

INTERNAL AUDIT QUALITY: A MULTI-STAKEHOLDER ANALYSIS

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SUMMARY

The internal audit function (IAF) is a key component in an organization's corporate governance system. Despite the importance of the IAF to organizations, little is known about IAF quality beyond the viewpoint of the external auditor or beyond the IAFs role of assuring financial reporting. To better understand the concept of IAF quality we consider the experiences of a number of corporate governance stakeholders by conducting 36 interviews with participants from very large Australian firms including audit committee members and chairs, senior management, heads of in-house IAFs, and partners of internal audit divisions from the major accounting firms. The interviews are used to examine how IAF stakeholders judge IAF quality and determine if different IAF stakeholders judge IAF quality differently. The key insights from this study reveal that IAF quality is complex, multi-dimensional and is assessed differently by various IAF stakeholders who use a select number of information cues in their judgment process.

Keywords: corporate governance, cues, internal audit, interviews, judgment, quality

INTRODUCTION

Heightened pressure and accountability on corporate governance actors has increased the prominence and reliance on the internal audit function (IAF) (Cohen et al., 2010; Desai et al., 2010; Glover et al., 2008). The IAF is a key component of a firm's corporate governance system (Anderson et al., 2012; Glover et al., 2008; Krishnamoorthy and Maletta, 2008; Prawitt et al., 2011; Prawitt et al., 2009) and a resource to a number of governance stakeholders, such as the audit committee, senior management and external auditors (Bame-Aldred et al., 2013; Gramling et al., 2004; Trotman and Trotman, 2014). The IAF provides these stakeholders with information on a range of important issues. As the judgments and decisions of these stakeholders are often critical to their organizations, the quality of information they receive from the IAF is of significant importance. Information is a critical resource in contemporary organizations and the quality of information is fundamental to decision making (Stvilia et al., 2007). For example, professional accounting bodies report that the quality of information received is a principle challenge facing audit committees in executing their responsibilities effectively (ICAA et al. 2012). As such, it is expected that IAF stakeholders consider the quality of the IAF before relying on IAF information, as the quality of information is a fundamental determinant in the use of that information and the resulting quality of their judgments, decisions and actions of a person relying on the information (Groysberg and Lee, 2008; Neely and Cook, 2011; Thayer, 2011).

Research on IAF quality establishes that variations exist among the quality of IAFs and the importance of IAF quality to external financial reporting and external audit (Abbott et al., 2012; Felix et al., 2001; Lin et al., 2011; Prawitt et al., 2012; Prawitt et al., 2009). However, the existing research on IAF quality has focused on the relationship between IAF quality and the external audit(or). Outside of this relationship, little is known about other stakeholder

perspectives and judgments of IAF quality, or how IAF quality influences stakeholders' reliance on information provided from the IAF.¹

IAF quality measures have almost exclusively focused on three components of quality prescribed in external audit standards: competence, objectivity and work performed (AICPA 1990; PCAOB 2007; IFAC 2009c). These 'three factors' proposed in external audit standards are solely input factors. Other business and psychology disciplines (e.g. service marketing and team performance) show that measuring quality is complex, multi-dimensional and contingent on the needs of the client(s). Quality measures developed in these disciplines include a number of determinants beyond input factors (for e.g. Brady and Cronin, 2001). With an increased reliance on the IAF by multiple governance stakeholders there is a need for the quality of the IAF to be better understood as internal audit is only a valuable resource if it is viewed as possessing an appropriate level of quality (Desai et al., 2010; Gramling et al., 2004).

The way IAF stakeholders, besides the external auditor, judge IAF quality and their reliance on the IAF has generally not been addressed in the literature. Judgments on quality can differ amongst stakeholders depending on their relationship with the other party and the lens through which they judge quality (Aguilera et al., 2008; Cohen et al., 2013; Gramling et al., 2004; ICEAW 2010; IAASB 2011; Lampe and Sutton, 1994). Differences may exist among various IAF stakeholders' views as each stakeholder has different and diverse needs and views compared to the external auditor (Cohen et al., 2004).

We conducted 36 in-depth interviews with key governance stakeholders, namely audit committee members and chairs, senior management, heads of in-house IAFs, and partners of internal audit divisions from large accounting firms, to understand how these stakeholders

¹ For an exception, see Lampe and Sutton (1994) who investigate internal auditors' views of IAF quality factors compared to external auditors' views.

make judgments of IAF quality and whether there are differences among IAF quality views between different stakeholders. We find that IAF stakeholder groups judge IAF quality differently and the IAF stakeholder groups use a select number of information cues in their judgment process. Judgments for audit committees are based on IAF outputs; senior management judgments are based predominantly on IAF outcomes, supplemented by IAF outputs; in-house internal auditor judgments are based on IAF processes; and internal audit partner judgments are based on both IAF outputs and outcomes.

This study makes two major contributions. First, we examine the concept of IAF quality from a multi-stakeholder perspective, thereby extending prior literature beyond the sole perspective of the external auditor. A salient feature of this study is that dimensions and attributes of quality are identified by users and preparers of internal audit based on their experiences, in contrast to factors prescribed by external audit standards or researchers.

Second, a contribution is made outside of the internal audit field to the broader quality measurement literature and the body of conceptual quality frameworks. In particular, the professional accounting bodies are investing considerable effort in the development of external audit quality frameworks (IAASB 2011; KPMG 2010; e.g. FRC 2008). Whilst not assessing external audit quality, our results contribute a new way of determining important quality factors and support the appropriateness of current external audit quality frameworks in including multiple dimensions and stakeholders.

The remainder of this paper is structured as follows: In the next section, we discuss the background and relevant theory for this study. The third section details the methodology employed. The fourth section presents the findings. The final section provides a discussion of our findings and the conclusion for this study.

BACKGROUND AND THEORY

The internal audit function (IAF) is an integral component within corporate governance (Anderson et al., 2012; Bame-Aldred et al., 2013; Desai et al., 2010; Glover et al., 2008; Prawitt et al., 2009). In fact, Cohen et al.'s (2004) model of corporate governance includes internal audit as one of five internal governance stakeholders along with the audit committee, management, external auditors and the board of directors. Their model identifies that the IAF has direct relationships with the audit committee, senior management and external auditors, hereafter collectively referred to as the 'users' of the IAF, whilst internal auditors are referred to as 'providers'. Together, the 'users' and 'providers' are collectively referred to as 'IAF stakeholders'.

Gramling et al. (2004) provide a comprehensive review of IAF quality research and note that "the literature on IAF quality has almost exclusively been examined from the view of the external auditor" (Gramling et al., 2004, p. 210). Consistent with Gramling et al.'s (2004) earlier observations, the focus of recent research has primarily been on the external auditors' views of IAF quality and IAF quality's impact on financial reporting activities. This research finds that high IAF quality improves both firm outcomes (Lin et al., 2011; Prawitt et al., 2012; Prawitt et al., 2009) and increases external auditor reliance (Desai et al., 2011; Felix et al., 2001, 2005; Glover et al., 2008; Krishnamoorthy and Maletta, 2008; Messier et al., 2011; Pizzini et al., 2012). However, an IAF serves each of the internal governance stakeholders, but little consideration has been given to these other stakeholders and how they assess quality. In addition, research documents the evolving role of internal audit beyond an extension of the external audit, primarily focused on financial controls (e.g. Burton et al., 2012; Carcello et al., 2005; Cohen et al., 2010; E&Y, 2011; Gramling et al., 2012).

The pervasive external audit perspective of IAF quality has also limited how research measures IAF quality. Researchers have based IAF quality measures upon a prescriptive

model of three factors advocated within external audit standards (AICPA 1990; IFAC 2009; PCAOB 2007). These standards contend that for an external auditor to rely on internal audit work, the external auditor must exercise professional judgment in assessing IAF quality including internal auditor competence and objectivity and that the nature and scope of the work performed by the IAF is relevant to financial reporting and financial statement audits. These three external audit standard factors – competence, objectivity and work performance – are hereafter referred to as the ‘three factors’.

