

Forum of Commonwealth Agencies  
Seminar, Sydney, NSW

**The Australian National Audit  
Office's Program of National  
Audits**

23 August 2002

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# The Australian National Audit Office's Program of National Audits

## INTRODUCTION

I welcome the opportunity to talk to you as Regional Heads of agencies in NSW about the Australian National Audit Office's (ANAO's) program of national audits. Many of you will be aware of a number of aspects that I will address today, by virtue of your contact with the ANAO's planning and conduct of audits. Often the usefulness of a talk such as this lies in bringing these aspects together in order to appreciate the broader picture and explain the thinking and intentions behind it.

For the ANAO, a key issue is getting the balance right between control and innovation<sup>1</sup> in order to provide the guidance and the leadership demanded by a rapidly changing world virtually shrunk by modern communications and transport. The aim is to get the right mix of products and services by recruiting and retaining highly achieving staff to anticipate and plan for the challenges of the future. In setting its agenda for the future, the ANAO relies on intelligence garnered through the review and analysis of some 300 Commonwealth entities as well as ongoing feedback and guidance from the Parliament and other audit clients as to the areas they see as adding most value to public administration.

My talk will cover three broad areas:

- the ANAO's approach to auditing;
- integrated planning; and
- review of our performance.

## 1. APPROACH TO AUDITING

Our vision – We want to be recognised for excellence in the provision of independent public sector audit and related services.

The ANAO independently reviews public sector performance and accountability regimes and aims to add value to public sector performance. We aim to do this by delivering:

- independent assessment of the performance of selected Commonwealth public sector activities including the scope for improving efficiency and administrative effectiveness (improvement in public administration); and
- independent assurance of Commonwealth public sector reporting, administration, control and accountability (assurance).

To understand the ANAO's approach to auditing requires an appreciation of the wider environment within which it operates. The first part of this paper identifies the principal aspects of this environment that influence the planning and conduct of audits, namely:

- auditor independence;
- focus on relationships;
- audit committees;
- the ANAO's outcomes/outputs framework;
- range of products; and
- outline of products coverage.

## **Independence**

The *Auditor-General Act 1997* (the Act) provides a robust legislative framework for the Commonwealth Auditor-General and the ANAO to provide support to Parliament. The Act establishes the Auditor-General as an '*independent officer of the Parliament*' – a title that symbolises the Auditor-General's unique relationship with the Parliament. The Act is based on the important notion of audit independence. It has generally been recognised as better practice audit legislation. Consequently, while the ANAO is part of the changed contemporary auditing landscape currently challenging both public and private sector auditors, we are also set apart from it due to our clear statutory independence. This is one of our major strengths, which enhances our reputation and effectiveness. The Act also outlines the mandate and powers of the Auditor-General and the functions of the ANAO, as the external auditor of Commonwealth public sector entities.

Corresponding with public sector changes, the role of the Auditor-General and the place of auditing in democratic government have also changed. While the accountability imperative remains constant, the role of the ANAO has evolved to take account of, and respond positively to, the public sector reform agenda. In today's environment, our role includes providing independent assurance on the performance, as well as the accountability, of the public sector in delivering the government's programs and services and implementing effectively a wide range of public sector reforms. As the public and private sectors converge; as the business environment becomes inherently riskier; and as concerns for public accountability heighten; it is vital that Auditors-General have all the professional and functional freedom required to fulfil, fearlessly and independently, the role demanded of them by Parliament.

The debate over audit independence is not new, although it has attained an increased popular profile in the wake of the collapse of Enron and WorldCom in the United States, and OneTel, Ansett and HIH in Australia. Audit bodies and the accounting profession worldwide have been actively engaged in clarifying and reinforcing independence for many years. However, recent events have put the debate on to a different plane with higher level expectations being generated. While the ANAO takes

a professional interest in this ongoing debate, it is also set apart from it by virtue of its statutory and functional independence. Nevertheless, there is also an operational imperative with the ANAO outsourcing a not insignificant proportion of its audit work to private sector accounting firms. As well, with the increasing use of such firms by the public sector for internal audit, we are often dependent on their work in coming to an audit opinion on organisations' control environments and financial statements.

## **Focus on relationships**

A responsive relationship with the Parliament and the Australian Public Service (APS) is integral to the ANAO's ability to continue to deliver products that add value in the contemporary public sector environment. The notion of getting the 'right mix' to provide adequate assurance and suggest improvements in administration highlights the symbiotic nature of our relationship with the Parliament and the APS. The success of the relationship depends on its ability to support, and reinforce, frank and open dialogue on trends challenging public sector accountability in the Commonwealth context.

As Dr Allan Hawke, Secretary, Department of Defence, recently noted:

*each and every interaction – whether that be in person, by letter, e-mail or whatever – is what Jan Carlsson called a Moment of Truth. It is in those moments that relationships are further cemented or damaged. It takes considerable time and effort to establish trust and a nanosecond's careless remark to destroy it.<sup>2</sup>*

### ***Relationship with the Parliament***

The ANAO regards its primary client as the Parliament. Indeed, it could be argued that, given our proximity to the day-to-day operations of the APS, we are Parliament's 'eyes and ears' on Commonwealth administration. We take this responsibility seriously, as the support of the Parliament for the work of the ANAO is vital to its success. The ANAO could not continue to be relevant without Parliament supporting our annual work program, our audit recommendations, and assisting us in determining appropriate accountability standards for the APS.

Relationship management is important to us. Indeed, such is the strategic importance of meeting our clients' needs, it comprises the first of our four key results areas. Our objective is to satisfy the needs and expectations of the Parliament, the Executive Government and our audit clients in relation to performance assurance and accountability. We aim to do this by, among other things, enhancing our dialogue and relationship with all members of Parliament, particularly the Joint Committee of Public Accounts and Audit (JCPAA) and other Parliamentary Committees, so that they are well informed about our activities and so that we, in turn, can provide them with timely and constructive information and assistance.

As part of its regular business, the ANAO provides briefings to Ministers, Shadow Ministers, Parliamentary Committees and their staff on audit reports tabled in the Parliament. ANAO officers also liaise closely with Committees, with staff often

being seconded to assist Committees on more complex matters and their inquiries. Senior executives at the ANAO have individual targets for Parliamentary liaison, and the Office as a whole has performance targets linked to the satisfaction of Parliament. For example, each year we aim to have JCPAA support for all of our reports tabled in Parliament. In particular, we aim to have at least 95 per cent of our audit recommendations supported by the JCPAA and other Parliamentary Committees.

