

Auditing the Public Sector

FUTURE



Closer Look

Managing Expectations, Delivering Results

Arthur Piper



CBOK

The Global Internal Audit
Common Body of Knowledge

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About CBOK

SURVEY FACTS

Respondents	14,518*
Countries	166
Languages	23

EMPLOYEE LEVELS

Chief audit executive (CAE)	26%
Director	13%
Manager	17%
Staff	44%

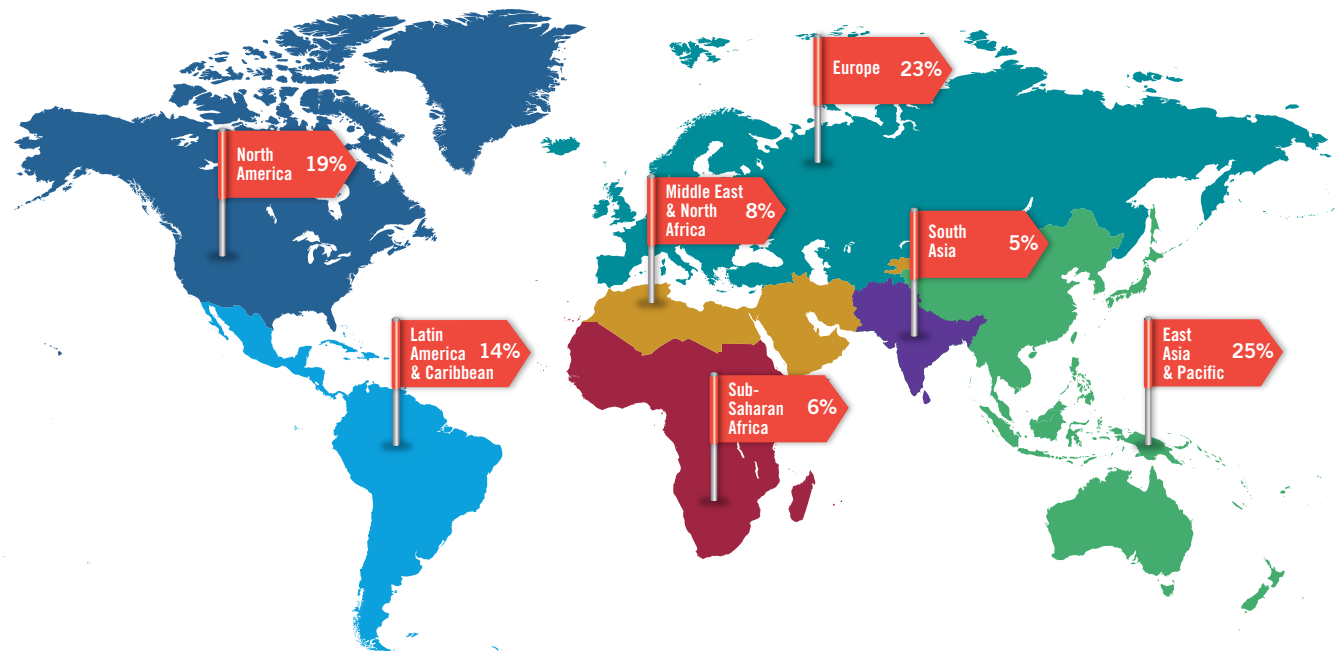
*Response rates vary per question.

The Global Internal Audit Common Body of Knowledge (CBOK) is the world's largest ongoing study of the internal audit profession, including studies of internal audit practitioners and their stakeholders. One of the key components of CBOK 2015 is the global practitioner survey, which provides a comprehensive look at the activities and characteristics of internal auditors worldwide. This project builds on two previous global surveys of internal audit practitioners conducted by The IIA Research Foundation in 2006 (9,366 responses) and 2010 (13,582 responses).

Reports will be released on a monthly basis through July 2016 and can be downloaded free of charge thanks to the generous contributions and support from individuals, professional organizations, IIA chapters, and IIA institutes. More than 25 reports are planned in three formats: 1) core reports, which discuss broad topics, 2) closer looks, which dive deeper into key issues, and 3) fast facts, which focus on a specific region or idea. These reports will explore different aspects of eight knowledge tracks, including technology, risk, talent, and others.

Visit the CBOK Resource Exchange at www.theiia.org/goto/CBOK to download the latest reports as they become available.

CBOK 2015 Practitioner Survey: Participation from Global Regions



Note: Global regions are based on World Bank categories. For Europe, fewer than 1% of respondents were from Central Asia. Survey responses were collected from February 2, 2015, to April 1, 2015. The online survey link was distributed via institute email lists, IIA websites, newsletters, and social media. Partially completed surveys were included in analysis as long as the demographic questions were fully completed. In CBOK 2015 reports, specific questions are referenced as Q1, Q2, and so on. A complete list of survey questions can be downloaded from the CBOK Resource Exchange.

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Risk



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Executive Summary

A significant proportion of internal auditors work in the public sector—about 1 out of 4 respondents to the CBOK 2015 Global Internal Audit Practitioner Survey. Given that they must satisfy both their internal stakeholders—chief executives, boards, divisional service heads—and also be accountable to both politicians and the public, they face a unique set of challenges. This report aims to assess how well they are coping with that role and how they might improve their practices for the future.

Globally, many areas of the public sector say they have insufficient funding for their scope of work. In most regions, twice as many public sector auditors say they are underfunded compared to their counterparts outside the public sector. In addition, greater public transparency and accountability within governments has increased demand for audit work, as well as growing threats from cyber risk and other emerging risks.

The public sector has fewer audit committees than other sectors, and the quality and composition of the audit committees can vary greatly. In some cases, this presents significant threats to internal audit independence.

Despite their challenges, many internal auditors in the public sector are getting involved in their organization's strategic business risks, and they are using The IIA's *International Standards for the Professional Practice of Internal Auditing (Standards)* nearly as much as those in the non-public sector. Notably, 86% of respondents say they use some or all of the *Standards*—a great achievement given that some government auditing requirements are not completely in line with the *Standards*.

Finally, public sector internal auditors receive more hours of training per year than those in other sectors, but they also tend to miss out on some of the benefits of working in the non-public sector, such as the opportunity to receive bonuses. While staff retention is often difficult given government audit pay scales, many public sector employers are providing additional benefits—such as good working conditions, job security, and skills training—to compensate for less pay.