Studies assessing external auditor reliance on the IAF have used the ‘three factors’ as the basis for their measurement (Desai et al., 2011; Desai et al., 2010; Felix et al., 2005; Glover et al., 2008; Messier et al., 2011). In addition, studies investigating IAF quality and firm outcomes (Kaplan and Schultz, 2007; Lin et al., 2011; Prawitt et al., 2012; Prawitt et al., 2009) have also based their quality measurement on these standards.² We suggest that the ‘three factors’ employed in IAF quality measurement to date are inputs to the IAF. However, the concept of IAF quality is broader than solely the quality of inputs and that the problem with focusing solely on inputs to assess quality is that other critical factors that may affect quality are not considered and potentially limits the ability to fully explain variability in IAF quality. We expect there will be differences among internal auditor’s decisions and processes, and the outputs of the IAF, such as their findings, are also likely to differ.³

With a lack of clear direction or theory of IAF quality, we take an interdisciplinary approach and draw from literatures within multiple business and organizational psychology disciplines that conceptualise quality of services and tasks. Specifically, the following disciplines are reviewed: external audit, information systems; service quality; internal service quality; team performance and collective judgments. Each are briefly discussed below. The

² Lin et al. (2011) note their measures are based on both external audit standards and internal audit standards.

³ While high quality input factors should correlate with higher quality processes and outputs, this does not automatically follow. The same inputs could be associated with different processes, auditor judgments and decisions, and outputs; thereby, resulting in potentially different levels of IAF quality.

key insight from this review is that quality is a multi-dimensional construct and various parties to the task or service such as users and providers may judge quality differently.

The literature on external audit quality can be categorised into archival, judgment and decision making (JDM), and professional practice literature. Much of the archival external audit quality literature relies on DeAngelo's definition of external audit quality which suggests external audit quality is a function of the market's perception of (a) auditor competence and (b) auditor independence (DeAngelo, 1981, p. 186). Important here is the term 'market perception' which infers that external audit quality is not simply the function of auditor competence and independence but the markets perception of the auditor's reputation. A recent framework of external audit quality developed by Francis (2011) suggests external audit quality is affected at each unit of analysis within the framework which included: audit inputs, audit process, accounting firms, audit industry and audit markets, institutions, and economic consequences of audit outcomes. Currently key measures of audit quality are output and outcome based including discretionary accruals and financial restatements (Francis, 2011). Further, the perceptions of external audit quality varies between the multiple stakeholders (Peecher et al., 2013).

The basic premise of the JDM external audit quality literature is that the quality of external auditor judgments influences the quality of the external audit and as such treats auditor JDM quality as external audit quality (Peecher et al., 2007). This literature attempts to understand and evaluate external auditors' performance and judgments – how good is their performance, how good are their judgments, and how can these be enhanced to improve the external audit process (Libby and Luft, 1993; Nelson and Tan, 2005; Solomon and Trotman, 2003).

A number of professional frameworks on external audit quality also exist. The International Auditing and Assurance Standards Board (IAASB 2011) views audit quality in

terms of inputs, outputs and contextual dimensions. The Financial Reporting Council (UKFRC) audit quality framework identifies the following five key drivers of external audit quality: the culture within an audit firm; the skills and personal qualities of auditors; the effectiveness of the audit process; the reliability and usefulness of audit reporting; and factors outside the control of auditors affecting audit quality (UKFRC 2008). Within the accounting firms, there is a similar view to external audit quality. For example, KPMG (2008) view external audit quality as a combination between their seven drivers of audit quality (mapped to the FRC framework) and their people: individual auditor's commitment, professional judgment, skepticism and technical competence. Overall, the diversity in views of external audit quality drivers demonstrates that quality even within a sub-discipline is not uni-dimensional.⁴

Information system literature views the quality of information as contextual with the measurement of quality dependent on the intended use of the information (Stvilia et al., 2007). Information users make decisions in different environments, and use information in different contexts and for different purposes (e.g. Jackson et al., 1997; Neely and Cook, 2011; Stvilia et al., 2007; Tayi and Ballou, 1998; Wang and Strong, 1996). The quality of data and information produced by information systems is generally measured by the following seven criteria: accuracy, timeliness, precision, reliability, currency, completeness and relevance (Neely and Cook, 2011; Wang and Strong, 1996). Overall, this literature generally contends that information quality is multi-dimensional (Neely and Cook, 2011; Wang and Strong, 1996).

⁴ While internal and external audit have a number of similarities, such as audit techniques (Abdolmohammadi, 2012), differences between the two functions limit the use of external audit quality measures to measure the quality of the IAF. For example: there are differences in the principle party they serve (Sarens et al., 2009); respective audit standards and required conformance (Abdolmohammadi, 2012); internal audit has a wider role and provides value added activities (Stefaniak et al., 2012); and the outputs of the audits also differ (external audit reports are largely homogenous with standard wording). Further, many external audit quality measures, such as those outlined by Francis (2011) (discretionary accruals, material misstatements and external audit failure) do not apply to internal audit.

The service marketing literature focuses on client perception of quality as objective measures are unavailable and because quality for one service user may be different to another user (Brady and Cronin, 2001; Johnson, 1995; Mills and Ungson, 2001; Oliver, 1993; Parasuraman et al., 1985). Two competing service quality perspectives have been established providing the basis for much of the proceeding service quality research (Brady and Cronin, 2001). Both models are based on the disconfirmation paradigm (Cardozo, 1965; Oliver, 1980, 1993) which is the gap between a customer's expectation of service quality and the level of quality received. Parasuraman et al.'s (1988) SERVQUAL model identifies five attributes of service quality: reliability, responsiveness, empathy, assurances and tangibles. Whereas, Gronroos (1984) identifies two dimensions of service quality: technical quality (output from, and outcome of, the service) and functional quality (service interactions and delivery). Brady and Cronin (2001) identify that the two perspectives are related and suggest that customer perceptions of service quality are formed via the evaluation of three factors: outcome, interaction, and environmental quality – each having multiple sub-dimensions. Overall, this literature identifies that quality is multi-dimensional and consists of both technical and service dimensions.

Internal service quality is the quality of service provided to (from) other departments within the organization (Brandon-Jones and Silvestro, 2010; Schneider et al., 1998) and its measurement has commonly followed the service quality literature. However, transferring service quality measures (developed for external customers) to internal service quality (developed for internal customers) has issues, for example, internal customers generally have little choice over their service provider (Brandon-Jones and Silvestro, 2010; Lusch et al., 1992). Bruhn (2003) conceptualised a generic measure of internal service quality into twelve dimensions which are abstracted into three core dimensions: inputs, service interaction and outcomes.

In the organizational psychology literature, the assessment of team/group performance is dominated by a systems approach model that characterises performance quality via three dimensions: inputs, processes and outputs. Early research in this area argued the systems approach was a linear progression; that is, greater input quality led to better quality processes, which create higher quality outputs (and in turn lead to high quality outcomes) (e.g. Hackman, 1987; McGrath, 1984; Steiner, 1972). However, recent research in this area documents that these three dimensions are linked but not causal as there are interactions between the three dimensions, outputs ‘loop back’ to inform inputs and processes, inputs can be of high quality but the other dimensions are not automatically of high quality, and emergent states develop over the life of the team which interact with the three dimensions (De Dreu and Weingart, 2003; Dirks, 1999; Ilgen et al., 2005; Taggar, 2002). Hart (1985) provided three interrelated criteria for the quality assessment of collective judgments and decisions of teams. The criteria were the process by which the decision was made; the content of the decision; and the outcome of the decision. Hart suggested that to assess quality, any assessment must successfully blend these three criteria.