### *Relationship with APS Agencies*

It is vital that the ANAO continues to be an active participant in the public sector's negotiation of the changed governance environment. While, in the past, the ANAO's prime focus may have been on ensuring compliance with legislation, this has now been subsumed as part of a broader approach to assist agencies in improving public sector administration. To be successful, this approach requires considerable cooperation between the ANAO and agencies.

Our relationships are managed responsively and there is no single formula for success. The ANAO's clients are extremely varied. This necessitates tailored approaches to our audit strategies. Audit bodies can no longer afford to take the traditional 'big stick' approach, although the need for powerful independent review bodies supported by robust legislation should also not be understated in the current climate. However, the ANAO emphasises the importance of building strong relationships with agencies and other stakeholders to foster a culture of accountability in preference to imposition of a more prescriptive approach. We aim to focus more on outcomes and results to provide products and services that suit the needs of both the audited agencies and the Parliament.

We encourage agencies to make early contact where they are faced with new or difficult administrative issues. Our experience across a range of issues both in Australia and overseas allows us to assist agencies in understanding the opportunities and risks inherent in diverse management approaches. We do limited basic research but we observe, learn and disseminate intelligence gained from our audit activity. We are always mindful, however, of the need to maintain our independence whilst assisting agencies at the 'front end'. It is for public sector managers to make their own decisions on whether or not to accept ANAO advice based on the particular risks and opportunities identified in their own business environments.

It is crucial that we work cooperatively with agencies at all stages of the audit process to gain genuine acceptance of our recommendations. This is essential if we are to add value and maintain our credibility. Our preferred approach is to give agencies encouragement to get their own house in order and achieve required results. We acknowledge and reinforce any such action taken in the course of audits. We endeavour to meet formally and informally with agency top management throughout the year. In particular, we promote their interest and involvement at the start of each audit and in our planning processes, notably in our audit strategy statements for individual agencies and in our Audit Work Program (AWP).

Finally, we aim to meet our clients' needs by periodically reviewing the relevance and mix of our products and services, striving for innovative approaches, and improving our quality and effectiveness. The above initiatives are aimed at securing the

engagement and commitment of all stakeholders to our work. In that sense, we aim to be catalysts for better results. In many cases, we disseminate better practice identified from our audits, not in the sense of ‘one size fits all’, but to open minds to other possibilities involving different approaches and/or adaptation to the specific requirements of particular agencies.

## **Audit Committees**

Each agency is required to have an audit committee that fulfils section 46 of the *Financial Management and Accountability Act 1997* (FMA Act). Section 32 of the *Commonwealth Authorities and Companies Act 1997* (CAC Act)<sup>3</sup> also requires the establishment of an audit committee. The ANAO Better Practice Guide on ‘Audit Committees’ issued in July 1997 states that ‘*an effective committee has the potential to strengthen the control environment (of which it is a part) and assist the governing body fulfil its stewardship, leadership and control responsibilities*’.<sup>4</sup>

ANAO audit managers and senior executives are invited to attend audit committee meetings within those agencies for which they are responsible. This is an important medium for the exchange of information and ideas, and assists us in fine-tuning our work over time. Participation with agencies in their audit committees:

- facilitates the implementation of audit (both internal and external) recommendations;
- assists relationship building on both formal and informal levels;
- helps the ANAO understand the organisation’s business;
- provides a forum to discuss possible and future audits, before, during and after the formal AWP process; and
- facilitates feedback on past audits and future joint directions.

Audit committees provide a complementary vehicle for implementing relevant control systems incorporating sound risk management plans. This view is shared by the private sector, where effective audit committees and risk management plans are an indication of best practice and markedly improve company performance, including decision-making. The internal auditing function of an organisation plays an important role in this respect by examining and reporting on control structures and risk exposures and the agency’s risk management efforts to the agency governance team.

An effective audit committee can improve communication and coordination between management and internal as well as external audit, and strengthen internal control frameworks and structures to assist Chief Executive Officers (CEOs) and boards meet their statutory and fiduciary duties. The committee’s strength is its demonstrated independence and power to seek explanations and information, as well as its understanding of the various accountability relationships and their impact, particularly on financial performance. Both internal and external audit have an important part to play in assisting the committee to be effective in this goal. In turn, the committee

plays a significant role in ensuring the effectiveness of the various audit processes and operations, including the implementation of audit recommendations.

A recent Canadian publication <sup>5</sup> states that, for audit committees, there are three key outcomes that need to be achieved and, additionally, the committee mandate should explicitly recognise them. These outcomes are as follows:

- The audit committee needs to assure itself that the auditors are independent. It must have access to all information about the audit firm's relationship with the corporation that is necessary in order to come to a reasonable conclusion.
- The audit committee needs to assure itself that the external auditors are satisfied that the accounting estimates and judgements made by management, and management's selection of accounting principles, reflect an appropriate application of Generally Accepted Accounting Principles (GAAP).
- The audit committee must develop a relationship with the external auditors that allows for full, frank and timely discussion of all material issues, with or without management as appropriate in the circumstances.<sup>6</sup>

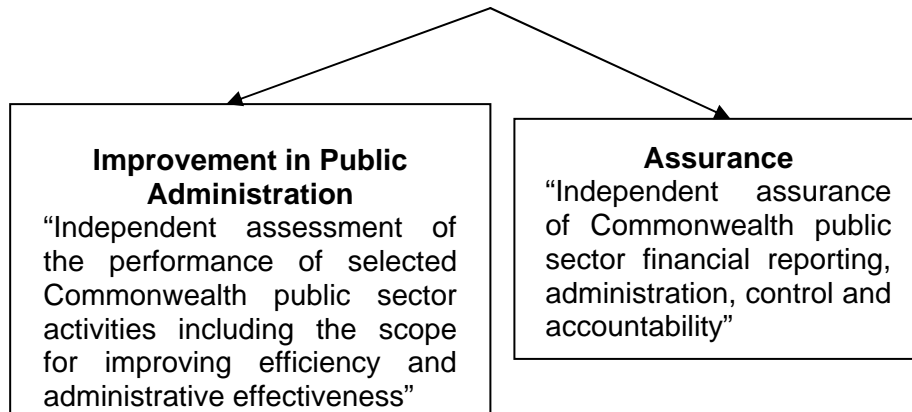
The ANAO will continue to be involved with agencies in their audit committees to strengthen our relationships with them and to assist agencies with the difficult task of maintaining strong and independent audit committees.

