



Public Accounts Committee

TRIENNIAL REVIEW OF THE AUDIT OFFICE
OF NEW SOUTH WALES

Final Report

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Mr Matthew Brown MP
Chairman
Legislative Assembly Public Accounts Committee
Parliament House
Macquarie Street
SYDNEY NSW 2000

8th October 2003

Dear Mr Brown

TRIENNIAL REVIEW OF THE NSW AUDIT OFFICE

Acumen Alliance have pleasure in submitting our final report on the Triennial Review of the NSW Audit Office pursuant to Section 48A of the *Public Finance and Audit Act 1983*. As per the requirements of the *Public Finance and Audit Act 1983*, an initial draft report ("the 28 day report") was provided to the Auditor General. This final report incorporates comments received from the Auditor General on our '28 day draft report' and includes a response by Acumen to those comments.

In submitting our final report there are a number of matters of concern which Acumen Alliance needs to bring to your attention including:

- Commentary as to the exhaustive and detailed manner in which this review was conducted as a result of direct concerns levelled at the professionalism of our firms work; and
- A specific response to the concerns raised by the Auditor General in his letter to you dated 12 September 2003 (the covering letter for the Report on the Triennial Review of the NSW Audit Office).

CONDUCT OF THE TRIENNIAL REVIEW:

The Auditor General has raised concerns about the views provided in our report on the Audit Office's performance and suggests that our view is unbalanced and that we have relied on uncorroborated evidence in developing our conclusions. Our final report has been prepared in accordance with standards issued by the Institute of Internal Auditors.

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The findings and recommendations contained in the report are based on evidence gathered through a lengthy and consultative process, that included the following.

1. At the commencement of this review a detailed scope and boundary was provided to the Auditor General and Deputy Auditor General. This document dated 30 January 2003 was discussed with both the Auditor General and the Deputy Auditor General at a meeting with Acumen Alliance on 29 January 2003. During this meeting we discussed the planned approach to the audit and agreed an Acumen contact and an Audit Office contact be specified for each of the areas of review.

We were advised by the Auditor General and the Deputy Auditor General at this meeting that no substantive changes were required by them to the scope and boundary document. We were provided with the nominated Audit Office contact for each area of the review shortly after this meeting.

2. In the detailed scope and boundary document, reporting processes were set out as thus:
 - Emerging issues – raise issues as they arise and obtain AO management comment;
 - Exit discussion – conduct formal exit discussion with each area and obtain formal AO management comment;
 - Prepare draft report based on review, analysis and discussions and provide to AO for comment as required by Section 48A of the Act; and
 - Prepare and issue final report to the Auditor General.
3. In relation to the conduct of our review we completed detailed reviews of Audit Files and Audit Office Documentation across financial/compliance and performance audit and held detailed meetings with staff of the Audit Office and Audit Office clients. *In addition, our review involved detailed assessment of each of the 27 performance audit reports issued during the period under review, including reading all reports and client responses.* All matters of concern noted during this detailed fieldwork phase were subsequently corroborated prior to them being included in the findings and recommendations for this review.

During the emerging issues phase of the review (as set out above), we can confirm that detailed meetings were conducted with Audit Office staff to discuss issues/concerns that Acumen Alliance had identified during the fieldwork phase. Unfortunately, it now appears that the Audit Office staff we spoke with did not perceive these meetings to be 'official' or in the nature of 'formal exit interviews' and accordingly now deny their legitimacy.

A full oral debrief on the findings and recommendations for each area was provided to the Auditor General and Deputy Auditor General by Acumen Alliance on 10 March 2003, involving some hours. At this point, in terms of our responsibilities under the *Public Finance and Audit Act 1983*, Acumen Alliance were entitled to move straight to the '28 day draft report' and to submit this report to the Auditor General for comment. However, Acumen Alliance chose to be more detailed and conciliatory in the conduct of this review and preliminary draft reports were prepared for each area. These individual reports were subsequently provided to the Audit Office for comment. This process was conducted to ensure that we could meet with the Audit Office to clarify and amend any matters in the findings and recommendations that may not have been factually correct prior to releasing the '28 day report'.

Acumen Alliance then met with the contact Officer for each area and the Deputy Auditor General to work through the Preliminary Draft Reports in detail. As a result of these exit interviews a number of 'wording changes' were made to the reports. The majority of issues raised during these discussions did not change the context or detail of our findings and recommendations. Subsequent to these exit meetings, Acumen Alliance prepared the 28 day draft report.

As a result of further concerns raised by the Auditor General on the first '28 day draft report' we again met with the Audit Office on 5 August 2003 to clarify a number of issues. It was agreed at this point that some further minor wording changes would be made to the report and a 'revised 28 day report' would be issued.

On 12 August 2003, the Auditor General emailed Acumen Alliance indicating that subject to a few small additional wording changes to the draft report, that it was his suggestion that Acumen move to the official 28 day version of the report. All changes suggested in the Auditor General's email were made to the report prior to moving to the 'revised 28 day draft report'. It was, therefore, our belief at this time that the Auditor General

was satisfied that all wording corrections that had been raised in our meeting of 5 August 2003, had been addressed to his satisfaction. Rather than a suggestion that Acumen has not made changes as agreed to the 'revised 28 day draft report' and is as a result bordering on being unprofessional and negligent, it is our strong opinion that any blame/concern falls squarely at the feet of the Auditor General.

We believe that our consultative approach was exhaustive and went significantly beyond what was required of us under the terms of our briefing for this review.

In summary, our review involved:

- detailed review of documentary evidence in the Audit Office;
- detailed interviews with staff within the Audit Office;
- and interviews with selected Agencies in relation to Financial/Compliance/Performance Audit; and
- detailed interviews with other State Audit Offices.

All work was subject to full independent Partner review. The findings in the '28 day draft report' reflect the exhaustive work that was undertaken. Our draft report was also subject to detailed quality assurance review by two Partners within our firm who were both satisfied that the findings and conclusions in our report were fully supportable.

As stated previously, Acumen Alliance went through an exhaustive and consultative process with the Audit Office to ensure that all issues had been adequately addressed. All issues that the Audit Office had raised with Acumen Alliance, both verbally and in writing had been taken into account and included in the final report.

It is therefore disappointing that the Auditor General, in his letter dated 12 September 2003, has chosen to attack the professionalism of Acumen Alliance by stating, "despite raising this inconsistency with Acumen representatives a number of times (including in writing), Acumen has - for whatever reason - allowed it to remain. This is unprofessional, bordering on negligence."

The Auditor General further states that, "the ultimate result of the review's shortcomings is that it will be difficult for the Public Accounts Committee and others to judge the Audit Office's performance."

Given the consultative process that we have followed and in light of the Auditor-Generals e-mail of 12 August 2003, we find the attack on the professionalism of Acumen Alliance staff who conducted this review to be out of order and not objective.

CONCLUSION:

Our final report on the Triennial Review of the NSW Audit Office provides a significant amount of detail and commentary on the current management of the Office. Our findings and recommendations satisfactorily address all terms of reference required by the Public Accounts Committee and provide a balanced, corroborated assessment of the performance of the Audit Office over the period subject to review. Further, we believe that the Public Accounts Committee will not only find this report informative, but helpful in bringing about significant change in the manner in which the Audit Office conducts its independent audit work throughout the NSW Government.

We would be more than happy should you require it, to attend a full hearing of the Public Accounts Committee to provide a briefing on our report. Should you wish to discuss any aspect of our report, or to organize for us to attend a briefing please do not hesitate to contact myself in the first instance on (02) 6230 1997 or Chris Le Mesurier on 0414 846 277.

Yours sincerely

Robert Buker FCA
Partner

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1 Executive Summary

INTRODUCTION:

The Public Accounts Committee, as required by section 48A of the Public Finance and Audit Act 1983 (the Act), requested that a review of the Auditor-General's Office be undertaken. The review was to examine the auditing practices and standards of the Auditor-General and to determine whether the Auditor-General was complying with those practices and standards.

Acumen Alliance, a management consulting firm, was appointed in accordance with the Act to undertake the review. Acumen Alliance were given, by virtue of sub-section 48A(6) of the Act, the same powers of access given to the Auditor-General under sections 36, 37 and 38 of the Act.

Robert Buker, Chairman of Acumen Alliance and Chris Le Mesurier, Partner, Acumen Alliance (NSW) Pty Ltd oversighted and conducted this review with the assistance of their management consulting team.

BACKGROUND:

The Audit Office of New South Wales 2002 Annual Report summarises the roles and responsibilities of the New South Wales Auditor General and the Audit Office:

"THE NEW SOUTH WALES AUDITOR GENERAL

- Helps the New South Wales Parliament hold Government accountable for its use of public resources;
- Is independent of Government and reports directly to Parliament; and
- Operates under the Public Finance and Audit Act 1983.

THE AUDIT OFFICE

- Supports the Auditor General in his work;
- Reviews more than 400 New South Wales Government Agencies to:
 - Give Parliament reasonable certainty that Agencies financial reports are prepared correctly
 - Confirm that Agencies adhere to specific laws, regulations and Government directions.

- Investigates allegations of serious and substantial waste of public money;
- Determines whether an Agency or Government activity is achieving what is set out to do, economically, efficiently and according to the law.

VISION

- To be recognised as a centre of excellence in auditing.

MISSION

- Assist Parliament to improve the accountability and performance of the State.

VALUES

- Independence – work without fear or favour;
- Equity – be fair, just and impartial;
- Integrity – be open, honest and reliable;
- Empathy – be understanding of others;
- Customer focus – be courteous, professional and add value;
- Continuous Improvement – listen, think, challenge and work smarter.

CLIENTS

- Our clients are the Parliament of NSW, the Government and its Agencies and ultimately the Public of NSW¹.

The Auditor General has a clear and unequivocal role to play in the Westminster System of Government and his independence and role in providing accountability within the New South Wales Government should never be questioned, nor in the view of Acumen Alliance, minimised.

THE FORMAT OF OUR REPORT:

This document reports separately against each term of reference that the NSW Public Accounts Committee asked to be reviewed and analysed under the auspices of this assignment. Section 2 provides the Terms of Reference for this Review, with Section 3 providing our detailed recommendations against each Term of Reference. Sections 4 through 15 provide the detailed findings of our review.

¹ The Audit Office of New South Wales, Annual Report, 2002, Page 1.

CONDUCT OF THIS REVIEW:

Our review utilised the following mechanisms during its conduct:

- Detailed review of Audit Office files, documents and records;
- Interviews with key Audit Office Staff;
- Interviews with twenty client Agencies of the Audit Office at the CEO/Director-General and CFO level; and
- Detailed interviews with two other Australian State Audit Offices.

DETAILED FINDINGS AND CONCLUSIONS:

The body of this report provides our detailed findings, conclusions and recommendations in detail. Recognition needs to be given, that a number of findings and recommendations cross over a number of areas of the terms of reference for this review and the report should be read in this context.

We provide below a summary of findings and conclusions considered key:

FINANCIAL AUDIT

The Audit Office has clear and concise methodologies and practices in place for the conduct of financial audits. Acumen noted that these were followed consistently by staff when conducting Financial Audits. These processes also extend to the issuing of audit opinions by the Office, which Acumen noted throughout the review period complied with all Professional Auditing Standards.

Acumen notes, through interviews with Agencies and detailed review of Audit Office documentation that there could be greater utilisation of the Internal Audit work performed by Agencies. It was clear during discussions with Agencies that they were generally unaware of how the Audit Office placed reliance on Internal Audit, nor whether this use may have impacted the fees charged for their financial audit.

Greater focus should be given to increasing efficiency and effectiveness within the Financial Audit Process, particularly in relation to the use of automated working papers.

COMPLIANCE AUDIT

The Compliance Audit Program is currently set on a subjective basis. Acumen Alliance believes that topic selection should have a closer alignment with the Financial Audit “Whole of Government Risk Assessment”, so that there is a clear and demonstrated basis for topics chosen.

Focus needs to be placed on developing and implementing a continuous improvement cycle for the Compliance Audit Program to demonstrate its efficiency and effectiveness.

Acumen Alliance believes that there needs to be more transparency with Agencies as to what the Compliance Audit Program will cover in detail. Whilst supporting the development of a national standard for Compliance Audit, it is believed that the Audit Office should develop guidelines together with clear scope and boundaries for every Compliance Audit to provide greater transparency to Agencies subject to audit.

PERFORMANCE AUDIT

Performance Audit has produced audits of variable quality over the past three years. While it is difficult to directly measure the effectiveness of the audits undertaken, it is the opinion of Acumen Alliance that the program has not been as effective as intended in either promoting greater accountability or improving the performance of the NSW Public Sector. In terms of efficiency and economy the program has largely achieved its aims and compares favourably with other audit jurisdictions.

Acumen Alliance’s review of the Performance Audit Branch included analysis of all Performance

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Audit Reports tabled during the review period, detailed review of working paper files for five audits conducted during the period and discussions with the CEO/Director Generals that had been subject to a Performance Audit in their Agency during the period under review.

Clear feedback from Agencies interviewed during this review was that performance audit reports lack balance, that analysis of issues is at times superficial and that conclusions drawn on the evidence presented is at times inappropriate. There is a significant level of dissatisfaction with the usefulness of audit recommendations and hence the value or worth of the audits produced.

Acumen's review of detailed working papers and review of every Performance Audit Report issued during the review period supports this view.

Urgent management attention is required in relation to:

- The appropriateness of output and timeframe targets given resources applied to the Performance Audit Function;
- Ensuring appropriate staffing with relevant expertise for all Performance Audits undertaken;
- Establishing clear and relevant audit objectives and appropriate evaluation criteria; and
- The approach to communication with audit clients as part of the audit process and ongoing relationship management and communication with the Office's key strategic clients.

**STAFF OF THE AUDIT
OFFICE AND
ADMINISTRATION**

The Audit Office has recently launched a new Human Resources Strategy focusing on key attributes necessary to build the Audit Office to become a centre of excellence.

There however appears to be a clear difference of opinion amongst stakeholders as to who the clients of the Audit Office are. The Audit Office clearly and quite rightly sees the Parliament as its major primary client. Whilst recognising this, Acumen Alliance believes that other key stakeholders such as Departments and Agencies need to be given greater focus. It would be simplistic to consider the two needs separately as each are linked at the Ministerial level, legislative level and the policy level. It is therefore the belief of Acumen Alliance that the Human Resources Strategy needs to identify how staff will be trained to reconcile and manage the diverse needs of its stakeholder base.

Our review indicates a number of key issues need to be addressed including:

- Fast tracking some key initiatives within the Human Resources Strategy to obtain some early wins with staff;
- Undertaking a training gap analysis to align the needs of clients and the Audit Office with the learning outcomes of staff;
- Review of 'active' versus 'passive' recruitment techniques;
- Analysing the resources allocated to the implementation of the Human Resources Strategy both in terms of number and expertise;
- Determination of whether it would be appropriate to review the current non-SES levels of auditor and where possible reduce these to enable staff to have access to a more streamlined promotion and remuneration process;

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- Development of formal succession planning strategies to address the impact of the departure of senior staff.

As part of this review, the Public Accounts Committee specifically requested Acumen Alliance to provide feedback as to whether commencing Sections 33A and 33B of the Public Finance and Audit Act 1983 could lead to some improvement in the management of the Audit Office. Whilst this may be the case, given the level and extent of work being undertaken by the Audit Office in relation to Human Resources at this time, Acumen Alliance does not support the commencement of these Sections of the Act, until full consideration of the service wide implications and costs are analysed in detail.

However, in the interim, consideration should be given to payment of an allowance to professional staff to reflect differentials currently in place between auditing professionals in the public and private sector.

COSTS AND CHARGES

Our review of costs and charges indicated there were a number of areas, particularly in relation to Financial Audit, that required urgent attention by the Audit Office. Despite the cyclical nature of Financial Audit, as a monopoly provider with a fixed and known client base, the Audit Office should be able to schedule its Financial Audit activity, based on known commitments across the year with maximum efficiency. The monopoly position means that it does not compete for business as a private sector firm does. Thus comparative to a similar private sector firm, the Audit Office should have low or no overheads in relation to marketing, business development and the risk of staff not being utilised due to the loss of key clients.

Acumen Alliance has concluded based on its detailed review that Financial Audit charges are not reasonable for a number of reasons:

- The inclusion of a Performance Audit surcharge to fund half the costs of Performance Audits undertaken by the Audit Office;
- Costs of Compliance Audits are included within Financial Audit fees even though the Compliance Audit work undertaken may not impact upon the Financial Audit, and if it does, it may not be material in the context of a particular client's Financial Audit; and
- The fact that the Audit Office is not meeting their own production targets and is charging a premium for its Financial Audit Services due to there possibly being an excess number of staff currently employed (We are informed that staff have also performed a number of non billable functions by being assigned onto other internal corporate assignments which would reduce the opportunity to achieve their targets).

It is the opinion of Acumen Alliance that the Audit Office should not cross subsidise the Performance and Compliance Audit Programs through fees charged for Financial Audits.

Acumen Alliance is extremely appreciative of the time given during the conduct of this review by staff of the Audit Office, together with NSW Government Agencies and other State Audit Offices.

2 Terms of Reference

SCOPE OF THE REVIEW

The review was wide ranging, covering the following aspects of the Audit Office's processes and outputs:

- Auditing Standards and Practices
 - Financial Audits
 - Compliance Audits
 - Performance Audits
 - Partnership of Interests
 - Audit Communication
- Audit Office Management
 - Staff of the Audit Office
 - Audit Office Administration
 - Costs and Charges
 - Outsourcing
- Audit Office Performance
 - Performance Measurement
 - Quality Assurance Programs
- Reporting to Parliament
 - Efficiency
 - Expectations on the Reporting of Public Sector Audit
- General
 - Any matter that may be referred to the reviewer by the Committee during the course of the review.

DETAILED TERMS OF REFERENCE:

AREA	TERM OF REFERENCE
AUDIT PRACTICES AND STANDARDS	
FINANCIAL AUDIT	
FA (1)	Whether the Audit Office has adequate and appropriate methodology, practices and procedures.
FA (2)	Whether the audit opinions issued by the Office comply with applicable professional standards and practices.
FA (3)	Whether the audits are supported by adequate plans and work papers, appropriate audit evidence and appropriate quality control procedures.
FA (4)	Whether the audits are appropriately planned and co-ordinated, having regard to agencies' internal audit and technology inside the Audit Office
COMPLIANCE AUDIT	
CA (1)	Whether the Auditor-General should develop an internal standard for compliance auditing or, alternatively, whether the Auditor-General should join with other public sector agencies and develop a compliance auditing standard that would apply across Australia.
CA (2)	The effectiveness of compliance audits and their reporting in NSW.

CA (3)	How the effectiveness of compliance auditing is assessed by the Audit Office in the absence of an Australian Auditing Standard for Compliance Audits.
PERFORMANCE AUDIT	
PA (1)	Determine the extent to which the Audit Office has: <ul style="list-style-type: none"> ➤ Complied with the performance auditing standards; and ➤ Complied with the statutory requirement to avoid comment on matters of government policy, including whether the Audit Office has appropriate processes to make sure it complies with this requirement.
PA (2)	The extent to which the final reports on performance audits have stayed within the scope and objectives.
PA (3)	Whether final audit reports on performance audit reports are only issued after key data and factual information critical to the audit findings have been cleared with the agency concerned.
PA (4)	Whether the performance audits represent value for money.
PA (5)	The criteria the Audit Office uses in selecting performance audits including: <ul style="list-style-type: none"> ➤ Compliance with the criteria; ➤ Whether the focus of the reports should be consistent with the criteria; ➤ Whether the criteria are adequate and capable of attaining the best value for money

	<p>from performance auditing; and</p> <p>➤ Transparency in applying the criteria.</p>
PA (6)	<p>Following the 2001 amendments to the Public Finance and Audit Act 1983, the Audit Office now includes a section on performance issues for the larger agencies, which generally comprises material on performance indicators.</p> <p>The reviewer should examine and evaluate the Auditor-General’s reporting on performance issues in his general reports to Parliament, including any possible improvements.</p>
PARTNERSHIPS OF INTEREST	
POI (1)	<p>Whether it would be appropriate for the Auditor-General, once he has fulfilled his assurance role, to assist Agencies in achieving their corporate goals and reduce their exposure to risk.</p>
POI (2)	<p>Whether the Auditor-General could also assist in addressing issues common to Agencies across the public sector.</p>
POI (3)	<p>Whether Audit Office guidance has been inconsistent with guidance from central or other agencies and, if so, whether this has created difficulties for agencies in their dealings with those “guidance” agencies or the Audit Office.</p>
POI (4)	<p>How the Audit Office should co-ordinate this work with Central Agencies and other Agencies that provide guidance.</p>

AUDIT COMMUNICATION	
AC (1)	The effectiveness of communication between the Audit Office and the audited Agencies.
AUDIT OFFICE MANAGEMENT	
STAFF OF THE AUDIT OFFICE	
SAO (1)	The Audit Office's current practices in the recruitment, training, competency, remuneration, retention and professional development of staff, and whether they equip the Audit Office to achieve its task, both for financial/compliance audits and performance audits.
SAO (2)	Whether appropriate internal reporting practices are in place to enable the Auditor-General and his management to ensure value for money is being obtained in undertaking audit engagements.
SAO (3)	Whether there are appropriate time recording and costing systems in place to establish the costs of resources.
ADMINISTRATION	
Admin (1)	Whether the fact the Audit Office is under the governance of the Public Sector Employment and Management Act 2002 is an impediment to its good administration.

Admin (2)	Whether commencing Sections 33A and 33B of the Public Finance and Audit Act 1983 or introducing some other private sector model would improve the management of the Office.
COSTS AND CHARGES	
CC (1)	Whether a private sector competitive tender process would be useful in assessing the comparative costs of audit.
CC (2)	Whether the audit fees charged for financial audits are reasonable.
CC (3)	Whether the Audit Office should be able to provide non-audit services to clients on a fee for service basis and how to manage any possible conflict of interest.
CC (4)	Whether the Audit Office should cross subsidise the costs of performance and compliance audits with the profit made from financial statement audits.
OUTSOURCING	
OS (1)	The Audit Office's procedures for evaluating tenders from private audit contractors to carry out public sector audits.
OS (2)	The Audit Office's procedures for contract management, quality control and assurance.
OS (3)	The Audit Office's systems for rotating public and private sector auditors.

PERFORMANCE MEASUREMENT	
PM (1)	Whether key performance indicators are an appropriate method of determining the performance of the Auditor-General and his Office
PM (2)	The Audit Office's performance indicators and targets.
PM (3)	The Audit Office's reporting of its performance against the indicators and targets.
PM (4)	Whether the Audit Office uses the indicators to improve its own performance.
QUALITY ASSURANCE	
QA (1)	The effectiveness of the Audit Office's quality assurance programs.
QA (2)	Whether these programs ensure the Audit Office has well developed and appropriate methodologies and that these methodologies are consistently applied.
QA (3)	The external and internal verification of the effectiveness of the quality assurance processes.
QA (4)	Whether the quality assurance procedures in the Audit Office extend to financial audits, compliance audits, performance audits, audit reporting and the internal administration of the Audit Office.

REPORTING TO PARLIAMENT - EFFICIENCY	
RP (1)	Whether the Auditor-General's Reports to Parliament contain information already reported to Parliament.
RP (2)	Whether the Parliament is better informed by a separate discussion and analysis of the operations of Departments and Agencies as prepared by the Auditor-General and his staff.
RP (3)	The costs of the Auditor-General in preparing the reports to Parliament and whether the reports provide value for money.
RP (4)	Whether there are lower cost options in the style, format and contents for the Auditor-General's Annual Reports to Parliament.
EXPECTATIONS ON REPORTING	
ER (1)	How the Audit Office ascertains the expectations of the various users of the Auditor-General's reports and whether it meets them.
ER (2)	How the Audit Office reconciles the varying expectations of users with legislative requirements and audit practice.

3 Summary of Recommendations

Our recommendations have been grouped under separate headings for each term of reference for this review and have been classified as high, medium and low priority. We would expect that high priority recommendations would be implemented within three months of this report being tabled in Parliament, medium priority within six months and low priority with twelve months.

AREA OF SCOPE	RECOMMENDATION	AUDIT OFFICE RESPONSE	FOLLOW UP REVIEW COMMENTS
FINANCIAL AUDIT			
FA (1)	<p>RECOMMENDATION 1 (LOW PRIORITY):</p> <p>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.</p>	<p>Accepted.</p> <p>We will continue our surveillance of the market. We will document our view on an annual basis on retention of the current methodology/technology.</p>	<p>No further comment.</p>
FA (2)	<p>RECOMMENDATION 2 (LOW PRIORITY):</p> <p>The Review Team supports the Audit Office in its recent move to using plain English IAR's. However, it is recommended that the Audit Office continue to monitor developments in Audit Reporting within the wider profession and where appropriate review and revise the wording of its IAR's.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>We commenced issuing "plain English" Independent Audit Reports in respect of our 31 December 2002 audits.</p>	<p>No further comment.</p>

FA (3)	There are no recommendations for this finding.		
FA (4)	<p>RECOMMENDATION 3 (HIGH PRIORITY):</p> <p>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.</p>	<p>Accepted in part.</p> <p>Acumen has not understood our methodology. Our methodology already requires an assessment of internal audit for all agencies in our planning documents. If we assess that reliance can be placed on internal audit, then the methodology already requires the completion of the Preliminary Assessment of the Internal Audit Function. We will reinforce with the audit teams the importance of emphasising our reliance on Internal Audit at the preparation and presentation of the Client Service Plan.</p>	<p>We do not accept the Audit Office response to our recommendation. As part of our audit we reviewed the use of AS2 documentation relating to the use of Internal Audit on 20 Audits. Clear issues with documentary differences were noted. Examples were provided to the Audit Office as part of exit discussions.</p> <p>This is also an issue of Agency perceptions. The majority of Agencies interviewed during this audit indicated that they were not aware of how the Audit Office was utilising their Internal Audit functions. Whilst the Audit Office may argue that they always assess the Internal Audit Function and this is clearly demonstrated in the client service plan, if the Agencies provide feedback stating that they do not know how the Audit Office has used their Internal Audit Activity then a clear communication issue exists and this needs to be addressed.</p>

			<p>It is not correct to state that we do not understand the Audit Office methodology. There is a difference between having a methodology and it being applied. In this recommendation we are commenting on issues identified during our review that clearly demonstrated that there was an inconsistent approach to the documentation of Internal Audit Activity.</p>
	<p>RECOMMENDATION 4 (HIGH PRIORITY):</p> <p>Each engagement manager should ensure there is a focus on automating work papers, including client prepared schedules. This includes preparation of lead sheets and supporting schedules in spreadsheets to enable import into AS2. Similarly export of management reports into spreadsheets to enable easy analysis and incorporation into the AS2 files should be considered.</p> <p>This initiative would be enhanced through review and tailoring of the “client assistance schedules” to encourage use of electronic working papers.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>Our officers already encourage agencies to provide workpapers in the form that is most efficient for them to use. At times this will be in an automated form. Our client assistance letter is tailored each year in consultation with the relevant agency.</p>	<p>We do not accept the Audit Office response to our recommendation. This recommendation has been made as it was clear that there is inconsistency in the automation of working papers by audit staff currently. Whilst the Audit Office may indicate that the recommendation confirms the position that the Office has already taken, our review of audit files indicates that further work should be undertaken. We believe that the Audit Office should indicate in their response how they intend to improve this process to ensure maximum utilisation of technology. There should also be clear linkages into the efficiency review of AS2 and SAGE.</p>

	<p>RECOMMENDATION 5 (HIGH PRIORITY):</p> <p>It is understood that the Audit Office intends to conduct a review of the use of SAGE and AS2 during the period January to March 2004. Acumen supports this review and also recommends that this review include specific consideration of the application of AS2 to small and very small clients.</p>	<p>No additional action required.</p>	<p>No further comment.</p>
<p>NSW GRAINS BOARD</p>	<p>There are no recommendations for this finding.</p>		
<p>COMPLIANCE AUDIT</p>			
<p>CA (1)</p>	<p>RECOMMENDATION 6 (MEDIUM PRIORITY):</p> <p>The continuing role of the Auditor General through membership of the AusASB to assist in the AARF project for the development of a compliance auditing standard or guidance statement is supported. It is also recommended that the Auditor-General liaise with the Public Accounts Committee as to their involvement in this process.</p>	<p>No additional action required.</p> <p>It should be noted that while the Auditor-General is a member of the AuASB, it is up to that Board to decide how it wants to involve external parties in developing standards.</p>	<p>No further comment.</p>

	<p>RECOMMENDATION 7 (MEDIUM PRIORITY):</p> <p>Prior to the development of an Australian Standard on Compliance Audit, to assist in the communication of the role of compliance reviews in the NSW Public Sector, the Auditor-General should consider development of guidelines for the conduct of compliance audits. The guidelines should include an overview of the Compliance Audit Program, audit approach, methodology and reporting process. These Guidelines should be clearly communicated to all Agencies. Alternatively, if felt more appropriate, the Audit Office could make available to each Department and Agency a copy of relevant sections of the Compliance Audit Manual and Program for that respective financial year.</p>	<p>Not accepted.</p> <p>We believe an appropriate level of communication will be achieved through enhancement of the Client Service Plan.</p>	<p>We do not accept the Audit Office response to our recommendation, unless the Client Service Plan is significantly adjusted so that current communication issues are overcome. As long as the Client Service Plan clearly sets out the overview of the Compliance Audit Program, Audit Approach, Methodology and Reporting Processes then we would be prepared to accept the Audit Office response.</p>
	<p>RECOMMENDATION 8 (HIGH PRIORITY):</p> <p>For every Compliance Audit to be conducted a formal scope and boundary document should be established. This should clearly set out the objectives of the audit, the sample of Agencies to be reviewed, the scope of the review, the boundary for the review and the expected time frame of</p>	<p>Not accepted.</p> <p>Again, the context and content of compliance work will be effectively communicated through enhancement of the Client Service Plan.</p>	<p>We do not accept the Audit Office response to our recommendation. There is a clear communication issue involved here. If the Client Service Plan was significantly enhanced to encapsulate the recommendations of Acumen Alliance, then it may be an</p>

	<p>the review. This formal document should be provided to all Agencies that will be audited as part of that Compliance Audit process.</p>		<p>acceptable alternative. However, unless the Client Service Plan is significantly enhanced, we believe that our recommendation should be implemented in the interests of transparency with Agencies and obviously ensuring that Agencies are fully aware of the extent of the program.</p>
<p>CA (2) and CA (3)</p>	<p>RECOMMENDATION 9 (MEDIUM PRIORITY):</p> <p>The whole of government risk assessment conducted by the Audit Office should be expanded to include Compliance Audit. The risk assessment framework should follow and be consistent with AS/NZS3640, "Risk Management".</p>	<p>No additional action required.</p> <p>The whole of government risk assessment identifies areas of risk that, where appropriate, are included in the Compliance Audit work program.</p>	<p>We do not accept the Audit Office response to our recommendation. As set out in our report and agreed in our exit interview with the Audit Office, the Compliance Audit Program is set on a subjective basis. Our review work indicated that there were no linkages to the whole of government risk assessment undertaken for Financial Audit. This was confirmed in our exit interview.</p> <p>It is our belief that the Compliance Audit Program would be significantly enhanced if it were to be set using a risk assessment framework, whereby the Audit Office were able to ensure that areas of highest risk to government were included in the program. Without</p>



			<p>use of a risk assessment framework for setting the Compliance Audit Program, the Audit Office is not able to effectively demonstrate that it has effectively captured all compliance risks to government and come up with strategies for reviewing these.</p>
	<p>RECOMMENDATION 10 (MEDIUM PRIORITY):</p> <p>Additional involvement of Agencies in relation to the discussion of where their major compliance risks are and involvement by Agencies in the development of the APG's would strengthen the Compliance Audit process by helping ensure the significant compliance risks are considered.</p>	<p>Not accepted.</p> <p>The compliance audit program is based on "across the public service" compliance. The major compliance risks to a single agency are the responsibility of the financial audit teams assigned to each audit. These teams involve the agencies in the identification of appropriate risks and the planning of the audit.</p>	<p>Acumen Alliance does not support the Audit Office response to our recommendation. There is a difference between analysis of risks to individual agencies and risks across government. Compliance risks to Agencies, we agree, would normally be reviewed and tested as part of the normal Financial Audit process. However, we believe that in identifying across the board, 'whole of government issues' that it would be beneficial to obtain Agency involvement.</p>

	<p>RECOMMENDATION 11 (MEDIUM PRIORITY):</p> <p>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.</p>	<p>Accepted in part.</p> <p>Conducting a follow-up review in the following financial year is too soon as compliance reports are not tabled until 5-6 months into that year. We believe our process of allowing central agencies time to write new policies or legislation and agencies time to adopt them and put them into practice with a subsequent follow-up review by the Audit Office is more appropriate.</p>	<p>We are pleased that overall the Audit Office has accepted our recommendation. The development and implementation of a continuous improvement cycle for Compliance Audit is imperative, in particular, for measuring the effectiveness of the program. As long as in the continuous improvement program established by the Audit Office it is clearly demonstrated when 'key points of review' will be undertaken, we would agree with a follow up review not occurring until new policies/legislation has been implemented. However, the Audit Office should also play an important role in 'quality assuring' these polices/legislation changes prior to them being implemented, so that they can be comfortable that the changes recommended will address the original concerns raised.</p>
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	<p>RECOMMENDATION 12 (HIGH PRIORITY):</p> <p>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.</p>	<p>Accepted.</p> <p>However, costs of compliance reviews at the agency level are already monitored by each of the audit teams.</p>	<p>Whilst we are pleased that the Audit Office has accepted our recommendation, the reason for our recommendation is that there is currently no formal overall assessment conducted by the Audit Office of the Compliance Audit Program as to the Programs effectiveness, nor a tracking of the costs versus benefits of conducting each Compliance Audit.</p> <p>It is true that costs of compliance reviews at the Agency level are already monitored by each of the Audit Teams. However, our recommendation is suggesting that these costs and those other costs associated with the program be analysed to determine the costs versus benefits of having conducted the whole of government Compliance Audit.</p>
	<p>RECOMMENDATION 13 (MEDIUM PRIORITY):</p> <p>In addition to providing Agencies with comments in their management letter where concerns have been noted as a result of Compliance Audits</p>	<p>Not accepted.</p> <p>Our report to Parliament has always facilitated this. The secrecy</p>	<p>We do not accept the Audit Office response to our recommendation. Agencies clearly communicated to Acumen Alliance that they would</p>

	<p>conducted, the Audit Office should provide each Agency with a brief as to how they are performing in that particular area relevant to the rest of Agencies reviewed.</p>	<p>provisions of the <i>Public Finance and Audit Act</i> prevent us from naming other agencies when discussing results with an individual agency. However, we will encourage the agencies to review the reports to Parliament.</p>	<p>like to be advised of how they were performing compared to other Agencies that were audited as part of a particular compliance audit. This could be undertaken very easily on a 'no names basis'. For example, Agency A ranked fifth out of fifteen Agencies in respect of compliance issue XYZ.</p>
PERFORMANCE AUDIT			
PA (1)	<p>RECOMMENDATION 14 (HIGH PRIORITY):</p> <p>Resource planning and scheduling and the timing of proposed audits be coordinated to take account of the specialisations of current performance audit staff.</p>	<p>No additional action required.</p> <p>The planning of individual audits already takes into account the availability of staff within the Branch and their particular experience. However it is a common misunderstanding that audit staff need to have formal skills in the area they audit. What is more important is that they have experience and skills in reviewing how others manage projects and services.</p>	<p>Acumen Alliance do not accept the Audit Office response to this recommendation. There are two issues here being communication and skills of staff.</p> <p>In relation to communication, the most recent Auditor General's survey indicates that the level of client satisfaction with the Audit Office's 'understanding of Agency's business' and 'appropriateness of skills and expertise' is significantly below the desired standard set by the Audit Office itself. It is clear that this issue must be discussed with Agencies and resolved. The majority of Agencies interviewed during this audit indicated that they had to spend</p>

			<p>significant amounts of time, 'training the Audit Office staff' in the area being reviewed and were not entirely confident throughout the audit process being conducted that the Audit Office staff had a clear understanding and knowledge of the area being reviewed that would allow them to make meaningful findings and recommendations.</p> <p>Secondly in relation to key specialisations in the areas of audit, it is best practice to ensure that staff undertaking performance audits have the requisite skills and knowledge of the area that they are auditing. Performance Audit Managers are currently allocated topics on the basis of the 'next cab off the rank' within each organisational unit. This was confirmed by our interviews with Performance Audit staff and review of Performance Audit Reports. Under this approach it was observed that a number of staff with specialisations relevant to a particular audit being conducted were not being allocated to that audit. This is a critical issue and one that must be addressed by the Audit Office.</p>
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	<p>RECOMMENDATION 15 (HIGH PRIORITY):</p> <p>A preliminary assessment of the expertise and skills required to undertake each performance audit should be conducted at the commencement of each audit and compared with the assigned resources. The results of this assessment, including any recommendation to engage specialist staff or other experts, should be included in the audit scoping document. This may include seconding staff with specialist skills from the Agency being reviewed. The final decision on the need for and use of specialists and subject matter experts should be included in the audit plan. Where specialists and subject matter experts are not included in the audit team, a statement as to how the necessary knowledge and skills will be obtained should be included in the audit plan.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>This is already part of our Planning Process. The Planning Checklist and internal guidelines already require teams to consider the need for external expertise. Proposals form part of the budget submitted for each audit.</p>	<p>Acumen Alliance do not accept the response to our recommendation by the Audit Office. It was clear from our research, that managers are allocated performance audits on the basis of 'next cab off the rank'. No evidence was provided to us during the audit that would indicate that staff were matched based on their skills against the audit to be conducted. In addition, the financial cost relating to the use of financial experts clearly indicates that experts are not being utilised on audits as much as in past years.</p> <p>Our recommendation that the use of secondments from Agency's be used as part of the Audit Process is not one that compromises independence as they would be under the full supervision and quality assurance of the performance audit team. It is believed that the use of secondments from Agencies could significantly add to the level of ownership that an Agency has in the review process, which in turn would lead to a more likely outcome of improvement in that Agency as a result of the audit.</p>
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	<p>RECOMMENDATION 16 (HIGH PRIORITY):</p> <p>PAECs conduct reviews of the detailed working papers generated by audit teams throughout the audit engagement, particularly those generated by the Audit Manager. As a minimum a review should be undertaken at the end of the planning and detailed fieldwork phases of the audit. Evidence of the review should be retained on the audit files including any review notes generated and evidence that these have been appropriately cleared.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>Our quality assurance processes already require working papers to be reviewed during the audit. Checklists that form a critical part of our Quality Assurance processes require PAECs to sign off that workpapers have been reviewed.</p>	<p>Acumen Alliance do not support the Audit Office response to our recommendation. Evidence to demonstrate quality assurance processes were provided to us by the Audit Office during this review. These processes related to ISO9001, which leads to an argument of substance over form as an ISO9001 review merely reviews an organisation against its policies and procedures to ensure that these are being appropriately followed, rather than taking the next step and reviewing the underlying working papers. <i>There was little evidence from our review of working papers that either the AAG or PAEC undertook a detailed review of the working papers generated by the Audit Teams.</i> It is our belief that the AAG and PAEC should review working papers generated as part of the audit in detail and ensure that these are signed off as reviewed and there is a clear trail between audit findings, conclusions and recommendations flowing from this review into the draft report generated for the audit.</p>
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	<p>RECOMMENDATION 17 (HIGH PRIORITY):</p> <p>The Audit Office should ensure that where they might appear to be commenting on Government policy objectives, that they state their understanding of the policy objectives before they provide commentary. This should ensure that it is clear to the reader that the Audit Office is not questioning the merits of policy objectives.</p>	<p>Not accepted.</p> <p>We already have adequate controls in place to ensure we do not comment on the merits of government policy objectives.</p> <p>At the start of each performance audit, the relevant Minister is asked to indicate what policy objectives apply in the area of the audit.</p> <p>Each report is checked at various draft stages to ensure we are not questioning the merits of Government policy objectives. Report drafts are also exposed to the agency and the responsible Minister before they are tabled in Parliament.</p>	<p>Acumen Alliance do not support the Audit Office response to our recommendation. We agree that the approach adopted by the Audit Office is to seek input from relevant Ministers at the commencement of an audit. However, this does not always yield specific and clear statements of policies or policy objectives. It was not clear to Acumen, that after this approach any significant further attempt was made by the Audit Office to clarify policy or policy objectives.</p> <p>We stand by our recommendation in this regard, and believe that further controls should be put in place by the Audit Office as stated by our recommendation.</p>
<p>PA (2)</p>	<p>RECOMMENDATION 18 (HIGH PRIORITY):</p> <p>Detailed context specific audit objectives be formulated and reported for each audit in lieu of generic objectives.</p>	<p>Accepted.</p>	<p>No further comment.</p>

	<p>RECOMMENDATION 19 (HIGH PRIORITY):</p> <p>The statement of audit objectives accurately reflect the aspects of the mandate dealt with in the audit report.</p>	<p>Accepted.</p>	<p>No further comment.</p>
	<p>RECOMMENDATION 20 (HIGH PRIORITY):</p> <p>Audit criteria be clearly linked to the audit objectives.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>Detailed criteria are included in the audit plan which is provided to clients. Audit criteria in the report are sufficiently detailed to meet the reader's requirements.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. Our report contains detailed evidence to support the fact that audit criteria are not consistently linked to the Audit Objectives.</p> <p>It is our professional opinion that the current action being taken by the Audit Office is not sufficient and needs to be strengthened. We are therefore of the opinion that the Audit Office should implement our recommendation as it stands.</p>
	<p>RECOMMENDATION 21 (HIGH PRIORITY):</p> <p>Taking into account current Crown Solicitors Advice, the Audit Office should seek further independent legal advice on the interpretation of the</p>	<p>Not accepted.</p> <p>Acumen is wrong in saying that our interpretation of what constitutes a performance audit</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation.</p> <p>Our review of the Performance Audit</p>

	<p>provisions of section 38B as it impacts on the objectives of a performance audit.</p>	<p>constitutes a performance audit differs from that of the Australian National Audit Office and the Victorian Audit Office. Hence there is no need to obtain legal advice.</p> <p>However most Auditors-General would agree that performance audits have tended to focus more on the criterion of efficiency and that they need to do more in assessing effectiveness. Part of the difficulty is that many government programs do not have well-specified objectives or outcomes and this makes it more difficult to assess effectiveness.</p>	<p>process within the Audit Office indicates, in our professional opinion, that, the Audit Office interpretation of a performance audit differs from that of the Australian National Audit Office and the Victorian Audit Office.</p> <p>It is our belief that the Audit Office does not in all cases address the entire mandate in terms of efficiency, effectiveness and economy. We stand by our opinion that the Audit Office should make it clear in their reports which aspects of the mandate have been reviewed as part of the audit and how these have impacted on the objectives of the audit. This is critical in terms of engendering transparency in the performance audit process. It also assists in the interpretation and understanding of the findings and allows users to determine the extent to which the Audit Office has fulfilled its mandate.</p>
	<p>RECOMMENDATION 22 (HIGH PRIORITY):</p> <p>Changes in scope during an audit be clearly identified and explained in the final audit report.</p>	<p>Not accepted.</p> <p>Parliament has given the Auditor-General the right to determine the</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. As we state in our report, the issue here is one of</p>