1 The Roles of Internal Auditors in the Public Sector

Public sector auditors are in a unique position when it comes to serving their stakeholders. Not only do they need to satisfy the needs of their CEOs, boards, divisional managers, and regulators, they often have to balance those requirements with their political and public stakeholders. This report provides insights into how those pressures, coupled with rapid changes in technology and business practices, are affecting public sector auditors.

Based on findings from CBOK 2015, the largest ongoing study of internal audit professionals in the world, and interviews with leading public sector audit practitioners, this report offers both a snapshot of where auditors are today and a potential roadmap for tomorrow. It specifically addresses the roles internal auditors play in the public sector, the impact of funding shortages on the sector, threats to independence and objectivity, new and changing risks, the lack of funding for audit technologies, conformance with the *Standards*, and how well chief audit executives (CAEs) attract and retain talent.

Internal Auditors in the Public Sector

Among survey respondents worldwide, an average of 1 out of 4 internal auditors work in the public sector (see **exhibit 1**). Although the survey is not based on a scientific sample, this is certainly an

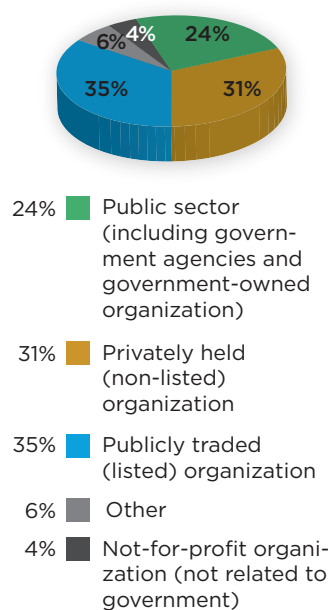
indication of the significant proportion within the public sector.

While most regions are near the global average of 24%, two regions are substantially higher: Sub-Saharan Africa (41%) and the Middle East & North Africa (33%). (See **exhibit 2**.) On the other end of the scale, South Asia had only 12 respondents from the public sector (representing only 2% of their respondents). Due to this small percentage, South Asia is combined with East Asia & Pacific for the regional breakouts in this report, and this area is referenced as Asia & Pacific.

In Which Areas of the Public Sector Do Internal Auditors Work?

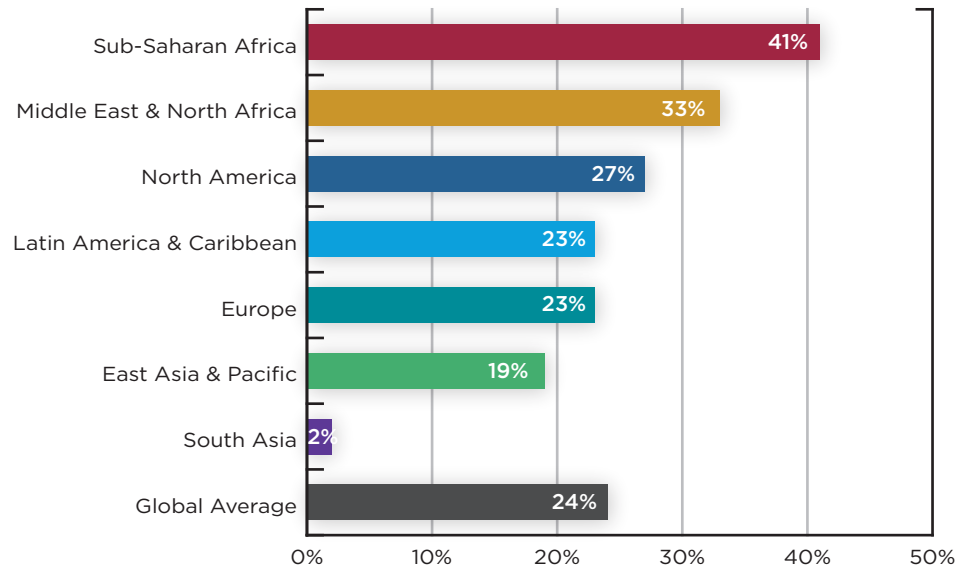
Internal auditors in the public sector find themselves in a variety of roles, especially depending on the government structure of the region in which they work. Globally, about 2 out of 3 public sector respondents (61%) say they work in core government (including agencies). Another 24% work for a government-owned market enterprise or public sector, and the remaining 15% are in government-operated services (such as schools, hospitals, or mail delivery). These percentages are fairly consistent across the different regions, except for the Middle East and North Africa, where internal auditors are equally split between core government and government-owned enterprises (see **exhibit 3**).

Exhibit 1 Organization Types Among Survey Respondents



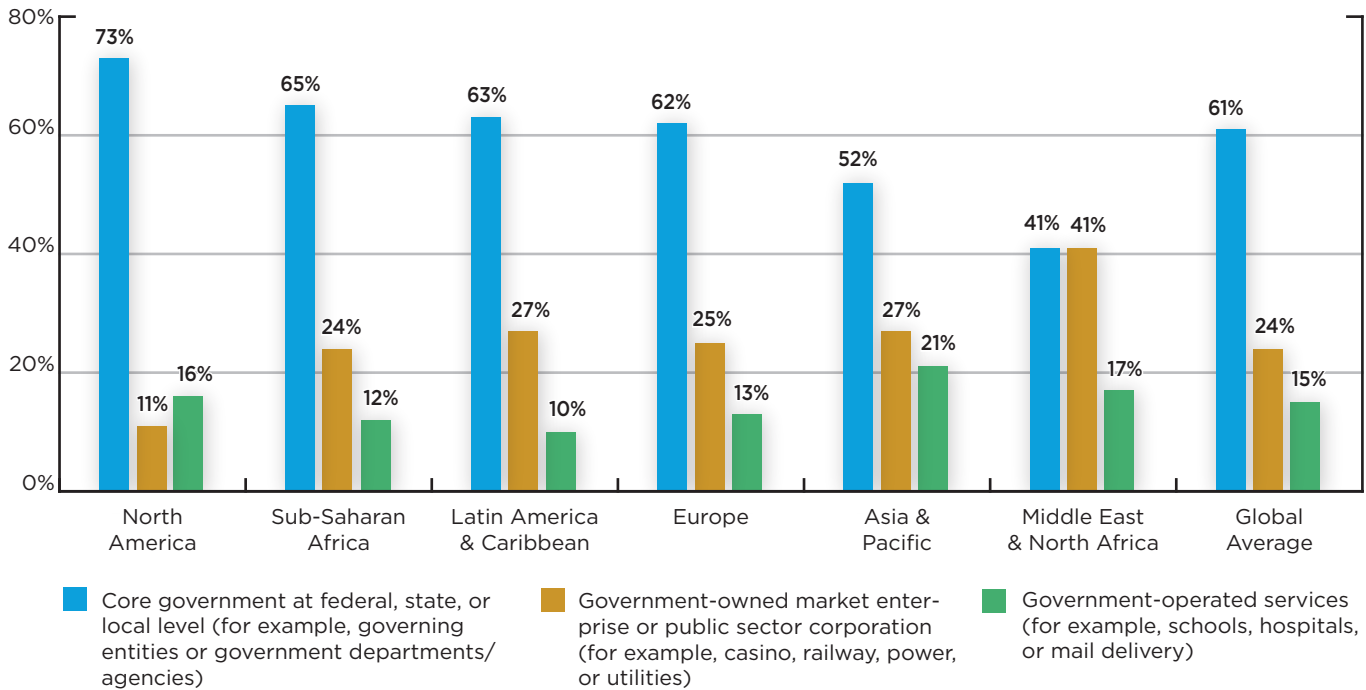
Note: Q15: What is the type of organization for which you currently work? $n = 13,032$.