## **Outcomes/outputs of ANAO**

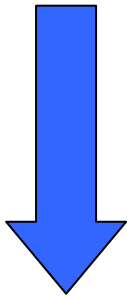
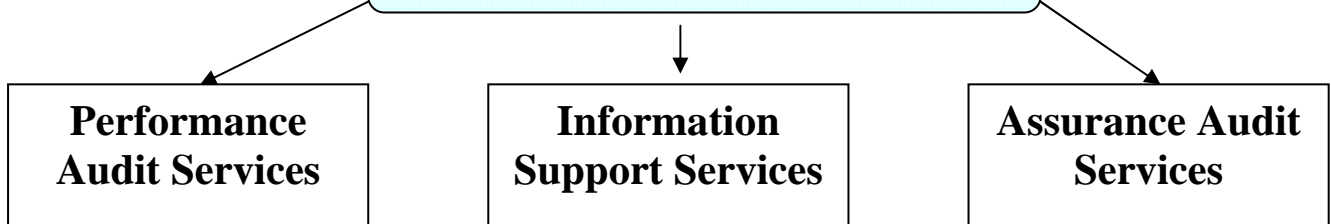
As mentioned above, the *Auditor-General Act 1997* establishes the mandate of the Auditor-General to undertake audits in public sector bodies. The Auditor-General's mandate extends to some 300 public sector bodies. The *Auditor-General Act 1997*, the *Financial Management and Accountability Act 1997* (FMA Act) and the *Commonwealth Authorities and Companies Act 1997* (CAC Act) provide authority to undertake financial statement audit and related services. The *Auditor-General Act 1997* provides the authority to undertake performance audits and to provide other information support services, including development of better practice guides and benchmarking services.

The above mandate underpins the ANAO's outcomes and outputs/products, which are set out below:

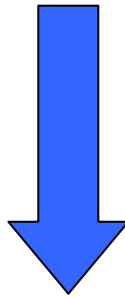
## ANAO OUTCOMES



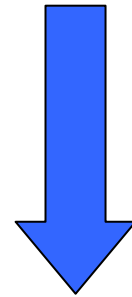
## ANAO OUTPUT GROUPS



- Performance Audit Reports
- Other audit and related products



- Assistance to the Parliament
- Client seminars
- National and international representation
- Benchmarking reports
- Better practice guides



- Financial statement audit reports
- Other assurance reports
- Business support process audit reports
- Protective security audit reports



## Range of products

In order to meet our clients' changing needs, the ANAO has moved towards a more strategic, risk-based audit approach. Our goal is to add value through audit products that are state of the art. We encourage innovation within a clearly defined auditing standards framework. The ANAO is committed to working closely with our national and international colleagues to ensure that we remain at the leading edge and that we have the 'right mix' of assurance, compliance, accountability, and performance products at any point in time and over time.

ANAO audit products run the continuum from high-level performance audits that may target particular issues across the APS, to the traditional financial statement and financial control and administration products that provide assurance as to the stewardship of public funds in individual agencies. In addition, the ANAO disseminates better practice through a series of Better Practice Guides, generally arising out of performance audits, in particular Business Support Process Audit reports, on a range of issues challenging the contemporary APS. The reports are evidentially based and authoritative. Our annual audit of the Consolidated Financial Statements and our assessment of agency control structures, for example, provide a unique overview as to the ongoing financial performance of some 300 Commonwealth entities.

In addition to leveraging off our Australian and international colleagues, the ANAO is committed to an integrated auditing framework that draws on the strengths of each side of our business; that is, financial (assurance) and performance audits. These audits are tailored to the assessed situation (needs) of public sector organisations. The approach capitalises on intelligence gathered in each field and allows us to target areas for audit activity that add most value. In addition, it allows us to assess the value of our products over time, and to fine-tune our outputs. Our objective is to deliver high quality audit products that maintain and improve the high standards and professionalism of our audit and related services.

## Outline of products

### *Performance Audits*

The ANAO produces performance audit reports, better practice guides, and other audit and related products. The *Auditor-General Act 1997* allows the Auditor-General to conduct a performance audit of an agency, a Commonwealth authority or company (other than a GBE or any of its subsidiaries). The Act defines a performance audit as a '*review or examination of any aspect of the operations of a body or person*'. The Explanatory Memorandum to the Bill expands on the definition by saying 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.*<sup>7</sup>

The ANAO has an annual target of 50 performance audit products, and produced 57 such reports during the 2001-02 financial year. Overall, with assurance audits, the Office tabled a record 67 audit reports in the Parliament in that year.

In accordance with accepted auditing practice, performance audits are an independent, objective and systematic examination of the operations of a body for the purposes of forming an opinion on whether:

- the operations have been managed in an economical, efficient and effective manner;
- internal procedures for promoting and monitoring economy, efficiency and effectiveness are adequate; and
- improvements might be made to management practices (including procedures for promoting and monitoring performance).

ANAO performance audit reports are tabled in the Parliament. Typically, performance audits examine the use of resources, information systems, performance measures, monitoring systems and legal compliance. In seeking to improve administration, performance audits often identify exemplary practices in both the public and the private sector, which are then incorporated into better practice guides for dissemination throughout the APS, as I indicated earlier.

Performance audits are conducted in all ministerial portfolios with the main concentration being directed to portfolios with significant government outlays or revenues. Because of the size, complexity and diversity of most Commonwealth entities, a performance audit usually examines selected segments of their operations. Normally this sample enables the auditors to form an opinion on the administration of those operations. General performance audits address the same issue or activity in a number of entities and may have application across the Commonwealth public sector. Audit topics are selected on two grounds:

- activities where an audit can be expected to add the greatest value in improved accountability, economy, efficiency and administrative effectiveness; and
- to ensure appropriate coverage of entity operations within available audit resources.

### *Cross portfolio audits*

The ANAO is uniquely placed to provide an analysis of performance across the APS. This is important as agencies increasingly find new methods to deal with common issues, and form alliances and partnerships, including with the private sector, to deliver government services. In considering the future of the APS, the Prime Minister has indicated that:

*Whole of government approaches, collectively owned by several Ministers, will increasingly become a common response.*<sup>8</sup>

Recent years have seen an increase in the number of ‘across the board’ and cross-portfolio audits undertaken that compare experiences in a range of agencies. For example, the ANAO has recently undertaken cross portfolio analysis of, among other things, internet security, the management of bank accounts, and performance information in Portfolio Budget Statements. Our ability to compare operations across the public sector, and sometimes the private sector, as well as our statutory independence, are significant strengths and add value to a wide range of stakeholders.