Core Insights into the Concept of Quality

While it is apparent that quality is assessed differently in each of the above literatures, two fundamental insights are evident and consistent across the disciplines. First, quality is contextual and differs according to the perspective of the user, therefore quality is regarded as a user perspective, where different users may judge quality differently. Second, quality is multi-dimensional consisting of a range of dimensions including inputs, processes, outputs, outcomes and contextual/environmental factors, each with multiple determinant factors. This multi-dimensional aspect contrasts with the focus of IAF quality research to date which has focused on a single stakeholder and limited to an input dimension of quality. We discuss each

of these five dimensions briefly below highlighting how the dimension can influence quality and identifying why quality measurement should not be restricted to any single dimension.

Inputs to a service or task include the personal attributes of the provider and the structural elements of the function, including the function's objectives and resources (IAASB 2011; Johnson, 1995; West and Anderson, 1996). Input factors can explain a large proportion of variation in quality (West and Anderson, 1996) and inputs have been shown to be important in external auditor assessments of IAF quality (Gramling et al., 2004). However, there is not always a direct relationship between input quality and output quality (ICEAW Chinander and Schweitzer, 2003, p. 243; 2010). Despite this, inputs are often used in quality measures as they are easier to measure and more readily available (therefore less costly) than process and output information (Chinander and Schweitzer, 2003; ICEAW 2010; O'Reilly, 1982).

Processes are the actions, steps, conduct, behaviours and JDM involved in how the provider of a service/task achieves their output (Bonner, 2008; Francis, 2011; Johnson, 1995; Lampe and Sutton, 1994; Sutton, 1993). Processes are an important part of an assessment of quality as the quality of outputs and outcomes can be affected by the quality of processes. For example, outputs can be of low quality as there are a number of steps in a judgment process, and judgments by highly competent individuals are vulnerable to systematic traps and biases (KPMG et al., 2012). The external audit literature strongly focuses on judgments and decisions as part of quality; Bell et al. (2005) suggest judgments are the very essence of external auditing affecting quality through the entire external audit. Processes are likely to be important in IAF users' assessments as internal auditing requires various professional judgments (Abdolmohammadi, 2012) and fieldwork quality is critical in IAF assurance activities (Lin et al., 2011).

Outputs are what is produced as a result of the service/task and are the reason for the existence of teams, functions or services (Bonner, 2008, pp. 26-28; Ilgen, 1999; Johnson, 1995). Audit firms often judge a professional's judgments based on their output, and third parties who rely on the work of others generally are most concerned whether the information provider gives the 'correct answer' (Bonner, 2008). IAF users are expected to be concerned with output as the internal audit report is the key deliverable of the IAF and research has shown that to rely on IAF information, the information must be reliable, timely, relevant and effectively communicated (Burton et al., 2012).

Outcomes are the state of nature, events, or increased confidence, achieved based on outputs of the service or task (Bonner, 2008, p. 26; Sutton and Lampe, 1991). Outcome quality is largely a perceptual construct and is typically unobservable; however outcomes are a determinant in an assessment of service quality (Czepiel et al., 1985). Assessment of quality via outcomes is often driven by practical reasons (Ilgen et al., 2005). However, the JDM external audit quality literature identifies issues with measuring quality via outcomes: often there is no right answer, or timely outcome, for a task; quality outcomes can be achieved by poor processes, and poor outcomes can occur even when there has been quality processes; and actual outcomes often cannot be exclusively associated to a task (Bonner, 2008, pp. 27-28; Davis and Solomon, 1989; Peecher et al., 2013). Outcomes may be used as indications of IAF quality as the core purpose of the IAF is to provide value to their users.

Contextual factors are factors that may influence the quality of a service, often outside the control of the service provider. Contextual factors can affect a decision maker and therefore need to be understood if one is to assess their decisions (Ashton, 1990; Gibbins and Newton, 1994). A number of contextual factors have been found to affect external auditor assessment and reliance on IAF work, for example: audit committee quality (Cohen et al., 2007; Krishnamoorthy and Maletta, 2008), inherent risk (Glover et al., 2008; Maletta, 1993;

Maletta and Kida, 1993), and corporate governance quality (Desai et al., 2010). The impact of these contextual factors on external auditor reliance suggests that by extension it is likely other governance stakeholders would consider and include contextual factors in their assessment of IAF quality.

Based on the preceding argument, where quality is affected at each dimension and therefore each dimension is important (Ilgen et al., 2005; Turnock and Handler, 1997; West and Anderson, 1996) we propose a theoretical framework of IAF quality incorporating each of the above five important dimensions. The framework (Figure 1) depicts IAF quality consisting of four dimensions: inputs, processes, outputs, and outcomes, each of which can be impacted by a fifth dimension, contextual factors.

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While a range of input, process, output, outcome and contextual factors may all be possible information cues to a stakeholder on IAF quality, cue reduction is natural (Einhorn and Hogarth, 1981). Psychology and accounting research highlights that people have difficulty combining multiple pieces of information to make judgments; therefore, people simplify their judgments by focusing, and weighting, on subsets of information (Ashton, 1974; Bazerman et al., 2002; Libby, 1981; Shanteau, 1992; Tversky and Kahneman, 1974). As such, RQ1 is designed to identify the main information cues used by the IAF stakeholders in their judgment of IAF quality and under which of the five dimensions these fall.

RQ1: What are the main information cues used by IAF stakeholders to judge IAF quality?

Prior research identifies that different corporate governance stakeholders have different needs and demands of the IAF (Abbott et al., 2010), that different governance actors will often have different perceptions of quality (Cohen et al., 2004) and judge quality differently

(Aguilera et al., 2008). While it is likely that each of the IAF stakeholder groups will share a common desire for a high quality IAF, with different uses of the IAF and different motivating factors, each of the stakeholders are likely to view and assess IAF quality differently. These differences may occur between the multiple users (such as the audit committee, senior management and external auditors) and/or between users and the service provider. Therefore, the second research question addresses whether different IAF stakeholders view and judge IAF quality differently to one another and differently to that of the external auditor.

RQ2: Do different IAF stakeholders judge IAF quality differently?

METHOD

The objective of this study is to provide insights into IAF quality from key IAF stakeholders. To gather these insights we chose an interview method as interviews allow a researcher to gain insights and understanding into issues and complexities of a phenomenon which are difficult to obtain via archival methods (Beasley et al., 2009; Gendron, 2009; Lillis, 1999; Radcliffe, 2010). We conducted 36 interviews with audit committee members and chairs, senior management and internal auditors to capture the information cues used in their judgments of IAF quality.

Of the 36 participants, 18 were ‘users’ of internal audit: nine audit committee members/chairs and nine senior managers (CFO’s and financial controllers); and 18 ‘providers’ of internal audit, including ten heads of in-house internal audit departments, and seven partners, and one director, of internal audit divisions from large accounting firms.⁵ The following abbreviations are used to identify participants: AC = audit committee member/chair; SM = senior manager; IA Head = heads of in-house internal audit departments; IA Partner = partners of internal audit divisions from large accounting firms.

⁵ In Australia, some accounting firms use the term director to indicate the level between manager and partner. This position does involve in-charge-responsibilities for clients. For convenience, all accounting firm participants are referred to as partners (IA Partners) in this paper.

----- INSERT TABLES 1 – 3 HERE -----

Participants were from large Australian publicly listed firms (listed on the Australian Securities Exchange (ASX));⁶ large accounting firms (including each of the Big 4 and one second tier firm) and one unlisted financial organization. Tables 1 – 3 provide demographic details of participants and their associated firms. Audit committee members and senior managers represent the ‘users’ of internal audit. CFOs and financial controllers were chosen as the senior management participants as the Auditor Director Roundtable (2007) found internal audit’s primary reporting relationship was to the audit committee, whilst their secondary reporting relationship was to the CFO and included financial controllers. These two users are also part of the key triangle of communication with the IAF (Abdolmohammadi et al., 2013). Both in-house internal audit and outsourced internal audit providers were chosen as participant groups to allow comparison between the service provider and the client (the ‘users’) (Gramling et al., 2004). Further, differences in the interpretations of IAF quality may occur between the two providers as in-house IAF departments and outsourced providers have different motivations and incentives, and there are differences in the nature of their relationships with clients (Desai et al., 2011; Glover et al., 2008).

