THE INTERNAL AUDITOR AS AN AGENT OF ORGANIZATIONAL LEARNING:

ENHANCING THE VALUE OF INTERNAL AUDITING IN THE PUBLIC SECTOR

A research report written for the Government Internal Auditors Council of Canada

Luc Juillet

With the collaboration of Catherine Liston-Heyes, James R. Mitchell and David Zussman

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The Government Internal Auditors Council of Canada (GIACC) represents the internal audit communities within the Federal Government of Canada and the governmental internal audit functions of all 10 Canadian provinces and 3 territories. GIACC was created to serve as a focal point for the exchange of information and practices for the benefit of all its members and is dedicated to the ongoing strengthening of internal auditing. It is devoted to sharing information and supporting the continued development of internal audit research, audit methodology, practices and professional development.

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EXECUTIVE SUMMARY

In a fast-changing environment, public managers are asked to become more innovative, to meet higher standards of accountability and to deliver better value, often with fewer resources. This demanding environment is also challenging internal auditors in Canada's public sector. While internal auditing has been considerably strengthened in many jurisdictions over the last decade, public sector internal auditors must look to the future and consider how they can deliver even more value to their organizations, helping them innovate and perform better. Based on a national survey of Canadian public sector internal auditors, two panel discussions involving senior professionals, a set of 47 interviews with chief audit executives, audit committee members and non-audit senior executives as well as a review of the academic and professional literature, this study offers a way of thinking about enhancing the value of internal auditing in the public sector and clarifies how internal auditors can help build a more innovative public sector. It also identifies eight areas where improvements are possible to deliver more value in the years ahead.

The value of internal auditing is about organizational learning as much as assurance

Internal auditing delivers value in two main ways: (1) it provides comfort and reassurance, mainly for senior officials, as a review and accountability function and (2) it fosters organizational learning on how to improve management controls, governance processes and risk management through audit and advisory services beneficial to managers and executives involved in operations. Moreover, learning contributes to comfort by helping reassure senior officials that audit findings and expertise are being used to improve performance and avert future problems.

While the provision of comfort and reassurance remains essential, we found that the elements of audit services that are currently considered to be of best value are those associated with organizational learning. As such, the core finding of the study is that enhancing internal auditors’ contribution to organizational learning is the most promising pathway to enhancing the function’s value to the public sector in the future.

Current drivers of value and effectiveness of public sector internal auditing

The factors associated with internal audit effectiveness in the private sector are also seen as driving effectiveness and value in the Canadian public sector. These factors include the use of risk-based audit plans, a focus on evaluating and improving internal controls (as opposed to a more traditional focus on compliance and financial transaction audits), a highly qualified and diversified audit team, a respected chief audit executive who communicates well, an appropriate level of independence from management, strong support for the audit function from senior executives, and auditors who have in-depth knowledge of operations and are sensitive to the needs of program managers.

While we found consensus on the importance of these factors and attributes, we also found that:

- While audits focused on the effectiveness of internal controls or on value-for-money are generally considered of greater value and should be encouraged, organizations should still carefully build their audit plans based on a careful assessment of their risks, their state of development and their business strategy. There is no single best formula.
While most jurisdictions seem to provide adequate levels of independence to their audit function, in some jurisdictions, such as Québec and Saskatchewan, providing internal auditors in the core public service with stronger protection and central support could increase the effectiveness and value of internal auditing.

In most jurisdictions, the attraction and retention of a highly qualified diversified staff is an important challenge due to insufficient pay and classification. While most survey respondents and interviews agreed that adhering to IIA standards helped bolster auditors’ professional competence, the recruitment of employees with specialized knowledge (e.g. information technology) and good “soft skills” (e.g. interpersonal and communication skills) is a more prevalent concern for chief audit executives than expanding the share of employees with audit certifications.

The auditor as an agent of learning: Key findings on how to improve the value of audit services

Beyond these attributes of effectiveness, the study identifies eight areas where changes should be considered to enhance the value of internal auditing by improving its contribution to organizational learning:

1. Expanding the use of advisory services: While assurance services should remain the core function of internal auditing, a large majority of our respondents and interviewees believe that internal auditors could improve the value of their contribution by offering more advisory services. Moreover, in some jurisdictions, internal guidance was seen as unduly restricting the provision of advisory services, preventing internal auditors from offering more timely support to managers that could serve to prevent future problems for the organization.

2. Improving auditors’ knowledge of operations: A good knowledge of the client’s business and an understanding of the context of program operations are essential for offering high-value audit services. Our study found that this is an area that should be improved. The recruitment of auditors with program management experience, the use of rotational assignments to help auditors spend time in operations, the temporary assignment of non-auditors to audit teams for specific projects and, in some circumstances, the appointment of experienced non-audit executives as chief audit executives should be considered as ways of helping internal audit functions improve in this regard.

3. Improving the communication of audit findings: The effective communication of audit findings is essential to ensure that audit services achieve their full impact. In this regard, many organizations should consider moving to shorter and more strategic audit reports, with fewer and less prescriptive recommendations focused on core issues. At the moment, some organizations used standardized formats that can be highly constraining and require long writing and vetting processes that consume a lot of audit resources and hinder auditors’ ability to provide timely feedback. Internal auditors should also be encouraged to experiment with alternative methods of communication, more likely to effectively convey key messages to busy managers and executives in a convincing and timely manner.
4. Balancing the need for transparency, accountability and learning: The extent of public disclosure of internal audit reports currently varies across jurisdictions. At the federal level, internal audit reports are automatically disclosed to the public through departmental websites. In provincial jurisdictions, reports are typically accessible on demand through the access-to-information system. Our study found that, while they support government transparency, most audit executives believe that automatic disclosure makes it more challenging to use audit reports as a tool of learning and to build relationships of trust with auditees. The fear that audit findings could be used to blame ministers and executives, sometimes even be misconstrued by the media, encourages auditees to view auditors as "organizational cops" and creates an incentive against candid discussions of audit findings. As a result, to maximize the value of audit services as a learning and management tool, provincial jurisdictions should carefully consider the balance between accountability and learning before moving toward automatic public disclosure of internal audit reports.

5. Leveraging audit findings for enterprise-wide improvements: By conducting audits across their entire organization, internal auditors are in a unique position to gather intelligence about common weaknesses and particular best practices. To maximize the value of their services, internal audit units should ensure that they systematically leverage the findings of audits for the benefit of the entire organization. For example, audit units or central agencies should consider systematically reviewing audit reports for lessons (e.g. common weaknesses or best practices) that would benefit managers across their organization or even the entire public service and share these lessons widely to allow programs that have not been audited to learn from others' experience. Similarly, when common weaknesses are found, auditors should take the lead in developing enterprise-wide corrective measures or offering training to managers to help prevent future problems.

6. Engaging in a more concerted effort to expand the use of data analytics: Expanding the use of data analytics can help internal auditors deliver more value to their organization. These new tools and techniques will not only free some audit resources through the automation of some procedures, but they also promise to deliver faster, more reliable and more insightful analyses. We have found widespread support for greater use of data analytics across the country. However, to capture this potential, internal audit units will need to engage, sometime in partnership with central agencies, in more concerted efforts to overcome problems of data management and lack of qualified personnel. The central pooling of technical expertise should be considered in some organizations. Moreover, concerted efforts must be made to further explore and teach the potential of these techniques across the internal audit community, including with executives and auditors who will never acquire these technical skills. Deploying data analytics to good effect is not merely a technical challenge, but also a cultural one as it first requires entire audit teams to think differently about the use of data in auditing.

7. Expanding the role of internal auditing in enterprise-wide risk management: Internal auditors are specialists in risk management and the smart use of internal controls. To fully exploit their potential, internal auditors should go beyond auditing their organization's enterprise-wide risk management (ERM) framework and actively contribute to the development of a more sophisticated approach to risk management across their organization.
While carefully avoiding taking any direct responsibility for the creation and management of the ERM framework, auditors should champion the adoption of such a framework and, more generally, provide services that will help managers better understand and identify risks (e.g. teaching or facilitating risk self-assessment exercises) as well as develop good controls and risk management strategies. In many organizations, internal auditors should clarify their relationship with the risk management function and explore more collaboration, including through the sharing of risk information and the secondment of personnel.

8. Improving collaboration with the program evaluation function: In many organizations with a program evaluation function, closer collaboration with internal auditors could help enhance the value of both functions. At the moment, organizational silos and differences in professional identities limit such collaboration in many organizations, but, as centralised review functions, evaluation and auditing would mutually benefit from sharing more information and insights on their organization’s programs and processes and even from sharing resources when the same expertise is required to complete part of an audit or evaluation. Moreover, better coordination would help avoid audit fatigue for managers who must collaborate with both functions within a short timeframe. While bringing both functions under common leadership would facilitate collaboration in many organizations, with some effort, improvements could often be realised without any restructuring.

**Internal auditors are well positioned to help their organization become more innovative**

Given their focus on the assessment and improvement of controls and processes, internal auditors are naturally well positioned to help their organizations innovate. In a public sector too often characterised by resistance to change, their professional commitment to continuous improvement is especially valuable. In this perspective, while internal auditors might profitably develop and offer some innovation-specific services (e.g. audits of learning culture or innovation benchmarks), their most important contribution to an emerging innovation agenda in government is more likely to come through their role as agents of organizational learning. Organizational learning is an essential ingredient of innovation. By maximizing this aspect of their contribution, internal auditors will improve the public sector’s capacity to innovate and to meet the expectations of governments and the public in the future. Providing more advisory services, especially on transformation projects, and helping managers overcome excessive risk aversion by helping them understand risks better and use controls more efficiently could prove especially useful to several public organizations striving to innovate.
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Over the last decade, internal auditing has made significant strides in Canada’s public sector. In fact, while progress has not been uniform across the country, it does not seem exaggerated to say that, in some jurisdictions, internal auditing is living a bit of a “golden age”. At the federal level, in Ontario and in Nova Scotia, for example, it’s hard to think of an era when the internal audit function of the public service has been better resourced, more professional and better institutionalised than it is currently. To be sure, challenges remain in these jurisdictions as well as in others where strategic choices and fiscal pressures have not supported the development of internal auditing to the same extent. Nevertheless, on the whole, the Canadian public sector is now better supported by professional internal auditing than it has been for much of its history.

However, while internal auditing was being strengthened and professionalized, the public sector was also coming under pressure to adapt to a demanding and fast-changing environment. Despite significant reforms to improve in this regard, public demand for more accountability and better stewardship of public resources is unrelenting. As a result, public managers are continuously being asked to deliver better services more efficiently, exercise better control over limited public resources and provide more accountability for their performance. At the same time, in the face of global competition, demographic change and technological transformation, public managers are also being challenged to take more risk, innovate and find new ways to meet the public’s changing needs. This demanding environment is not only a challenge for ministers, senior executives and managers; it also raises questions about what internal auditors can do to help the public sector perform under these conditions.

Our mandate

In this perspective, the central question that we were asked to explore is: how should internal auditing position itself to maximize the value that it will bring to the public sector in the future? In the coming years, public sector leaders will face strategic choices about how to best use and develop the internal audit function. How should they think about these choices? How can they offer more effective and valued services? As public organizations struggle to become more effective, efficient and innovative, how can they maximize the value that they get from their internal auditors?

This broad line of inquiry led us to contemplate a set of ancillary questions. What is the value that internal auditing currently brings to the public sector? In the context of modern internal auditing, value is a broad, somewhat ambiguous concept, which certainly goes far beyond fraud prevention and the financial savings derived from audit work. So how should we think about the value of internal auditing? Are some audit roles or practices more valuable than others? Are there some higher-value activities that can be emphasized and expanded? Are there some audit processes and practices that could be reviewed and improved to help auditors contribute more value to their organizations? As the public sector seeks to become more effective, efficient and innovative, what
role should internal auditing play in the achievement of these goals? Is the changing context calling for a new approach to internal auditing? A simple consolidation of recent gains? An acceleration of existing trends?

Given the great diversity of resources, organizational designs and environmental pressures currently characterizing internal auditing across the Canadian public sector, it is clear that there is no single “right answer” to these questions. Depending on the particularities of their context and their specific strategic objectives, organizations will rightly focus on different priorities to maximize the value of their internal audit services. Hence, while our report offers some concrete recommendations, it mainly aims to stimulate and inform the thinking of practitioners – hopefully even trigger some debate – about the way forward for internal auditing in the Canadian public sector. Based on a combination of conceptual and empirical work, we propose a way of thinking about maximizing the value of an internal audit function at this point in time and offer a menu of possible changes in audit practice that can be considered in light of the readers’ particular circumstances.

Methods

This research report is not a “desk study”, solely based on a review of existing literature and academic musings about the nature of internal auditing and its role in today’s public organizations. While our reflection is certainly informed by a review of the academic and professional literature on internal auditing and on related matters, such as organizational learning and public sector innovation, we first-and-foremost turned to practitioners themselves to form a view of the current state of internal auditing and what the function can do for the public sector in the future. Consequently, our findings and recommendations are essentially derived from our analysis of the descriptive and normative information provided by close to five hundred internal auditors, audit executives and managers, non-audit executives and members of audit committees who agreed to participate in our study.

To gather this data, the project used several sources and a combination of methods. We began by holding a group discussion with twelve federal and two provincial audit executives or managers at the University of Ottawa in September 2015. This meeting was organized in collaboration with the federal Office of the Comptroller General. During this discussion, participants were asked to share their views on the state of internal auditing, the challenges that they face and how they saw the potential for change and innovation in the future. Over the winter, we also observed a few meetings of a federal committee of chief audit executives on innovation, listening to presentations and the discussion of the committee’s members on innovation in the federal Public Service. We also consulted some of the research reports and other documents prepared for those meetings.

Then in November 2015, we brought together eleven high-level professionals related to the internal audit community from the Ontario and federal public sectors for a roundtable also held at the University of Ottawa. Amongst others, the participants included the Comptroller General of Canada, the Auditor General of Canada, a deputy minister involved in driving innovation across the federal Public Service, several former deputy ministers who now chair or serve as members
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of audit committees for federal departments, the chair of the audit committee of a large Crown corporation in Ontario and a representative of the Internal Audit Division of the Treasury Board Secretariat of the Ontario Public Service. During this roundtable, participants debated internal auditing’s current strengths and weaknesses, its potential for innovation and its role in fostering innovation across the public sector. The views expressed at those two events were recorded as data for our project, but we also used the insights gained from those early discussions to prepare the next steps in data collection: a series of one-on-one semi-structured interviews with key informants from federal, provincial and territorial public organizations and an online survey sent out to internal auditors across the country’s public sector.

From January to June 2016, we completed 47 interviews, each lasting typically between one hour and one hour-and-a half, with chief audit executives, audit managers, members of audit committees, non-audit executives, executives from legislative audit agencies and a professor with expertise and experience in public sector auditing. 18 interviews were conducted at the federal level and 28 were done with auditors or executives in ministries or agencies from ten different provincial or territorial jurisdictions. The interviews were guided by a common set of open-ended questions. However, as is standard in semi-structured interviews, the conversation took different directions based on the interviewees’ context, experience and expertise. Interviewees were offered anonymity to encourage them to speak freely and offer candid opinions about the state and future of internal auditing in their organization. 13 interviews were conducted in French. However, to better protect anonymity and to make the report easier to read, excerpts from these interviews used in this report have been translated in English.

Finally, we conducted an online survey of internal auditors from the public sector in the spring of 2016. Delivered in partnership with the Institute of Internal Auditors (IIA), the survey comprised approximately 110 questions, including an open-ended question where respondents were asked to briefly describe a change they would make in their organization to enhance the value offered by the internal audit function. We obtained 400 completed questionnaires. 51.3% of our respondents work for federal agencies or departments and 37.5% work at the provincial level. The remaining 11.4% work in the broader public sector (e.g. hospitals, school boards, municipalities) or for a private firm working for public sector clients. More information on methods is available in appendix A.

Our message

Based on our review of the professional and academic literature as well as the empirical material gathered specifically for this study, we argue that, as it is currently practiced, internal auditing services deliver value in two main ways: (1) they provide comfort or reassurance, mainly for the senior leadership, as a review and accountability function and (2) they foster organizational learning on how to improve management controls, governance processes and risk management through services that more extensively involve line managers and executives directly responsible for operations. Through our research, we found that, while the provision of comfort and reassurance remains essential, the elements of audit services that are considered to be of best value and to hold most promise for maximizing the function’s value in the future are mostly associated with its contribution to organizational learning.
To be clear, we do not advocate weakening or abandoning internal audit’s core role as a provider of comfort to the governing bodies or senior administrative leaders of public organizations on issues related to controls, governance and risks. However, we argue that, as the public sector faces the challenge of innovating and adapting to a fast-changing environment, more attention should be paid to the internal auditor’s valuable contribution as an agent of organizational learning. By maximizing this aspect of internal audit’s contribution through its assurance and advisory services, the public sector will improve its capacity to meet the expectations of governments and the public in the future.

In most public organizations, moving in this direction will not require a fundamental repositioning of the internal audit function, but it will require a considered and concerted effort to look at internal auditing through a learning lens and practice it in a way that fulfils its potential in this regard. Based on the data collected for this project, the report discusses eight areas where some changes in policy, structure or practice could help public organizations move in this direction. We hope that these suggestions, essentially drawn from practitioners, will help other practitioners think about how to maximize the future contribution of internal auditing in the public sector.

A good deal of the current discourse around internal auditing tends to emphasize its “defensive” nature: as the third line of defence, it represents the final safeguard against lapses in the stewardship of organizational resources. Without questioning the importance of internal auditing in preventing such gaps and breakdowns in stewardship, this emphasis on its “defensive” role is framing the value of internal auditing in a manner that runs the risk of actually underplaying its already important contribution to organizational change. At a time when public organizations are expected more than ever to continuously improve and innovate, we fear that an excessive focus on its “defensive” virtue could leave internal audit’s potential unfulfilled.

Structure of the report

The report is divided into four parts. In the first, drawing from the academic and professional literature, we examine how we can think about the value that internal auditing brings to the public sector. We argue that, while the traditional focus on the provision of reassurance to the higher level of the organization remains core to the IA function, its current “value proposition” is in fact broader and multifaceted. In particular, auditors already play – and increasingly so – an important role in raising awareness, providing advice and helping managers learn about the efficient use of controls, the proper design of governance processes and the effective management of operational risks. Comfort and learning are the backbone of internal audit value.

The second part of the report then looks at the drivers of internal audit effectiveness and value: what are the factors that can be associated with an effective and high-value internal audit function? To do so, we reviewed the academic literature on internal auditing, much of it dealing with the private sector, and compared its findings with what we heard from our interviews with public sector auditors and other officials. We found that the main drivers of value and effectiveness identified in the private sector are also present in the public sector, although, in some cases, a more contextualised interpretation of those factors is required. In this regard, in addition to
providing a list of effectiveness and value drivers, this section discusses three factors at greater length: human resources challenges, the role of traditional financial and compliance audits, and the need to strengthen the independence of the function in some jurisdictions.

In the third part of the report, based on our interviews and our survey, we identify eight areas where some changes in policy or practice could help internal audit functions deliver more value to their organization. These areas include: offering more advisory services; finding mechanisms to help auditors enhance their knowledge of their clients’ business; rethinking how audit findings are communicated, particularly the role and format of audit reports; rethinking the balance between transparency, accountability and learning; increasing the enterprise-wide dissemination of lessons drawn from audit work; having the internal audit function offer training in selected areas; expanding the use of data analytics tools; enhancing the role of audit in strengthening enterprise-wide risk management; and, in some jurisdictions, improving the collaboration between the audit and evaluation functions. In all those areas, we discuss the views collected through our research and offer some suggestions on how to move forward.