		<p>scope of performance audits undertaken without having to justify his decisions. It is therefore illogical to require him to justify any changes to the scope that become necessary during the course of the audit.</p> <p>However any changes are always discussed with the agency concerned.</p>	<p>effective communication.</p> <p>Whilst recognising that Parliament has given the Auditor-General the right to determine the scope of performance audits undertaken without having to justify his decisions, to drive change in government, it is our professional opinion that an Agency needs to have ownership in any audit undertaken within its organisation. As an organisation that sees its role as assisting in improving accountability in government, we find it somewhat interesting that the Audit Office is not prepared to clearly identify and explain in the final audit report, for sake of clarity to the reader, where changes in scope have been made and why. Our report clearly identifies that in two performance audits where the scope was changed, whilst it was discussed with the Agencies concerned, both Agencies expressed some concern that they did not understand and/or agree with the reason for the change in scope. Both indicated that they did not believe that the increased scope was relevant to the original audit objectives.</p>
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			<p>Without compromising independence, to achieve maximum ownership and therefore change in an Agency, surely the most effective approach is to be as transparent as possible with the Agency being audited. To approach an audit without such an approach leads to antagonism and reluctance to work with the Audit Office and suggests an approach to audit that is 'old school and confrontational'. In our opinion this increases the likelihood that the audit will not be successful in engendering the maximum change possible within government.</p>
	<p>RECOMMENDATION 23 (HIGH PRIORITY):</p> <p>Disagreements with the audit client about the appropriateness and relevance of the scope compared to the stated audit objectives, be canvassed in the audit report.</p>	<p>Not accepted.</p> <p>See also our response to Recommendation 25.</p> <p>The scope of the audit is always discussed with the agency at the start of the audit. Where there are disagreements, it is our practice to attempt to resolve them. However agencies may well be subject to self-interest in seeking to limit or change the scope. Requiring an</p>	<p>Acumen Alliance does not support the Audit Office response to our recommendation.</p> <p>It is not a question, in our professional opinion, of forcing the Auditor-General to justify his decisions at all, nor of limiting his role as entrusted to him by Parliament.</p> <p>As stated in our report it is within the remit of the Auditor-General to determine the objectives and scope of</p>

		<p>Auditor-General to justify his decisions is tantamount to limiting the role entrusted to him by Parliament.</p>	<p>a performance audit and it is his prerogative to change the objectives and scope during the course of the audit.</p> <p>However, in the interests of effective communication between the Audit Office and Agencies, and ultimately the reader of the report it would engender greater transparency were the Audit Office to clearly outline whether the Agency had fully agreed to the appropriateness and relevance of the audit scope compared to the stated audit objectives. Where disagreements occur, it does not limit the role of the Auditor-General in his role to the Parliament, but assists the reader to understand why he believes the relevance of the scope compared to the audit objectives was satisfactory and why he has chosen the interpretation that he has.</p>
<p>PA (3)</p>	<p>RECOMMENDATION 24 (HIGH PRIORITY):</p> <p>The audit communication strategy for performance audits be amended to provide for ongoing assessment and review of the effectiveness of communication.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>The communication strategy is</p>	<p>Acumen Alliance does not support the Audit Office response to our recommendation.</p> <p>The issue here is one of effective communication and in our professional opinion, communication</p>

		<p>reviewed constantly to see how we can improve it.</p>	<p>between the Audit Office and Agency's subject to performance audits clearly require improvement. Interviews with Agencies during the review clearly supported our finding in relation to communication requiring improvement.</p> <p>As stated in our report, "The Audit Office has established procedures for a formal communication process with the client during an audit (including establishing a liaison officer within the client and providing written audit plans and draft reports to the Chief Executive Officer). However, it is important that the auditor assess the effectiveness of communication throughout the course of the audit."</p>
	<p>RECOMMENDATION 25 (HIGH PRIORITY):</p> <p>Given the duration of audits the strategy also provide for regular meetings between the executive of the audit client and PAEC (or AAG if necessary) throughout the conduct of the audit.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>The agency being audited is already given numerous opportunities to discuss the audit with the PAEC and the AAG.</p>	<p>Acumen Alliance does not support the Audit Office response to our recommendation. As noted in our report, "There is evidence that the PAEC and AAG do not take a hands-on participative role in the conduct of performance audits, except at the planning and report writing stage as demonstrated by the tables at the front of this Section of the Report</p>

		<p>with the PAEC and the AAG. Communication strategies are developed at the commencement of the audit as part of the planning process.</p>	<p>(Performance Audit Section). There was little evidence in the audits reviewed that the PAEC or AAG held regular meetings with the audit client executive management to brief them on the progress of the audit or on significant issues as they arose and as documented in our report, Agencies interviewed by us informed us of the lack of such on going meetings. It is our professional opinion that such communication processes require significant improvement.</p>
	<p>RECOMMENDATION 26 (HIGH PRIORITY):</p> <p>The communication strategy be formalised as an agreed communication protocol that is included in the audit plan.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>A communication strategy is already formulated as part of each audit plan. The channel and means of communication are already included in the opening letter to the CEO at the start of each audit.</p>	<p>Acumen Alliance is satisfied with the response of the Audit Office in this regard, as long as communication mechanisms are clearly improved, expanded and included in the audit plan provided to each Agency to be subject to a Performance Audit.</p> <p>This is again a question of communication and clear feedback from Agencies interviewed as part of this review, indicated that this area required significant improvement.</p>

<p>PA (4)</p>	<p>RECOMMENDATION 27 (HIGH PRIORITY):</p> <p>The AAG and Directors develop and implement a communication strategy for ongoing dialogue with key clients including the Members of Parliament and Parliamentary Committees and with major NSW public sector agencies.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>We already have an Office-wide communication strategy that includes the Auditor-General and Deputy Auditor-General meeting with a wide selection of Parliamentarians, including Members of Committees, and agency heads.</p>	<p>Acumen Alliance does not accept the Audit Office response to this recommendation. We refer to our report where we state, "However there is considered scope for the Executive of the Performance Audit Branch to take a greater role in intelligence gathering through more direct communication with audit clients and with the Parliament". Our report goes on to say, by way of footnote, "Indeed during the course of this review the Audit Office was not able to advance sufficient evidence to demonstrate that a sufficient level of resources was aimed at establishing links with both members of Parliament and its Committees." Indeed in interviews with the Auditor-General he expressed his view to us that he believed further work could be undertaken in this area to improve the level of communication.</p> <p>It is therefore our professional opinion, that the recommendation, as suggested, should be implemented by the Audit Office.</p>
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	<p>RECOMMENDATION 28 (HIGH PRIORITY):</p> <p>The application of the ‘complexity’ and ‘public interest’ criteria be reviewed for relevance and appropriateness. If necessary, the resource allocation model be modified to ensure that audit topics achieving the highest rating are undertaken before considering other topics.</p>	<p>Not accepted.</p> <p>The selection criteria are reviewed periodically. We consider that they are appropriate as applied. The ‘complexity’ criterion considers the difficulties we may experience to undertake an audit. We have to have regard to our resources.</p> <p>Equally, we consider that “public interest” is a valid and appropriate consideration. One of our aims is to provide assurance to the public at large. This criterion satisfies that intention.</p> <p>The second sentence ignores the cost of each audit in comparison to its benefit. If adopted, it could mean that one marginally higher rating, but far more expensive audit is carried out rather than 2 or 3 other audits whose collective ratings are higher.</p>	<p>Acumen Alliance does not support the Audit Office response to our recommendation.</p> <p>As stated in our report, “In discussions with Audit Office executives and staff there was no clear and consistent articulation of what was meant or intended by the ‘public interest’. Further, in our professional opinion, use of current criterion and the implications that could be drawn from it, exposes the Audit Office to the charge that it seeks to select topics that will generate a lot of publicity. This can and has been interpreted by a significant number of clients, as the Office being more interested in ‘media hits’ than in genuinely wanting to improve performance.</p> <p>It is our professional opinion therefore that that Audit Office should implement our recommendation as it stands.</p>
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	<p>RECOMMENDATION 29 (HIGH PRIORITY):</p> <p>The audit scoping process be used to formally review and update the screening assessment and the results of this review be included in the scoping document.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>The “screening” and scoping process was already the subject of a revision before Acumen started its review. A new process has already been implemented with our current program.</p>	<p>As stated in our report, the purpose of the scoping exercise is to validate the original rationale for the audit. Review of scoping papers for selected audits revealed that there is little or no reference to the original screening criteria. There is no commentary in the scoping papers reviewed or other evidence to suggest that the initial assessment had been reviewed and validated.</p> <p>Acumen Alliance is therefore prepared to accept the Audit Office response to our recommendation if the ‘revision’ being conducted provides a process where the audit scoping process is used to formally review and update the screening assessment and the results of this are then included within the scoping document.</p> <p>Prior to receiving comments from the Audit Office on this report, Acumen Alliance had not been made aware that the screening and scoping process was already the subject of a revision.</p>
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	<p>RECOMMENDATION 30 (HIGH PRIORITY):</p> <p>The audit plan provided to the client and the report to Parliament include reference to the original rationale for selection of the topic and whether the initial assessment (particularly in terms of expected outcomes) was validated by the audit.</p>	<p>Not accepted.</p> <p>The Auditor-General’s Foreword to each performance audit report provides the reader with a concise, non-technical explanation of why the topic was selected for audit.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. In our report we state, “.....This is also evident in the final audit report that is tabled in Parliament. The reports make no direct reference to the criteria (i.e. original rationale for the selection of the topic and whether the initial assessment (particularly in terms of expected outcomes) was validated by the audit.”</p> <p>It is our professional opinion that the Auditor-General’s Foreword to each performance audit report should be enhanced.</p>
	<p>RECOMMENDATION 31 (HIGH PRIORITY):</p> <p>The Auditor-General facilitate a forum whereby the Audit Office, IPART and ICAC discuss planned review programs to ensure maximum review coverage of government and to avoid the risk of ‘cross-overs’ in work conducted.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>A procedure has already been in place for some time whereby before each audit we canvass ICAC and the</p>	<p>No further comment.</p>

		Ombudsman as to their views about our proposed audit. This provides the opportunity to identify any “cross-overs”. It is very unlikely that IPART and the Audit Office would both address the same issue as IPART has a substantially different role and its reviews are largely the result of specific references from government.	
	<p>RECOMMENDATION 32 (HIGH PRIORITY):</p> <p>The Audit Office, should review the appropriateness of output and timeframe targets given resources applied to the Performance Audit function. This will obviously be impacted by the ability of the Audit Office to achieve full Treasury funding for the Performance Audit program as recommended in the section on Costs and Charges.</p>	<p>No additional action required.</p> <p>The Office was already reviewing this issue before the Acumen review was undertaken.</p>	<p>Acumen Alliance were not provided with evidence during the conduct of this review to indicate that the Audit Office were reviewing the appropriateness of output and timeframe targets given resources applied to the Performance Audit function. If this process is now being undertaken, we are satisfied with the Audit Office response to our recommendation.</p>
	<p>RECOMMENDATION 33 (MEDIUM PRIORITY):</p> <p>The Audit Office, should formalise a policy that sets the framework for how performance audit topic selection should be undertaken. This policy</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. As stated in our report, “The Audit Office seeks input from a number of sources to identify</p>

	<p>should encapsulate a risk management process.</p>	<p>taken.</p> <p>We already have a policy that has been in place for many years. It is reviewed periodically and was revised last year.</p> <p>It is not clear what Acumen intends in respect of risk management. A formal risk assessment is carried out in respect of each audit and is documented.</p>	<p>from a number of sources to identify potential audit topics. Ministers and other Members of Parliament and Agency Heads are asked each year to contribute potential topics. Financial Audit Staff within the Audit Office are also canvassed. Finally, staff in the Performance Audit Branch also suggest topics. Discussions with audit staff indicated that there is limited opportunity to directly gather and analyse 'intelligence' at an agency level or service-wide, to assist in the identification of potential topics. It was stated that there was 'not much science' involved in the identification of topics. The process was also characterised as more of a 'clerical, form filling exercise'."</p> <p>Acumen Alliance were not provided with evidence to demonstrate that a formal risk assessment is carried out in respect of each audit and that it is documented.</p> <p>In terms of ensuring highest risks to government are identified and included within the Performance Audit Program, it is our professional opinion that a risk management process would be the most effective mechanism to be utilised, rather than</p>
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			<p>the current processes utilised where it appears that, there is not much science in the selection of topics.</p> <p>In terms of formulating this recommendation, it was aimed at external, not internal reporting mechanisms.</p>
PA (5)	<p>RECOMMENDATION 34 (HIGH PRIORITY):</p> <p>The composite 'client satisfaction' and 'chargeable time' measures be disaggregated and reported separately for performance audits and financial audits.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>This was already being considered at the time of the Acumen review and the 'client satisfaction' and 'chargeable time' measure have been disaggregated in our 2003 corporate plan. Both these measures have been available to PAB management for some time and are used to monitor performance.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. Whilst we agree that KPI information is disaggregated and reported internally, it is not currently reported externally by the Audit Office. This was confirmed in meetings with the Audit Office during discussions relating to our preliminary draft audit report. We stand by the comment in our report where we state, "If the Office is to achieve its mission of improved performance as well as improved accountability it needs to better track its effectiveness.</p>
	<p>RECOMMENDATION 35 (HIGH PRIORITY):</p> <p>The approach to the resolution and public reporting of disagreements with audit clients be reviewed.</p>	<p>Not accepted.</p> <p>We reject the implication in the</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. The issue here is</p>

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	<p>audit clients be reviewed. Consideration be given to moving to an 'agreed report' model or to the incorporation of management comments at relevant sections throughout the report.</p>	<p>recommendation that we do not make every effort to resolve disagreements with audited agencies either during the audit or at the final report stage.</p> <p>We have reviewed reporting styles and report structures many times. We do not think incorporating management comments throughout the report is effective in resolving differences in views with agencies.</p> <p>The "agreed report" model (as used by the UK National Audit Office) can add substantially to the cost and duration of audits.</p>	<p>clearly one of communication and is set out in detail in our report.</p> <p>We believe that the Audit Office should implement our recommendation as stated.</p>
	<p>RECOMMENDATION 36 (HIGH PRIORITY):</p> <p>The proportion of audit recommendations accepted by the client be used and reported as an effectiveness indicator for performance audits. This information be captured prior to the tabling of the audit report and incorporated in the appendix to the report together with efficiency and effectiveness performance information</p>	<p>Not accepted.</p> <p>Most Auditors-General do not accept that this is a very meaningful measure.</p> <p>We already have procedures to capture agencies' comments and reaction to recommendations. That information is retained on file and used when a 'follow-up' audit is</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. It may be that most Auditor-General's do not accept that this is a very meaningful measure. However, in our opinion, in the wider profession, a clear performance indicator placed on auditors is one where the proportion of audit recommendations accepted by the client be used and reported as</p>

	<p>on cost and cycle time.</p>	<p>undertaken. We know our 'success rate' with the recommendations over recent years is between 80 and 90 per cent.</p>	<p>an effectiveness indicator to enable effective evaluation of the success of the audit process/program.</p> <p>In relation to a success rate with recommendations over recent years of between 80 and 90 per cent, we draw attention to the detail of our report where we state that the Audit Office does not systematically monitor and review the overall level of acceptance and implementation of the recommendations that it makes. We also draw attention to current Agency concerns and responses to recommendations made by the Audit Office as detailed in our report.</p> <p>It is our professional opinion that the Audit Office should implement our recommendation as it stands.</p>
	<p>RECOMMENDATION 37 (HIGH PRIORITY):</p> <p>References made to audit reports in the Parliament be tracked where a cost-effective method of data capture can be developed.</p>	<p>Not accepted.</p> <p>Parliament does not have a system to allow these data to be readily captured. The cost of collecting these data could be prohibitive. The proposal also ignores the frequent references to our reports made by Members outside Parliament</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. Rather than state that the cost of collecting these data could be prohibitive, it would be more appropriate for the Audit Office to firstly review what the expected costs of undertaking such a process may be and if they are</p>

		Members outside Parliament, particularly for reports that are released out-of-session.	prohibitive to find an alternative, robust approach. We also note that the Audit Office maintains detailed files of where comments are made in public by Ministers on Audit Office reports, so collection of this data should therefore be relatively straight forward.
PARTNERSHIPS OF INTEREST			
POI (1)	There are no recommendations for this finding.		
POI (2)	<p>RECOMMENDATION 38 (MEDIUM PRIORITY):</p> <p>The Audit Office to actively identify and pursue issues where it can provide common assistance to Agencies across the public sector including provision of workshops on issues relating to risk management, audit techniques and accounting applications.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>Acumen acknowledges that while there is a role for the Audit Office to play on issues relating to risk management and accounting applications, the primary role falls to Treasury in the areas of risk management and accounting.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. Whilst we note in our report that the primary role falls to Treasury in the areas of risk management and accounting, it is our professional opinion that the Audit Office, in attempting to engender greater efficiency/improvements in government processes, should actively identify and pursue issues where it can provide common assistance to Agencies. This may involve undertaking joint work with the NSW Department of Treasury.</p>
POI (3)	There are no recommendations for this finding.		

<p>POI (4)</p>	<p>RECOMMENDATION 39 (LOW PRIORITY):</p> <p>It is recommended that the Audit Office continue its practice prior to publishing guides of requesting comment on the content from other Central or Authority Agencies to ensure that duplication of guidance is eliminated.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p>	<p>No further comment.</p>
<p>AUDIT COMMUNICATION</p>			
<p>AC (1)</p>	<p>RECOMMENDATION 40 (HIGH PRIORITY):</p> <p>A formal communication strategy be issued and made available to all clients. This has been successfully undertaken in other jurisdictions such as the US GAO. The communication strategy can be used as part of a “quasi client service level agreement to strengthen client relationships. Much of this strategy would be based on the existing protocols included in the Audit Office Practice Manual.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>The current Client Service Plan outlines the communications that the agency will receive as part of the audit process.</p>	<p>We do not accept the response to our recommendation by the Audit Office. Clear communication issues exist and the current Client Service Plan does not provide enough detail to Agencies. This issue was raised by a significant number of Agencies interviewed as part of this review and was discussed with the Audit Office during exit discussions on our preliminary draft report.</p>

	<p>RECOMMENDATION 41 (HIGH PRIORITY):</p> <p>Increased focus by Engagement Managers and Controllers on ensuring timely communication of issues to management. Specifically this could include some innovations in audit communication, such as:</p> <ul style="list-style-type: none"> ➤ always ensuring management letters are raised following interim audit work where issues arise; and ➤ provision of weekly (or on a timeframe considered reasonable between the client and the Audit Office) “audit issues” papers to clients, outlining the issue and who is dealing with it from both an Audit Office and Client perspective. 	<p>No additional action required.</p> <p>Where significant issues arise from interim audit work, the current practice is for management letters to be issued. The provision of weekly “audit issues” papers is not practical. It could also add substantially to Audit Office costs and hence fees charged.</p>	<p>We do not accept the Audit Office response to our recommendation. It would be relatively simple in ensuring effective communication to spend fifteen minutes, jotting down ‘bullet points’ of issues so that management in an Agency are fully aware of matters of concern and this will help them be resolved more efficiently and effectively. Provision of a simple document such as this, would not, we believe add significantly to audit costs and hence fees charged. In addition, implementing such a process would add significant value in the communication process as part of an audit.</p>
	<p>RECOMMENDATION 42 (HIGH PRIORITY):</p> <p>A client feedback survey (over and above the two yearly client survey currently conducted) be introduced as</p>	<p>Not accepted.</p> <p>A mandatory client feedback survey</p>	<p>We do not accept the response to our recommendation. Development of such a survey</p>

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	<p>currently conducted) be introduced as part of the audit finalisation. This survey should be made mandatory and the issuing, collation and reporting of survey results should be the responsibility of the Policy & Research Branch to provide independence. Feedback on individual staff performance as a result of receipt of the survey should be fed into the staff performance appraisal process.</p>	<p>as part of audit finalisation on top of our client survey is excessive. The current Client Service Report already gives clients the opportunity to provide comments on the conduct of the audit. It would be difficult to compel clients to respond to a further survey.</p>	<p>would add significant value in 'continuous improvement' within the audit process. It would also be a pro-active way of enhancing staff performance appraisal processes. The survey, in our opinion, could be standard (no more than one page) and provided to clients at the end of the financial audit process. We believe that clients would respond to such a concise survey in a positive manner and it would help to improve communication processes between the Agencies and the Audit Office.</p> <p>We believe that this process is also vital in ensuring that the staff performance appraisal process can give direct and open feedback about how clients have found the 'professionalism' and 'technical competence' of the auditor being reviewed.</p>
<p>STAFF OF THE AUDIT OFFICE</p>			
<p>SAO (1)</p>	<p>RECOMMENDATION 43 (HIGH PRIORITY):</p> <p>It is recommended that the timeline set for implementation of the Human Resources strategy be reviewed and</p>	<p>Not accepted.</p> <p>The Office has developed an</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation.</p>

	<p>implementation of key activities be brought forward.</p> <p>In particular, it is recommended that activities associated with performance management, resource management, work practices and resource planning be addressed by December 2003.</p> <p>At the same time, the opportunity for “early wins” be identified and facilitated to facilitate the continued support of staff.</p>	<p>integrated plan for implementing its HR Strategy. The plan identifies 20 major workstreams, covering a wide range of aspects of HR within the Office, as well as program co-ordination and management activities. A significant factor in the planning was the interdependency of various activities within the program, and this is reflected in the timing adopted. It is not feasible to bring forward the activities proposed by Acumen in the context of those dependencies, other recent initiatives and ongoing activities within the Office.</p> <p>We recognise the value of identifying and achieving “early wins” to facilitate continued staff support. We continue to focus on this in a number of ways, both within and outside the HR Strategy implementation program.</p>	<p>Whilst it is accepted that major change initiatives can require an incremental process to facilitate large-scale outcomes, by implementing change at the rate set out by the NSW AGO there is a significant risk that the broad initiative will either:</p> <ul style="list-style-type: none"> • Lose track because staff lose confidence in the ability of management to deliver change; or • Be impacted significantly by environmental public sector/governmental issues that may lessen the capacity to facilitate organisational outcomes. <p>It is our view that the activities mentioned in our report, in particular performance management, resource planning and work practices should be “fast tracked” to provide a strong foundation for the following change activities.</p>
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	<p>RECOMMENDATION 44 (HIGH PRIORITY):</p> <p>Whilst recognising that the Audit Office has already issued RFP's to obtain expert resources externally to assist with the strategy and that an external program advisor has been appointed, it is recommended by Acumen Alliance that the staff resources allocated to the implementation of the Human Resources strategy still be reviewed, both in terms of numbers and expertise.</p>	<p>No additional action required.</p> <p>The Board identified at the outset that the success of the program would depend on ensuring that appropriate levels of skill and resource were available for the various workstreams within the program. In setting the budget for the program, we identified specific areas requiring the use of external consultants, including ongoing input from a program advisor. We also estimated the internal resource needs in relation to each workstream and in relation to management of program activities. This requirement is reviewed regularly by the Board.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation.</p> <p>In developing this recommendation Acumen was cognisant of the skills and dedication of staff currently engaged in facilitating the HR Strategy outcomes. However, in a project of the significance as this there is a need to ensure that the number and competencies of staff involved are aligned with the context of the project. Our view, which we understand from our debriefing meeting with the Audit Office was at least partly shared, was that there were issues in the alignment of the skills and numbers of staff currently employed in the project. We believe the resources are possibly not adequate, which can impact on the timings and outcomes of the strategy.</p>
	<p>RECOMMENDATION 45 (MEDIUM PRIORITY):</p> <p>It is recommended that a greater use of recruitment consultants be utilised in</p>	<p>No additional action required.</p> <p>The HR Strategy program includes a</p>	<p>No further comment.</p>

	<p>non-SES positions, and that when recruiting for non-base level positions experience in agencies or industries in addition to high-level technical skills be emphasised.</p>	<p>specific workstream which will address recruitment processes in light of the Office’s competency model and other aspects of the program deliverables. The scope of that task would include the aspects raised by Acumen.</p>	
	<p>RECOMMENDATION 46 (HIGH PRIORITY):</p> <p>A formal training needs analysis be undertaken that will assist in providing an alignment between the needs of clients and the AO with the learning outcomes of staff training. The training needs analysis should examine:</p> <ul style="list-style-type: none"> ➤ Currency of professional qualifications; ➤ Client and key stakeholder needs; ➤ Management training issues; ➤ Developments in the auditing profession; ➤ Developments in the agencies audited. 	<p>No additional action required.</p> <p>The Office recognises the importance of ensuring that learning and development programs are aligned with Office objectives and individual needs. The HR Strategy envisages that this will occur through a Learning and Development Strategy, which will be based on the Audit Office competency model. Needs analysis is occurring through various means, including individual development action plans agreed as part of the performance management process.</p> <p>A formal training needs analysis in the short term will not assist in achieving more effective outcomes, but rather conflict with the</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation.</p> <p>Whilst it is recognised by the AO that there is a need to ensure the alignment of learning and development program, current organisational systems do not reflect this understanding. The issue here seems to revolve around timing. The Audit Office is of the opinion that the eventual Learning and Development strategy will address this issue. Acumen is of the opinion that in developing a strategy there is a need to conduct a training needs analysis first to ensure that adequate information on the training and development environment is available to effectively determine the</p>

		but rather conflict with the implementation of other elements of the HR Strategy implementation program.	strategy.
	<p>RECOMMENDATION 47 (MEDIUM PRIORITY):</p> <p>Additional opportunities be provided for AO personnel to gain a detailed understanding of client agencies operations and activities. This may be achieved through outplacements, attendance of training at client premises or the utilisation of client personnel in the development of in-house training programs.</p>	<p>No additional action required.</p> <p>The Office already places specific focus on this aspect of learning and development through a range of activities, including secondments, Industry Specialty discussion groups and participation in industry based training programs and events. The learning and development strategy will provide the framework for ongoing focus on this area of competency.</p>	<p>Acumen Alliance does not support the Audit Office response to our recommendation.</p> <p>This appears again to be an issue around timing. We were unable to locate a formal strategy regarding the use of secondments and, even if there is, the practice surrounding them appears to be "ad-hoc". It is hoped, based on the Audit Office response to our recommendation that perhaps the Learning and Development strategy will address this.</p>
	<p>RECOMMENDATION 48 (MEDIUM PRIORITY):</p> <p>Whilst acknowledging that the Audit Office is on the way to this, the current non-SES levels of auditor be reviewed and where possible reduced to enable staff to have access to a more streamlined promotion and remuneration process. These levels</p>	<p>No additional action required.</p> <p>This is one of the key areas to be addressed in the HR Strategy workstreams relating to Competency Profile, Organisation Structure and Reward and Recognition.</p>	<p>No further comment.</p>

	<p>should be similar to:</p> <ul style="list-style-type: none"> ➤ Trainee Auditor ➤ Senior Auditor ➤ Managers 		
	<p>RECOMMENDATION 49 (HIGH PRIORITY):</p> <p>It is recommended that the AO develop and adopt formal succession planning strategies to address the impact of the departure of senior staff.</p> <ul style="list-style-type: none"> ➤ The AO should identify its existing competencies, related to both its internal leadership needs as well as the needs of the public sector. ➤ The AO needs to evaluate and assesses current middle management employees to determine how they meet the needs of the AO for senior management positions. ➤ The AO introduces where appropriate coaching, mentoring, training, and 	<p>No additional action required.</p> <p>These issues are core to our HR Strategy and will be addressed in the implementation program.</p>	<p>No further comment.</p>

	recruiting methods that match personnel requirements – and future needs.		
SAO (2)	<p>RECOMMENDATION 50 (HIGH PRIORITY):</p> <p>It is recommended that the services currently provided by TOPS be put out to tender to identify whether alternative options are available in the marketplace that can meet AO requirements within an affordable budget. In reviewing alternative options to TOPS it is recommended that the degree of integration available within current AO management information systems be reviewed with the goal to facilitate greater integration.</p>	<p>Not accepted.</p> <p>We are currently reviewing our Information Management and Technology Strategic Plan. That review will take into account the investment in the current system, changing technologies and operating environment, cost of new systems, organisational impact and relative priority of other initiatives. It would be premature to put out a tender for a new Practice Management System until that review is complete.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation.</p> <p>Notwithstanding the issues raised by the Audit Office, there appears to be evidence of issues surrounding the continuing operation of TOPS, including significant issues regarding the capacity of the Audit Office to support the system.</p> <p>It would be expected that the review to be undertaken by the Audit Office may well develop findings that are in agreement with our recommendation.</p>
ADMINISTRATION			
Admin (1) & Admin (2)	<p>RECOMMENDATION 51 (LOW PRIORITY):</p> <p>That commencement of sections 33A and 33B of the Public Finance and Audit Act 1983 not take place until full</p>	<p>No additional action required.</p> <p>The Office has made no decision on</p>	<p>No further comment.</p>

	<p>Audit Act 1983 not take place until full consideration of the costs and service-wide implications takes place. In particular, it is important to note:</p> <ul style="list-style-type: none"> ➤ Level of alignment between the HR strategy and alternative recruitment and conditions of service; ➤ Service-wide implications of any changes in pay and conditions; and ➤ The cost of any changes, and sources for funding of those changes. 	<p>this issue and will not do so until issues such as those raised by Acumen are considered.</p>	
	<p>RECOMMENDATION 52 (MEDIUM PRIORITY):</p> <p>Noting the complexities of the Public Sector Employment and Management Act 2002, consideration should be given to the payment of an allowance to reflect differentials currently in place between auditing professionals in the public and the private sector. This level of this allowance be determined annually, and be based on</p>	<p>No additional action required.</p> <p>Remuneration and other conditions of employment are being addressed as part of our HR Strategy. It would not be appropriate to address one aspect in isolation. In any event, the section of the Act referred to by Acumen only applies to staff below the SES level.</p>	<p>No further comment.</p>

	research and advice undertaken by the Public Sector Employment Office.		
COSTS AND CHARGES			
CC (1)	<p>RECOMMENDATION 53 (HIGH PRIORITY):</p> <p>It is recommended that the Audit Office undertake a formal benchmarking exercise of currently contracted out audits to determine whether the comparative costs of audits charged by the private sector and the hours applied to the job is comparable with those charged by the Audit Office.</p>	<p>No additional action required.</p> <p>The Audit Office already has a Benchmarking Task Force whose responsibilities include benchmarking contracted audits.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation.</p> <p>Additional action is required to undertake the benchmarking exercise.</p> <p>At the time of audit the task force had not undertaken any benchmarking and had not addressed benchmarking issues.</p>
	<p>RECOMMENDATION 54 (HIGH PRIORITY):</p> <p>It is recommended that the Audit Office should review its on cost percentage application for contracted out audits and align it with actual hours charged so that it is more equitable.</p>	<p>No additional action required.</p> <p>The Audit Office already reviews its on-costs for contracted out audits on a job by job basis.</p> <p>In its analysis, Acumen failed to include all costs. If all costs are included, the average on-cost would have been approximately</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. There was no documentation provided to Acumen Alliance during this review to indicate that the Audit Office already reviews its on-costs for contracted out audits on a job by job basis.</p> <p>Information provided to us by the Audit Office during this review</p>

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		15%, not 7% as quoted by Acumen in its report.	Audit Office during this review indicated that we have included all costs in our summation. At the time of discussing our preliminary draft report on this area with the Audit Office, no questions were raised in relation to our analysis of the numbers being incorrect.
CC (2)	<p>RECOMMENDATION 55 (HIGH PRIORITY):</p> <p>It is recommended that the Audit Office review its billable target and actual achievement of that target to improve its billable percentage to a more reasonable rate.</p>	<p>No additional action required.</p> <p>The Audit Office reviews its billable targets annually</p>	No further comment.
CC (3)	<p>RECOMMENDATION 56 (LOW PRIORITY):</p> <p>To protect the independence of the Audit Office, it is considered that fee for service work should not be undertaken by the Office.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p>	No further comment.
CC (4)	<p>RECOMMENDATION 57 (HIGH PRIORITY):</p> <p>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</p>	<p>Accepted in part.</p> <p>The Office has previously initiated discussions with Treasury regarding the level of funding for its performance audit programme, and has commenced a cost analysis.</p>	Whilst Acumen Alliance is satisfied with the response of the Audit Office to the level of funding for the performance audit program, it is not satisfied with the response relating to compliance audits.

	<p>Compliance and Performance Audit Programs.</p>	<p>We view compliance audits as part of the broader financial audit of agencies and as such their costs are recovered in the financial audit fee.</p>	<p>We understand the Audit Office view in this regard. However, this is a clear issue of transparency and accountability. In our professional opinion, whilst financial audits would include compliance testing as part of normal fieldwork, the Compliance Audit Program targets areas that would not necessarily be reviewed as part of normal financial audit processes. It is our opinion that the compliance work undertaken during a financial audit should be the minimum necessary in order to support the audit opinion placed on the financial statements. Whole of Government Compliance Audits conducted, we believe, are outside normal financial audit parameters and should be funded separately. Agencies have also indicated that they would prefer transparency of fees charged.</p>
	<p>RECOMMENDATION 58 (HIGH PRIORITY): Financial Audit fees charged to Departments and Agencies should reflect only work required to be undertaken to express an opinion on the financial statements as to whether</p>	<p>Not accepted. The Office’s approach to determining its fees is based on its view that the Parliament expects the Auditor-General to conduct a</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. In our professional opinion the financial statement audit program should reflect only work required to be</p>

	<p>or not they are fairly stated.</p>	<p>wider “public sector” audit. Matters of probity, waste and accountability are an integral part of this audit.</p>	<p>undertaken to express an audit opinion on the financial statements as to whether or not they are fairly stated. This was also clearly the opinion of Agency’s interviewed as part of this review.</p> <p>Matters of probity, waste and accountability should fall within the gambit of the Compliance or Performance Audit Program and be subject to separate funding. Probity and waste issues do not impact on the audit opinion being formed as to whether financial statements are or are not fairly stated.</p>
	<p>RECOMMENDATION 59 (HIGH PRIORITY):</p> <p>As part of the audit planning process in each financial year, the Audit Office should provide detailed explanation to its clients as to how their audit fee has been determined.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>Agencies are provided with information in their annual client service plan as to how their fees have been determined.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. This is clearly an issue of communication. The majority of Agency’s interviewed as part of this review indicated that the Audit Office did not adequately explain how their financial audit fee had been determined for that respective financial year. Thus, the Audit Office needs to evaluate how it can provide more transparent and</p>

			<p>effective communication with Agencies when describing how financial audit fees have been set.</p>
	<p>RECOMMENDATION 60 (HIGH PRIORITY):</p> <p>Each Performance Audit Report should detail the costs to the Audit Office and to the Agencies involved in providing detailed assistance to the Audit Office as part of that review.</p>	<p>Not accepted.</p> <p>Disclosing the Audit Office’s cost of each performance audit provides Parliament with information as to how its funding is being utilised.</p> <p>While we may see the reasoning behind the suggestion to include agencies’ costs, this is not required for any other regulatory function in the public sector. Having to record costs would itself be a further imposition on agencies.</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. In terms of measuring the costs versus benefits of the end product, Parliament should be provided with a ‘true cost’ in relation to the conduct of the Performance Audit. Including the Audit Office costs is only one aspect of this area. Agency’s expend significant resources in assisting the Audit Office when a performance audit is conducted within their Agency. In a world of scarce and limited resources, this means that an Agency has to divert resources away from other projects that it has committed to Parliament to undertake/complete during a financial year. It is therefore believed that it would be appropriate for Parliamentarians to gain understanding of the impact on an Agency that has been subject to a Performance Audit.</p>

OUTSOURCING			
OS (1)	<p>RECOMMENDATION 61 (MEDIUM PRIORITY):</p> <p>It is recommended that the classification of agencies be reviewed to ensure that the criterion for establishing suitability for contracting out versus retention in house is fully documented and clear. In undertaking this review, regard should be had to the processes in place within other State and Federal Government jurisdictions in Australia for contracting out of audits (as a basis for comparison).</p> <p>It is also recommended that as part of this process the Audit Office determine a formal policy for how benchmarking of outsourced providers will be undertaken.</p>	<p>No additional action required.</p> <p>Our current policy document on the Contracting Out of Audit Services provides clear criteria and adequate classification of agencies for contracting out purposes.</p> <p>Our Benchmarking Task Force has established a program that includes the benchmarking of audit service providers. A deliverable of the Contracting Out Task Force is "A program for receiving and monitoring the success of the plan (ie contracting out). This will cover both the QA aspects and measure the achievement of the intended benefits".</p>	<p>Acumen Alliance does not accept the Audit Office response to our recommendation. As our report indicates, whilst there are criteria set for determining which Agencies could be contracted out, these criteria could be used to justify almost any level of contracting out without regard to efficiency and effectiveness.</p> <p>We were advised in our exit meeting for our draft report that the Auditor-General had set the rate of outsourced audits to be at a level of 10%. However, this level was entirely subjective and we could not see how it linked to the policy document on the Contracting Out of Audit Services.</p> <p>At the time of our audit, there was no formal policy setting out how the Audit Office would determine how benchmarking of outsourced providers would be undertaken, nor had any benchmarking activity been undertaken.</p>

<p>OS (2)</p>	<p>RECOMMENDATION 62 (HIGH PRIORITY):</p> <p>The Contract Management, Quality Control and Assurance Procedures be amended to ensure that all steps are made mandatory.</p>	<p>No additional action required.</p> <p>At the time of the Review, our Contract Audit Agents Manual (CAAM) was in the process of review. All steps suggested by Acumen were amended and given a mandatory status. Copies of the updated documentation were supplied to Acumen at the time of discussion of its draft report.</p>	<p>Acumen Alliance is not satisfied with the Audit Office response to our recommendation. At the exit discussions for our preliminary draft report in this area, we were promised copies of updated documentation, but these were not subsequently provided to us.</p>
	<p>RECOMMENDATION 63 (HIGH PRIORITY):</p> <p>All files for contracted out audits be reviewed to ensure that appropriate documentation is maintained to evidence that the required Contract Management, Quality Control And Assurance Procedures have been undertaken in all cases and accord with the CAAM and AUS 602.</p>	<p>No additional action required.</p> <p>Our Contracting Out Task Force annually reviews a selection of files for contracted out audits to ensure adherence to the established quality control and assurance procedures.</p> <p>Reference to AUS 602 is inappropriate since contractors are “agents” and not independent of us. Furthermore AUS 602 specifically refers to “uses the work of another auditor on the financial information of one or more</p>	<p>Acumen Alliance is not satisfied with the Audit Office response to our recommendation. The files reviewed by Acumen Alliance during this review did not contain evidence to indicate that files for contracted out audits were actually reviewed to ensure adherence to the established quality control and assurance procedures. This would indicate that the Contracting Out Task Force annual reviews of a selection of files may not be effective.</p>

		components included in the financial report of the entity" ie it does not relate to whole audit engagements where the principal auditor is able to direct and control the secondary auditor.	AUS 602 was provided as guidance only. We also note the requirements of the Institute of Chartered Accountants that requires the signing auditor to ensure that all staff used on an audit have sufficient skills and qualifications and are properly reviewed and quality assured during conduct of the audit.
	<p>RECOMMENDATION 64 (HIGH PRIORITY):</p> <p>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.</p>	<p>Accepted in part.</p> <p>This is already undertaken for individual audits. This will now be consolidated annually.</p>	<p>The sample of files selected by Acumen Alliance during our review indicated that formal assessment of the outsourced providers work had not been done. We are pleased that this is now to be undertaken formally and consolidated annually.</p>
	<p>RECOMMENDATION 65 (HIGH PRIORITY):</p> <p>The Audit Office should undertake a formal overall analysis of its outsourcing program to determine that work conducted by outsourced audit providers is satisfactory and that</p>	<p>No additional action required.</p> <p>See response to Recommendation 64.</p>	<p>No further comment.</p>

	issues identified by individual audit managers are satisfactorily dealt with and used by senior management for evaluation of the program.		
OS (3)	<p>RECOMMENDATION 66 (HIGH PRIORITY):</p> <p>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.</p>	<p>Accepted.</p> <p>A database of possible outsourced audit clients is now maintained which records full particulars on current and potential audit service providers. The database will in future provide full reasons for rotation of clients as well as particulars on partner/manager engagement periods. Periodic review of the database by the Task Force should ensure that audit partner rotation etc is appropriate.</p>	No further comment.
PERFORMANCE MEASUREMENT			
PM (1)	There are no recommendations for this finding.		
PM (2) & PM(3)	<p>RECOMMENDATION 67 (HIGH PRIORITY):</p> <p>As part of its continuous improvement process the Audit Office should review</p>	Accepted in part.	No further comment.

	and expand the nature and detail of its performance indicators, given the outcome of our analysis above.	<p>We support the concept of greater accountability and will continue to review our performance indicators and expand as appropriate.</p> <p>We already review what other Audit Offices report and are working with them to make published indicators more comparable.</p>	
	<p>RECOMMENDATION 68 (HIGH PRIORITY):</p> <p>Performance indicators, including input/output efficiency, should be strengthened by division into key outputs – Financial Audit, Compliance Audit and Performance Audit.</p>	<p>No additional action required.</p> <p>The Audit Office reports a number of measures externally for the Office overall. For internal purposes, we measure and report on a number of indicators in each of the Financial Audit, Performance Audit and Corporate Services Branches.</p> <p>We will continue to review our performance indicators as part of the ACAG benchmarking exercise.</p>	<p>It is our opinion that splitting Key Performance Indicators’s into the three key output areas is best practice. Such a practice promotes greater accountability and enables the Parliament to more effectively analyse performance across the three key program areas of the Office. It also is imperative for the Audit Office to recognise and demonstrate to the Parliament that they have three distinct products.</p>
	<p>RECOMMENDATION 69 (MEDIUM PRIORITY):</p> <p>The NSW Audit Office should continue to work with ACAG to produce comparable benchmark</p>	<p>No additional action required.</p> <p>The recommendation confirms the</p>	<p>No further comment.</p>

	produce comparable benchmark information.	position the Office has already taken. The Audit Office has always strongly supported the work of ACAG in producing benchmark information.	
PM (4)	There are no recommendations for this finding.		
QUALITY ASSURANCE			
QA (1)	RECOMMENDATION 70 (HIGH PRIORITY): Review of QARC operation and resourcing be finalised as soon as possible and the Practice Manual be updated accordingly.	Accepted. The review of QARC's operation and resourcing is one aspect of a more comprehensive review of the quality assurance framework throughout the Office.	No further comment.
	RECOMMENDATION 71 (MEDIUM PRIORITY): Quality Reviews should occur as soon as possible after completion of the financial audit cycle, eg in the Nov-Dec period for June year ends. This ensures any outcomes/issues flowing from the reviews can be addressed at the planning stage for the next years financial audit.	No additional action required. The recommendation confirms the position the Office has already taken. Acumen does not understand the timing of our financial audit cycle. Because of our reporting	We do not accept the Audit Office response to our recommendation. The audit cycle is not the issue in this case, better practice is. Resources should be made available to ensure on-going review, including 'hot reviews' of files during the Financial Audit process.

		obligations to Parliament, audits are not generally completed until late November. However our quality reviews are undertaken in time for outcomes/issues to be incorporated in the following year's audit.	The current timing of the quality assurance process (April/May) does not occur with sufficient time, in the opinion of Acumen Alliance to ensure outcomes/issues can be addressed at the planning stage for the next years' financial audit.
	<p>RECOMMENDATION 72 (HIGH PRIORITY):</p> <p>The Quality Review framework used by the QARC should ensure comprehensive coverage of all aspects of an audit including efficiency and effectiveness considerations and the rationale for all audit work undertaken.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>The quality review framework already covers efficiency, effectiveness and the rationale for all audit work undertaken.</p>	<p>We do not accept the Audit Office response to our recommendation. As we have noted in our report, the mini QARC's that were run did not include comprehensive coverage of all aspects of an Audit including efficiency and effectiveness considerations.</p>
	<p>RECOMMENDATION 73 (HIGH PRIORITY):</p> <p>Consideration should be given to the performance of "hot reviews" as a method of providing quality review assurance immediately prior to sign off on a selection of financial audits. Such hot reviews should be undertaken by an Assistant Auditor-General who is independent of the financial audit</p>	<p>No additional action required.</p> <p>Reviews are already undertaken on a range of larger and higher risk audits by appropriately skilled people, often an Assistant Auditor-General. These reviews are conducted throughout the audit. This provides a superior level of</p>	<p>The response by the Audit Office is accepted in part. By 'hot review' we mean reviews by an Assistant Auditor General independent of the financial audit being conducted. We were advised during our review that this did not occur. We agree that such a review is too late once the Financial Audit is at the stage</p>

	being conducted.	quality assurance than a simple "hot review" immediately prior to signing the audit opinion.	where the audit opinion is about to be signed. The 'hot review' process should also be encapsulated in QARC reviews and continuous improvement processes.
QA (2)	<p>RECOMMENDATION 74 (HIGH PRIORITY):</p> <p>Consideration be given to returning responsibility for the QARC to the Policy and Research Branch. This will help ensure the nexus between quality review findings and their impact on methodology is maintained and provide a Chinese wall between the audit function and the quality review process.</p>	<p>Not accepted.</p> <p>The Audit Operations Committee (the Deputy and Assistant Auditors-General) is responsible for quality review findings and their impact on the methodology. This responsibility recognises that it is important there be a nexus between an understanding of the methodology itself, its application, the results of its application, and quality review findings.</p>	<p>The rationale for our recommendation is based on our professional opinion as to where responsibility for the QARC process should be, based on transparency and independence. Accordingly, we do not accept the response to our recommendation by the Audit Office.</p>
	<p>RECOMMENDATION 75 (HIGH PRIORITY):</p> <p>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</p>	<p>Accepted.</p>	<p>No further comment.</p>

	<p>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.</p> <p>This process should ideally be reported through the Audit Committee.</p>		
QA (3)	<p>RECOMMENDATION 76 (MEDIUM PRIORITY):</p> <p>Consideration should be given to the performance of a regular Quality Review under the auspices of ACAG (similar to those which occurred in WA and New Zealand) or from a third party under the frameworks provided by the Institute of Chartered Accountants and Australian Society of CPA's. This will assist in better practice benchmarking.</p>	<p>No additional action required.</p> <p>As Acumen was aware, this was already on our Internal Audit program, but had been deferred pending completion of this triennial review.</p>	<p>Acumen Alliance were not aware of the ACAG review and it was not on the plan provided to us during this review by the Audit Office. During our exit interview we were led to believe by the Audit Office that this process was not currently occurring.</p>
QA (4)	<p>There are no recommendations for this finding.</p>		

REPORTING TO PARLIAMENT - EFFICIENCY			
RP (1)	<p>RECOMMENDATION 77 (HIGH PRIORITY):</p> <p>As part of the Auditor General's own continuous improvement process, consideration should be given to assessing whether information included in his reports to Parliament could be further streamlined, avoiding duplication.</p>	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>There is no evidence that Parliamentarians find the current coverage excessive. However, we continually monitor the contents and quality of the Reports to Parliament.</p>	<p>This recommendation was made based on our review of current Audit Office practices and our opinion that further streamlining was possible. At the time this review was undertaken the most recent Parliamentary Satisfaction Survey that had been undertaken did not provide sufficient responses to be able to draw conclusions about the satisfaction level of Parliamentarians.</p>
RP (2) & PA (6)	<p>RECOMMENDATION 78 (MEDIUM PRIORITY):</p> <p>Subsequent to legislative backing, the Auditor-General facilitate establishment of a high level Committee with the Department of Treasury and the Premier's 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</p>	<p>Accepted in part.</p> <p>We have already raised the need for a performance indicator framework in at least three reports to Parliament and have written to the Premier twice on this matter.</p> <p>We would be fully prepared to assist the central agencies on this issue but responsibility lies clearly</p>	<p>No further comment.</p>

	<p>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.</p>	<p>with Executive Government.</p> <p>If the framework is established and the Auditor-General given the mandate to audit performance indicators, then our Reports to Parliament would include the type of comments suggested by Acumen.</p>	
<p>RP (3)</p>	<p>RECOMMENDATION 79 (HIGH PRIORITY):</p> <p>The decision of the Auditor-General to undertake a new survey of Parliamentarians subsequent to the State Election, with results to be reported by 30 June 2003 is supported. The survey should include questions such as whether:</p> <ul style="list-style-type: none"> ➤ the content of the reports was easily understood; 	<p>No additional action required.</p> <p>The recommendation confirms the position the Office has already taken.</p> <p>The survey was undertaken in May/June 2003.</p>	<p>No further comment.</p>

	<p>easily understood;</p> <ul style="list-style-type: none"> ➤ the relative importance of issues raised in the report was clear; and ➤ relevant issues had been chosen to report. <p>It is also suggested that the Auditor-General run workshops and structured interviews with Members of Parliament.</p>		
	<p>RECOMMENDATION 80 (HIGH PRIORITY):</p> <p>A formal review of costs that are accumulated by staff to the Reports to Parliament, by client and overall, be undertaken prior to the issue of each bill to ensure they appear reasonable.</p>	<p>No additional action required.</p> <p>A formal review of costs by client and overall does occur.</p>	<p>We do not accept the response to our recommendation. No evidence was provided during our review to demonstrate that this process was performed.</p>
RP (4)	<p>RECOMMENDATION 81 (HIGH PRIORITY):</p> <p>Through the results of the parliamentarians questionnaire follow up on the impact of changing the scope of reporting. Consider cost reduction initiatives including:</p>	<p>Not accepted.</p> <p>See our response to Recommendation 80.</p>	<p>This recommendation was made based on our review of current Audit Office practices and our opinion that further streamlining and cost savings were possible. At the time this review was undertaken (Jan to March 2003) the most recent Parliamentary</p>

	<ul style="list-style-type: none"> ➤ Reporting by exception only; ➤ Reporting through the Statutory Audit Reports; or ➤ Reporting on a Ministerial basis only. 		<p>Satisfaction Survey that had been undertaken did not provide sufficient responses to be able to draw conclusions about the satisfaction level of Parliamentarians. If the survey that was conducted in May/June provides sufficient responses to be able to draw appropriate conclusions then this recommendation should be addressed.</p>
EXPECTATIONS ON REPORTING			
ER (1)	There are no recommendations for this finding.		
ER (2)	<p>RECOMMENDATION 82 (MEDIUM PRIORITY):</p> <p>Once the expectations of users have been formally ascertained a gap analysis be undertaken to reconcile expectations against current reporting.</p>	<p>No additional action required.</p> <p>Our surveys of Parliamentarians and clients already address the usefulness of our reports.</p>	<p>We do not accept the Audit Office response to our recommendation. If the survey of Parliamentarians conducted during May/June has drawn sufficient responses to allow meaningful conclusions to be drawn then a gap analysis should, in our opinion, be undertaken.</p>

4 Financial Audit

INTRODUCTION

Under the Public Finance & Audit Act 1983 the New South Wales Auditor General is responsible for the provision of an independent opinion on the prescribed (under Div 4, Part 3 of the Act) NSW Government Agencies financial reports.

