, 2014), pages 88-89
- › “Governance, Risk Management and Control: Internal Audit Leading Practices Case Studies from Asia”, Case study 2 - Stepping up to deliver superior performance – Implementing a balanced scorecard at the Australian Taxation Office, (Asian Development Bank, September 2010), pages 37-59
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- › Sally-Anne Pitt, Internal Audit Quality (Hoboken New Jersey, John Wiley & Sons Inc, 2014), page 19
- › “Sawyer’s Internal Auditing: Enhancing and Protecting Organizational Value” (Lake Mary, FL: Internal Audit Foundation, 2019), pages 174-175

Purpose of White Papers

A White Paper is a report authored and peer reviewed by experienced practitioners to provide guidance on a particular subject related to governance, risk management or control. It seeks to inform readers about an issue and present ideas and options on how it might be managed. It does not necessarily represent the position or philosophy of the Institute of Internal Auditors–Global and the Institute of Internal Auditors–Australia.

Author’s Biography

Written by Bruce Turner AM
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Bruce remains active as an audit and risk committee chair, company director, executive coach, mentor, and white ribbon ambassador. He has held board and independent audit committee roles over the last decade in twenty-five diverse organisations, including six years on the IIA-Australia Board to mid-2018.

His forty years of practitioner and leadership experience in internal auditing across the globe traverses the energy, financial services (commercial, merchant and central banking), government, manufacturing, and transport sectors. Prior to his retirement in 2012, he held Chief Audit Executive roles at the

State Rail Authority of NSW, Integral Energy Australia, and ultimately the Australian Taxation Office.

Bruce has used and championed balanced scorecard reporting through his various CAE and audit committee roles. He sees the merits of aligning the internal audit and organisational strategies, then providing clarity of reporting on the overarching performance of the internal audit function with a direct line of sight for the auditors who deliver the effort on the ground.

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The Institute of Internal Auditors (IIA) is the global professional association for Internal Auditors, with global headquarters in the USA and affiliated Institutes and Chapters throughout the world. As the chief advocate of the Internal Audit profession, the IIA serves as the profession’s international standard-setter, sole provider of globally accepted internal auditing certifications, and principal researcher and educator.

The IIA sets the bar for Internal Audit integrity and professionalism around the world with its ‘International Professional Practices Framework’ (IPPF), a collection of guidance that includes the ‘International Standards for the Professional Practice of Internal Auditing’ and the ‘Code of Ethics’.

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