Finally, in the last part of the report, we discuss more directly the relationship between internal auditing and innovation in the public sector. What role should internal auditing play in supporting innovation in their organization? Based on our empirical research and our review of the academic literature, we argue that, while internal auditors might profitably develop and offer some innovation-specific services (e.g. audits of learning culture or innovation benchmarks), the most important contributions that the function could make to innovation is more likely to come through its role in organizational learning, including through the provision of advisory services and the dissemination of a more sophisticated, balanced approach to risk management.
1. THINKING ABOUT THE VALUE OF INTERNAL AUDITING
ENHANCING THE VALUE OF INTERNAL AUDITING IN THE PUBLIC SECTOR

As the standards-setting body of the profession, the Institute of Internal Auditors (IIA) defines internal auditing as “an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations”. Hence, the provision of value-added services is considered the very purpose of the profession. An internal audit function that would not generate net benefits to its organization would not be worth having (Chambers et al., 1987; D’Onza et al., 2015: 182). On this basic point, there is not much debate. However, asking exactly how internal auditors bring value to their organization and how to approach auditing or design audit services to maximize this value does not yield a similarly straightforward or unanimous answer.

In sum, audit value is both difficult to define and difficult to observe or measure. Much depends on the organizational context and on the effectiveness of important but not always tangible contributions.

The complexity stems partly from the fact that audit value means different things to different people: like beauty, it often lies in the eye of the beholder. Depending on one’s understanding of the current needs of the organization as well as the role and potential of the internal audit function, different executives may well find some types of audit activities more valuable than others. What serves an invaluable purpose in an organization may well be marginal to another organization operating in a different context and pursuing a different business strategy.

Moreover, even assuming that the “right things” are done, the quality and effectiveness of audits are difficult to assess. An audit’s effectiveness is often not completely, directly observable, except when it fails (Lenz, D’Onza and D’Silva, 2014: 126). As the head of internal audit of the UK Civil Service recently pointed out to a critical parliamentary committee:

“It is really quite difficult to assess the value for money of an internal audit service. [...] Partly that is the nature of what we do: it is very difficult to prove a negative. If interventions from internal audit have been instrumental in bringing about better outcomes, it is very difficult to prove. It is far easier to look at failures and ask the question, ‘Where were the auditors?’”1

The problem is not helped by the fact that internal auditing has become incredibly diverse and now plays a more complex, multifaceted role in organizations. The years when the profession saw the control of transactions, the validation of financial information and the detection of fraud as its main purpose are long gone. As our societies have changed, our understanding of risks has evolved and organizations have grown more complex, the scope of internal auditing has greatly expanded and its methods have diversified. In recent years, the IIA’s global survey of internal audit trends has shown that the typical audit department now only dedicates about 20% of its resources to financial audits, while twice as much is spent looking at other aspects of operations or at compliance with policies and regulations (Kranacher, 2012: 18). Moreover, from procurement, cyber security, staffing and ethics to environmental management, it has become hard to think of an area where auditing is absent or considered inapplicable. As Michael Power argues, industrialised societies have undergone a veritable “audit explosion” since the 1980s (Power, 1999; 2015).

Such diversity in internal audit practice is also found in the Canadian public sector where verifying compliance against legislative and policy requirements, reviewing the effectiveness of internal controls and risk management as well as assessing performance and “value-for-money” have come to occupy much of the time of many internal auditors. While some public organizations still devote almost all of their resources to traditional financial audits, the internal audit functions of some provincial and territorial public services have abandoned them altogether in favour of operational or value-for-money audits. In fact, even if 44.8% of our survey respondents still see assuring compliance as their most important function, most chief audit executives and senior executives interviewed in this study believe that the best value now lies in audits that assess and improve internal controls or assess whether programs deliver value for money.
Moreover, in addition to “core” audit services, many public sector internal audit units now spend a considerable part of their time and resources on ancillary services. For example in some provincial public services, the provision of advisory services already represents about half of the “audit” engagements completed in a given year. In some smaller jurisdictions and agencies, administrative investigations can eat up more than a third of the audit team’s time. In the Québec Public Service, departmental auditors even spend 22% of their time validating the reliability of data presented in departmental annual reports, as much time as they spend on compliance audits and more than twice as much they devote to the auditing of risk management, operational efficiency or performance (Vérificateur général du Québec, 2016: 15).

This multiplicity of services is no doubt illustrative of the potential of internal audit as an independent review function in today’s public sector. However, the combination of limited resources and multiple possible services means that audit committees, senior executives and chief audit executives must make hard choices about how to best use the resources available to them. In order to guide these choices, they need to think about the type of value delivered by various services or how different ways of approaching their audit role might generate more value for their particular organization. In the end, these choices will (and should) vary across organizations: an organization’s context, strategy and state of development will always mean that different audit services will be more or less fitting and valuable. However, in this report, we offer some guidance on how to think about audit value and consequently inform these choices.

Some specific tools can undoubtedly contribute to enhance value across most organizations. For example, risk-based audit plans, which most of our interviewees reported using, although with varying degrees of sophistication, certainly constitute an important tool to help make some annual allocation decisions. For any organization, provided sufficient flexibility is retained and plans are frequently updated, it makes eminent sense to have internal audit focus on issues and areas believed to represent greater risks. In this perspective, the larger the problems avoided, the more valuable the contribution made by internal auditing. For this reason, risk-based auditing is now widely recognized as a key characteristic of an effective internal audit function (Lenz and Hahn, 2015: 14; Lenz, Sarens and D'Silva, 2014: 133; Allegrini and D’Onza, 2003).

However, risk-based audit planning only partially addresses the question of how to best use internal audit resources to maximize their contribution to an organization’s performance. For example, it does not shine much light on whether some types of audits are generally considered to add more value than others, on whether advisory or non-audit services should be encouraged or on whether changing how audit engagements are performed (as opposed to the nature of those engagements) could generate more value.

To offer some guidance on these broader questions, it is then necessary to examine more closely how internal auditing is currently seen as a value-added activity and whether, despite the diversity of organizational needs and conditions in which internal auditing operates, it is possible to identify common characteristics, approaches or practices associated with a high-value public sector internal audit function. To start addressing some of these questions, we first examine how the role of the internal audit function and its value has been formally conceptualized in the academic and professional literature.

1.1 The fundamental value of an internal audit function: comfort and learning

Despite considerable changes in the profession’s scope and methods, the value of internal auditing remains strongly associated with the provision of assurance to the organization’s senior executives, audit committee or governing body. In this traditional view, the function’s core value lies in offering an impartial and professional assessment of the organization’s management controls, governance processes and risk management in order to reassure its governing body and/or top executives that its
resources are properly managed. These assessments also reassure top executives that they have sound information to use in making decisions and rendering accounts for the organization’s performance. In the academic literature, this contribution of the internal audit function is well documented and at times labelled the “comfort” value of auditing (Pentland, 1993; Carrington and Catasus, 2007; Sarens et al., 2009; Abela and Mitchell, 2014: 7-10).

To fully deliver this kind of value, internal auditing must rest on high levels of technical skills, strict adherence to professional standards and clear independence from the organization’s operations. Independence is especially important in this context: no senior executive could be reassured about the conformity and effectiveness of management processes unless she can be confident that such judgements are based on a rigorous, fact-based study and reached in full independence of the managers directly involved in designing and operating the process reviewed. Ideally, the internal audit function should also not only have direct access to the most senior executives of the organization but also its governing body (or one of its committees) to ensure that management does not filter its opinions. While the unique requirements of democratic governance in much of the public sector makes the lines of reporting typically more complex, the emergence of audit committees in most public organizations certainly reflects similar ideals of independence, accountability and oversight.3

The comfort value of internal auditing is manifest in the “three lines of defense” model “strongly recommended” by the Institute of Internal Auditors (2013).4 This model emphasizes the need to clearly distinguish among operational managers (the first line of defense) who own and manage risks, the risk management, control and compliance functions (the second line of defense) that monitor and support managers as they operate internal controls and manage risks, and internal auditors (the third line of defense) who assess the effectiveness of governance, risk management and internal controls in order to provide assurance to the organization’s governing body and senior management. In this model, what distinguishes internal audit from the other lines and makes it so valuable is its unique capacity to provide senior leaders with an independent opinion on the performance of processes designed and operated by managers.5

The IIA recognizes that, under resource constraints, organizations may exceptionally be forced to combine some of these lines, but the guidance is clear that effective risk management depends on clearly separating (and coordinating) these three functional levels (Institute of Internal Auditors, 2013: 7). Only under such proper conditions of independence and distance from operations can internal auditing deliver the kind of effective protection and assurance that should make it a “requirement” for all organizations (Institute of Internal Auditors, 2013: 5-6). To this way of thinking, it is clear that internal auditing’s core contribution to the organization’s performance is to help “defend” or “protect” it against internal and external threats.

Since the early 2000s, the growth of internal auditing in the private and public sectors is largely attributable to an increase in external demand for such comfort value through the provision of higher levels of assurance (Spira and Page, 2002: 654). In the private sector, financial and accounting scandals have led to a series of policy and legislative reforms, most recently the Sarbanes-Oxley Act in the US and Bill 198 in Ontario, that have bolstered the role of internal auditing in corporate governance.

Similarly, in the Canadian public sector, the strengthening of internal auditing has often been associated with scandals and public demand for greater accountability. This may have been most evident at the federal level, where the “sponsorship scandal” was the main impetus for the adoption of the Federal Accountability Act, the re-creation of the Office of the Comptroller General and the adoption of the 2006 Policy on Internal Audit (Benoit and Frank, 2006; Free and Radcliffe, 2008; Neu, Everett and Ramahan, 2013).6 These reforms led to a considerable strengthening of the audit function, including the statutory obligation...
for departments to maintain audit functions and independent departmental audit committees with a majority of external members (Larson and Zussman, 2010). However, a similar pattern of reform can also be observed in some of the provinces, such as Newfoundland and Labrador where the MLAs’ constituency allowance scandal and the Green Report triggered a substantial rebuilding of the internal audit function (Review Commission on Constituency Allowances and Related Matters, 2007).

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Despite this strong rhetoric of accountability, protection and defense, it is equally clear that internal audit’s main stakeholders are now expecting something more than simple reassurance. Internal auditors are more than “experts in providing comfort” (Sarens and al., 2009: 100). In its official definition, the IIA itself defines internal auditing as a function designed to improve an organization’s operations and, in its explanatory material, the value of internal auditing is presented as the result of a combination of objectivity, assurance and insight.7 Hence, more than opinions about the effectiveness of controls and risk processes, auditors are expected to generate insights and recommendations that will be taken up by management and will lead to actual changes in the organization. As Rick Kennedy and Terry Hunt put it in the context of the Canadian public sector, fundamentally, the role of internal auditing is also to equip executives with strategic insights on the design and operation of the governance, risk management and control processes of their organizations (2015: 24).

However, as an independent review function, internal audit cannot (and should not) impose operational changes. As a consequence, to have an impact on operations, senior executives and, maybe more importantly, auditees must understand, trust and value the function’s insights, believe its recommendations to be helpful and relevant, and readily attempt to use them to improve their work. In sum, despite the standard “management action plan” officially responding to audit findings, the effectiveness – and more generally the value – of internal auditors will depend significantly on their ability to understand the business of the auditees, to gain their trust and to provide information and expert advice from which they improve their operations. In this perspective, internal auditors are not solely “protectors” or “defenders” of their organization: they must be facilitators of organizational learning and agents of change in a process of continuous improvement of their organization.

For internal auditors to deliver “learning value”, the submission of a formal audit report primarily aimed at reassuring or alerting the top of the organization will not do. To realize their potential as agents of organizational learning, internal auditors need to be particularly attentive to their relationship with another set of stakeholders: operational managers and the executives directly responsible for delivering programs and operating processes. They need to ensure the development of a trust relationship with those stakeholders. They need to focus on how to best identify and communicate solutions to those who will need to adopt and implement them in their particular context. They need to consider how they can have a more profound and lasting impact by changing how managers and executives will improve the way they deal with risk, governance or controls in the future, including in the context of other non-audited operations.

In the context of the Canadian public sector, this more complex value proposition might have been best recognized in a recent research report written for the Institute of Internal Auditors Canada by Carmen Abela and James R. Mitchell. In Unlocking the Power of Internal Audit in the Public Sector (Abela and Mitchell, 2014), the authors identify a “three-pronged value proposition” that presents internal auditors not only as protectors but also as educators and business advisors. In particular, drawing from interviews with deputy heads from the federal public service, they note that, in addition to supporting their accountability responsibilities by providing some oversight of operations, senior executives also expect auditors to spread the knowledge of managerial best practices throughout the organization and even offer forward-looking
solutions anticipating emerging problems and risks. In sum, more than simple reassurance about existing controls, the executives interviewed were expecting auditors to help managers become better informed and skilled in the strategic use of controls and risk management. They were also expecting auditors to be a source of foresight as the organization faces a turbulent environment.

Abela and Mitchell are not the only ones looking beyond traditional assurance. The literature on internal auditing in the private sector also highlights how the profession has diversified its services in an attempt to demonstrate its value to sceptical stakeholders and more actively support the achievement of business objectives (e.g. Bou-Raad, 2000; Mihret and Woldeyohannis, 2008; Arena and Azzone, 2009: 44). The ability to trigger and support the continuous improvement of business processes is an important dimension of this “value-added” approach to auditing and seeks to meet managerial expectations. As a senior manager puts it in a study done by Gerrit Sarens and his colleagues, an important source of value comes from the auditor “being able to make things happen” (Sarens et al., 2009: 99). Some of the core processes of organizational learning – knowledge creation (through quality auditing), acquisition (including trends and best practices from external sources), interpretation (through transferring and adapting knowledge to the organization’s context) and dissemination (through effective communication with auditees and executives) – are crucial to the internal audit function’s to contribute to such process improvements.

In a study of the American and Belgian private sectors, Sarens and De Beelde also find an important “teaching role” being played by the internal audit function, especially in relation to the improvement of risk management. The authors argue that this “pioneering role in the creation of a higher level of risk and control awareness” is an opportunity to “demonstrate their value” to their organization (Sarens and De Beerle, 2006: 63). Examining the evolution of internal auditing in Australia, Bou-Raad similarly notes a trend toward more “learning-based” models where auditors help auditees improve their understanding of business processes (e.g. through control self-assessments) and learn how to improve their practice (Bou-Raad, 2000). Furthermore, in his study of high-value, innovative internal audit functions, Roth also notes that, in these departments, “auditors are encouraged to be trainers, coaches, and counselors of internal control, not just evaluators” (Roth, 2003: 36). And, of course, the growth in consulting / advisory services to supplement the traditional focus on assurance has been well documented and encouraged by the IIA (e.g. Anderson, 2004; Lenz and Sarens, 2012).

In sum, from the ultimate defender/protector to a catalyst of organizational change, a management educator and a trusted advisor to executives, the internal auditor is now expected to play a multiplicity of organizational roles. There is no doubt that this trend has created a fair degree of confusion and debate about the internal audit function’s “primary client” and its “real” role in the organization (e.g. Soh and Martinov-Bennie, 2011: 611-612; Lenz and Sarens, 2012: 541-542). In practice, few would claim that most internal audit functions are fulfilling all these roles, let alone meeting the expectations of all these various stakeholders. On this score, several professional reports and academic studies have noted “expectations gaps” and the difficulty that internal auditors face in meeting such varied demands in practice.

However, as we consider these evolving expectations, we see that, despite the diversity of their roles and the services that they offer, internal auditors ultimately make two types of valuable contribution to public sector organizations: (1) they provide comfort to their stakeholders, mostly senior executives but also often audit committee members or sometimes even ministers, as they discharge their accountability requirements and (2) they help executives and managers learn about the state of their operations and about ways to improve them, especially in the face of challenges. On the whole, through both assurance and advisory services, comfort and learning are the two cornerstones of internal audit value.8
Over the course of our research, as we asked interviewees how they were adding value and how they could improve, it was striking how few comments were directed at the provision of comfort to senior executives – how to provide greater confidence about compliance, effectiveness or even value-for-money. Reassuring deputy heads and audit committee members obviously remained important in the minds of the chief audit executives that we interviewed, but, when asked about how to deliver value to their organization, the vast majority of interviewees talked about issues related to organizational learning – how to meet line managers’ needs, how to help them improve organizational processes, better understand and manage risks, etc. These contributions, whether they come in the guise of assurance or advisory services, are essentially about helping the organization learn from its current performance, consider best practices from outside and improve itself.

Relatedly, when our interviewees talked about the importance of meeting the “customer’s needs” and of knowing the “clients’ business”, which they did a lot, they were seldom talking about people occupying the top floor of the executive suite: they were mostly referring to the line managers “owning” the business processes and the executives most directly responsible for meeting program objectives. Again, it was not that chief audit executives seemed dismissive of the needs of chief executives and audit committees – that was clearly not the case – but rather that they obviously felt that an important part of meeting their expectations involved having an impact on the frontlines of the organization. As it has been pointed out in previous studies (e.g. Gendron et al., 2004; Sarens et al., 2009), helping deliver improvements in business processes, raising awareness about risks, educating managers in the better use of controls – all those activities dependent on organizational learning – also contribute to the sense of comfort and reassurance of audit committee members and senior management. Learning and comfort go hand in hand.

However, to enhance the value that internal audit activities can bring to an organization, it is imperative to explicitly consider how they can be approached and organized to maximize organizational learning. As we will see, the eight areas identified for consideration and potential improvement in the third section of our report largely focus on this problem. But, before we discuss these areas, the next section examines the academic literature on internal auditing and draws from our empirical data to identify the factors commonly associated with high value and effectiveness of internal audit functions.
ENHANCING THE VALUE OF INTERNAL AUDITING IN THE PUBLIC SECTOR
2.

THE DETERMINANTS OF INTERNAL AUDIT EFFECTIVENESS AND VALUE
Table 1

Factors associated with ability of the internal audit function to be effective and add value

<table>
<thead>
<tr>
<th>Main drivers of value or effectiveness identified in academic literature</th>
<th>Factors cited by interviewees</th>
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<tbody>
<tr>
<td>Agreement on an audit charter with audit committee and senior management</td>
<td>✓</td>
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<tr>
<td>Independence / direct functional reporting to a strong audit committee</td>
<td>✓✓✓</td>
</tr>
<tr>
<td>IA appreciation and strong support from senior management</td>
<td>✓✓✓</td>
</tr>
<tr>
<td>Stature, IIA membership, political acumen and communication skills of the CAE</td>
<td>✓✓✓</td>
</tr>
<tr>
<td>Offering a larger number / diversity of services (incl. advisory services)</td>
<td>✓✓✓</td>
</tr>
<tr>
<td>Focus on evaluating and improving internal controls (vs compliance, financial)</td>
<td>✓✓✓</td>
</tr>
<tr>
<td>Grading audit reports and/or specific observations (e.g. traffic light system)</td>
<td>✓</td>
</tr>
<tr>
<td>Technical skills of internal auditors (incl. prevalence of training, certifications)</td>
<td>✓✓</td>
</tr>
<tr>
<td>Soft skills of internal auditors (e.g. communication, diplomacy, courage)</td>
<td>✓✓</td>
</tr>
</tbody>
</table>
Some of these drivers of effectiveness and value will be discussed in greater detail in the second part of the report. However, we can already note that the overall picture that emerges from the literature review and interviews is one where a high-value internal audit function rests on a diversified team of skilled auditors who focus on high-risk areas, cultivate good trusting relationships with line management, ensuring an in-depth understanding of their business, and offer a wide range of services, using a diversity of tools, seeking to help the organization improve its processes. It is also led by a savvy and respected chief audit executive who, through good communication, nurtures strong relationships with senior management and the audit committee, gaining their trust and support for the internal audit function. While assembling or developing all these characteristics may be challenging for any internal audit function, the overall picture should nevertheless be familiar to practitioners.

That being said, the list of determinants in Table 1 should be considered with care and proper consideration for the context of each public organization.

It is not a simple formula for effectiveness or value creation, but rather a list of factors identified in the literature and supported by our interviews. However, not all studies or interviewees have identified all these factors as sine qua non requirements for adding more value and, for some of those factors, academic studies on internal auditing effectiveness have in fact turned up ambiguous or contradictory results.