Under Part 3 Audit, Div 1 27B(4) “the Auditor-General may exercise his or her functions in such a manner as the Auditor-General thinks fit. However, the Auditor-General is required:

- a) to have regard to recognised professional standards and practices, and
- b) to comply with any relevant requirements imposed by law.”

To this end the Audit Office has adopted all Australian Auditing and Assurance Standards as issued by the Auditing and Assurance Standards Board of the Australian Accounting Research Foundation (AUS). AUS 202 “Objectives and general principles governing an audit of a financial report” states “the objective of an audit of a financial report is to enable the auditor to express an opinion whether the financial report is prepared, in all material respects, in accordance with an identified financial reporting framework.”

Parliament has determined that the identified reporting framework for NSW Public Sector agencies should be:

- Applicable Accounting Standards and other mandatory professional reporting requirements; and
- Statutory provisions relating to the form and content of the financial report.”

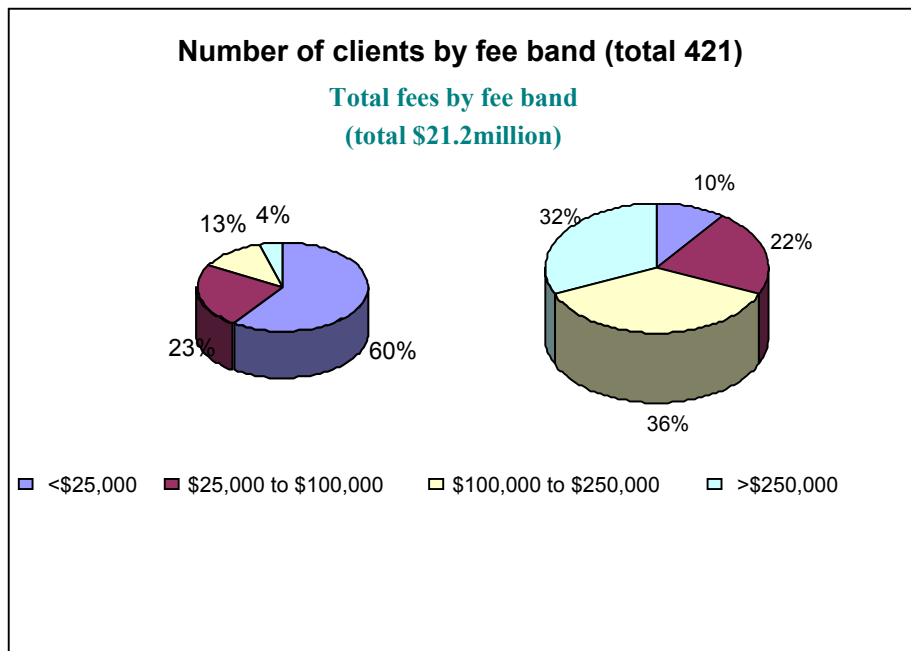
AUS 106 provides an “explanatory framework for standards on Audit and Audit related services”. Importantly it notes that in relation to an audit, the level of assurance “is designed to provide a high but not absolute level of assurance on an accountability matter. The auditor expresses this as reasonable assurance in recognition of the fact that absolute assurance is rarely attainable due to such factors as the need for judgement, the use of testing, the inherent limitations on internal control and the fact that much of the evidence available to the auditor is persuasive rather than conclusive in nature.”

FINANCIAL AUDIT BRANCH

Financial Audit Reports were issued on 421 Government agencies during the 2001-02 year. The majority of audits are conducted by staff from the Financial Audit Branch of the Audit Office. Where necessary in house resources are supplemented by contract audit staff during the busy May-September period. In addition, a number of financial audits are outsourced to Independent Contract Audit Agents (see section on outsourcing).

During 2001-2002 the Financial Audit Branch was reorganised under nine industry groups, with similar risk profiles, dealing with similar government clients. At 31 December 2002 the Financial Audit Branch had 150 FTE staff including 17 staff with the delegation to sign audit opinions, in the Director and Assistant Auditor General category. The Financial Audit Branch are supported by Information Systems Audit (12 FTE staff) and Policy and Research (5 FTE staff).

Total fees for financial audit for 2001-2002 amounted to \$21.2 million, of which \$1.7 million was paid to the contract audit agents. An analysis of the number of audit clients and fees is as follows:



FA (1) – WHETHER THE AUDIT OFFICE HAS ADEQUATE AND APPROPRIATE METHODOLOGIES, PRACTICES AND PROCEDURES.

FINDINGS:

AUDIT METHODOLOGY AND TECHNOLOGY

The Audit Office uses the SAGE (System for Auditing Government Entities) methodology, combined with an automated technology tool called “AS2”, as the core basis for all of the financial audits performed in house. Where financial audits are outsourced then the providers use their own methodology.

The Audit Office’s External Audit methodology, SAGE, was purchased from Deloitte Touche Tohmatsu in 1997. This methodology was customised by the Office to meet the requirements of public sector audit. The initial licence and support contract was for a period of five years with two one year options. The Audit Office is currently in the first option year and we are advised that it will be exercising the second. The methodology is supported by automated working papers, technology known as AS/2.

The Audit Office has an Audit Practice Manual. The Audit Practice Manual is maintained online by the Policy and Research Branch and contains all policies and procedures staff are required to follow when conducting financial audits. Staff are informed of updates to the manual and methodology through numerous mechanisms including email, technical updates, user forums etc.

SAGE is a risk based audit methodology and it focuses on a risk analysis and evaluation of the controls surrounding core business cycles during the planning phase. Audit plans developed using the methodology direct the conduct of work and the results feed up into the audit reporting and completion stage. In addition, the automated working papers provide an inbuilt quality assurance mechanism to test the integrity of the audit file data and whether quality aspects of the audit file and its contents have been satisfied.

The AS2 automated working papers support three types of audit pack for Large, Small and Very Small entities. The working papers provide a standard file structure with a number of embedded forms which require consideration and completion.

Key forms feed up into one another to help ensure the integrity of the system. Updates and changes to AS2 automated working papers are processed by Deloitte Touche Tohmatsu and are then tested through the Information Systems Audit Branch in the Audit Office before release.

Audit methodologies have varied over the years in the Auditing Profession. Consolidation of the large accountancy firms has resulted in refinements or changes to audit methodology and technology, with the aim of increasing audit efficiency and information management through automation where possible. In addition, in light of recent corporate collapses it is the belief of the Review Team that the major firms may have reviewed their audit processes.

During discussions with the Audit Office, views were expressed to the Review Team that the Deloitte Touche Tohmatsu AS/2 automated working papers were considered to be the best currently available on the market. The Audit Office clearly stated that they kept abreast of changes in the auditing profession in this regard and were not aware of any other product that would provide similar or better functionality and efficiency than the product currently being utilised. The Review Team also notes that the Audit Office has already put in place an arrangement with Deloitte Touche Tohmatsu that will enable it to use SAGE and AS/2 on the same terms and conditions after the expiry of the second option year.

PRACTICES AND PROCEDURES

The Audit Office Practice Manual provides the main source of Audit Office policy and guidance for use in the planning and performance of audit engagements. It was first introduced in its current form for the financial reporting periods ending on or after 30 June 1999. The manual is kept in electronic form on a shared drive, with any updates being controlled through the Policy & Research Branch and notified to staff via email.

The Audit Office Practice Manual details policy and guidance for use in the planning and performing of audit engagements. SAGE provides the methodology for use on audits. Both documents comply with the Professional Auditing Standards, which provide the overall framework for the conduct of Audits.

The Audit Office Practice Manual outlines the adoption by the Audit Office of all Australian Auditing and Assurance Standards, including a requirement that Financial reports prepared by Agencies and subject to audit by the Audit Office are prepared under the terms of the Public Finance & Audit Act 1983.

The Review Team believes that the practice manual provides comprehensive guidance on the framework and implementation of the financial audit role of the Audit Office.

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.

FA (2) – WHETHER THE AUDIT OPINIONS ISSUED BY THE OFFICE COMPLY WITH APPLICABLE PROFESSIONAL STANDARDS AND PRACTICES.

FINDINGS:

Audit Office clients receive both a Statutory Audit Report (SAR) and an Independent Audit Report (IAR). The SAR provides a detailed analysis of the organisation audited including analysis of financial results and matters requiring management attention. The IAR represents the independent opinion on the organisations financial statements as to whether or not they are fairly stated.

Under the Public Finance & Audit Act 1983 the Auditor-General or delegated officer is required to report to the Treasurer, Minister and the Head of the Organization, as to the results of any inspection or audit and as to such irregularities or other matters that call for special mention. Thus the SAR provides the opportunity to report major issues that have arisen during an audit. The SAR is issued at the same time as the IAR.

The IAR is addressed to the members of the New South Wales Parliament. The structure of the IAR is in accordance with AUS702 “Audit Report on a General Purpose Financial Report” and other applicable professional standards and practices.

The Audit Office has recently introduced a plain English IAR. This revised plain English report is more user friendly by starting off with the Opinion and includes more detailed discussion on the role of audit and management in relation to the financial statements. This plain English IAR is in accordance with the Australian Auditing Standards.

QUALIFIED AUDIT OPINIONS

During the period from 9 November 2001 to 5 November 2002 the Audit Office issued twenty one qualified audit opinions, nineteen of these were of an “except for” nature. This was a reduction on the qualifications issued in previous years.

“Except for” opinions occur when the auditor concludes that an unqualified opinion is inappropriate because of a disagreement with management, a conflict between applicable financial reporting frameworks or a scope limitation, the effects or possible effects of which are not of such a magnitude or so pervasive or fundamental as to require the expression of an adverse opinion or an inability to form an opinion.

Other types of qualified opinion include “Adverse opinions” or an “inability to form an opinion”. Adverse opinions occur when the effects of a disagreement with management or a conflict between applicable financial reporting frameworks is of such a magnitude or is so pervasive or fundamental that the financial report taken as a whole is, in the opinion of the auditor, misleading or of little use to the addressee of the audit report. An inability to form an opinion is expressed when a scope limitation exists.

The AO has well developed procedures in relation to the issue of qualified opinions or “modified audit reports”. These include consideration by the Engagement Controller, Engagement Reviewer and Policy and Research Branch, prior to review by the Modified Audit Report Panel. The Modified Audit Report Panel consists of the Deputy Auditor General and Assistant Auditor-Generals from each Financial Audit Business Unit. They provide a final recommendation to the Auditor-General, who signs all such reports.

Our sample of clients interviewed (twenty Agencies were interviewed as part of this review) included a number who had received modified IAR’s on their financial statements. Concerns were raised by client management about the validity of some qualifications, one being in the light of conflicting advice received from professional accounting firms, which supported the accounting treatment of the item subject to qualification. In this case the issue was discussed by the Auditor General in his report to Parliament *and was in the opinion of the Review Team addressed appropriately.*

We reviewed a number of the modified IAR’s issued by the Auditor-General in 2002 and confirmed compliance with Audit Office internal procedures. It must be noted of course that where qualifications concern the interpretation of applicable Accounting Standards decisions are not always black and white. The level of accountability which the Auditor-General is aiming to achieve through current review processes for qualified audit opinions is sound and aimed at ensuring all due consideration is given to differing opinions prior to determining that the qualification is valid and appropriate.

RECOMMENDATION 2 (LOW PRIORITY):

The Review Team supports the Audit Office in its recent move to using plain English IAR’s. However, it is recommended that the Audit Office continue to monitor developments in Audit Reporting within the wider profession and where appropriate review and revise the wording of its IAR’s.

FA (3) – WHETHER THE AUDITS ARE SUPPORTED BY ADEQUATE WORKING PLANS, WORKING PAPERS, APPROPRIATE AUDIT EVIDENCE AND APPROPRIATE QUALITY CONTROL PROCEDURES.

FINDINGS:

As part of our work we undertook a detailed review of a sample of Audit files in relation to audits undertaken by the Audit Office. Our sample covered a range of agencies both small and large across different portfolios. The methodology used for our review was based on the quality assurance audit tools used by the Institute of Chartered Accountants in Australia.

Our review of audits during this review indicated that audits conducted by the NSW Audit Office are adequately planned and contain sufficient working papers and audit evidence to support the audit conclusions drawn.

AUDIT PLANNING:

The planning process inherent within the AS2 technology provides a comprehensive test basis for the development of a structured audit plan based on an assessment of risk across various account balances.

AUDIT EVIDENCE:

Audit evidence is documented through a mixture of embedded workpapers, word documents, excel spreadsheet and client prepared schedules.

QUALITY CONTROL:

The detailed quality control process is generally the responsibility of the Engagement Manager, with the Engagement Controller providing an overview role. On more complex audits a second independent review is undertaken by an Assistant Auditor General. These roles and responsibilities are set out in the Audit Office Practice Manual. The issue of quality assurance is considered in later sections of our report.

There are no recommendations for this finding.

FA (4) – WHETHER THE AUDITS ARE APPROPRIATELY PLANNED AND CO-ORDINATED, HAVING REGARD TO AGENCIES’ INTERNAL AUDIT AND TECHNOLOGY INSIDE THE AUDIT OFFICE.

FINDINGS:

USE OF INTERNAL AUDIT

The role of many Agencies Internal Audit functions have changed over recent years, often moving away from pure financial compliance work to more efficiency and effectiveness reviews, which are seen as providing more value to management. This has had an adverse affect on the level of reliance External Auditors can place on the work of Internal Audit.

The approach to reliance on the work of Internal Audit is outlined in the Audit Office’s Audit Practice Manual. It incorporates the requirements of the relevant profession standards.

As part of our detail review of financial audits we considered whether those audits had been properly planned and coordinated in regard to respective Agencies Internal Audit. In addition, we reviewed 20 AS2 audit files for financial statement audits conducted during the financial year ended 30 June 2002 to assess whether reliance on Internal Audit had been considered and how it had been assessed.

Internal Audit plans or the minutes of meetings were generally appended to the AS2 files in manual or automated format. In addition, on a number of the files for larger jobs a “Preliminary Assessment of the Internal Audit Function Form” was completed. However, there was little evidence of any detailed consideration of Internal Audit activity across each of the business cycles subject to financial statement review, as reviewed through AS2.

The majority of Audit Office clients interviewed as part of this review indicated that they were not aware of the Office making any use of their Internal Audit functions, nor how the use of Internal Audit may have affected their respective financial audit fees. This included a lack of co-ordinated approach between Internal and External Audit to ensure that areas of common interest were recognised and not over/under audited.

It is the belief of Acumen Alliance that there is a general lack of overall analysis of how Internal Audit may be used and the resultant reduction in required external audit work that may be achieved (including a reduction in external audit fees).

USE OF TECHNOLOGY INSIDE THE AUDIT OFFICE

AS2 provides the principal technology platform utilised by the Audit Office in the conduct of its Financial Audits. All audits use the AS2 automated working papers as a method of file control and to ensure audit integrity, using the various size of AS2 packs available.

During our detailed review of audit files we considered the conduct of audits and whether full reliance was placed on the use of the automated working papers or whether there was still a strong reliance on the use of manual audit working papers.

The use of Audit office technology varies greatly between jobs. In particular the automation of workpapers (and client prepared schedules) to improve audit efficiency is variable. This can be most easily indicated by the amount of hard copy working papers currently used to support audits (i.e. the more hard copy documentation on file the less efficient the process).

Acumen Alliance understands that the Auditor-General is aware of these differences in approach and has scheduled in his Internal Audit plan a review of the efficiency and effectiveness of the automated working papers.

In addition, the use of the AS2 automated working papers may result in additional costs being incurred in the completion of small and very small audits, due to the number of forms requiring completion to ensure the integrity of the system. This could have an impact on the current review of reporting requirements for small agencies being undertaken by the Public Accounts Committee. We believe this issue should be encompassed in the forthcoming review of SAGE / AS2 audit efficiency, included in the Internal Audit plan.

RECOMMENDATION 3 (HIGH PRIORITY):

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 an 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.

RECOMMENDATION 4 (HIGH PRIORITY):

Each engagement manager should ensure there is a focus on automating work papers, including client prepared schedules. This includes preparation of lead sheets and supporting schedules in spreadsheets to enable import into AS2. Similarly export of management reports into spreadsheets to enable easy analysis and incorporation into the AS2 files should be considered.

This initiative would be enhanced through review and tailoring of the "client assistance schedules" to encourage use of electronic working papers.

RECOMMENDATION 5 (HIGH PRIORITY):

It is understood that the Audit Office intends to conduct a review of the use of SAGE and AS2 during the period January to March 2004. Acumen supports this review and also recommends that this review include specific consideration of the application of AS2 to small and very small clients.

NSW GRAINS BOARD FINANCIAL AUDIT

BACKGROUND:

During scoping discussions for the Triennial Review of the Audit Office of NSW, the Public Accounts Committee requested Acumen Alliance to review the financial audit working papers for the NSW Grains Board for the year ended 31 August 1999.

It is our understanding that this request was made by the Public Accounts Committee to enable them to determine whether:

- The financial statement audit of the NSW Grains Board for the financial year ended 31 August 1999 had been undertaken in accordance with the Public Finance and Audit Act 1983, internal policies and procedures of the NSW Audit Office and in accordance with professional auditing standards; and
- The underlying audit working papers supported the conclusions reached by the Auditor-General to issue an unqualified audit opinion on the financial statements of the NSW Grains Board for the financial year ended 31 August 1999.

Acumen Alliance also understood that the Public Accounts Committee wished to identify, where any shortcomings had been identified in the planning, conduct or conclusion of the audit, what action the NSW Audit Office had taken to improve and review its practices.

In his report to Parliament in 2002², the Auditor General provides a detailed summation of NSW Grains Board situation. In this summation he states:

"In April 2001 the Administrator wrote requesting our audit workpapers and documents on the Grains Board to assist his investigations into any potential recovery of monies.

Based on earlier legal advice on Section 38 of the Public Finance and Audit Act 1983 from the Crown Solicitor, we advised the Administrator that we were prohibited from providing or communicating the contents of working papers and other documents. Section 38 obliges us to preserve

² Auditor-General's Report to Parliament 2002, Volume Six, Pages 81-82.

secrecy with respect to all matters that come to us in the exercise of our functions.

In July 2002 the Administrator repeated his request for audit workpapers to be provided. He advised us that the Minister for Agriculture had authorised him to conduct examinations of Audit office staff and that production of the workpapers would serve the public interest and would be required if examinations or other measures were taken. Again the Administrator was told that our legal advice was that we would be breaking the law if we disclosed such information.

Notwithstanding, the Administrator commenced an 'originating process' under the Corporations Law to summon Audit Office staff and gain access to audit workpapers. The Administrator's affidavit to the NSW Supreme Court argued that the secrecy provisions of the Act were not an appropriate basis for the Court to refuse the examination orders he was seeking. The Audit Office challenged this originating process.

On 3 October 2002, the Court dismissed the Administrator's originating process. It found that the secrecy provisions of the Act prevented us disclosing audit information.

In late October 2002 the Administrator requested certain documents other than audit workpapers that he could not find. The Crown Solicitor has advised that we are able to provide some documents to the Administrator if they are documents originally supplied or received from the Grains Board."

COMMENTARY:

During conversations between Acumen Alliance, the Auditor-General and the Deputy Auditor-General on 9 February 2003, access to the audit working papers for the NSW Grains Board for the financial year ended 31 August 1999 for the purposes of this review were requested.

As a result of this request, the Auditor-General wrote to Acumen Alliance on 10 February 2003 stating his concerns with provision of these files. These concerns included:

- A belief that nothing in the Terms of Reference for our review would seem to have called for a review of the Grains Board files;

- That the audit of the Grains Board was undertaken during the period covered by the previous triennial review and that it was believed that Parliament's intention in legislating for the triennial reviews was that they were to cover sequential periods and not be open ended; and
- That were Acumen Alliance to review the audit working papers – whether or not any disclosure or comments were subsequently made in our report to the Public Accounts Committee – that review could well become the subject of contention in any future litigation that may be undertaken against the NSW Audit Office by the Administrator of the Grains Board.

On 11 February 2003, Acumen Alliance responded in writing to the Auditor-General setting out additional reasons as to why we believed we should be provided with access to the audit files.

The Auditor-General responded in writing to our request on 13 February 2003 and included legal advice that he had obtained from the Crown Solicitor. This advice clearly stated that:

- Acumen Alliance did not have the power under Section 48A of the Public Finance and Audit Act 1983 to undertake a review of compliance with auditing practices and standards in a period covered by a previous Section 48A review.

As we have not had access to the audit working papers for the NSW Grains Board for the financial year ended 31 August 1999 we are unable to provide any opinion or comment on the conduct of the audit by the NSW Audit Office, nor whether there are issues/matters that could be considered 'endemic' problems with the audit processes and procedures used the Audit Office that may impact upon the conduct of other financial audits by the Office.

There are no recommendations for this finding.

5 Compliance Audit

INTRODUCTION

The Compliance Audit Group (CAG) is integrated within the Financial Audit Branch of the Audit Office. In recent years the approach to compliance audits has changed, with the current focus being undertaking a range of audits, performed across a sample of Agencies that covers legislation, internal policy and directions issued by the central agencies such as Treasury and Premiers.

Depending on the nature of the compliance reviews they are undertaken by dedicated staff or as part of the financial audit process.

Ten compliance audit review reports were issued during 2001-2002 covering areas as diverse as Credit Card Use and the Operation of Audit Committees. An overall report is produced together with reference in individual agency reports in the Auditor-General's reports to Parliament.

A summary of the reviews undertaken over the last three years is given in the table below (source CAG audit manual and program 2002-03):

1999-2000	2000-2001	2001-2002
PSM Act and Regulations	Superannuation	Audit Committees
CEO Contracts	Credit Card Usage	Government Owned Training Facilities
Core Business	Delegations	Public Authorities (Financial Arrangements) Act
Special Deposit Account	Fines & Penalties	GST
Year end Transactions	Extended Leave	State Records Act
Academic Leave (Universities)	Fully Depreciated Assets	Donations and Bequests
	Fleet Operations & Fuel Card Usage	Annual Reports
	Financial Reporting Requirements	Legislation

BACKGROUND TO COMPLIANCE AUDIT

PLANNING

Currently a plan for the annual Compliance Audit Program is presented for approval to the Audit Operations Committee of the Audit Office in September each year. Following approval by the Committee the annual Financial Compliance Audit Manual and program is developed, together with detailed Audit Practice Guides (APG) for each review. The APG's detail the audit approach and testing plans to be undertaken.

Topics for review are generally chosen from a running list of areas. Thirty five topics were listed for the 2002-2003 program, varying between items such as Corporate Governance, to Taxation – GST and Annual Reports. In addition there were sixteen “across the board” reviews such as Use of Cabcharge, Mobile phones and Major Contracts. Across the board topics tend to focus on a specific type of transaction, where problems have been reported. Topics are identified by Audit Office staff or through requests from central agencies, examples of which included the 2002 State Records Act review and a planned Employer Superannuation Contributions review for 2003.

It is noted by the Review Team that an “Integrated Planning Approach” is currently being co-ordinated by the Assistant Auditor-General, Performance Audit and that when this approach is introduced it will allow greater input for compliance work from Parliamentarians and Agencies.

Whilst a Government Wide Risk Analysis is undertaken by the Audit Office with respect to financial audit, there is no direct linkage between this risk assessment and topic selection for the Compliance Audit program.

Of the thirty five topics suggested for the Compliance Audit Program for the financial year ended 30 June 2003, ten reviews have been chosen to be undertaken including two for Universities. To ensure appropriate coverage for each review with the limited resources available a sample basis is chosen for each review, which varies between 5 and 15 Agencies for the current year. Only Agencies where there is considered to be a risk of non-compliance are included in the chosen sample and these risks are as advised by Engagement Controllers.

Current Audit Office policy is for at least one compliance review to be undertaken annually in all medium and large agencies, with two of these in the top 49 agencies. If reviews are not allocated to an Agency as part of the Compliance Audit Program, then it is up to the Engagement Controller responsible for the financial audit of that Agency to nominate an appropriate area from the current or previous years CAG program, or an agency specific review, to be undertaken and reported as part of the audit process for that Agency.

RESOURCING

Compliance reviews are normally undertaken by the Financial Audit teams using the specially prepared APGs. Training/Information sessions are held for financial audit staff where this is considered necessary.

The Compliance Audit Group undertake some reviews using a team put together from financial audit staff based on the nature of the review and specific areas requiring detailed knowledge.

Staff charge time to specific audit clients on which they are conducting compliance reviews or a general compliance audit code when planning and consolidating the reviews. The Audit Office estimated the total cost of the compliance audit program to be \$0.562 million for the 2001-02 financial year. More detailed consideration of the costs of the Compliance Auditing Program are assessed in the Costs and Charges section of this report.

Agencies are advised of the Compliance reviews through their Client Service Plans.

REPORTING

Reporting is through general or specific management letters, together with commentary in the Auditor General's Report to Parliament on the Agency.

In addition a consolidated report is presented in the Auditor General's Report to Parliament. Responses to the draft consolidated report are normally sought from Treasury and/or Premiers as the areas responsible for policy/legislation, and incorporated into the final report.

A summary of compliance reports are also emailed to Agency heads.

As part of our review process we undertook a detailed review of a selection of Audit Office compliance audits together with discussion with Office clients on their views of the Compliance Audit Program.

In general we found that the Compliance Audit process appears sound.

CA (1) - WHETHER THE AUDITOR - GENERAL SHOULD DEVELOP AN INTERNAL STANDARD FOR COMPLIANCE AUDITING OR, ALTERNATIVELY, WHETHER THE AUDITOR-GENERAL SHOULD JOIN WITH OTHER PUBLIC SECTOR AUDIT AGENCIES AND DEVELOP A COMPLIANCE AUDITING STANDARD THAT WOULD APPLY ACROSS AUSTRALIA.

FINDINGS:

Whilst there are professional auditing standards dealing with audits issued by the Australian Accounting Research Foundation and extensive standards for the conduct of Internal Audit issued by the International Institute of Internal Auditors, there is no formal standard relating to Compliance Auditing at this time. Exposure Draft 30: Compliance Auditing was issued in 1989 and remains the main guidance in Australia. Its definition of compliance auditing is “a systematic examination by an independent party of some or all of an entity’s policies, organisational structure, operations, information system and other information contained in its external reports, for the purposes of establishing whether the entity has complied with the specific conditions which govern its activities including the legality and control of operations and the probity of those dealing with the funds of the entity.....”³

The exposure draft goes on to provide guidance on the responsibility of management, applicability of other Auditing standards, audit scope and reporting.

The Australian Accounting Research Foundation (“AARF”) has had the review of a Compliance Auditing Standard on its agenda for more than two years, with an impetus being on Auditor General’s to assist in its development, as they would be the key users, due to the level of compliance auditing undertaken in the various jurisdictions. The current NSW Auditor-General is a member of the Australian Auditing and Assurance Standards Board (AusASB) one of the two professional boards of AARF.

Research in this area by Acumen Alliance, discussions with the Auditor-General and interviews with a number of Audit Office clients during this review raised the following issues:

³ Auditing Exposure Drafts ED 30, Australian Accounting Research Foundation, 1989.

- It would be expected that in setting a standard for Compliance Auditing, that the Board would –
 - a) Define what is expected to be achieved through the Compliance Audit Process;
 - b) How the auditor is to scope, conduct and report on the results of a Compliance Audit;
 - c) Prescribe application of risk management techniques to Compliance Audit, including how materiality should be assessed;
 - d) Define supervision and quality assurance over work conducted by auditors responsible for conducting Compliance Audits;
 - e) Define parameters for how audit evidence should be obtained, retained and documented.

It could be argued that there is sufficient guidance to auditors through the Audit Standards of the Institute of Internal Auditors and the Australian Auditing Standards issued by the Australian Accounting Research Foundation and that therefore a further standard for Compliance Audit is simply not warranted.

In discussions with the Auditor-General it was clear that his preferred approach was to have a formalised standard dedicated to Compliance Auditing on the basis that there needed to be a formal established process for how such audits should be conducted. This was based on the premise that Compliance Auditing in the public sector was dissimilar in its role and nature to the standard audits that would be conducted by the private sector and also dissimilar to the conduct of financial audits. To this end the Audit Office would see that Compliance Audits would focus on areas of public accountability, assessing compliance with relevant legislation and directions issued by Agencies such as Treasury and Premiers.

During interviews with clients of the Audit Office the independent and important role of the Auditor-General in reviewing and commenting on efficiency and effectiveness and public accountability issues was strongly supported. In this context the Compliance Audit Program of the Audit Office was also strongly supported. However, Agencies were not clear as to the role and function of Compliance Audit, nor what the Audit Office was typically going to cover when it conducted Compliance Audits through their organisation.

Whilst there is a formalised Compliance Audit Manual put together for each years Audit Program, this is not a formal scope and boundary document and is only given to internal staff of the Audit Office. Engagement Controllers include the names of the Compliance Audits to be conducted in an Agency in their Client Service Plan and these are discussed with the client. However, an overall document setting out the framework for the objectives, planning, conduct and reporting for Compliance Audits that could be issued to Agencies is currently missing. There are three issues here:

- a) A formalised standard on Compliance Auditing would assist Agencies to understand the parameters in which such an audit would operate and how it would be conducted.
- b) Formal scope and boundaries are not set for Compliance Audits at the moment by the Audit Office, nor does there appear to be formal communication to Audit Office clients as to the approach and manner in which a particular Compliance Audit will be conducted; and
- c) Release of a formal standard on Compliance Auditing in itself will not necessarily bridge the 'expectation or understanding gap' between Auditor and Auditee.

It would appear that if the Audit Office chose to undertake a process to have a formalised Compliance Audit Standard set that it should:

- a) Promulgate this Standard to all Agencies and assist them in understanding how the framework for the Standard and how it would be applied; and
- b) Establish detailed terms of reference, including full scope and boundary and test mechanisms to be used for each Compliance Audit. These terms of reference should be communicated to all clients prior to commencement of the Compliance Audit Program in any financial year.

Given that the issue of Compliance Audit is one that is faced by all Auditor-Generals throughout Australia, it could be seen as more helpful to have an Australian Standard, rather than each State and Territory going its own way. A consistent standard applied throughout each jurisdiction would be useful for comparison/benchmarking purposes.

Discussions with the Public Accounts Committee during the conduct of this review indicated that they were keen to be involved with the Auditor-General in the development of such a Standard.

RECOMMENDATION 6 (MEDIUM PRIORITY):

The continuing role of the Auditor General through membership of the AusASB to assist in the AARF project for the development of a compliance auditing standard or guidance statement is supported. It is also recommended that the Auditor-General liaise with the Public Accounts Committee as to their involvement in this process.

RECOMMENDATION 7 (MEDIUM PRIORITY):

Prior to the development of an Australian Standard on Compliance Audit, to assist in the communication of the role of compliance reviews in the NSW Public Sector, the Auditor-General should consider development of guidelines for the conduct of compliance audits. The guidelines should include an overview of the Compliance Audit Program, audit approach, methodology and reporting process. These Guidelines should be clearly communicated to all Agencies. Alternatively, if felt more appropriate, the Audit Office could make available to each Department and Agency a copy of relevant sections of the Compliance Audit Manual and Program for that respective financial year.

RECOMMENDATION 8 (HIGH PRIORITY):

For every Compliance Audit to be conducted a formal scope and boundary document should be established. This should clearly set out the objectives of the audit, the sample of Agencies to be reviewed, the scope of the review, the boundary for the review and the expected time frame of the review. This formal document should be provided to all Agencies that will be audited as part of that Compliance Audit process.

CA (2) - THE EFFECTIVENESS OF COMPLIANCE AUDITS AND THEIR REPORTING IN NSW.

CA (3) - HOW THE EFFECTIVENESS OF COMPLIANCE AUDITING IS ASSESSED BY THE AUDIT OFFICE IN THE ABSENCE OF AN AUSTRALIAN AUDITING STANDARD FOR COMPLIANCE AUDITS.

FINDINGS:

Whilst the Audit Office conducts a whole of government risk assessment for its Financial Audit Program, there are no linkages from this risk assessment to the Compliance Audit Program and no separate risk assessment conducted to analyse topics that would be the most appropriate for inclusion in the program. At present topics chosen to be included in any given financial years Compliance Audit Program are set on a subjective basis. There is currently no formal overall assessment conducted by the Audit Office of the Compliance Audit Program as to the Programs effectiveness, nor a tracking of costs versus benefits of conducting each Compliance Audit. Whilst we note that presently two reviews performed each year are follow up reviews from two to three years before, with results reported to Parliament, this is not a process that provides an indicative overall assessment of the results of the Compliance Audit Program.

In assessing a continuous improvement cycle and whether the Compliance Audit Program has been successful we would expect to see the following framework:

- Establishment of goals, objectives and scope and boundary for a Compliance Audit as set out in our previous findings above;
- Conduct of the Compliance Audit Program for the financial year with a summary of the results of the audit work conducted;
- A document prepared by the Audit Office indicating as a result of their audit work and the recommendations made how they will assess whether improvement has occurred across government;
- Formal follow up by respective audit teams in the following financial year in every Agency in which that particular compliance audit was conducted to assess whether recommendations were implemented and what improvements have occurred; and

- A formal benchmarking process that assesses effectiveness of a particular area prior to and after the follow up audit has been conducted.

In measuring effectiveness distinction must be drawn between an “Auditing Standard” and the “conduct, performance and implementation of the results of a Compliance Audit”.

Acumen Alliance do not believe that the absence of an Australian Auditing Standard for Compliance Audits has had an impact on the ability to assess effectiveness. The reason for this is that the key focus of the Compliance Audit program is to assess compliance with legislation and public accountability. Lack of a standard for compliance auditing would not impact on the ability to assess improvement in these areas.

The results of Compliance Reviews are generally reported to agencies through either general or specific management letters, which are sent out by the Engagement Controller. The SAGE audit methodology requires consideration of previously reported issues in the planning of next years review. Generally, we were able to review the documentation of this assessment on prior year management letter points, in the sample of audits we reviewed. Issues raised were often cleared at the time between Management and the Audit Office. However, in some cases where issues had not been dealt with appropriately, in the opinion of the Audit Office, they were raised as “repeat issues” in the current year management letter.

During our interviews with Agencies the advice of the results of compliance reviews through management letters was confirmed. However, there was no debrief, according to Agencies as to how they were performing comparatively to others, which was felt to be of significant importance.

It should be clearly noted, that whilst we believe that emphasis on risk management and effectiveness would improve the Compliance Audit Program, our review of the manner in which the current Compliance Audits were conducted and reported indicated that the approach of the Audit Office was sound.

RECOMMENDATION 9 (MEDIUM PRIORITY):

The whole of government risk assessment conducted by the Audit Office should be expanded to include Compliance Audit. The risk assessment framework should follow and be consistent with AS/NZS3640, “Risk Management”.

RECOMMENDATION 10 (MEDIUM PRIORITY):

Additional involvement of Agencies in relation to the discussion of where their major compliance risks are and involvement by Agencies in the development of the APG's would strengthen the Compliance Audit process by helping ensure the significant compliance risks are considered.

RECOMMENDATION 11 (MEDIUM PRIORITY):

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.

RECOMMENDATION 13 (MEDIUM PRIORITY):

In addition to providing Agencies with comments in their management letter where concerns have been noted as a result of Compliance Audits conducted, the Audit Office should provide each Agency with a brief as to how they are performing in that particular area relevant to the rest of Agencies reviewed.

6 Performance Audit

INTRODUCTION:

This section of the report deals with the Performance Audit program undertaken by the Audit Office.

Performance Auditing is governed in Australia by pronouncements issued by the Australian Accounting Research Foundation on behalf of the two professional accounting bodies – CPA Australia and the Institute of Chartered Accountants in Australia.

Auditing Standard AUS 806 ‘Performance Auditing’ defines a performance audit as:

‘an audit of all or part of an entity’s or entities’ activities to assess economy and/or efficiency and/or effectiveness’.

The definition provides that a performance audit may consider any or all of the “three E’s” –economy, efficiency and effectiveness. ‘Economy’ is used as a term to describe the acquisition of resources at the lowest cost and at the appropriate time. ‘Efficiency’ is used to describe the use of resources acquired such that output is maximised for a given input or that inputs are minimised for a given output. ‘Effectiveness’ deals with the achievement of objectives or other intended outcomes.

The mandate for the Audit Office to undertake performance audits is derived from the Public Finance and Audit Act 1983 (the Act). Section 38B of the Act provides:

‘The Auditor-General may conduct an audit of all or any particular activities of an authority to determine whether the authority is carrying out those activities effectively and doing so economically and efficiently and in compliance with all relevant laws’.

The operation of this Act and the professional standards provide the basis for the approach, methodology, practices and procedures adopted by the Audit Office.

It is clear that the main aim of performance audit should be to provide commentary on an organisations efficiency, effectiveness, economy and compliance with relevant laws and to assist the organisation in improving in any of these areas where it is agreed that improvements are possible.

TERMS OF REFERENCE

The review's terms of reference require examination and evaluation of a number of audits to determine the extent to which the Audit Office has complied with:

- The performance auditing standards; and
- The statutory requirement to avoid comment on government policy.

In relation to final audit reports tabled in the Parliament the review also sought to establish:

- the extent to which reports stayed within the stated scope and objectives; and
- whether reports are issued only after key date and factual information critical to the audit findings have been cleared with the agency concerned.

In relation to the criteria used by the Audit Office to select performance audit topics the review sought to establish:

- Audit Office compliance with its stated criteria;
- whether the focus of reports should be consistent with the criteria;
- whether the criteria are adequate and capable of attaining the best value for money from performance auditing; and
- transparency in applying the criteria.

Finally, the review sought to establish whether performance audits undertaken by the Audit Office represent value for money.

STRUCTURE OF THIS SECTION

The findings in this section of the report are structured in line with the above terms of reference. It is observed however that the terms of reference are inter-related and that contributing factors and root causes are common to a number of findings.