The majority of participants (23) were acquired through personal or university-related contacts. Ten participants were identified through “snowball procedures” (Tremblay and Gendron, 2011). Two heads of in-house IAFs and one internal audit partner were attained through the assistance of the Institute of Internal Auditors (IIA) Australia.⁷ Non-response to requests solicited by the IIA and through the snowball procedure is unknown. Of the potential participants personally approached, only two declined to be interviewed as they were

⁶ 44% of the sample represented publicly listed firms ranked in the top 30 ASX companies by market capitalisation.

⁷ Further individuals identified by IIA Australia indicated willingness to participate in this study, however the number of participants used from this source was limited by the researcher due to potential bias of close affiliation with the internal audit professions leading body (Beasley et al., 2009).

overseas for extended periods of time during data collection; four others did not respond to our email request.

Consistent with similar research (e.g. Beasley et al., 2009; Cohen et al., 2002; Tremblay and Gendron, 2011) our sample contained some minor nuances. One senior manager had recently retired, one non Big 4 firm was included, one firm had very recently been delisted due to corporate merger firm, and finally one participant represented a large unlisted financial organization. However, despite these nuances, it is believed the insights from these participants added value to the study and should remain in the sample. These participants had the experience required to discuss IAF quality within large organizations, and the nature of the research questions were designed to examine the processes used by governance stakeholders to judge IAF quality, not to determine IAF quality within specific companies

Interviews were conducted between April and August 2012 in major Australian cities. The length of the interviews ranged from 44 to 81 minutes, with an approximate average of 54 minutes. All interviews were conducted face-to-face with one exception, which was conducted via telephone due to logistical limitations.⁸ Each of the interviews were conducted by the one researcher enabling consistency amongst interviews in the asking of questions and probing of relevant themes.

A standardised interview guide was used for all interviews to provide a consistent approach and coverage of themes in each interview (Beasley et al., 2009; Patton, 2002, p. 343). The interview guide was customised for each group of interviewees;⁹ and each interviewee was not asked all questions.¹⁰ The interview guide was reviewed by six

⁸ A similar approach was taken by Cohen et al. (2013) and Graham et al. (2005).

⁹ Only minor changes were made. The emphasis and themes of the questions were not changed; simply, questions were restructured for participants various positions such as 'providers' or 'users'.

¹⁰ Following Hirst and Koonce (1996), as the purpose of this study was to increase our understanding of IAF quality in practice, the benefit gained from exploring interviewee responses outweighed an attempt to limit the interviewee to the pre-established questions due to time constraints. Further, Radcliffe (2010) suggests using

academics within accounting and psychology disciplines for relevance, clarity and completeness (Cohen et al., 2010). Three pilot tests were also conducted which were not included in the subject pool. The research instrument evolved and was revised as necessary over the course of the interviews when new themes arose or when a theme was discovered revealing a need for deeper questioning and insights (Anderson and Lillis, 2011; Cohen et al., 2002; Gendron and Bédard, 2006; Hirst and Koonce, 1996).

Each interview began with measures to reduce participants' reluctance to freely provide their insights by drawing heavily on the approaches taken by Cohen et al. (2002), Gendron (2001, 2002), Gendron and Bédard (2006) and Hirst and Koonce (1996). First, we discussed the broad objective of our research, our interest in their experiences and the planned use of the data collected. Second, participants were assured of the anonymity of their answers for themselves and their firm, and that their responses would not be shared with anyone else from their organization. Third, the researcher highlighted the benefits of recording the interview and asked for participant's permission to allow the interview to be recorded.¹¹ Fourth, participants were informed they would be given the opportunity to verify the interview transcript to remain comfortable with what they had said after the fact.¹² These approaches help to build trustworthiness of the interviewee (Tremblay and Gendron, 2011) and limit response bias (Gendron, 2002). This process was followed by initial questions asking factual background information on participants' experience, demographics and their organization to help set the scene for the remainder of the interview and to have participants ease into the

less structure in semi-structured interviews to pursue important and interesting insights, so as to understand the meaning of these insights.

¹¹ With permission, all but two interviews were recorded and signed consent was acquired. For the two interviews not recorded, the 'memory-transcript' method was used; that is, key notes were taken during the interview and detailed notes were made immediately following the interview (Gendron, 2001, 2002).

¹² Eleven of the 36 participants accepted this offer. Only minor modifications were made to the transcripts by three interviewees. Four participants did not make any changes, whilst three participants did not reply. One participant requested to be contacted if any of their quotes were to be used to verify they were used in context.

recorded interview, before proceeding to questions based on the research questions (Hirst and Koonce, 1996).

Neither a definition of IAF quality or attributes of IAF quality were discussed by the researcher due to the exploratory nature of the research and the potential of leading respondents to answers (Schroeder et al., 1986) or responses being artefacts of the interview process (Malina and Selto, 2001). Also, when asking probing questions the researcher refrained from introducing or highlighting potential quality determinants therefore allowing respondents to provide responses from their own experiences (Anderson and Lillis, 2011; Carcello et al., 1992; Gendron, 2002; Schroeder et al., 1986). Following Hirst and Koonce (1996), Beasley, et al. (2009) and Cohen et al. (2010; 2002) when interviewee responses indicated an important path, this path was pursued before returning to the interview guide. If a participants response answered a forthcoming question, the question was not asked or rephrased in a way to gain deeper insight (McCracken et al., 2008).

Interview questions were derived from the literature on IAF quality and the interdisciplinary review of disciplines who have conceptualised quality of services and tasks, the extant internal audit literature, professional literature (including relevant internal and external audit standards, professional body and institution publications) and a focus group conducted in the developmental stage of this research with five internal auditors. Broad and critical questions of this study were asked early in the interview, responding to suggestions by Hermanson et al. (2012) for researchers to ask broad questions early to give participants the opportunity to delve deeply into the issues under study. Questions were designed to focus on participant experiences and not their opinions (Cohen et al., 2010); to overcome perceptual bias in participant responses, and to be able to draw valid contextual information from participants, it has been suggested that an interviewer must ask respondents about experiences with a certain phenomenon and not simply opinions or insights (Gibbins and Qu,

2005). Therefore, the main questions of the interview guide were anchored around participants' experiences rather than asking directly about how they make judgments of IAF quality or the determinants of a quality IAF.¹³ This protocol of anchoring participants' responses on their experiences is often used in qualitative accounting studies employing data collection methods, such as interviews and experimental questionnaires (for example Cohen et al., 2010; Gibbins et al., 2005; Gibbins et al., 2007; Gibbins and Qu, 2005; Gibbins and Trotman, 2002; McCracken et al., 2008; Nelson et al., 2002; Rennie et al., 2010).

Prior to each interview, available documents produced by the interviewee's organization were reviewed including annual reports, corporate governance statements and policies, audit committee and internal audit charters, risk management policies, the organization's website, and any relevant recent press. This enables the interviewer to pursue salient areas that arise in the interview with potential background knowledge and to contextualise and understand responses gathered during fieldwork.

As data collection began with a theoretical framework, a preliminary coding scheme was developed reflecting this framework and was consistent with questions in the interview guide. Initial coding was conducted during the fieldwork period. All transcripts were reviewed and coded in line with an established code book to identify key themes in the data (Gendron, 2002; McCracken et al., 2008). Each transcript was coded by one of the authors and a graduate research assistant who was independent of the research and the research questions. The two coders achieved reliability of 86%, indicating a high level of inter-coder reliability (Cohen et al., 2010; Cohen et al., 2013). Any disagreements between coders were

¹³ Specific experiences/examples were of the participant's choice. Prior to the commencement of the interview questions, participants were informed that they would be asked for examples and that these examples could be experiences from their current organization which they represent or a previous organization. Examples from previous organization were acceptable as the company itself was not influential to the research questions or results, and the objective was not to ascertain the quality of the internal audit for a specific company. However, participants were requested to choose examples, where possible, where they had the same or similar role. The reason for this was many audit committee members were former external audit partners or CFO's.

discussed and mutually resolved. Where mutual agreement could not be obtained a final decision was made by the other author which was necessary for only one passage of data.