Exhibit 2 Percentage of Public Sector Respondents per Region



Note: Q15: What is the type of organization for which you currently work? $n = 12,852$.

Exhibit 3 Public Sector Areas: Core Government, Government-Owned Enterprises, and Government-Operated Services



Note: Q15a: In which part of the public sector do you work or provide audit services? $n = 2,770$.

In Which Government Levels Do Internal Auditors Work?

In some parts of the world, the majority of internal auditors are working at the national level (Latin America, Sub-Saharan Africa, and Europe). However, in the Middle East & North Africa, the highest percentage work at the local level. In North America, internal auditors are mostly at the local and regional level, while in Asia, they are at the local and national levels (see **exhibit 4**).

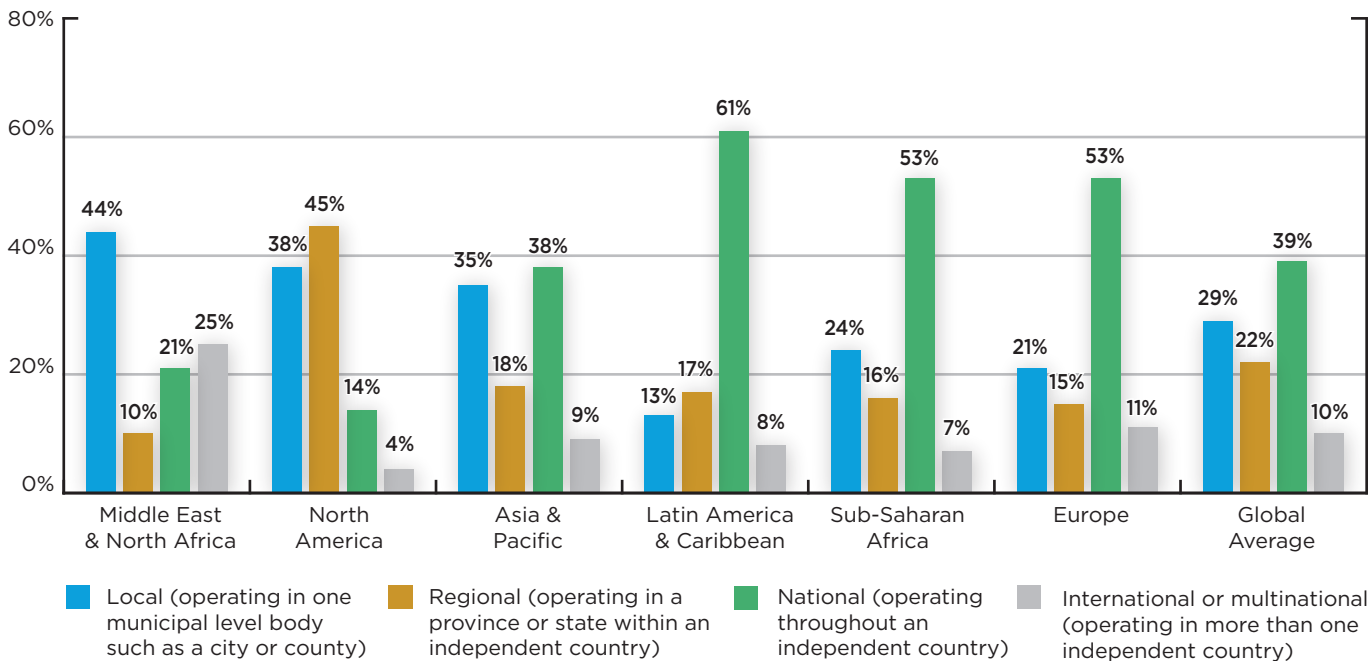
mandated by law, with a regional high of 88% in Latin America & Caribbean and a low of about 60% in North America and Asia (see **exhibit 5**).

Given the variety of roles and responsibilities of public sector internal auditors around the globe, this report takes a high-level view of the challenges they face and the strategies they adopt to meet them. It is hoped they find both insight and inspiration.

Which Public Sector Audit Functions Are Mandated by Law?

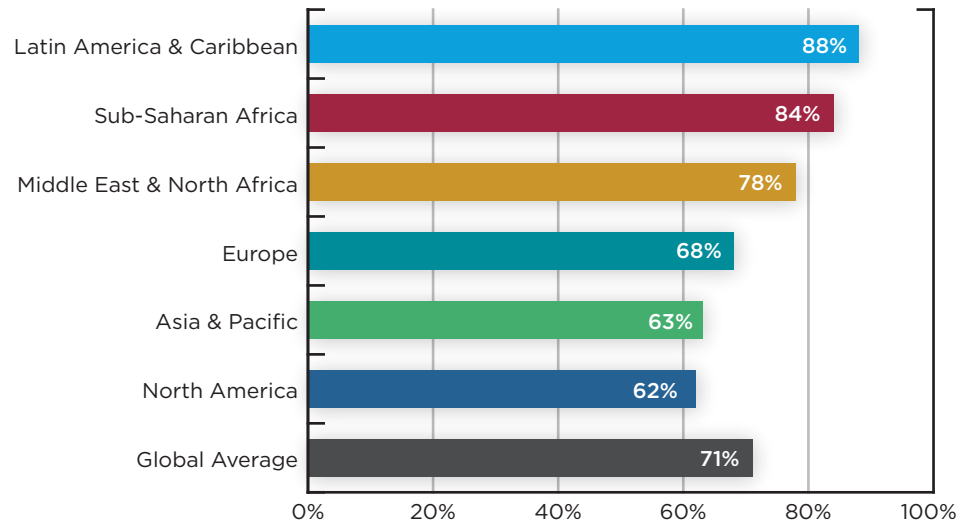
Among survey respondents, a global average of about 7 out of 10 say the existence of their internal audit function is

Exhibit 4 Geographic Scope of Public Sector Organizations



Note: Q17: What is the geographic scope of your organization or government entity? n = 3,032.