For instance, using a small number of in-depth case studies, Roth found that high-value world-class internal audit functions had a high percentage (more than 75%) of certified auditors. However, in a study of 153 Italian companies, Arena and Azzone did not find any correlation between the percentage of audit recommendations implemented and the use of auditors with a professional audit certification (Arena and Azzone, 2009: 54). Moreover, using data from the 2010 CBOK survey, D’Onza et al. did not even find a correlation between the use of IIA standards and the “ability to add value” (as perceived by the internal auditors surveyed) (D’Onza et al., 2015: 190). More generally, Roussy has found that, when assessing the competence of their internal auditors’ in-depth knowledge of their organization ✓✓✓
Size and range of expertise of audit team (e.g. accounting, operations, IT, legal) ✓✓
Selective use of co-sourcing and outsourcing ✓
Use of data analytics / computer-assisted auditing tools ✓✓✓
Using a risk-based approach to audit planning ✓✓✓
Using control self-assessment techniques ✓✓
Focus on the needs of senior management (incl. alignment with firm strategy) ✓✓
Focus on the needs of line managers ✓✓✓

Legend: ✓ = mentioned by at least one interviewee, ✓✓ = mentioned frequently, ✓✓✓ = mentioned frequently and emphasized as an important factor by several interviewees
auditors, members of audit committees in the provincial public sector in Québec stressed the need for some core values (e.g. courage, integrity) and “soft skills” (e.g. interpersonal and communication skills, judgement, political acumen, etc.) instead of their technical expertise (Roussy, 2012). Clearly, more work is needed to better understand the relationship between standards, certifications and audit effectiveness.

Our own study provides similarly qualified results on this score for the Canadian public sector. On the one hand, while only 42% of our survey respondents agreed to any extent that the IIA standards were well adapted to the public sector, 85.4% believed that adhering to the standards strengthened their professional competence. A few survey respondents even thought that making certification mandatory for all auditors would be one of the most important steps that could be taken to deliver greater value to the public sector.

On the other hand, many of our interviewees were more equivocal. While most chief internal auditors viewed certifications favourably, many of them warned that they should not be taken as a guarantee of expertise, that “on the job” training was at least equally and often more important and that more attention needed to be paid to some of the “soft skills” of auditors, especially communication skills, and the availability of specialized expertise (e.g. IT, cyber security). Moreover, the recruitment and retention of qualified auditors was a very important preoccupation in many jurisdictions, including concerns with gaining appropriate classification levels for auditors and offering competitive salaries. Amongst all of these personnel issues, which were clearly significant issues to address to ensure more effective internal auditing functions in many jurisdictions, few interviewees actually talked about certification as a key step to enhance value in the future.

Secondly, in considering the relative importance of effectiveness drivers, proper attention to the context of each organization is clearly important. For example, most of our interviewees confirmed that, generally, traditional financial and compliance audits were not the best way to add value to their organization, compared with audits focused on the design and effectiveness of internal controls or value-for-money audits. For example, the chief audit executive of a provincial agency in Québec told us:

“...In my organization, we spend 80% of our time on compliance, especially financial compliance, and, frankly, it does not result in a lot of value. We’re moving toward more advice, more resource optimization and value-for-money. That’s how internal audit should be used now, but we’re a relatively ‘young’ [internal audit function] and it takes some time.”

This view was widely shared by our interviewees.

That being said, several interviews also made the point that, in some circumstances, more traditional audits remain essential. For example, in cases where there is a significant probability that a breach in compliance will occur and lead to sizeable material losses, legal or reputational repercussions or even loss of life, regular compliance audits represent an excellent value for the organization.

Similarly, in cases where a public organization is struggling with recurring and significant problems of fraud or mismanagement, it makes perfect sense that financial and compliance audits would play a bigger role. As the chief audit executive of a provincial public service put it:

“We shouldn’t get wrapped up in the trend of the day. Compliance audits that ensure that we have proper financial controls already ring terrific value to the government. So, yes, performance audits could help us save some money, but, if we end up lacking good...
Likewise, another audit executive explained:

“Generally, we try to stay away from compliance audits. They bring very little value to the organization and, by the way, they often say what the managers already know. The work that focuses on the optimization of processes is very important. That said, we give out millions of checks per week, so some amount of financial compliance work is certainly necessary. It still has to be a mix.”

In sum, while we found strong support for the view that evaluating the performance of controls and helping improve them or using audits to assess value-for-money were higher value activities, in the end, a careful assessment of the organization’s maturity, context and risk environment should remain determinant.

Finally, in considering the determinants of effectiveness and value, some differences between the private and public sectors should also be taken into account. In particular, the independence of the function is bound to hold a different meaning and to beget different institutional consequences in the public sector than in the private sector. In large publicly owned private corporations, independent audit committees are agents of the board of directors and, with the help of non-executive members, represent the interests of shareholders. Internal audit functions typically functionally report to them, while still holding a reporting relationship with senior management that, in theory, should be mostly focused on formal operational matters (e.g. budget, staffing).

While this generic governance model does not do justice to the diversity of situations actually found in the private sector or to the complexity of the function’s relationship with senior management, it does represent a strong idealized model of internal audit independence that has been promoted, including through legislation, in the aftermath of major scandals about fifteen years ago. Far from receding, calls for strong guarantees of independence have been rekindled, even amplified, in the aftermath of the more recent financial crisis, with some scholars advocating entirely removing the reporting line to senior management and having audit committees take control of the funding of the internal audit function (e.g. Chambers and Odar, 2015). In any case, as we noted in our table listing key determinants, a strong relationship with the audit committee and other guarantees of independence from management are now widely considered to be critical to audit value and effectiveness in the private sector.

The situation is slightly different in the Canadian public sector. While independence is also seen as very important, the identity of the “ultimate client” of internal auditing is more ambiguous. While most Crown corporations have institutional structures, including boards, that are similar to private corporations, the typical departmental form used in the core public service complicates matters. In the public service, cabinet and individual ministers are accountable to the legislature for the conduct of government business. As such, they could be considered as the proper equivalent of the corporate board of private companies. However, the senior permanent administrator (or deputy head) of a typical government department is also legally entrusted with the responsibility for the management of resources and the performance of the organization and this responsibility is at times associated with direct and exclusive parliamentary accountability obligations. Under
“The [2006] reforms made a huge difference for us. The legal requirements, the audit committees, but also the audit policy and the support of the [Office of the Comptroller General]. Even now, I don’t know what would happen if you took the [Policy on Internal Audit] out. I don’t think that internal auditing is part of the culture of government. I would not count on it.”

In almost all jurisdictions, it is clearly not. With the exception of the British Columbia Public Service, internal audit functions do not report directly to cabinet committees (or only through the submission of summary reports). The standard practice is rather to functionally report to a departmental or government-wide audit committee composed of senior executives. In the case of departmental audit committees, members are typically a mix of senior executives from one’s own department and a selected number of other departments. Across the country, the federal public service stands out with its legislative requirement that departments have audit committees composed of a majority of members recruited from outside the federal administration. In sum, in the public sector, independence mostly means being independent from line management and having direct access to senior executives.\(^{12}\)

It is important to stress that these institutional differences do not detract from the need for independence as an important safeguard of objectivity. In fact, our research strongly confirmed that independence is also seen as essential to audit effectiveness and value in the public sector. Without a good measure of independence, the reality and perception of objectivity would be hard to maintain and, under these circumstances, the internal audit function’s ability to provide assurance and to offer valuable insights on the effectiveness of controls, risk management and governance processes would be severely compromised. On this score, both interviewees and survey respondents agreed. For example, 79.2% of surveyed auditors either agreed or strongly agreed that independence is their “most important asset as an internal auditor”. Expressing a widely shared view, a federal chief audit executive said:

In sum, some institutional guarantees of independence, including central support in large public organizations with a decentralised structure, were largely seen as essential to the effectiveness of the internal audit function.

However, the extent to which the internal audit function is and must be independent does not seem to be as settled as in the private sector. In some provinces, interviewees clearly felt that greater independence was needed to deliver better value and more effective services. For instance, several interviewees with experience working in departments of the Québec Public Service (as opposed to the main provincial Crown corporations) felt that their internal audit functions lacked sufficient independence and central support. While the provincial government adopted an internal audit policy in 2006 asking deputy heads to create audit committees that should include at least one member from outside the department (but not necessarily from outside the public service),\(^{13}\) the strength of departmental audit functions still largely depends on the preferences of the department’s deputy head and, consequently, varies considerably across departments. In many cases, this very decentralised structure has led to a difficult environment for internal auditors and most interviewees believed that it has hampered the function’s effectiveness in many departments. In a characteristic comment, a senior chief audit executive stated: “the recognition of the role and importance of internal audit by the ‘centre’, with
2. THE DETERMINANTS OF INTERNAL AUDIT EFFECTIVENESS AND VALUE

The internal audit function of the Saskatchewan Public Service is equally decentralised. There is no government-wide audit committee and, amongst the few departments with an internal audit function, some still lack audit committees and even a clear chief audit executive. In the Department of Finance, the internal audit function is essentially conceived as an instrument for the Comptroller General to use as he fulfills his legislative duties related to financial management. As a result, the function has kept a narrower financial scope, reports directly to the Comptroller General and does not offer much central support or protection to departmental audit functions. In the last few years, the province has been considering an expansion of the internal audit function. A study published by the provincial Auditor General also recommended that a more centralized model be considered and that departmental audit committees be established or strengthened (Office of the Auditor General of Saskatchewan, 2012). Hence, it is clear that, in jurisdictions like Québec and Saskatchewan, the effectiveness and value of the internal audit function could benefit from stronger institutional guarantees of their independence or, at least, stronger central support for internal auditing across the public service.

On the other hand, most provincial internal audit functions did not seem to feel that they needed as strong institutional safeguards as those found in the federal public service to ensure their independence. In particular, several provincial chief audit executives were sceptical of the need of having external members on government-wide or departmental audit committees. Some of them stressed the distinctive nature of the public sector and wondered whether private sector members would really understand the complexity of public administration and unique pressures at play in the public sector. One of them also wondered whether internal members would feel at ease to have completely frank discussions with external members.

These views may not be unwarranted. While our federal interviewees were virtually unanimous in saying that the creation of departmental audit committees had improved their effectiveness, it should be pointed out that a considerable number of external members of those committees are actually former public servants. A recent study by Larson and Zussman points out that members from the private sector can feel less comfortable with the culture of the public sector and feel somewhat excluded from the “old-boys club” feeling that the presence of former deputy ministers can give to some committees. Some of them also feel uneasy about the more limited independence, more advisory role of the committees, compared to audit committees found in the private sector (Larson and Zussman, 2010: 13). In this perspective, reliance on former public servants could be seen as a way to alleviate some of the provincial concerns about bolstering committee independence through the appointment of external members. In any case, none of the provincial interviewees that had an audit committee presented the inclusion of external members as a potentially important step forward for their organization.

Moreover, even at the federal level, some of our interviews warned against putting too much emphasis on independence, for fear that it would encourage too much distance between internal auditors and the rest of the organization. The need to temper independence with responsiveness and a strong attention to the needs and realities of line managers and senior executives was raised by several interviewees. For example, the chief audit executive of a federal department told us:

“Now, there are some auditors out there arguing that management should have no say whatsoever in what I do or the scope of what I do. I would say that’s clearly wrong. We are an instrument of management […] and to take such a high road puts you in a position whereby management would
not want to come and seek your advice or assistance, [...] For me, it’s a very interesting walk to balance yourself where you have the appropriate mix of independence, objectivity, professional standards and, at the same time, being of value to management. If you can’t do that, then your value to the organization disappears.”

The chair of a federal audit committee, an external member, made a similar point when he recounted his experience in another department that had a director of audit who placed a lot of emphasis on his independence.

“He really interpreted his role as being independent from everybody in the department, including the deputy minister, and felt that he was really only accountable to the Comptroller General. He was a strong auditor, very smart guy, but the relationship was such that the audit committee had to play a role in helping the deputy minister manage this ‘rogue’ CAE. The department responded [to audits] in a ‘paper way’, but the relationship was not constructive and audits had less impact than could have been the case.”

While this situation is certainly not the norm, the story does highlight the kind of delicate balance between independence, responsiveness and engagement on which an effective internal audit function depends.

Interviewing audit committee members in the Québec public sector, Roussy documented similar views at the provincial level: her interviewees stressed that, in their view, one of the characteris-tics of a competent internal auditor is his ability to “balance proximity and distance” from line management (Roussy, 2012, 45). Without the objectivity that independence makes possible, the internal auditor has little of value to offer, whether he seeks to provide assurance or advice. However, if this independence creates too much of a distance with the executives and managers who run the business, he runs the risk of focusing on issues of lesser relevance, being seen as out-of-touch with the organization’s real concerns and seeing his findings and advice dismissed as poorly rooted in reality.

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We saw that, while the private and public sectors largely share the same determinants of effectiveness and value, some of them require careful interpretation and contextualisation. Nevertheless, in our view, we note that the internal audit function of some jurisdictions would particularly benefit from more independence and central support and that, across the country, human resources challenges are common. We also note that, while traditional financial and compliance audits are widely seen as less valuable, the optimal composition of an audit plan is best determined by context-specific risk-based assessment. As a result, the calls to move to more value-for-money auditing, for example, should be tempered by such considerations.

However, on the whole, we also note that many of the key drivers of value and effectiveness relate to the need for an internal audit function to remain closely attuned to the diverse needs of its “clients”, especially line managers and program executives, to understand their business and the conditions in which they must deliver on their objectives, and to effectively communicate valued insights that can lead to improvements in their use of internal controls, their governance processes and their management of risks. In the next part of the report, these issues are discussed further in the context of eight areas where our interviewees and survey respondents saw some potential for improvements that would deliver better value.
2. THE DETERMINANTS OF INTERNAL AUDIT EFFECTIVENESS AND VALUE
ENHANCING THE VALUE OF INTERNAL AUDITING IN THE PUBLIC SECTOR
3. MAXIMIZING THE VALUE OF INTERNAL AUDITING
At our panel discussions, during interviews and through our survey, we asked hundreds of internal auditors, chief audit executives, audit committee members and senior administrators how the performance and value of internal audit functions could be improved in the Canadian public sector. As should be expected, we heard a diversity of viewpoints. However, we found remarkable consensus that, in the following areas, a different approach or some modest changes could increase the value that internal auditing currently brings to the public sector. Some of these potential changes concern policy or process changes, others involve changes in the skills or even the attitudes of auditors.

Through our research, we also observed a remarkable degree of openness to change and a dedication to continuously improve. It was evident in our interviews with most chief audit executives, but, based on our survey results, we also believe that most internal auditors similarly open to change. For instance, while 64% of our respondents believe that “the current internal audit practices of their organization function well”, 81% of them think that “internal auditing in government should be more innovative”. Far from suffering from “reform fatigue”, only 8% think that “internal audit processes change too frequently”. These findings suggest that there is an appetite for more innovation. We hope that the following findings, observations and suggestions will be of some help in this regard.

3.1 Reconsidering the balance between assurance and advisory services

Rethinking the balance between assurance and advisory services in order to offer more and a wider range of advisory services is one of the areas that was most often identified as having the potential to enhance the value of internal auditing in the public sector. Most interviewees certainly agreed that assurance and advisory engagements can be equally necessary and valuable, depending on the circumstances, and no one suggested that the provision of assurance to senior management should be neglected. That being said, most interviewees also saw advisory engagements as currently adding more value to their organization and holding more potential to add value in the future.

Some interviewees reported that their organization had already shifted toward more advisory engagements over the last decade or made plans to add more advisory services in the years ahead. For example, “advice and education is definitely where we are adding more value at the moment”, said an experienced provincial chief audit executive. “Currently, it’s only maybe 10% of our projects, but we’re hoping to move up to 30% in the coming years. Then, there is a lot of advisory work that is done more informally. But increasing the share of advisory work and maybe even setting the ratio in policy will be key to improve [the contribution of the internal audit function].” An audit executive in a provincial Crown corporation also said: “Our advisory role is clearly the one that is most valued by management. So, while now we are doing a lot more assurance, we’re taking an ‘advisory turn’, especially to help with emerging risks and the management of large projects.”

Respondents to our survey similarly endorsed doing more advisory work. As we can see in the following table, 63% of respondents agreed that their contribution as internal auditors would “improve by taking on a greater advisory or consulting role”. Only 18% of respondents disagreed with this proposition. Only 20% of respondents actually thought that internal auditors should only play a “limited advisory role” and 71% thought that internal auditing could bring more value to the public sector by offering a broader range of services. Finally, only 34% of respondents agreed to any extent that, as internal auditors, they could bring more value to their organization by providing assurance services rather than advice. There were no significant differences in the views of federal and provincial respondents on these questions.

In describing the value of advisory services, interviewees raised three main factors. The first is timeliness. Across jurisdictions and organizations, many interviewees were concerned that, in an increasingly fast-paced environment, internal
### Table 2

<table>
<thead>
<tr>
<th>Public sector internal auditing and advisory services</th>
<th>Entirely agree, agree, somewhat agree</th>
<th>Neither agree or disagree</th>
<th>Entirely disagree, disagree, somewhat disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>My contribution as an internal auditor would improve by taking on a greater advisory / consultancy role.</td>
<td>63.2%</td>
<td>18.9%</td>
<td>17.8%</td>
</tr>
<tr>
<td>Internal auditing could bring more value to the public sector if it offered a broader range of services.</td>
<td>71.3%</td>
<td>16.5%</td>
<td>12.2%</td>
</tr>
<tr>
<td>Internal auditors should only play a limited advisory / consulting role.</td>
<td>20.2%</td>
<td>13.5%</td>
<td>66.3%</td>
</tr>
<tr>
<td>Managers routinely seek my advice on management issues.</td>
<td>37.3%</td>
<td>18.6%</td>
<td>44.1%</td>
</tr>
<tr>
<td>I see no conflicts between assurance and advisory / consultancy services.</td>
<td>44.3%</td>
<td>19.2%</td>
<td>36.5%</td>
</tr>
<tr>
<td>As an internal auditor, I can bring more value to my organization by providing assurance services rather than advice.</td>
<td>34.0%</td>
<td>26.1%</td>
<td>39.9%</td>
</tr>
<tr>
<td>I should not be involved in determining what the administrative controls in my organization should be.</td>
<td>29.1%</td>
<td>17.0%</td>
<td>53.9%</td>
</tr>
<tr>
<td>A greater advisory/consultancy role would widen my career opportunities.</td>
<td>71.9%</td>
<td>18.9%</td>
<td>9.2%</td>
</tr>
</tbody>
</table>

Auditors were struggling to deliver audit results and recommendations in a timely manner, a weakness that lessened the value of their service. For example, a federal chief audit executive explained:

"Would you rather have a lower level of assurance right away that things are working well or that something should be fixed or would you rather have a higher level assurance in 18 months, when things have had time to go wrong? As an auditor, it can be uncomfortable to provide an opinion or
In some circumstances, advisory engagements provide an opportunity to deliver assistance faster.

A second factor is the value inherent in preventing problems that might occur later by helping design better controls or governance processes at the outset. As a provincial chief audit executive argued: “Providing advice to managers and helping them think about their work, about how to improve their program or a process is much better value than what you would get from the potential result of an audit that we may never do because we lack the time.” Moreover, a non-audit senior executive argued: “doing more advisory work will also reduce the problems you’ll find in assurance jobs down the road. To my mind, [internal auditing] should focus on helping us getting things right in the first place at least as much as helping us fixing problems after they happen.”

In sum, there may be greater value is preventing future problems and their associated value destruction (e.g. financial and reputational losses, legal liability) than in coming in after the damage is done. The importance of early intervention was especially stressed for organizations that are undergoing significant transformations. With the support of internal audit, significant problems can be averted in those key periods when organizational objectives, risks and processes must be carefully considered.