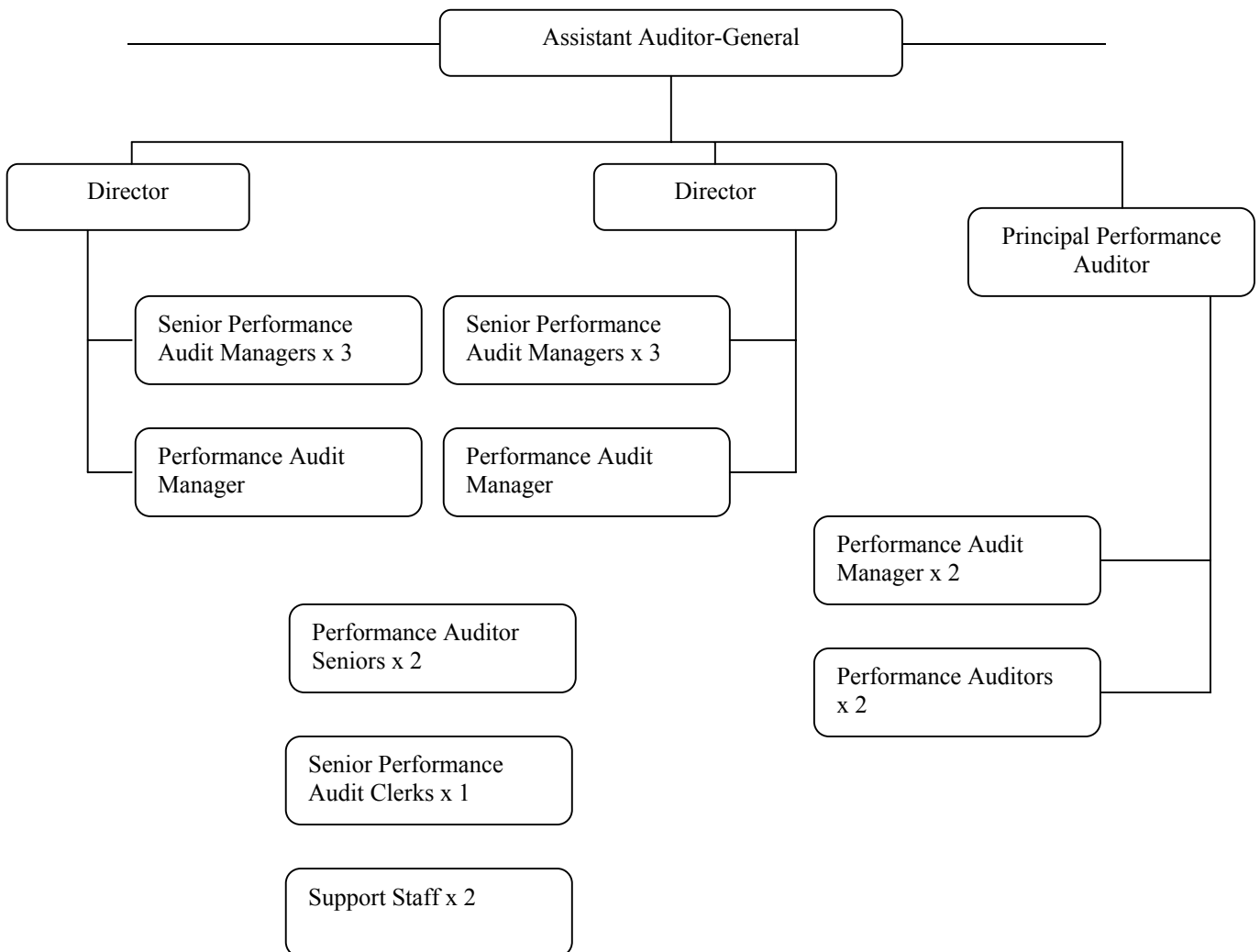
Prior to consideration of the detailed findings, the next section provides an overview of the Performance Audit program.

CONTEXT:

ORGANISATIONAL STRUCTURE:

Performance audits are undertaken by a dedicated organisational unit within the Audit Office headed by an Assistant Auditor-General. Staff in this unit only conduct performance audits. They do not participate in financial audits or compliance audits. The following chart summarises the current organisation structure.

Figure 1: Current Organisation Structure for Performance Auditing⁴



⁴ Table data provided to Acumen Alliance by the Assistant Auditor-General, Performance Audit.

The unit is separated into 3 sections led by senior executives. Two of these are headed by a Director and the third by a Principal Auditor. The position of Principal Auditor was established to provide a career path for progression to Director level. The distinction between the different classifications relates to the role of the occupants. All three positions are designated as Performance Audit Engagement Controllers (PAECs) and are responsible for the quality of the audit product. However, the Director positions oversight performance audits undertaken by Senior Performance Audit Managers. The Principal Auditor both undertakes audits and oversees audits undertaken by Performance Audit Managers. Compared with the Principal Auditor position, Directors have a less hands-on role in a performance audit.

The different role of the PAECs is reflected in the time charged to each audit by those positions. As PAECs the Directors averaged 13% of the total hours charged to an audit, whereas the Principal Auditor averaged 31%.

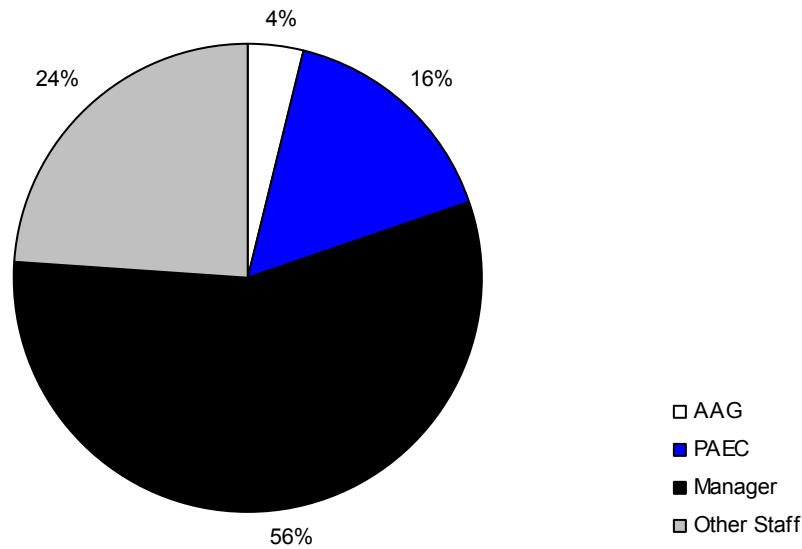
The Principal Auditor and the Senior Performance Audit Managers are allocated performance audit topics designated by the Audit Office as 'complex'. For planning purposes the elapsed timeframes allocated for 'complex' audits are 9 to 12 months. Performance Audit Managers are allocated 'non-complex' audits with planned duration of between 6 and 9 months.

The Audit Manager is by and large responsible for the conduct of the audit and undertakes the bulk of the work on each task. This is reflected in the fact that the average time charged to each task by the Audit Manager accounts for 56% of the total hours charged.

As there is limited resources in the branch each task is allocated to a single auditor. The allocation is necessitated by the combination of available audit resources and the timing and number of audits planned each year.

The following figure summarises the allocation of audit staff to audits during the period.

Figure 2: Average time applied to a performance audit by classification⁵



PERFORMANCE AUDIT PROGRAM:

This review examined performance audits tabled in the period from July 2000 to December 2002. In this period the Audit Office has tabled 27 Performance Audit Reports (2 of these following-up on previous audit reports) and produced 4 Better Practice Guides. Appendix A summarises the audit program for the period. *Our review involved detailed assessment of each of the 27 reports, including reading all reports and client responses and discussing a number of the audits with clients.* In addition, we reviewed working papers for five of the 27 audits conducted during this period in detail.

Cost of Audits

The average cost of the performance audit reports (excluding the Better Practice Guides) over this period was \$191,900. The average cost of audits

⁵ Information supplied to Acumen Alliance from Audit Office Management Systems by the Performance Audit Branch.

tabled in each year has dropped slightly over the period of the review from \$195,000 in 2000-01 to \$182,500 in the current year to date.

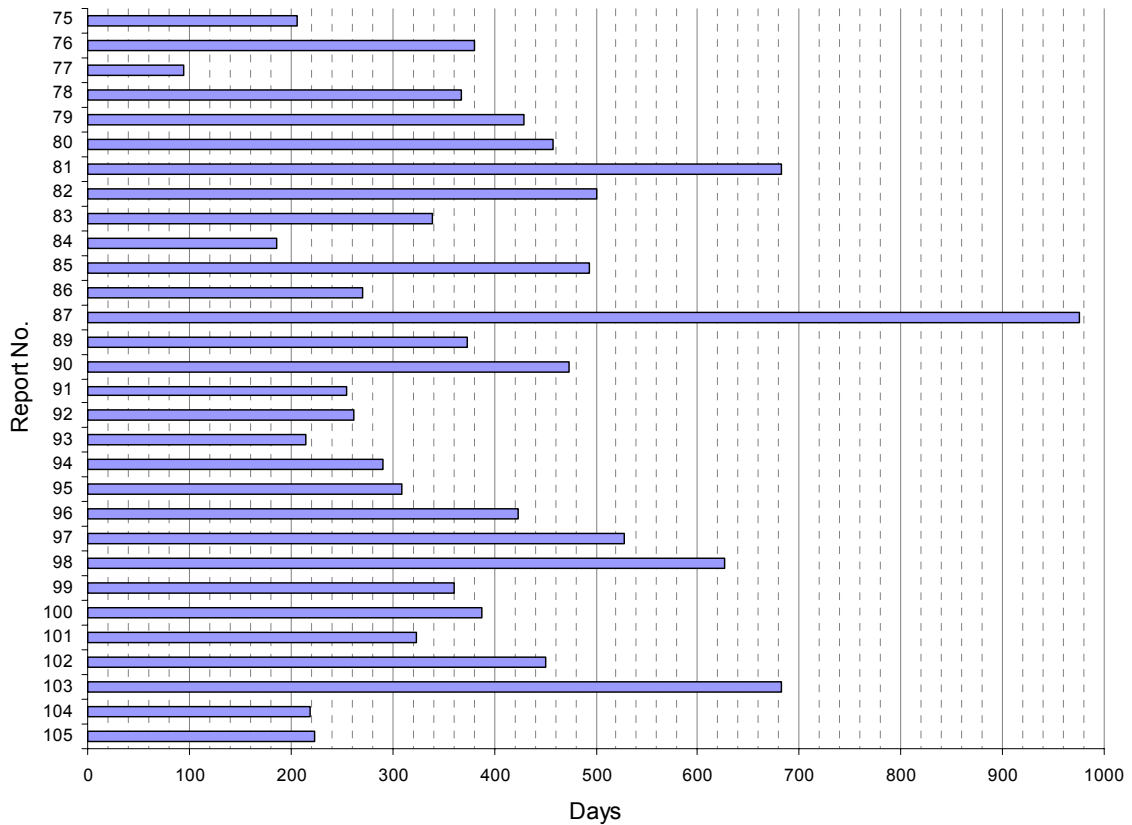
Some audits were significantly in excess of this average cost. The E-Government review of the Use of the Internet (Report 87) cost approximately \$600,000. The review of the NSW Ambulance Service (Report 80) cost \$363,000. By contrast the lowest cost audits in the period related to follow-up of past audit reports (Reports 84 and 86) which averaged around \$100,000 each.

Cycle Time for Audits

Data on cycle times to complete audits was not readily available. The current management information system did not contain data on audits conducted prior to its implementation. The total cycle time for an audit may be measured from its inception to completion. On this basis a number of audits in the period can be considered to have a long gestation.

The following charts illustrates the time from the start date of the audit (as recorded in the Audit Office management information system) and the tabling of the audit report, as provided to us by the Performance Audit Branch. However, it is the belief of Acumen Alliance that the table may contain misleading data as the Management Information System is poorly maintained, with many audits not having all milestones recorded against them. Discussions with Performance Audit Staff during this review indicated our belief to be correct. However, taking this into account the information in this table does provide some useful guidance in terms of elapsed days from inception of audit topics to audit finalisation.

Figure 3: Elapsed days from inception of audit topic to finalisation⁶



The Audit Office internal target is to complete all performance audits within 12 months from their start. However to determine achievement of this target much depends on the point chosen from when the start of an audit is measured. The above chart demonstrates that for a number of audits a significant period had elapsed from the start of the audit to its completion. It is understood however that the “actual audit” may not start for a significant period after it is recorded as an audit to be undertaken in the management system.

Our previous chart shows very long cycle times for performance audits because of the inconsistent manner in which the Management Information System has been maintained over the audit period. To obtain a more balanced view of the actual cycle times achieved for audits, an analysis of

⁶ The data in this table was provided to Acumen Alliance by the Performance Audit Branch of the Audit Office.

the phases of each audit was undertaken where data was available. The lack of available data is a result of the incomplete recording of milestones in Audit Office Management Systems. The results of this analysis are summarised in the following table:

Figure 4: Average cycle times for performance audits

Phase of the Audit ⁷	Average Cycle Time (Days)	Cumulative Cycle Time (Days)
Start of audit to end of scoping	68	
End of scoping to end of planning	38	105
End of planning to end of conduct	94	199
End of conduct to internal clearance of draft report	58	257
End of internal reporting to draft exit report	14	270
End of draft exit report to final '28 day' draft	22	292
End of final '28 day' draft report to tabling	41	333

Note: data based on 17 audits primarily from 2001-02 and 2002-03.

⁷ This information where available was provided to Acumen Alliance by Performance Audit Staff. It should be noted that during discussions with the Assistant Auditor General Performance Audit Branch, that he disagreed that the start of the audit to the end of scoping would take 68 days. It was his belief that scoping would seldom be more than one to two weeks. However, it would appear that the only reliable source to gather the above information is from the Audit Office TOPS System, which is where the data in the table above is gathered from. If in fact the figure of 68 days is incorrect and information maintained within the TOPS system is misleading, then the Audit Office should undertake an urgent review of its Management Information System for Performance Audit as it is evidently relying on incorrect information in managing its practice.

This data shows that performance audits are generally completed within 12 months from commencement of planning. It also shows that on average 30% of cycle time is utilised for planning the audit and 30% for audit conduct. Forty per cent of the cycle time of an audit is taken up in the reporting phase.

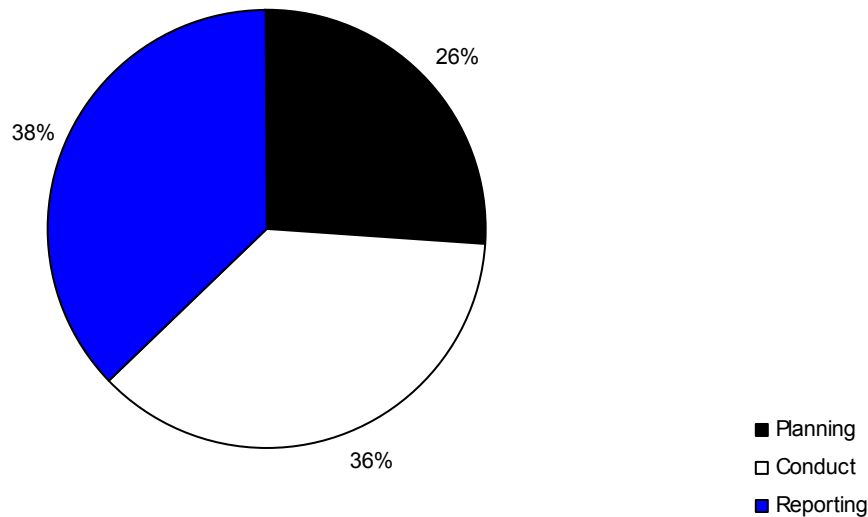
On average 270 days (81% of cycle time) is taken from the start of an audit to produce an exit report for discussion with the audit client. Twenty two days on average is taken to discuss this draft with the audit client and make agreed changes prior to the issue of a formal '28 day' draft report. As its title suggests, the audit client has 28 days to provide a formal response to this report. Where provided, this response is required to be incorporated into the tabled audit report.

Hours applied to audit phases

The allocation of effort to each phase approximates the above cycle times closely. This is largely a function of the fact that as most of the audit effort is undertaken by an individual, so elapsed time will roughly equate to hours charged and therefore to the actual audit costs per phase.

The following figure illustrates this.

Figure 5: Analysis of average hours recorded against each phase of a performance audit



RESOURCES APPLIED TO THE PERFORMANCE AUDITING PROGRAM:

The Performance Audit section is comprised of 21 audit staff from a total audit staff of 177 for the Office at 30 June 2002.

The total cost of the performance audit program for the 2001-02 financial year was \$2.77 million⁸ which is approximately 11% of the total cost of the Office. Hours recorded against performance audits for that year were 22,439 or approximately 10% of the total production of the Office.

The Audit Office receives \$1.3 million per annum in appropriation revenue from the Government to fund the Performance Audit program. The balance of the cost of the program is met from revenues received from financial audit fees that are charged to audit clients.

⁸ Source: Audit Office ACAG Macro-Benchmarking. It should be noted that the Audit Office Internal Management Information Systems indicate the cost to be \$2.335 million. The Assistant Auditor General, Performance Audit Branch was unable to identify why this discrepancy existed.

PREVIOUS REVIEWS:

The results and recommendations arising from past reviews of the Audit Office⁹ have been considered in this section of the report where relevant.

OVERALL CONCLUSION:

Performance Audit has produced audits of variable quality over the past three years. While it is difficult to directly measure the effectiveness of the audits undertaken, it is the opinion of Acumen Alliance that the program has not been as effective as intended in either promoting greater accountability or improving the performance of the NSW public sector. In terms of efficiency and economy the program has largely achieved its aims and compares favourably with other audit jurisdictions.

There remains scope for improvement in a number of areas. The focus on increased output and improved timeliness of audit reports is considered to have had a negative impact on the quality of the audit program and places the current program at greater risk.

During this review, Acumen interviewed twenty client agencies at the Chief Executive/Director General or Chief Financial Officer level, of which eleven had been subject to Performance Audits of their organisations within the review period. The clear feedback from these senior executives in ten out of the eleven interviews conducted was that performance audit reports lack balance, that analysis of issues is at times superficial and that conclusions drawn on the evidence presented is at times inappropriate. There is a significant level of client dissatisfaction with the usefulness of audit recommendations and hence the value or worth of the audits produced.

Clear feedback from the senior executives was that they were not prepared to get into a 'bun fight' with the Audit Office over recommendations and therefore undertook detailed work to get the reports to a stage where they were could 'live with the outcome', rather than simply rejecting the majority of recommendations out of hand. This was seen by most senior executives as a more palatable result, rather than provision of strong management comments disputing the audit conducted and the resulting concern that it would end up in a battle in the public arena.

⁹ 1996: Coopers and Lybrand; 1999: Professor Craswell

Such views, while not universal, pose a threat to the credibility of the Audit Office and the future viability of the performance audit program. Unless significant improvement is made in terms of quality and value for money there may be an increased risk that the funding for Performance Audit may be significantly reduced by Government. The small number of audits produced each year and the visibility of the performance audit product in terms of media interest, demands that the quality of the output be uniformly high. One or two audits of poor quality have the capacity to 'taint' the entire output. The perception that the conclusions drawn in performance audits are not reliable and that recommendations are not useful, reduces the likelihood that agencies will accept findings and take the necessary action to correct any legitimate deficiencies that may have been found.

Urgent management attention is required in relation to:

- The appropriateness of output and timeframe targets given resources applied to the performance audit function;
- Establishing clear and relevant audit objectives and appropriate evaluation criteria; and
- The approach to communication with audit clients as part of the audit process and ongoing relationship management and communication with the Office's key strategic clients.

PA (1) DETERMINE THE EXTENT TO WHICH THE AUDIT OFFICE HAS COMPLIED WITH THE PERFORMANCE AUDITING STANDARDS.

CONCLUSION

The Audit Office has established policies and guidance material that are consistent with Australian Auditing Standards. The application of policy and procedures is generally in accordance with the performance auditing standards. Aspects of the planning (being skills, competence and knowledge) and quality control of some performance audits do not always accord with the requirements of the standards.

BACKGROUND

There are two standards that deal explicitly with performance auditing. As mentioned in the Introduction to this section of the report, AUS 806 deals generally with performance auditing. It establishes the objectives and general principles of a performance audit and provides specific direction and guidance on matters addressed in other auditing standards such as audit evidence, planning, using the work of an expert, and reporting. AUS 806 is supported by AUS 808 'Planning Performance Audits'.

In addressing this term of reference the review considered the guidance material promulgated by the Audit Office (specifically the 'Performance Audit Policy Manual' and related 'Guidance Notes'). In addition working papers and correspondence files for five audits were reviewed in detail on site in the Performance Audit Branch and all members of the audit teams, including the PAEC's, that had been involved in conducting these audits were interviewed.¹⁰

POLICY AND PROCEDURES

The Audit Office maintains comprehensive policies and procedures governing the planning, conduct and reporting of performance audits. The contents of these documents are consistent with the requirements of the performance auditing standards.

APPLICATION OF POLICY AND PROCEDURES

The review found that Audit Office staff complied with their internal policies and procedures and therefore with the Auditing Standards in

¹⁰ It should be noted that Acumen Alliance interviewed approximately 50% of the staff employed within the Performance Audit Branch as part of this review.

most respects. However, some areas of practice were identified where compliance was considered to be partial or ineffective:

- Skills, Competence and Knowledge; and
- Quality Control.

SKILLS, COMPETENCE AND KNOWLEDGE

AUS 808 requires:

“.22 The auditor assess whether the audit staff have adequate skills, competence and knowledge to undertake the audit, and where knowledge of specialised areas is essential, whether it is appropriate to engage an expert or include specialists as part of the audit team”.

The Audit Office Policy Manual provides that the PAEC is responsible for ensuring there are ‘appropriate skills and information available for the conduct of the audit’.

Discussions with the Executive management of the Performance Audit program indicated that the selection of potential audit topics was “not constrained by the limitations of staff [knowledge, skills and experience]”. Notwithstanding this, the current practice is that the use of specialists, including engaging experts, was generally not factored into the audit plan but may be contemplated during the course of the audit. Interviews with audit staff confirmed this approach and in fact they made it clear to Acumen Alliance that the use of specialists was actively discouraged.

The rationale for the use of experts is based on the complexity of issues arising throughout the audit or where the audit findings are considered to be controversial or sensitive. In these cases the Audit Office may engage an expert to utilise as a ‘sounding board’ and to advise on the validity and wording of findings.

Experts are rarely engaged to undertake fieldwork directly on the audit topics – while there are limited examples of this over the period subject to review, analysis of cost data on the use of consultants suggests a recent strong trend to rely primarily on ‘in-house’ resources.

For all audits in the review period the average cost of consultants was \$32,200 which represented 16.8% of the total average cost of an audit.

¹¹However, for audits completed since 1 July 2001 the average cost of consultants was \$6,500 or 3.4% of the total cost of an audit. These figures

¹¹ These figures are based on information provided to Acumen Alliance by the Performance Audit Branch from Audit Office Management Information Systems.

are halved again when the cost of consultants for the E-Government audit (Report 87) of \$66,000 is removed from the analysis (these costs represented the use of a facilitator for forums conducted as part of the audit).

In relation to 'in-house' staff expertise and skills it was observed that many performance audit staff had multi-disciplinary backgrounds in terms of both qualifications and work experience. However, allocation of staff with relevant specialisations to audits was not a primary consideration in resource planning for each audit. Our review of the allocation of staff to Performance Audit assignments indicates that managers are allocated audit topics on the basis of the 'next cab off the rank' within each organisational unit (i.e. the next available resource is allocated the next available topic). This was confirmed by our interviews with staff and review of Performance Audit Reports.

Under this approach it was observed that a number of staff with specialisations relevant to a particular audit being conducted were not allocated to that audit. The failure of the Audit Office to allocate managers with relevant specialisations to relevant audit topics is considered to arise from a failure to plan the timing of proposed audits to take account of resource availability. This problem is exacerbated by a lack of flexibility in resource allocation given the limited 'in-house' resource base and the number of audit topics planned for completion each year.

The majority of Performance Audit Staff interviewed by Acumen Alliance during this review indicated that the Branch places some reliance on the liaison officer nominated by the audit client to provide necessary expertise where required. However, the liaison officer is not part of the audit team and does not contribute to the audit fieldwork. Their primary role is to facilitate the audit process.

The perception of audit clients interviewed as part of this review, is of interest in regard to the use of experts and specialists. In ten out of eleven client interviews conducted with senior executives that had been subject to performance audits, the majority expressed the view that they felt that the audit team did not have a sufficient understanding both of their business and of the subject matter of the audit topic. Interviews with Audit Office staff indicate that most faced a "very steep learning curve" at the commencement of an audit in both these respects. This is reflected in the large proportion of audit time (30%) expended in the planning phase of an audit.

The information obtained from interviews with audit clients is corroborated by the results of the Audit Office's own surveys of client satisfaction. In the February 2001 survey, a major perceived deficiency was reported in relation to *"the Audit Office thoroughly understanding the subject matter of the Performance Audit"*¹².

The Audit Office has recently conducted a new client satisfaction survey. The preliminary results from this survey, in the form of a statistical analysis, were provided to the Audit Office in February 2003. The results have yet to be formally reviewed and accepted by the Audit Office.¹³

Analysis of results from the most recent survey indicate that the level of client satisfaction with the Audit Office's *'understanding of Agency's business' and 'appropriateness of skills and expertise'* is significantly below the desired standard set by the Audit Office. Respondents to the survey rated the performance of the Audit Office against these two criteria well below the importance to the respondents.

The evidence indicates that insufficient attention is given to matching the expertise of auditors with the subject matter of audits. Audit Office staff during interviews indicated that there is also an increasing reluctance to utilise experts on performance audits, except in an advisory role only. Resource limitations, in terms of funds available for engaging consultants and the number of staff compared with the number of audits conducted each year, are considered to be significant contributing factors to this issue.

RECOMMENDATION 14 (HIGH PRIORITY):

Resource planning and scheduling and the timing of proposed audits be coordinated to take account of the specialisations of current performance audit staff.

¹² 'Client Satisfaction Benchmarking and Measurement - Performance Audit Clients', Sweeney Research, 2001

¹³ This included a survey of Parliamentarians. Unfortunately insufficient responses were received from Parliamentarians to make the survey statistically valid. Our review of other mechanisms of ascertaining the needs of Parliament during this review and detailed interviews with both the Auditor General and Deputy Auditor General indicated that the Audit Office do not actively communicate with Parliament, particularly at the Assistant Auditor General Performance Audit Branch and PAEC level.

RECOMMENDATION 15 (HIGH PRIORITY):

A preliminary assessment of the expertise and skills required to undertake each performance audit should be conducted at the commencement of each audit and compared with the assigned resources. The results of this assessment, including any recommendation to engage specialist staff or other experts, should be included in the audit scoping document. This may include seconding staff with specialist skills from the Agency being reviewed. The final decision on the need for and use of specialists and subject matter experts should be included in the audit plan. Where specialists and subject matter experts are not included in the audit team, a statement as to how the necessary knowledge and skills will be obtained should be included in the audit plan.

QUALITY CONTROL

The Standards require that where work is delegated to team members “the auditor should carefully direct, supervise and review the work delegated”¹⁴. The PAEC is responsible for the quality control of each performance audit, in accordance with the Audit Office’s policy statements.

The rationale for this standard, in part, is that the PAEC must have an ‘adequate appreciation of the methods, assumptions and source data used by all team members, particularly specialists, to be able to assess the reasonableness and significance of their findings’. One means of obtaining this understanding is through direct review of working papers generated by the audit team.

The review determined that the AAG and PAEC were actively involved in the direction and supervision of performance audits at a strategic level. There was evidence that regular progress meetings were scheduled with the AAG to provide an update on the progress of each audit and of issues arising. The AAG and PAEC were involved in the planning of each audit and approved the Audit Plan.

However, our review of working paper files, other relevant documentation and interviews with staff indicates that there was less direct evidence that either the AAG or the PAEC undertook a detailed review of the working papers generated by the audit teams.¹⁵ Discussions

¹⁴ AUS 806, clause 19.

¹⁵ Acumen Alliance were advised by the Assistant Auditor General, Performance Audit that the Branch had been quality audited against the ISO:9001 standards and that this

with the PAECs and their staff revealed that most of their time is spent at the report drafting stage in editing the audit findings. There was little evidence on working paper files to indicate that the PAECs had actually reviewed the detailed working papers and supporting data on which the audit findings and draft report were based. Based on the Standards which require careful control we believe the Audit Office processes are currently failing to meet the professional auditing standards.

Accordingly, understanding of approaches adopted, data utilised and audit findings generated by the audit team, was based largely on discussions held with the team and a review of the draft audit reports.

The lack of evidence of review of working papers is supported by observations made by audit staff interviewed and through consideration of the level of involvement in an audit as indicated by the time charged to each task by the AAG and PAEC. Figure 2 indicates that AAG involvement averaged 4% and PAEC involvement 16% of the total audit time.

While editing the draft report is an appropriate role for the PAEC given their responsibilities, it is considered important that the PAEC gains an 'adequate appreciation' through review of the work undertaken by the audit team. The review process also allows the PAEC to determine directly that auditing standards have been complied with and that sufficient, appropriate evidence has been obtained to support the audit report.

review did not identify any departure from established procedures and control for any of the Branch's operations including planning, quality control and report writing. However, this is clearly an argument of substance over form. An ISO:9001 audit merely reviews an organization against its policies and procedures to ensure that these are being appropriately followed. These reviews do not go behind the policies and procedures to ascertain that the underlying work is satisfactory and sufficient to support the end product. Australian Auditing Standards clearly require that a more extensive review be undertaken, whereby the underlying audit work to support a report issued is reviewed in detail and that the Principal Auditor responsible for the audit is satisfied that the audit work conducted is satisfactory to meet all conclusions reached.

RECOMMENDATION 16 (HIGH PRIORITY):

PAECs conduct reviews of the detailed working papers generated by audit teams throughout the audit engagement, particularly those generated by the Audit Manager. As a minimum a review should be undertaken at the end of the planning and detailed fieldwork phases of the audit. Evidence of the review should be retained on the audit files including any review notes generated and evidence that these have been appropriately cleared.

PA (1) DETERMINE THE EXTENT TO WHICH THE AUDIT OFFICE HAS COMPLIED WITH THE STATUTORY REQUIREMENT TO AVOID COMMENT ON MATTERS OF GOVERNMENT POLICY, INCLUDING WHETHER THE AUDIT OFFICE HAS APPROPRIATE PROCESSES TO MAKE SURE IT COMPLIES WITH THIS REQUIREMENT

CONCLUSION

The Audit Office has policies and procedures in place which minimise the likelihood that it will include in its reports inappropriate comments in relation to government policy.

It is the opinion of Acumen Alliance that evidence exists to indicate that the Audit Office has at times 'strayed' into this arena but it is not clear that this was intentional nor is it considered a systemic issue.¹⁶

BACKGROUND

Section 27B(6) of the Act provides:

"Nothing in this Act entitles the Auditor-General to question the merits of policy objectives of the Government including:

- (a) any policy objective of the Government contained in a record of a policy decision of Cabinet; and
- (b) a policy direction of a Minister; and
- (c) a policy statement in any Budget Paper or any other document evidencing a policy decision of the Cabinet or a Minister."

This legislative prohibition reflects the common understanding that the role of Auditors-General is to consider and assess the administration of government policy rather than the policy itself. Similar legislative restrictions apply in other Australian State jurisdictions and overseas.

¹⁶ For example Performance Audit 97, Bus Maintenance and Bus Contracts, dated 29 May 2002, states on page 21 that, "At present 69% of State Transit bus routes are unprofitable suggesting that services on some routes may exceed demand or are inefficient". We note that the Chief Executive of State Transit in his response to the audit indicated that "What the audit does not acknowledge is that public transport is a community service which is expected to operate at times and in places where there is no possibility of full cost recovery, and that it does so in the public interest". It could be argued that government policy is to meet the public interest and provide a community service in terms of its bus service, yet the Audit Office report fails to recognize this in the body of the report. It could be reasonably argued that stating in the report that 69% of State Transit routes are unprofitable is therefore straying into commentary on an area of government policy.

Mulgan's views that "performance auditing...is conducted within a framework that takes objectives as given, as properly determined by elected ministers" and that "performance auditing comes in at the next stage, to investigate whether government objectives have been met with due effectiveness, efficiency and economy"¹⁷ reflects a broad consensus understanding of an Auditor-Generals' mandate.

POLICIES AND PROCEDURES

This requirement not to comment on policy is not questioned by the Audit Office and the legislative restriction is clearly understood by Audit Office staff at all levels involved in performance audits. Policies and procedures accord with this understanding and are designed to minimise the risk that the Office will, or will be perceived to, question the merits of government policy objectives.

At the commencement of each performance audit Ministers are formally advised of the audit topic and audit objectives. Within this formal advice the Audit Office seeks advice from the Minister of 'any government policy objectives which may be relevant to the topic'.

APPLICATION OF POLICIES AND PROCEDURES

The test of whether the Audit Office has in fact commented on the merits of government policy objectives in its audit reports is largely subjective and open to the interpretation of the reader.

The perception of questioning the merits of policy objectives may arise for example, where the Audit Office criticises the effectiveness of the implementation of policy. But this would be to confuse the legislative and accepted legitimate role of the Auditor-General. It is open to the Auditor-General to question whether policy objectives have been achieved. It is not open to question whether the policy objective is appropriate or whether an alternative policy objective would be more appropriate.

In cases where the Auditor-General questions the effectiveness of the implementation of policy, it will be important that the wording used in any report is clear and that there is appropriate discussion of the policy objectives to set the context for any audit findings.

This is not always a straight forward proposition. The approach adopted by the Audit Office to seek input from relevant Ministers at the commencement of an audit does not always yield specific and clear statements of policy or policy objectives. It was not clear that after this

¹⁷ p. 32 Mulgan, R. 'Auditors-General: Cuckoos in the Managerialist Nest?', Australian Journal of Public Administration, June 2001

approach, any significant further attempt was made by the Audit Office to clarify policy or policy objectives.

The discussion of policy therefore generally arises at the completion of the audit with the presentation of the draft audit report, initially to the audit client, and in final form to the client and to the Minister.

The detailed review of selected audits and general review of audit reports incorporating audit client responses, for the period subject to examination did not reveal any indications of systemic failure by the Audit Office to comply with the legislative requirement.

RECOMMENDATION 17 (HIGH PRIORITY):

The Audit Office should ensure that where they might appear to be commenting on Government policy objectives, that they state their understanding of the policy objectives before they provide commentary. This should ensure that it is clear to the reader that the Audit Office is not questioning the merits of policy objectives.

PA (2) – THE EXTENT TO WHICH THE FINAL REPORTS ON PERFORMANCE AUDITS HAVE STAYED WITHIN THE SCOPE AND OBJECTIVES.

CONCLUSION

Audit objectives are poorly defined in many cases making it difficult for the reader of a report to establish whether and to what extent audits have achieved their objectives or whether and to what extent the audit has stayed within its stated objectives. Part of the reason for this is the lack of clear linkage between the stated audit objectives and the audit evaluation criteria.

There have been a few cases where the scope of the audit has changed significantly during its course. Communication with the audit client of changes in scope and of the rationale for these changes was not always effective.

BACKGROUND

The performance audit mandate provides that the Audit Office may examine issues of economy, efficiency, effectiveness and compliance with laws. Within the constraint of this mandate the auditing standards provide that for each audit undertaken the auditor must establish ‘audit objectives’.

The general objective of a performance audit is to form an opinion on one, all or a combination of the three E’s and/or on compliance. However, there is an expectation, from a reading of the standard, that more specific audit objectives will be formulated for a given audit topic.

The clear articulation of audit objectives is designed in the first instance to assist the auditor determine the matters to be audited and reported.

Auditing Standard AUS 806 states at paragraph 33:

“the auditor needs to give particular attention to clearly describing the scope and objectives of the audit where the purpose of the audit...is highly specialised or the audit opinion could mislead users if taken out of context”.

The audit scope is closely related to the audit objective. The audit scope covers matters such as the organisational unit, functions, process or activity subject to audit and the time period of the audit.

The standard accepts that decisions on the audit scope often change as new information is obtained. Where changes in scope are required after the initial plan has been provided to the audit client the standard indicates that it would be appropriate for the auditor to communicate these changes. Such an approach is consistent with the Audit Offices policy of 'no surprises'.

AUDIT OBJECTIVES

Examination of the reports produced by the Audit Office during the review period reveals a dichotomy in the approach to defining audit objectives. In some cases the audit has specific objectives that relate in some sense to the general performance audit objectives. In other cases, and more recently, the trend has been toward a simple statement that the audit objectives are to examine or consider or evaluate "efficiency and effectiveness".

Where specific objectives had been developed it was not always clear how these related to the mandate. Some audits considered the 'management' of activities or functions. Report number 101 (Clearing of Native Vegetation) and report number 105 (Managing Hospital Waste) are examples.

Many reports use generic objectives. Report number 89 (Intellectual Property), report number 96 (Animal Disease Emergencies) and report number 100 (Managing Sick Leave) are examples.

A review of the use of generic statements of audit objectives raises two issues. First, there is no reference to economy and/or compliance – although these matters may actually be addressed in the audit report. Secondly, there is no clear linkage between the audit evaluation criteria and the audit objectives. Where a generic reference is used the criteria developed by the auditor to form the audit opinion need to be clearly associated with the audit objectives.

USE OF GENERIC OBJECTIVES

The first issue is a matter of transparency and accountability. It should be made clear to the reader of an audit report which parts of the audit mandate were dealt with by the audit. This assists in the interpretation and understanding of the findings and also allows users to determine the extent to which the Audit Office has fulfilled its mandate.

A different but related issue is the question of whether the objectives of every performance audit should always address all of the mandate. A literal reading of section 38B of the Act could construe the use of the word 'and' as a conjunction to require the Audit Office to consider the three E's and compliance in each audit:

“...whether the authority is carrying out those activities effectively and doing so economically and efficiently and in compliance with all relevant laws.”

It is understood this construction has been adopted by the Auditor-General of Victoria (where a similar legislative provision exists) and the Australian National Audit Office¹⁸. This interpretation has not been adopted by the NSW Audit Office. Were it the intent of the Act that each performance audit address the entire mandate, this would have a significant impact on the scope of each audit and consequently on the approach to how they are resourced and executed.

AUDIT CRITERIA

The use of generic audit objectives can be in part be addressed through the clear articulation of the criteria the auditor uses to assess performance and form the audit opinion. Criteria are defined in AUS 806 as 'reasonable and attainable standards of performance against which the extent of economy, efficiency and effectiveness of activities can be assessed.'

A review of audit reports for the period subject to examination indicates a variety of approaches to establishing and reporting of audit criteria. In some instances audit criteria were not clearly articulated in the audit report (typically criteria are included in an Appendix to each report which also outlines the audit objectives, scope and cost). Report numbers 87 (Use of the Internet), 91 (Educational Testing Centre) and 103 (IT Outsourcing) are examples. However, review of planning documentation indicated that evaluation criteria had been established and the issue here is more of transparency in reporting.

Where criteria were developed and reported the review found it difficult to establish clear linkages between the audit objectives and the evaluation criteria. While the criteria were generally specific to the context of the

¹⁸ Refer to “[Public Sector Auditing: ANAO Approaches and Practices - Address by Pat Barrett AM, Auditor General for Australia, Macquarie University, NSW, August 2002](#)”. In this address the Auditor General for Australia discusses the Explanatory Memorandum to the Auditor-General Act 1997 and states that the aim of a performance audit is to: “Examine and report to the Parliament on the economy, efficiency and effectiveness of the operations of the administration of the Commonwealth and to recommend ways in which these may be improved”.

audit topic, it was not always clear how each criteria related to any or all of the stated audit objectives of 'efficiency and effectiveness'.

In some audits criteria had been developed utilising widely recognised better practice models of processes and of 'internal control structures'¹⁹. Report number 92 (Environmental Impact Assessment) and number 100 (Managing Sick Leave) are examples. While this approach has merit, it does not of itself provide a direct and clear linkage to the audit objectives. There is an implication in this approach that satisfaction of the criteria will mean that the agency has achieved 'efficient and effective' outcomes, and alternately that failure to satisfy the criteria would mean that this is not the case. However, it is not clear that the criteria are comprehensive or that there are no other criteria by which efficiency and effectiveness may be assessed.

In fact, review of the actual criteria utilised in most audits indicate that few, if any, can be related directly or indirectly to the 'efficiency' objective. In addition, in some cases, criteria include references to policy and regulatory compliance without this being articulated as a specific audit objective.

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.

RECOMMENDATION 20 (HIGH PRIORITY):

Audit criteria be clearly linked to the audit objectives.

¹⁹ The Internal Control framework developed by the Committee of Sponsoring Organisations of the US Treadway Commission is an example.

RECOMMENDATION 21 (HIGH PRIORITY):

Taking into account current Crown Solicitors Advice, the Audit Office should seek further independent legal advice on the interpretation of the provisions of section 38B as it impacts on the objectives of a performance audit.

AUDIT SCOPE

The review found the audit scope to be clearly defined at the commencement of the audit. The detailed audit plan containing the scope is communicated to the audit client. The client is afforded the opportunity to comment on the plan, including the proposed scope.

Comparison of the audit scope at the planning stage to that included in the final report revealed that there is generally little change to scope. Where there is a change in scope the audit reports accurately detail the final scope. However, there is not necessarily an explanation or rationale provided in the final report for the reason for the change in scope.

In discussions with two of the eleven clients interviewed in relation to Performance Audit during this review, reference was made to changes in the scope of the audit during the course of fieldwork. In both cases the scope had been increased to include an additional activity or function that had not been identified in the initial planning document. Both clients had been made aware of the change in scope, in accordance with the Audit Office's 'no surprises' policy. However, both clients expressed some concern that they did not understand and or agree with the reason for the change in scope. Both indicated they did not believe that the increased scope was relevant to the original audit objectives.

This issue is a matter of effective communication. It is within the remit of the Auditor-General to determine the objectives and scope of a performance audit and it is his prerogative to change the objectives and scope during the course of an audit. This is contemplated within the auditing standards.

Where an audit undertaken ostensibly for one purpose discovers other potentially serious issues that may or may not be related to the original audit objective, the auditing standards impose a duty on the auditor to investigate these issues and report on the results of this investigation to management, and in the case of a Performance Audit, to the Parliament.

However, there is an expectation in the auditing standards that the auditor would not simply communicate the change in objectives or scope but would also seek to provide a rationale for the change. It could also reasonably be expected that this issue be included in the report to provide greater transparency and accountability for the decisions and actions of the Audit Office.

This matter of effective communication arises in a number of contexts including the clearance of data and the discussion of the draft audit report with the client. It will be dealt with more fully in those terms of reference. In the context of this term of reference the issue is that rationale for the change in scope or disagreements with the audit client about the relevance of the scope to the audit objectives are not clearly reported.

RECOMMENDATION 22 (HIGH PRIORITY):

Changes in scope during an audit be clearly identified and explained in the final audit report.

RECOMMENDATION 23 (HIGH PRIORITY):

Disagreements with the audit client about the appropriateness and relevance of the scope compared to the stated audit objectives, be canvassed in the audit report.

PA (3) – WHETHER FINAL AUDIT REPORTS ON PERFORMANCE AUDIT REPORTS ARE ONLY ISSUED AFTER KEY DATA AND FACTUAL INFORMATION CRITICAL TO THE AUDIT FINDINGS HAVE BEEN CLEARED WITH THE AGENCY CONCERNED.

CONCLUSION

The Audit Office has established processes to clear key data and factual information with the audit client. These processes are not always effective in terms of their timing and the organisational level at which clearance is obtained, however there are no indications of systemic failure.

BACKGROUND

The auditing standards require the auditor to obtain ‘sufficient and appropriate audit evidence to support their conclusions’. Evidence may be either qualitative (and hence largely subjective) or quantitative in nature. Evidence is gathered during both the planning and conduct phases of the audit. It is also gathered from both internal and external sources. It is important that any evidence obtained is relevant, reliable and balanced. This implies that it be both accurate and comprehensive.

The Audit Office maintains a ‘substantiation’ file for each audit where the data and findings in the audit report are cross-referenced to supporting documentation. This approach should ensure that all data is able to be supported.²⁰

In addition to the use of the substantiation file, a key step in confirming the accuracy of data is to afford the audit client the opportunity to review and confirm the data. For this process to be effective the audit client needs to be given sufficient time to consider data and needs to be able to have their point of view ‘heard’. Where it is found through this process that data was inaccurate or incomplete (i.e. additional relevant data is provided) this needs to be reflected in the audit report.