Exhibit 5 Internal Audit Mandated by Law (Public Sector Only)



Note: Q68: Is the existence of an internal audit department mandated by law for your organization? Public sector respondents only. $n = 2,572$.

2 The Impact of Funding Shortages

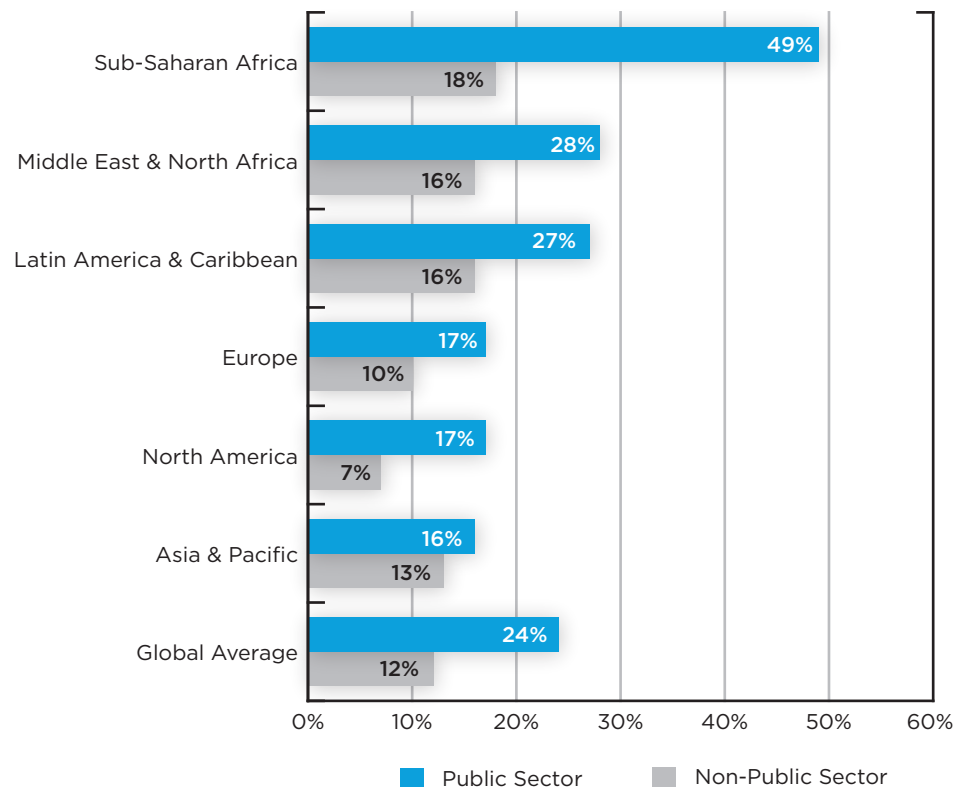
Over the past five years, most governments across the globe have cut funding to public services in the continuing aftermath of the financial crisis of 2007/2008.

The CBOK 2015 Global Practitioner Survey found that 24% of public sector CAEs say their budgets are not at all sufficient relative to the extent of their audit responsibilities, while only 12% of CAEs

in non-public sectors report this (see **exhibit 6**, which also includes regional differences).

There may be light on the horizon for some. About a third of public sector CAEs say their budgets increased in the previous year (34%), although this lags behind the non-public sector average of 42% (Q27, $n = 3,107$). In terms of full-time permanent staff positions, the

Exhibit 6 Funding Is “Not at All Sufficient” (Public Sector Compared to Non-Public Sector)



Note: Q28: In your opinion, how sufficient is the funding for your internal audit department relative to the extent of its audit responsibilities? CAEs only. $n = 788$.

public sector also saw increases from the previous year, but again, not at the same rate as the non-public sector. About 25%

of CAEs in the public sector reported an increase, compared with 31% in the non-public sector (Q25, $n = 3,247$).

HIGHER EXPECTATIONS FOR PUBLIC SECTOR INTERNAL AUDITORS

Although internal auditors in the public sector are experiencing funding shortages, they also face increased expectations, says Simon Edge, a public sector internal audit change consultant who has worked for the Wales Audit Office, the UK Audit Commission, and has served as an independent member of Surrey County Council. He is currently interim director, culture and change, at the charity Victim Support. He says while funding has decreased, public sector bodies in the United Kingdom are facing increased scrutiny by the public, including the use of statutory access rights (enabled by freedom of information legislation) to publish audit reports and papers in the public domain.

“This is leading to additional work from issues raised by members of the public,” he says. “They [the public] are becoming more challenging of public services and of internal audit’s ability to ‘resolve’ issues to their satisfaction, which is promoting an expectations gap.”

“Austerity is continuing and will do so for some years yet,” Edge says. He observes that internal audit must do more with less in the current circumstances. That could mean sharing internal audit services across multiple agencies.

“But with repeated cutting there comes a point when the internal audit services the organization is willing to pay for are not adequate—just at a time when those charged with governance need audit assurance the most,” he says. He adds that these pressures are likely to make internal audit’s relationship with senior management and those charged with governance more difficult, increasing the need for good relationship management and demonstrable audit quality.

3 Threats to Independence and Objectivity

“Lack of financial expertise on the audit committee is likely to affect the quality of the audit planning process, especially if they do not understand what internal audit could or should be doing. In addition, they may just remove the chief audit executive if they don’t agree with him or her.”