## *Promoting Better Practice*

### *Better Practice Guides*

In terms of getting the ‘right mix’ for the contemporary environment, my Office has fine-tuned its focus on products that add value by bringing together lessons learnt across the public sector. In particular, our Better Practice Guides (BPGs) have been well received by program managers interested in learning from the experiences of others. BPGs serve a dual purpose:

- they provide a unique analysis of approaches and trends affecting the public service as a whole; and
- they provide a very valuable source of audit criteria for future work in related fields.

BPGs aim to improve public administration by ensuring that better practices employed in individual organisations in Australia and overseas are promulgated to the whole of the public sector.

Depending on the subject and nature of information collected during an audit, BPGs are often produced in conjunction with a performance audit. Alternatively, a BPG might be prepared as a result of a perceived need to provide guidance material in a particular area of public administration. Recent BPGs produced cover a wide range of topics including: grant administration; contract management; planning for the workforce of the future; internet delivery decision-making; life cycle costing; rehabilitation issues; developing policy advice; and financial reporting (*AMODEL* accounts).

### *AMODEL Accounts*

*AMODEL* accounts are a set of two BPGs that are in their eighth year of production. These BPGs have been prepared to assist Commonwealth agencies and authorities in the preparation of their financial statements.

*AMODEL Agency* is produced for all agencies that are administered under the FMA Act. *AMODEL Non-Commercial Authority* is produced for Commonwealth authorities that are administered under the CAC Act. The Guides provide examples of better practice in Commonwealth public sector financial reporting and disclosure. The *AMODEL* BPGs are a very useful product for authorities and agencies, and are used extensively in the APS for the preparation of financial statements.

### *Benchmarking Studies*

Benchmarking is a widely accepted approach for achieving business performance improvements. Our benchmarking services have initially comprised functional reviews of the major corporate support areas. The overall results of these reviews are published generically and tabled in the Parliament. At the audit client level, a customised report is provided to all entities participating in the study. Our most recent Benchmarking study examined the management of the human resource function in 14 agencies<sup>9</sup>.

### *Assurance Audits*

Through the conduct of financial statement audits, business support process audits, protective security audits and other services associated with the conduct of financial statement audits, the ANAO provides assurance to individual entities, Ministers and the Parliament about the financial administration and accountability of public sector entities.

### *Financial Statement Audits*

The Auditor-General conducts financial statement audits to express an opinion on whether financial statements of Commonwealth Government entities have been prepared in accordance with the Government's reporting framework and Australian Accounting Standards. In addition to the audit opinion, the ANAO provides each entity with a report that deals with the results of the financial audit process. A report on the outcome of the financial audit process is also provided to the responsible Minister for each entity and a report summarising the results is provided to Parliament. In addition, the ANAO now provides a report to Parliament detailing the results of an assessment of the control structure of each entity, as noted earlier.

### *Business Support Process Audits*

Business Support Process (BSP) Audits examine business processes that support the delivery of outputs provided by public sector agencies. The focus of BSP audit reports is:

- the effectiveness of the accountability mechanisms operating within public sector entities;
- the efficacy of the design and implementation of internal controls;
- the components of the control structure, including:
  - a) risk management;
  - b) the control environment;
  - c) specific control measures;
  - d) monitoring and review processes;
  - e) management information systems;
  - f) communication processes; and

- the extent of legal compliance; and of compliance with internal and external policies and procedures.

The audits are normally conducted in a number of organisations. Although the audit findings are usually reported to Parliament in generic terms without attribution to particular organisations, the organisations subject to audit are separately identified. In addition, individual reports are provided to client organisations. Output from these audits also includes the development of better practice guides.

### *Protective Security Audits*

Protective Security audits are conducted at a range of organisations, similar to the approach taken for the BSP audits. Protective Security audits examine three key aspects of security, namely, information security, personnel security and physical security. A Protective Security audit of Physical Security is currently under way and is due to be tabled in Spring 2002.

## **2. INTEGRATED PLANNING**

The requirements of providing assurance and assessing performance and the need to address any expectation gaps in the audit process are met at two levels with a focussed and integrated approach to audit selection – reflecting both the emerging environment and the circumstances of individual agencies.

At the broader public sector level, the ANAO ensures that its product mix and coverage are tailored to the environment in which it operates and to the accountability needs of our principal client, the Parliament. As the environment changes, so do the associated accountability arrangements. We have to regularly ask ourselves ‘have we got the balance right?’ As well we also need to ensure the expectation of an audit presence across the public sector within a reasonable timeframe.

The second level of the ANAO’s integrated approach applies to individual agencies or entities where we aim to ensure that our audit services assist public sector organisations to improve their performance and accountability, as well as to better manage their functions and/or business. In developing an audit strategy for a particular agency or entity the ANAO looks at the perceived relative strengths and weaknesses of the organisation in terms of its performance and accountability, and to take into account any complementary internal or external reviews, investigations and evaluations. The objective here is to minimise any unnecessary overlap and duplication of such activity and its impact on the organisations concerned.

The ANAO’s range of audit products, particularly performance and financial statement audits, aims to provide assurance that the risks facing the APS and good management of its finances and programs are being adequately addressed through a holistic and integrated audit approach addressing the observed circumstances of each agency and public sector body. In response to the increasing focus on agency performance and results within the Commonwealth outcomes and outputs framework and the need to provide assurance to the Parliament, including on the ‘health’ of public sector agencies, the ANAO aims for comprehensive performance audit coverage over time.

To maximise our efforts and the value added to public sector administration by the ANAO with finite resources, we are conducting more 'Across the Board' or 'Cross Portfolio' audits. These audits provide an analysis of performance across the Commonwealth public sector. In getting the 'right mix', my Office has focussed on products that add value by bringing together lessons learnt across the public sector. The ability to leverage off these multi-agency audits is providing a significant return for the audit effort involved.

This part of my talk highlights the key inputs in the development of the ANAO's annual Audit Work Program (AWP).

## **Audit themes**

Each year, the Audit Work Program is developed collaboratively between assurance and performance auditors at the ANAO. The program is developed against the background of the APS environment, including the business risks that are likely to impact on the APS during the period under review. These risks are taken into account in identifying themes to be addressed in the annual performance audit program and in evaluating and assessing potential financial statement issues to be addressed during financial statement audits.

In planning our performance audit coverage, we also have regard to the need to:

- provide the Parliament with an assurance, over time, of the full range of performance of public sector agencies;
- respond to emerging issues of interest to the Parliament; and
- add value to public administration.

For the current financial year consideration of these emerging issues together with the previously mentioned business risks lead to the following themes being identified as part of the strategic planning process:

- Human Resource Management including Workforce Planning;
- Financial Management and Reporting;
- Performance Management and Measurement;
- Procurement and Contract Management;
- Application of Information Technology & Resources; and
- Service Delivery.

