



## **Request for Tender 2006 Review of the Audit Office of NSW**

### **Background to Request**

The *Public Finance and Audit Act 1983* (the Act) details the legal basis for the accounting and auditing arrangements for the NSW Public Sector. The public sector for the purposes of the Act includes the central revenue and spending powers of the State, the various government departments, statutory authorities and related bodies such as Area Health Services and State Owned Corporations.

Under section 48A of the Act, the Public Accounts Committee is obliged to appoint a Reviewer to conduct a review of the Auditor-General and his or her Office at least every three years. The review is to examine the auditing practices and standards of the Auditor-General and to determine whether the Auditor-General is complying with those practices and standards. The most recent such independent review was published by the Committee in November 2003.

The Committee is responsible for determining the terms and conditions for the Reviewer's appointment as well as being able to give the Reviewer binding directions.

Consistent with the practice for the most recent previous review in 2003, the Committee prepared for this review by consulting with all members of the NSW Parliament, agencies (through Ministers), the Audit Office, industry bodies, accounting firms and equivalent committees in other Australasian jurisdictions. The Committee also examined the agreed and partly agreed recommendations of the 2003 review which are included at Attachment B.

The Committee has used the results of this process to draw up the Terms of Reference for the review at Attachment A. These present opportunities to either improve the Audit Office's operations or resolve issues between the Audit Office and its stakeholders.

### **The Public Accounts Committee**

The Public Accounts Committee is established under the Act as a statutory committee of the New South Wales Parliament consisting of six members of the Legislative Assembly appointed for the duration of the four year Parliament. Under the Act, the Committee has a broad charter to review and report on the financial management and accountability matters across the NSW public sector on behalf of the Parliament.

The Committee's role includes a limited oversight role of the Auditor-General by virtue of:

- its power under section 57A of the Act of veto over the appointment of candidates to the position; and
- its power under section 48A of the Act to appoint a Reviewer to conduct an independent review of the Auditor-General.

The Committee is also empowered under the Act to examine any report of the Auditor-General and many of the Committee's recent reports have followed up issues raised by the Auditor-General. The Committee meets regularly with the current Auditor-General and attempts to improve knowledge of the Auditor-General's work within the Parliament by hosting briefing sessions for members on the Auditor-General's reports.

## The Auditor-General

The Auditor-General is the external auditor for the NSW public sector. The Auditor-General is appointed to office by the Governor for a non-renewable term of seven years following a selection process that, since 1992, has involved the Public Accounts Committee considering whether it would exercise its power of veto over a proposed appointment. The appointment of the current Auditor-General expires in September 2006.

## The Audit Office of NSW

The Audit Office of NSW consists of slightly more than 200 full time equivalent employees whose role is to provide the Auditor-General with the staff and resources to undertake his responsibilities. In 2005, amendments to the Act removed the Audit Office from Chapter 2 of the *Public Sector Employment and Management Act 2002*. The Auditor-General was thus empowered to determine the conditions and benefits of employment of members of the staff of the Audit Office and a new Audit Office Award commenced in January 2005. Combined with a restructure of the office, these arrangements were designed to improve flexibility in meeting audit work cycle needs, provide far more attractive career progression opportunities and improve the Office's ability to attract and retain high quality staff.

In some cases whole or part of audit engagements are contracted out to audit firms in the private sector. Private sector audit contractors are usually engaged on the basis of specialist skills required for specific audits or for audit engagements located in areas where it is more economical to contract out the whole audit process.

## Types of Public Sector Audits

Under Australian Auditing standards and in accordance with accepted audit practice, auditing in Australia, particularly public sector audits comprise the following:

- **Financial audits** where the audit report is a short form audit report in the form and content laid down in the standards. The Auditor-General also reports to Parliament on any issues arising from each of his financial report audits such as probity and financial prudence. The Audit Office of NSW conducts more than 450 of these audits annually.
- **Compliance audits** involving the examination of compliance with, for example, laws and regulations and policy directives of central agencies. There is no defined format for reporting on compliance audits. The Audit Office conducts around nine of these audits annually.

- **Performance audits** considering the economy, efficiency and effectiveness of agencies, particular functions of agencies or an activity across a number of agencies. The usual form of reporting is a long form report. Under the Australian auditing standards, the auditor must include in the report “a description of facts and findings that form the basis for the auditor’s opinion.” The standards also provide that the audit report on a performance audit must include “the objectives and scope of the audit report.” In 2004-05 the Audit Office adopted the International Organisation of Supreme Audit Institutions (INTOSAI) performance audit method. The Audit Office completed 15 performance audits in 2004-05.