TIMING OF CLEARANCE PROCESS

The Audit Office approach to reporting includes the option of providing the audit client with a ‘Client Issues Paper’ in advance of the draft audit report. Where utilised this discussion paper provides the client with the first formal opportunity to review the data and other factual information that the auditor intends to rely upon in drafting their report.

²⁰ However, as is noted earlier in this Section on Performance Audit, there is a lack of evidence to show that a detailed review of these files is undertaken by PAEC’s or the AAG to ensure that the work performed is satisfactory and that the data is in fact correct.

However, issues papers are not always utilised. In these cases the audit client will formally obtain access to the data and factual information being relied upon by the auditor when they receive a copy of the draft report. The draft is generally provided to the nominated 'liaison' officer unofficially for comment before it is formally issued to the Chief Executive Officer of the Agency.

Examination of audit working papers found that errors identified by the audit client in data or other factual information were generally corrected by the auditor as part of the discussion of the draft report. In some instances additional data was provided by the audit client. However, this additional data was not necessarily utilised in the audit report. Where it was included in the report there was no evidence that its veracity had been tested to the same standard as that applied to other evidence gathered during the audit conduct. This is considered to be largely an issue of timing.

From a review of audit files it is clear there is a reluctance on behalf of the Audit Office to extend or delay the audit process to address any new data provided. It is either accepted on face value or it is not incorporated in the final report.

Discussions with staff indicated that the emphasis on meeting target tabling dates and restraining the costs of audits means that data obtained from the audit client 'late' in the audit process (especially at the draft report stage) is not able to be critically evaluated.

The analysis of audit cycle times in the previous section shows that 36 days on average elapse from internal clearance of the proposed draft report and its finalisation. This is a little over 10% of the total elapsed time for an audit. This was considered too long a process.

LEVEL OF CLEARANCE

It was observed through discussions with Audit Office staff, audit clients and a review of audit files that the level at which findings and supporting data and other information is cleared by the client during the conduct of the audit was not always effective.

A number of clients indicated that there were major disagreements with some of the data and findings at the draft audit clearance phase. However, in the final audit report, management responses generally did not question basic facts.

It was observed that, despite the practice formally providing audit plans and issues papers to Chief Executive Officers of Agencies, in some audits it was not always possible to effectively 'engage' the audit client at the Executive level until toward the end of the audit process when the 'exit interview' or the '28 day draft' had been provided.

It was at this stage, when the audit client was able to ascertain how the data obtained was proposed to be reported and what findings and conclusions were to be drawn from the data, that significant attention was paid to the audit at the executive level. In discussions, Audit Office staff indicated a level of frustration that relevant data and other information was advanced at this late stage in the audit.

This is as much an issue for the Audit Office as for the audit client. It is a further indication of the lack of effective communication with the audit client, raised in the previous term of reference on audit scope changes. The Audit Office has established procedures for a formal communication process with the audit client during an audit²¹ (including establishing a liaison officer inside the client and providing written audit plans and draft reports to the Chief Executive Officer). However, it is important that the auditor assess the effectiveness of communication throughout the course of the audit.

It is particularly important that potentially serious issues are raised in a timely manner at an appropriate level within the audit client. It was suggested by the Audit Office that on occasions the fault lay with the liaison officer nominated by the audit client. In circumstances where the auditor is of the view that liaison arrangements are not functioning effectively, it is incumbent on them to raise this matter with the executive management of the client.

Such a role is appropriate for the PAEC and/or the AAG. As discussed in section 2.1 Context and 3.2 Quality Control, our discussions with Performance Audit Staff and NSW Government Agencies, our review of the Audit Office Time Billing System and our review of working paper files, indicates that there is evidence that the PAEC and AAG do not take a hands-on participative role in the conduct of performance audits, except at the planning and report writing stage of a Performance Audit. There was little evidence in the audits reviewed that either the PAEC or AAG held regular meetings with the audit client executive management to brief them on the progress of the audit or on significant issues as they arose.

²¹ Guidance Note 3 - Client Liaison

This was corroborated in discussions with the Chief Executives and Senior Executives of the majority of the eleven audit clients interviewed whose Agency had been subjected to a performance audit during the period under the review.

However, instances were cited by the Audit Office where they had offered briefings to the audit client executive, generally at the completion of the audit conduct phase and after the draft report had been internally cleared. The ability to offer earlier briefings is to some extent constrained by the level and nature of involvement of the PAEC during the audit conduct phase.

RECOMMENDATION 24 (HIGH PRIORITY):

The audit communication strategy for performance audits be amended to provide for ongoing assessment and review of the effectiveness of communication.

RECOMMENDATION 25 (HIGH PRIORITY):

Given the duration of audits the strategy also provide for regular meetings between the executive of the audit client and PAEC (or AAG if necessary) throughout the conduct of the audit.

RECOMMENDATION 26 (HIGH PRIORITY):

The communication strategy be formalised as an agreed communication protocol that is included in the audit plan.

PA (4) – THE CRITERIA THE AUDIT OFFICE USES IN SELECTING PERFORMANCE AUDIT TOPICS.

CONCLUSION

The criteria used by the Audit Office to select audit topics are adequate and capable of attaining the best value for money from performance auditing. However, it is difficult to determine whether and to what extent the criteria have been complied with due to the subjective nature of the evaluation and a lack of detailed documentation of assessments against the criteria.

The application of the criteria to the NSW public sector and hence potential for identifying topics that attain the best value for money is inhibited by a lack of systematic and structured intelligence gathering beyond the limited approach discussed below.

Greater transparency and accountability is required at both the planning stage of the audit and in the public report.

BACKGROUND

The selection of performance audit topics is a key decision. The limitation on resources against the size and complexity of the NSW public sector will always mean that potentially useful audit topics will not be able to be included in the program. It is important therefore that the Audit Office has a basis for firstly identifying suitable topics and secondly prioritising these topics to focus on those most likely to either improve accountability and/or performance.

A two step process exists for the identification of a list of potential audit topics and the subsequent selection of audit topics for inclusion in the annual work program of the Office.

IDENTIFICATION OF POTENTIAL TOPICS

The Audit Office seeks input from a number of sources to identify potential audit topics. Ministers and other Members of Parliament and agency heads are asked each year to contribute potential topics. Financial audit staff within the Audit Office are also canvassed. Finally, staff in the Performance Audit Branch also suggest topics.

Discussions with audit staff indicated that there is limited opportunity to directly gather and analyse ‘intelligence’ at an agency level or service-wide, to assist in the identification of potential topics. It was stated that there was “‘not much science’ involved in the identification of topics. The process was also characterised as a more of a “clerical, form filling exercise”.

Discussions with audit clients indicated a general reluctance to provide input to topic selection. This was particularly the case for clients who felt they had been unfairly treated by the Audit Office in past audits. Analysis of suggestions received from outside the Office indicate that almost all come from Members of Parliament. However the majority of potential topics are suggested by Audit Office staff.

The Performance Audit Branch does not possess sufficient resources in the context of its planned program of audits, to be able divert these resources to a general information gathering and analysis role. By contrast some other audit jurisdictions invest a significant amount of resources, time and effort in establishing links with both Members of the Parliament and its Committees and with audit clients. Dedicated liaison sections have been established in both New Zealand and in Victoria. These sections undertake environmental scans and sectoral analysis to identify and scope potential audit topics.

Given its size, it is debatable whether such an approach is feasible for the Audit Office. It would require a significant increase in resources or would significantly reduce the number of audits able to be undertaken each year.

However, there is considered to be scope for the Executive of the Performance Audit Branch to take a greater role in intelligence gathering through more direct communication with audit clients and with the Parliament.²²

In this regard the review considered the nature and extent of the strategic relationship of the executive with their clients (i.e. outside the audit process), including the approach to communication. There was little evidence to suggest the Performance Audit Executive has established an effective ongoing relationship with its primary client (the Parliament) or with its audit clients. Communication is central to this issue.

Ongoing contact with key clients outside the audit process would foster greater understanding of the role and products of the Office and would

²² Indeed during the course of this review the Audit Office were not able to advance sufficient evidence to demonstrate that a sufficient level of resources was aimed at establishing links with both members of Parliament and its Committees.

increase the likelihood of generating useful intelligence and interest in the performance audit program. This would militate against the impact of the limitations of existing resources on audit topic identification.

SELECTION OF TOPICS

Given the above limitations it is important that potential audit topics identified are critically evaluated to ensure that scarce resources are not diverted to subjects of less importance or consequence.

The development and application of appropriate screening criteria which allow for an assessment of relative impact and significance will assist this evaluation.

The Audit Office utilises such criteria to first screen all suggested topics and to prioritise these topics. It utilises these criteria in conjunction with other parameters to determine its annual audit program. Figure 6 following summarises the criteria that have been utilised by the Audit Office since January 2001. For comparison the first column shows the criteria that were used prior to 2001. Each criteria is given a rating from 1 to 5 to allow for relative ranking and comparison.

The first three criteria are considered to be the most important in terms of increasing the likelihood that audit topics will result in the best value for money for the performance audit program. However, there is little internal guidance on how an assessment of 'significance' and 'impact' is to be made. Accordingly this is a subjective process. At the time of topic selection it is also the case that there is little 'hard' intelligence on which to base these assessments.

The latter criteria (apart from the 'public interest' criterion) serve to constrain the inclusion of audit topics on the program from a practical perspective. Consideration is given to whether there has been, and the extent of, previous coverage of the portfolio and the audit client.

Consideration is also given to the complexity of the audit topic. This criteria assumes importance in topic selection from a purely pragmatic view based on the resource allocation model adopted by the Audit Office. Non-complex audits are allocated to Performance Audit Managers (PAMs) whereas complex audits are allocated to Senior Performance Audit Managers (SPAMs). As there is a fixed number of SPAMs there is a fixed number of complex audits that can be undertaken. By corollary a certain number of non-complex audits must be programmed each year.

There is not necessarily a direct relationship between complexity and impact/significance of an audit topic. However the current approach to resource allocation increases the likelihood that audit topics are included on the annual program for PAMs that have a relatively lower consequence and or impact rating than audit topics that are excluded.

An alternative approach would be to modify the existing strategy for resource allocation to audit topics so that the choice of topic is not constrained by staff availability. This would help to ensure that only topics that are rated as of most consequence are included on the program. It would however require a change to the target number of audits based on the need to establish audit teams that may consist of a SPAM and a PAM.

Table 6: Criteria for screening potential audit topics

Previous Criteria	Current Criteria	Explanation
Financial magnitude	Financial materiality	The value in financial and/or economic senses of the agency, program or activity.
Significance	Significance	The importance of the review topic in terms of its strategic and operational impact on agency/public sector operations.
Impact of the audit Savings	Possible Outcomes	The potential for the audit to identify opportunities for improvements other than allocating more resources to solve the problem and/or whether the review would identify financial savings that is economies in the program, function, activity inputs and/or improved revenues and hence reduced public subsidies.
Complexity	Complexity	Whether there are adequate methodologies, tools, data, skills and resources available to conduct an audit. Whether these inputs are available internally or whether contracting/ consultants would be needed.
Time Period for the Audit	-	This has been related to complexity with 6 to 9 months being allocated to non-complex audits and 9 to 12 months to complex audits.
Precedent	Coverage	Whether there has been any coverage of the topic/subject matter by not only the Audit Office but also other audit jurisdictions and knowledgeable independent reviewers.
Application to the public sector	Service Wide	Whether the topic being reviewed would be able to be undertaken as, and/or applied on, a service wide basis.
-	Risk	The level of inherent risk that is thought to exist in respect of the program's, function's and /or other activities achievement of value for money, financial management and performance.
-	Public Interest	Whether the topic being reviewed is a mater which is of potential and/or current appeal/attention to political and social interests and could also conceivably raise the profile of the Audit Office.

Source: Audit Office - Guidance Note 1

The 'public interest' criterion is related to impact and significance only in terms of the 'visibility' of the topic and the interest likely to be generated. The reference to the 'profile of the Audit Office' is interesting as this does not relate directly to the mission of the Office or to its stated objectives. Based on the research conducted by Acumen Alliance during the course of this review, it is difficult to understand how a criterion relating to the impact on the Office's profile, is a useful screening tool for selecting audit topics.

The 'public interest' criterion is also used by the Office as a basis for classification of its audit topics. The current guidance note on topic selection²³ states:

"Performance audits to be undertaken by the Branch will have two major streams. One will be Themes and the other is Public Interest audits. It is expected that about half of the resources will be devoted to each."

In discussions with Audit Office executives and staff there was no clear and consistent articulation of what was meant or intended by the 'public interest'. Reference was made to "topics that the public are interested in" – such as health, education and public safety. A proposal developed for a suggested topic included the following reference under this criterion – "a very sexy topic for the public and the parliament". In correspondence seeking suggested topics from external sources the reference to public interest audits is couched in terms of "one-off audits of topical interest".

Whilst Acumen Alliance is not suggesting that Performance Audit topics previously chosen were not legitimate, use of a criterion such as that discussed above and the implications that can be drawn from it, exposes the Audit Office to the charge that it seeks to select topics that will generate a lot of publicity. This can and has been interpreted by a significant number of clients, as the Office being more interested in 'media hits' than in genuinely wishing to improve performance.

There were also no formalised processes demonstrated to us by the Audit Office to show that other 'independent regulators' such as the Audit Office, Independent Commission Against Corruption (ICAC) and the Independent Pricing and Regulatory Tribunal (IPART) meet to discuss planned work programs. Although letters are sent out to these Regulators at the same that letters are sent to Ministers asking them to provide Performance Audit topics, it is felt that a more formalised consultative approach could be beneficial. Such a process could be considered helpful

²³ Guidance Note 1 – Project Selection

in terms of minimising 'cross overs' and also to ensure the most appropriate organisation undertakes a particular review. Should such a process be undertaken there would be no loss of independence on the part of the Auditor-General as it is considered that there would be no barrier preventing the Auditor-General from undertaking a review of the work of the other 'independent' Agencies to ensure that the objectives of the review had been achieved and that it was effective in enjoining efficiency and effectiveness changes in Government.

TRANSPARENCY

The initial assessment and rating of the screening criteria for a potential audit topic is undertaken when the annual audit program is being formulated. There is further opportunity to review the criteria and the assessment at the time an audit is due to commence.

At the inception of the audit planning phase for a selected topic the audit manager undertakes a 'scoping' exercise for which around 40 hours is generally allocated. The purpose of the scoping exercise is to validate the original rationale for the audit. Review of scoping papers for selected audits revealed that there is little or no reference to the original screening criteria. There is no commentary in the scoping papers reviewed or other evidence to suggest that the initial assessment had been reviewed and validated.

Scoping papers document the audit objectives, scope and approach and identify potential audit issues – generally as potential adverse findings. There was no direct references in the scoping paper of the materiality, significance and potential outcomes from the audit as described in the table above. Given that the original screening process may be undertaken significantly before an audit is commenced and involves limited 'intelligence' gathering, it is considered important that part of the scoping process be to update and revalidate the original assessment.

Review of plans developed for each topic that are issued to the audit clients revealed that there is little or no discussion of the criteria used to determine the choice of the topic or the assessment of the criteria. It is considered useful from a transparency and accountability viewpoint to inform the client of the rationale for the audit and of the expected outcomes and impacts.

In discussions with audit clients it was made clear by many that they were not aware of how or why a particular audit topic was selected, and in the case of cross-agency audits, why their organisation was included. This inhibited their ability to participate positively in discussions of audit scope

and approach at the planning phase. In some cases it also caused doubt and suspicion as to the true motives of the Audit Office.

The majority of clients interviewed during this review indicated that in their opinion the Audit Office went on 'fishing expeditions' and had a 'gotcha' mentality and this arose partly from the lack of understanding of the rationale for the audit.

This is an issue of effective communication with audit clients that has been a common theme running through each term of reference. The Audit Office has only recently made its planned annual performance audit program publicly available via the Internet. For the first time last year it wrote to agencies that had been selected for an audit at the beginning of the year. This increased openness is positive. However, it is evident that more is needed.

This is also evident in the final audit report that is tabled in Parliament. The reports make no direct reference to the criteria. They may contain an indication of the materiality and significance of the topic in an introduction but this approach is not uniform.

A similar issue was raised in a peer review of another Audit Office in which staff from the NSW Audit Office participated. In that review the following opportunity for improvement was identified:

"Transparency could be improved by better reporting of the rationale behind selection, thereby satisfying the desire expressed by a number of stakeholders to have a better understanding of how performance audits in particular are selected".

RECOMMENDATION 27 (HIGH PRIORITY):

The AAG and Directors develop and implement a communication strategy for ongoing dialogue with key clients including the Members of Parliament and Parliamentary Committees and with major NSW public sector agencies.

RECOMMENDATION 28 (HIGH PRIORITY):

The application of the 'complexity' and 'public interest' criteria be reviewed for relevance and appropriateness. If necessary, the resource allocation model be modified to ensure that audit topics achieving the highest rating are undertaken before considering other topics.

RECOMMENDATION 29 (HIGH PRIORITY):

The audit scoping process be used to formally review and update the screening assessment and the results of this review be included in the scoping document.

RECOMMENDATION 30 (HIGH PRIORITY):

The audit plan provided to the client and the report to parliament include reference to the original rationale for selection of the topic and whether the initial assessment (particularly in terms of expected outcomes) was validated by the audit.

RECOMMENDATION 31 (HIGH PRIORITY):

The Auditor-General facilitate a forum whereby the Audit Office, IPART and ICAC discuss planned review programs to ensure maximum review coverage of government and to avoid the risk of 'cross-overs' in work conducted.

RECOMMENDATION 32 (HIGH PRIORITY):

The Audit Office, should review the appropriateness of output and timeframe targets given resources applied to the Performance Audit function. This will obviously be impacted by the ability of the Audit Office to achieve full Treasury funding for the Performance Audit program as recommended in the section on Costs and Charges.

RECOMMENDATION 33 (MEDIUM PRIORITY):

The Audit Office, should formalise a policy that sets the framework for how performance audit topic selection should be undertaken. This policy should encapsulate a risk management process.

PA (5) WHETHER THE PERFORMANCE AUDITS REPRESENT VALUE FOR MONEY (VFM)

CONCLUSION

There is growing indications the quality and effectiveness of the performance audit product requires significant improvement. The credibility of performance audits are jeopardised where there is unresolved public disputation by the audit client with audit findings and conclusions.

Greater attention is required in developing a balanced suite of effectiveness measures and systematically capturing the information required to ascertain actual performance.

BACKGROUND

The concept of value for money is closely allied to the objectives of a performance audit. On one hand it considers the cost of an output against the benefits gained from it – in other words the economy of inputs and the efficiency with which they are converted to outputs, balanced against the effectiveness of the outputs.

It is a question of balance. Achievement of a low cost outcome may not be desirable if the quality of the product (in terms of its usefulness or relevance for example) is inferior. Conversely a high cost outcome is not necessarily a poor result if the quality of the product is far superior to other similar products.

To ascertain whether performance audits represent value for money it is necessary to utilise relevant and reliable performance measures and indicators (KPIs) of economy, efficiency and effectiveness.

The starting point for development of such measures is the Audit Office's own set of KPIs. The Annual Report for 2001-02²⁴ includes four measures relating to the performance audit program:

- Parliamentarian and Client satisfaction index;
- Chargeable time;
- Average cost of performance audit publication; and
- Number of publications.

²⁴ pp 4-5, 10

The first two are composite measures incorporating results for the financial audit program and staff. Chargeable time is measured for all Audit Office staff and is defined as hours charged to an audit compared to total available hours. A more relevant measure would be the hours charged by professional audit staff only compared with their total available hours.

A target has been set for the first three measures. There is no publicly reported target for the number of publications. However, it is understood that this year an internal target of 15 publications has been set.

These measures are relevant to assessing both the effectiveness and efficiency of the performance audit program. However, a number of other measures can be utilised. The 1996 review of the office identified the following measures:

Efficiency

- Cost per unit output – cost of a performance audit report
- Time utilisation – amount of time taken to complete a task against a standard
- Productivity – relationship between work output and staff input, and
- Cycle time – elapsed time between commencement and completion of a performance audit

Effectiveness

- Quantity – number of reports produced and comparison with planned numbers
- Timeliness – whether reports meet scheduled completion dates and are provided within a reasonable timeframe
- Acceptance – extent to which recommendations are accepted and will be implemented
- Quality – validity of findings and recommendations, relevance and usefulness of reports, and
- Client satisfaction – extent of conformance with customer or client expectations.

Source: p.p. 2-4, Coopers and Lybrand Consultants, 1996

EFFICIENCY

As discussed previously in this section, the review found that the indicators of efficiency for the performance audit program are positive. Cycle times and the cost per audit are within or below the results achieved by other jurisdictions. It is also apparent that the Audit Office produces a relatively large number of publications each year so that an assessment of effectiveness from the point of view of quantity and timeliness criteria is also positive.

However, the review identified some areas of concern in relation to the acceptance, quality and client satisfaction criteria.

EFFECTIVENESS

The Audit Office does not systematically monitor and review the overall level of acceptance and implementation of the recommendations it makes²⁵. It has initiated a practice of writing to agencies involved in an audit after the tabling of the audit report, to ascertain that agency's acceptance of audit recommendations and proposed action.

The Audit Office is able to utilise these responses, in conjunction with its 'follow-up' audit program to obtain information on the rate of acceptance and extent of implementation of audit recommendations. Review of responses by agencies indicates a generally high level of acceptance of recommendations. It is considered that this would be a useful indicator of effectiveness for individual audits and overall for the audit program.

However, some caution is required in this regard as there is no clear public accountability mechanism within the NSW public sector to track progress of and report on the implementation of recommendations. In the absence of external accountability the ostensible acceptance of recommendations alone by audit clients does not necessarily lead to real changes and so may neither improve accountability or improve agency performance.

Management's response to Audit Office findings and the effectiveness of action taken to address audit recommendations will depend critically on the perceived 'quality' of the audit product. This was evidenced through

²⁵ Acumen Alliance were provided files by the Performance Audit Branch during this review which purported to show the follow up action taken by the Branch to monitor and review the overall level of acceptance and implementation of the recommendations it makes. This file was clearly incomplete and did not show regular follow up or contact with Agencies. Thus we concluded that there was no systematic monitoring of the level of acceptance and implementation of recommendations.

comments from Audit Office clients interviewed during the course of this review. This is an area of significant concern for a number of audit clients.

The recent client survey identified the following high priority areas of concern requiring immediate action in relation to performance audit reports:

- produce fair and reasonable findings;
- clearly identify significant issues and their implications;
- produce useful recommendations; and
- listens to agency responses on audit issues.

Discussions held with the senior executives of eleven key government agencies during the course of this review corroborated the survey results.

As discussed previously there was generally a low level of concern with the accuracy of data and other factual information in tabled audit reports. There are some instances where the basic facts reported in some audits were challenged. The review of selected audits also found isolated examples where 'facts' presented in tabled reports were not supported in the working papers. However, there was no evidence of systematic failure in this regard.

Audit client concern with quality stems more from the quality of the analysis and interpretation of data and conclusion drawn from it. A number of clients interviewed expressed concern that often the analysis of data in an audit was 'too simplistic' and 'superficial'. Some performance audits were characterised as 'desk reviews' not supported by direct examination of source data.

There was some concern that the Office placed reliance for their data primarily on other analyses and reports undertaken by or on behalf of the Audit Client. Audits therefore did not identify any information that was not already known to the client. Nor did audit reports provide any useful insights into how to address known problems.

Agencies also indicated some concern about the lack of balance in reporting audit findings. This included the lack of context within which findings were discussed and the use of emotive language, in either the reports themselves or in statements to the media.

The extent to which these concerns manifest themselves in the quality and effectiveness of the audit product, can be ascertained from a review of management responses in tabled reports. A number of reports tabled in

the period subject to review contain responses which seriously challenge the validity of the audit findings and throw into question its credibility.

It is difficult to see how such public disputation improves either accountability or agency performance. On the face of it, the reader of the audit report is not able to ascertain whether and to what extent the management response invalidates the audit findings.

As a consequence of the public disputation, an agency is also more likely to find itself defending its position publicly, in many cases through the media.

Some agencies expressed concern that they were not able to 'get a fair hearing' at the report drafting stage to address what they perceived to be misunderstandings and misinterpretations by the Audit Office. There were indications that the Office did not want to hear what they had to say or was fixed in its viewpoint and was not receptive to some suggested changes. Agencies felt they could only address their concerns through the formal management response.

This experience added to the perception expressed clearly by ten of the eleven agencies that had been subject to Performance Audit and were interviewed during the course of this review, that while the Audit Office does not actively seek out or 'court' the media, it nevertheless measures its effectiveness at least partially through media interest. It is therefore in its interest to be controversial. Allied to the earlier concerns expressed in relation to the selection of 'public interest' topics, this perception by clients of media 'bias', exposes the Office to a loss of credibility in the sector within which it is trying to 'improve performance'.

The review considered whether this perception was grounded in reality. It is observed that a Reporting Strategy is required to be prepared for each audit. This strategy includes the need to prepare a 'media leaflet' and 'media kit'. It also lists the radio, television and print media outlets that will be sent or faxed the media leaflet and the audit report.

Unlike some other jurisdictions the Audit Office does not provide embargoed copies of audit reports to the media prior to tabling. However, it does pre-notify the media of the proposed report and the planned tabling date one week in advance.

After an audit is tabled a report is prepared and disseminated within the Office on the number of media stories generated. By contrast there was no evidence to indicate that references made to audit reports in other accountability forums (eg Question time, Estimates' and Standing Committees) are systematically monitored and reviewed.

It was also observed that audit working paper files contained copies of the media articles produced. Finally, an instance was noted of an internal email communication to performance audit staff where the fact that a number of media references had been made to audit reports in a major metropolitan newspaper in one week, was acclaimed as 'not a bad result'.

This evidence tends to suggest that there is a culture within the Audit Office that media interest is a legitimate measure of the effectiveness of an audit in terms of improving public accountability.²⁶ This would not necessarily be an issue provided that it was one (minor) measure of many.

As it stands there are few other measures of output effectiveness utilised or available to the Office. Recent results in relation to these other measures suggest that the quality and credibility of the performance audit product is not as high as it needs to be. If the Office is to achieve its mission of improved performance as well as improved accountability it needs to better track its effectiveness.

RECOMMENDATION 34 (HIGH PRIORITY):

The composite 'client satisfaction' and 'chargeable time' measures be disaggregated and reported separately for performance audits and financial audits.

RECOMMENDATION 35 (HIGH PRIORITY):

The approach to the resolution and public reporting of disagreements with audit clients be reviewed. Consideration be given to moving to an 'agreed report' model or to the incorporation of management comments at relevant sections throughout the report.

²⁶ The email referred to in this section was provided to us by staff from the Performance Audit Branch and provides evidence to support our statement that the Audit Office focuses on 'media hits'. This email, dated 21 February 2003, from the Auditor General to the Assistant Auditor General Performance Audit stated, "Three SMH editorials in the one week referring to our reports - not bad!!". The Assistant Auditor General Performance Audit then forwarded this email to all Performance Audit Branch Staff stating, "Let's take a bow everyone. Not a bad result!!"

RECOMMENDATION 36 (HIGH PRIORITY):

The proportion of audit recommendations accepted by the client be used and reported as an effectiveness indicator for performance audits. This information be captured prior to the tabling of the audit report and incorporated in the appendix to the report together with efficiency and effectiveness performance information on cost and cycle time.

RECOMMENDATION 37 (HIGH PRIORITY):

References made to audit reports in the Parliament be tracked where a cost-effective method of data capture can be developed.

7 Partnerships of Interest

POI (1) WHETHER IT WOULD BE APPROPRIATE FOR THE AUDITOR-GENERAL, ONCE HE HAS FULFILLED HIS ASSURANCE ROLE, TO ASSIST AGENCIES IN ACHIEVING THEIR CORPORATE GOALS AND REDUCE THEIR EXPOSURE TO RISK.

FINDINGS:

The Audit Office's mission is to "assist the Parliament to improve the accountability and performance of the State". That mission is compatible with the Auditor-General, once he has fulfilled his assurance role, assisting Agencies in achieving their corporate goals and reducing their exposure to risk.

Whether the Auditor-General should do so revolves around the degree to which the assistance would put at risk the Audit Office's "Audit Independence" either actual or perceived. Actual independence is at risk where the auditor is performing management functions or making management decisions and perceived independence is at risk where there is a perception that the auditor is too closely aligned with the entity's management.

Whether audit independence is compromised depends on the type of activity undertaken. As noted in Costs and Charges (3) that while there may not be concrete evidence that the provision of non-audit services on a fee for service basis impairs independence, within the private sector there is a move to separate the audit function from the consulting arm of many of the large international firms of accountants. The same argument is raised in relation to the Audit Office assisting agencies in achieving their corporate goals and reducing their exposure to risk.

Trends in role and reporting approaches in other jurisdictions has led to a number of State and Federal jurisdictions producing Better Practice Guides which are not seen to impact audit independence.

The Audit Office Better Practice Guides are written to assist agency management and are useful in assessing how an Agency rates in terms of better practice. The Audit Office produces a number of publications including:

- Better Practice Guides;
- Questionnaires used when conducting Audits;
- Professional Update (six monthly); and
- Awareness Newsletters (monthly):

It is the opinion of Acumen Alliance that the Audit Office should be encouraged to continue providing assistance to Departments and Agencies in achieving their corporate goals as long as it does not compromise their audit independence and is not fee for service work as suggested in the recommendations in our section on costs and charges.

POI (2) WHETHER THE AUDITOR-GENERAL COULD ALSO ASSIST IN ADDRESSING ISSUES COMMON TO AGENCIES ACROSS THE PUBLIC SECTOR.

FINDINGS:

The Audit Office is in a unique position as it regularly reviews all Government Agencies in New South Wales and has a wide mandate to report on waste of public resources or lack of probity or financial prudence in the management or application of public resources. Clearly the Audit Office could assist in addressing issues common to Agencies across the public sector. However, the assistance would have to be provided so as not to compromise Audit Independence.

The Audit Office addresses issues common to Agencies across the Public Sector through its special reviews which generally include reviews of Government Agency compliance with laws, regulations and government directions and other matters of importance. Recent reviews have covered:

- Collapse of HIH Insurance
- Compliance Review of Credit Card Use
- Compliance Review of Fully Depreciated Assets
- Compliance Review of NSW Government Superannuation Schemes
- Compliance Review of the Operations of Audit Committees
- Compliance Review of the Timing Requirements of the Annual Reports Legislation
- Compliance Review on Long Service Leave Entitlements
- Compliance Review on Motor Vehicle Operations and the Usage of Fuel Cards
- Compliance Review on Production of Year-end Financial Reporting Requirements
- Compliance Review on the Delegation of Authority
- Compliance Review on the Issuing of Fines and Penalties
- Cost of the Olympic and Paralympic Games
- Maintenance of Infrastructure Assets
- Use of Public Resources for Political Purposes.

The Audit Office could assist in identification of issues which need to be addressed centrally. Issues which would clearly impact audit independence should be referred to the appropriate central agency or authority for address.

Discussions with Audit clients indicated that the Audit Office could perform an assistance role through the provision of workshops on issues relating to risk management, audit techniques and accounting applications. During conduct of this review the Audit Office indicated to the Review Team that it felt that whilst there was a role for the Audit Office to play in provision of such workshops, that the primary role falls to Treasury in the areas of risk management and accounting. Whilst recognising this, there is a clear role as the independent regulator in New South Wales, for the Audit Office to facilitate and assist Agencies in understanding better practice risk management etc and how Agencies can create greater accountability and efficiencies in their organisations.

RECOMMENDATION 38 (MEDIUM PRIORITY):

The Audit Office to actively identify and pursue issues where it can provide common assistance to Agencies across the public sector including provision of workshops on issues relating to risk management, audit techniques and accounting applications.

POI (3) WHETHER AUDIT OFFICE GUIDANCE HAS BEEN INCONSISTENT WITH GUIDANCE FROM CENTRAL OR OTHER AGENCIES AND, IF SO, WHETHER THIS CREATED DIFFICULTIES FOR AGENCIES IN THEIR DEALINGS WITH THOSE "GUIDANCE" AGENCIES OR THE AUDIT OFFICE.

FINDINGS:

The review did not identify any specific Audit Office guidance that had been inconsistent with guidance from Central or other Agencies.

Discussions with Audit clients did not identify any specific difficulties for Departments and Agencies in their dealings, created by guidance from various Central Agencies.

There are no recommendations for this finding.

POI (4) HOW THE AUDIT OFFICE SHOULD COORDINATE THIS WORK WITH CENTRAL AGENCIES AND OTHER AGENCIES THAT PROVIDE GUIDANCE.

FINDINGS:

Discussions with Audit clients indicated that while the Audit Office guidance and that from other jurisdictions was helpful there is a considerable number of central and regulatory agencies. Independent Pricing and Regulatory Tribunal (IPART), Independent Commission Against Corruption (ICAC), Environment Protection Authority (EPA), Ombudsman's Office, NSW Treasury, Premier's Department, Department of Public Works and Services (DPWS) and Department of Information Technology and Management (DITM) together with a number professional bodies are currently producing guidance on a range of issues. The view expressed by the Audit clients is that there is considerable guidance being produced but there is a need for a coordinated approach to the production of the guidance.

The view expressed by Audit clients in discussion was that while the Audit Office has a central role in relation to accounting, auditing and risk management issues, there was however a need where issues are determined to be common to Agencies across the Public Sector for a better network amongst the various Agencies to determine which Agency should be the authority on a particular issue. That authority should then produce guidance which may be commented on by other Agencies prior to issue and implementation.

RECOMMENDATION 39 (LOW PRIORITY):

It is recommended that the Audit Office continue its practice prior to publishing guides of requesting comment on the content from other Central or Authority Agencies to ensure that duplication of guidance is eliminated.

8 Audit Communication

AC (1) - THE EFFECTIVENESS OF COMMUNICATION BETWEEN THE AUDIT OFFICE AND THE AUDITED AGENCIES

FINDINGS:

The AG has recognised the importance of ensuring effective communications between his office and audited agencies. A key action of the Corporate Plan is the external communications strategy, which includes the biennial client survey and a proposed review of the communications component of the financial and performance audit processes. However, this communication strategy is an internal document.

As discussed in other chapters of this report, as part of this review Acumen interviewed a number of Audit Office clients. During these interviews, performance, compliance and financial audit were discussed in detail.

Audit Office clients in the majority of instances were strongly supportive of the Financial Audit Branch of the Audit Office and felt that a very strong working relationship existed between themselves and the Audit Office. Whilst the level of satisfaction with the Financial Audit Branch of the Audit Office was high, the same could not be said for Performance Audit.

Communication concerns raised by Audit Clients in relation to Performance Audit and Compliance Audit have been covered within the Performance Audit and Compliance Audit components of this report and will not be repeated here. Accordingly, within this Section we will deal directly with Financial Audit Communication.

FINANCIAL AUDIT:

Key written communication to Audit Clients include the engagement letter, client service plan, client assistance schedule, client service report (on large audits) and management letter. The client service plan includes as an appendix a "Guarantee of Service" which outlines the Audit Offices standards of service delivery, including elements in relation to audit communication.

The Audit Office Practice Manual states that client service plans should be delivered where possible by the Engagement Controller to the Audit Committee of the client.

There is detailed guidance on the timing and nature of management letters contained within the Audit Office Practice Manual which is aimed at ensuring compliance with AUS 710 "Communicating with Management on Matters Arising from an Audit". One of the Audit Office's performance indicators reported in its Annual Report is on the timeliness of draft management letters.

In addition, following amendments to the Finance & Audit Act 1983 under Section 52(4), the Auditor-General is now providing the Head of each Agency a summary of the relevant section of each proposed report to Parliament. These reports are also being provided to Agency staff during the course of production to ensure factual accuracy and alert Agency staff to any critical comments.

Whilst noting the overall level of satisfaction with the services provided by the Financial Audit Branch of the Audit Office, discussions with a range of clients indicated a number of areas that could be improved: These included:

- Management letter points not being raised with the appropriate level of Agency staff on a timely basis;
- A lack of discussion on issues prior to inclusion in draft reports. Based on our discussions with clients it would appear that the key point here is that issues need to be discussed upfront, with the appropriate level of client management, facilitating the "no surprises" approach adopted by the Audit Office; and
- A lack of time to consider the issues in the Reports to Parliament.

The framework for appropriate client communication is included within the Audit Office Practice Manual. However, the issue appears to be communication of these protocols and ensuring they are applied.

Some of the clients interviewed indicated apparent poor change management, when senior members of the Audit team change. Specifically this resulted in a lack of understanding of audit issues and changes in the Audit Office's stance on certain long-term issues.

RECOMMENDATION 40 (HIGH PRIORITY):

A formal communication strategy be issued and made available to all clients. This has been successfully undertaken in other jurisdictions such as the US GAO. The communication strategy can be used as part of a "quasi client service level agreement to strengthen client relationships. Much of this strategy would be based on the existing protocols included in the Audit Office Practice Manual.

RECOMMENDATION 41 (HIGH PRIORITY):

Increased focus by Engagement Managers and Controllers on ensuring timely communication of issues to management. Specifically this could include some innovations in audit communication, such as:

- always ensuring management letters are raised following interim audit work where issues arise; and
- provision of weekly (or on a timeframe considered reasonable between the client and the Audit Office) "audit issues" papers to clients, outlining the issue and who is dealing with it from both an Audit Office and Client perspective.

RECOMMENDATION 42 (HIGH PRIORITY):

A client feedback survey (over and above the two yearly client survey currently conducted) be introduced as part of the audit finalisation. This survey should be made mandatory and the issuing, collation and reporting of survey results should be the responsibility of the Policy & Research Branch to provide independence. Feedback on individual staff performance as a result of receipt of the survey should be fed into the staff performance appraisal process.

9 Staff of the Audit Office and Administration

SAO (1) - THE AUDIT OFFICE'S CURRENT PRACTICES IN THE RECRUITMENT, TRAINING, COMPETENCY, REMUNERATION, RETENTION AND PROFESSIONAL DEVELOPMENT OF STAFF, AND WHETHER THEY EQUIP THE AUDIT OFFICE TO ACHIEVE ITS TASK, BOTH FOR FINANCIAL/COMPLIANCE AUDITS AND PERFORMANCE AUDITS.

FINDINGS:

The vision of the Audit Office of NSW is:

“To be Recognised as a Centre of Excellence in Auditing”.

Its stated mission is:

“Assisting Parliament improve the Accountability and Performance of the State”.

This is a significant role that the AO has assumed. The AG in a speech to staff launching the AO Human Resources Strategy²⁷ noted that the office is

“...responsible for reporting on the operations of the second largest consolidated group of entities in the nation, with net assets of almost \$100 billion and revenues of over \$45 billion. We are providers of professional audit services to both the Parliament and 450 NSW government agencies. This includes 47 of the Top 1,000 Australian corporations as listed by the BRW.”

Such responsibilities require an organisational structure, processes, rewards and people that are integrated in a manner that facilitates the outcomes sought internally by the Audit Office, by clients and key stakeholders as well as the expectations of the accounting profession and the NSW public.

²⁷ Human Resources Strategy, launch to staff 27 November 2002

There appears to be a difference of opinion amongst stakeholders as to who the clients of the Audit Office are. In undertaking performance/compliance audits, the client is the NSW Parliament and not the Agency/Department. In undertaking financial audits it could be argued that whilst Parliament is the ultimate client that the Agencies/Departments are also clients. The AO recognise that whilst it sees Parliament as its primary client, its clients are:

- The NSW Parliament
- Government Departments and Agencies
- Ultimately NSW taxpayers

This is recognised in the AO Practice Manual.

The difficulty the AO faces is the reconciliation of the disparate needs of the NSW Parliament and client departments and agencies. From an agency perspective, there is a need for reports from the AO to contain advice that is practicable and workable and that reflects a proper appreciation of the environment that the organisation works within. From a government perspective there is a need for reports that, inter alia, can provide early advice on issues that may impact on the delivery of government services. These diverse needs are not irreconcilable. However, AO staff need to be aware of the differing emphases in the reports to ensure that client and stakeholder needs are met effectively.

There are a number of implications inherent within the Vision and Mission statements of the AO. The first is that the office actively seeks recognition by the groups noted above as possessing staff, systems, policies and procedures that reflect best practice. In itself, this is an admirable aim for the organisation. However, the backgrounds of a broad range of clients and stakeholders will have an impact on the ability of the AO to meet such a diverse range of needs.

The Audit Office Human Resources Strategy defines what the Audit Office considers to be a centre of excellence, although the major aim of the Strategy is aimed at Parliament being the main client of the Audit Office, with a much lower focus on other key stakeholders such as Departments/Agencies. Thus the manner in which a centre of excellence is established would focus staff on predominantly the needs of only one stakeholder, being Parliament.

The Review Team would see the client base of the Audit Office in the broader sense of including Parliament and the Departments and Agencies. Whilst Parliament is the primary client, Departments and Agencies are part of Government. It would be simplistic to consider the two needs separately as each are linked at the Ministerial level, legislative level and the policy level. Politicians who head agencies are an intrinsic part of Parliament. The question therefore to be asked is how can one be addressed without the other?

Given the current strategy focuses only on the needs of Parliament as the main client, Acumen Alliance sees an inherent danger that the needs of Parliament may conflict in part with the needs of other key stakeholders. Thus, there may be occasions where the needs of Parliament conflict with the stated requirements of Departments and agencies who utilise the services of the Audit Office and thus the Audit Office becomes the 'meat in the sandwich'. It is therefore the belief of Acumen Alliance that the strategy needs to identify how staff will be trained to reconcile and manage these diverse needs.

HUMAN RESOURCES STRATEGY:

In November 2002 the AO Human Resources Strategy was launched by the Auditor-General. The strategy focuses on the key attributes necessary to build the AO to become a Centre of Excellence. These attributes include addressing:

- Organising, including structure and methodologies;
- Attracting, motivating and retaining staff;
- Developing staff, and
- Performance, including the alignment of organisational and individual goals and focussing on the right competencies for staff.

This strategy and the focus of its activities are strong and well founded. It reflects an organisation with a view to the future and a well developed plan to take itself forward. The workstream timeline set within the strategy document sets out a number of activities that extend right November 2002 through to June 2004 and the strategy is now in the first phase of its development.

Acumen Alliance is of the view that whilst Parliament may be seen by the Audit Office as the primary client, we believe that the client base must also considered to be Departments and Agencies. Our views are therefore

expressed on this basis. Given this view there are therefore a small number of issues that require clarification and consideration.

Whilst acknowledging the need for staff to take a client-centred approach and reflecting on the direct accountabilities to the NSW Parliament, the strategy does not provide detail regarding other stakeholder needs, expectations and assumptions, i.e. Departments and Agencies. This lack of detail makes it difficult to develop specific activities that reflect not just the present needs of the client base but also the future needs. For the strategy to provide a level of confidence to staff, Parliament and the many agencies that the AO provides services to it is important that their views be represented in strategic documentation for the office, including an understanding of what the needs of Departments/Agencies are.

In 2001 a market research firm was commissioned to, inter alia, assess how the AO is perceived by Parliament and audit clients. Whilst the broad range of respondents from the three client groups (Parliamentarians, Performance Audit Clients and Financial Audit clients) was generally positive, there were a number of issues that were of concern. These included:

- A considerable turnover in the composition of their allocated financial audit teams
- The allocation of staff to perform audits in a timely manner
- Having professional, competent staff working on audits
- A perception that auditors were too legalistic and pedantic.

Audit Office staff interviewed during the conduct of this review indicated that the issues arising from the 2001 survey had been fully addressed.

The draft report from the Client Satisfaction Survey conducted in January 2003 has recently also been received by the Audit Office. The response rate was over 50% including 81 CEO's to a shortened version and 77 (mainly CFO's) to a longer version of a financial audit survey and 15 respondees to a performance audit survey. This included a high client satisfaction index result. However there were a number of issues identified as requiring a quick response that link in with the human resources strategy.

The findings were backed up by a smaller survey undertaken by the review team of large, medium and small Departments and Agencies which found that clients were critical of a number of aspects of service delivery, especially in areas to do with performance audit. This is discussed in more detail in our section on Performance Audit.

It will be important to factor feedback from the 2003 Client Satisfaction Survey into the Audit Office Human Resources Strategy and to ensure a process of monitoring takes place after implementation of the strategy to ensure that the concerns raised by clients are adequately dealt with.