FINDINGS

RQ1 addresses what are the main information cues used by IAF stakeholders to judge IAF quality. The information cues used by the IAF stakeholders to judge IAF quality are summarised below in Table 4. The information cues used are separated into primary information cues and secondary information cues where this weighting was identified in participant responses. The four different groups used either, or a combination of, the process, output or outcome dimensions comprised in the IAF quality framework. Specifically, ACs judge IAF quality via outputs; SMs predominantly via outcomes, and secondarily via outputs. Within the provider groups, IA Heads judge IAF quality via processes; and, IA Partners judge via both outputs and outcomes. Figure 2 provides an overview of different dimensions used in the judgment of IAF quality by the four stakeholder groups. External auditors have been included in the figure to indicate that their judgment of IAF quality is different to other IAF stakeholders (based on previous research). RQ2 investigates if the different IAF stakeholder groups judge IAF quality differently. As can be identified from Figure 2 and the analysis, participants used cues from different dimensions in the judgment of IAF quality. Below we discuss these judgments for the four groups.

----- INSERT TABLE 4 HERE -----

----- INSERT FIGURE 2 HERE -----

Audit Committee

A consistent sentiment among AC participants is that they observe little about how an audit is performed. As a result, audit committee members can only rely on what information is available to them for making their judgment of IAF quality. The information used by ACs

to judge the quality of the IAF clearly fell under two distinct cues. First the outputs of the IAF in the form of IAF reports (reports), and second, the views held by other IAF stakeholders as to the quality of the IAF.

Each AC participant indicated the predominant cue used in their judgement of IAF quality is IAF outputs. This includes the quality and substance of reports, the quality of findings, and any presentation of findings to the audit committee. Thus, the quality of reports are a significant cue for ACs to assess IAF quality. Reports contain the IAF's findings and the quality of these findings were specified by ACs as the strongest indicator of IAF quality and the predominant information cue used within IAF reports. For example, in discussing why an audit was of high quality the following AC illustrates the importance of findings on quality assessments:

You know from the reports that come to you ... as to the quality of the findings. I'd be very worried if [the IAF] found nothing, continually found nothing on most assignments. And sometimes the findings can be pretty assertoric you know - and so you say 'yeah he's digging, he understands what that is about'. If I kept getting reports that pretty much confirmed 'no problems, no problems, no problems, I thank management for their cooperation', I would be pretty nervous. But I know that you occasionally get that hard-hitting report and then you get other reports that come up with findings that would indicate yeah the guy is doing his job. So it is an overall feeling of quality rather than program by program, job by job. (AC)

This quote identifies the importance of reports but also alludes that an IAF quality judgment is made over a collection of IAF reports, not just a single report.

The substance of reports influences the confidence of the audit committee that an IAF is of an acceptable level of quality. For instance, an AC referred to the lack of confidence he received from the IAF at a former company where he was the Audit Committee Chairman:

So we had an internal audit report on [the recording of inventory] which just did not address the issues. It just sort of skated over it ... it did not address the issues and certainly didn't point to how we could actually gain any confidence that we were accounting for the [inventory]. ... So just doing a report on the documentation or the end of the process, that wasn't going to do it. (AC)

The AC providing this quote emphasized that the report gave him/her no confidence in the internal auditor, or that the internal auditor was performing a quality role. The AC then compared this reporting to his/her current AC position where the IAF produces substantive reports focusing on the risks and implications for the audit committee and the business. This style of reporting was suggested to provide the audit committee greater comfort and an indication of higher IAF quality.

The IAF's prioritisation and weighting of audit findings and business risks in reports is also an indication to the ACs of IAF quality. Many ACs commented on the process of how they look at these rankings and make a judgment on the quality of the IAF according to how they as an AC member would have prioritised the findings or risks. When ACs do not agree with the IAF's categorisation, the ACs have trouble viewing the IAF as high quality, as implied in the following excerpts:

Probably the single best index for me is that, you know characteristically they will categorise their findings in probably three boxes... this is high risk, this is moderate, this is relatively low. If their judgement about categorisation consistently resonates with me, then I have a high degree of confidence in the audit team. But if they rate something that is moderate which I actually think is a very high risk, or they start picking up routine ... and turn that into a high, except around maybe some very critical function like the Treasury function, then I say that you are not showing good judgement, that is unrealistic. ... So it's that consistency in the judgement. (AC)

I read reports thoroughly and I look at the soundness of the reasoning. Where you get reports, you have effectively got to rely on the facts as stated in the reports. So what thinking goes into how you differentiate between what is a major risk, what is not so great, what is important – that would probably be the major way of assessing. (AC)

This last AC continued:

I always have the internal auditor present at the Audit Committee meeting where a report is presented. ... So the combination of looking at the detail, and the logic, and the recommendation, that comes out of it [the report] combined with what effectively is a cross examination of the person or the people involved ... it has got to stand up. (AC)

This last quote identifies two ways this AC uses reports as information cues relating to the quality of the IAF. First, the report itself and second the presentation of the report's findings. This process was mentioned by many ACs who indicated they make part of their judgment of the IAF based on the presentation of the findings (report) by internal auditors and how internal auditors conduct themselves in audit committee meetings. Illustrating this point is a quote by one AC, who questioned the Chief Internal Auditor at a company where the AC had just taken on the role of Audit Committee Chairman. Along with major risks associated with the specific industry, this company has very large risks associated with previous employee fatalities (due to poor maintenance of equipment) and business interruptions (through being unable to meet capacity requirements). The internal auditor's response to the AC's question gave the AC a clear indication of the quality of this internal auditor:

I asked the auditor what was the major risk within the organization that he thought the Board should be on top of. And this person turned around, and he said, 'you know your payroll system, there's not a manual check of some of the changes made to it' or something or other. And I just fell off my chair and had to pick myself up and resuscitate myself. Because ... it's at the edge compared to what we had in the business, and there was a total disconnect. So did I have any confidence in that person doing a proper audit of the organization? Absolutely not. Did it give me any confidence in signing of the accounts that he had done the right work? Absolutely not. ... if you have a weak internal audit, I don't think you can actually sign off. (AC)

The second information cue ACs consider in their judgment of IAF quality is the perceptions of other IAF stakeholders. ACs suggested that beyond judgment of IAF reports, they incorporate the view of IAF quality from a number of their associates. These associates include the external auditor, the CEO and divisional management. For example:

When we were doing an external audit, we were asking them 'how have they found internal audit?' ... We ask the CEO ... and we also get a good view by talking to business unit heads. (AC)

This quote implies the ACs are proactive and discuss quality of the IAF with a number of associates. Other ACs only discuss receiving the view from a single stakeholder, such as the external auditor:

It is part of our practice in any of the committees I sit on, that we will grill the external auditor about their view of the quality of [the] internal audit function; to what extent they were willing to place reliance on internal audit (and the finance function). So you do get a crosscheck and you are also using internal audit and the finance function to check the ambitions of your external auditor.
(AC)

In contrast, the following AC, while suggesting it is a strong business practice to understand others' views of IAF quality, suggests that it is not common in his/her experience:

The Managing Director does a performance review of the internal auditor which he shares with the Audit Committee on at least an annual basis. And the Audit Committee ... provides its views on the effectiveness of the internal auditor and internal audit function to the Managing Director; so it's an interactive session. It's the only Board where we do that, and I sit on eight; and I think that is probably the most mature in terms of having gone to that extent.
(AC)

Related to using the views of others in the assessment of IAF quality, some ACs suggest that management's acceptance of the IAF and IAF recommendations is an adverse indicator they use in their judgment of IAF quality. Again, noting how ACs have limited views of how each audit is conducted (the audit process) an AC suggested:

If you hear back that either management refuses to respond in a timely way to recommendations, or rejects a number of the recommendations and you get stuck with what looks like a lot of compromises, that tends to be the evidence that says this isn't going well. (AC)

Senior Management

SMs use two main information cues to judge IAF quality. The predominant information cue is the value created by the IAF. Value is derived from how the IAF has helped to improve the business, and is an outcome driven cue in judgment of IAF quality. Many SMs also consider the quality of IAF outputs, particularly findings and recommendations, as a

secondary information cue to IAF quality. The following quote from a SM suggests that an audit is not of low quality just because there are no major issues found, but they did judge the quality of a recent audit on the value and insight provided:

You can't really judge the quality of audit on recommendations because if you have a fantastic process and there are no recommendations, you can't say that wasn't a good audit. But there was just more value-add in terms of the issues that they raised and evidence of the recommendations at work. ... It just added value to our system and the way people manage the processes. And it's very practical too. (SM)

Similarly, another SM suggests that the IAF is judged on the value created, not merely on coming up with simple findings:

Specifically what they're going to be judged on in terms of performance ... it's not a matter of saying 'well yeah we've found a heap of non-compliant things' ... well that's a given, you're going to do that, it's part of your job. But where can you add value to the business as a consequence of conducting your audit; you know, how will the business be better as a result of that audit having been conducted. (SM)

This quote suggests management perceive value when internal audit brings insight to the organization that will improve business systems and performance. Another SM indicates they judge the quality of the IAF via the value that is produced, suggesting:

They [internal audit] need to look at the genuine issues and how they can improve the business. Business improvement is the key. I'm looking that they actually deliver insight to help improve the business, not just a bunch of little problems they have found. Just providing a list of small things that are really not going to improve anything, you know when they just try to find things to prove they can, or, little things that anyone could find, what are they adding to the business? But if you [internal audit] give me something that will save us, something we didn't know – "Wow. Great!" – That's when I'd see it as a quality audit. (SM)

This quote highlights how this SM views an IAF as being of high quality when the IAF produces findings that management are unaware of and that can really benefit the business.

This quote also suggests that value does not occur when the IAF simply identifies a number of non-compliant issues or issues that are trivial. Many SMs identified that low quality audits

are caused by an IAF adopting a ‘tick-the-box’ or ‘tick-and-flick’ audit approach. That is, those audits which are just looking at whether an action was completed or not (such as compliance with internal policies and procedures). For example:

Basically, the audit lacked in its thoroughness. It was a more cursory, tick-the-box audit. It didn’t get to the important detail of what we really needed. (SM)

It’s a question of whether the internal auditor ... whether they are just trying to tick boxes or whether they are really trying to add value. (SM)

Many SMs provided examples of high quality audits emphasising the value produced by the IAF. For example, the following SM indicates that he/she made a judgment of IAF quality via the value produced and resulting outcomes that the IAF helped the business achieve; discussing their experience at a previous company:

The internal audit manager ... took a very strategic view, and a very strong risk management view, and was actually responsible for driving a significant improvement in project management activities right across [Organization XYZ] as a means of improving cross functional/cross divisional communication on large projects which had significant financial risk. And my view would be that particular activity saved [Organization XYZ] many millions of dollars over quite a short period, over a 2 to 5 year period. (SM)

SMs also provided discussion on some output factors of the IAF that influence their judgment of IAF quality. First, SMs indicated that recommendations provided by the IAF are influential to their view of quality and reliance on the IAF work. For example, an SM stated:

What would stop me relying on recommendations of the actions would be overkill. One of my criticisms of internal audit and risk officers in organizations, if I can be crass, it’s the cover your ass syndrome. It’s ‘if I’m not sure, I want to cover my ass, put it in writing, so then I can point and say I told you if you’d done all those procedures you would have been safe’. (SM)

Secondly, SMs suggest the quality of the draft reports they are provided at the closeout stage of the audit provide an indication of the quality of the IAF and the potential value from the audit. One SM provided the following comment:

... I'm having I think version number five or six at the moment, and it will be version number seven before it will get to the audit and risk committee. And the first version when I received it, we were trying to read it and we didn't understand what they were trying to tell us. It was like a copy of a template taken from, I would call it a milk bar business, with some charts and whatever and we were just sitting there thinking what are they trying, what are they telling us? (SM)

The practicality of findings and recommendations was often raised by SMs as an indicator of the IAF's quality with SMs describing this as auditing with common sense.

IA Heads

IA Heads' judgment of IAF quality was based on IAF processes. This group employs a notion of 'completeness' as their information cue in IAF quality assessment. Specifically, IA Heads look at how the IAF arrives at their findings to identify the quality of those findings and the audit. Hence, IA Heads' information cues for judging IAF quality are largely based on the soundness of the processes performed to achieve their output. To identify completeness, most IA Heads indicated they ask a series of questions and if they are satisfied with responses, this indicates to them a high level of quality. As one IA Head explains:

I step back at the end and ask the questions: how have we got to that conclusion? What have we done? And have we tried this, and what about this? (IA Head)

Many IA Heads suggest that often their assessment on the completeness of the audit is based on their intuition. The following IA Head clearly articulates their use of intuition in assessing completeness:

Probably if I have had an audit where I just don't feel we have got to the bottom of something. That could be something where you are using quite a standard practice or a process – a payables or expense or something – and maybe the results come out and everything looks satisfactory, but I may be left with a feeling of have we really turned over the stones with this one ... just auditors intuition that we might not have got to the bottom of something. (IA Head)

IA Heads indicated they also make judgments via the completeness of processes including the appropriateness of the audit scope and the evidence to support findings:

Quality would be the scope of what they do and how well is it aligned to the risks in the business. ... So I suppose that's the scope, and the breadth, are they looking at the right things? Then you get into the quality of the work, how well have they done the work and how well have they documented it, and I guess you can only really do that by [reviewing the] documentation. (IA Head)

Interestingly while IA Heads clearly identified completeness as the key to judge IAF quality, they often recalled previous high quality audits as those that had provided value to the client, as the following quote illustrates:

But where at the end of it you come out with a result and can say, and management also say 'well we didn't know, that is terrific, that is exactly what we want you to do'. Those are the ones that I would remember as being quality and really making a difference. (IA Head)

Two IA Heads provided alternative information cues as most important to them for IAF quality judgments. One IA Head's cue is the competence of the internal auditor (an input attribute) and whether the audit is conducted in conformance to IIA standards. The other IA Head suggests their assessment, of IAF quality is orientated under a service professional view, indicating quality will be different for different users and that overall quality is meeting their most important stakeholder needs.

IA Partners

There were two main information cues used for an IA Partners' judgment of IAF quality. The first cue is the reports produced by their team (an output) and the second cue is the value internal audit provides to their clients (an outcome). IA Partners are also very mindful that in order to make a judgment of IAF quality, it is important to first understand the client's view of quality.