Finally, some interviewees pointed out that advisory engagements can also have benefits in terms of better relationships with line managers and new insights into the organization’s risks and challenges. For example, one senior audit executive also pointed out that doing good advisory work can have spill over benefits on the assurance side as it allows internal auditors to build trust with program managers who are then less likely to react negatively when it’s time to perform an assurance audit or even an investigation that they did not initiate. It can change their perception of internal audit. Moreover, through advisory engagements, internal auditors can learn a lot about the realities of their organization, striking the kind of dialogue with managers that may be more difficult to achieve in a traditional assurance engagement. Better understanding of the business of the organization is an essential asset for auditors to add value in the future.

However, despite the emphasis on the value of advisory services, we should note that some auditors remain uneasy about the advisory side of their role. In our survey, while 44% of respondents did not see any conflict between offering advice and providing assurance, 37% disagreed. Based on our interviews and the answers to the open-ended question at the end of our survey, it seems fair to assume that many of the concerns turn around the fear that the provision of advice might compromise the independence and objectivity of auditors who might eventually have to audit processes or programs that were designed partly with the help of their advice.

Undoubtedly, this is a legitimate concern. At the very least, internal auditors should not cross the line between providing advice and actually making decisions about the design and operation of controls or risk systems. However, providing a clear understanding of the boundaries and the role of auditors, the near totality of our interviewees did not believe that more advisory work would compromise the function’s objectivity. Only one of the chief audit executives that we interviewed expressed concerns on this score.
The potential for doing more advisory work, and the changes that this might entail, differs across the Canadian public sector because the current balance between advisory and assurance work varies considerably. In the federal Public Service, past guidance required departmental internal audit functions not to devote more than 20% of their annual work to advisory engagements. This official target, built into the performance assessment of chief internal auditors, was seemingly meant to ensure that the internal auditing remains firmly focused on the provision of assurance to deputy heads and audit committees. Such a concern would be easily explained by the context surrounding past reforms, with the onus placed on the accountability of senior officials.

More recently, the leadership of the internal audit community has spoken of the need for more flexibility in assessing the proper balance. Certainly, most interviewees from the federal Public Service believed that this target was too constraining and prevented them from delivering as much value as they could to their organization. “Currently, it’s 80% assurance and 20% advisory. It should really be 50% / 50%, if not 20% / 80%”, a chief audit executive told us. “We need more flexibility under the policy to do more advisory work, although we still need to keep a balance”, said another. “The 80 / 20 rule should be more flexible, allowing us to move between 60 / 40 and 40 / 60 depending on the year”, said a third. On the whole, most federal interviewees argued for changes that would allow offering more advisory services.

In contrast, in Ontario, the internal audit division’s official target is already more generous, requiring that 60% of its work be dedicated to the provision of assurance and 40% to advisory engagements. The policy is also flexible, allowing the annual balance to vary based on the needs identified by departments. In the other jurisdictions, internal audit units do not generally use official targets for the balance between assurance and advisory services. So while some of those provincial and territorial administrations still dedicate between 75 to 90% of their activity to assurance services, those that have already decided to expand their offering of advisory services will not be constrained by a “binding target”.

Of course, assurance and advisory services are not entirely mutually exclusive. When reporting on an assurance engagement, auditors are called upon by the IIA standards to include “applicable recommendations”, which really represents a form of advice. Conversely, the standards also require internal auditors to report any control, governance and risk issues uncovered in the course of an advisory project. Clearly, the two types of engagements can overlap, whether or not it is done by design. In fact, some provincial interviewees reported “not accounting for projects in this way” and paying little attention to the difference. A provincial chief audit executive explained: “We draw up a plan and respond to requests based on our assessment of the priorities of the Public Service and where we think we can make a difference. And then, that’s what we do, irrespective of whether it’s considered assurance or advice.”

Even at the federal level, where auditors seem to place more emphasis on the distinction between assurance and advice, the line is often blurred. In fact, a CAE in the federal Public Service told us that, in order to ensure that audit services contribute as much as possible, he regularly asks his auditors to “do some advice work within an audit”. When an audit uncovers an issue where a faster but less comprehensive opinion is likely to help management, he’ll ask the auditors to quickly write up a short report on this specific issue before continuing with the audit, so that the manager can get assistance without waiting for the audit report to be ready weeks or months later.

As Head, Reding and Riddle (2010) argue, such “blended engagements” that purposely combine elements of assurance and consulting may be a way to generate more value by addressing diverse needs through a single project and using audit resources more efficiently. However, as the authors argue, some basic principles must be observed to ensure that explicitly blended engagements can be successful. For example, it is important that auditees do not feel that an advisory engagement or
a training session was used in a deceptive attempt at getting information to be used to support a critical appraisal of their operations. In this perspective, if poorly managed, some blended engagements could end up undermining trust in the audit function (for more critical questions on blended engagements, see also Anderson, 2004: 119-120).

3.2 Enhancing auditors’ knowledge of the client’s business

To maximize their effectiveness (and hence value), it is imperative that internal auditors possess a very good understanding of their organization’s business and the context in which it operates. This is true for both comfort and learning. This point was emphasized in several interviews and corroborates some of the research on internal auditing. For example, Sarens et al. found, in a study of European firms, that a balance between conceptual knowledge in risk management or internal controls and sufficient familiarity with the business is a key attribute of internal auditors’ capacity to effectively deliver comfort to audit committees (Sarens et al., 2009). Conversely, some studies have noted that internal audit effectiveness is impaired by line managers doubting that auditors have enough business knowledge to provide useful advice, and consequently discarding their recommendations (Van Peursem, 2004, 2005; Griffiths, 1999).

In a study of the Danish private sector, Arena and Jeppesen also found that, in a majority of the companies included in the study, internal audit was largely seen as “something that has to be done to ensure compliance with the regulation”, but that the managers who were really convinced about the valuable contribution of internal auditing were those who believed that their auditors really understood the business. As an executive quoted in the study put it, when auditors understand the business, “they can really suggest some improvements” (Arena and Jeppesen, 2010: 120-121).

Most executives and managers interviewed for this project wished that their internal audit function had a better understanding of their business and a better appreciation for the environment that they face as they try to deliver on organizational objectives. A recent audit released by Québec’s auditor general also found reason to worry on this score: when she surveyed departmental audit executives, 29% of the respondents estimated that their units only had a minimal understanding of their organization’s important systems and 58% reported that their units had a poor knowledge of their organization’s controls and risks (Vérificateur général du Québec, 2016: 13). Not surprisingly, the auditor general recommended some improvements in this area in order to ensure a more effective internal audit function in the province.

However, across jurisdictions, contextual knowledge and business acumen were seen as an area for improvement even by executives who praised internal auditing’s current performance and saw the function as a great asset. “I wish they knew our business better”, said a senior executive in one of the provinces. “Sometimes we’re given advice or they recommend that we adopt a best practice, and we have to explain to them how what they’re proposing is simply inapplicable because of the way things are set up in the province.” Underscoring the importance of contextual knowledge, another provincial executive recounted his poor experience with the audit services he once received from a private audit firm, saying that their lack of understanding of the public sector meant that they faced a steep learning curve and often provided poor advice.14

Several chief audit executives also emphasized the importance of knowledge of operations or experience with program management. For instance, at the federal level, one of them argued that, to increase the value of internal auditing in the future, auditors “should have more knowledge about the context of the programs and the policy environment in which they do the work. [...] Utopia is kind of the benchmark for most auditors.”

A senior audit executive with a long career in the federal government made the point that knowledge of the context of operations may be especially important for public sector auditing:
This emphasis on the need for more context-sensitive insights and solutions is also in direct keeping with some of the findings of the academic literature, which emphasizes that organizational knowledge and learning is context-specific (Rashman, Withers and Hartley, 2009: 472; Nutley and Davies, 2001).

Finally, the internal auditors who responded to our survey would clearly concur with these views: 79.8% of them are of the view that “their broad knowledge of their organization enables them to provide useful advice to managers and executives” and 77.4% believe that “acquiring experience in non-internal audit roles would enable them to improve their contribution as internal auditors.

In sum, experience in management, appreciation for the realities of the frontline and an in-depth knowledge of the organization’s business, context and strategic objectives are all seen as important assets for internal auditors to be more effective and deliver greater value. How can such contextual knowledge be enhanced? Recruitment, career management and more attention to broader organizational developments are the main areas where our interviewees saw some potential solutions.

As we pointed in the previous section, several interviewees reported facing serious recruitment challenges. Classification levels, pay scales and budgetary constraints, in particular, have made the recruitment and retention of qualified auditors difficult in many organizations. Moreover, in some speciality areas, such as information technologies, the lack of expertise is hindering the potential of internal audit functions to properly cover some risk areas. In this context, some audit executives argued that more creativity is needed in human resource management.

Some executives argued that the recruitment pool should be broadened by diversifying the educational and professional backgrounds of new recruits. “I think that professionalization is important but sometimes we’re losing the opportunity to get excellent people with different backgrounds. Certifications are one thing, but it’s not all”, said one chief audit executive. “We recruit many accountants who have strong methods, but the outlook is narrow. We focus too much on the financial side. We would need people with better knowledge in other areas, like technologies, especially in more senior positions where they would have an influence on the development of the function”, said another federal chief audit executive.

Another strategy would be to experiment or expand the use of rotational assignments allowing the audit function to integrate “guest auditors” for a period of time, staff from other units with specialized expertise or operational experience who could assist a team of professional auditors in doing assurance and advisory work where such experience and expertise is needed. In addition to help to better deliver on some projects, through close collaboration, guest auditors could help professional auditors acquire a better understanding of some sectors of the organization. Conversely, the guest auditors would eventually go back to their main responsibilities with a better appreciation for the potential of internal
auditing and its contribution to the organization. It would help change the dated perceptions of some managers and build better relationships with different parts of the organization.

In larger internal audit functions, where staff numbers provide some flexibility, rotational assignments could also help deepen the expertise and experience of internal auditors by allowing some of them to spend some time in operations. As an executive who occupied leadership positions in the audit community at both the provincial and federal levels told us: “We largely have a model of life-long auditors, with no experience of what it’s really like to have to deliver, what’s possible, realistic. We have to find ways to be creative and go beyond this model, or make it work better.” Rotational assignments for auditors could serve this objective.

In our interviews, drawing from his experience, a few executives emphasized the benefit of such experience. For example, a chief audit executive at the federal level told us:

“What has served me well is I spent a fair amount of time in management, in operations, so I have gained perspective on the pressures that management faces, what they need to do and how one tries to balance risks and reward, so I don’t approach internal audit from a highly theoretical perspective. […] I am a firm believer that every internal auditor needs to spend some time in operations, be it finance, be it the operations of the organization, so that you get a much clearer appreciation and understanding of the risks that the organization is trying to manage to achieve its objectives. It helps to remove [the audit work] from a simple theoretical exercise.”

Similarly, a provincial chief audit executive recounted her own experience: “You know, when you work in audit, you’re told that you don’t know how to manage. So, at one point, I did program management to know what operations is like and I must say that it made a difference, including in my relationship with managers”. Another federal chief audit executive made the same point: “Spending time outside of audit is important. If you have been a manager, you take a broader view. You learn to be more strategic, less prescriptive. […] CAEs in particular should have spent time outside because then you think more strategically.”

Finally, several chief audit executives spoke about the need for some organized and sustained efforts to ensure that the internal audit team remains well connected with the broader life of their organization. For example, one of them talked about how he had to encourage his staff to pay more attention to broader trends in the organization. “The way our offices are set up, we’re even physically isolated and often they don’t follow enough what is happening in the Public Service, the broader trends in HR, our programs, the department’s budget. They don’t even take advantage of the information out there.” To help to change this situation and emphasise the importance of keeping abreast of departmental issues, the executive had a few sessions organized with people from central agencies to discuss some relevant issues.

Another chief audit executive recounted a similar experience. Concerned that his auditors lacked an appreciation for some of the changes and pressures affecting line managers, he decided to organize some regular sessions with some of the department’s senior executives, so that they could better understand the organization’s strategic orientations. Such efforts are small-scale, low cost measures, but they were seen as worthwhile in helping auditors better understand organizational realities, something that could indirectly help deliver a higher impact product.

In his study of “world-class” innovative internal audit departments, Roth reported similar efforts in the private sector. Some of the high-performance
audit functions that he studied even appointed “relationship managers”, usually a senior auditor, who is tasked with building relationships and staying on top of developments in specific sectors of the organization. They would do so through a combination of periodic formal meetings but also regular informal discussions with line managers. Through these exchanges, they would make sure that the internal audit function remained current on the objectives and challenges faced by key areas of the business, simultaneously keeping in touch with the organization’s evolving risk environment. Such relationships would also help build mutual trust and allow line managers to better understand internal audit’s outlook and potential contribution (Roth, 2003: 36).

A final practice that elicited some contrasting views is the appointment of chief audit executives who do not have an internal audit background. Some interviewees expressed a concern that the appointment of non-auditors in those key leadership positions might be a step back in the professionalization and credibility of the function within their organization. As we pointed earlier, some of the internal audit functions of the Canadian public sector underwent a significant boost in professionalization and independence following scandals about a decade ago. For some interviewees, the appointment of professional auditors in chief audit executive positions is an important step in this direction. Professional auditing credentials and experience also helps in exercising leadership within the internal audit function.

However, for other interviewees, including the external chairs of some federal audit committees, the appointment of some non-auditors in those key positions was seen as an excellent practice, a way of ensuring that someone with a broader experience of management would handle the interface with the internal audit function. Leaders with this broader background, the argument was made, would have an easier time ensuring and convincing the rest of the organization, including the senior leadership, that the audit function is sensitive to their needs. Often, they might also be in a better position to ensure that the internal audit staff remains attentive to the broader strategic concerns of the organization.

In this regard, an executive who experienced heading an internal audit function without a background in auditing recounted to us how the experience made him a better executive, especially improving his knowledge of risk management and developing his skills in stakeholder relations through the work he had to do for the audit group. However, he also remembered how his deputy minister had appointed him in this position both as a developmental assignment and as a means to ensure that the audit function would remain relevant and well received by the rest of the department. “Probably the biggest part of my job”, he said, “was to adjust our audit reports for narrative, tone, level of prescription, etc. There was a real adjustment needed to ensure that we offered more useful feedback.”

To be clear, we are not arguing for a specific profile for chief audit executives. Clearly, an assessment of the needs of a specific organization at a particular point in time might call for someone with stronger, more visible auditing experience and credentials. In the course of this project, we have met remarkable audit leaders who were career auditors, had deep knowledge of their organization’s business, were very clearly costumer-focused and admired by their staff. However, in some cases, appointing a non-auditor in a leadership role might provide valuable help in changing the outlook and the perception of the internal audit function at a time when it is seen as insufficiently attuned to an organization’s requirements. Such a strategy might well help some organizations extract more value from its internal audit function. Consequently, we would not rule out the possibility of appointing non-auditors in such leadership roles in the name of the professionalization of the function, which was advocated by some of our interviewees.

3.3 Improving the communication of audit findings

The importance of good communication skills for the effectiveness of an internal auditor has been
well documented (Lenz and Hahn, 2015: 13; Chambers, 2008; Van Peursem, 2005; Roussy, 2012). They can help gather better evidence for audits, establish good relations with managers and executives, and deliver audit findings and recommendations more effectively. Through our interviews, communication issues, especially around formal audit reports, were also widely identified as an area where some improvements would help increase the effectiveness and value of internal auditing in many organizations. Sometimes the changes advocated were more subtle matters of style and tone of communication, but policy changes were also deemed necessary in some organizations.

The chief audit executive of a federal department thought that improving communications is the most important challenge of internal auditing in the public service, the change that could make the biggest difference in value. “It’s like going from an IBM to a Mac. The function is solid, but our outputs are often poorly communicated. […] Our auditors are rigorous and very focused on details, but, often, they are not as good for communicating.” He argued that improving communications should start before the audit report by adopting a more strategic focus for many audits. “We run tests without considering whether they will allow us to offer useful opinions, say something that will really be useful, relevant, strategic… […] Sometimes I cut entire sections of draft audit reports because they confuse our message by focusing on issues that have no strategic value and don’t say much that is useful for managers.”

Some of the program managers that we interviewed called for similar changes. For example, a senior program executive interviewed in one of the provinces argued that, in her experience, the communication of findings need to be improved mostly by better framing observed weaknesses in terms of relative risks and placing them in context, with due consideration for the programs’ delivery objectives. She thought that, while still useful, too many audit reports tended to present every control failure or weakness as equally risky or problematic and that auditors did not give enough consideration to how their proposed changes might impact delivery objectives.

Several other interviewees also stressed the need for a more strategic approach, focusing on a few strong messages on issues of greater import for the organization. They talked about their efforts to move toward fewer and less prescriptive recommendations meant to help program managers’ make their own calls about appropriate controls or needed trade-offs between risks and results. According to them, audit reports should also aim to be shorter and punchier, making them easier to absorb by busy managers.

In one province, the chief audit executive talked about the importance of the tone used to communicate with managers. “Tone is key. We need to be tactful in the way that we communicate. […] Unfortunately, I think sometimes the professional standards have led to some arrogance: we’re the experts, we know better than management, here’s what should have been done. […] That’s not useful. You need to bring people in.” Similarly, the head of audit in a provincial Crown corporation recounted that their communications had changed significantly in recent years. While they still emphasize straight talk, the function is now trying to find the “right tone” and to “accompany managers in understanding the recommendations” in an effort to improve the impact of the audit work.

At the federal level, some federal chief audit executives also emphasized the importance of “getting the tone right”. One of them considered it one of the most important part of his job and frequently edits draft reports to adjust the tone or reframe how the findings and recommendations were presented so they would be more likely to be valued and accepted by managers. Discussing similar practices, the head of audit in one province said: “We’re trying to change our language to be more constructive, focus on possibilities rather than blame.”

Amidst concerns for the tone of communications and the need for a more strategic focus, the usefulness of audit reports was even questioned.
For example, a senior executive with over twenty years of experience in auditing felt rather strongly about moving beyond the traditional audit report:

“Internal audit cannot just come out with this blessed, awful thing called an audit report – if I could burn them all, I would – because, talking about value-added, talk about something that doesn’t add value! You spend a fortune on these things, enormous amounts of time. Months after, you give it to an executive who’s too busy to read it anyway and who’s not that thrilled having an auditor around in the first place, and you give him some more work to do. Timeliness. Making sure you work with the client, you understand his business, the pressures he’s under. Then, you can add value. Giving him a report six months after he needs help, what’s that about?”

While few interviewees expressed views so passionately, many shared his sentiment. Timeliness was cited as an issue, especially at the federal level. “It might take us six months to do an audit, but then we spend another six months clearing the report”, explained a chief audit executive. While the length of the process is partly explained by the federal public disclosure requirements, which create an incentive for the cautious wording of each report, these delays had to broader concerns about the need for faster communication of results.

Expectedly, some of these concerns can be addressed through more informal communication channels. “The formal report is the least important part of the process”, said an experienced chief audit executive. “It’s a high-level review of what we found. [...] The real value is in the meetings when we present our findings directly to the clients and the verbal debriefs on what we saw, stuff that will not be in the report.” The chair of a federal departmental audit committee also explained that his committee tried to allocate as much time to informal briefings on draft reports and what auditors were finding than to formal meetings officially receiving audit reports. The informal discussions of on-going audit work were often more useful and engaging for senior executives than the discussions of the formal report.

However, several interviewees also called for more experimentation and a loosening of central constraints on the means of communication. For example, a federal chief audit executive argued that communication is currently hindered by the policies imposed by central agencies: “The standards are good. They brought us to where we are. It’s in their interpretation that the rules become too constraining. For example, we’re imposed strict norms on audit reports: we need written reports; there is a very precise format. But sometimes a presentation, a PowerPoint deck or a simpler written note would do as well and may be even better to get our findings and our message across to managers. We need more flexibility to do a better job with communicating our work.” Another departmental chief audit executive made the same point. Asked what could be changed to help internal audit deliver more value, she said: “We also need to find different ways to communicate: oral presentations, management letters, maybe even videos like the OAG. We need to try new things to get our message across.”