## **Audit selection**

There is obviously little discretion about the financial statement audits the ANAO conducts. In addition to the APS wide issues, factors affecting the performance audits we conduct in individual agencies include:

- the structure of governance and accountability in the agency;
- the extent of public/private interface in service delivery;
- the involvement of private sector contractors and the extent to which they are subject to Commonwealth legislation, including the Public Service Act, Freedom of Information Act, and the financial management legislation and associated required level of accountability; and
- extent of recent audit coverage, including internal and other external reviews of agency operations.

Our knowledge of these factors, together with identification of business risks, is part of gaining an understanding of the business of the agency.

Potential audit topics for each agency are identified and ranked against criteria such as:

- estimated audit impact, including financial benefits;
- risks to good management;
- significance of the program/process;
- visibility of the program (national importance or political sensitivity);
- financial materiality; and
- extent of recent audit coverage, including internal and external review.

Of major importance in the selection of audit topics is the added value expected from the audit. This focus on outcomes guides audit teams through all stages of the audit, from the initial identification of potential topics to the reporting of findings and recommendations to the Parliament. A preliminary estimate of the audit's benefits is made, where possible, during strategic planning. Expected benefits can take many forms. Audits that realise financial benefits are highly regarded by Parliament. However, the audit process is more pervasive. Nevertheless, one of the ANAO key performance indicators addresses financial benefits/savings from audits compared against the cost of the performance audit program.

An important input to the planning process is the assessment of risks to good performance in the agency. An agency output or activity that is more complex to

manage and operates in an uncertain environment could be expected to represent a greater risk to the organization. Indicators of high complexity and uncertainty include government policy changes, highly decentralised operations with devolved management decision-making responsibilities, restructuring of operations, time critical issues of operations and a multiplicity of interested parties.

The significance of an audit topic has regard to the magnitude of its organisational impacts. It will depend on whether the activity is comparatively minor or whether shortcomings in the area concerned could flow on to other activities within the entity. For example, a small organisational unit with low materiality may be responsible for decisions with long-lasting strategic and operational impacts on the organization, its costs and effectiveness. Similarly, weaknesses in a particular system may have widespread effects, while another may be comparatively self-contained and therefore limited in its impact on the systems and activities of the organisation.

Visibility is similar to significance but is more concerned with the external impact of the program. It is related to the social and environmental aspects of the activity and the importance of its operations to the Parliament and the public. Some weight is attached to the impact of an error or irregularity on public accountability. It would also have regard to the degree of parliamentary and public interest in the outcome of the audit

## **Resourcing the audit work program**

The ANAO's financial and performance audit work program is developed within the context of our budget. The Auditor-General's mandate extends to some 300 public sector bodies, including approximately 290 financial statement audits expected to be completed this year. As mentioned earlier, there is little discretion about financial statement audits. In planning to complete these audits and the annual target of 50 performance audit reports, resource estimates for audits in the work program are compared to forecast staffing available to conduct the audits. ANAO capacity is supplemented as necessary by contracting in private sector resources. For financial statement audits contracting in is used at times of peak workloads. The use of contractors on performance audits addresses staff shortages from time to time, including to ensure larger audits are completed in an appropriate timeframe.

We also use the private sector for strategic advantage; including in situations where we require specialist and other skills and because of the location of our audit clients where it is more cost effective to employ locally-based auditors for particular periods of the year. In some cases a financial statement audit is outsourced to a private sector firm with expertise in auditing organisations in a particular industry. While the audit firm conducts the audit, the Auditor-General is responsible for issuing the audit opinion and the ANAO controls the audit, including a review of the work of the audit firm.

## **Consultation**

The ANAO builds regular and ongoing liaison into its annual schedule of activities. As discussed above, annual themes are used in selecting topics to ensure that the audit program is targeted appropriately to add value to public administration. An integral



part of this planning process is the early engagement of stakeholders including agency heads and the Parliament, through the JCPAA, to ensure that the work program is optimally targeted.

### *Agencies*

As discussed earlier in this paper, audit committees play an essential role in fostering both formal and informal communication between agencies and the ANAO. In the very early phases of the formation of the draft AWP, discussions are held to introduce the themes of the AWP for the upcoming financial year. The ‘no surprises’ policy is upheld during meetings throughout the year between agency and ANAO SES Officers.

Agency Heads are sent sections of the draft AWP that are relevant to their portfolio (including cross-agency audits) and are invited to provide comments/suggestions on the ANAO’s proposed audit program. While the final AWP is determined by the Auditor-General, an AWP that does not take account of agency feedback potentially reduces opportunities to add value to the APS during the coming year.

### *JCPAA/Parliament*

Section 10 of the *Auditor-General Act 1997* requires the Auditor-General to have regard to the audit priorities of the Parliament determined by the Joint Committee of Public Accounts and Audit (JCPAA). As such, the JCPAA is the key conduit for ongoing Parliamentary input to our work, including responsibility for bringing together issues of Parliamentary interest for consideration in the ANAO’s planning processes.

Earlier I commented on the value the ANAO places on a good working relationship with the Parliament, particularly the JCPAA. This relationship facilitates an effective exchange between the JCPAA, on behalf of Parliament, and the ANAO regarding the issues or areas of the APS that the Parliament would like to see included in the ANAO’s audit work program for the coming year.

## **Keeping Parliament and the APS informed**

The ANAO aims to keep Parliament and the APS up to date on its ongoing audit activity – from the audit work program planning process right through to assistance to Committees of Inquiry reviewing ANAO reports. Some of our ‘global’ reporting initiatives are discussed later. As well as working with Parliament and agencies on specific issues under review, we aim to be accessible to all stakeholders through a variety of forums.

The ANAO website ([www.anao.gov.au](http://www.anao.gov.au)) has recently been enhanced to provide improved functionality and content. The website has links to all of our publications including audit reports, better practice guides and speeches. It includes a list of audits in progress, a tabling schedule, information on tenders and contracts, recruitment details, and links to our national and international colleagues. The website

incorporates information on relevant contacts for each of the ANAO's business units, and a request form for further information.

## **Audits by request**

Recent years have seen an increasing tendency for direct requests to be made by Ministers for audits of particular programs or issues. While this represents a useful measure of our ongoing relevance and credibility, it also has the potential to challenge the issue of the Auditor-General's independence. The Office must ensure that, where direct requests for audits are accepted, such audits are in the public interest. Direct requests for audits are also considered in light of the planned audit work program and potential resource implications.