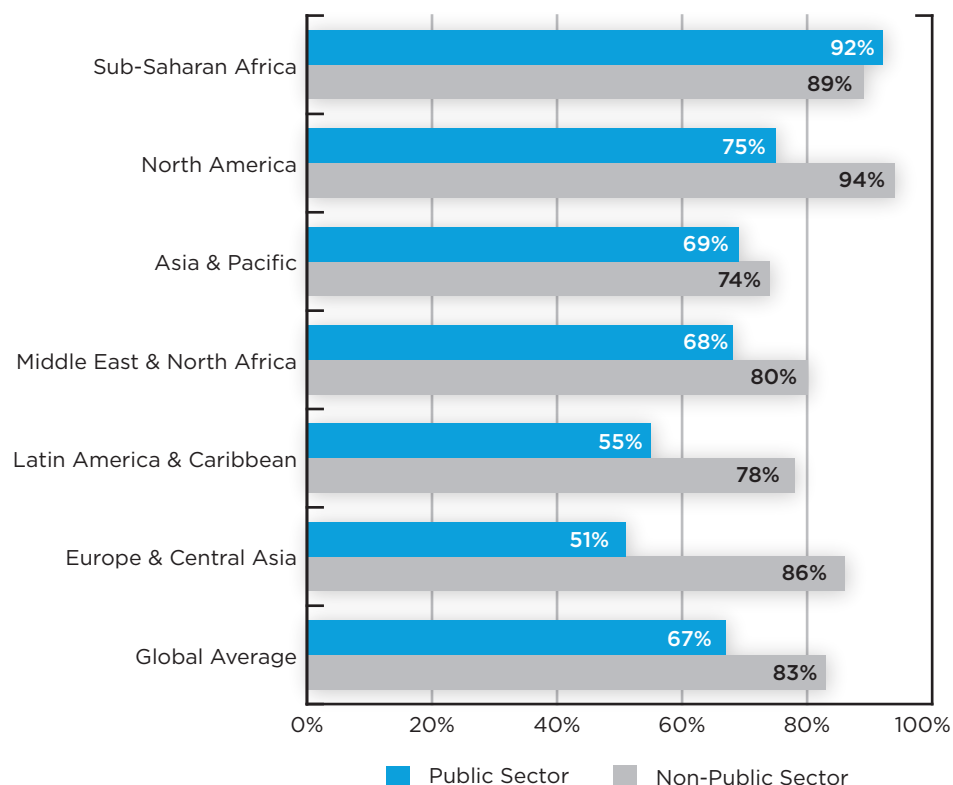
—Christie O’Loughlin, Principal at Christie O’Loughlin and Associates, Olympia, Washington, United States

One of internal audit’s key roles is to provide objective assurance to its stakeholders. A key way of achieving this is to be seen as independent from management and other stakeholders—something that is often easier said than done.

Only an average of 67% of public sector respondents say they have audit committees, compared to 83% among non-public sector respondents (see

exhibit 7). Sub-Saharan Africa has the highest proportion of audit committees (92%) and Europe has the lowest (51%). Also of note: in almost all regions of the world, the public sector has a lower percentage of audit committees than other sectors (except in Sub-Saharan Africa). In addition, according to interviews, the quality and composition of audit

Exhibit 7 Audit Committee Existence (Public Sector Compared to Non-Public Sector)



Note: Q78: Is there an audit committee or equivalent in your organization? n = 2,621 for public sector. n = 8,464 for non-public sector.

committees and boards vary greatly, with single-person boards being common.

Structural problems can threaten internal audit's independence and its ability to provide objective assurance. In Tanzania, for example, the Public Finance Regulations say that public sector audit committees must be comprised of senior members of the management team—the very people who are to be audited. This situation creates extra challenges for CAEs, says Ahadi Chacha, director of performance audit at Surface and Marine Transport Regulatory Authority, Dar Es Salaam, United Republic of Tanzania. He says CAEs in such organizations need to focus on educating the audit committee on internal audit's role and, where possible, leverage the expertise and support of external members.

Challenges to independence can create ethical issues. In general, about 1 out of 4 public sector CAEs say they have faced pressure during their careers to alter valid audit findings, with that proportion

somewhat higher in Sub-Saharan Africa and lower in Asia & Pacific (see **exhibit 8**). The pressure is most commonly felt from CEOs and operations management, although the board of directors is also involved in some regions (particularly Europe and Latin America) (Q77b, *n* = 187).

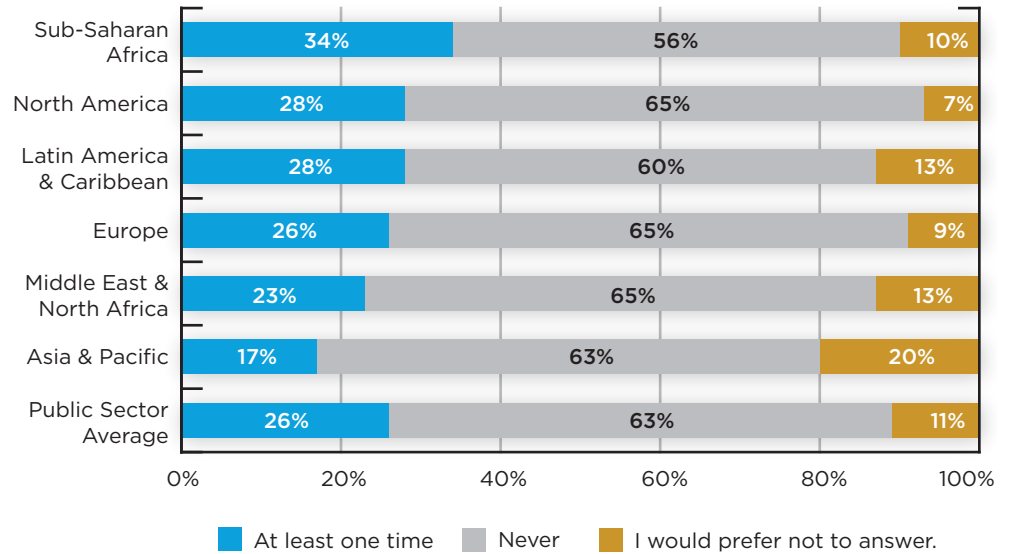
Public sector auditors must satisfy a wide stakeholder base without always being able to consult with them about their specific needs. Stakeholders can include the party requesting the audit, the audited body, another government body, public officials—such as mayors—and public interest groups, as well as taxpayers.

“It is not easy to know who the stakeholders are,” says Didier Eyssartier, inspecteur à l'IGAS at Inspection Générale des Affaires Sociales, Paris, France. “In France, at the state level, our solution has been to say that in every department and government body, there must be an audit committee with external members.”