One interviewee pointed out that the IIA standards do not actually require writing a report, but rather stresses the effective communication of findings. Internal audit policies are often a greater source of constraints, imposing stringent conditions on content and format. Some of these policies should be reconsidered. Obviously, we are not advocating doing away with reports. At the very least, they are important “symbols of comfort” (Power, 1999) and they provide an important source of institutional memory. However, based on our interviews, it is hard not to conclude that comprehensive and excessively standardized audit reports currently consume a lot of time and energy in some jurisdictions while delivering limited value. An easing of internal policies coupled with the encouragement of
experimentation in methods of communication and central support in disseminating lessons about what works best could go some way toward crafting higher-value audit products.

### 3.4 Balancing the need for transparency, accountability and learning

The potentially negative effect of publicly disclosing audit reports was raised by many of interviewees at the federal, provincial and territorial levels. Public disclosure requirements vary across jurisdictions. On this score as well, the federal Public Service is an outlier because its **Policy on Internal Audit** (section 6.1.5) requires the public release of every report, which are posted on departmental websites. To our knowledge, no other jurisdiction has such a requirement and audit reports are more typically accessible on demand through access-to-information legislation. However, in some provinces, more extensive or automatic disclosure has been discussed in recent years as part of “open government” initiatives, a development that could well become a common occurrence in light of the widespread push for greater government transparency (Meijer, 2014).

Interviewees nearly unanimously expressed concern about the deleterious effect that more extensive public disclosure could have on the contribution of their internal audit function. The value of more extensive public disclosure lies in more public accountability: it not only provides more information to citizens about the workings of their government but it also creates public pressure for organizations to act on the findings and recommendations of audits. It also provides information to journalists that can be used to investigate in areas where there could be more problems of public interest. This is ostensibly the reason that led to the introduction of the automatic disclosure requirement at the federal level in 2006, in the wake of the “sponsorship scandal”.

Unfortunately, a more expansive disclosure policy also comes at a cost. The higher the likelihood that an audit will be used to publicly blame the government or the organization’s leadership for mismanagement or poor performance, the lesser the probability that managers will see their internal audit function as an instrument to foster a candid and critical self-review meant to improve organizational performance. As Michael Power, a leading academic authority on auditing, reminds us, “the balance between blame and learning in the treatment of auditees” may be the most basic issue for the design of auditing processes, but striking this balance is often difficult, not least because the auditor does not fully control the environment in which the audit relationship unfolds (Power, 1999: 336). In this perspective, the anticipation of a potentially negative public reception of audit findings can complicate the internal audit function’s relationship with the rest of the organization.

In this perspective, several audit executives expressed their concern about too much disclosure. As one provincial chief audit executive explained: “I am very much against the publication of our reports. In my discussions with departments, I emphasize that we are here to help, not to denounce them in public.” Pointing out that he had to work hard to gain the trust of many senior executives, he feared that this trust might be undermined by more extensive disclosure. Another provincial chief audit executive recounted taking part in recent discussion in the context of an open government initiative:

> “I felt very, very strongly that IA reports should not be made public. A lot of departments are now very receptive [to the services of the internal audit function]. Publishing audits would cause irreparable damage to our relationship with managers. […] I mean that’s why we have an Office of the Auditor General: he’s the public one. We’re internal confidential advisers.”

Finally, the chief audit executive of another province thought that the current level of transparency was as much as would be compatible with an effective audit function: “We’re saved by not having to
MAXIMIZING THE VALUE OF INTERNAL AUDITING

These concerns about more extensive disclosure are partly validated by the federal experience. On the one hand, it would clearly be wrong to think that automatic disclosure has made it impossible to forge constructive and positive relationships between internal audit functions and managers in the federal Public Service. Moreover, posting reports on websites is now routine and internal audits don’t grab the headlines that frequently. On the other hand, according to our interviewees, the more extensive disclosure requirement has made the formal audit reports less effective as a tool of communication and an instrument to leverage changes in organizational practice. Considerable efforts must now be invested in vetting the language of each report, often resulting in diluted content and opaque language. For example, a departmental audit executive noted that a lot of time is spent carefully screening the language of each report to minimize the risk that the media would misinterpret its findings or quote a bolder statement out of context in their coverage. “Transparency is another challenge”, said another audit executive. “It’s limiting: you cannot say exactly what you want.” The head of audit of a third department described a similar process where auditees feel that they have to challenge how everything is worded in the reports for fear that something might reflect badly on them. As a result, the department ends up spending a lot of time reviewing reports until everyone is satisfied that there is no cause to worry about their publication. In sum, according to our interviewees, this concern about the potential political backlash resulting from media coverage is wasting some valuable audit time, but it’s also encouraging excessive caution and stifling discussion. “Real value comes from getting at real issues”, a chief audit executive pointed out. “Having honest conversations about problems and action plans, not worrying about what’s in the published report.”

In our survey, we also asked internal auditors whether they felt that the public disclosure requirements of their organization limit their capacity to effectively communicate their audit findings: 42% of our federal respondents and 29% of our provincial respondents said that they did. It is very likely that this difference results from the more extensive disclosure requirements at the federal level.

The issue worried our federal interviewees to varying extent. When asked what he would change to improve the value of internal auditing in the federal public service, one of them said: “The change that would have the biggest impact would be to stop publishing our audit reports”. However, most of our interviewees did not go so far. Nevertheless, they clearly saw public disclosure, on balance, to be a limitation on their ability to deliver maximum value to their organization. As we saw in the previous section, frank critical discussion can still occur through less formal, internal discussions. The audit report is an important communication tool, but it’s not the only one. However, if one believes in the potential of internal auditing as a systematic, powerful tool of organizational learning, the dynamic engendered by more extensive disclosure seems limiting.

David Good is an academic who also spent decades in the federal Public Service, including as an assistant deputy minister of the Human Resources Development Canada (HRDC) when the department was engulfed in a huge controversy as a result of the public release of an internal audit of its grants and contributions program. The HRDC scandal was partly fuelled by a misinterpretation of the audit’s findings by the national media and, after occupying the center stage of Canadian politics for several months and absorbing much of the department executives’ time, it initially resulted in a multiplication of controls that killed attempts at more efficient program management.16

Reflecting on his experience, Good seems to usefully capture the challenge presented by transparency to a public sector internal audit regime when, in his book on this controversy, he writes that some officials may see accountability mechanisms, such
as internal auditing, as a source of learning. But, in fact, they are naïve to believe that:

“accountability can be primarily about the positive aspects of learning without the negative aspects of ‘assigning blame and punishing wrongdoing’. [..] Over time, these officials come to learn that it is better to be smart than to be naïve. In short, they must curtail their appetite for learning. Rather than maximizing every opportunity for learning, they come to minimize most, but not all, opportunities for mistakes” (Good, 2003: 173).

This is surely a dire conclusion, but it does raise the importance of ways to balance accountability, transparency and learning. Without such balance, the value of internal auditing as a source of organizational learning – and the general appetite for public service innovation – would be seriously compromised.

How to strike such a balance is a difficult question. A member of a federal departmental audit committee argued that:

“there is no way that we are going back on transparency, so the only solution is to be prepared to defend a degree of failure. [..] The tone has to be set at the top, probably by the President of the Treasury Board or even the Prime Minister. I think that it happened to some extent in New Brunswick with McKenna years ago, but leaders have to take the heat and lead. Otherwise, people won't feel conformable talking about mistakes and internal audit will continue to be seen as a threat by many executives.”

While we certainly share the hope for the emergence of a political culture more tolerant of administrative failures, we see little reason to be optimistic in this regard.

As far as enhancing the value of internal auditing in the public sector in the medium term, we would encourage provincial jurisdictions to resist subjecting audit reports to more extensive public disclosure. Their release through access-to-information procedures appears to be a more balanced approach. Canadian jurisdictions already greatly benefit from the work of strong legislative auditors. Experience has shown that, across the country, the auditor general of each jurisdiction provides a strong mechanism of public accountability. The internal audit functions should be preserved as primarily management tools.

In jurisdictions where a different equilibrium is sought, one could consider using confidential internal documents geared toward management learning, coupled with the public release of more summary information (although, at some point, that might not be of much use to the public) or the “confidential public disclosure” of audit reports to the Office of the Auditor General (who would then decide on the need for full public disclosure or the pursuit of her own audit). Such alternative models might provide a more productive balance among transparency, accountability and learning.

3.5 Increasing the enterprise-wide dissemination of knowledge and insights drawn from audits

The wider dissemination of lessons learned and best practices identified through audit engagements is also an important area where the internal audit function could improve and contribute to enterprise-wide learning, enhancing its value to the organization. The standard audit practice is to consider each audit as a discrete engagement: auditors go in to review a particular program or process, draw some conclusions from their observations, and communicate their findings to the audit committee, the senior leadership and the program or process owner. Then, management
action plan in hand, in most organizations, some work would be done to follow up on the implementation of the audit’s recommendations.

Through this standard process, auditors undoubtedly contribute to organizational improvement. However, as some interviewees observed, they also gather intelligence about common weaknesses and particular best practices within their organization. This intelligence can be used to inform future audits, but few audit groups seem to have more systematic mechanisms to ensure that they leverage this information to the benefit of the entire organization. In order for internal audit to truly maximize its value to the public sector, consideration should be given to the establishment of standard practices or institutional processes that would mine the audits performed each year for lessons and best practices that would benefit the entire organization and ensure their proactive dissemination to managers across the enterprise.

Ontario and Nova Scotia may stand as good examples of leading practices in this regard. In Ontario, the Ontario Public Service’s Ontario Internal Audit Division operates an Enterprise-Wide Lessons Learned reporting system that allows for a wider dissemination of the lessons drawn from its audits. Its enterprise-wide audit team reviews the observations and findings of numerous reports stemming from assurance and advisory engagements completed by different audit teams across several ministries and agencies. It then draws broader lessons that could be useful for other organizations across the Ontario Public Service that operate similar programs or processes and it presents those lessons in a report that is sent to key stakeholders throughout the Public Service.

For example, the team might review the findings of over twenty engagement reports done in a year across the OPS and that, to various degrees and in different ways, touched on the management of transfer payments to outside agencies that deliver services on behalf of the government. These transfer payments are an important component of public spending in many areas of government activity. The lessons drawn from the review are then communicated through a lessons-learned report sent to the Corporate Audit Committee, some of the ministries’ audit committees, and selected senior managers responsible for the operation and oversight of relevant transfer programs. Obviously, the findings are also shared with audit directors across the public service.

This effort to leverage completed audits to the benefit of the wider organization enhances the value of internal audit work in different ways. Most obviously, it draws the attention of executives and managers who own similar processes to potential problems and solutions observed elsewhere in the Public Service. The information can lead to organizational improvements and the adoption of mitigation measures preventing future losses without requiring as much expense as the conduct of new audits. In sum, it simply extracts more value from existing audit engagements. Moreover, the different ministries and audit committees can consider these findings when they prepare their annual risk-based audit plans or, over the course of the year, it can help them decide whether an ad hoc engagement might be warranted in their own organization.

The internal audit function of the Nova Scotia Public Service showed similar leadership when it spearheaded the creation of a government-wide fraud management committee to strengthen the province’s approach on fraud prevention. The committee brought together key people from various departments, reviewed existing practices and helped develop better policies. The initiative is a good example of the kind of leadership that internal auditors can exercise to raise awareness, spread knowledge and strengthen practices across the public service. It also embodies a “preventive” approach to the value of internal auditing, leveraging internal audit knowledge and resources to improve systems before problems occur. The internal audit function has also been using a similar model on other issues. When it finds some problems through its audits, it works to see if they also occur in other departments. Then, when the situation warrants it, it brings together managers
across departments to share its findings, raise awareness and collaboratively develop common solutions for the government as a whole.

There are clearly other ways in which internal auditors can work to disseminate the findings or best practices across their organization. On a more modest scale or a more passive manner, the Office of the Auditor General of Manitoba, in a guide on how to provide leading edge internal auditing in the public sector, stresses the importance of writing audit reports that “educate and promote best practices” throughout the provincial public service. It proposes that audit reports provide supplementary information in appendices on best practices related to the audit’s findings. Such a practice, the report suggests, would help ensure that internal audit services add greater value to the public sector (Office of the Auditor General of Manitoba, 2006: 18). This suggestion is in line with the work of Sarens and De Beelde who, in a 2006 study, have concluded that the internal audit function can have a “crucial role in the spread of best practices” through an organization and act as an important benchmarking source for managers (Sarens and De Beelde, 2006: 76).

The involvement of the audit function in training in key areas within its expertise also rests on the belief that, from the organization’s standpoint, there is much to be gained by avoiding problems due to a better-trained workforce rather than spending resources on corrective actions once the problems have occurred or the weaknesses have been detected through the occasional audit. However, only a few chief audit executives interviewed for the project reported currently doing some training as part of their current portfolio of activities, but many interviewees noted that offering training to managers on carefully selected issues of concern or importance, such as contract management or fraud prevention, is an area where internal audit professionals could expand its value.

The internal audit function of the Newfoundland and Labrador Public Service is amongst the organizations that have already reaped the benefits of such a strategy. A few years ago, it delivered training on how to manage the risk of fraud to a number of departmental executives. This training effort also included the development and use of a fraud risk assessment tool that could then be used across the public service. In Quebec, some Crown corporations also spoke of their use of training sessions to address gaps that audits had identified in employees’ understanding of ethics rules and in contract management practices. In all cases, these efforts were described as having been a valuable investment of audit resources, helping organizations strengthen their practices and systems in areas observed to be weak.

It is also useful to note that this kind of training engagements and enterprise-wide collaborations can also have ancillary benefits. They can lead to relationship building as participating managers come to see audit services – and auditors themselves – in a new light, countering some of the out-dated perceptions of the auditor as the unimaginative and isolated organizational cop. For auditors, the conversations that are bound to occur as the training or collaborations unfold can provide valuable insights on current practices across the organization and resulting in a better understanding of the challenges faced by operational
managers, contributing to their business acumen. Finally, these activities can also lead to – or even be accompanied by – other types of engagements, such as the provision of advice on new controls or the facilitation of self-assessment processes, thereby leading to more direct changes in systems and practices (e.g. Anderson, 2004: 120-221).

In sum, assisting a larger number of line managers or executives acquire better practices is often likely to have a wider impact on the stewardship of an organization’s resources than helping to fix problems one-by-one as they emerge through audit work. Moreover, internal auditors benefit from an exceptional advantage by their ability to monitor developments across the entire organization and by building relationships with its various sectors. Whether it is through training, horizontal working groups or initiatives, or simply new systemic products aimed at disseminating more widely the fruits of audit work already performed, internal auditors should seek opportunities to make the most of their advantageous vantage point to help the entire organization (and not only the occasional auditee or the audit committee) benefit from its intelligence and expertise.

3.6 Engaging in a more concerted effort to expand the use of data analytics

None of our interviewees talked about data analytics as a current strength of the internal audit function of their organization, and it was frequently identified as a weakness. At the same time, the expansion of the use of data analytics was widely seen as a promising means to increase the effectiveness and value of internal auditing in the future. “It’s a must. We’re eager to do more, in a big way”, said the head of internal audit in a provincial public service. In another province, the chief audit executive explained that data analytics was currently mainly used to spot areas where audits should be conducted, but that, as part of a province-wide initiative, there were now plans to expand its use for more substantive analyses in audit work.

Many chief audit executives talked about similar intentions to increase the use of these techniques. In some cases, they were mentioned as a means of identifying potentially problematic areas to be further investigated or as a means of improving the quality of audits by moving away from sampling. Several interviewees also talked about the promise of continuous auditing – the automation of the audit of large volumes of transactions – in delivering faster and more frequent assurance but also in freeing up the valuable of auditors who could then be tasked with more complex, higher value auditing work. Finally, most chief audit executives hoped that these new tools would allow auditors to deliver more and better insights by using new sources of data in more creative ways. In sum, chief audit executives clearly see multiple ways through which these techniques could be used to deliver more value.

Our survey respondents were equally enthusiastic about using data analytics. 70% of our respondents agreed that greater use of data analytics would enhance the quality of their work. 75% of them believed that receiving more training in the area would improve their capacity to add value to their organization. 75% of our respondents also predicted that data analytics would be a major source of innovation in internal auditing in the next decade. In sum, it seems that internal auditors are big believers in the future of data analytics. In this regard, they may not be different from executives across public organizations. The annual survey of public sector executives released by Deloitte and the Institute of Public Administration of Canada (IPAC) in 2015 showed that 75% of Canadian public sector executives believe that advanced analytics will be important or very important for how they manage in the coming years.
However, this enthusiasm for the future of data analytics was clearly tempered by some of the practical difficulties actually experienced by many organizations in putting these techniques to work. As we pointed out earlier, none of our interviewees thought they were doing particularly well in this regard. We also asked our survey respondents how often they were using these techniques. Only 26% stated using data analytics frequently. 37% declared to never or rarely use them, while another 37% use them on occasion. Given the frequent remarks about generational differences related to technology use, we tested the data and found no statistically significant patterns relating to age with respect to respondents’ views or declared behaviour. Federal and provincial respondents also exhibited identical response patterns.

Of course, these difficulties are not exclusive to the public sector. A Survey on Data and Analytics-enabled Internal Audit done by KPMG in 2015 found that 60% of respondents indicated that their organization was not effective in incorporating data analytics in its internal audit work. The survey did not find any difference between private and public sector respondents. However, it remains that capitalizing on the potential of data analytics will require surmounting some obstacles. When asked to explain why their organization was not further ahead in the use of these tools, audit executives talked about three main barriers: the availability and quality of data, the difficulties in acquiring and keeping qualified personnel, and, more importantly, ensuring that auditors can better understand the potential of these tools in specific circumstances.

Interviewees at all levels frequently mentioned problems with the quality of available data. One senior federal audit executive put it starkly: “once you look into it, often the data is junk”. “We have a LOT of data, but it’s often of poor quality. We saw it in some projects where we tried to use data to finally realize that it simply was not reliable”, said a chief audit executive in Ottawa. Other chief audit executives spoke about the substantial work that must be put into ensuring that the data is reliable and actually captures the variables that you need. In some cases, these comments may reflect a realization that the use of these tools is more complex and entails more work than initially anticipated, but it is clear that many interviewees felt that the potential for the use of data analytics
in auditing was being partly constrained by larger problems with the data management systems in their organization.

The lack of employees with technical knowledge related to data analytics is also a challenge in many organizations. Data analytics has not been part of the training of most current auditors. Most internal audit functions are either trying to recruit younger employees who acquired these skills through their post-secondary education or by sending some of their current auditors for short training courses. A surprising 42% of our survey respondents declared having received some form of data analytics training in the last five years. In many organizations, newly trained auditors are expected to help train other auditors or provide some support in the use of these techniques when an audit requires it. Some chief audit executives are also creating “data analytics teams” within their group to provide such expertise or technical support (e.g. in using ACL) or working groups where auditors with technical skills work with others to teach them those skills through actual use in on-going audits.

Despite these efforts, people often reported mixed results. For example, the chief audit executive of a public agency in Québec told us:

“There is a world of potential in data analytics, but you need the expertise and the skills. Unfortunately, it’s not frequent in the public sector in Québec. It had become standard in [a big private firm where the auditor worked before joining the public sector], but I don’t see much of it since I’ve been in public sector. In our case, we cannot afford to have someone full time doing data analytics, so we need someone who will invest in getting the expertise but will also do other things. Many procedures are not replicable on many occasions, so the return on investment is limited. And then this person has to stay with the organization once he’s got the skills. Otherwise you have to start over.”

Obviously, these difficulties seemed to be more prevalent in smaller internal audit functions, where specialized skills and redundancies tend to be more limited, but these smaller units are frequent in the public sector.

Finally, beyond the technical skills, many of interviewees spoke about the need for auditors to be more creative and better understand how to actually use data analytics in the context of their audit work. For example, a federal audit executive explained that his department had a centralised group of data specialists that auditors could approach for assistance when needed. However, this expertise was poorly used because few auditors could see the potential of these tools. They easily recognized their potential in the abstract, but knowing how and where to use them in their audit work was more difficult. This more creative, conceptual task was often proving to be the real problem, not the access to the technical expertise.