Recent examples of requested audits are:

- Report No.50 2001-2002 *A Preliminary Examination into the Allocation of Grant Funding for the Co-Location of National General Practice Organisations*<sup>10</sup>; and
- Report No.40 2001-2002 *Corporate Governance in the Australian Broadcasting Authority*<sup>11</sup>.

Report No.50 was requested by both the Shadow Minister for Health and Ageing, and the Federal President of the Australian Medical Association, requesting a comprehensive audit of funding decisions by the Minister for Health and Ageing. Report No.40 was undertaken following a request from the JCPAA seeking assurance that ABC programming adequately reflected the ABC's Charter.

## **Making audit recommendations effective**

It is important that agencies see the ANAO as engaging in a partnership that will help them achieve better practice in the area of public administration for which they are responsible. My staff work hard to ensure that agencies are fully informed about, and understand each stage of, a performance audit, that is from the first contact to the final report. In essence there should not be any surprises. This approach helps ensure the audit recommendations are practical and therefore capable of implementation and also have a degree of acceptance from the agency concerned. The process also helps our auditees understand the reasoning behind any adverse recommendations.

One way to judge whether performance audits add value to public administration and accountability is the level of acceptance of the audit recommendations. A performance audit is regarded as a success when the majority of recommendations are accepted and implemented by the agency. A useful benchmark is that 90 per cent of the ANAO's recommendations are accepted. We have been able to achieve this goal since the mid-1990s.

It is finding this balance between independent assurance to Parliament, and genuinely improving public administration that is the key for effective audit recommendations. As each audit is different in many ways, a case-by-case approach is best for determining this balance, but audit teams take account of the following:

- give credit for action taken;

- expect that some issues will be resolved through the process of the audit;
- have reasonable expectations of the agency's resource capability to implement the recommendations; and
- identify and prioritise the recommendations and other suggestions made for improvement.

Planning of audit coverage in individual agencies includes consideration of an agency's progress in implementing recommendations from previous audits. As previously indicated, the ANAO works closely with audit committees of public sector organisations to monitor the implementation of its recommendations. However, the most effective action is the JCPAA's quarterly public hearings on selected audit reports and any JCPAA inquiry conducted as a result of these reports. It is in the interests of agency senior management to not only agree to take corrective action, but to follow through and implement such action. While agencies do not know which audits the JCPAA will review in a public hearing, they can be assured that audits involving any disagreement with audit recommendations or indicating any reluctance to implement corrective action, will attract the JCPAA's attention.

The ANAO also conducts its own follow-up audits to monitor the implementation of recommendations, as well as to report on any other emerging issues that may be of interest to Parliament. It is important to us that our recommendations are both accepted and implemented, and that Parliament and agencies consider that our audit activity adds value to public sector administration.

## **Triple bottom line reporting (TBL)**

One issue currently challenging public sector auditors and our clients that I would like to draw to your attention is that of triple bottom line reporting. Triple bottom line reporting incorporates economic, social and environmental performance considerations. Key issues are the disclosure of true costs using full cost accounting methodologies, as well as sustainability accounting, auditing and reporting. Generally this is likely to be an area of increasing interest in terms of better practice and cost effective methodologies. These matters still have some way to go before the methodologies are sufficiently robust and broadly comparable across all sectors, but already there are some positive examples from the private sector that illustrate what can be achieved<sup>12</sup>. Significantly, the Victorian Public Accounts and Estimates Committee has recently announced its intention to work with the Commonwealth in pursuing an Australian Environmental Accounting Standard<sup>13</sup>.

The definition of the 'triple bottom line' has recently been expanded to include not only economic, social and environmental concerns, but also governance issues. The phrase 'quadruple bottom line' has now entered the professional lexicon. The trend to quadruple bottom line reporting is currently moving fastest in the United States, particularly in the wake of major company collapses which have turned the spotlight on governance and social responsibility.<sup>14</sup>

Public sector agencies have the responsibility to ensure that their operations meet the highest standards expected by the community. The introduction of public reporting on Ecologically Sustainable Development (ESD) is now a requirement in Commonwealth agency annual reports and the ANAO will be conducting an audit in this area later this year. This parallels the requirement for company directors to report whether their performance had environmental significance under the Commonwealth Corporations Law. This has been complex for companies as, at present, Australia does not have an accounting standard for dealing directly and fully with environmental issues<sup>15</sup>.

In the United Kingdom, where reporting on TBL is currently voluntary, 103 of the country's largest 250 FTSE listed companies reported on environment and social performance during 2001-02<sup>16</sup>. The quality of the reports varied, with only 36 of the 250 being independently verified<sup>17</sup>. The need for continuous improvement and independent verification of such reports is an issue that will continue to challenge both public and private sector auditors into the future.

The ANAO is participating in a Commonwealth Group being led by the Department of Family and Community Services, which is facilitating the development of a core set of social indicators which will contribute to a robust TBL reporting framework. This development is complementing a similar process for environmental indicators being undertaken by Environment Australia. Recently, it was reported that the Sustainable Investment Research Institute has received \$55 000 from the Federal Government to develop a "Sustainability Reporter" tool to rate the Australian Stock Exchange's largest 300 companies on their environmental and social performance.<sup>18</sup>

The public reputation of agencies is very important and this is made more complex as expectations change over time. Nevertheless, it is important that public sector agencies see themselves as part of the broader social system in which they operate. Client focus and the adequacy of stakeholder consultation is very important within this context. Triple (or Quadruple) Bottom Line reporting is clearly a 'greenfield' area for research and development as far as audit is concerned. In addition, the trans-border and global issues inherent in this form of reporting suggest that the development of appropriate methodologies and indicators would benefit enormously from international input. The ANAO actively participates in international environmental auditing networks to this effect.

### **3. REVIEW OF PERFORMANCE**

#### **Annual report**

The ANAO's annual report is the most public and comprehensive mechanism for demonstrating accountability to the Parliament. We aim to include an analysis of our achievements to date, as well as challenges outstanding for the future. In this way, we provide Parliament with a comprehensive overview of our performance over the preceding financial year and an indication of areas of interest for the future.

The Annual Report includes an assessment of the Office's achievements against its annual scorecard. The scorecard incorporates the ANAO performance indicators set

out in its Portfolio Budget Statements. Performance measures relate to three Output groups: performance audit services, information support services and assurance audit services. These link back to the ANAO's twin Outcomes: improvement in public administration and assurance. The scorecard includes both quantitative and qualitative measures and is intended to provide interested parties with an understanding of the link between the ANAO's products and their resulting impacts. It is then possible to assess how cost-effectively the ANAO is delivering its products and to what extent the ANAO is achieving its agreed outcomes. This provides Parliament with assurance that we have appropriate systems in place to produce reliable reports.