The range of activities proposed to be undertaken within the Human Resource Strategy has resulted in a significant time frame being envisaged within the report. There is a danger from a change perspective that staff of the AO will slowly lose confidence with and commitment to the outcomes sought in the strategy if substantial change is not initiated and undertaken within the next 6 months. Rather than undertaking an incremental approach to change within the office, there would be significant advantages if the speed of strategy implementation was increased and a number of "early wins" realised to facilitate the continued support from AO staff to the change process.

RECOMMENDATION 43 (HIGH PRIORITY):

It is recommended that the timeline set for implementation of the Human Resources strategy be reviewed and implementation of key activities be brought forward.

In particular, it is recommended that activities associated with performance management, resource management, work practices and resource planning be addressed by December 2003.

At the same time, the opportunity for "early wins" be identified and facilitated to facilitate the continued support of staff.

The scope of change underlined in the Strategy will require significant resources and expertise within the AO to ensure that the necessary initiatives are undertaken successfully. In reviewing the resources allocated to the tasks by Acumen Alliance and our interviews with a number of Audit Staff during this review, concerns were raised regarding the capacity of the HR team to undertake these tasks within the current set timeframe. It is also the professional opinion of Acumen Alliance that the current team lacks adequate resources to fully facilitate the full range of change activities.

It is essential that the strategy implementation process be undertaken in a manner that reflects on the professionalism of the Audit Office. There is significant evidence that this professionalism has been amply demonstrated in terms of the strategy development and communication activities undertaken so far. The risk inherent however in taking the strategy forward to implementation is the scope of staff resources, both in terms of numbers and expertise.

RECOMMENDATION 44 (HIGH PRIORITY):

Whilst recognising that the Audit Office has already issued RFP's to obtain expert resources externally to assist with the strategy and that an external program advisor has been appointed, it is recommended by Acumen Alliance that the staff resources allocated to the implementation of the Human Resources strategy still be reviewed, both in terms of numbers and expertise.

RECRUITMENT

The recruitment of AO staff is undertaken utilising one of the following options:

- Advertising in the Public Sector Notices
- Graduate recruitment through universities
- School-leaver recruitment
- Newspapers advertisements
- Utilisation of recruitment consultants.

Whilst noting the numbers of Graduate staff and School Leavers employed from external sources by the Audit Office, the majority of audit positions advertised in the period 2000-2002 were filled by internal applicants.

Figure 1-Successful applicants for period 2000-2002

Grade	Internal	External
SES	1	
Senior Officer	3	1
Audit Manager	12	
Auditor	18	1
Audit Senior	33	10
Audit Clerk 1/2	4	
Total	71	12

Whilst over 83 positions were available for filling in the period, 17% of positions were filled by suitable applicants external to the AO.

The Audit Office wishes to be recognised as a Centre of Excellence in Auditing. Whilst the Audit Office as part of its HR Strategy is focussing, in part, on the learning and development aspects of its current staff it currently utilises a “passive” approach to recruitment. Other than in graduate recruitment the Audit Office does not appear to actively seek out staff who possess the competencies and experience to take them to the “Centre of Excellence” level. Instead, the organisation relies on quality applicants responding to internal public sector advertising. Whilst Acumen Alliance notes that the NSW Government favours a passive approach to recruitment, the lack of an active approach to recruitment where appropriate personnel are sought out using means other than internal public sector advertising results in the Audit Office having little choice in who applies and who they choose from the small pool of applicants.

An alternative approach would be to make greater use of recruitment consultants for middle to senior management positions. Whilst the Audit Office has utilised this approach in a small fashion to date, it is the opinion of Acumen Alliance that it should be given more focus and priority. The approach of utilising recruitment consultants would not be taken in isolation to the traditional forms of recruitment but would be utilised side by side. The benefits of this approach would be that the pool of potential recruits would be widened, the focus of recruitment could be focussed on particular skills and/or experience and individuals in particular agencies or industries could be targeted based on their experience and/or expertise. It should be emphasised that any changes should continue to reflect public service recruitment standards in relation to any new or revised policies and procedures.

An additional issue identified in reviewing recruitment was the lack of specific industry expertise sought when engaging new staff into the organisation. Client survey results, and consistent feedback from AO clients interviewed as part of this review, identified an issue from an agency perspective that AO staff lacked an understanding or expertise of the “industry” the agencies worked within.

This can have a significant impact on the capacity of individual staff working within agencies to develop an in-depth knowledge within a comparatively short period of time and to utilise their analysis skills to identify issues of importance. If in recruiting the AO specifically sought experience in particular agencies or industries as well as technical expertise it is suggested that significant benefits would be reflected in client feedback.

Whilst it is understood that staff develop expertise over time in particular areas of agency environments, there appears to be little attention placed on attracting staff who already possess this expertise. To improve the level of expertise within the Audit Office there is a need to look to the private sector to develop internally the expertise, experiences and competencies required. Whilst it is acknowledged that the Audit Office send staff on conferences, this is hardly sufficient and resource intensive to get staff to a sufficient level of knowledge in terms of a detailed understanding of industries.

RECOMMENDATION 45 (MEDIUM PRIORITY):

It is recommended that a greater use of recruitment consultants be utilised in non-SES positions, and that when recruiting for non-base level positions experience in agencies or industries in addition to high-level technical skills be emphasised.

TRAINING, PROFESSIONAL DEVELOPMENT AND COMPETENCIES

The Audit Office currently has in place a one year Learning and Development Plan for 2002-2003. This has been designed as an interim measure prior to the formal rollout of the learning and development programmes contained within the new Human Resources Strategy.

Specific areas for greater focus in 2002-2003 have been identified as the provision of:

- SES Development training;

- Technical and non-technical skills
- Supervisory and managerial skills across the office.

The Audit office does not set a target for training hours against positions other than in hours contained within area budgets. The individual needs of staff are ascertained through the performance management process to determine the type and amount of training to be provided. Senior Audit Office Management advised Acumen Alliance during this review that all staff had recently undergone full performance assessments.

During the course of this audit we interviewed a large number of Audit Office Staff. Whilst a number of staff who were interviewed indicated a level of satisfaction with the Performance Management process, five staff advised that they had not yet undertaken a formal performance management process, providing contrary opinion to that provided to us by Senior Management.

Whilst this is a matter of concern, it is understood that the new performance appraisal process is still being “bedded down” within the AO, and it is expected that all staff will eventually be managed along the new system.

Figure 2-Training Hours for Audit Staff Feb 02-03²⁸

Title	Level	Number of Staff ²⁹	Training Hours	Average
Auditor-General	SES Level 7	1	6	6
Deputy Auditor-General	SES Level 5	1	35	35
Assistant Auditor-General	SES Level 4	4	91	23
Director of Audit	SES Level 2	14	443	32
Principal Performance Auditor	SES Level 1	1	27	27
Senior Audit Manager	Clerk Gr 11-12	25	609	24
Audit Manager	Clerk Gr 9-10	16	615	38
Assistant Director of Audit	Senior Officer Grade 1	3	66	22
Auditor	Clerk Gr 7-8	48	1062	22
Audit Senior	Clerk Gr 5-6	44	1275	29
Senior Audit Clerk	Clerk Gr 3-4	21	1286	61
Trainee Auditor	Clerk Gr 1-2	24	2815	117

The above diagram lists the number of training hours undertaken by staff against their level within the Audit Office. As can be seen from the diagram, staff at the Trainee Auditor (117 hours) and Senior Audit Clerk (61 hours) levels receive by far the greatest allocation of training in the organisation compared to their colleagues.

The type of training undertaken by staff is mixed, and emanates from the need to maintain professional qualifications, feedback from supervisors during performance reviews, office wide needs, initiatives from senior management and individual needs assessment.

It would be expected given the need to ensure Trainees and Graduates understand and are competent in Auditing that as newcomers to the profession they would receive a high level of training in the first years of

²⁸ Data based on information supplied from the AO

²⁹ This is a reference to the number of staff who undertook training Feb 02- Feb 03, and not to the total number of staff in this classification.

their employment. There is also a professional requirement on all professional staff within the office holding CPA or CA qualifications to meet the ongoing CPE requirements of those professional bodies.

Training records should reflect the training provided to staff internally, as well as reflect all training that professional staff have undertaken externally.

In reviewing the broad range of technical and generalist skills training provided to staff over the last twelve months there appears to be little evidence of a structured approach to determining learning outcomes linked to performance management and organisational needs. Our detailed review of Audit Office documentation and detailed interviews of staff during this review indicated that, excluding organisational-wide initiatives emanating from the Audit Office's senior management and professional competency requirements, many of the courses undertaken lack consistency or alignment. A degree of training appears to have been determined simply on an appreciation between the manager and staff member on what would be useful for the staff member, without an apparent link to organisational needs as indicated in the Human Resources strategy. This approach, whereby training is based more on individual preference rather than linking training to performance management and operational needs is considered problematic.

RECOMMENDATION 46 (HIGH PRIORITY):

A formal training needs analysis be undertaken that will assist in providing an alignment between the needs of clients and the AO with the learning outcomes of staff training. The training needs analysis should examine:

- Currency of professional qualifications;
- Client and key stakeholder needs;
- Management training issues;
- Developments in the auditing profession;
- Developments in the agencies audited.

An area of training which does not appear to be generally identified either in program documentation or in records of training undertaken is the development of specific understandings of client agency environments. Whilst there is evidence that officers of the AO possess significant technical skills, the training provided in-house does not appear to include significant learning in areas dealing with client environments.³⁰ The impact of this is that inexperienced staff may be utilised on projects requiring a significant understanding of a client agencies operations, environment and outputs.

RECOMMENDATION 47 (MEDIUM PRIORITY):

Additional opportunities be provided for AO personnel to gain a detailed understanding of client agencies operations and activities. This may be achieved through outplacements, attendance of training at client premises or the utilisation of client personnel in the development of in-house training programs.

REMUNERATION

The remuneration of staff was considered in the light of the high resignation rate of graduate audit staff. There was strong anecdotal evidence presented to the review team that many graduate accountants leave the AO after around 3 years experience having completed the CA Program of the Institute of chartered Accountants in Australia and obtaining their CA designation. The project team spoke to a number of graduates who indicated that whilst there was an excellent working environment within the AO, the larger accounting firms were in a position to pay higher salaries for CA's with a few years experience and that promotion and work experience was seen to be better within the private sector.

The review team examined salary scales for auditors within the public sector compared to the private sector. As soon as audit staff gained their professional qualifications and had a number years experience the private sector salary ranges appeared to exceed what was generally available to public sector staff.

³⁰ Whilst acknowledging this we do make note of the 2001-2002 Annual Report which details a number of placements made by the AO, which included:

- Eight staff to other state government agencies;
- Four staff from other agencies worked temporarily in the NSW AO; and
- Nine staff travelled and worked overseas, mostly in UK government audit agencies.

With 2-3 years experience auditors in Sydney can expect a average remuneration package of around \$55,000, up to an average of \$68,000 with 5+ years experience. Audit managers can earn between \$80,000 to \$135,000 in the private sector, again depending on experience.

Figure 3-Public Sector Auditor Salaries Audit Senior-Senior Audit Manager

Audit Senior	
1st year	49,764
2nd Year	51,334
3rd Year	53,346
4th Year	54,910
Auditor	
1st Year	56,554
2nd Year	58,246
3rd Year	60,673
4th Year	62,601
Audit Manager	
1st Year	64,466
2nd Year	66,279
3rd Year	68,986
4th Year	71,041
Senior Audit Manager	
1st Year	74,562
2nd Year	77,724
3rd year	82,593
4th Year	86,231

The Audit Office faces a difficult position with the remuneration of staff. Whilst its starting salaries and provision of paid professional development attract many graduates, the salary differentials that occur as soon as staff gain professional qualifications and experience in the office mean that many promising auditors will leave the AO within 5 years of joining.

An issue that was raised in discussions with staff were the many salary levels extant within the AO. There are currently seven levels between trainee auditor and the most senior non-SES position within the office. This potentially has an impact on the capacity of talented staff to rise rapidly within the AO and to achieve some degree of parity with those in the private sector. There would be value in the AO reviewing the levels currently in place with a view to reducing the levels to potentially three:

- Trainee Auditor
- Senior Auditor
- Managers

Within each level it would be possible to create a small number of increments which would be payable based on the training undertaken and experience of staff members.

RECOMMENDATION 48 (MEDIUM PRIORITY):

Whilst acknowledging that the Audit Office is on the way to this, the current non-SES levels of auditor be reviewed and where possible reduced to enable staff to have access to a more streamlined promotion and remuneration process. These levels should be similar to:

- Trainee Auditor
- Senior Auditor
- Managers

RETENTION

The NSW Audit Office experienced 26 employee resignations in 2001/2002, which represented a turnover of 12.5%³¹ This rate of turnover, whilst not significant overall compared to other public and private sector audit organisations, is of relevance when reviewing which groups within the AO was the figure most significant.

The following matrix shows the resignation rate of trainee auditors within the NSW AO. As has been noted earlier, trainee auditors as a resource are a significant cost to the AO. However, it is understood from discussions with the Auditor General and the Deputy Auditor General that the Audit Office views the cost as not highly significant compared to the value new

³¹ This turnover rate was a significant improvement on the rate over the previous two years, which were 17.5% in 1999/2000 and 23% in 2000/2001.

auditors bring to the office in terms of capability, capacity for promotion and the ability to bring fresh approaches to the organisation.

Figure 4-Trainee Auditor Resignation Rate³²

Commencement year	Number of Resignations from Total Intake for Year	% of total intake for year
2002	2/20	10%
2001	4/20	20%
2000	10/21	48%
1999	9/21	43%
1998	16/25	64%
1997	17/19	89%
1996	13/14	93%

As can be seen from the matrix, the resignation rate percentage of trainee auditors increases significantly the longer the individuals have stayed in the organisation, from a 10% separation rate from the intake in 2002 up to 93% from the intake in 1996.



This loss of talented staff has serious implications for the AO. The AO has invested heavily in recruiting and training its graduate staff. Graduate trainees cannot be considered 100% “effective”³³ as auditors until they have had at least 1-2 years experience working within the government environment. Yet within 3 years, when graduate staff have gained a significant level of experience, nearly 50% will have resigned from the AO. There is also another issue associated with the high resignation rate of graduates. These officers are the potential middle managers and senior

³² Based on data provided by the Audit Office

³³ By “effective” it is meant that the staff member possesses both the theoretical knowledge as well as practical on the job knowledge sufficient for them to undertake their roles effectively.

managers for the future. With experience, both as auditors and as managers within the workplace it can be expected that a number of them will successfully compete for senior managerial positions. Yet such a high resignation rate leaves far fewer officers to progress within the system. Instead, after a couple of years experience many are leaving to join large private sector accounting firms or accounting positions in other government agencies.

The experience of the AO currently with retention of graduates is in our opinion no different to that experienced by the big accounting firms, where the experience of the loss of recent graduates is similar. The answer is not that the AO should stop employing graduates, because the organisation will always have a need for staff to undertake the important yet more basic aspects of the work of the organisation.

Indeed, the AO believes that there would be a significant level of difficulty attracting staff if experienced staff were employed for this work and this would have a significant impact over a number of years time on the staffing profile (which would potentially impact fees and the ability to do the work that they require).



Whilst a significant number of staff leave at lower levels, at the more senior middle management and senior management levels there would appear to be a much higher retention rate. However, it is understood that a significant percentage of senior management will in the next few years be reaching retirement age, which will have an impact on the senior management level of the office. Collectively, a significant degree of experience and expertise will leave the AO. Whilst the Audit Office recognises that there will be a significant issue with senior staff about to retire and has stated this in its HR Strategy, it is the opinion of Acumen Alliance that greater evidence of specific activities to address this issue could be demonstrated. It appears that other than creating three new positions within current structures, which do not in themselves address the fundamental problem, the Audit Office has done little to facilitate a long term solution.

RECOMMENDATION 49 (HIGH PRIORITY):

It is recommended that the AO develop and adopt formal succession planning strategies to address the impact of the departure of senior staff.

- The AO should identify its existing competencies, related to both its internal leadership needs as well as the needs of the public sector.
- The AO needs to evaluate and assesses current middle management employees to determine how they meet the needs of the AO for senior management positions.
- The AO introduces where appropriate coaching, mentoring, training, and recruiting methods that match personnel requirements – and future needs.

A number of staff when requested for reasons for their departure expressed a level of dissatisfaction with promotion opportunities. Interestingly, many of the reasons for leaving provided in the sample did not indicate a willingness to move to the private sector, but were more concerned with the lack of ability to gain promotion within the small office. The streamlining of positions within the Audit Office recommended above will address some of the issues arising from this concern.

Figure 5-Reasons for Departure 07/01-06/02

Position	Type of Separation	Reason for Leaving
Deputy Auditor-General	Excess officer	Excess
Director of Audit	Retired	Retirement
Audit Manager	Voluntary	Senior executive promotion
Performance Audit Manager	Voluntary	Dissatisfied with promotion progress
Auditor	Voluntary	Dissatisfied with AO client
Auditor	Voluntary	Family reasons
Audit Senior	Medical Retirement	Medically retired
Audit Senior	Voluntary	Dissatisfied with AO client
Audit Senior	Voluntary	Private sector audit firm
Audit Senior	Voluntary	Another area of accounting
Audit Senior	Voluntary	Dissatisfied with promotion progress
Audit Senior	Voluntary	Career change
Audit Senior	Voluntary	Dissatisfied with promotion progress
Senior Audit Clerk	Voluntary	Another field of accounting
Senior Audit Clerk	Voluntary	Work overseas
Senior Audit Clerk	Voluntary	Ill health
Trainee Auditor	Voluntary	Another area of accounting
Trainee Auditor	Voluntary	Career change
Trainee Auditor	Voluntary	Career change

SAO (2) - WHETHER APPROPRIATE INTERNAL REPORTING PRACTICES ARE IN PLACE TO ENABLE THE AUDITOR-GENERAL AND HIS MANAGEMENT TO ENSURE VALUE FOR MONEY IS BEING OBTAINED IN UNDERTAKING AUDIT ENGAGEMENTS.

FINDINGS:

Do internal reporting practices ensure value for money, and are current recording and costing systems appropriate?

The Audit Office manages a number of systems to capture costs, provide human resources data and facilitate management reports. These systems include:

- TOPS
- CHRIS
- Sun Systems.

In reviewing the management reports as currently developed the subject matter contained within the documentation appeared to lack:

- Analysis of quantity and price variances when comparing standard costing with actual cost;
- VFM reporting in terms of quality and effectiveness indicators;
- Internal benchmarking between Financial Statement audit engagements and evidence of reporting on this;
- Alignment between different reporting systems.

It is understood that the proprietor of the TOPS system is currently in liquidation, and that expertise and support for TOPS currently resides with one officer within the Audit Office. There is potential risk in the current arrangement. Whilst it is understood that TOPS at is currently configured broadly meets Audit Office requirements, the lack of support for the system outside the Office means that significant issues that may affect the system cannot be addressed other than through the skills and expertise of one officer within the organisation. If that officer was to leave the Audit Office the organisation would find itself in a particularly difficult position regarding its ability to support the system.

We understand from discussions with the Audit Office that a number of Audit Offices use the system, that they find the system stable and that the Audit Office believes that it can operate with the level of reports that are currently available within the system. However, given the above analysis it would be prudent and appropriate to test the market to ascertain whether an appropriate replacement can be found.

Similarly, there appeared to be weaknesses in the capacity of the financial, business and HR systems to align and integrate the data created. High level management reports require not just data but information to enable effective knowledge management processes to operate effectively within the organisation. The reports currently generated lacked a significant degree of integration and appeared to facilitate a greater degree of data, rather than management information. These issues were exacerbated by inconsistencies found by the review team in the way staff charge their time accurately against reports.

RECOMMENDATION 50 (HIGH PRIORITY):

It is recommended that the services currently provided by TOPS be put out to tender to identify whether alternative options are available in the marketplace that can meet AO requirements within an affordable budget. In reviewing alternative options to TOPS it is recommended that the degree of integration available within current AO management information systems be reviewed with the goal to facilitate greater integration.

ADMIN (1) - WHETHER THE FACT THAT THE AUDIT OFFICE IS UNDER THE GOVERNANCE OF THE PUBLIC SECTOR EMPLOYMENT AND MANAGEMENT ACT 2002 IS AN IMPEDIMENT TO ITS GOOD ADMINISTRATION.

ADMIN (2) - WHETHER COMMENCING SECTIONS 33A AND 33B OF THE PUBLIC FINANCE AND AUDIT ACT 1983 OR INTRODUCING SOME OTHER PRIVATE SECTOR MODEL WOULD IMPROVE THE MANAGEMENT OF THE OFFICE.

FINDINGS:

Legislation and the Management of the Office

Officers of the NSW Audit Office are employed under the provisions of the Public Sector Employment and Management Act 2002 (the Act). This legislation serves to address public sector employment and management in the NSW public sector, and repeals the Public Sector Management Act 1988.

Through the employment of public sector staff under the Act there is limited flexibility for departmental and agency heads to make decisions regarding some aspects of the running of their organisations. This is most apparent in the area of pay and conditions for staff.

Heads of departments and agencies within the NSW public sector are not able to make unilateral decisions regarding pay and conditions for staff. Rather, these matters are determined centrally by the government based upon recommendations from the Premiers Department. Agency heads may however make a case to the Director-General through section 130 of the Act which provides for changes in determinations being made in respect of the conditions and benefits of employment of officers and their salary, wages and other remuneration.

Not all NSW public servants are employed under the Act. Police officers, teachers and nurses within NSW are employed under legislation separate from the Act and enjoy pay and conditions different from other public servants.

Sections 33A and 33B of the Public Finance and Audit Act 1983 would allow the Auditor-General to constitute the Office as a body corporate for the employment of staff, and thus be in a position to determine pay and conditions for his staff separate from the rest of the public sector. This would mean that the Auditor-General would be in a position to unilaterally determine what salaries and conditions of service he would wish to pay. These sections have as yet neither been assented to nor commenced.

During detailed interviews with the NSW Public Sector Employment Office and Senior Audit Office Staff, opinions were raised that commencement of these sections should take place in order to provide the Auditor-General the opportunity to attract high quality staff from the private sector and other public sector agencies, as well as to assist in retaining high quality staff within the Office.

There are a number of considerations that need to be taken account of in this matter, including benefits as well as potentially negative consequences.

As has been noted elsewhere in this report and based on discussions during this review with the Auditor General and Audit Office Staff who had experience in both public and private sector auditing, professional audit staff within the Office are paid well as recent graduates as well as enjoying conditions of service in their professional qualifications years that are not equalled elsewhere within the market.

However, there is anecdotal evidence that suggests that as the auditing professionals stay longer within the office and successfully seek promotion the differentials that exist in their favour start losing their significance until, usually after three to four years, trained and experienced staff leave the Office for more lucrative careers in the private sector. There are a number of reasons why staff leave -this has been addressed elsewhere in this report. However, the lack of parity in terms of pay and conditions between the office and the private sector must be understood to be of particular significance.

If sections 33A and 33B were to be commenced the Auditor-General would be in a position where he could review the market rates for professional auditing staff and make a determination regarding the most appropriate increments of pay for his staff that could reflect or better market rates. In the short to medium term this approach would no doubt be successful in retaining current staff and attracting new staff.

However, there are a number of issues that would potentially impact on the benefits of a freeing up of pay and conditions within the Office. Chief amongst these is the potential for market forces to change in the medium term. Enquiries with a number of organisations suggest there is a lack of trained, well qualified auditors in the market. This has resulted in auditing staff commencing salaries in the private sector which are higher than some similarly trained occupations in the market. Whilst the Auditor-General may in the short to medium term attract more qualified staff by increasing salaries to reflect market trends, there is a risk that as the number of trained and qualified auditors grow and the market salaries differences lessen, staff within the Audit office will enjoy a high salary that is out of step once again with the rest of the market. This would potentially result in negative connotations for the Office and the government should the NSW public gain an impression that public sector staff are paid significantly more than their private sector counterparts as well as enjoying conditions of service that are not matched elsewhere. It would be difficult for the Auditor-General to address this issue once the decision had been made to increase salaries- whilst it is comparatively easy to raise salaries in line with market trends, it is not so easy in a public sector environment to lower salaries should there be a market decline. Acumen Alliance notes that there are other Departments within the NSW Government employing 'professionals' that face similar issues to that of the NSW Audit Office.

Whilst recognising the complexities of the Act, as noted earlier, there is flexibility in the system under section 130 of the Act for the Auditor-General to make a case for changes to be made in the rates of pay or allowances for staff of the Office to be made. However, the Director-General of the Public Sector Employment Office will, in making his recommendations to Government, be cognisant of the implications to the rest of the NSW public sector should professional staff in the Office gain an improvement in wages and/or conditions. Similarly, any increases in conditions will need to be backed up by either increases in revenues from work undertaken for other agencies, which is bound to prove unpopular, or through a case made to the Treasury for an increase in budget funding to meet the budget shortfall, which could also prove difficult in the current climate.

An alternative approach that may address the concerns raised regarding salary and conditions differentials would be to instigate a yearly allowance for staff that would “top up” the salaries of professional staff and lessen the differentials between public sector staff and private sector employees. It is understood that a number of agencies within the NSW public sector employ this approach when dealing with employment environments where public sector staff operate at a disadvantage compared to their contemporaries in the labour market eg. teachers working in certain rural areas.

The key advantage of this approach is its flexibility-salaries and conditions remain in line with the broader public sector, whilst an annual assessment may be made of the differentials in the labour market and reflected in the value of the allowance. As the differentials change each year, either up or down, so could the value of the allowance. This approach would not require commencement of ss 33A or B of the Public Finance and Audit Act, but could rather be undertaken under s. 130 of the Act. The assistance of Public Sector Employment Office could be sought to undertake an annual review of the market and could make recommendations to the Audit Office regarding parities and appropriate levels of allowance payable.

RECOMMENDATION 51 (LOW PRIORITY):

That commencement of sections 33A and 33B of the Public Finance and Audit Act 1983 not take place until full consideration of the costs and service-wide implications takes place. In particular, it is important to note:

- Level of alignment between the HR strategy and alternative recruitment and conditions of service;
- Service-wide implications of any changes in pay and conditions; and
- The cost of any changes, and sources for funding of those changes.

RECOMMENDATION 52 (MEDIUM PRIORITY):

Noting the complexities of the Public Sector Employment and Management Act 2002, consideration should be given to the payment of an allowance to reflect differentials currently in place between auditing professionals in the public and the private sector. This level of this allowance be determined annually, and be based on research and advice undertaken by the Public Sector Employment Office.

10 Costs and Charges

CC (1) WHETHER A PRIVATE SECTOR COMPETITIVE TENDER PROCESS WOULD BE USEFUL IN ASSESSING THE COMPARATIVE COSTS OF AUDIT.

FINDINGS

OUTSOURCING

The Audit Office undertakes a private competitive tender process, as set out in the Section of our Report dealing with Outsourcing, to ensure the provision of cost effective audit services and to enable the efficiency of in house audits to be benchmarked against those undertaken by the private sector contractors.

While the Audit Office acknowledges that a competitive tender process is useful in assessing the comparative costs of audit, the Audit Office does not however formally assess as part of the tender process whether its own costs and hours applied to an audit are comparable to that of the private sector.

The Audit Office does not maintain management information to identify the cost effectiveness of audit services or to benchmark Contract Audit Agents against in house work. While the Audit Office does have information detailing the Manager and Staff mix for audits contracted out it does not use the information to measure its own Manager and Staff mix for the same or similar audits. There is no database of information for management review of audits contracted out, regarding the number of contracts where performance was satisfactory, unsatisfactory (and the reason for that conclusion), where warnings are given or where contracts have been terminated (and the reason for termination).

Apart from a review of outsourced Area Health Services in 2001, there has been no recent internal benchmarking undertaken on the current contractors utilised by the Audit Office. As stated in the Section of our Report on Outsourcing, whilst the Audit Office has established a Benchmarking Committee there has been little progress related to either internal benchmarking or benchmarking outsourced service providers against internal Audit Office staff.

Our analysis shows that the outsourcing of 23 audits for the financial year ended 30 June 2003 resulted in a potential average reduction of the cost of audit by 10% while increasing the time spent on audit by 2% over the 2002 total. This would indicate that the competitive tender process is useful in assessing the comparative costs of audit.

However, the Audit Office has not evaluated whether the services provided by Contract Audit Agents are cost effective. The spread of fees bid for the 23 contracted out audits ranged between 148% and 48% of the 2002 fees, while the spread of hours indicated to be applied to the audits (as noted in the tender evaluation documentation) ranged between 168% and 64% of the 2002 figures. Without analysis of the variations in both costs and hours it is not clear whether contracting out results in a more cost effective audit or not.

MANAGEMENT FEES:

The fee the Audit Office charges the Audit client includes an amount to cover the Office's project management costs associated with outsourcing audits. The Audit Office provided us with an analysis that they had undertaken for Area Health Services Audits that had been outsourced. For Area Health Services the amount of increase is on average 15% of the outsourced service providers contract audit fee. Analysis of the Audit Office's hours charged to audits outsourced for the year ended 2002 shows that the additional hours used by the Audit Office to manage those Area Health Services outsourced service providers ranged between 3% and 14%. The average however was 7%. It is unclear on what basis the Audit Office 15% on cost was therefore calculated. However, it is clear that it is excessive in some instances where the actual on cost is calculated at 3% and needs to be reviewed and recalculated. A similar project should be undertaken for all other contracted out audits to ensure that the fees added on for project management by the Audit Office are reasonable.

RECOMMENDATION 53 (HIGH PRIORITY):

It is recommended that the Audit Office undertake a formal benchmarking exercise of currently contracted out audits to determine whether the comparative costs of audits charged by the private sector and the hours applied to the job is comparable with those charged by the Audit Office.

RECOMMENDATION 54 (HIGH PRIORITY):

It is recommended that the Audit Office should review its on cost percentage application for contracted out audits and align it with actual hours charged so that it is more equitable.

CC (2) – WHETHER THE AUDIT FEES CHARGED FOR FINANCIAL AUDITS ARE REASONABLE.

FINDINGS

Whether audit fees charged for financial audit are reasonable depends on how the fees are calculated and what the client is charged for. The reasonableness of the fees may be assessed by measuring the Audit Office's fees against benchmarks. Private sector fees for similar services, the method of calculation of the fees charged by the Audit Office and the levels of productivity and efficiency within the Audit Office which impact the fee structure can be used to determine reasonableness. The fees must be assessed in the light of any competitive advantage enjoyed by the Audit Office.

As a monopoly provider with a fixed and known client base the Audit Office should be able to schedule its audit activity, based on known commitments across the year, with maximum efficiency. The monopoly position means that it does not compete for business as a private sector firm does. Thus comparative to a similar private sector firm, the Audit Office should have low or no overheads in relation to marketing, business development and the risk of staff not being utilised due to loss of key clients.

A combination of input unit costs being lower than or comparable to the private sector and utilisation rates for staff (based on meeting reasonable targets), should result in audit fees (based on a full cost recovery model) being very competitive and reasonable.

For the year ended 30 June 2002 the total revenues from audit activities for the Audit Office was \$21.2m derived from audit fees charged to audit clients for financial statement audits. Included in the fee charged to clients is an amount of approximately \$1.3m that is a contribution to the cost of the Performance Audit program.

PRODUCTIVITY

Billable target hours for each staff level are determined after deducting from 260 total work days, 35 days for leave and professional development leaving 225 days for billable work.

Based on reports produced from TOPS (the Audit Office's management information system) the primary Financial Audit Branches have achieved 91% of billable targets. This has left a shortfall of around 30,000 billable hours or around 22 Full Time Equivalent staff. In assessing these figures it should be noted that:

- A number of staff were used during the year on major corporate projects;
- The majority of staff recruitment takes place in one month (University Graduates and School leavers joining the Office in January); and
- In some years attrition during the following twelve months is greater than estimated resulting in understaffing, whilst in other years the reverse occurs.

However, the impact of current billable results indicates that costs and fees are above that which they should be.

FEES CHARGED

Fees charged to clients for Financial Audits are not considered reasonable for a number of reasons including:

- Inclusion of Performance Audit surcharge to fund half of the cost of Performance Audits undertaken by the Audit Office;
- Cost of compliance work being included. However the Compliance Audit work may not impact the Financial Audit, and if it does, it may not be material in the context of a particular client's Financial Audit;
- The Audit Office makes profits on some tasks and losses on others and has a formal process for write-on and write-off of costs; and
- The fact that the Audit Office is not meeting their productive targets and is charging a premium for its Financial Audit services due to the excess number of staff currently being carried.

RECOMMENDATION 55 (HIGH PRIORITY):

It is recommended that the Audit Office review its billable target and actual achievement of that target to improve its billable percentage to a more reasonable rate.

CC (3) – WHETHER THE AUDIT OFFICE SHOULD BE ABLE TO PROVIDE NON-AUDIT SERVICES TO CLIENTS ON A FEE FOR SERVICE BASIS AND HOW TO MANAGE ANY POSSIBLE CONFLICTS OF INTEREST.

FINDINGS:

In the Auditor-General's Report to Parliament 2002 Volume One the Auditor-General provided a letter covering the "Services Provided by the Audit Office". The purpose of the letter was to assist Parliament's understanding of the Audit Office role. The legislation allows the Auditor-General to audit and to provide audit-related services to the Parliament, the Treasurer and Ministers at their request.

In the past the Audit Office has produced a number of Best Practice Guides, however the number of guides produced, has reduced in recent years.

There seems to be no clear mandate for the Audit Office to provide non-audit services to clients on a fee for service basis. Our understanding from discussions with the Audit Office during conduct of this review is that there is no desire by the Audit Office to provide such services. The core competencies of the Audit Office would also limit the ability of the Audit Office to provide non-audit services.

Interviews held with clients of the Audit Office during the course of this review did not present a strong opinion, one way or the other as to whether the provision of non-audit services to clients on a fee for service basis would be either desirable or beneficial.

There is a view currently in the private sector that the provision of non-audit services to clients on a fee for service basis may reduce the independence of the firm when providing audit services. The fear is that the provision of non-audit services could cause the audit firm's independence and judgement to be compromised as it may be put in the position of reviewing its own work or providing a less than rigorous audit as it may become over dependant on the fees from non-audit work. While there may not be concrete evidence that the provision of non-audit services on a fee for service basis impairs independence there is a move within the private sector to separate the audit function from the consulting arm of many of the large international firms of accountants.

In 2002, the Federal Government issued Corporate Law Economic Reform Program Paper 9 (CLERP 9), for comment within the wider community, in response to regulatory and public criticisms of audit independence. CLERP 9 addresses specific non-audit services provision problems. Any service that threatens audit independence is prohibited, fees must be disclosed and the Audit Committee of the Board must publish a statement to the effect that provision of any non-audit services is incompatible with audit independence.

CLERP 9 reinforces Australian Auditing Standard, AUP 32 "Audit Independence" and particularly paragraph 36 which states "An auditor might be asked to conduct a range of "other" services for past, present, or potential audit clients. In principle there is no objection to providing a client with services additional to audit services. However, care should be taken to ensure that:

- Actual independence is not at risk by the auditor performing management functions or making management decisions; and
- Perceived independence is not at risk because of a perception that the auditor is too closely aligned with the entity's management."

RECOMMENDATION 56 (LOW PRIORITY):

To protect the independence of the Audit Office, it is considered that fee for service work should not be undertaken by the Office.

CC (4) – WHETHER THE AUDIT OFFICE SHOULD CROSS SUBSIDISE THE COSTS OF PERFORMANCE AND COMPLIANCE AUDITS WITH THE PROFIT MADE FROM FINANCIAL STATEMENT AUDITS.

FINDINGS:

In his report dated 1999 on the last triennial review of the Audit Office Allen T Craswell noted that concern was expressed by a number of Executives and Managers of Departments and Agencies that the cost of Financial Audits was inflated by a surcharge which is used by the Audit Office to fund some of the Performance Audit program. The report noted that the process was not without precedent as Queensland Audit Office's Performance Audits were not directly funded and recourse was had to "savings" accumulated within the Office to undertake them. The report went on to argue that the focus of the Performance Audits in New South Wales tended to be on accountability which is the primary interest of the Parliament and that it was questionable whether Agencies that pay for the audits received any benefit. The report did not recommend any particular course of action on the issue of funding.

In the Auditor-General's Report to Parliament 2002 Volume One the Auditor-General provided a letter covering the Services Provided by the Audit Office. In that letter under the heading Audit Fees it was explained that Agencies are charged for financial report audits. The fee is based on time and direct out-of-pocket expenses plus the goods and services tax where applicable. Any separate inspections or examinations under the Act are subject to an additional fee. Further a contribution from Treasury covers approximately half the cost of Performance Audits.

While not stated it was implied that the Audit Office recovers the other half of the cost of performance audits through a contribution from or surcharge on the fees charged to all clients for financial report audits.

In discussions with Audit clients during the course of this review, it was clear that the majority were unaware that the Audit Office recovers half of the cost of Performance Audits through a contribution from the fees charged to all clients for Financial Audits. The costs of the Compliance Audit Program are also included in the Financial Audit fees charged to clients. This was not separately disclosed to clients, nor was it clear what proportion of the fees covered the Compliance Audit work.

The majority view expressed by Audit clients was that the fees appeared to be non negotiable. However there was a strong view that the practice of recovering half of the cost of Performance Audits through a contribution from the fees charged to all clients for Financial Audits was inappropriate and lacked transparency. There was a general lack of support for the practice of cross subsidisation to support Performance Audit amongst Audit clients.

The prevailing view amongst Audit clients was that as the Audit clients rarely requested that Performance Audits be undertaken and the audits were seen to be for the benefit of the Parliament then the total cost of Performance Audit should be borne by Treasury rather than subsidised by all Audit clients. There also was a view expressed by Audit clients that have had Performance Audit undertaken within their agency, that they would not be prepared to pay for the audit at all as they received little value from the process and the report (this is discussed in detail in our Section on Performance Audit).

In addition, whilst the Performance Audit Reports detail the costs to the Audit Office of conducting the audit, there is no cost attributed to the Agency resources allocated, when a Performance Audit is being conducted in their organisation. The majority of Agencies indicated that the cost in terms of staff time to provide liaison support and to provide detailed information to the Audit Office was significant. In many instances the need to dedicate such resources to a Performance Audit had not been budgeted for and Agencies indicated that this placed a strain on them being able to undertake their normal program duties. Without the true cost of Agency resources provided and used in assisting the Audit Office when they conduct a Performance Audit, the true costs to Government of undertaking Performance Audits is understated.

Information provided by other jurisdictions shows that Parliaments in Queensland and Victoria fund the full cost of the performance audits undertaken in those States.

The main objective of an audit of a financial report is to enable the auditor to express an opinion whether the financial report is prepared, in all material respects, in accordance with an identified financial reporting framework.³⁴ The role of the auditor is to undertake the minimum work necessary to express an opinion on the financial report as to whether or not it is fairly stated. Whilst it is often argued that the Financial Audit of a public sector entity is more detailed than that of a private sector

³⁴ AUS 202 "Objectives and General Principles Governing an Audit of a Financial Report", Australian Accounting Research Foundation 2002.

organisation, we would not concur with this view. The Auditor-General clearly has a role to ensure accountability and efficiency and effectiveness in Government. However, this role should be seen as separate from that of expressing an opinion on Department and Agency financial statements. It is therefore the belief of Acumen Alliance, that the work performed for Financial Audits should be only that required to form an opinion about whether the financial statements are fairly stated. All other matters coming within the Auditor-Generals role in terms of accountability of government and efficiency and effectiveness should be undertaken through separate work of the Auditor-General in the Compliance and Performance Audit programs and should not be cross-subsidised by the Financial Audit program.

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.

RECOMMENDATION 58 (HIGH PRIORITY):

Financial Audit fees charged to Departments and Agencies should reflect only work required to be undertaken to express an opinion on the financial statements as to whether or not they are fairly stated.

RECOMMENDATION 59 (HIGH PRIORITY):

As part of the audit planning process in each financial year, the Audit Office should provide detailed explanation to its clients as to how their audit fee has been determined.

RECOMMENDATION 60 (HIGH PRIORITY):

Each Performance Audit Report should detail the costs to the Audit Office and to the Agencies involved in providing detailed assistance to the Audit Office as part of that review.

11 Outsourcing

BACKGROUND:

The Audit Office policy for contracting out is specified in the Contract Audit Agents Manual (refer Attachment 1) and is based on the expected benefits to be realised as opposed to the expected associated costs. The Policy states that to ensure the provision of cost-effective audit services, sufficient financial attest audits should be contracted out to enable the efficiency of in-house audits to be benchmarked against those undertaken by private sector contractors.

The policy does not state what is sufficient, how the Audit Office will assess whether audit services are cost effective and how the efficiency of in-house audits will be benchmarked. Without a framework and a process for establishing sufficiency, cost-effectiveness and efficiency by benchmarking within their policy document, it is considered that the policy is flawed.

The Audit Office has taken some steps to address this issue with the establishment of a Contracting Out Taskforce. It has the objective of developing a corporate policy for contracting out and a strategy for contracting out. The Taskforce has developed a 3-5 year rotational plan to decide what and why work is contracted out and a program for reviewing and monitoring the success of the plan. This covers both the quality assurance aspects and measure the achievement of the intended benefits.

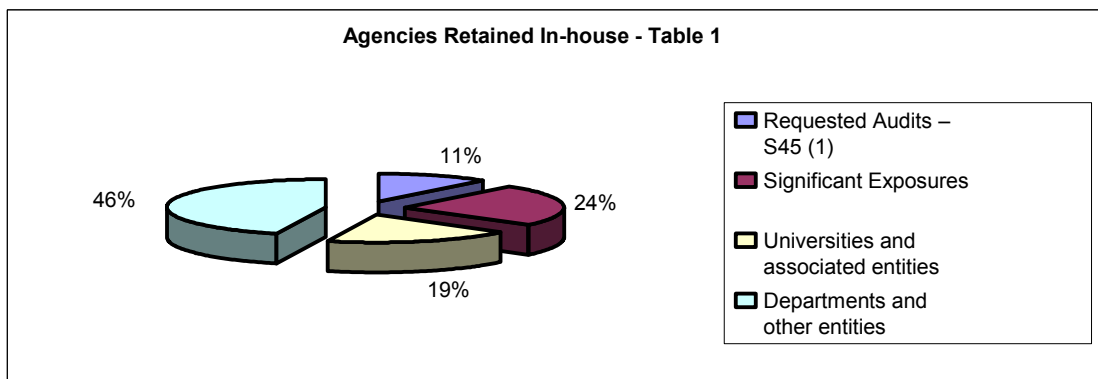
To address the issues involved with benchmarking the Audit Office has established a Benchmarking Committee with an overall objective, to review financial audits and to recommend changes that will result in the most efficient and effective practices. The Committee has not yet produced analysis to support benchmark measures.

The policy sets out the criteria for determining the suitability of audits for contracting out. Agencies which interface across government (e.g. Treasury, Premier's Department etc.), core government departments and those agencies which have significant exposures to taxpayers (e.g. WorkCover Authority, State Superannuation and Public Transport) will continue to utilise in-house resources to undertake the audit of those agencies.

Audits suitable for contracting out would be selected from government trading enterprises, corporatised entities, marketing boards and other statutory authorities. To maintain expertise and industry knowledge within industry segments the policy states that the Office will retain strategic audits to enable it to maintain an involvement with both the issues facing the industry segment and maintain better control of contract agents. The policy also requires that audits contracted out should involve the consent of the audit client prior to the outsourcing process occurring.

An extensive Contractor Audit Agents Manual (CAAM) has been developed by the Audit Office, which covers what is expected from auditing in the Public Sector. The CAAM details the NSW Public Accountability Model, a guide to the Budget Papers, Budget Process and Financial Documents, the Tender Process and Evaluation and the Ongoing Quality Assurance Process. A copy of this Manual is provided to the contractor audit agents so that they are aware of and follow Audit Office requirements when undertaking their audit work.