Another interviewee recounted a similar experience. The audit function built a data analytics group only to take it apart three years later when it concluded that having data analytics as a separate business line was not delivering the expected results. The younger employees who had been recruited for their technical skills lacked the audit expertise, the experience and the knowledge of the organization to know when and where to use their skills, while the rest of the audit team, including the chief audit executive, had a hard time “seeing what was possible” with the new tools. The result, it was felt, was a misuse of resources and unfulfilled potential. The audit team now hopes to draw on data analytics expertise elsewhere in the organization when the need arises.
This story illustrates a broader point made by many interviewees, including a former senior audit executive with extensive experience in data analytics: while acquiring the needed technical skills can be a real challenge, the greater difficulty is getting the whole audit team, including the chief audit executive, to “internalize” a new way of thinking about the use of data in internal auditing. The tendency to send younger auditors on a course or to recruit young employees with these skills is bound to have a limited impact since they will likely be isolated while the rest of the audit group more or less goes about its usual business. As the former senior executive put it, “to successfully use data analytics requires a concerted effort that is generally lacking”. Without such a concerted effort, the potential of data analytics will remain largely unexploited. Hence, expanding the use of data analytics in public sector internal auditing appears to be as much about a change in culture and outlook as about skills acquisition and overcoming technical difficulties.

These observations lead us to think that more corporate-wide efforts might be needed to help internal audit capture the potential of data analytics. In some organizations, the central pooling of technical expertise might help with human resources challenges, but broader efforts to help all internal auditors, including those who will never acquire advanced technical skills, and executives to see the full potential of data analytics may also be required. Central support and visible commitment to this agenda by leaders would help send supportive signal and rally people around a more concerted effort in this regard. The dissemination of knowledge on best practices in the field and examples of its successful use in the public sector could also contribute to these efforts. In any case, it seems that part of the success of such initiatives will also depend on wider corporate efforts to strengthen data management and analytics beyond its use in audit.

3.7 Expanding the role of internal audit in enterprise-wide risk management

A formal risk function and a developed enterprise risk management system are not present or are still in their infancy in several organizations. However, where they exist or are being developed, these functions have the potential to overlap with the internal audit function. Despite the distinction between the roles and responsibilities of the second and third lines of defence (Institute of Internal Auditors, 2013), both functions are clearly part of a common enterprise dedicated to improving the management of risk in their organization. According to many interviewees, ensuring better collaboration with the risk management function would be a promising way to ensure better value from internal audit by optimizing the use of organizational resources or by providing internal auditors with new opportunities to offer their expertise. However, even in the absence of a formal enterprise risk management (ERM) framework, many interviewees saw the strengthening of risk management practices and “risk education” more generally as areas where a more active internal audit function could add more value to the public sector.

Providing assurance by evaluating risk management processes (including the ERM framework) as well as how risks are assessed and reported is already considered to be a core responsibility of internal auditing (Institute of Internal Auditors, 2004). However, internal auditors can also be legitimately involved in other dimensions of the deployment of better risk management practices across their organization. They can facilitate the identification and evaluation of risks. They can coach management on how to respond to the risks that they face. They can assist in the development of the enterprise risk management framework or specific risk management strategies. When it is absent or fledging in its implementation, auditors can also champion the creation or strengthening of the enterprise risk management framework of their organization.
Many of our interviewees advocated such a role for public sector internal audit functions. This seem to be in good part because they believe that public managers need a better understanding of risk management and that, while some improvement would come through the discussion of risks through particular audit engagements, wider and more systemic efforts might be more effective. For example, one federal interviewee argued:

“A good, active internal audit function could become a catalyst of more sophisticated discussions around risk across the Public Service. [...] It’s not just about auditing. It’s the whole thinking about risks, controls and oversight that is often lacking in the Public Service. [...] Managers often think that you must fix everything, that risk management means no risk. But, in fact, what you need is a more explicit, sophisticated understanding of your risks and what you can tolerate given your resources and performance objectives.”

As Sarens and De Beelde also noted in their study of private sector internal auditors’ involvement in risk management, such a proactive advisory role in the development or improvement of internal controls in light of a changing risk environment can be seen as an additional opportunity for auditors to “demonstrate their value” (Sarens and De Beelde, 2006: 71). According to the authors, this involvement takes many forms. In addition to providing advice on specific cases, private sector internal auditors have helped design control/risk assessment questionnaires, helped facilitate self-assessments, provided management training on risk management and helped write management manuals related to risks and controls (Sarens and De Beelde, 2006: 73). This is an area where more value could be provided.

A senior program executive in a province highlighted the potential for such involvement:

“The fact is that a more sophisticated approach to risk at the level of the enterprise would allow us to weigh particular risks more appropriately and see controls in the broader context of what we do and why we do it, [...] You would find that you could eliminate redundant controls and reduce your risk exposure at the same time. [...] We did a systematic review a few years ago for [an important program shared by several departments]. We ended up plugging some gaps, but we also got rid of 40% of the controls, some that needlessly duplicated others and some that weren’t attached to anything – orphan controls that didn’t mitigate anything. [...] The program and the environment had changed but people relied on controls added over the years.”
A senior executive in a provincial central agency thought that more extensive collaboration among internal auditors, enterprise risk management and officials responsible for setting policies on internal controls would also be beneficial. For example, the findings of assurance audit reports could contribute more systematically to the development of a central risk/control database that could play a valuable communication function in the operation of the control and risk management frameworks of the organization. Close collaboration with the risk management function would also ensure that a common “terminology” is used in talking about risk with managers. At the moment, he said, managers are not necessarily presented with a coherent picture of the organization’s approach and expectations. Collaboration could also reduce some potential duplication in resources spent on gathering information from operational units on how they deal with risk.

These benefits would seem easy enough to capture. However, some interviewees argued that internal auditors can resist closer collaboration with risk management, for fear that their independence and objectivity would be compromised. These concerns are obviously legitimate. As we pointed earlier, confusion between the second and third lines of defence could end up weakening the effectiveness of the internal audit function. We would certainly not advocate that internal auditors be in charge of determining acceptable levels of risk tolerance for their organization or bear the direct responsibility for the risk management process (its design and operation). However, there is much that can still be done in the enterprise risk management area that would be beneficial and would not compromise the independence of internal auditors.

Our survey results also suggest that internal auditors are generally ready to revisit their relationship with risk management: 65% of our respondents agreed that auditors needed to do so. At the moment, only 62% of respondents think that their role in supporting risk management is clear and 40% feel that they could assume a greater role in risk management in their organization. At the very least, some clarification of the expected contribution of internal auditing to better risk management would seem beneficial in some public organizations. While we believe that, in most cases, the internal audit function could add more value by carefully expanding its role in promoting risk management across the organization, it is also possible that, in some organizations where the second line of defense is weak, the effectiveness and value of internal audit might be bolstered by guarding it against some forms of involvement. For example, on this score, we find it surprising that 23% of our survey respondents stated that they are playing “a leadership role in determining the risk tolerance” of their organization.

At a minimum, enhancing the value of internal auditing by expanding its role in enterprise-wide risk management will mean making the effort to network and establish good relationships with those members of the “second line of defence”, but more structured collaboration are also possible. Such more explicit collaboration could come through an active involvement in the implementation of a formal ERM system. At the moment, the internal audit group of some provinces have been largely left out of ERM initiatives in their organization, which seems a missed opportunity. As a federal head of audit also argued, auditors “should help develop [their organization’s] capacity to identify and assess future risks because we have the advantage of a broader perspective. We know about risk but we also see the whole organization.”

Concrete collaborative efforts can also be more specific and limited, such as the development and use of joint databases with the control and risk functions. Robert Kuling, a former public sector auditor who is now a partner with Deloitte & Touche, even recounts a positive experience from his days in a public sector agency where a risk management officer was regularly seconded to join an audit team, building the team’s capacity and allowing the officer to develop his knowledge of the audited business (Kulig, 2016: 57). Given that, as we pointed out earlier, many chief audit executives report struggling with staffing levels, such collaborative practices might also be beneficial on this score.
Audit engagements could also be more systematically attentive to how risks have been identified, assessed and mitigated by managers, using these traditional engagements to further risk education or promote risk management thinking across the organization. As a senior executive in a provincial central agency argued, “as the government is moving toward better ERM, one role of audit should be to help educate managers about how to identify and assess risks “. Whether this is done through the interaction with managers through auditing work, the provision of particular advisory services (e.g. facilitation of risk self-assessments) or even collaborating to formal training activities, a large number of our interviewees believed that such efforts could provide lasting value to the public sector.

3.8 Improving the collaboration of internal audit with the evaluation function

In some jurisdictions, a final option to enhance the effectiveness of the internal audit function would be to improve its collaboration with the group responsible for program evaluation. On this score, public organizations vary a great deal. In some jurisdictions and organizations, the evaluation function is not well developed, limiting the potential for both collaboration and overlap.
In other organizations, both functions are relatively strong and do not collaborate much. In other cases, both review functions are actually located within a common directorate. However, even in those cases, the degree of collaboration between auditors and evaluators seem to vary considerably.

When asked how they could enhance their value and improve their effectiveness, many of our interviewees spoke about the need improve the collaboration between those two functions. A chief audit executive in the federal Public Service said: “We need to do more than pay lip service to better collaboration between evaluation and audit”. Another head of audit with long years of service at the federal level also said: “Unfortunately, I think that evaluation has become the poor cousin of auditing. Great collaboration between evaluation and auditing has taken place in some departments, but it does not happen as much as it should.” Another chief audit executive who lived through a reorganization that brought both functions under the same unit stressed how the ensuing collaboration led to the improvement of both functions.

In discussing the benefit of collaboration, four benefits were generally mentioned: lessening the burden on managers facing the two functions, the opportunity to provide a more integrated review of the performance of programs, the sharing of resources and the sharing of information. The avoidance of “audit fatigue” is the most obvious advantage of closer cooperation and was raised by several interviewees. As an audit executive explained: “Audits and evaluations take time for the managers as well, and most clients don’t even distinguish between evaluation and audit – for many of them, it’s all the same. So, when you can use the same process, consultations, let’s do it. Let’s collect data together and then do our own work.”

For some executives, better collaboration was also needed to avoid needless duplication or unproductive overlap. It is interesting to note that only half of our survey respondents found that the boundaries between internal auditing and evaluation are clearly defined in their organization. This finding reminds us of a chief audit executive who, in talking about the absence of collaboration with evaluators, half-jokingly said: “Yes. We have some evaluators. I’m not quite sure what they are doing. It seems to be non-auditors doing performance audits.” The Australian Government’s Better Practice Guide for public sector internal auditing takes a similar view when asking that, to “maximise the effectiveness of internal audit, its role should be considered in the context of other elements of an entity’s assurance framework so that internal audit complements, rather than duplicates, the responsibilities of others.”

In the same vein, in some instances, more extensive coordination could help deliver a higher impact product to managers. For example, the head of audit in a federal department explained the reasons for a recent collaborative effort in this fashion: “We’re doing a project with evaluation in my department. By combining evaluation’s insights on outcomes and our work on process, we will give an integrated view of the performance of the program. It will be better for the department. [...] But this kind of innovation requires to work together more than we’ve done in the past.” 41% of our survey respondents also thought that they would need to collaborate more extensively with evaluation to offer more effective advisory services to managers. 31% thought that it would help them promote innovation in their organization.

The actual coordination of evaluation and audit work can be difficult. As an interviewee explained, evaluations can take a lot longer than audits, which are already often taking too long considering the need for better risk management. Evaluation reports also tend to be very long, while audit reports should be even shorter than they currently are so that audit results are better communicated faster to busy managers. Such challenges partly explain why many interviewees advocated a lesser form of collaboration. For them, the main benefits would come from the sharing resources and information across functions.

For example, one chief audit executive pointed out that some common techniques are used to collect and analyze data in both professions. When
3. MAXIMIZING THE VALUE OF INTERNAL AUDITING

resources are tight or when a specific employee has a better skillset using one of those techniques, more extensive coordination of evaluation and audit work would allow the function to allocate resources more efficiently. Similarly, a better exchange of information could assist both functions in understanding particular programs and gather intelligence that could be useful in preparing specific audits or informing the preparation of the audit plan. These benefits are simple enough. Yet, in some organizations, the organizational and cultural divisions between the two functions prevent such fruitful exchanges.

At the federal level, one of the barriers to closer collaboration appears to lie in the history of the Public Service. Several interviewees explained that many federal auditors still remember a period in the 1990s when auditors and evaluators worked together to produce “reviews” that were neither proper evaluations nor audits living up to professional standards. These reviews, they argued, often lacked rigour and credibility and produced limited value for departments. Because of this history, many internal auditors may now be fearful of changes that would erode the remarkable gains in professionalization, independence and credibility that have been made over the last decade. As one interviewee put it, “the ‘true’ auditors still wear the scars of that period”. Hence, for most of our interviewees, while closer collaboration was seen as a useful way to improve the function’s effectiveness, it was equally important that this collaboration be built on a clear distinction between the two fields, respecting each other’s professional practice standards.

Notwithstanding those concerns, a majority of the internal auditors, including at the federal level, thought that internal auditors should revisit their relationship with evaluation. Revisiting this relationship need not entail organizational restructuring. Through our interviews, we observed some internal audit functions taking steps in this direction despite both functions being separated. At the same time, it seems obvious that the likelihood of effective collaboration would be enhanced in many organizations if both review functions fell under a common leadership, dedicated to making such collaboration work while respecting the professional identity of both groups.

### Table 5:

<table>
<thead>
<tr>
<th>Collaboration with program evaluation</th>
<th>Entirely agree, agree, somewhat agree</th>
<th>Neither agree or disagree</th>
<th>Entirely disagree, disagree, somewhat disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal auditors need to revisit their relationship with evaluation.</td>
<td>52.9%</td>
<td>29.0%</td>
<td>18.1%</td>
</tr>
<tr>
<td>In my organization, boundaries between internal auditing and evaluation are clearly defined.</td>
<td>50.4%</td>
<td>21.3%</td>
<td>28.4%</td>
</tr>
<tr>
<td>I would need to cooperate more extensively with evaluation to offer more effective advisory / consulting services.</td>
<td>41.4%</td>
<td>24.6%</td>
<td>34.1%</td>
</tr>
<tr>
<td>My ability to promote innovation would be enhanced if I worked more closely with evaluation.</td>
<td>30.8%</td>
<td>32.8%</td>
<td>36.4%</td>
</tr>
</tbody>
</table>
4. INTERNAL AUDITING AND INNOVATION IN THE PUBLIC SECTOR
As a secondary part of our mandate, we were also asked to consider whether and how internal auditing could contribute to innovation in the public sector. As we pointed out at the outset of the report, the public sector currently faces significant pressures to address new or intractable social problems, to deliver better services more efficiently and economically, and to adapt both its policy responses and its methods of service delivery to a fast-changing society characterized by rapid technological change, increasing social diversity and growing exposure to uncontrollable global forces. To meet those expectations and thrive in this environment, public organizations will need to become more innovative. They will need to find and successfully implement new ways of doing things, while meeting high standards of public accountability.

Obviously, the public sector is keenly aware of the need to become more innovative, as illustrated by the proliferation of innovation units (labs, hubs, etc.) and the creation of high-level innovation committees in recent years in some public services. The annual survey of public sector executives released by Deloitte and the Institute of Public Administration of Canada (IPAC) in 2015 also shows that public sector leaders are concerned about it. When asked to assess the importance of over a dozen areas for their organization in the next few years, 75% of the Canadian executives who responded to the survey identified “implementing innovative methods or solutions to public sector service delivery” as being important or very important. The implementation of innovations came second only to “focusing programs on measuring outcomes rather than outputs” (79% of respondents) as the most important area. Clearly, if internal audit could support the adoption of process and program innovations, it would align itself with an important objective of the public sector and potentially enhance its value.

But what should be the role of internal audit in public sector innovation? Our review of the academic literature on internal auditing and on public sector innovation did not find any significant research specifically focused on the role of internal auditing in innovation. On the one hand, as a review function without direct control over the levers of operation or much say in policy formulation, this role would seem necessarily to be limited and indirect. On the other hand, as professionals dedicated to the continuous improvement of their organization, internal auditors should be well positioned to assist in the process of innovation. In this last part of the report, we draw on our interviews, our survey and the academic literature to offer some perspective on what the role of internal auditing should be in building a more innovative public sector.

4.1 The nature and drivers of innovation in the public sector

While a comprehensive review of the literature on public sector innovation is beyond the scope of this report, it will be useful to note a few characteristics of innovation and some of the findings about what drives it. Firstly, innovation is not an easy and unequivocal concept. Everyone will concede that the Apple Watch and Google’s self-driving car are innovations, but they are hardly representative of the kind of changes that are typically recognized as innovative in both the private and public sectors. Many of them do not take the form of a product or service, but rather concern the way an organization operates. Most innovations are also more modest departures from the status quo.

In grappling with the diversity of innovations, scholars have long distinguished between technological (e.g. new products and services) and administrative innovations (e.g. new procedures, policies and organizational forms) (Damanpour, 1991). While entirely new services or technologies are clearly possible in the public sector, administrative innovations are more common and tend to be driven by different dynamics, where organizational learning and continuous improvement play a larger role (Moore, 2005). In fact, studies of innovations that have won or have been nominated for public sector awards in Canada found that they are predominantly incremental in nature as opposed to effecting truly transformative change or representing radically new departures (Bernier, Hafsi and Deschamps, 2015: 835).
Reflecting this broader reality, the literature on innovation contains a number of definitions, although many are derived from Rogers’ classic statement that an innovation is “an idea, practice or object that is perceived as new by an individual or other unit of adoption” (Rogers, 2003: 12). Moreover, while the actual impact of innovation is a matter for empirical assessment, innovations are consciously sought as means to make an organization more successful, to improve its performance in some respect. Hence, for the purpose of our report, we simply defined innovation as the conscious adoption of a change in service, process or practice that is meant to improve an organization’s performance.

In the public sector, most innovations seem motivated by the need to improve the quality of service delivery or find efficiencies in operations (Albury, 2005; Walker, 2007; De Vries, Bekkers and Tummers, 2016). Proactive problem solving is their primary driver (Borins, 2014b: 18-19). Innovations are also mainly transferred and adopted from other organizations rather than the result of original creations, i.e. they are new to the organization adopting them but not unique services, organizational forms or processes. The majority of public sector innovations, especially in Westminster systems, are initiated by middle managers and frontline employees rather than senior executives or governing bodies (Borins, 2014b: 31-32; Bernier, Hafsi and Deschamps, 2015: 836).

Some environmental factors have been correlated with higher rates of successful innovation. For example, larger public organizations are more likely to innovate, presumably because of the availability of slack resources. Relatedly, governments also innovate more when they enjoy budgetary surpluses, at least up to a point (Bernier, Hafsi and Dechamps, 2015). Public agencies that have more specialized mandates and enjoy more autonomy from government than traditional departments and central agencies are also more likely to innovate, presumably because this distance allows more risk-taking (Bernier, Hafsi and Dechamps, 2013).

In addition to such environmental factors, many studies have shown the importance of leadership and the attitude of senior executives (e.g. Borins, 2014a; Damanpour and Schneider, 2006) as well as the influence of an organizational culture that encourages such values as diversity, flexibility, dialogue, creativity and learning (Martins and Terblanche, 2003: 70-71). Risk aversion and how organizations respond to mistakes are also important factors: a balanced approach to risk and the creation of opportunities to openly and safely discuss and learn from mistakes are more conducive to innovation (Martins and Terblanche, 2003: 72).

Finally, organizational learning is a key determinant of innovation. To be good innovators, organizations need to be effective at acquiring knowledge from their external environment, developing knowledge from a critical understanding of their own practices, making the most of this consolidated knowledge base (through effective knowledge storage and dissemination) as well as exploiting their knowledge for their own strategic purpose (by transposing and interpreting knowledge in light of their own circumstances) (see Ferguson, Burford and Kennedy, 2013; Jimenez-Jimenez and Sanz-Valle, 2011: 409-410). While some of these capabilities are dependent on more intangible organizational culture, they are also created through purposeful knowledge management processes and administrative practices.