Each year, our Annual Report also includes results of quality assurance processes including peer review and benchmarking activities. It also includes commentary on the key strategic issues targeted by the ANAO for the next 12 months. This commentary, together with the publication of the results of our audits every six months in the activity reports, allows us to contribute to contemporary debate on a broad range of issues facing the APS. Importantly, it also provides a focus for ongoing discussion with the Parliament in relation to setting strategies for the future.

## **Audit activity reports**

As well as our Annual Report, we table two Audit Activity Reports each year in Parliament, which provide a summary of audit outcomes for the previous six months.<sup>19</sup> These reports summarise audit and other related ANAO activities for the six-month period. The purpose of these reports is to:

- inform the Parliament of the major issues the ANAO is examining in working with agencies to encourage, and provide assurance about, a better performing and more accountable public sector;
- provide the Parliament with a consolidated summary of the audit reports tabled, as well as details of better practice guides and other audit services provided in the period; and
- focus on, and highlight, some of the major lessons learned from the audit services provided by the ANAO.

## **Financial Statement Audit Reports**

The ANAO also provides two cross-entity assurance reports each year to Parliament. The first, *Control Structures as part of the Audits of the Financial Statements of Major Commonwealth Entities for the Year*, details the results of an assessment of the control structure of major entities. The second, *Audits of the Financial Statements of Commonwealth Entities*, provides a summary commentary on the results of all financial statement audits undertaken in the 12 month audit cycle ending in October each year.

The Controls Report summarises audit findings relating to entity internal control structures, including the internal control environment, information systems and control processes. The findings are based on the ANAO's interim audit activities

conducted over the first nine months of the financial year. The report also provides an update on the broader corporate governance issues that impact on financial management and reporting.

The annual Financial Statements report summarises the final result of the audits of the financial statements of Commonwealth entities including the Commonwealth Government of Australia Consolidated Financial Statements. In addition, the report provides commentary on a number of contemporary issues relating to the Commonwealth Financial Reporting Framework, focusing on the Commonwealth Government's Consolidated Financial Statements.

## **Client surveys**

Another important performance management and assessment mechanism is the entity survey. After each performance audit is tabled, feedback on the audit process is sought independently from the senior manager responsible for the audited program by means of a questionnaire and interview. An independent consultant performs this evaluation. The results of the most recent survey were positive on the whole. Managers continued to support the ANAO's efforts to move to a more 'value adding' approach. They also referred to the value of ANAO reports and recommendations in providing assurance and in providing leverage to facilitate particular activities. The entity survey is one of the most direct ways we have to test that our ongoing commitment to relationship management is achieving results. A similar survey program is used to assess our financial statement audits.

In addition, as well as the regular contact that we have with the JCPAA and other Parliamentary Committees, the ANAO conducts face-to-face surveys of parliamentarians. These surveys are conducted periodically to ensure that we are hitting the mark in terms of our product mix. This ensures that we will continue to be able to respond to the challenges of the future, and that we have a shared understanding of appropriate standards of accountability to lead and guide agencies into the future.

## **External scrutiny**

As well as our internal review and quality assurance procedures, the ANAO is subject to several layers of external scrutiny, including those applying to all other APS entities such as portfolio budget statements, and reviews by a Senate Estimates Committee. The most important of these, in terms of demonstrating our accountability to Parliament, is the JCPAA. The JCPAA reviews all of our reports. Consequently, a strong and dynamic relationship with this Committee, as our main point of contact with the Parliament, is crucial to our ongoing viability. I have also previously mentioned the scrutiny and assessment by entity audit committees. As well, we are under constant challenge by agencies to justify our decisions and our findings. All our products are subject to public scrutiny and included on our web site, as noted earlier.

The Independent Auditor of the ANAO carries out both the audit of the ANAO's financial statements and selected performance audits of the ANAO. The Act (Section 43) requires the Independent Auditor to have regard to the audit priorities of the

Parliament as determined by the JCPAA, in the conduct of performance activities. Performance audits conducted over the years range from an overall assessment of the economy, efficiency and effectiveness of the Office<sup>20,21</sup>, our human resource management<sup>22</sup>, benchmarking of our performance<sup>23</sup>, our strategic planning framework<sup>24</sup>, our planning and resource allocation processes<sup>25</sup>, and our audit management processes<sup>26</sup>.

## **Quality assurance reviews**

An integral part of quality control within the ANAO is the annual quality assurance program, which involves reviews of a sample of completed financial and performance audits. The overall objective of the program is to assess whether ANAO audits are conducted in accordance with auditing standards and policies. The reviews include assessments as to whether:

- the audit findings and conclusions are supported by quality audit evidence and analysis;
- the audit approaches and analysis used are appropriate;
- audit processes were documented appropriately;
- quality control was adequate; and
- audits were cost effective and timely.

## **Peer reviews**

Like our counterparts in the Australian States and overseas, we are engaged in identifying areas of risk, and opportunities for improvement, in setting our strategic agenda. Managing public sector businesses effectively in the international marketplace of the future will undoubtedly be challenging, with the increased emphasis on monitoring and reporting on intangible performance elements such as values, ethics, social and environmental responsibility. All public sector agencies, as well as the ANAO, need to continue to engage globally in identifying national approaches and solutions for greater effectiveness.

The ANAO supplements its internal quality assurance reviews with peer reviews to assess our performance audit reports, methodologies and processes, and benchmark with other audit offices. Recent peer reviews have been conducted, as part of reciprocal arrangements, with the Office of the Auditor-General in New Zealand and the National Audit Office of the United Kingdom. Such reviews provide:

- a level of assurance that the audits reviewed were carried out in accordance with auditing standards and policies;
- recommendations for improvement; and
- examples of good practice for the audit office conducting the review.

## CONCLUSION

The ANAO supports the Parliament in holding the Executive to account as part of the democratic process, while at the same time helping agencies to improve their performance in the changing accountability environment. While our independence is an essential element of our work, we can only meet our objectives if we earn the trust and respect of the Parliament. Clearly, we have that respect, and we will continue to work hard through ongoing quality assurance and review to ensure that the relationship remains strong and positive. It is worth reiterating that we regard the relationship as symbiotic in that we provide vital support to Parliament in terms of our assessment of the quality of administration across the APS to inform its deliberations, while we also rely on Parliament for advice as to appropriate accountability boundaries and for ongoing priority-setting. Our advice and support is complementary and, it is to be hoped, mutually beneficial.