IA Partners recognise that reports are internal audits' deliverable product. These reports are what the client sees and are likely to be the basis of clients' quality judgments. Therefore, reports are considered very important. The following IA Partner's perspective elaborates on the importance of reports to IA Partners in assessing IAF quality:

Often the clients, they don't see, you know they don't really see the testing so their judgment of quality is on what does the output of the report look like. Is it well written, concise, does it convey the issues properly? And again, that sort of, for internal audit that is your deliverable. That is the quality. And what's that report look like, what sort of value does it give the client? (IA Partner)

A noticeable feature of this quote is the emergence of the concept of value, and the value that a client receives from an audit report. Another IA Partner links outputs to quality and value, as the output is the deliverable:

I often say to people: if you are selling a car, you don't see car adverts showing you pictures of the engine. What they show you is this beautiful car driving down a winding road in the Alps, and it looks fantastic, and wind through the hair. It's all about the final product and how it makes you feel and that sort of stuff. You know, they don't pick apart the engine and show how everything connects together and all that sort of stuff. And often I think internal audit can get a bit stuck in that sort of internal imagination aspects of it. I still think at the end of the day, a lot of it is, what value are you giving? And value is different to different people, so you have to define that. (IA Partner)

Reports are also used as an information cue to IAF quality as they are indicative of performance. The following quote is an example provided by an IA Partner who judged an audit to be of low quality based on their view of the reports quality; the quote highlights the consumer perspective taken by IA Partners to reports and the quality of the IAF, a consistent theme emerging within this group:

That you can actually pick up the report and understand what the issue is would be an indicator of high quality. Where there is enough, where it tells a story, the actual findings that you're detailing actually provide enough evidence for people to understand what the issue is. So for instance, I reviewed a report yesterday ... it was hard to understand from that finding that whether it was because [of a data issue] or whether the system itself had an issue. (IA Partner)

Another IA Partner elaborates on reports and client value for assessing IAF quality:

Low quality audits tend to be things where, and I'd say in the most part tend to manifest themselves in the execution and reporting. ... So you get your client criticising you by saying, 'I agree with your observation, but your implications or your recommendations I don't agree with; I don't think they are practical, commercial, there's no insight'. To me, that's when I think about a low quality engagement, we haven't given the client anything of value – that to me is low quality. (IA Partner)

Two insights into IAF quality information cues are provided in this quote, management's response and client value. This quote suggests that management's response to IAF reports (including findings and recommendations) is an indication of quality, as predominantly a negative reaction by management is caused by a low quality audit. When the IAF have performed to a high level of quality, management are very likely to address the finding or action the recommendation(s). The above quote, which reinforces the undertone of many previous quotes, links the quality of the IAF output with the value provided to the client. Most IA Partner participants justified their assessment of IAF reports based on the value the report will provide to the client. For example:

So when I think of what we've done with clients that [the audits'] were of high quality, we've tended to identify things that they weren't aware of. We've articulated really well. It's given them something to action to improve their business, to close control gaps, to improve business performance, that sort of thing. You know it has saved the company some money. That's what I would judge to be a high quality audit. (IA Partner)

Not only do IA Partners make a link between quality reports and value, but many IA Partners discussed value and quality interchangeably, suggesting the two are inextricably linked as implied by the following excerpt:

As a professional services firm, one of the key drivers for us is, is our client happy at the end of the day with what we have given them? So in theory, you could do a technically high quality audit and the client isn't particularly over the moon with the outcomes. Equally, there is a model where technically it's not the best and the client can still be very happy with the outputs. ... So in terms of what's a high quality, part of what I think is, is my client happy at the end of the day with the outcomes they've received? (IA Partner)

IA Partners consistently raised this sentiment of knowing and understanding both the client's expectations of the audit and their views of quality. IA Partners argue that client expectations must be taken into consideration when making judgments on quality. The following quote illustrates the common sentiment that IA Partners are cognisant that clients want different things from the audit:

The first thing you need to do is find what people mean by quality in internal audit engagements. And that comes down, I think, to understanding what different stakeholders want from that particular engagement. ... So the quality judgement comes down to understanding what each of those stakeholders would expect in terms of the outcomes and whether there is sufficient depth that goes into achieving those outcomes. (IA Partner)

DISCUSSION AND CONCLUSIONS

The concept of IAF quality has been largely examined exclusively via the viewpoint of the external auditor and with the IAFs role in relation to external financial reporting. Assessment of IAF quality in the literature has also been based on three input factors to the IAF prescribed for IAF quality within external audit standards. We expand on this base of knowledge by conducting 36 in-depth interviews with other key governance stakeholders, namely: audit committee members and chairs, senior managers and internal auditors (in-house and outsourced partners from accounting firms), to determine how these stakeholders make judgments of IAF quality. Broadening our knowledge to include multiple key IAF stakeholders is important as the IAF is a key component of an organizations corporate governance system (Anderson et al., 2012; Prawitt et al., 2009).

We develop a theoretical framework based on an inter-disciplinary review of business and organizational psychology disciplines with conceptualisations of quality for services and tasks. The framework contends IAF quality consists of five inter-related but non-causal dimensions, namely inputs, processes, outputs, outcomes and contextual factors. Based on

this framework, we find that each of the four IAF stakeholder groups use different information cues within different dimensions of the framework in making judgment on the quality of the IAF. Audit committee information cues focus on the output dimension; senior management predominantly use outcomes as their information cue, supplemented by outputs. The IA Heads information cue is based on the process dimension, whilst IA Partners use both outputs and outcomes as their information cues. These findings differ from that of an external auditor, whose information cues (established in prior literature) are based on factors within the input dimension. Overall, the insights reveal that quality is more complex than has been considered in previous internal audit literature and important corporate governance actors will judge IAF quality differently based on different information cues.

Stakeholders were expected to judge IAF quality differently as quality is contingent on stakeholder needs and objectives which differ across stakeholders (Aguilera et al., 2008; Cohen et al., 2004). Therefore, it is not surprising to find differences between the AC group and the SM group, and between these two user groups and the providers. However, interestingly, the providers' judgments were quite different. IA Partners appear to be more closely aligned in their judgments with the user groups than IA Heads. Potential reasons for these differences and the potential driving forces behind judgments of IAF quality are addressed below, where we consider the audit committee, senior management, IA Heads and IA Partners in turn.

The two information cues used by the AC are IAF reports and the other stakeholder views of IAF quality. Thus, ACs use both evaluation (reports) and search (views of others) strategies to judge IAF quality (Einhorn and Hogarth, 1981). Overall, the ACs contend that a quality IAF focuses on the key risks of the organization to attain strategic objectives of management and the audit committee. A quality internal audit is a comfort to the AC by not only adding value to their monitoring role of management but also provides insight into

improving the business. The ACs suggested that reports are the best indicator of whether there has been a focus on key risks and the attainment of objectives. Therefore, reports are the main information cue for the AC to judge the quality of the IAF. The degree of comfort with the quality of the IAF gained from reports is increased by face-to-face interactions and IAF presentations where the AC can confirm their judgement and increase their confidence in IAF quality, similar to findings by Gendron et al. (2004) where audit committees use meetings and presentations to establish the credibility of external auditors. The second information cue used by ACs is the view held by other IAF stakeholders including executive and departmental managers and the external auditor. This is an indirect cue used by the AC, but consistent with findings by Gendron and Bédard (2006) and Beasley et al. (2009) that audit committees use informal practices to help fulfil their obligations.

The two information cues used by SM participants to judge IAF quality are the value created by the IAF and the IAF outputs such as findings and recommendations. SMs view the IAF as a resource to help them with uncertainty about risks, provide insight to what management does not know, and to help make business improvements so that management can achieve their objectives. SMs see the internal audit as high quality when the audit creates value for the SM's role or the organization. The second information cue for SMs is the quality of findings and recommendations. SM's assess the quality of findings and recommendations as they are an indication of the value potentially forthcoming and they increase their confidence that value will be created. SM's do not see value in internal-compliance type audits and many suggested they do not see value in the IAF auditing financial reporting activities as the external auditors are doing this. SMs were adamant that quality and value is about strategic and operational risks. A number of SMs indicated they found it rare for the IAF to add value; therefore their perceptions and judgments are that the IAF is not of high quality.

IA Heads emphasis was on processes as they employ a notion of completeness as their main information cue used to judge the quality of an IAF. Completeness of the audit is used as it provides IA Heads with confidence that what they deliver to their clients will be valuable and enhance the business in a positive way. IA Heads clearly recognised that adding value is their ultimate objective and question what changes will occur as a result of the audit being conducted. The IA Heads' emphasis on the soundness and completeness of the audit engagement to create a quality audit shows signs that IA Heads are motivated to do the best for the organization and align with organizational objectives (Davis et al., 1997; Nicholson and Kiel, 2007). IA Head motivation may also be driven by their need to protect their own reputation and that of the IAF as a whole (Nicholson and Kiel, 2007) as completeness indicates that they have done everything in their power to conduct a quality audit.