This summary review of the research findings on public sector innovation suggests that internal auditing practices can indeed contribute to the development of more or less innovative public organizations. As we will see, this will be especially true to the extent that the internal audit function supports organizational learning and encourages a productive attitude toward risk management.
4.2 The potential contribution of internal auditing to public sector innovation

Before we further discuss the role that internal auditors can play in support of public sector innovation, it is important to first note that, according to our survey results, internal auditors are already keen to support innovation in their organization. More than 80% of our respondents declared currently supporting and encouraging innovation in their organization. Only 7% said that this was not the case. It is interesting to note that, as a matter of contrast, only 57% of respondents felt that the senior executives of their organization were themselves encouraging innovation. Moreover, only 16% of our respondents believe that it is not their role, as internal auditors, to support innovation. In sum, internal auditors see themselves having a part to play in public sector innovation.

Despite the unequivocal views of our survey respondents, the chief audit executives that we interviewed often provided a more nuanced perspective about the current and future relation of internal audit to public sector innovation. “No. Internal audit is not supporting or encouraging innovation at the moment and, depending on how it’s done, we can certainly discourage it by promoting more process”, said the head of audit of a federal department. “I am not sure if internal auditing should be promoting innovation. Our priority should be making sure things are working properly and that we’re in compliance, but, for sure, we shouldn’t be standing in the way”, argued the chief audit executive of another department. Notwithstanding these sorts of qualifications, interviewees nevertheless agreed that the internal audit function should be mindful of its potential impact on innovation and most of them thought that the function was already making or could make in the future a positive contribution to efforts to make the public sector more innovative. We will now discuss three main areas that could be considered in this regard.

Table 6:

<table>
<thead>
<tr>
<th>Internal audit’s role in public sector innovation</th>
<th>Entirely agree, agree, somewhat agree</th>
<th>Neither agree or disagree</th>
<th>Entirely disagree, disagree, somewhat disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>As an internal auditor, I support and encourage innovation in my organization.</td>
<td>80.5%</td>
<td>12.7%</td>
<td>6.9%</td>
</tr>
<tr>
<td>It is not my role as an internal auditor to support innovation.</td>
<td>15.8%</td>
<td>12.8%</td>
<td>71.4%</td>
</tr>
<tr>
<td>Senior executives in my organization encourage innovation.</td>
<td>57.1%</td>
<td>20.7%</td>
<td>22.2%</td>
</tr>
</tbody>
</table>
4. INTERNAL AUDITING AND INNOVATION IN THE PUBLIC SECTOR

4.2.1 Auditing innovation and advising on transformation processes

When asked about how the internal audit function could help their organization innovate, several interviewees first raised the possibility of auditing the “innovation process” itself. As a senior audit leader put it, “audit is an approach, a set of techniques. We can pretty much audit anything. If the government sets targets for innovation or new rules, for example about required investments in experimentation, we could audit them.” “Where it makes sense, innovation could be included as an explicit objective of the program, so that we would look at it when we audit”, proposed another departmental chief audit executive. Amongst the more specific audit work that could be undertaken in this regard, interviewees also raised the possibility of auditing departments against some recognized benchmarks, such as the percentage of programs experimenting with new delivery methods or whether programs have tried new policy tools (e.g. nudge techniques, founded on behavioural psychology insights) in recent years.

Another idea is to conduct some “innovation audits” using a readiness or maturity model to assess an organization’s preparedness for innovation. The research on innovation and organizational learning has developed survey instruments to measure to what extent an organization possesses a learning culture and the types of knowledge management processes that can lead to innovation (e.g. Garvin, Edmondson and Gino, 2008). Such diagnostic and survey tools could contribute to such “innovation readiness” auditing. In fact, given internal auditing’s impressive diffusion to new areas over the last decade (e.g. ethics, environmental management), such an approach would even seem to conform to an overall pattern in the profession’s development.

However, we should point out that this approach to the use of auditing to support innovation also met with some criticism during our interviews. As one chief audit executive put it, “at best I can try to assess our maturity level for innovation, but I know that my deputy [head] will find it’s a waste of audit time. We’re already stretched. Management support is what is needed.” Moreover, given the intricate – and still largely intangible and contingent – dynamics leading to innovation, other interviewees were also sceptical that innovation could be usefully audited. While they conceded that these new services might lead to some useful diagnostics (e.g. comparing one’s learning culture to some benchmark), several interviewees were less confident about being able to tell managers how to become more innovative.

Maybe in part due to such concerns, some interviewees argued that internal auditors might be more supportive of innovation by simply continuing or expanding the kind of advisory services that they currently offer to help (re)design business processes. For example, when asked if he thought that internal auditors were creating barriers to innovation, a provincial non-audit executive said:

“I had the opposite experience! A few years ago, we changed the way we deliver [an internal service] to departments, so that we could pool the current expertise, save money on consultants and give a better service. The new system was designed with the advice of the [Ontario Internal Audit Division]. They helped us innovate by doing the design better.”

This basic argument – building the role of internal auditors as business advisers might be the most sensible thing to do to have them contribute to public sector innovation – was made by several audit executives.

Finally, several interviewees also spoke about the possibility of leveraging audit services to push more specific elements of the overarching management reform agenda of their organization. The specifics would vary across jurisdictions, but they could include the implementation of “lean” methodologies and evidence-based decision-making systems (e.g. the “deliverology” agenda in some jurisdictions).
These enterprise-wide initiatives are meant to transform how public management is done in their respective jurisdictions. As trusted advisors in the design of management controls and programs, internal auditors could help managers better understand and apply the principles and practices associated with these reform initiatives when they are called upon to provide advice on on-going projects or review existing processes or programs. In addition to offering advisory services related to these processes, auditors can also pinpoint where these methods could be useful in addressing weaknesses uncovered through an assurance audit. Obviously, to play such a role, internal auditors need themselves to be well versed in these principles and methodologies. In this perspective, some internal audit functions, such as the internal audit group of the Nova Scotia Public Service, have trained some of their auditors in techniques of lean management. However, in addition to acquiring the expertise, internal auditors must also remain closely connected to the broader strategic orientation of their organization, an element that is sometimes missing. Moreover, to fully capture this opportunity, the internal audit function might also have to collaborate more closely with other parts of its organization and be recognized as a potentially useful ally by the units driving these overarching initiatives. As some of our interviewees pointed out, in some provinces, these wider management reforms have often been driven by units located in the cabinet office or the treasury without any involvement by the internal audit function. “We’re just not seen as having this role or this potential by the center”, deplored one of our interviewees. Hence, in some jurisdictions and organizations, it might still be necessarily to overcome some out-dated perceptions about the potential role of internal auditors before they can contribute to those wider transformation efforts.

Whether it is advice on business process design, help in implementing new management reform initiatives or more novel innovation audits, this approach to supporting public sector innovation mostly entails expanding advisory services as part of the internal audit function’s portfolio. We already advocated such a development earlier in the report, noting that a broader range of services has been shown to correlate with more valued or effective internal audit functions in the academic literature and that our interviewees largely supported this development.

### 4.2.2 Risk aversion and the management of risk in the public sector

As we pointed out earlier, risk aversion has long been identified as barrier to innovation in the public sector (e.g. Borins, 2000, 2001, 2014; Bason, 2010; De Vries, Bekkers and Tummers, 2016). In Canada, a number of recent studies by prominent think tanks, such as the Public Policy Forum (2016), the Mowat Centre (Jarvis, 2016), the Institute for Competitiveness and Prosperity (2016) and the Canadian Comprehensive Audit Foundation (2010), have all identified excessive risk aversion as a significant problem across the Canadian public sector, hindering its performance, its capacity to innovate and limiting its contribution to the well-being and prosperity of Canadians. All have urged that measures be taken to change the culture of public organizations to allow for greater tolerance of experimentation, risk-taking and failure in the hope that they would become more innovative.

The vast majority of our interviewees similarly saw risk aversion as a problem. “There is too much process and risk aversion. You don’t fail in the Public Service”, said a chief audit executive somewhat sarcastically. The head of audit in a federal department made a similar point:

“We live in an extremely risk-averse environment. Even at the management table, you cannot have an honest conversation about failures. Everything is seen as personal criticism. Conversations are often about preventing headlines. How can you be smart and strategic about managing risks if you cannot talk about failures?”

A senior executive in a provincial ministry, recounting an experience to illustrate the problem, explained: “We tried to build a risk management framework, then we realized that we
had zero tolerance for risk... You don't need very sophisticated risk management when you want to mitigate *every* risk as much as possible!"

The internal auditors who answered our survey largely would seem largely to agree with this diagnostic. 62% of our respondents think that more public sector innovation is not possible without a greater tolerance for risk. 72% also believe that more innovation will not be possible without better risk management and 63% are of the view that more innovation requires better management of administrative controls.

If risk aversion and poor risk management are hindering innovation, then it clearly suggests a role for internal auditors in supporting a shift to a more innovative public sector. As we argued earlier in the report, a greater involvement of internal auditors in risk management education and the deployment of enterprise risk management is a promising avenue to help internal audit further enhance its contribution to the public sector. In this perspective, 49% of our survey respondents believe that their capacity to help their organization innovate would be enhanced if they worked more closely with risk management. Only 25% disagreed. Better understanding of risk management and its tools would help public organizations develop a “risk-smart culture” (Canadian Comprehensive Audit Foundation, 2010: 23-24).

Obviously, internal auditors will not shift the culture of their organization by themselves. Risk aversion is the result of a complex set of social and political forces that far exceed their reach. As a deputy minister interviewed in one of the provinces reminded us: “The risk aversion problem is real, but the fundamental issue is what’s coming from the media and opposition politics. The auditors can add to the problem, but they’re not the problem”.

**Table 7:**

<table>
<thead>
<tr>
<th>Internal audit, risk and innovation</th>
<th>Entirely agree, agree, somewhat agree</th>
<th>Neither agree or disagree</th>
<th>Entirely disagree, disagree, somewhat disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>More public sector innovation is not possible without a greater tolerance for risk.</td>
<td>62.1%</td>
<td>18.7%</td>
<td>19.2%</td>
</tr>
<tr>
<td>More public sector innovation is not possible without a better management of risk.</td>
<td>71.9%</td>
<td>17.1%</td>
<td>11.0%</td>
</tr>
<tr>
<td>More public sector innovation is not possible without a better management of controls.</td>
<td>63.2%</td>
<td>22.5%</td>
<td>14.3%</td>
</tr>
<tr>
<td>My ability to promote innovation would be enhanced if I worked more closely with risk management.</td>
<td>49.1%</td>
<td>25.4%</td>
<td>25.4%</td>
</tr>
<tr>
<td>Failures are a necessary part of the innovation process.</td>
<td>75.3%</td>
<td>15.3%</td>
<td>9.4%</td>
</tr>
<tr>
<td>There is a lower tolerance to project failure in the public sector than in the private sector.</td>
<td>46.4%</td>
<td>24.2%</td>
<td>29.3%</td>
</tr>
<tr>
<td>As an internal auditor, I feel I cannot promote anything that increases overall risk to my organization.</td>
<td>36.8%</td>
<td>23.6%</td>
<td>39.2%</td>
</tr>
</tbody>
</table>
That being said, internal audit’s contribution should not be underestimated. As the Canadian Comprehensive Audit Foundation noted, such “cultural change requires reinforcement from many angles” (Canadian Comprehensive Audit Foundation, 2010: 24). Given their expertise on balancing risks and controls, auditors can certainly make a significant contribution to such a shift in culture.

In fact, the role of internal auditors may be especially important because they are or have the potential to be “guardians of the corporate culture” (Sarens et al., 2009: 103), using their cross-cutting central position to help spread and reproduce organizational norms, both formal and implicit, about how to approach risk and administrative controls in both their advisory and assurance work. For example, the issues addressed, the language used in describing management shortcomings or strengths, and the substance and presentation of recommendations send signals throughout the organization about expected standards of conduct and (un)desirable attitudes toward risk-taking. In the event of failure, public entrepreneurs should not be needlessly chastised and audits that spot problems should also highlight good work in managing risks. As a federal head of audit put it: “We should be careful not to slap down people because they took a bit more risk to find ways to do things better. To me, it’s a tone, a communication issue as much as it is about the way audits are done: we should not make it sound like they were wrong for trying something new”. Of course, audit reports should also play a role in ensuring that as much as possible is learned from attempts at innovation.

Our interviewees largely supported such a role for internal audit, but some of them also noted that the promotion of this change in organizational culture would sometimes require internal auditors to be mindful of their own attitude toward risks and controls. As a deputy minister in a province argued:

“Audit has this huge opportunity to help the public sector understand how to fail in a useful way, how to ‘fail forward’, but there is still a lot of work to be done in the audit community to get their head around what is their role in this regard. And the managers also have to learn to relate to the auditors in this way, to seek help and be open to advice”.

A federal chief audit executive also pointed out that:

“Managers often actually want us to tell them what controls to put in but we really have to try to get them to better know their risks and help them think about how to come up with their own appropriate trade-offs. [...] On our side, sometimes we push controls too much. It’s an easy answer. But we should also ask if managers ‘over control’ things. Controls are often there because of history without any periodic rethinking of where the real risks lie”.

The head of audit in another department made a similar point:

“At the moment, I have to say that risk management is still an afterthought, an administrative obligation [for managers]. [...] There’s a lot to do before we meet our objective to have ‘smart controls’ – as few as possible but smart ones that do the job. For us, it’s always easier to recommend new controls, so it’s a change in mind-set for managers and internal auditors.”
On this score, it is also interesting to note that, despite a majority of our respondents seeing a need for greater risk tolerance and better risk management, 37% of our respondents still felt that they could not promote anything that would result in an increase in overall risk for their organization.

Still, the opportunity is there for internal auditors to help the public sector become more innovative by helping change the culture of risk aversion and supporting the acquisition of better risk management practices. The head of internal audit in a province might have summed it best:

“Public sector executives have an adequate understanding of risks, but below the managers have a fair to poor understanding. They’re just too focused on the day-to-day to have time to step back and see the broader picture. There are not enough conversations about risk tolerance. [...] So, better risk management is part of what’s needed for innovation and internal audit can play a key role in helping people understand risk. That’s a key contribution that we can make to innovation”.

4.2.3 Internal auditing and the facilitators of organizational learning

As we saw earlier, there is more to public sector innovation than higher risk tolerance and smarter risk management. A high level of organizational learning is also particularly important. In the private sector, organizational learning has been shown to lead to innovation. In fact, the management literature shows a positive relationship among organizational learning, innovation and performance, with innovation mediating the relationship between learning and performance (Jimenez-Jimenez and Sanz-Valle, 2011). Given that one of the main sources of value offered by an internal audit function is its contribution to organizational learning, there is an obvious convergence between a more effective, value-adding internal audit function and the development of a more innovative public sector. In other words, most of the changes discussed in the third part of this report, from more systematically and widely disseminating the lessons drawn from audit work to improving the communication of audit findings and more effectively using data analytics, would not only increase the value and effectiveness of internal audit; they would also enhance the capacity of the public sector to learn and innovate from the expertise and work of auditors.

The research on organizational learning provides evidence that should enhance confidence in this strategy. This literature makes clear that there is much more to organizational learning than the simple generation of information and knowledge. Assuming that an organization will instinctively make the most of available information and knowledge, including internal auditors’ findings and expertise, would be excessively optimistic. The leadership, culture, structural arrangements and processes of organizations affect how knowledge is acquired, interpreted, disseminated, used by managers and eventually stored for future retrieval (e.g. Argysis and Schon, 1978; Senge, 1990; Huber, 1991; Brodtrick, 1998; Finger and Brand, 1999; Reagans and McEvily, 2003; Naot, Lipshitz and Popper, 2004; Lopez, Peon and Ordas, 2005; Garvin, Edmondson and Gino, 2008). Some organizations are undoubtedly better than others at embedding learning processes in their organizational routines (Rashman, Withers and Hartley, 2009: 476).

Hence, for internal auditors eager to have an impact on their organization, focusing on the generation of insights through high quality auditing and rigorous analysis is, at best, only half the battle. To maximize its “learning value”, an internal audit function must also seriously consider how its design and practices facilitate not only the generation and acquisition of knowledge about controls, risk management and sound governance, but also its transfer to potential users, the conditions of its reception, its dissemination through the organization, etc. To help in this process, it is worth noting what
are some the concrete learning mechanisms and facilitators of organizational learning that have been observed as effective in the Canadian public sector by previous research. 19

In this respect, drawing from the views of hundreds of executives from the federal public service, Jacques Barette and his colleagues provide one of the few studies seeking to identify the facilitators of organizational learning in the Canadian public sector (Barette et al., 2012). The study identified 29 facilitators of organizational learning grouped under five categories: knowledge acquisition and transformation, organizational learning support, organizational learning culture, leadership of learning and strategic management. In the next table, we list 18 of those facilitators that appear to be highly relevant to the practice of internal auditing.

As we can see, an internal audit function can naturally contribute to organizational learning by supporting or providing many of those facilitators. For example, in discussing their unique value to their organization, many interviewees stressed the advantage of being an horizontal function, drawing intelligence from all corners of their organization, developing a cross-cutting view on organizational performance and challenges, and being able to disseminate knowledge throughout the organization. As such, the internal audit function is well positioned to encourage the sharing of information across units, one of the facilitators of organizational learning.

By its very nature, the internal audit function is also a key provider of regular assessment of processes and resource use. Through its audit work, it should support an evidence-based and rigorous questioning of the value and utility of existing administrative rules. By bringing to bear its expertise on the use of controls and risk management, it can also bring in and disseminate new ideas about best practices in its areas of responsibility. Furthermore, the internal audit function, through its reviews and assessments of processes and practices, is well positioned to identify key training needs, as well as potentially supply such training, in its domains of expertise (e.g. fraud, ethics or risk assessment).

All these activities speak directly to some of the key facilitators of organizational learning.

In sum, the current internal audit function is naturally positioned to support broader processes and dynamics of organizational learning across the three key dimensions of knowledge acquisition and transformation, organizational learning support and the nurturing of an organizational learning culture. What may be needed, depending on the organization, are some changes in structures, policy or practices to allow the internal audit function to deliver even more value in this regard. In the third part of this report, we discussed eight areas where such changes can be profitably considered, but there are undoubtedly other possibilities. However, to fully capture these opportunities, it would be imperative for chief audit executives, and internal auditors more generally, to think more explicitly in terms of organizational learning and consider more systematically how their internal audit function performs with regards to knowledge management practices.

This approach to supporting public sector innovation may also be justified by the fact that internal auditors themselves appear to have a fairly critical view of their organization’s current learning capacity. Our survey asked a number of standard questions related to organizational learning. Amongst our respondents, only 28% believe that their organization is open to constructive criticism and only 35% thought that it is encouraging productive conflict and debate in internal discussions. 34% of our respondents also agreed that, in their organization, well-established perspectives and assumptions are simply never challenged or questioned and only 33% said that their organization encourages experimentation and alternative ways of getting work done. Finally, only 30% of the respondents said that their organization had procedures to ensure that lessons learned in the course of a project are passed along to others doing similar tasks. In sum, it seems clear that most internal auditors think that much can still be done to transform their organization into a learning one.