Because of the changing business environment we face in the public sector, auditing needs to be adaptive and alert to the risks involved to ensure that we target the issues of most interest and value to Parliament, the public and contemporary public sector managers. The governance landscape has changed, and managers need access to better practice, leadership and guidance to ensure that their own business strategies are effectively determined and put in place. Our statutory independence, as well as our expertise and experience across all Commonwealth departments and agencies, gives us a unique position within the accountability framework. It is crucial that we capitalise on these strengths in setting our agenda and strategies for the future. That agenda, including strategic directions, will continue the assurance and advisory roles for which we are well known and respected. However, we will also need to ensure that we continue to recruit and retain the best resources. The ANAO has been monitoring trends in public sector change and determining our responses accordingly. This ensures that our approach and coverage will continue to be relevant and add value to public administration.

The ANAO recognises the importance of being an active participant in the process of change. This allows us to target products that span the accountability continuum from the assurance based products for which we are traditionally known and on which Parliament relies, through to our better practice guides and benchmarking studies that can add specific value to agencies' operations. While our approach needs to be monitored and reviewed for effectiveness over time, it should allow us to capitalise on our traditional strengths and to move into new value-adding areas in the future. We have pursued a focus on quality products as an essential element of our corporate planning which will assist us in meeting the objective of adding value to public administration.

In an environment where citizens have ever increasing expectations of government, where they expect government services to be delivered with the same degree of efficiency as private sector services, and private sector services are expected to be 'world's best practice', public sector auditing has played an important role in contributing to a world class public service.

However, there is still always scope for improvement in the delivery of Government programs and ANAO audits will continue to encourage that improvement. As



technology changes, as services change and new ways of delivering services are introduced, so our auditing methodologies and practices will adapt. What will not change is our commitment to improving public sector performance and accountability through quality products and services.

## NOTES AND REFERENCES

<sup>1</sup> It should be observed that risk management can minimise the uncertainty surrounding innovation, by requiring the assessment of a range of options in terms of the likely opportunities for improved service delivery and program outcomes, and what needs to be done to manage the risks associated with each option. See, for example, Northern Ireland Audit Office 2002 *Investing in Partnership: Government Grants to Voluntary and Community Bodies*, Belfast, 16 May.

<sup>2</sup> Hawke, A. Dr 2002, *Effective Communication*, Paper based on address by Allan Hawke, Secretary of Defence, to the Twilight Seminar of the National Institute for Governance, Canberra, 25 July, p.8.

<sup>3</sup> Section 32, Audit Committee

- (1) The directors of a Commonwealth authority must establish and maintain an audit committee with functions that include:
  - (a) helping the authority and its directors to comply with obligations under this Act; and
  - (b) providing a forum for communication between the directors, the senior managers of the authority and the internal and external auditors of the authority.
- (2) If the regulations state how the committee is to be constituted, it must be constituted in accordance with the regulations.

<sup>4</sup> ANAO, 1997. *Audit Committees*, Canberra. July.

<sup>5</sup> Joint Committee on Corporate Governance, 2001. *Beyond Compliance – Building a Governance Culture*, Final Report, Canada, November.

<sup>6</sup> *Ibid*, p. 30-31

<sup>7</sup> The Auditor-General Bill 1996.

<sup>8</sup> Howard, J. The Hon 2001, *The Centenary of the APS Oration*, Presentation to the Centenary Conference of the Institute of Public Administration Australia, Canberra, 19 June, p.5.

<sup>9</sup> ANAO 2002, *Managing People for Business Outcomes*, Report No.61, Canberra, 25 May.

<sup>10</sup> ANAO 2002, *A Preliminary Examination into the Allocation of Grant Funding for the Co-Location of National General Practice Organisations*, Report No.50, Canberra, 16 May.

<sup>11</sup> ANAO 2002, *Corporate Governance in the Australian Broadcasting Corporation*, Report No.40, Canberra, 8 April.

<sup>12</sup> Deegan, C 1999, 'Implementing Triple Bottom Line Performance and Reporting Mechanisms', *Charter*, vol. 70, no. 4, May, pp. 40-42. See also Royal Dutch / Shell Group 2001, *The Shell Report: People, planet and profits*; and Global Reporting Initiative 2000, *Sustainability Reporting Guidelines on Economic, Environmental, and Social Performance* – <http://www.globalreporting.org>.

<sup>13</sup> Public Accounts and Estimates Committee 2002, *Final Report on Environmental Accounting and Reporting*, Report No. 46, Melbourne, March, p. 132.

<sup>14</sup> Callick, R 2002, 'Miners dig deep for greener image', *Australian Financial Review*, 17 April 2002, p. 1 & p. 53.

<sup>15</sup> Public Accounts and Estimates Committee 2002, *Final Report on Environmental Accounting and Reporting*, Report No. 46, Melbourne, March, p. 17.

<sup>16</sup> Maitland, A 2002, *Rise in environmental reporting*, Financial Times, 29 July, p. 4.

<sup>17</sup> *Ibid*.

- <sup>18</sup> *Data, Science and Technology Section, The Canberra Times, 1 August 2002. p.18*
- <sup>19</sup> See ANAO 2002 *Audit Activity Report: July to December 2001*. Report No 31. Canberra, 13 February.
- <sup>20</sup> Sharpe, Michael 1990. *Report of the Independent Auditor on an Efficiency Audit of the Australian National Audit Office in accordance with the Audit Act 1901*. AGPS, Canberra, 16 October.
- <sup>21</sup> Sharpe, Michael 1992. *Report of the Independent Auditor on an Efficiency Audit of the Australian National Audit Office in accordance with the Audit Act 1901*. AGPS, Canberra, 18 September.
- <sup>22</sup> Boymal, David G 1996. *Performance Audit of Human Resource Management in the Australian National Audit Office*. AGPS, Canberra, 30 October.
- <sup>23</sup> Boymal, David G 1997. *Review of Benchmarking in the Australian National Audit Office*. AGPS, Canberra, 18 December.
- <sup>24</sup> Coleman, Michael 2000. *Report on Results of a Performance Audit of the Strategic Planning Framework of the Australian National Audit Office*. Commonwealth of Australia. Canberra, 3 April.
- <sup>25</sup> Coleman, Michael 2000. *Report on the Results of a Performance Audit of the Planning and Resource Allocation Processes in the Australian National Audit Office*. Commonwealth of Australia, Canberra, 22 December.
- <sup>26</sup> Coleman, Michael 2001. *Report on the Results of a Performance Audit of the ANAO Audit Management Processes*. Commonwealth of Australia, Canberra, 18 October.