## **The Reviewer**

The Act provides for the Audit Office to be reviewed by an independent Reviewer every three years. The Public Accounts Committee has the responsibility for the selection and appointment of the Reviewer, and for determining the terms and conditions of appointment and remuneration. When conducting the review process, the Reviewer must comply with any directions given by the Committee.

The Reviewer does not have an on-going role in the review of the Audit Office beyond the specific terms and conditions of the review.

## **Post Review Engagements**

The Public Accounts Committee does not have a firm policy position that prohibits post review engagements between the Auditor-General, the Reviewer, and business associates of the Reviewer. However, the Committee would expect that a reasonable period of time, such as twelve months, should elapse between engagements so as to demonstrate the independence of the review process and any subsequent engagements between the Reviewer and the Auditor-General. In addition, the Auditor-General has a policy of excluding any firm contracted to undertake the review from tendering for any Audit Office service for the duration of the review.

## **Confidentiality and the Review Process**

In addition to the client confidentiality provisions of the Code of Professional Conduct issued by the Professional Accounting Bodies, the Act has specific secrecy provisions that apply to the Auditor-General and staff and contractors of the Audit Office. Under section 48A, these conditions also apply to the Reviewer and support staff undertaking the review.

The general features of the review contract, however, will be subject to disclosure by the Committee 90 days after the award of the contract, as discussed in Premier’s Memorandum 2000-11.

## **Communication during the Review**

During the course of the review, the Reviewer is to inform the Public Accounts Committee, as appropriate, as to the progress of the review and the extent to which agreed target dates are being met. It is likely communication between the Public Accounts Committee and the Reviewer will take the form of liaison between the manager of the Committee and the Reviewer and could include briefings by the Reviewer to the Public Accounts Committee.

The Committee is open to discussion during the review process for the Reviewer to make comment and suggestion for additional matters to be included or modified or otherwise dealt with. Under the Act, the Committee has sole responsibility for the terms and conditions of the review.

## **Liaison with the Auditor-General**

During the course of the review, the Reviewer will be required to liaise with the Auditor-General and his staff in order to plan the conduct the review. The Public Accounts Committee anticipates the usual professional courtesies would be maintained between auditor and client and that the Reviewer will abide by any agreed approach to conducting the review, particularly the consultation periods required under the Act.

Potential bidders should be aware that the Audit Office will take a keen interest in the conduct of the review and planning should include sufficient time for reasonable requests for meetings.

## **The Reviewer's Report**

The reporting requirements for the review are fully detailed under section 48A of the Act, and are summarised for the purposes of this paper:

- The Reviewer is to report to the Auditor-General as to the results of the review and may include such other matters “as in the judgment of the Reviewer call for special notice.”
- Before making a report, the Reviewer must give the Auditor-General a summary of the findings and proposed recommendations at least 28 days before the Reviewer proposes to complete the report on the review.
- The Reviewer must include in the report any written submission or agreed summary of submissions and comments by the Auditor-General.
- The Reviewer's report:
  - may include such information as the Reviewer thinks desirable in relation to the subject of the review;

- must set out reasons for opinions expressed in the report; and
- may include such recommendations arising out of the review as the Reviewer thinks fit to make.

The Auditor-General is to forward the report of the Reviewer to the Public Accounts Committee within two months of the receipt of the report and the Chair of the Public Accounts Committee is to table the report in accordance with the usual Parliamentary practices. The report is not to be publicly released by any method, other than by tabling in the Parliament.

### **Timing of the Review**

The Committee would prefer that the Review be completed before the retirement of the current Auditor-General in September 2006.

### **Selection Criteria and Capability Statement**

The selection criteria for the tender are:

- The degree of understanding of the Committee's requirements demonstrated by the bidder.
- The appropriateness and quality of the method the bidder proposes to follow, including the approach to the task and the proposed schedule and timetable of activities.
- The bidder's relevant experience and familiarity with public sector auditing practices.
- The expertise and relevant experience of the people proposed to do the work.
- The total cost, including any significant additional use of the Parliament's personnel and facilities etc, a bid might require.