Finally, for other leaders in the public sector, there is a clear opportunity to use internal auditing
Table 8: 

<table>
<thead>
<tr>
<th>Selected facilitators of organizational learning in the federal Public Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>Horizontal structures encourage sharing between units or the entire organization</td>
</tr>
<tr>
<td>New ideas are quickly disseminated throughout the entire organization</td>
</tr>
<tr>
<td>Systems distribute information in an easy-to-understand, accessible format</td>
</tr>
<tr>
<td>Useful work practices are shared between employees</td>
</tr>
<tr>
<td>Managers ensure that information is disseminated throughout the entire organization</td>
</tr>
<tr>
<td>There is examination and reflection to analyze why a project/program succeeded or failed</td>
</tr>
<tr>
<td>There is a regular assessment of objectives, activities, methods and resources use</td>
</tr>
<tr>
<td>Others in the organization are informed of lessons learned from past actions</td>
</tr>
<tr>
<td>Organization makes key information available through information systems</td>
</tr>
<tr>
<td>Organization reviews available reports in anticipation of change</td>
</tr>
<tr>
<td>There is concrete support (e.g. resources, tools) for managers learning and professional development</td>
</tr>
<tr>
<td>Employees are given training on identified needs</td>
</tr>
<tr>
<td>Employees can apply at work what is learned in training</td>
</tr>
<tr>
<td>Organization is open to change and innovation</td>
</tr>
<tr>
<td>Organization encourages sharing and mutual assistance</td>
</tr>
<tr>
<td>Formal rules can be questioned for utility and value</td>
</tr>
<tr>
<td>Organization encourages an experimental attitude</td>
</tr>
<tr>
<td>Organization perceives any changes as an opportunity, not a threat</td>
</tr>
<tr>
<td>Source: Adapted from Barette et al., 2012: 143.</td>
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</table>

Processes to further “embed” learning systems and routines in their organization, one of the common features associated with a successful learning organization (see Rashman, Withers and Hartley, 2009: 476) and, ultimately, one that is more innovative and performs better. Beyond accountability and assurance, an effective internal audit function resolved to maximize its learning value is surely deserving of strong and consistent support as part of a broader strategy to make the public sector more innovative, evidence-based and high performing.
CONCLUSION

We were asked to investigate how internal audit functions could enhance their effectiveness and maximize the value that they deliver to the public sector in the future. Through a review of the academic literature and some empirical research, we conclude that the value of internal audit fundamentally rests on its ability to deliver reassurance and comfort to senior executives and to foster organizational learning in support of administrative improvements across their organization. We further conclude that much of the gains in effectiveness and value that currently seem possible and desirable would come from enhancing internal audit’s contribution to organizational learning. Moreover, at a time when the public sector is asked to become more frugal, efficient and innovative, a focus on maximizing learning and continuous improvement in even more important.

There is no doubt that internal auditors play a valuable role for the public sector by providing an effective “third line of defence” against ineffective controls, poor governance and defective risk management. But playing good defence does not exhaust the value that an effective audit function brings to a public organization. A good defence must also proactively support the capacity of its team to perform. Today’s internal auditors can also play an important role in facilitating organizational learning and even successful innovation across the public sector. However, to fulfil this potential, more attention must be paid to the ways in which auditors can more effectively collect, analyse and distribute relevant knowledge and know-how across their organization. We hope that our report will have provided some possibilities on how to do so.

It is a cliché that academics like to end research reports by stressing the need for more research. Still, we would be remiss not to point out the paucity of studies specifically dedicated to better understanding internal auditing in the public sector. There is a wide range of questions and issues that would warrant academic investigation. For example, much could be learned from looking at how line managers and program executives perceive their audit function, what impact audits actually have on their work, their attitude to risk or their understanding of controls, etc. To fully understand the relationship between internal auditing, organizational performance and innovation, we need to know more about the behavioural impact of auditing practices on auditees. But, from the interplay between the audit and risk management functions to the effects of specific audit practices or the efforts dedicated to use of data analytics, there are numerous other possibilities. There is no doubt that some of this research could help cast further light on the possible future of internal auditing in government. We hope that this report will also have made a modest contribution in this respect.
References


Rashman, L., E. Withers and J. Hartley (2009) “Organizational Learning and Knowledge in Public


Secretariat of the Treasury Board of Canada (undated) *History of Internal Audit in the Federal Government*, Ottawa, 5 pages.


Appendix A: Sources and Methods

The project’s methodological approach was reviewed by the University of Ottawa’s Ethics Committee to ensure compliance with the Tri-Council Policy Statement on the Ethical Conduct for Research Involving Humans (2nd ed. 2010). Ethical approval of the project (file number 09-15-07) was granted on October 13th 2015.

Three different primary data collection methods were used in this project: roundtable discussions, open-ended face-to-face and telephone interviews, and an online survey.

Roundtable (November 16th, 2015)

The roundtable took place on November 16th, 2015 at the University of Ottawa. There were 11 active participants, a moderator, two observers, and two researchers. The roundtable lasted approximately two hours. Participating members included high ranking senior executives from the Canadian Federal Government, the Government of Ontario and the Institute of Internal Auditors as well as a group of former public servants who sit on or chair Departmental Audit Committees.

Participants were informed ahead of time of the questions they would be asked to discuss during the event. More concretely, they were invited to discuss how they see 1) the current strengths and weaknesses of internal auditing in government; 2) the areas where participants believe internal auditing itself has the greatest potential to innovate; and 3) the ways in which internal auditing could facilitate greater innovation across the Public Service. The discussion was conducted under Chatham House Rule and the information gathered informed the design of the interviews and survey instrument.

Open-Ended Interviews (n=47) (February - May 2016)

A total of 47 interviews were held with audit executives working across the Canadian Public Sector. Interviews took place face-to-face whenever possible, by phone otherwise. They lasted on average between 60 and 90 minutes. Potential participants were identified with the help of GIACC, the IIA, through independent contact with known key informants, website searches or referrals from colleagues or other interviewees. Most of our interviewees were chief audit executives (exact titles vary), but we also interviewed audit managers, the comptroller general in two jurisdictions, a provincial deputy minister, an assistant auditor general, a few chairs or members of departmental audit committees, some senior program managers / non-audit executives and a professor with expertise in internal auditing. 18 respondents work for the federal departments or agencies, while 28 are employed at the provincial or territorial level. Despite our best effort, we were unable to secure interviews from Prince Edward Island, New Brunswick and Alberta.

Interviewees were told that the project is a collaboration between GIACC and the University of Ottawa and were informed that the anonymized results of the study would be published in a GIACC report and used in subsequent academic publications. The interviews were semi-structured. They were guided by six open-ended questions examining how the IA function adds value to organisations, perceived strengths and weaknesses, its capacity to adapt to a rapidly changing environment and its potential for supporting public sector innovation more generally. However, interviewees were also encouraged to speak freely and openly about the issues they found important to the future of IA in Canada’s public sector. In general, interviewees spoke remarkably candidly and were extremely generous with their time.

Online Survey (April 21st- June 10th)

The roundtable and the open-ended interviews in addition to the academic literature on internal auditing and public sector governance informed the design of an online survey targeting Canadian public sector IA practitioners across the country. A preliminary paper version of the survey was pre-tested on a small group of IAs. The final amended version was translated into French and converted to an online format by the IIA’s (Orlando, FL) technical team who also distributed it through its own IIA members’ list. Initially, the survey used
fixed URL addresses but monitoring of response rates indicated that we were unlikely to reach a sufficient portion of our target audience. Consequently a link to the survey was posted on the Canadian Public Sector Audit Centre and a more portable open link was circulated on May 5th through 50 personalised emails to Canadian Public Sector audit executives and members of the IA community asking their help in distributing the survey through their respective networks. Using this ‘snowballing’ approach, we obtained 459 responses, 400 of which are useable. The IIA-Canada’s executive director estimates the target population to be around 1500 IAs yielding an approximated response rate of 31% (27% useable responses). We are extremely grateful to Matthew Inman, Karina Santoro, Shelley Pelkey and James Go for their help in reaching our target audience.

Depending on the number of filters, the survey contained approximated 110 questions – most of these associated with a seven point Likert scale – and took around 30 minutes to complete. The first part of the survey collects information about the respondent’s background, work experience and familiarity with IIA standards. It also asked them to rank statements about what they see as their most important role. This section is followed by 82 statements where respondents are asked to rank on a seven-points Likert Scale (1=Entirely Disagree; 7=Entirely Agree). For the purpose of this report, these responses were regrouped into three categories (1= Entirely Agree, Agree, Somewhat Agree; 2= Neither Agree or Disagree; 3= Entirely Disagree, Disagree and Somewhat Disagree) to improve readability. These statements explore how IAs perceive their role in the organization more generally and specifically in relation to risk management, innovation, and in the provision of advisory/consulting services. We also include questions that target the role of professional bodies and the potential for innovation within the internal audit function itself. The final section of the survey collected demographic information about the respondents, their certifications, and their usage of data analytics.

It was a relatively taxing survey that required IAs to reflect carefully on various aspects of their work. Moreover, the diverse nature of the IA function implies that a ‘one-size fits all’ questionnaire was not possible (e.g. in some units, IA and evaluation are joined up). The IA community has been unusually cooperative in this respect as exemplified by the 338 relatively detailed responses we received to the voluntary and open-ended question located towards the end of the survey asking respondents their views on what would be the more important change to make (if any) to the internal audit function so it can enhance the value of its contribution to the public sector. These comments were subsequently coded into 26 distinct categories.

As with most survey instrument, our approach suffers from a number of caveats. Firstly, we were unable to obtain a precise figure as to the number of public sector IAs in Canada. Our response rate is based on an estimate produced by the IIA. We are also conscious that the survey was taxing and relatively long which may have generated non-responses and contributed to the 4% of non-useable responses. We received three comments about the survey – one indicating confusion about the lack of don’t know option (the respondent did not consider a score of 4 (neither agree or disagree) to be a suitable alternative) and one indicating confusion about whether ‘organisation’ referred to the department or the Audit function. The reference to organisation was defined in the preamble but with hindsight we should have reminded respondents at key location throughout the survey.

Data Analyses

The data collected through these three approaches is substantial, very rich and will take some time to analyse thoroughly. The roundtables and the interviews provide qualitative insights into the issues faced by the IA function while the online survey delivers a more quantitative snapshot of how practitioners across the country perceive these issues. The software SPSS was used to code and organize the data in the first instance and subsequently to compute descriptive statistics of the responses. A number of t-tests and Chi-Square tests were used to investigate differences between provincial and federal IA responses. These results were used to complement the discursive accounts. Throughout this report, we have endeavoured to stay as objective as possible in depicting our findings in accordance with our mandate. Our recommendations may consequently appear somewhat timid but they are based on a systematic and representative account of Canadian public sector IAs’ own views of their function, its strengths and weaknesses, its value-added, and its capacity to innovate and support innovation.
Endnotes


2 In Québec, departments must prepare annual reports assessing their performance against their strategic plan. The report, tabled in the legislature, must contain an affirmation by the deputy head that the information presented is reliable and supported by adequate internal controls. See section 24 of the Loi sur l'administration publique: http://www2.publicationsduquebec.gouv.qc.ca/dynamicSearch/telecharge.php?type=2&file=A_6_01/A6_01.html Many interviewees have questioned the value of having the internal audit function dedicated so much time supporting the production of these annual reports.

3 In the public sector, the issues of the “primary client” and the reporting line of the internal audit function are even more complex than in the private sector. While private organizations typically have a board acting as their governing body (and an audit committee dealing with internal auditing on its behalf), it is only the case in some public organizations. In Canada, for the core public administration, the governing body is really the cabinet, but internal audit functions rarely report to the cabinet or one of its committees. To our knowledge, this is only really the case in British Columbia, although more cursory reports are submitted to cabinet committees in some other provincial jurisdictions. In most jurisdictions, the internal audit function functionally reports to an audit committee mainly composed of senior executives (deputy and assistant deputy heads) and, at times, external members. However, it should be noted that, in order to protect the impartiality of the public service, deputy heads of public service departments are often legally required to directly account for the conformity and performance of some key administrative processes under their authority (e.g. staffing, expenditure management). In such circumstances, it makes imminent sense for the internal audit function to support them rather than ministers.

4 The three lines of defense model is set out in a “position papers”, which, as a part of the IIA’s International Professional Practices Framework, offer non-mandatory but “strongly recommended” guidance.

5 For example, this conception is clearly embodied in an unpublished working paper by the federal OCG, which attempts to craft a vision for the future of the profession within the federal Public Service. See Office of the Comptroller General of Canada (2013) A Value Proposition: A recognized and sustainable professional internal audit community across the Government of Canada to strengthen the accounting officer model, Ottawa, unpublished report.

6 While these reforms were crucial, it is worth noting that the efforts to strengthen and recenter federal internal auditing on assurance engagements had begun in the late 1990s with the « Modern Comptrollership » initiative, the (re-)separation of the internal audit and evaluation functions, and the adoption of a new Policy on Internal Audit (Secretariat of the Treasury Board of Canada, undated: 4).

7 See, for example, the Institute’s webpage entitled “Value proposition: Internal auditing’s value to stakeholders” at https://na.theiia.org/about-us/about-ia/Pages/Value-Proposition.aspx

8 While it is analytically useful to separate the two, learning and comfort are in fact related. As studies on auditing in the private sector have pointed out, audit committee members obtain a greater sense of comfort about their organization’s control environment when they are confident that operational managers are learning from audit findings and use them to improve their processes and practices (Gendron et al., 2004; Sarens et al., 2009). In this sense, effective learning outcomes also help internal audit meet the senior leadership’s demand for comfort.

9 There is an important conceptual difference between value and effectiveness. However, one can easily imagine an internal audit function effectively delivering an audit service that holds little value for its organization. Hence, while being ineffective at delivering a high value service implies that some potential value is not being realized, internal audit effectiveness should not be considered synonymous with value-added audit services. Unfortunately, the internal audit literature (both industry reports and academic articles) often uses both terms interchangeably. In this report, we work on the premise that effectiveness is an important component – but only a component – of the value-generation process for an internal audit function.

10 It should be noted that, given the methodological challenges, most of those studies rely in good part on the self-assessment and perceptions of internal auditors, especially chief audit executives in the private sector, to identify key characteristics. In other words, there are few objectives measures of value or effectiveness. The value of some
ENHANCING THE VALUE OF INTERNAL AUDITING IN THE PUBLIC SECTOR

recent attempts at more objective measures, such using “percentage of audit recommendations implemented” as an indicator of effectiveness, could be debated as providing only a crude and partial measure of the concept, and even such an indicator necessarily depends on self-reporting and in-house estimates. For a discussion of process, output and outcome measures of audit effectiveness used in the literature, see Arena and Azzone, 2009: 48-49.

11 Given the structural differences between the private and public sectors, we ignored some of the factors discussed in the internal audit literature but that were not applicable to a public sector setting.

12 In some public services, the independence of the function is bolstered by some additional institutional protections. For example, in the federal public service, the Office of the Comptroller General protects internal auditing budgets. This is also partly the case in Ontario, where some funding is allocated centrally while other funding comes from departments.


14 In fact, as Nutley and Davies (2001) argue, attention to context might be even more important to organizational learning in the public sector because of the organizational dynamics created by the more contested and political nature of service processes and outcomes as well as the effects of the unique accountability expectations. It can prove difficult to transplant more generic solutions or private sector management best practices to such an environment.

15 Exceptions are made, for example, for audit reports that could jeopardize the security of the public, endanger government operations or provide information that could be used to defraud the government.

16 The controversy concerned an internal audit of eight grants and contributions programs delivered by the federal department of Human Resources Development (HRDC), which was proactively released in 2000. The audit randomly reviewed 459 project files to assess whether they contained the proper documentation and found that a significant proportion of the files lacked some of the expected documents, such as the original application form (15% of the files), cash flow forecasts (72% of the files) or a proper description of the expected results of the funded project (11% of the files). Given these shortcomings, the audit called for better project monitoring, contracting procedures and financial practices. The department agreed with the audit’s recommendations and about half of the audit report released to the public was dedicated to describing a comprehensive action plan to improve the programs’ management.

However, using the total estimated budget of the eight programs, the national media misconstrued the audit’s findings as proving that the government “had lost a billion dollars”. Fuelled by partisan politics, the audit soon gave rise to a national political controversy that lasted for months, was the subject of more than 800 questions asked by the Official Opposition to the minister of HRDC and eventually led to the adoption of new grant application procedures that imposed a stunning level of work on the department and applicants, many of whom were small community groups. The approval procedures introduced in response to the controversy initially required the completion of 24 separate forms and checklists, some of them with 1 800 individual fields of information (Good, 2003: 117). Meanwhile, almost a year after the controversy erupted, a departmental review of 17 000 project files actually only found $85 000 in overpayments under the programs covered by the audit.

The HRDC scandal arguably became the ultimate example of an internal audit, initially used as a tool for improving management and ending up inflicting considerable damage on the organization’s reputation, reducing the trust of citizens and triggering a multiplication of controls. It is instructive to note, more than fifteen years after the events, several federal executives and audit committee members interviewed for this project still mentioned the “HRDC scandal” to illustrate the dangers of internal auditing in a political system driven by conflict and fuelled by a media prone to sensationalism. The HRDC scandal is clearly a complex event, with multiple causes and opened to various interpretations. It is also an outlier in the history of public sector auditing. However, it is clear that, in the circles of the federal public administration, the controversy still stands as an example of how internal auditing can inadvertently lead to dire consequences for auditees. “Look at the HRDC $1 billion ‘boondoggle’ that turned out into some misspending way below the materiality threshold”, a chief audit executive explained, “it’s no surprise that our audit reports don’t say much about why you recommend x or y. You don’t say a lot because it’s public! We can’t be blunt in our assessments, like they can be in the private sector, because the stakes are high and the issues are often misconstrued by the media.”

18 We would like to thank the Institute of Public Administration of Canada for generously providing us with the data specific to Canadian public sector executives. The global survey covers four countries (Australia, Canada, the United Kingdom and United Arab Emirates) and its overall results are presented in the report *Public Sector Executive Survey: Global Executive Summary (January 2015)*, published by Deloitte and Institute of Public Administration of Canada.

19 As scholars frequently noted, the actual cognitive processes of organizational learning are difficult to observe directly. For this reason, a considerable part of the empirical literature is dedicated to the study of either cultural traits, procedural arrangements or concrete learning practices that are correlated to observable changes in an organization's pattern of activities, indicating the transfer of individual-level learning into organizational norms and procedures. In this perspective, relying on various methods, scholars have attempted to identify concrete organizational learning mechanisms or facilitators associated with effective learning organizations, which is why we focus on facilitators in this part of the report. (For a discussion of this problem and strategy, see Popper and Lipshitz, 2000: 182-185; DiBella, 2001).
Luc Juillet

Luc Juillet is a professor of public administration and policy at the Graduate School of Public and International Affairs at the University of Ottawa. In the recent past, his research has mainly focused on the evolution of personnel systems in Westminster countries as well as the regulation of conflicts of interests and transparency in government. From 2006 to 2012, he served as the founding director of the Graduate School of Public and International Affairs and Associate Dean of the Faculty of Social Sciences at the University of Ottawa. In 2012, he was a Visiting Professor at the University of Melbourne in Australia. Over the years, he also worked as a consultant for various public organizations on matters of policymaking and administrative reforms. Most recently, he was an expert witness for the Department of Justice, the Federal Court of Canada and the Cour supérieure du Québec on matters related to public service legislation and he worked as an international expert for the Ministry of Administrative Reforms of the Government of Greece on issues related to ethics and personnel administration.

Catherine Liston-Heyes

Catherine Liston-Heyes is an economist by training with degrees from University of Ottawa and McGill University. From 1993 to 2011 she has been a member of faculty at the School of Management at Royal Holloway College, University of London, where she was PhD director and subsequently Head of its Accounting, Finance and Economics group. Her research is invariably motivated by and anchored in real public policy questions and controversies, and in addition to academic work she has advised the OECD on regulatory and transport matters. She has extensive experience in teaching university-level executive and professional in London, Hong Kong, New York and Singapore. She is currently director of the Graduate School of Public and International Affairs.

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David Zussman is a senior fellow at the Graduate School of Public and International Affairs at the University of Ottawa, where he also held the Jariwaysky Chair in Public Sector Management from 2005 to 2015. He also served as President of the Public Policy Forum (1995 to 2003), Executive Vice President of Ekos Research (2003 to 2005), Dean of the Faculty of Management at the University of Ottawa (1988 to 1992), and Assistant Secretary to the Cabinet (Machinery) at the Privy Council Office (1994 to 1995).
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**Business Report (Graph)**

[Graph showing data distribution]