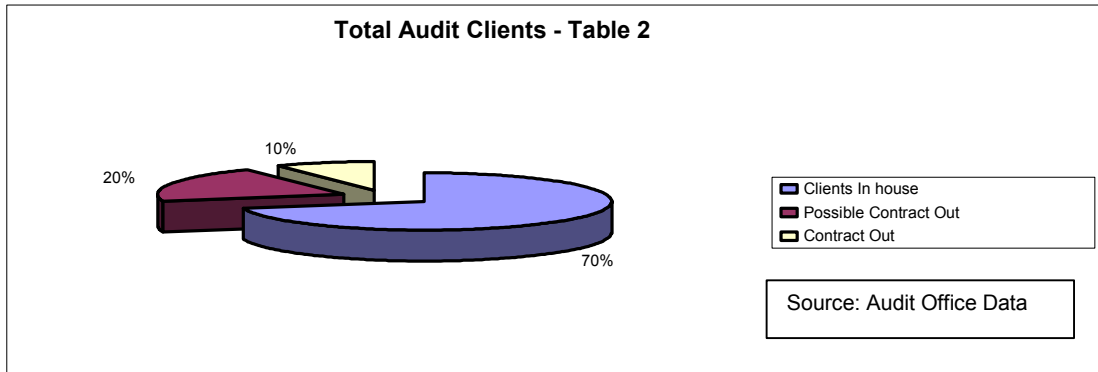
The Contracting Out Task Force, has by the application of the policy, identified approximately 30% of the Audit Office’s financial audits that it considers, are appropriate for contracting out. The remaining 70% of audits have been classified according to the policy and will be undertaken in-house. These audits will not be contracted out as they are Requested Audits – S45 (1), those determined to have Significant Exposures, Universities and associated entities, Departments and Defacto Departments.



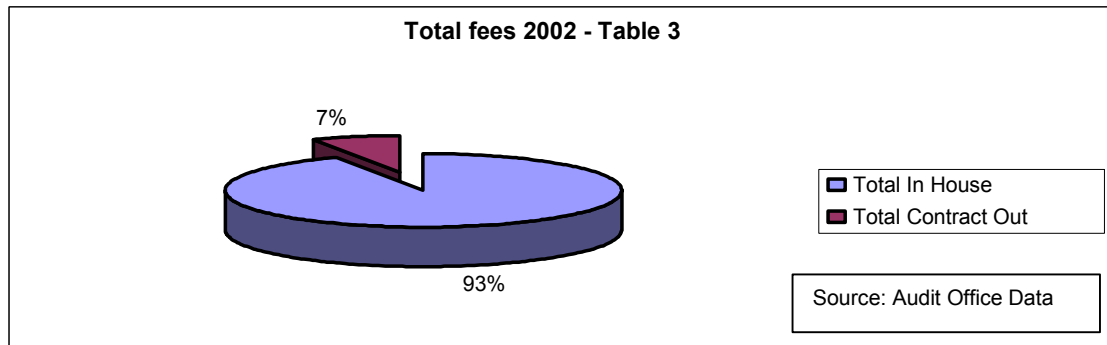
The proportion of agency audits contracted out in 2001-02 was 41 of the 421 agencies while fees of \$1.671 million were paid to contract agents for contracted out audits. The Audit Office adds, for their review and

management time, an oncost on top of the contract agent's fee, which is then oncharged to the audit client.

The table below shows the approximate proportion of audits outsourced, possible audits that could be outsourced and audits retained in-house.



The table below looks at fees paid to contract agents as a percentage of total fees received from clients.



OS (1) – THE AUDIT OFFICE’S PROCEDURES FOR EVALUATING TENDERS FROM PRIVATE SECTOR CONTRACTORS TO CARRY OUT PUBLIC SECTOR AUDITS.

FINDINGS:

THE POLICY

The policy criteria developed for determining the suitability of audits for contracting out is considered to be broad and could be used to exclude any agencies from being subject to contracting out. While there is a process undertaken to determine which agencies could be contracted out, the reasoning for including or excluding agencies in one group or another is not fully documented nor is it clear.

The number of agencies determined to be suitable for contracting out is approximately a third of the total agencies. As seen in table 2 the NSW Audit Office currently outsources 10 % of their financial audits. The Review Team was advised that the decision to outsource 10% of audits was that of the Auditor General. However, it is the opinion of the Review Team that there appears to be no formal basis for having determined that this level of outsourcing is appropriate. It is noted that in other jurisdictions that the percentage of agencies contracted out is more significant indicating that the Audit Office assigns a higher degree of sensitivity to its audits than do other jurisdictions³⁵.

RECOMMENDATION 61 (MEDIUM PRIORITY):

It is recommended that the classification of agencies be reviewed to ensure that the criterion for establishing suitability for contracting out versus retention in house is fully documented and clear. In undertaking this review, regard should be had to the processes in place within other State and Federal Government jurisdictions in Australia for contracting out of audits (as a basis for comparison).

It is also recommended that as part of this process the Audit Office determine a formal policy for how benchmarking of outsourced providers will be undertaken.

³⁵ Approximately 68% and 50% of financial audits are outsourced by the Victorian Audit Office and the Queensland Audit Office respectively.

PROCEDURES FOR EVALUATING TENDERS

Initially the Engagement Controller responsible for the financial audit being considered for outsourcing submits a minute to the Auditor-General seeking approval to contract out the engagement. Once the decision has been made to contract the audit out a Tender Evaluation Committee is established.

The CAAM details the processes to be followed for the contracting out of an audit. The steps in the process include:

- Obtaining a statement of qualifications from private sector audit firms, to allow registration of Audit Service Providers (ASP);
- Receipt of advice from Audit Clients, to assess any conflicts of interest or anything that may preclude the audit being contracted out and to request a representative from the Agency to be involved in the tender process;
- Obtaining expressions of interest from ASP's and shortlisting of these to determine which firms should be asked to tender;
- Provision of an information session to provide tenderers with specific information about the audit;
- Tender document preparation and statement of requirements;
- Undertaking tender evaluation. This is based on a two part process, firstly assessing technical criteria and weighting and secondly fees;
- Organising a formal audit contract. The Auditor-General typically contracts with the firm and the partner within the firm to be responsible for the audit for four years with fixed fees in first year and the opportunity for annual fee adjustments thereafter.

It is considered that current procedures are robust, comprehensive and appropriate in relation to contracting audits out.

REVIEW OF TENDER EVALUATIONS

The contracting out of 23 audits for the year ended 30 June 2003, finalised on 17 December 2002 was reviewed. The documents on file supported that the contracting out procedures had been followed.

OS (2) - THE AUDIT OFFICE'S PROCEDURES FOR CONTRACT MANAGEMENT, QUALITY CONTROL AND ASSURANCE.

FINDINGS:

PROCEDURES FOR CONTRACT MANAGEMENT, QUALITY CONTROL AND ASSURANCE

Auditing Standard AUS 602, "Using the Work of Another Auditor" establishes standards and provides guidance when an auditor, reporting on the financial report of an entity, uses the work of another auditor on the financial information of one or more components included in the financial report of the entity. When the principal auditor (in this case of course the Auditor-General) uses the work of another auditor, the Standard requires that the principal auditor should:

- Determine how the work of the other auditor will effect the audit;
- Consider whether the Principal auditor's own participation is sufficient to be able to act in that capacity;
- Assure oneself of the professional competence of the other auditor in the context of the specific assignment;
- Perform procedures to obtain sufficient appropriate audit evidence that the work of the other auditor is adequate for the principal auditor's purpose in the context of the specific assignment;
- Consider the significant findings of the other auditor;
- Establish co-operation with the other auditor and vice versa;
- In cases where the principal auditor concludes that the work of the other auditor cannot be used, and the principal auditor has not been able to perform sufficient additional procedures, undertake procedures to express a qualified opinion; and
- Not refer to the work of another auditor in an audit report unless required by legislation or as part of a qualification.

The CAAM states, under “Ongoing Quality Assessment”, that the Audit Office is responsible for all reports and correspondence arising from the audit and should obtain reasonable assurance that the work performed by the outsourced audit provider is adequate for this purpose. It is our opinion that current Audit Office quality controls have been established in accordance with the above professional auditing standards and are appropriate for the Audit Office.

The steps in the outsourced audit process typically include:

- Initial Contact - the Audit Office Engagement Controller/Manager establishes contact with the client and the outsourced audit provider to agree the terms of the relationship;
- Review of Audit Plans - prior to commencing interim work the outsourced audit provider is required to complete the audit plan. The CAAM states that the Audit Office may review this. In addition, the Client Service Plan is required to be prepared by the outsourced audit provider and to be reviewed by the Audit Office prior to being sent to the client. Form A, “Planning Review” is to be completed by the outsourced audit provider as part of this process;
- A Review of Interim Audit Work - to ensure procedures in the plan are followed, the CAAM requires the Audit Office to review the interim audit work;
- The outsourced audit provider completing Form B, “Approval in Principle” which is essentially advice to the Audit Office that the financial statements are materially correct;
- Final Review - The Audit Office reviews the work performed after the outsourced audit provider has completed Form C, “Final Review” to indicate work on the audit has been satisfactorily completed;
- Payment of Contract Audit Agents Fees - The outsourced audit provider advises of their fees using Form D, “Contract Audit Agent’s Claim for Fees”;
- Claims for Additional Fees - Where additional fees are to be claimed the outsourced audit provider completes Form E, “Contract Audit Agent’s Claim for Additional Fees and gives this to the Audit Office;

- Calendar of Audit Events - the outsourced audit provider advises the Audit Office of a chronology of how the audit is to be conducted using Form G, "Proforma Calendar of Audit Events";
- Additional Services - Should the outsourced audit provider wish to provide additional services to the client then a form is completed and provided to the Auditor-General for approval;
- Concerns of the CAA and the Audit Client - The Engagement Controller completes Form H, "Contract Audit Agent Annual Performance Evaluation" and requests the Audit Client to complete Form I, "Client Feedback on Performance by Contract Audit Agents" and
- Assessment of any apparent or actual breaches of contract.

While the procedures are reasonable for Contract Management, Quality Control And Assurance, the procedures provided to the Review Team at the time of our audit clearly indicated to us that the procedures lack sufficient detail for undertaking all contract management and quality assurance requirements. In a number of instances the words indicate a choice, however the particular step should be mandatory and should be evidenced by the contract manager that the step has been undertaken. For example:

- Review of Audit Plans - "The CAAM states that the Audit Office may review the plan". AUS 602.09 (b) notes that the principal auditor would advise the other auditor of the use to be made of the other auditor's work and report and make sufficient arrangements for the coordination of their efforts at the initial planning stage. It is our belief that this would always involve the principal auditor undertaking a detailed review of the proposed audit plan;
- Review of Interim Audit Work - The CAAM states that the Audit Office may review all work Papers and undertake a final review of work performed. AUS 602.08 notes the principal auditor should perform procedures to obtain sufficient appropriate audit evidence that the work of the other auditor is adequate for the principal auditor's purpose in the context of the specific assignment. It is our belief that this would require the principal auditor to review all interim and final audit work conducted and evidence this review on file by signing the detailed audit working papers;

- Concerns of the CAA and the Audit client - The CAAM states that the outsourced audit provider and the audit Client should be encouraged to contact the Audit Office with any comments, recommendations for improvements or concerns". Rather than encouraged, the outsourced audit provider and Audit Client should be required to contact the Audit Office in writing to improve the process.

REVIEW OF CONTRACT MANAGEMENT, QUALITY CONTROL AND ASSURANCE

A review of a sample of outsourced audits for the 30 June 2002 has shown that the procedures required by the CAAM had been followed except for the following:

- The files reviewed did not evidence that all processes and steps required by the CAAM and AUS 602 had been followed. This could indicate that some steps had been undertaken but not documented or had been omitted;
- While there appears to be a standard file profile for the Contract Management, Quality Control And Assurance process it is only partly used by individual contract managers;
- Files did not contain evidence of the Contract Audit Agents Checklist having been actioned, planning, interim review and final review being undertaken or if they had been reviewed who undertook the review;
- No file contained any concerns of the outsourced audit provider, the Audit Client or the Engagement Controller, nor was Form H, "Contract Audit Agent Annual Performance Evaluation" or Form I, "Client Feedback on Performance by Contract Audit Agents" completed; and
- There was no evidence of assessment as to whether breaches of contract had occurred or whether the Audit Office were satisfied that all work undertaken by the outsourced audit provider was undertaken appropriately.

It was noted on a number of files that the Contract Manager had undertaken lengthy and detailed reviews of the financial statements and that this had resulted in a number of issues being raised with the outsourced audit provider. However there was no documentation on file to show that the performance of the contract agent had been assessed as either appropriate or inappropriate and what further follow-up action should be taken if any. With outsourced audits, the Audit Office still retains its role of signing the Independent Audit Opinion on the financial statements of the entity being audited. Accordingly under Australian Auditing Standards, the Audit Office is required to ensure that the work of the Contract Audit Agent has been conducted in a manner and to a degree that supports the Audit Opinion placed on the financial statements by the Audit Office.

There are procedural forms in the CAAM that enable the Audit Office to document the performance of contactors. However there was no evidence to show that these were completed. This results in formal and documented performance evaluation not being undertaken. There is evidence that detailed review of aspects of the outsourced audit providers work is undertaken and in some cases memos are used to request further information or work to enable the issue of the Independent Audit Opinion. However without data relating to the assessment of outsourced audit providers performance the benefits of outsourcing cannot be assessed. Such an assessment is critical in playing a part in future selection processes. In addition, no overall assessment is provided to senior management for evaluation of the outsourcing program.

In discussion with Audit clients during the conduct of this review there was a request that they be able to formally provide feedback on the outsourced audit providers performance, so as to add value to the service provided by the provider.

RECOMMENDATION 62 (HIGH PRIORITY):

The Contract Management, Quality Control and Assurance Procedures be amended to ensure that all steps are made mandatory.

RECOMMENDATION 63 (HIGH PRIORITY):

All files for contracted out audits be reviewed to ensure that appropriate documentation is maintained to evidence that the required Contract Management, Quality Control And Assurance Procedures have been undertaken in all cases and accord with the CAAM and AUS 602.

RECOMMENDATION 64 (HIGH PRIORITY):

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 65 (HIGH PRIORITY):

The Audit Office should undertake a formal overall analysis of its outsourcing program to determine that work conducted by outsourced audit providers is satisfactory and that issues identified by individual audit managers are satisfactorily dealt with and used by senior management for evaluation of the program.

OS (3) - THE AUDIT OFFICE'S SYSTEMS FOR ROTATING PUBLIC AND PRIVATE SECTOR AUDITORS.

FINDINGS:

There are a range of issues associated with the appointment, tenure, removal and resignation of company auditors. There are divergent views on whether it should be mandatory for rotation of audit partners in accordance with the principles laid down in AUP 32 Audit Independence, for all listed companies.

The Government released Professor Ramsay's report on the Independence of Australian Company Auditors (Ramsay report) in October 2001. The report endorsed the principle that there be mandatory rotation of audit partners. However, Ramsay considered that AUP 32 is not adequate in this respect. AUP 32 only requires 'the periodic rotation of audit staff between audit engagements'. Some firms may interpret this as only requiring rotation after many years.

The Ramsay report did not believe it appropriate to mandate rotation of audit firms as 'the anticipated cost, disruption and loss of experience to companies is considered unacceptably high, as is the unwarranted restriction on the freedom of companies to choose their own auditors'.

In its policy paper, Corporate Law Economic Reform Program (CLERP 9) the Government has stated that it will make audit partner rotation compulsory after five years for top 500 companies. The new requirement will apply to the lead engagement partner and the review partner. To maintain continuity of knowledge, the appointment of these partners could be staggered.

In line with the wider profession, the Audit Office has a policy for rotation of financial audit staff, which enables improved independence, and opportunities for development of staff. The policy is based on and follows AUP 32 "Audit Independence". The Assistant Auditors-General review staff requirements on an annual basis and examine the requirement to rotate staff and engagement controllers. The process involves voluntary rotation where possible.

The Audit Office has not had a clear policy nor has there been a systematic approach to the process to guide the rotation of public and private sector auditors, although it has rotated public and private sector auditors in the past. This was certainly evidenced during our discussions with Agencies as part of this review. The Contracting Out Task force has recently been established to develop a rotation plan. A plan has recently been developed although it does not contain a history of previous contracted out Audit clients whose contracts have expired and have been brought back in house or have been contracted out a number of times in a row to either the same or a different outsourced audit provider. The Audit Office has not maintained a database to enable the prior contracted out Audit client's history to be easily identified.

The 2003 rotation plan does show the current Audit clients contracted out and the year in which the contract will terminate. The plan will be used to determine which Audit clients will be contracted out, rolled over or brought back in house.

The process to manage and monitor the rotation of public and private sector auditors is being developed under the Contracting Out Task force and appears to be appropriate.

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.

12 Performance Measurement

INTRODUCTION

The Audit Office has developed a set of performance targets, outputs and benchmarks which are outlined in its Corporate Plan and reported in its Annual Report. These are outlined in Table 1 and 2:

Table 1: The Audit Offices Performance Indicators and Targets (source AO annual report 2002)		
Measure (Performance Indicator)	Annual Target	Result 2001-02
Objective: Satisfy the needs and expectations of Parliament, other clients and stakeholders		
<ul style="list-style-type: none"> - Parliamentarian satisfaction index - Client satisfaction index 	At least 80% agree we have a positive impact on State accountability and performance (* both for 2000-01 only as bi-annual)	79%* 85%*
Objective: Ensure our processes are efficient and meet relevant standards		
Timeliness of: <ul style="list-style-type: none"> - audit opinions - reports to client management - reports to parliament Cost Efficiency Measures <ul style="list-style-type: none"> - chargeable time - average cost per performance audit - certification to ISO 9001 quality management system 	90% issued within 10 weeks of receipt of financial report 90% issued within 4 weeks of audit opinion 95% of audits reported to parliament within 6mths of balance date 60% less then \$200,000 Maintain	85% 74% 95% 54% \$184,000 Yes
Objective: Have Knowledgeable and satisfied people		
<ul style="list-style-type: none"> - Staff satisfaction index - Sick leave - Training days per person 	More then 70% Less then 5 days More then 7 days. (^ for 1999-2000 only)	68%^ 7.7 7.0
Objective: Be financially self-sufficient		
Positive Operating results	Positive Results	Yes

Table 2: Output reporting and efficiency benchmarks		
Reports to Parliament (source AO annual report 2002)	2000-01	2001-02
Financial Audit Reports:		
<ul style="list-style-type: none"> - Government agencies reported - Special reviews 	417 9	421 14

**The
Alternative.**

Performance audit reports and better practice guide	11	14
Efficiency Benchmarks (NSW AO against Australian Audit Offices average)		
<ul style="list-style-type: none"> - Total audit cost per \$'000 of total public sector assets - Total audit costs per \$'000 of total public sector operating transactions - Cost per financial audit opinion (Results in graphical presentation can be seen in the Annual Report 2002)		

The performance reporting in the 2001-02 Annual report includes a number of "Future actions" aimed at improving performance, under the four objectives. These include, under the four key objectives:

Objective 1: Satisfy the needs and expectations of Parliament, other clients and stakeholders

- Identify and report on issues that serve the interest of the public and public sector management;
- Refine "plain English" approach to report writing
- Continue to liaise with the Public Accounts Committee and other parliamentary committees
- Improve the use of the internet site

Objective 2: Ensure our processes are efficient and meet relevant standards

- Improve timeliness of reports
- Benchmark processes
- Implement quality assurance program
- Monitor and adapt to changes in the auditing environment

Objective 3: Have Knowledgeable and Satisfied People

- Develop integrated HR strategic plan
- Develop a strategy and framework for managing information and knowledge
- Implement internal communications strategy
- Implement effective records management policies and processes

Objective 4: Be financially self sufficient

- Enhance business processes

The Corporate Plan is supported by Branch Business Plans that include detailed actions aimed at meeting the mission vision and objectives. Progress towards achievement of these plans is reported each quarter through the Board of Management (BOM).

In addition there is monthly Audit Office financial reporting which considers standard audit practice management indicators including KPI's such as fees, headcount, debtor days, WIP Days and Employee Production.

PM (1) WHETHER KEY PERFORMANCE INDICATORS ARE AN APPROPRIATE METHOD OF DETERMINING THE PERFORMANCE OF THE AUDITOR-GENERAL AND OF HIS OFFICE.

FINDINGS:

Key performance indicators have been defined as “those indicators which give a comprehensive, high level overview of a program’s performance. They are particularly aimed at external users of performance information.”³⁶

The stated mission of the NSW Audit Office is to “Assist Parliament to improve the accountability and performance of the State”. Under that mission the AO has adopted a process of continuous improvement which includes enhancements to its own performance reporting to improve accountability.

In order to measure performance it is necessary to establish a performance measurement framework. The key steps of this process are:

- Define Objectives – the things you are trying to achieve. Without objectives that are specific, have a defined impact and can be measured then accountability cannot be assessed;
- Develop measures to assess the achievement of the stated objectives. Without such measures, performance cannot be assessed and hence the Audit Office cannot be held Accountable.

The approach adopted by the Audit Office, inline with the generally accepted performance management frameworks, has been to develop its performance measurement around its corporate planning activities. Here corporate planning is used to clarify objectives, identify the strategies to achieve those objectives, identify outputs and outcomes and set performance goals and targets.

The Audit Office Corporate Plan 2002-05 identifies objectives, strategies, performance measures and targets. The Corporate Plan is supported by actions in supporting business plans. Completion of these actions is aimed at improving performance across the various objectives.

It is our belief that Key Performance Indicators are an appropriate method of determining the performance of the Auditor-General and of his office.

³⁶ Reporting Performance : Better Practice Guide – The Audit Office of New South Wales 2000

However it is of critical importance to ensure the relevance and reliability of the chosen key performance indicators and to assess whether they are an appropriate measure of performance. This is considered in the next section.

**PM (2) THE AUDIT OFFICE'S PERFORMANCE INDICATORS AND TARGETS.
PM (3) THE AUDIT OFFICE'S REPORTING OF ITS PERFORMANCE AGAINST THE
INDICATORS AND TARGETS.**

FINDINGS:

Performance indicators "provide a means to measure how well an agency has performed in meeting its objectives. Performance indicators are not an exact measure of achievement but rather an indication of agency performance"³⁷.

The Audit Office have defined a number of performance indicators and targets in its Corporate Plan 2002-2005, which have been reported on in the 30 June 2002 Annual Report (see table 1 above). In addition it reports on some key outputs and efficiency benchmarks (see table 2 above).

The NSW Audit Office Better Practice Guide: Reporting Performance (2000) provides a useful framework in which to evaluate these performance indicators and targets. It states that "in Annual Reports agencies should:

- Report results and outcomes not just activities and outputs
- Relate outcomes directly to objectives
- Express outcomes in terms of impacts on the community
- Relate outcomes to goals and targets"

Outcomes are the results or consequences on the community of the actions or events (outputs) of an agency. Planned or desired outcomes are the results or impacts that the agency wishes to achieve. The mission of the audit office "to assist Parliament improve the accountability and performance of the State" is the Audit Offices desired outcome.

Comparison of the performance indicators in tables 1 and 2 shows that they are broadly in line with this framework. The performance indicators are arranged across the four key objectives of:

- Satisfy the needs and expectations of Parliament, other clients and stakeholders;
- Ensure our processes are efficient and meet relevant standards;
- Have knowledgeable and satisfied people; and
- Be financially self sufficient.

³⁷ Reporting Performance: Better Practice Guide – The Audit Office of NSW 2000.

CONSIDERATION OF OTHER JURISDICTIONS PERFORMANCE REPORTING

As part of our review we also considered the performance reporting of other jurisdictions. Whilst each Auditor General has different mandates, there are considered to be major similarities in their operations and we believe that overall it is possible to compare performance in a useful manner. Outlined in the following tables are our assessment of the performance reporting measures, with an indication of whether the Audit Offices performance indicators and reporting currently addresses these areas.

Area:	Measure:	NSW AO measure
Output Measures		
Quantity (output)	<ul style="list-style-type: none"> Matters of significance raised in Parliament Major and Minor audits undertaken 	<ul style="list-style-type: none"> No Yes (no split)
Quality (output)	<ul style="list-style-type: none"> Agreement in parliamentary survey that the matters of significance raised in reports clearly communicate issues Compliance with standards 	<ul style="list-style-type: none"> No No
Timeliness (output)	<ul style="list-style-type: none"> Agreement in parliamentary survey that the matters of significance raised in reports are timely Percentage of audit reports issued within statutory timeframes 	<ul style="list-style-type: none"> Only timing Yes
Cost (output)/ Efficiency (KPI)	<ul style="list-style-type: none"> Average cost of matter of significance Average cost per major and other audit 	<ul style="list-style-type: none"> N/a No - benchmark cost per opinion
Effectiveness (KPI's) (% agreement from parliamentarians survey)	<ul style="list-style-type: none"> The Auditor General's auditing approach and reporting contributed to improved public sector accountability. Useful or better performance by the Auditor General in respect to reports and services to parliament Reports dealt with matters of significance to Parliament The AG is effective in dealing with his desired outcome of informing Parliament on accountability and performance of the public sector 	Only: <ul style="list-style-type: none"> Parliamentarian satisfaction index Client satisfaction index Without any detailed break up of aspects of satisfaction

Table 4: Queensland (source: Annual report 2001-02)		
KPI Area:	Measure:	NSW AO measure
Financial Results	<ul style="list-style-type: none"> Level of recovery of audit costs through fee revenue 	<ul style="list-style-type: none"> No
Internal Results	<ul style="list-style-type: none"> Percentage of hours chargeable against available hours (billable) Percentage of productive hours spent on audits against available hours (productivity) 	<ul style="list-style-type: none"> Yes No
Innovation and Training	<ul style="list-style-type: none"> Number of innovations relating to audit methodology Number of non-audit methodology innovations Percentage of audit staff CPA/CA qualified 	<ul style="list-style-type: none"> In branch business plan only As above No
Customer Satisfaction	<ul style="list-style-type: none"> Level of satisfaction from our clients 	<ul style="list-style-type: none"> Client satisfaction index
Strategic Initiatives	<ul style="list-style-type: none"> Notes some of the key initiatives driving the strategic plan 	<ul style="list-style-type: none"> Future actions

KPI Area:	Measure:	NSW AO measure
Parliamentary reports and services - Performance against outputs	<ul style="list-style-type: none"> • Cost - delivery of reports and services within total output cost (\$ vs target, split reports and services) • Quantity - Reports expected to be tabled (number) • Timeliness - Reports completed within planned timeframes (%) • Quality - Overall level of external satisfaction with reports (%) 	<ul style="list-style-type: none"> • No report vs budget • No • Yes • Parliament satisfaction index
Audit reports on financial statements - Performance against outputs	<ul style="list-style-type: none"> • Cost - Delivery of service within total output cost (\$) • Quantity - Audit opinions issued to agencies (number) • Timeliness - Audit opinions issued within statutory deadlines (%) • Timeliness - Management letters and reports to ministers issued within established timeframes (%) • Quality - Overall level of external satisfaction with the conduct of financial statement audits (% on survey)) 	<ul style="list-style-type: none"> • No - except operating result • Yes • Yes • Yes • Client satisfaction index
Performance against corporate targets	<ul style="list-style-type: none"> • Targets generally related to specific actions. • Staff satisfaction • Enhancements to methodology (number) • Quality assurance reviews • Communication improvement strategies 	<ul style="list-style-type: none"> • No • Staff satisfaction index • No • No • No

A summary of our review on the NSW Audit Office performance indicators as grouped by the core objectives in Table 1 is as follows:

a) Satisfy the needs and expectations of Parliament, other clients and stakeholders

- It is recognised that the Audit Office undertakes a number of processes to measure the satisfaction of Parliamentarians and Agencies. Given the importance of the Parliamentarian and Client opinions, their satisfaction indicators should be assessed on an annual basis, given the nature of the Audit Offices mission this is the key quantitative assessment of effectiveness.

- Expanding the number of satisfaction indicators would provide better insight into where enhancement performance is required.

b) Ensure our processes are efficient and meet relevant standards

- The chargeable time percentage should be split up by branch (financial/ performance audit), to provide better transparency. The basis of this chargeable percentage should be outlined. Whilst the Audit Office currently reports on this internally, it is not reported externally, and the Review Team believes that this would be a helpful measure.
- A quality indicator should be included in relation to the Professional quality control standards, since these provide a more relevant and detailed basis for financial and performance audit adherence to professional standards than ISO9001.
- Other continuous improvement based indicators such as enhancements to methodology and efficiencies are useful and should also be included.

c) Have knowledgeable and satisfied people

- The staff satisfaction indicator should be reported annually
- Indicators used by other Auditor Generals, such as the percentage of qualified staff, provide a good quantitative indicator of the level of “knowledgeable” people.

d) Be financially self sufficient

- Greater transparency is required in the reporting of costs and expenditure by activity. Further analysis of this area is undertaken in the costs and charges section of our report.

BENCHMARKS

The inclusion of benchmarking (Table 2) provides an attempt by the Audit Office to assess its performance against peers. However, we do not believe the current benchmarks chosen provide a very effective performance indication, specifically:

- For total audit costs per \$000 of total public sector assets and operating transactions, one would expect the NSW Audit Office to have a very good performance result due to audit economies of scale, with NSW being the largest jurisdiction;

- Costs per financial audit opinion depends on the nature of each jurisdictions client base. For example Queensland and Victoria undertake the audits of local councils which may be expected to push down their average cost.

Benchmarking can be a useful exercise in assessing an entities performance. However effective benchmarking can only be achieved when the differences in measurement are clearly understood or eliminated and you are able to compare “apples with apples”. The benchmarks used in the Auditor General report are against figures collated through the Australasian Council of Auditor Generals (ACAG).

It is insightful to note that during our review we requested access to the individual ACAG benchmarking data provided by Audit Offices and in one instance that data was not forthcoming due to “some concerns with the comparability of the information.” We understand ACAG is aware of this issue and is working to improve the comparability of benchmark information.

RECOMMENDATION 67 (HIGH PRIORITY):

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.

RECOMMENDATION 68 (HIGH PRIORITY):

Performance indicators, including input/output efficiency, should be strengthened by division into key outputs – Financial Audit, Compliance Audit and Performance Audit.

RECOMMENDATION 69 (MEDIUM PRIORITY):

The NSW Audit Office should continue to work with ACAG to produce comparable benchmark information.

PM (4) WHETHER THE AUDIT OFFICE USES THE INDICATORS TO IMPROVE ITS OWN PERFORMANCE.

FINDINGS:

The Corporate planning and reporting framework of the Audit Office appears to provide a sound basis for the use of performance indicators to improve its own performance.

The Corporate Plan of the Audit Office outlines core objectives, the strategies to meet those objectives, performance measures and targets. Under the Corporate plan each Business Unit has its own business plan. These are structured around the core objectives, detailing strategies, actioning of responsibilities and performance measurement indicators.

A monthly financial report is also prepared for consideration by management. This includes key financial KPI's such as audit fees, headcount, debtors, work in progress and employee production (chargeability).

Progress towards the achievement of business plan targets and actions are formally reported on a quarterly basis and discussed at the Board of Management (BOM) Meeting. Progress on key actions are monitored through the BOM.

In addition, the Audit Office has put in place a "Continuous Improvement Working Group" as an integral part of its quality management system under ISO9001.

Specifically it is beneficial to highlight some of the actions that are underway to address areas where the Audit Office did not meet its targets as reported in its annual report 2002:

Performance Indicator	Result 2001-02	Key Action Items
Parliamentary satisfaction index 80%	79%	KA(1) Input from Parliament; KA(4) Meet with Parliamentarians/Committees; KA(5) Program to brief Parliamentarians on role of A-G KA(6): Communication strategy KA(16) Plan content and timing of reports KA(17) Ease of read reports
90% of audit opinions issued within 10 weeks of receiving financial report.	85%	KA(15) & (16) Plan content and timing of reports
90% of reports to client management issued with 4wks of opinion	74%	KA(15) & (16) Plan content and timing of reports
Chargeable time 60%	54%	KA(12),(13),(14) Benchmarking KA(18) HR Strategic Plan
Sick leave <5 days	7.7	KA(18) HR Strategic Plan KA(19) OH&S and EEO

Thus it can be seen that the framework is in place for the use of indicators to improve performance. The role of the Board of Management and Continuous Improvement Working Group will be critical to the success of this process.

We note from the minutes of the Board of Management, that progress on key actions is discussed at each Board meeting. The Review Team supports this approach.

There are no recommendations for this finding.

13 Quality Assurance

INTRODUCTION

The vision statement of the Audit Office is “to be recognised as a centre of excellence in auditing.” To assist in achieving this vision the Audit Office has adopted the professional standards issued by the Australian Accounting Standards Board. The key professional standards are:

- APS4 “Statement of Quality Control Standard”
- APS5 “Quality Control Policies and Procedures”
- AUS206 Quality Control for Audit Work.

APS4 “Statement of Quality Control Standard” defines a basic objective of an accounting practice is “to ensure that the professional services it provides conform with professional standards.” The standard defines that “a practice must establish and maintain quality control relevant to its operations having due regard to the following elements:

- a) Professional independence
- b) Assignment of personnel to engagements
- c) Guidance and assistance
- d) Supervision
- e) Employment
- f) Professional development
- g) Promotion
- h) Client evaluation
- i) Inspection and review
- j) Allocation of administrative and technical responsibilities”

The Audit Office Practice manual and SAGE methodology incorporates the requirements of AUS206 in relation to individual audit assignments. In seeking to comply with the profession requirements in relation to Financial Audits of APS4 the Audit Office has established the Quality Audit review Committee (QARC). In addition the Audit Office is accredited to ISO 9001 Quality Management Systems.

BACKGROUND TO QUALITY ASSURANCE

The Quality Assurance (QA) framework within the Audit Office consists of a number of different streams, namely:

- Financial Audit - Individual Engagement quality assurance, including AS2 file integrity and quality control procedures is undertaken by the Engagement Controllers and Managers. Responsibilities of the Engagement Controllers and Managers are covered in the Audit Office Practice Manual. Our analysis of financial audits during this review included the quality assurance mechanisms in place for individual financial audits reviewed;
- Performance Audit - Individual Engagement quality assurance is undertaken as set out in the Performance Audit manual. Our analysis of performance audits during this review included the quality assurance mechanisms used during that review by the Audit Office;
- Quality Audit Review Committee (QARC) operations which are structured to meet requirements of Professional Statement APS 4 and is considered in further detail below; and
- ISO 9001 Quality Assurance Processes implemented to ensure on-going compliance with the Audit Office's quality accreditation in relationship to quality management systems.

In addition, the Audit Committee of the Audit Office plays an important role in the overall governance framework. It is supported by Internal Audit, which is resourced through the Governance and Communications area.

The Audit Committee, as defined in its charter, has an overview function in relation to:

- Risk management and internal control;
- Audit functions;
- Financial reporting;
- Fraud prevention, probity and propriety; and
- Processes to ensure compliance with legislation, policies and procedures.

QA (1) – THE EFFECTIVENESS OF THE AUDIT OFFICE’S QUALITY ASSURANCE PROGRAMS.

FINDINGS:

Our analysis in this section will focus on the operation of the QARC.

Quality Audit Review Committee (QARC)

The QARC was established to meet the professional requirements relating to quality control, as detailed in the Audit Office Practice Manual. This covers the requirements of APS4 together with:

- “Examination of the effectiveness and efficiency of AS/2 and SAGE on the audits selected for review;
- Examination of the uniformity of the audit process across the Office;
- Identification of efficiencies in audit practices;
- Identifying any widespread inefficiencies; and
- Ensuring QARC reviews are carried out promptly so that they are of maximum relevance to field audit teams.”

Control and membership of the QARC operations was through the Governance Area. However, we understand a review of this structure, to be undertaken by one of the Assistant Auditor-General’s has been pending.

The Audit Office Practice Manual outlines QARC work is to be conducted through review of a selection of small and large attest audits.

No full QARC reviews have been undertaken for the last two years. In addition, the current QARC framework does not include quality assurance reviews of the Performance Audit Branch and this role has been given to the Assistant Auditor-General Performance Audit Branch. The QARC framework does also not specifically address the requirements of Compliance Audit. Our discussions in this Section therefore focus on quality assurance processes surrounding the Financial Audit Division only.

We understand, from discussions with a number of Audit Office Staff, that formal QARC reviews had resulted in a somewhat adversarial approach between reviewer and reviewee. Whilst a quality assurance review can at times be threatening to staff and cause some angst, if such reviews are undertaken in a collegiate manner then most staffing concerns should be overcome. It is imperative that an adversarial approach is avoided so that the QARC reviews can be as effective as possible.

Mini QARC

Acumen Alliance were advised that as a result of the adversarial concerns with the more formal QARC Reviews, Mini QARC reviews were undertaken during March-April 2002 on 30 June 2001 year end audits with an aim of ensuring compliance with Audit Office methodology. A key restriction in the scope of these reviews was to exclude an analysis of whether the rationale in applying certain audit steps was correct, or whether efficiency and effectiveness considerations had been assessed. We note from discussions with the Audit Office that negotiations with a 'Big 4' firm to undertake this work had occurred. However, they were unable to undertake this work prior to the busy period. We also note from discussions with the Audit Office that arrangements had been made with a University to undertake work regarding efficiency. This unfortunately was cancelled late last year because after eighteen months the respective University had still not done the work.

The Mini QARC was undertaken using a checklist by the Engagement Managers with review by a peer, prior to compilation. The general issues arising were fed back to all Engagement managers in early July 2002 after consideration by the Audit Operations Committee.

Based on our review of a number of financial audit files during this review, a number of the issues raised by the mini-QARC appear to remain, which is a little disappointing.

The outline of QARC activity provided in the Audit Office Practice Manual provides an effective basis for a quality review programme. However the review of its operations and an update of its manual should be completed as soon as possible.

Quality Review activity should be an on-going process. No formal Quality Review activity by the QARC has occurred since April 2002. Timely Quality Review is necessary to ensure issues identified are relevant and can be fed back into the audit process.

There are a number of better practice Quality Review techniques which should be considered to ensure maximum effectiveness from the process. These have been incorporated in the recommendations below.

RECOMMENDATION 70 (HIGH PRIORITY):

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

RECOMMENDATION 71 (MEDIUM PRIORITY):

Quality Reviews should occur as soon as possible after completion of the financial audit cycle, eg in the Nov-Dec period for June year ends. This ensures any outcomes/issues flowing from the reviews can be addressed at the planning stage for the next years financial audit.

RECOMMENDATION 72 (HIGH PRIORITY):

The Quality Review framework used by the QARC should ensure comprehensive coverage of all aspects of an audit including efficiency and effectiveness considerations and the rationale for all audit work undertaken.

RECOMMENDATION 73 (HIGH PRIORITY):

Consideration should be given to the performance of "hot reviews" as a method of providing quality review assurance immediately prior to sign off on a selection of financial audits. Such hot reviews should be undertaken by an Assistant Auditor-General who is independent of the financial audit being conducted.

QA(2) – WHETHER THESE PROGRAMS ENSURE THE AUDIT OFFICE HAS WELL-DEVELOPED AND APPROPRIATE METHODOLOGIES AND THAT THESE METHODOLOGIES ARE CONSISTENTLY APPLIED.

FINDINGS:

The QARC framework set up for the Audit Office provides a feedback mechanism into both the Audit Office Practice Manual and the SAGE Audit Methodology. However the limited scope of the last mini QARC meant that the application of the Sage and internal Audit Office Methodologies in the particular financial audits being reviewed was not questioned. In our opinion this compromised the effectiveness of the quality assurance review that was undertaken.

Updates to the Practice Manual and SAGE Methodology are controlled through the Policy and Research Branch. This Branch also assesses the impact of new professional standards, legislation and Treasury Pronouncements. Responsibility for Quality Reviews had previously been that of the Policy and Research Branch, although it was moved to the Corporate Quality area a number of years ago.

The responsibility for quality review in other jurisdictions such as Queensland and Victoria are held by the Policy and Research Branch.

Expansion of ongoing QARC activity is required to ensure there is effective feedback on the appropriateness of the methodologies and their application within the Audit process, as noted under recommendations in the previous section. In addition there should be a review of the responsibility for the QARC process to ensure the nexus to updating methodology is maintained.

RECOMMENDATION 74 (HIGH PRIORITY):

Consideration be given to returning responsibility for the QARC to the Policy and Research Branch. This will help ensure the nexus between quality review findings and their impact on methodology is maintained and provide a Chinese wall between the audit function and the quality review process.

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.

QA (3) - THE EXTERNAL AND INTERNAL VERIFICATION OF THE EFFECTIVENESS OF THE QUALITY ASSURANCE PROCESS.

FINDINGS:

FINANCIAL AUDIT

In late 2001 line responsibility for the Financial Audit Quality Review process was passed to an Assistant Auditor-General in the Financial Audit Branch, by the Audit Operations Committee. Initiatives included the March-April 2002 mini QARC review and attempts to get a third party efficiency and effectiveness review of the application of SAGE and AS2. These have not yet eventuated.

Following the last mini QARC a decision was taken to delay further Quality Reviews, subject to this review by Acumen Alliance, to minimise any double up. Quality review should be a continuous process and the delay has in effect stopped the operation of the QARC.

There has not been any external verification of the QA process during the last two years. However, two reviews of the mini QARC process by Internal Audit are scheduled for 2003. In addition a review of the efficiency and effectiveness of AS2 use has been included on the Internal Audit plan.

Another method of external verification would be under the auspices of the Australasian Council of Auditor Generals (ACAG) Staff from the Audit Office have assisted in other peer reviews sponsored through ACAG. Most recently the New Zealand Audit Office in 2001 and Western Australian Audit Office in 1999. It could be seen as useful to request another State Auditor-General's Office to provide resources to undertake quality assurance peer reviews of financial audits conducted by the NSW Audit Office on an ongoing basis.

PERFORMANCE AUDIT

This has been covered in the section on performance audit.

QUALITY MANAGEMENT

The Audit Office is accredited to the ISO9001:1994 quality management standard. During the course of our fieldwork the AO was subject to a triennial audit by an external service provider. The result of this was a recommendation for continued certification against ISO9001:1994.

The main issue coming out of the last review was the consideration of an "issue management tool" hosted on the intranet to deal with the follow up and resolution of issues from key management bodies such as the Board of Management, Audit Committee and Continuous Improvement Working Group. These bodies currently use action lists to monitor issues.

The aim of the Audit Office is to seek accreditation to the revised standard ISO9001:2000, once Internal Audit has undertaken a review on the implementation of required revisions to the quality management system. This is expected to occur with the next external surveillance audit scheduled for November/December 2003.

The ISO reviews do consider both Financial and Performance audits, however the scope of review in this area is limited to certain aspects of audit planning, internal communication, client communications, client satisfaction and end of audit reviews.

RECOMMENDATION 76 (MEDIUM PRIORITY):

Consideration should be given to the performance of a regular Quality Review under the auspices of ACAG (similar to those which occurred in WA and New Zealand) or from a third party under the frameworks provided by the Institute of Chartered Accountants and Australian Society of CPA's. This will assist in better practice benchmarking.

QA (4) - WHETHER THE QUALITY ASSURANCE PROCEDURES IN THE AUDIT OFFICE EXTEND TO FINANCIAL AUDITS, COMPLIANCE AUDITS, PERFORMANCE AUDITS, AUDIT REPORTING AND INTERNAL ADMINISTRATION OF THE AUDIT OFFICE.

FINDINGS:

Quality assurance procedures are undertaken throughout the Audit Office. The key quality assurance mechanisms across the various areas are:

- Financial Audit - Inherent quality assurance review procedures within assignments through review by Engagement Manager, Engagement Controller and Engagement Reviewer, where necessary. This is strengthened by the peer QARC processes.
- Compliance Audit - Inherent quality assurance review procedures within assignments by Engagement Manager and Controllers together with Compliance Audit Group during compilation of data.
- Performance audits - Inherent quality assurance review procedures within assignments by Engagement Manager and Controllers.
- Audit Reporting - Centralised reporting and version control mechanism with an ultimate sign off by the AG. Currently seeking client feedback on draft reports.
- Internal Administration - ISO 9001 quality assurance programme combined with internal audit review processes and the Continuous Improvement Working Group.

Thus quality assurance processes are in place across core activities.

However Quality Review procedures have principally been limited to the operation of the QARC and ISO quality accreditation.

There are no recommendations for this finding as previous recommendations in this section have adequately addressed our findings in this area.

14 Reporting to Parliament

INTRODUCTION

The Auditor-General has revised the form and content of his reports to Parliament since coming to office. In addition there has been a concerted effort to improve the quality of the reports through provision of a style guide and training for staff.