The Committee would wish to be assured staff nominated in the proposal would actually perform the majority of the work of the review. Any changes in the staff of the review team during the course of the review would require approval from the Public Accounts Committee prior to the change occurring.

The lowest or any proposal for the provision of services will not necessarily be accepted by the Committee.

### **Engagement**

The successful tenderer will be required to enter into terms of engagement, subject to negotiation, as specified in Appendix 1.

## Costs

In responding to this request, prospective bidders should indicate an appropriate break up of costs and a preferred pattern for progress payments, if required, covering work undertaken on a pro rata basis and reimbursement of any agreed outgoings.

## Quality Control

The Public Accounts Committee would expect the individual or firms undertaking the review would have in place and maintain appropriate quality control practices and procedures so as to demonstrate the highest level of competency and professional standards are maintained.

## Conflict of Interest

The Public Accounts Committee acknowledges that, during the course of the review, the appointed Reviewer, support staff and any associated firm face the potential of a conflict of interest in that they will have access to Audit Office records and working papers, including access to working papers of private sector firms under contract to the NSW Audit Office.

As an essential part of the tender process, all tenders must include details as to how the tenderer proposes to handle any conflict of interest situations.

## Contact

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## Lodgement of Tenders

The Public Accounts Committee will host a pre-tender briefing from 2.00 pm until 4.00 pm on Monday, 6 February 2005.

The briefing will include time for questions and prospective tenderers are encouraged to attend.

Tender documents, marked "**TENDER - REVIEW OF THE NEW SOUTH WALES AUDIT OFFICE**" should be lodged at the tender box at the front desk of the Legislative Assembly by 5.00 pm on Monday, 20 February 2006.

**ATTACHMENT A****TERMS OF REFERENCE****Scope**

The Reviewer will be required to assess and provide advice and recommendations about the auditing practices and standards of the Auditor-General and to determine whether the Auditor-General is complying with those practices and standards.

The purpose of the review is to determine whether the Auditor-General is performing his functions in accordance with the *Public Finance and Audit Act 1983* and professional and legal requirements. The review should also consider whether these functions are performed effectively and efficiently, in a way that and enhances the performance of the New South Wales public sector.

**Methodology:**

In conducting the review, the Reviewer should have regard to the Audit Office's strategic plans, policies, organisational structure, goals, operational management, corporate management and audit service provision.

**Particular issues**

The Reviewer should consider in particular:

**1. Auditing Function**

- a) Compliance with current professional standards and legal requirements in undertaking auditing of all types;
- b) Whether agencies' internal audit function has been adequately addressed in performing financial audits; and
- c) Audit Office efforts to prepare for the transition to new Australian equivalents to international financial reporting standards.

**2. Costs and Charges**

- a) Whether the Audit Office is providing value for money financial audit services in comparison with the services and fees of similar organisations; and
- b) Whether performance audits provide value for money by meeting their objectives and contributing to improved accountability by agencies within New South Wales.

**3. Planning**

- a) Whether the process of selecting topics for performance and compliance audits is based on robust methodology including a consideration of whole of government risk management and central agency priorities; and

- b) Whether the selection of agencies for inclusion in compliance audits is robust and based on a consideration of the particular risks of that agency.

#### **4. Management and Resources**

- a) Whether the Audit Office has adequate resources to conduct its functions; and
- b) Whether appropriately skilled staff are undertaking performance audits.

#### **5. Communication with Clients**

Effectiveness of communication with clients in particular in relation to:

- a) establishing a joint understanding of expected audit fees and potential variations;
- b) the scope of the performance and compliance programs and of individual audits within these programs; and
- c) provision of adequate notice of draft reports to Parliament for larger agencies to provide informed comment.

#### **6. Previous review**

The Reviewer should test the Audit Office's response to the agreed or partially agreed recommendations of the 2003 Review of the Audit Office which are included at Attachment B.

#### **7. General**

Any matter that may be referred to the Reviewer by the Committee during the course of the review.



**ATTACHMENT B****AGREED OR PARTLY AGREED RECOMMENDATIONS FROM 2003 REVIEW OF THE  
AUDIT OFFICE****1 Financial Audit****Recommendation 1 (Low Priority):**

The Audit Office should maintain their surveillance of the market in relation to changes in Audit Methodologies and automated technology solutions. Based on this surveillance, in line with standard government purchasing policy, it is recommended that on an annual basis, the Audit Office, formally document whether it is still appropriate to keep the current methodology and automated working papers or whether the market should be tested.