ACTION POINTS: PROMOTING INDEPENDENCE

- 1.** Focus on building strong, professional relationships with key stakeholders based on honesty, competence, and reliability.
- 2.** Seize the opportunity to facilitate a conversation leveraging the Three Lines of Defense Model. Internal audit can take on a consultative and educator role in helping key stakeholders understand the importance of an effective three lines of defense.

Exhibit 8 Pressure Felt to Change an Audit Finding (Public Sector Only)



Note: Q77: During your internal audit career, have you experienced a situation where you were directed to suppress, or significantly modify, a valid internal audit finding or report? Public sector respondents only. *n* = 2,585.

4 New and Changing Risks

Fast-changing risk areas—such as cyber threats, the ramifications of geopolitical events, and domestic economic turmoil—have given public sector internal audit departments the opportunity not just to audit the historical performance of their organizations, but to work with their organizations to come to a common understanding about new and changing risks. Many regions are well above the global average for

involvement with their organization’s strategic business risks (see **exhibit 9**).

Ideally, risk assessments are updated as needed throughout the year in order to respond to changing risks. Slightly more than half of public sector internal auditors say that they update their risk assessments periodically or continuously throughout the year. Another third say they conduct an annual risk assessment, but they do not have formal updates

Exhibit 9 Areas of Risk Focus (Public Sector Regions Compared to Non-Public Sector)

Risk Focus	North America	Europe	Sub-Saharan Africa	Middle East & North Africa	Asia & Pacific	Latin America & Caribbean	Global Average (Non-Public Sector)
Operational	86%	81%	76%	76%	75%	64%	78%
Compliance/regulatory	67%	61%	68%	57%	63%	82%	71%
Risk management assurance/effectiveness	51%	62%	70%	41%	73%	57%	58%
Strategic business risks	45%	51%	63%	65%	59%	60%	54%
Information technology (IT) not covered in other audits	54%	54%	39%	53%	47%	56%	55%

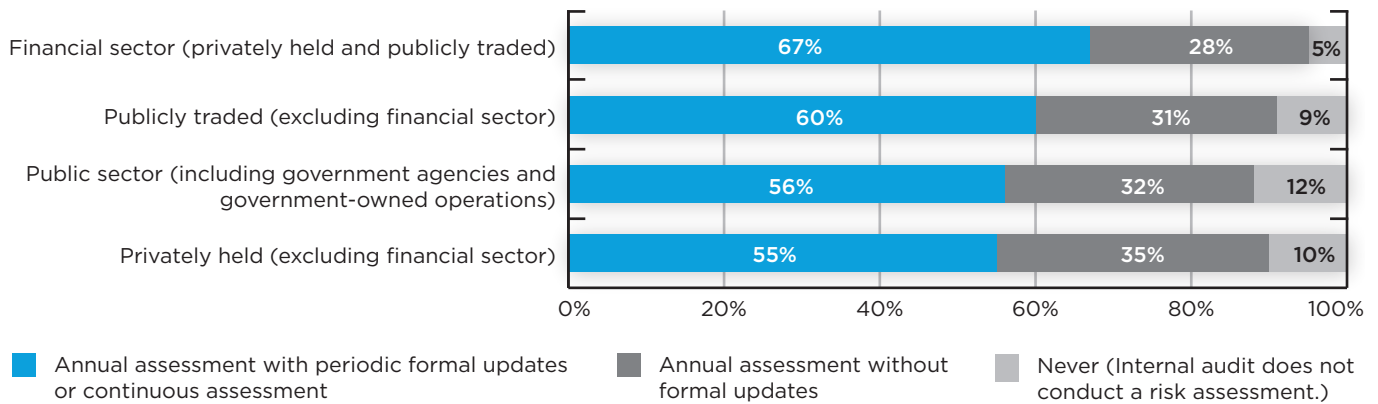
Note: Q66: Please identify the top five risks on which your internal audit department is focusing the greatest level of attention in 2015. Public sector CAEs only. Blue indicates more than 5% above the global average for non-public sector; while red indicates more than 5% below. *n* = 678 for public sector. *n* = 2,059 for global average.

throughout the year, which may cause a lack of awareness for changing risks. Finally, about 1 out of 10 say that internal audit does not conduct a risk assessment in their organizations. It is hoped that these organizations have some alternate manner of conducting an adequate risk assessment (see **exhibit 10**).

CAEs must communicate effectively with their stakeholders, informing them

of any emerging organizations' strategic objectives. In France, at the state level, departments now try to produce a formal statement on risk at least annually to that end, says Eyssartier. At the local government level, however, these mechanisms often do not exist, so CAEs may only be reporting to a limited number of stakeholders, many of whom have conflicting political interests.

Exhibit 10 Frequency of Risk Assessment (Organization Type View)



Note: Q42: How frequently does internal audit conduct a risk assessment? CAEs only. n = 2,986.

5 Lack of Funds for Technology

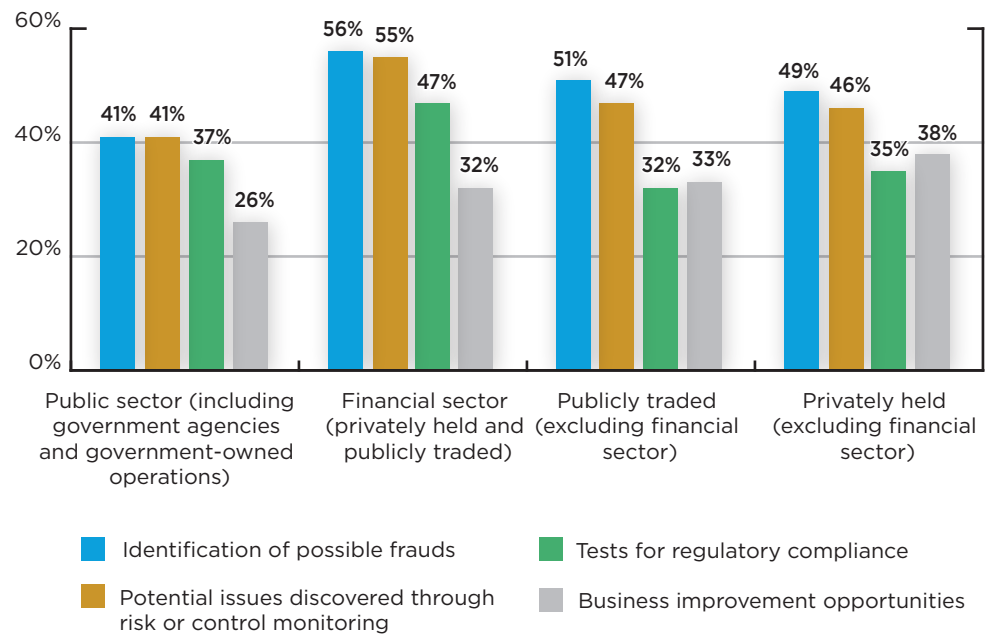
Internal auditors rate themselves highly when it comes to their skill levels in using data analytics and automated auditing tools—55% of public sector auditors rated themselves as expert or advanced, the same as did so globally over all sectors (Q86, $n = 10,010$).