The timing and contents of the Auditor-General's Reports to Parliament is summarised as follows: (source: Inside cover of AG's Report to Parliament 2002):

May	Contains commentary on Government agencies with a financial year-end between 1 July and 31 December. These relate mainly to universities and associated entities.
October	Contains commentary on Total State Sector Accounts.
November December	Contains commentary on Government agencies with a financial year-end between 1 January and 30 June. Material is included in these volumes progressively, depending on when each audit is completed.

RP (1) WHETHER THE AUDITOR-GENERAL'S REPORTS TO PARLIAMENT CONTAIN INFORMATION ALREADY REPORTED TO PARLIAMENT.

FINDINGS:

Under the Annual Reports Legislation³⁸ Agencies are required to submit, not later than four months after the end of their financial year, their annual report to the Appropriate Minister. The Minister is then required to lay the report before both Houses of Parliament within one month of receipt. In general this means the reports for Agencies with 30 June year ends are laid before Parliament before the end of November.

To assess whether the Auditor-General's Reports to Parliament contain information already reported to Parliament we reviewed a sample of Auditor-Generals reports to Parliament on Agencies. We compared these reports to the Annual Reports of Agencies, the other main source of reporting to Parliament, through the relevant Minister.

A guide at the front of Volume Six of the Auditor Generals reports 2002 outlines the standard contents of reports on agencies which now includes:

- Summary of the Audit Opinion – The key result of each audit;
- Key Issues identified during the audit – being significant findings or outcomes, major developments impacting on the Agency, key repeat findings and recommendations to Parliament;
- Performance Issues – covering key financial and operational statistics;
- Control Issues – outlining any significant shortcomings;
- Compliance Issues – based on the results of compliance audit activity performed on the Agency;
- Financial Information – summary income expenditure and financial information;
- Agency Activities – summary and reference; and
- Agency Response – where the Head of an Agency does not believe that the commentary in the Auditor-General's Report adequately reflects the Agency's position or actions taken.

³⁸ Annual Reports (Statutory Bodies) Act 1984 and Annual Reports (Departments) Act 1985

The timing of the Auditor-General's reports means they will often be tabled slightly after that of the Agencies .

Based on our review it is apparent that some of the information contained in the Auditor-General's report is included in the Annual Reports. Specifically this can include:

- Audit Opinion type;
- Summary financial information;
- Performance issues - although the Auditor Generals reports often include different indicators and benchmarks; and
- Agency activities

However, the Auditor-General Reports do provide a useful summary of audit outcomes and issues. In particular, many of the key issues raised in the Auditor-General's Report are not given the same prominence in Agency reports, since Agency Annual Reports tend to focus on operations and operational results rather than issues that have a financial audit impact.

RECOMMENDATION 77 (HIGH PRIORITY):

As part of the Auditor Generals own continuous improvement process, consideration should be given to assessing whether information included in his reports to Parliament could be further streamlined, avoiding duplication.

RP (2) WHETHER THE PARLIAMENT IS BETTER INFORMED BY A SEPARATE DISCUSSION AND ANALYSIS OF THE OPERATIONS OF DEPARTMENTS AND AGENCIES AS PREPARED BY THE AUDITOR-GENERAL AND HIS STAFF.

PA (6) FOLLOWING THE 2001 AMENDMENTS TO THE PUBLIC FINANCE AND AUDIT ACT 1983, THE AUDIT OFFICE NOW INCLUDES A SECTION ON PERFORMANCE ISSUES FOR LARGER AGENCIES, WHICH GENERALLY COMPRISES MATERIAL ON PERFORMANCE ISSUES. THE REVIEWER SHOULD EXAMINE AND EVALUATE THE AUDITOR GENERAL'S REPORTING ON PERFORMANCE ISSUES IN HIS GENERAL REPORTS TO PARLIAMENT, INCLUDING ANY POSSIBLE IMPROVEMENTS.

FINDINGS:

The relevant discussion and analysis of operations of Departments and Agencies included in the Auditor-General's reports consists primarily of the following areas (as defined in the Auditor-General's reports):

- Key Issues identified during the audit. These aim to include significant findings, major developments, key repeat findings and recommendations to Parliament; and
- Performance Issues which include key financial and operational statistics aimed at helping to understand how well the Agency is performing.

In addition the Auditor-General has prepared commentary on a sector wide basis such as for Universities and the Health sector.

In the introduction to his Report to Parliament 2002 Volume Five the Auditor-General provided comment on his reasons for inclusion of commentary on Agencies' performance. These reasons include a lack of a whole-of-government approach to performance reporting including benchmarking against Agencies in other jurisdictions. The Auditor-General noted that there is a tendency only to report the good news.

To assist in assessing whether Parliament is better informed by this information we compared the Auditor-General's report for a random sample of Agencies to information reported in the Agencies Annual Report. The main findings of this exercise were as follows:

KEY ISSUES

- The Auditor-Generals key issues were not always noted in the Agency Annual Reports with the same level of emphasis, since the focus in Annual Reports is on operational results rather than issues having a financial audit impact.

PERFORMANCE INFORMATION

- The Auditor-Generals Performance information was sometimes a summary of more detailed performance analysis information in Agency Annual Reports. As such there is a danger that the information reported by the Auditor-General could be misinterpreted due to a lack of full information. Examples include:
 - summary performance information on length of stay and bed occupancy in the Area Health Service reports; and
 - summary crime indicators and benchmarking against other States in the NSW Police report.

However, having said this, it is felt that the ability of Agency Heads to comment on the reports should address any major inconsistencies.

- Performance information is generally not analysed in the Auditor-General's Reports. Rather it is left for the reader to make up their own minds on the impact.
- In a number of instances the Auditor-General's report included benchmarking against other Australian State Jurisdictions, which had not been included in the Annual Report of the respective Department or Agency. However, once again there was limited discussion on the interpretation of benchmarks. The manner in which other State Jurisdictions set performance indicators for performance, or use and collect data to show the results of their operations could be undertaken in any manner of ways. In addition, the policy framework of Government's within each State and Territory and the resulting focus of activities within each of their Departments and Agencies is unlikely to be consistently similar with that of New South Wales. Thus benchmarking the performance of New South Wales Department's and Agencies by the Auditor-General against other State Jurisdictions may lead to inappropriate conclusions on performance levels without appropriate commentary. (NB: We note that the Auditor General, did allude to these problems in his introduction to the Auditor-General's Report to Parliament 2002 Volume Five).

The Auditor-General has publicly commented that he believes that NSW Departments and Agencies need to provide better information through their Annual Reports to demonstrate to the Parliament and the Public how they are efficiently and effectively utilising their resources (i.e the taxes paid by NSW Taxpayers)³⁹. There has been a concerted drive by the Auditor-General to therefore make comment on the efficient and effective use of resources by NSW Departments and Agencies within his reports to Parliament. The Auditor-General has also stated publicly through television interviews that key performance indicators and benchmarking data against other Australian State and Territory Jurisdictions should be reported on and included within Department and Agency Annual Reports.

Interviews with Audit Office Clients, including Central Agencies, during this review indicated support for including performance indicator information and benchmarking data within Annual Reports. Indeed in June 2002, the Department of Treasury advised all Departments and Agencies that they were to include key performance indicator information in their Annual reports.

However, it is the belief of Acumen Alliance that the framework for the use of key performance indicators and benchmarking against other States and Territories should be driven by Central Agencies such as the Department of Treasury and the Premiers Department, rather than the Auditor-General. Instead of the Auditor-General providing separate discussion and analysis of key performance indicators and benchmarking data within his Annual Report to Parliament we would be more supportive of a process whereby:

- A high level Committee containing representatives of the Department of Treasury, Premiers Department and the Auditor-General work together to establish a framework for the consistent setting and reporting of key performance indicators and benchmarking of performance information with other State Jurisdictions within Annual Reports;
- The Auditor-General facilitate high level workshops and presentations with Departments and Agencies to assist them in understanding how to set effective quantitative and qualitative performance indicators and how these should be measured;

³⁹ Stateline Interview shown on the ABC in November 2002.

- The Auditor-General then provides certification of the accuracy of the indicators to Parliament, through the Auditor-General's Report to Parliament, providing his opinion of the key performance indicator results in Department and Agency Annual Reports. This process could be aligned to that undertaken by the Office of the Western Australia Auditor General, whose relevant legislation specifically includes the audit of performance indicators.

The Auditor-General undertook an independent Parliamentary satisfaction survey in December 2002 which included a number of questions aimed at determining how important Parliamentarians viewed aspects of the Auditor-Generals reports to Parliament and how well the Auditor-General performed in that area. However only twenty responses to the survey were received and this was not considered to be a statistically relevant result to enable conclusions to be drawn. As a result the Auditor-General is planning to reissue the survey after the election and publish results by 30 June 2003.

RECOMMENDATION 78 (MEDIUM PRIORITY):

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.

RP (3) THE COSTS OF THE AUDITOR-GENERAL IN PREPARING THE REPORTS TO PARLIAMENT AND WHETHER THE REPORTS PROVIDE VALUE FOR MONEY.

FINDINGS:

The cost of the reports to Parliament for the last two years can be broken down as follows:

Year	2000-01	2001-02
Hours	10,113	9,396
Staff Costs	1,123,074	1,207,688
Printing costs	55,418	55,457
Other Costs	<u>20,090</u>	<u>32,421</u>
Total	<u>1,198,582</u>	<u>1,295,566</u>

Costs are recovered through a budget allocation, which stood at \$1,275,000 for the 2001-2002 year (\$1,205,000 for 2000-01).

Staff costs are accumulated on the Audit Office TOPS Practice Management System, using standard charge out rates. Time is charged by Engagement Controllers and staff in the preparation of individual reports on Agencies to specific Agency Auditor-General's report codes. Staff involved in the general review and proofing of the reports charge time to a general Auditor-General's Report code. Staff costs detailed in Table 1 above are a combination of the two.

Review of the detailed Auditor-General report codes cost breakdown by client for the current 2002-03 year revealed direct cost charges per client varied from less than \$200 up to \$37,812. We note that there is no current formal review of the time charged by staff by client for the Reports to Parliament, during the billing process.

Costs are accumulated on the above TOPS codes and a bill raised each time a report is tabled in Parliament. The timing of each report and billing means that a particular bill raised may not solely relate to a specific report, as either some drafting costs for the next report may already have been incurred, or not all direct costs may have been received.

⁴⁰ Breakdown from Audit Office TOPS and General ledger

In considering whether the Auditor-General's reports provide value for money we need to consider what applicable criteria there are to measure against. As there are no quantitative criteria available, then consideration needs to be given to the qualitative criteria.

The Audit Offices Corporate Plan identifies a key objective to "satisfy the needs and expectations of Parliament" together with a strategy of reporting on issues that best address accountability and performance, compliance and probity. The stated measure of achievement is in relation to response to the Parliamentarians satisfaction survey, which would appear to be an appropriate qualitative criteria.

RECOMMENDATION 79 (HIGH PRIORITY):

The decision of the Auditor-General to undertake a new survey of Parliamentarians subsequent to the State Election, with results to be reported by 30 June 2003 is supported. The survey should include questions such as whether:

- the content of the reports was easily understood;
- the relative importance of issues raised in the report was clear; and
- relevant issues had been chosen to report.

It is also suggested that the Auditor-General run workshops and structured interviews with Members of Parliament.

RECOMMENDATION 80 (HIGH PRIORITY):

A formal review of costs that are accumulated by staff to the Reports to Parliament, by client and overall, be undertaken prior to the issue of each bill to ensure they appear reasonable.

RP (4) WHETHER THERE ARE LOWER COST OPTIONS IN THE STYLE, FORMAT AND CONTENTS FOR THE AUDITOR-GENERAL'S ANNUAL REPORTS TO PARLIAMENT.

FINDINGS:

As detailed in table 1 above the vast majority of costs incurred in relation to the preparation of the Auditor-General's Annual Reports to Parliament are in relation to staff time.

To significantly reduce costs would require a significant reduction in staff time spent and charged. This could be undertaken through:

- Reporting only on an exception basis;
- Removal of information already included in Annual Reports;
- Including Agency report information in the Statutory Audit Reports provided to Ministers; or
- Reporting solely on a Ministerial basis (rather than by Agency) – as done by the Queensland Audit Office.

The Audit Office has focussed on trying to reduce indirect costs, including printing. All reports to Parliament are available for download on the Audit Office's website in pdf format. In addition notification when reports are tabled, is sent to interested parties via email, with link to the website.

In addition the Audit Office is considering ways to make the reports more accessible and easy to use, primarily through the introduction of CD-Rom versions of the report which will enable easy search and navigation.

RECOMMENDATION 81 (HIGH PRIORITY):

Through the results of the parliamentarians questionnaire follow up on the impact of changing the scope of reporting. Consider cost reduction initiatives including:

- Reporting by exception only;
- Reporting through the Statutory Audit Reports; or
- Reporting on a Ministerial basis only.

15 Expectations on Reporting

INTRODUCTION

Our section on Reporting to Parliament included a summary of the timing and content of the Auditor-General's Reports to Parliament. In considering whether Audit Office reports currently meet the needs of users it is important to identify who the various users of reports may be. Potentially users of Audit Office Reports could be seen to be:

- Client Agencies;
- Central Agencies - such as the Department of Treasury and the Premiers Department, who set policy and legislation;
- Parliament; and
- The Public.

The expectations of users are bound to vary as all would have different views on what was important for them. The challenge for the Auditor-General is to reconcile these differing needs within the Audit Office's overall mission to "Assist Parliament to improve the accountability and performance of the State."

ER (1) HOW THE AUDIT OFFICE ASCERTAINS THE EXPECTATIONS OF THE VARIOUS USERS OF THE AUDITOR GENERAL'S REPORTS AND WHETHER IT MEETS THEM.

FINDINGS:

The Public Accounts Committee of the NSW Parliament (Committee) in its report on the *Inquiry into the Collapse of the NSW Grains Board* in May 2001 found that:

- the Audit Office did not consider its audience in preparing the Auditor-General's reports to Parliament;
- the Auditor-General did not report repeat audit findings effectively; and
- the Auditor-General's focus and reporting on business risk was restricted.

The Committee in its report on the *First Home Owner Grant Scheme* in December 2002 noted that the Audit Office needed to indicate the degree of risk to the Government of issues it reports to Parliament. The Committee reiterated that this issue was identified in the report on the *Inquiry into the Collapse of the NSW Grains Board*.

As a result of the Committees findings in those two reports it has made a number of recommendations that the Audit office should take its wider audience into account in preparing the Auditor-General's reports. The reports should explain why listed issues are significant and their financial implications.

Whilst noting the above, the Auditor-General has clearly recognised the importance of effective reporting to various stakeholders and that his reports to Parliament are the key method in which his message can be delivered. To that end the Audit Office has recently adopted a "plain English" approach to report writing which was cascaded through the Audit Office through training for staff and the introduction of a new "style guide" for reports. However, in his Annual Report 2002 the Auditor-General recognises that there are still further improvements that can be made.

The Corporate Plan of the Audit Office identifies a key objective being to "satisfy the expectations of Parliament, other clients and stakeholders". Within the plan there are a number of Key Actions (KA) which have been developed to assist in meeting the objectives. Of relevance to ascertaining the expectations of users are:

- (KA 1) – Seek input from Parliament, other clients and stakeholders to identify contemporary themes that serve the interests of citizens and public sector management;
- (KA 4) – Meet with targeted representatives of Parliament / Committees at least annually to obtain information needs;
- (KA5) - Implement programs to brief Parliamentarians about the role and functions of the Auditor-General; and
- (KA6) – Implement external communications strategies.

Apart from the direct relationship with the Public Accounts Committee, the Auditor General also maintains a relationship with other key Parliamentary Committees, one aspect of which is to seek their information needs. These include:

- Public Bodies Review Committee; and
- Standing Committee No 1 – Finance and Treasury.

As indicated in the Section of our Report on Reporting to Parliament, whilst a survey of Parliamentarians was undertaken during 2003, insufficient responses to provide a statistically relevant conclusion were received.

The main formal process to specifically ascertain feedback from clients in relation to reporting is by way of the biannual Audit Office client satisfaction survey. However, the questions in this area primarily relate to the form and process rather than the content.

Expectations of the public are generally not actively sought. However, the Audit Office does receive correspondence in relation to issues and Reports to Parliament from individuals and lobby groups. As mentioned earlier the Public Accounts Committee has given specific detail of its expectations of reporting by the Auditor-General in its reports on the *Inquiry into the Collapse of the NSW Grains Board* and *First Home Owner Grant Scheme*. This correspondence is considered and replies made based on the ability of the Auditor-General to deal with the request.

Through discussion with the Auditor-General and Audit Office staff it is apparent that there has not been a coordinated approach to the documentation and ascertaining of the expectations of the varying users of the Reports to Parliament.

Recommendations for this finding have been covered in previous components of this report.

ER (2) HOW THE AUDIT OFFICE RECONCILES THE VARYING EXPECTATIONS OF USERS WITH LEGISLATIVE REQUIREMENTS AND AUDIT PRACTICE

FINDINGS:

LEGISLATIVE FRAMEWORK

The broad legislative requirements in relation to reporting by the Auditor General to Parliament are outlined in Section 52 of the Public Finance & Audit Act 1983. In addition to a report on the Total Public Sector Accounts the Auditor General "...may report on any matters that arises from or relates to the exercise of the audit or other functions of the Auditor-General and that in the opinion of the Auditor-General should be brought to the attention of Parliament"⁴¹.

Thus the legislation provides the Auditor-General wide scope in his ability to report items to Parliament, which is supported by Acumen Alliance. It is under these auspices that the Auditor-General has extended the content of his reports beyond simply financial issues to include commentary on Agencies' performance. His reasoning behind this was detailed in the introduction to the Auditor-General's Report to Parliament 2002 Volume Five.

AUDIT PRACTICE

The current approach and content of the Auditor Generals Reports to Parliament, particularly in relation to the inclusion of performance issues, means there is a certain level of "angst" with some clients. The issues surrounding this area have been discussed further under the section on Reporting to Parliament.

In a professional practice audit issues, and comments on performance, would often get reported. However, this information would only get reported to the Board and not become public. It is the Auditor-Generals mandate in reporting to Parliament that provides part of the basis for varied expectations.

Ultimately it is principally up to the professional judgement of the Auditor-General and staff of the Audit Office to decide what information "assists parliament to improve the accountability and performance of the State."

⁴¹ Part 3 Section 52 (3) Public Finance and Audit Act 1983.

RECOMMENDATION 82 (MEDIUM PRIORITY):

Once the expectations of users have been formally ascertained a gap analysis be undertaken to reconcile expectations against current reporting.

KEEPING WITHIN THE SCOPE OF LEGISLATIVE REPORTING REQUIREMENTS

We were requested by the Public Accounts Committee to specifically consider whether the Auditor-General has kept within his legislative reporting scope. Part 3 Section 27(B) subsection 6 of the Public Finance & Audit Act 1983 states:

- a) "Nothing in the Act entitles the Auditor-General to question the merits of policy objectives of the Government, including:
- b) Any policy objective of the Government contained in a record of a policy decision of Cabinet, and
- c) A policy direction of a Minister, and
- d) A policy statement in any Budget Paper or other document evidencing a policy direction of the Cabinet or a Minister."

Part of the difficulty faced in reviewing this area is in the consideration of knowing what is policy, however the Audit Office aims to apply the definitions used in the legislation. In addition the nature of Performance Audits means that the effect of a policy decision may well be analysed as part of the performance analysis.

As noted in the Performance Audit section of this report the Audit Office has in place a process to ascertain Government Policy in relation to any areas subject to audit. The policy includes writing to the relevant Ministers to ensure the latest policy is on hand for new Audits. Our review of Performance Audits did not reveal any instances where reports had "questioned the merits of policy objectives".

To assess whether the Auditor-General had overstepped his powers in relation to "questioning the merits of policy objectives" we also reviewed a number of media releases and interviews given by the Auditor-General.

Our reviews did not reveal any instances where the Auditor General had commented on the "merits of policy objectives".

Appendix A

Performance Audit Activity

Performance Audit Activity from 1 July 2000 to 31 December 2002

No.	Title	Agency	Tabling Date	Cost
75	Management of Road Passenger Transport Regulation	NSW Department of Transport	6 September 2000	\$114,757
76	Judging Performance from Annual Reports	Cross-agency	29 November 2000	\$155,094
77	Reporting Performance Better Practice Guide A Guide to Preparing Performance Information for Annual Reports		29 November 2000	\$34,056
78	Fare Evasion on Public Transport	State Rail Authority (CityRail) State Transit Authority	6 December 2000	\$267,442
79	Review of Administration	TAFE NSW	6 February 2001	\$193,566
80	Readiness to Respond	Ambulance Service of New South Wales	7 March 2001	\$362,777
81	Maintenance of Public Housing	Department of Housing	11 April 2001	\$150,058
82	Controlling and Reducing Pollution from Industry	Environment Protection Authority	18 April 2001	\$253,650
83	NSW Correctional Industries	Department of Corrective Services	13 June 2001	\$222,424
84	Follow Up Audit: Police Response to Calls for Assistance The Levying and Collection of Land Tax Coordination of Bushfire Fighting Activities	NSW Police Service NSW Treasury NSW Rural Fire Service	20 June 2001	\$106,793
85	Internal Financial Reporting including a Better Practice Guide		27 June 2001	\$132,792
86	Follow-up of Performance Audits: The School Accountability and Improvement Model The Management of Court Waiting Times	Department of Education Attorney-Generals' Department	14 September 2001	\$88,354

No.	Title	Agency	Tabling Date	Cost
87	E-Government Use of the Internet and related technologies to improve public sector performance, including Better Practice Guide.	Cross-agency	19 September 2001	\$599,565
88	e-steady, e-ready, e-government: e-government readiness assessment guide		19 September 2001	
89	Management of Intellectual Property	Cross-agency	17 October 2001	\$148,825
90	Management of Intellectual Property Better Practice Guide		17 October 2001	\$21,999
91	Educational Testing Centre	University of New South Wales	21 November 2001	\$186,967
92	Environmental Impact Assessment of Major Projects	Department of Urban Affairs and Planning	28 November 2001	\$149,124
93	Government Property Register	Department of Information Technology and Management	31 January 2002	\$56,645
94	Collecting Outstanding Fines and Penalties	State Debt Recovery Office	17 April 2002	\$109,011
95	Managing Environmental Issues	Road and Traffic Authority	29 April 2002	\$137,461
96	Managing Animal Disease Emergencies	NSW Agriculture	8 May 2002	\$219,119
97	Bus Maintenance and Bus Contracts	State Transit Authority Department of Transport	29 May 2002	\$275,030
98	Managing Risk in the NSW Public Sector	Cross-agency	18 June 2002	\$269,523
99	User-friendliness of Websites	Cross-agency	26 June 2002	\$79,240
100	Managing Sick Leave	NSW Police Department of Corrective Services	23 July 2002	\$172,630
101	Regulating the Clearing of Native Vegetation	Department of Land and Water Conservation	20 August 2002	\$181,066
102	Electronic Procurement of Hospital Supplies	Department of Health	25 September 2002	\$275,227

No.	Title	Agency	Tabling Date	Cost
103	Outsourcing Information Technology	Cross-agency	23 October 2002	\$239,524
104	Managing Grants	Ministry for the Arts Department of Community Services Department of Sport and Recreation	4 December 2002	\$130,738
105	Managing Hospital Waste	Department of Health Area Health Services Hospitals	10 December 2002	\$95,759

Appendix B

Audit Office Publications

Audit Office Publications

The Audit Office produces a number of publications including:

- **Better Practice Guides on the following topics:**
 - [Management of Intellectual Property](#) October 2001;
 - [e-ready, e-steady, e-government e-government readiness assessment guide](#) September 2001;
 - [Monitoring and reporting on performance audit recommendations](#) June 2001;
 - [Internal Financial Reporting](#) June 2001;
 - [Reporting Performance: A guide to preparing performance information for annual reports](#) November, 2000;
 - [Contracting Out Review Guide](#), June 1999;
 - [Public Sector Corporate Governance - Ready Reckoner](#), April 1999;
 - Methodology for the Review of Residential Services for People with Disabilities, June 1998;
 - [On Board: Guide to Better Practice for Public Sector Governing and Advisory Boards](#), April 1998;
 - [Corporate Credit Card](#) January, 1997;
 - [Debtors Administration](#) September, 1996;
 - [Administration of Grants](#) December, 1995;
 - [Joint Operations in the Education Sector](#) September, 1995;
 - Fraud Control [Volume 1: Conceptual Framework](#) March, 1994;
 - [Volume 2: Strategy](#) March, 1994;
 - [Volume 3: Diagnostics](#) March, 1994; and
 - [Volume 4: Fraud Control Self Audit Kit](#), March 1998;
- **Questionnaires used when conducting Audits:**
 - [Managing the Environment](#) July 2002; and
 - [Risk Management](#) June 2002.
- **Professional Update (six monthly) covering:**
 - Accounting Standards over the previous six months;
 - Financial Reports Checklist;
 - Urgent Issues Group;
 - Legislative Changes;
 - Auditing Standards;
 - Premier's Department Circulars;
 - Corporations Law;
 - Premier's Memoranda;
 - Auditing Guidance Statements;

- Treasury Circulars;
 - Audit and Assurance Alerts;
 - Treasury Policy Papers Exposure Drafts; and
 - Treasury Research Papers.
-
- **Awareness (monthly):**
 - Audit Office Update;
 - Miscellaneous Publications;
 - Accounting Update;
 - Legislative Changes Update;
 - Auditing Update;
 - Treasury Update;
 - Urgent Issues Group Update;
 - Premier's Department Update ;
 - International Update; and
 - Audit Office Better Practice Guides.

Appendix C

Contract Audit Agents Manual

CONTRACT AUDIT AGENTS MANUAL

CONTRACTING OUT POLICY

To ensure the provision of cost-effective audit services, sufficient financial attest audits should be contracted out to enable the efficiency of in-house audits to be benchmarked against those undertaken by private sector contractors.

To maintain expertise and industry knowledge within various industry segments, TAO (The Audit Office) needs to retain certain strategic audits within each industry. This will enable TAO to maintain an involvement with both the issues facing various industry segments and better control contract agents.

This will enable:

- the private sector auditors to have an opportunity to develop greater knowledge of the public sector audit, and
- an opportunity to improve our process through knowledge transfer and the adoption of innovative ideas.

The following criteria should be taken into account when determining the suitability of audits for contracting out:

- Agencies which interface across government (e.g. Treasury, Premier's Department etc.), core government departments and those agencies which have significant exposures to taxpayers (e.g. WorkCover Authority, State Superannuation and Public Transport) will continue to utilise in-house resources to undertake the audit of those agencies.
- Consideration should be given to the "grouping" of audits selected for outsourcing.
- Contracting out ought to involve the consent of the audit client.
- Audits considered suitable for contracting out would normally be selected from a combination of:
 - government trading enterprises
 - corporatised entities
 - marketing boards etc.
 - other statutory authorities

The decision to contract out an audit is made by the Auditor-General, and will generally be made in consultation with the Assistant Auditor-General (AAG) and Director of Audit (DoA) responsible for that audit.

The DoA is responsible for the audit and reporting, including all contracting arrangements and determining the reliance that may be placed on the work of the CAA.

AUDIT OFFICE POLICY ON AUDIT INDEPENDENCE

The CAA shall not, directly or indirectly, provide other services of any nature to an Audit client, either during the period of appointment, or for a further period of twelve calendar months immediately following completion or termination of this engagement.

The Auditor-General must approve any exceptions to this in advance and in writing. In any event, they will only cover services that the Auditor-General can provide under the Public Finance and Audit Act 1983.

The contract audit agent ought to exercise no more powers than Parliament has provided to the Auditor-General. Where approval has been given, the Director of Audit is responsible for ensuring that the above policy is being adhered to by the CAA.

Appendix D

Overall Audit Office Response to Acumen Alliance Report

THE ATTACHMENT A TO THE AUDITOR GENERAL'S COVERING LETTER ADDRESSES A NUMBER OF KEY CONCERNS THE AUDIT OFFICE HAS WITH ISSUES COVERED IN THE ACUMEN REPORT. THE ATTACHMENT IS NOT MEANT TO BE COMPREHENSIVE, BUT RATHER COVERS ISSUES WHERE WE BELIEVE THE REPORT HAS FUNDAMENTAL ERRORS, EITHER OF BASIC FACT OR OF UNDERSTANDING AUDIT OFFICE PRACTICES AND PROCEDURES.

AUDIT OFFICE "CLIENTS" (AUDITOR GENERAL'S COMMENT)

The report argues (Section 9, second page) that our HR Strategy "would focus staff predominantly on the needs of only one stakeholder, being Parliament".

This statement is not correct. It is made almost directly after Acumen notes that "the AO recognise[s] that whilst it sees Parliament as its primary client, its clients are the NSW Parliament, government departments and agencies and ultimately NSW taxpayers".

If a conflict did arise in our audit work between the needs of Parliament and those of a government agency, we make no apology for regarding Parliament as more important. In fact, Acumen appears to support this.

But for Acumen to then argue this means we focus *only* on Parliament's needs is clearly wrong. Our Corporate Plan, our business plans, our staff competency statements and our HR Strategy all recognise that we regard agencies as important stakeholders.

ACUMEN ALLIANCE RESPONSE:

It was clearly stated to Acumen Alliance during this review by the Performance Audit Branch and in exit discussions with the Deputy Auditor General and Head of Corporate when discussing our preliminary draft report on the Staff of the Audit Office and Administration that the primary client of the Audit Office was Parliament. Acumen clearly supports this in its report findings. However, during the course of our review when we discussed the needs of other stakeholders, such as Government Agencies, we were constantly reminded that the primary focus was on the needs of Parliament, not on Agencies. Current Audit Office documentation such as the Corporate Plans etc, as we state in our report, gives little focus to stakeholders such as Agencies. In fact we were advised by the Deputy Auditor General and Head of Corporate that the main aim of the HR strategy was aimed at meeting the needs of Parliament. Little evidence was provided by the Audit Office to demonstrate that sufficient focus was also given to other key stakeholders.

We stand by our comment that the Audit Office needs to ensure that its HR strategy identifies how staff will be trained to reconcile and manage the diverse needs of Parliament versus other key stakeholders such as Agencies.

HR ISSUES (AUDITOR GENERAL'S COMMENT)

Acumen notes (Section 9, text preceding Recommendation 49) that large numbers of senior Audit Office staff have reached retiring age or will do so over the next few years. It also notes the difficulties we face in attracting and retaining suitable staff and that the Office regards this as a serious issue.

These difficulties reflect the competition from private sector audit firms and the generally strong demand in the private sector for well-trained accounting professionals.

Acumen then argues that "the Audit Office has done little to facilitate a long term solution".

This is a very surprising statement. Acumen was fully aware that this issue was one of the key drivers of our new HR Strategy. This strategy (which Acumen discussed with us at length and which is referred to on numerous occasions in its report) has our ability to attract new staff as a key element.

Acumen was also given a copy of the presentation the Auditor-General made to all staff when the new HR Strategy was launched late last year. The presentation clearly showed, in graphical form, the age structure of senior staff levels, identified our concerns on this matter and indicated how this was one of the drivers of the new HR Strategy.

Because our new HR Strategy is so broad-based and comprehensive, it will take time to implement. Acumen has recommended that some key components of the Strategy should be fast-tracked. We do not believe this is possible. Acumen does not fully understand the inter-relationships between the many components of the Strategy or the complexities of dealing with HR issues in the public sector environment.

ACUMEN ALLIANCE RESPONSE:

There is no criticism levelled in our report as to the lack of knowledge of the issue of the pending retirement of staff within the Audit Office. However, in addressing the issue one would expect greater evidence of specific activities. The Audit Office has noted the issue in the HR Strategy and has noted that it will undertake activities to address it. It appears that other than creating three new positions, which do not in themselves address the fundamental problem, the Audit Office has done little to facilitate a long term solution.

AUDIT OFFICE ATTITUDE TO THE MEDIA (AUDITOR GENERAL'S COMMENT):

The Acumen report suggests that we select our performance audit topics on the basis of the media interest they will generate.

We reject this suggestion outright. We believe that Acumen has confused 'public interest' (which is one of the criteria that guide our topic selection) with 'media interest'. In our discussions with senior Acumen representatives, they were unable or unwilling to nominate even one of the performance audits we conducted over the last three years as an inappropriate topic.

One piece of "evidence" Acumen puts forward is the observation that our working papers contain copies of the media articles on our reports. It would be quite strange for any organisation (public or private sector) not to keep copies of media articles that referred to it.

A final piece of “evidence” put forward by Acumen is that we prepare a “media kit” for each report. This “media kit” is for our own use in responding to any media questions. It is simply a summary of the key findings made in the report, key background facts and draft answers to possible questions that may be asked. It is prepared to ensure that our responses are accurate and consistent with the report’s findings. We believe this is a completely acceptable practice and will continue with it.

ACUMEN ALLIANCE RESPONSE:

Our report provides strong evidence that the Audit Office uses ‘media interest’ as a key rationale for selecting performance audit topics. Within the report we note that the selection of performance audit topics is subjective and also provide clear evidence of internal emails that make it clear that staff are focusing on what will generate maximum media interest, when selecting topics to include in the performance audit program. There is quite clearly a difference between ‘media’ and ‘public’ interest and this is understood by Acumen Alliance. Mechanisms for selecting performance audit topics by the Audit Office appear to indicate that they see ‘media interest’ and ‘public interest’ as one and the same.

To state that because Acumen Alliance did not believe that any performance audit topics chosen during the review period were inappropriate and use this to justify the focus on ‘media interest’ is problematic. The fact is that there may have been many other areas just as worthy of being selected for a performance audit, yet they were not chosen due to the subjective nature of topic selection and the inappropriate focus on what would drive media interest.

QUALITY CONTROL OF PERFORMANCE AUDITS BY SENIOR OFFICERS (AUDITOR GENERAL’S COMMENT):

Acumen questions the understanding and involvement of senior officers with audits. Acumen says (‘Level of Clearance’ section under Term of Reference PA3) that: “there is evidence that the PAEC [Performance Audit Engagement Controllers] and the AAG do not take a hands-on participative role in the conduct of performance audits, except at the planning and reporting stage of a Performance Audit”.

No factual evidence is produced to support this conclusion. None of the officers concerned were interviewed to verify these findings.

We have valid evidence that indicates that both the engagement controller and the AAG are involved in all phases of every audit. In addition, quality control is demonstrated in various checklists and sign-offs that are part of our ISO 9001 certification. Acumen's comments demonstrate a serious lack of understanding of the processes we follow with our audits.

ACUMEN ALLIANCE RESPONSE:

Figure 2, in the Performance Audit Section of our report, sets out in detail based on information from Audit Office Management Systems the time that is applied by each level of Performance Audit Staff to Performance Audits. This information in itself is compelling as it clearly demonstrates that the AAG and PAEC's do not have, in our professional opinion, sufficient involvement in the conduct of Performance Audits. It is our belief that the AAG and PAEC time on Performance Audits should approximate between 50 and 60% of time allocated to the Audit. We dispute the fact that officers within the Performance Audit Branch were not interviewed in relation to time spent on audits by classification of staff. We have detailed interview notes that clearly demonstrate concern by staff within the Performance Audit Branch as to the amount of time that senior levels of staff dedicate to involvement in each audit.

As discussed during our exit discussions with the Performance Audit Branch, the argument of ISO 9001 quality control is one of substance over form. There is a clear difference between signing off checklists and doing a detailed review of an audit file. Clear evidence from our review of Performance Audit files indicated that quality control was a clear issue. The concerns that we had with review of Performance Audit Files during our review were corroborated through discussions with PAEC's and other staff from the Branch.

STAFF SPECIALISATIONS IN PERFORMANCE AUDIT (AUDITOR GENERAL'S COMMENT):

Acumen says (text preceding Recommendation 14, Term of Reference PA1) that "evidence indicates that insufficient attention is given to matching the expertise of auditors with the subject matter of audits".

No evidence is provided by Acumen to support that allegation. No discussion took place either with the PAECs or with the AAG to ascertain how projects are allocated.

We could have provided evidence to indicate that experience or knowledge of staff is always an issue for management in assigning projects. For example, staff involved in theme areas such as eGovernment, have continued to work in the area for 2-3 years, producing five reports.

Performance audit staff come from a variety of backgrounds. While formal tertiary qualifications in a relevant field are important, we have found that individuals' experience and skill levels are a more significant factor in contributing to the success of an audit.

ACUMEN ALLIANCE RESPONSE:

Evidence is indeed provided within our report. In fact we state within the text of our findings on Performance Audit, "Analysis of results from the most recent survey (client) indicate that the level of client satisfaction with the Audit Office's 'understanding of Agencies business' and 'appropriateness of skills and expertise' is significantly below the standard set by the Audit Office. Respondents to the Survey rated the performance of the Audit Office against these two criteria well below the importance to the respondents. The evidence suggests that insufficient attention is given to matching the expertise of auditors with the subject matter of audits. Audit Office staff during interviews indicated that there is also an increasing reluctance to utilise specialists on performance audits, except in an advisory role only."

Indeed during staff interviews, fully documented on our files, we were advised by staff within the Performance Audit Branch that they were placed on performance audit assignments based on 'next cab off the rank'.

THE USE OF EXPERTS IN PERFORMANCE AUDITS

Acumen states (text preceding Recommendation 14, Term of Reference PA1) "there is also an increasing reluctance to utilise experts on performance audits, except in an advisory role only".

No evidence is given to support this statement, other than Acumen's discussion with "staff". No attempt was made to verify this with senior staff of the Performance Audit Branch who would have refuted the statement.

The statement also demonstrates a lack of understanding as to what a performance audit is about.

Performance audits assess an agency's activities against some standard. That standard may represent best practice, the performance levels of similar operators or the agency's own policies and targets. Specialist technical advice and assistance is obtained on audits as, and when, required. But the purpose of performance audits is not to undertake a technical appraisal.

ACUMEN ALLIANCE RESPONSE:

Our report clearly sets out that a review of the use of experts in dollar terms and our discussions with staff within the Performance Audit Branch clearly demonstrated that there was an increasing reluctance to use experts. Financial data from Audit Office financial systems provides compelling evidence that the use of experts is minimal. The Audit Office were unable, or chose not to, refute the veracity of their own financial information in relation the use of experts. This matter was discussed with the Audit Office during our exit interviews for this review and we therefore find it problematic that the Audit Office is now suggesting that Senior Staff could have refuted our argument.

Acumen Alliance, in line with Australian Auditing Standard (AUS 806), is of the view that a 'performance audit' means an audit of all or part of an entity's activities to assess economy and/or efficiency and/or effectiveness. These performance audits are directed to:

- (a) the adequacy of an internal control structure intended to safeguard assets and to ensure due regard to economy, efficiency and effectiveness;
- (b) the extent to which resources have been managed economically and efficiently; and
- (c) the extent to which activities have been effective.

It is unlikely in the majority of cases that a 'generalist' performance auditor would have the requisite skills needed to cover all aspects of a performance audit of a specialist area, i.e. bus maintenance, security systems, hospital waiting times and as such would need experts to supplement their 'generalist' teams.

16 The Audit Office of New South Wales -
Covering Letter of 12 September 2003



THE AUDIT OFFICE
OF NEW SOUTH WALES

CONTACT NAME RJ Sendt
TELEPHONE 9285.0101
OUR REFERENCE A1185
YOUR REFERENCE

Mr Matthew Brown MP
Chairman
Legislative Assembly Public Accounts Committee
Parliament House
Macquarie Street
SYDNEY 2000

12 September 2003

Dear Mr Brown

Triennial Review of the NSW Audit Office

This letter and its attachments form my response to the review of the Audit Office carried out by Acumen Alliance. Acumen was appointed in December 2002 by the then Public Accounts Committee to conduct the triennial review required by section 48A of the *Public Finance and Audit Act 1983*.

The Audit Office and I welcome these independent reviews of our activities. We strongly believe that we should be no less accountable than the agencies we audit. A properly conducted review should also help us improve our processes. In fact over recent years, three of my senior staff have conducted (individually or as part of a team) similar reviews of three other audit offices in Australasia.

This covering letter comments briefly on the report's key findings on my Office's two main roles - financial audits and performance audits. Attachment A contains more detailed comments on a number of issues I have with the report. Attachment B contains my responses to the report's 82 recommendations.

Financial Audit

The Acumen report generally supports the standard of our work on financial audits.

It acknowledges that our methodology complies with professional Auditing Standards and that our Audit Office Practice Manual provides comprehensive guidance on the framework and implementation of the financial audit role. It also acknowledges our introduction of a plain English Independent Audit Report and comments on our well-developed procedures in relation to the issue of qualified opinions and 'modified audit reports'.

The report has also made some suggestions for minor improvement that we mostly support and will implement.

Performance Audit

The Acumen report is very critical of the way we select topics for performance audit and conduct the audits. While we accept that we can always improve (and we do accept a number of the Acumen recommendations), we believe that many of the key criticisms are not soundly based.

Much of the criticism seems to reflect the views of staff in some of the agencies that we have audited, rather than reflecting an independent professional assessment. Agencies will generally feel more strongly about performance audits, relative to financial audits. Partly this is because the shortcomings identified in our performance audits often relate to the core services the agencies deliver to the public. Partly it is because performance audit findings often involve a degree of subjectivity. It is inevitable in these circumstances that there will be a degree of tension between us and the agencies we audit. However we believe that we manage this tension in an appropriate and professional way.

Acumen states (Executive Summary, 'Performance Audit' section) that "the [performance audit] program has not been as effective as intended in either promoting greater accountability or improving the performance of the NSW public sector".

Acumen does not provide any hard evidence to support this generalisation. Instead Acumen has relied on its discussions with a selection of agencies. From those discussions, it concludes that while chief executives officially indicate in writing their agreement to our findings and recommendations, they harbour dissatisfaction with the exercise.

There are three important aspects of this assertion that require comment.

Firstly (as discussed above), holding agencies publicly to account for their performance is not always comfortable or pleasant for the agency. But it is what Parliament and the community expect.

Secondly, agencies publicly accept the vast majority of our recommendations. Acumen argues that agencies do this to avoid a confrontation with the Audit Office. We find this difficult to accept. Our experience is that agencies are more than willing to reject any finding or proposal if they consider it to be ill-founded.

Thirdly, and most importantly, our regular follow-up audits show substantial implementation of our recommendations.

Acumen did not regard this evidence as compelling, preferring instead to rely upon uncorroborated oral statements.

The report also contains internal inconsistencies. A very serious example of this relates to the issue of whether the Audit Office or I have questioned the merits of government policy objectives. If we did this we would be breaching section 27B(6) of the Act.

The report finds ('Conclusion' under Terms of Reference PA(1)) that -

It is the opinion of Acumen Alliance that evidence exists to indicate that the Audit Office has at times 'strayed' into this arena ...

Yet on the final page of the main body of the Report, Acumen twice contradicts this earlier statement -

Our review of Performance Audits did not reveal any instances where reports had 'questioned the merits of policy objectives'.

and

Our reviews did not reveal any instances where the Auditor-General had commented on the 'merits of policy objectives'.

My concern is that a reader, seeing only the earlier statement, might well conclude that I had breached the Act. (For the record, I formally deny that I have done so.)

Despite raising this inconsistency with Acumen representatives a number of times (including in writing), Acumen has - for whatever reason - allowed it to remain. This is unprofessional, bordering on negligence.

Conclusion

The ultimate result of the review's shortcomings is that it will be difficult for the Public Accounts Committee and others to judge the Audit Office's performance. The shortcomings will also make it difficult for us to identify which elements of the Report deserve to be pursued.

While recognising that we can always improve, a more balanced view of our performance would have noted the growing recognition of our work. This recognition comes nationally and internationally, and from both the private and public sectors. Our recent Parliamentary Survey showed equally strong satisfaction with the way we conduct both our Performance Audit and Financial Audit functions.

Despite the report's shortcomings, we will act quickly to implement those recommendations we accept. We are committed to the concept of continuous improvement and believe that this is supported by the quality of the services we provide. We will keep the Committee advised of our progress and would be pleased to discuss any of the report's findings with the Committee.

Yours sincerely



R J Sendt
Auditor-General