**Recommendation 3 (High Priority): (accepted in part)**

The Audit Office should reinforce with its staff the requirement to assess whether a client's Internal Audit function can be relied upon during the Financial Audit process. This should include a requirement that all audit files contain documentation setting out how any Agency's Internal Audit function has been assessed and the conclusions drawn by the Audit Team. The Audit Office should also ensure that Agencies are made fully aware through the Client Service Plan and through entrance meetings for all Financial Audits how its Internal Audit function will be used and what impact this has had on audit fees.

**2 Compliance Audit****Recommendation 11 (Medium Priority): (accepted in part)**

The Audit Office should develop and implement a continuous improvement cycle for its Compliance Audit Program to enable the efficiency and effectiveness of the program to be determined. This continuous improvement program should ensure that an area subject to a Compliance Audit is followed up and reviewed again in the following financial year. The results of this continuous improvement cycle should be reported to Parliament.

**Recommendation 12 (High Priority):**

The Audit Office should track the costs of each compliance review to assist in assessing cost / benefit. This would also assist in the planning for reviews by budgeting for proposed reviews to assess where resources would best be spent under the risk assessment framework.

**3 Performance Audit****Recommendation 18 (High Priority):**

Detailed context specific audit objectives be formulated and reported for each audit in lieu of generic objectives.

**Recommendation 19 (High Priority):**

The statement of audit objectives accurately reflect the aspects of the mandate dealt with in the audit report.

## 4 Costs and Charges

**Recommendation 57 (High Priority):**

Under consultation with the Public Accounts Committee, the Auditor-General should prepare a funding paper to be presented to the Department of Treasury seeking full funding for the costs of the Compliance and Performance Audit Programs.

## 5 Outsourcing

**Recommendation 64 (High Priority): (accepted in part)**

It should be required that a formal assessment of the outsourced providers work is undertaken by the completing of the "Contract Audit Agent Annual Performance Evaluation" and the "Client Feedback on Performance by Contract Audit Agents" each financial year at the completion of the audit process.

**Recommendation 66 (High Priority):**

It is recommended that the rationale for rotation and the reasons for rotation of individual Audit clients be clearly documented, retained in Audit Office databases and reported to the senior management for review by the Contracting out Taskforce.

**Recommendation 67 (High Priority): (accepted in part)**

As part of its continuous improvement process the Audit Office should review and expand the nature and detail of its performance indicators, given the outcome of our analysis above.

## 6 Quality Assurance

**Recommendation 70 (High Priority):**

Review of QARC operation and resourcing be finalised as soon as possible and the Practice Manual be updated accordingly.

**Recommendation 75 (High Priority):**

The review of QARC terms need to ensure there is a continuous improvement cycle whereby we could see recommendations flowing out of the QA reviews, a management plan as to how the recommendations are going to be implemented and then a follow up QA review that assesses whether recommendations have been satisfactorily implemented and whether there has therefore been improvement.

This process should ideally be reported through the Audit Committee.

## **7 Reporting to Parliament – Efficiency**

### **Recommendation 78 (Medium Priority): (Accepted in part)**

Subsequent to legislative backing, the Auditor-General facilitate establishment of a high level Committee with the Department of Treasury and the Premiers Department that has the aim of establishing a clear and concise framework for the use of key performance indicators and benchmarking data within Department and Agency Annual Reports. As a result of this process the Auditor-General should undertake high level workshops with Departments and Agencies to assist them in understanding how to set effective quantitative and qualitative performance indicators and how to undertake appropriate benchmarking of their activities. Once this framework has been established the Auditor-General should provide comment and opinion on the key performance indicators and benchmarking data within Department and Agency Annual Reports in his Annual Report to Parliament.

**ATTACHMENT C****Key References**

*Public Finance and Audit Act 1983*

Audit Office of NSW, 2005, *Annual Report 2005*, [online at [www.audit.nsw.gov.au](http://www.audit.nsw.gov.au)]

Acumen Alliance, 2003, *Review of the Audit Office under section 48A of the Public Finance and Audit Act 1983*, Public Accounts Committee, Parliament of NSW, Sydney

Craswell, A., 2000, *Review of the Audit Office of New South Wales under s 48A of the Public Finance and Audit Act 1983*, Public Accounts Committee, Parliament of NSW, Sydney.