However, internal auditors in the public sector are less active in using data mining and analysis than those in other organization types (see **exhibit 11**), particularly in the areas of identifying fraud (see the blue bars) and monitoring risk/

controls (see the gold bars). Anecdotally, CAEs say they struggle with having the funds to invest in appropriate software so that they can exploit such technologies, and many are still in the process of training their teams in the use of these applications.

Using big data techniques is also expensive because large amounts of data have to be cleaned up prior to analysis. “In addition, data is sometimes protected so that even auditors don’t have access to read it,” Eyssartier says.

Exhibit 11 Use of Data Analytics (Organization Type View)



Note: Q96: Does your internal audit department use data mining or data analytics for the following activities? (Choose all that apply.) $n = 10,088$.

To get the most out of these technologies, auditors need to ensure that their audits are aligned to their organization's strategic objectives. About 60% of public sector CAEs say they are fully or almost fully aligned, which is nearly as

high as the financial sector (63%) and higher than nonfinancial, privately held organizations (55%) and nonfinancial, publicly traded organizations (49%) (Q57, $n = 2,756$).

ACTION POINTS: IMPROVING TECHNOLOGY USE

- 1.** CAEs must be prepared to demonstrate a return on investment to stakeholders in an investment in effective data analysis tools and to illustrate how the data analytics will support the achievement of objectives.
- 2.** Audit departments that are just beginning to use data analytics can start small and focus on areas where the benefits are clear.
- 3.** With the right expertise, significant analysis can be done in readily available tools, such as Microsoft Excel.
- 4.** To facilitate the implementation of data analytics projects, CAEs should:
 - Identify existing competency gaps.
 - Frame a knowledge management strategy to address major gaps in expertise.
 - Develop an appropriate sourcing strategy.

6 Use of the *Standards*

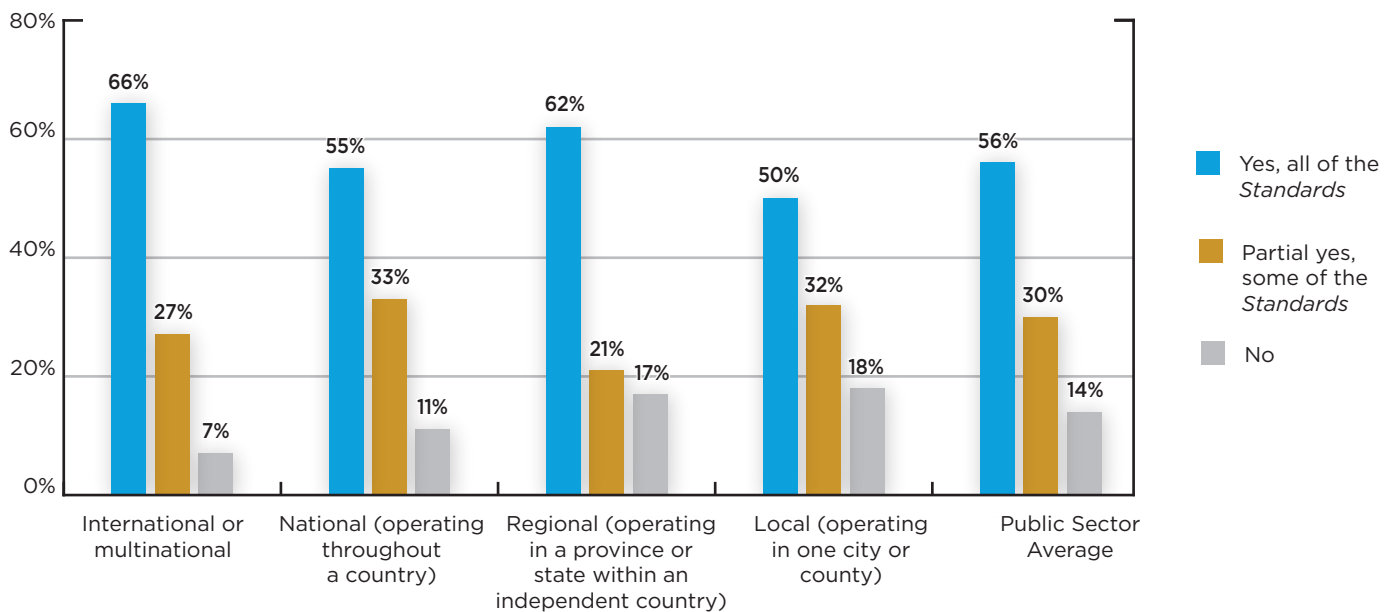
Within the public sector, the use of the *Standards* is complicated by other mandatory government guidelines or legal statutes, which vary between local, regional, or national levels. On average, 86% of respondents say they use all or some of the *Standards*. In general, use of the *Standards* is lowest at the local level and highest at the international level (see **exhibit 12**).

Across all regions, the public sector lags only slightly behind the non-public sector for use of the *Standards*. When the “use of all of the *Standards*” is analyzed,

more than half (56%) of public sector auditors say they use all of the *Standards*, which is only slightly lower than the global average of 60% for the non-public sector respondents. However, the “use of all of the *Standards*” varies widely between regions, with a high of 68% in North America and a low of 38% in Latin America (see **exhibit 13**).