IA Partners use two main information cues in their judgment of IAF quality, the reports produced and the value created for the client. IA Partners consider reports and value in their quality assessments as they recognise this is how clients will most likely make judgments of quality. Reports are considered according to how the recipient will receive value and how the report will be considered by the recipient. IA Partners indicated that they put themselves 'in the shoes of management' when judging reports, to ensure they meet client needs and objectives and do so in a positive manner. Reports are also reflective of team performance and so IA Partners use reports to monitor their own team. The second information cue for IA Partners is the value provided to the client. IA Partners determine the value to the client by assessing if the audit helped improve business performance, gain efficiencies and yield cost savings. Client happiness is also considered a key driver for IA Partners in conducting quality audits. When an internal audit is seen as providing value, it is a strong indication the audit was a quality internal audit. Value and quality are inextricably linked, with an interesting perspective that an audit can be of technically high quality but if it does not create value, or

the client is not happy, then the audit is of low quality. This value perspective is consistent with findings by McCracken et al. (2008) where external audit partners see their role as keeping the external audit client happy and being an advisor to management rather than a 'police officer'. In sum, IA Partners' judgements of IAF quality appear to be largely driven by a service-orientated and strategic perspective.

The findings of our study should be considered in light of certain limitations. Firstly, while the number of interviews in our sample is comparative or greater than recent governance studies it is small compared to archival and experimental research. Second, the participants of this study represent a non-random sample. Third, consistent with most previous interview research (see Cohen et al. 2013a for an exception) we did not attract a 'triad' of participants (an audit committee member, the CFO and the firm's internal auditor) from individual organizations. While our method increases the likelihood of candid discussion, it means we are unable to account for differences in IAF quality across firms. Future research may benefit from obtaining multiple participants from each firm to further examine the effect of differences due to the organization as opposed to the position.

We encourage future research on IAF quality based on findings within this study. An opportunity exists to use alternate research methods such as survey data or experiments, to corroborate our findings, particularly with a larger sample size. Experimental research can also examine under what conditions the dimensions of IAF quality are important and the strength of these dimensions in IAF quality assessments. Further, this research only identified the important dimensions not how to measure them. Based on this sample, our results indicate that IAF quality is more complex than established in prior literature. Using these findings and the IAF quality framework as a starting point, an opportunity exists to develop a comprehensive model of IAF quality extending IAF quality models (Desai et al., 2010; Krishnamoorthy, 2001) for external auditor assessment and reliance of the IAF.

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Table 1: Participant Demographics

Audit Committee (n = 9)			<i>n</i>	Percent	Mean	Min.	Max.
Position:	Chair		5	56			
	Member		4	44			
Qualifications:	Education level:	Bachelor	4	44			
		Master	2	22			
		Honours	1	11			
		Ph.D.	2	22			
	CA/CPA qualification		9	100			
Experience:	Prior experience as an internal auditor		0	0			
	Former Big-4 external audit partner		5	56			
	Number of audit committees currently serving ^a				3.7	1	8
	Number of audit committees previously served ^{a,b}				2.2	0	10+

Senior Management (n = 9)			<i>n</i>	Percent	Mean	Min.	Max.
Position:	CFO		5	56			
	Financial Controller		3	33			
	General Manager		1	11			
Qualifications:	Education level:	Bachelor	4	44			
		Master	2	22			
		MBA	3	33			
	CA/CPA qualification		8	89			
Experience:	Prior experience as an internal auditor		2	22			
	Professional experience in finance/ accounting (years)				20.9	8	41

Internal Audit Head (n = 10)			<i>n</i>	Percent	Mean	Min.	Max.
Position:	Head of Internal Audit		10	100			
Qualifications:	Education level:	Bachelor	7	70			
		Master	2	20			
		Honours	1	10			
	CA/CPA qualification		10	100			
Experience:	Internal audit experience (years)				16.2	2	29

Internal Audit Partner (n = 8)			<i>n</i>	Percent	Mean	Min.	Max.
Position:	Partner		7	88			
	Director		1	13			
Qualifications:	Education level:	Bachelor	8	100			
	CA/CPA qualification		8	100			
Experience:	Internal audit experience (years)				15.8	11	25

Notes:

^a Disclosed audit committee service including public and private organizations.

^b One participant reported their past service as '10+' audit committees; average was calculated on 10.

Table 2: Participant Industry

<i>(n = 36)</i> Industry Sector	Audit Committee		Senior Management		Internal Audit Head		Internal Audit Partner		Total	
	<i>n</i>	%	<i>n</i>	%	<i>n</i>	%	<i>n</i>	%	<i>n</i>	%
Financials	3	33	4	44	3	30	-	-	10	27.8
Industrials	4	44	2	22	0	0	-	-	6	16.7
Consumer Discretionary	1	11	1	11	2	20	-	-	4	11.1
Utilities	1	11	0	0	1	10	-	-	2	5.6
Consumer Staples	0	0	2	22	0	0	-	-	2	5.6
Materials	0	0	0	0	2	20	-	-	2	5.6
Energy	0	0	0	0	1	10	-	-	1	2.8
Health Care	0	0	0	0	1	10	-	-	1	2.8
Big 4	-	-	-	-	-	-	6	75	6	16.7
Non-Big 4	-	-	-	-	-	-	2	25	2	5.6
Total	9	100	9	100	10	100	8	100	36	100.00

Table 3: Participant Firm Size

(n = 27)^a

Market Capitalisation	Total Assets			Revenue							
	AC	SM	IA Head	AC	SM	IA Head					
\$0-999m	3	2	1	\$0-999m	1	2	0	\$0-999m	3	3	1
\$1b-9b	4	2	5	\$1b-9b	5	3	6	\$1b-9b	4	2	5
\$10b-49b	1	2	1	\$10b-49b	1	0	0	\$10b-49b	1	4	2
\$50b+	0	3	3	\$50b+	1	4	4	\$50b+	0	0	2
Average	4.4b	29.5b	36.5b	Average	7.9b	247.3b	110.0b	Average	2.9b	17.1b	21.1b

^a IA Partners not included in participant firm size. Data was also not available for the participant representing a non-listed financial organization.

Table 4: Information Cues Used to Judge IAF Quality

Stakeholder	Primary Information Cue(s)	Secondary Information Cue(s)
Audit Committee	IAF reports (output)	Quality views of other stakeholders (outcome) ^a
Senior Management	Value from the audit (outcome)	Findings and recommendations (output)
IA Heads	Completeness of the audit (process)	
IA Partners	IAF reports (output) Value provided to the client (outcome)	

^a While this information cue could be considered as an input to an audit committee's IAF judgment, it is an outcome of the IAF having been conducted.

Figure 1: Theoretical Framework of IAF Quality

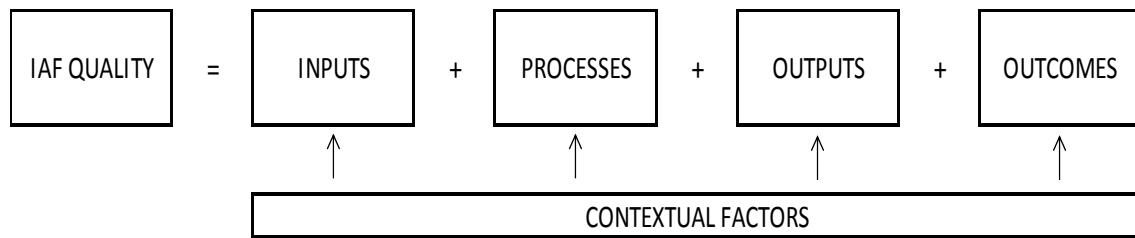


Figure 2: IAF Stakeholder Judgment Dimensions

	AC	SM	IA Head	IA Partner	External Auditor ^a
Input					
Process					
Output					
Outcome					

^a External auditor judgment dimension included for comparative purposes only.