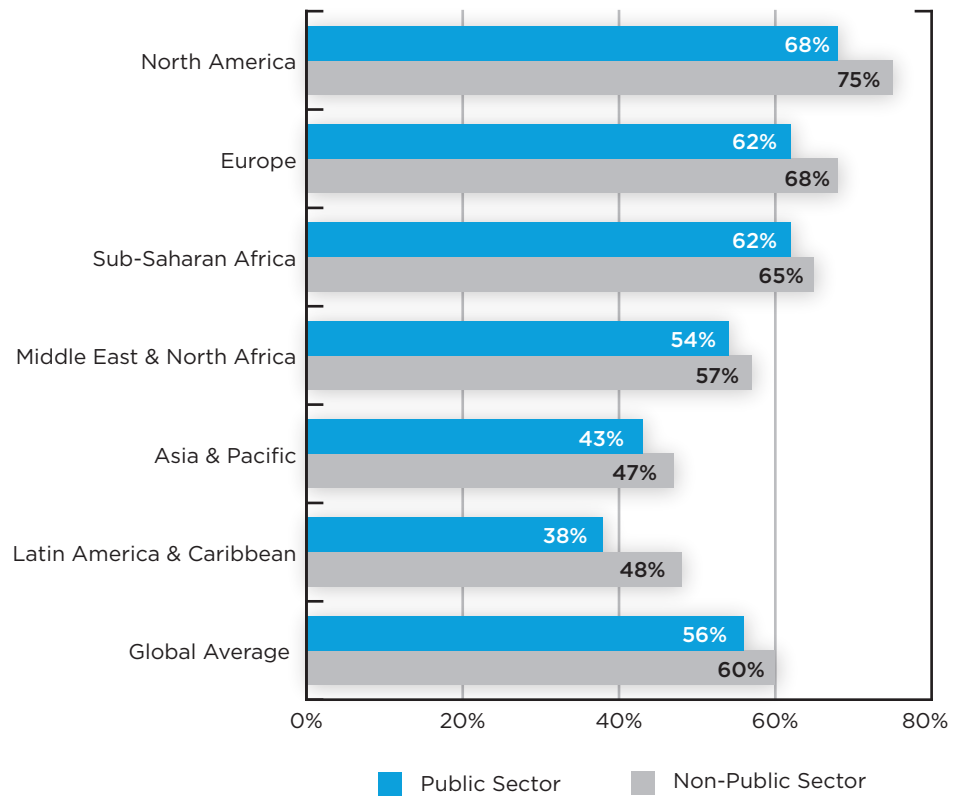
Local laws can impact internal audit’s ability to conform to the *Standards*. In Tanzania, for example, a national law (The Public Finance Regulations) defines internal audit and internal controls

Exhibit 12 Use of The IIA’s *Standards* (View by Public Sector Types)



Note: Q98: Does your organization use the *International Standards for the Professional Practice of Internal Auditing (Standards)*? *n* = 6,983 for non-public sector. *n* = 2,320 for public sector.

Exhibit 13 Use of All of The IIA’s Standards (Public Sector Compared to Non-Public Sector) (View by Region)



Note: Q98: Does your organization use the *International Standards for the Professional Practice of Internal Auditing (Standards)*? Topic: Yes, all of the *Standards*. n = 6,983 for non-public sector. n = 2,285 for public sector.

differently than The IIA’s International Professional Practices Framework (IPPF)—focusing primarily on compliance and financial controls. “The legal definition [of internal audit] does not explicitly address risk management and governance processes, nor does it cover consulting activity,” says Chacha. “CAEs in this position need to educate the board and senior managers so that they see the rationale for The IIA’s broader definition of internal auditing and internal controls.” In addition, when internal auditors adopt best practices in their work, they

can demonstrate the additional benefits of working with IPPF standards and practices, he says.

O’Loughlin says that CAEs need to have the courage to audit areas outside such narrow definitions if internal audit is to fulfil its proper role. “CAEs are often afraid to audit areas such as governance and strategy because doing so might put them at odds with boards and managers, but if internal auditors are to provide objective assurance, they need to have the courage to take on these challenges, even at the risk of being fired,” she says.

ACTION POINTS: USE OF THE *STANDARDS*

Differences in regional internal audit practices reinforce the need for a principles-focused, coherent framework that facilitates consistent development, interpretation, and application of concepts, methodologies, and techniques useful in the professional practice of internal auditing.

The overarching benefits of implementing professional auditing standards include:

- Defining basic principles that represent the practice of internal auditing
- Providing a framework for performing and promoting a broad range of value-added internal auditing
- Establishing the basis for the evaluation of internal audit performance
- Fostering improved organizational processes and operations

7 Attracting and Retaining Talent

Budget constraints have seriously affected the ability of public sector internal audit departments to attract and retain talent, especially in technical areas such as cybersecurity and data mining. In Mexico, for example, many government departments have reduced internal audit budgets, making training in risk and control critical for remaining employees, says Guadalupe Castillo, IIA–Mexico, Mexico City.

Private sector companies can obtain the most talented public sector auditors by enticing them with better pay. Given the continuing austerity measures in many government bodies globally and the culture of some public sector bodies,

there is limited scope to award bonuses to those working in the public sector. Only 40% in the public sector say they have the opportunity to earn a bonus, compared to 75% for those in other sectors (Q34, $n = 11,792$).

One of the strengths of working for the public sector is the level of training staff receive. Public sector employees receive more formal internal audit training than any other sector—49 hours per year compared to 44 for non-public sectors (Q14, $n = 12,998$). In most countries, public sector organizations support training for staff to an agreed level, although that still may not be enough to keep on top of fast-moving events.

ACTION POINTS: RETAINING TALENT

Public sector organizations often do well in providing training to their employees but, because of budget constraints and cultural issues, often have less flexibility with pay. Castillo suggests three lines of action to help retain staff:

1. Develop excellent internal training programs to keep the competencies and knowledge of staff up-to-date, including providing time off to attend workshops and conferences.
2. Create a good working environment and flexible employment conditions, where possible.
3. Foster a sense of belonging, so that auditors who may work in isolated areas connect regularly with their colleagues and also with their local IIA institutes and chapters.

Conclusion

Public sector internal auditors have their work cut out for them. They need to deal with both a broad stakeholder base and the increasing demands around the globe for better transparency and accountability among government agencies. This has boosted the demand for internal audit's services at a time when public sector internal auditors are twice as likely to say that they are underfunded, compared to their counterparts outside the public sector.

Despite their challenges, public sector internal auditors are getting involved with their organizations' strategic risks and using the *Standards* at a high rate. While the sector remains a challenging place to work, internal auditors are rising to the challenge and are well-placed to provide the kind of objective assurance and consulting that the public sector is looking for and needs.

About the Author

Arthur Piper, PhD, is an award-winning writer and editor with more than 20 years' experience specializing in internal auditing, risk management, corporate governance, and emerging technologies. He has been managing director of the editorial services company, Smith de Wint, since 1996. He has been Associate Research Fellow at the University of Nottingham (UK) in the Department of Culture, Film, and Media since 2006, and specializes in the critical understanding of emerging technologies.

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