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**Report of the  
2010 Strategic Review  
of the  
Queensland Audit Office**

**March 2010**

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# 2010 STRATEGIC REVIEW OF THE QUEENSLAND AUDIT OFFICE

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3 March 2010

The Honourable Anna Bligh MP  
Premier and Minister for the Arts  
Executive Building  
100 George St  
Brisbane Qld 4000

Dear Premier

We are pleased to provide herewith our Report on the 2010 Strategic Review of the Queensland Audit Office which has been undertaken in accordance with the relevant sections of the *Auditor-General Act 2009*, and also in accordance with our terms of appointment.

We have appreciated the cooperation and support we received from the Auditor-General and his staff and also officers of your Department which has been of immense assistance to us in the conduct of our Review. We have also appreciated the willingness of audit clients and other stakeholders to meet with us and provide valued input.

Our Report incorporates 57 conclusions and 44 recommendations which we commend to you, the Auditor-General and the Parliamentary Public Accounts and Public Works Committee to ensure that the Queensland Audit Office continues to be an important and effective element of public accountability and integrity in Queensland.

Yours sincerely



Graham Carpenter



Mark Gray



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## GLOSSARY OF TERMS

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AASB	Australian Accounting Standards Board
ACAG	Australasian Council of Auditors-General
ANAO	Australian National Audit Office
APES	Australian Professional and Ethical Standard
ASAE	Auditing Standard Assurance Engagement
ASPIRE	Auditing Systems by Planning Implementation Reporting and Evaluation
ARMC	Audit and Risk Management Committee
ASA	Auditing Standard Australia
ATOMS	Audit Time Online Management System
AURION	Aurion HR Software
AUASB	Auditing and Assurance Standards Board
CA	Chartered Accountant
CISA	Certified Information Systems Auditor
CPA	Certified Practising Accountant
CPI	Consumer Price Index
CRM	Client Relationship Management
EARC	Electoral and Administrative Review Commission
EMG	Executive Management Group of the Queensland Audit Office
ESG	Executive Staffing Group of the Queensland Audit Office
FMPM	Financial Management Practice Manual
FPMS	Financial and Performance Management Standard 2009
FTE	Full Time Equivalent
GOC	Government Owned Corporation
IFRS	International Financial Reporting Standard

IPSAM	Integrated Public Sector Audit Methodology
IS	Information Systems
ISC	Information Steering Committee
LaunchPAD	The Queensland Audit Office's Performance Assessment and Development Scheme
NAVISION	Navision Accounting Software
PAC	The former Public Accounts Committee of the Queensland Parliament
PASS	Professional Auditors Skills Scheme
PAPWC	Public Accounts and Public Works Committee of the Queensland Parliament (established 2009)
PMS Audit	Performance Management Systems Audit
QAO	Queensland Audit Office
Thomson Report	Governance and Audit Framework for Self Assessment and External Review, External Review of Queensland Audit Office, 30 <sup>th</sup> September – 2 <sup>nd</sup> October 2009 Conducted by Ms Sandy Thomson
VAGO	Victorian Auditor-General's Office
1997 Review	The 1997 Strategic Review of the Queensland Audit Office undertaken by Mr Tom Sheridan.
2004 Review	The 2004 Strategic Review of the Queensland Audit Office undertaken by Mr Henry Smerdon and Mr Richard Anderson

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## 1. EXECUTIVE SUMMARY

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### 1.1 Overview

The position of Auditor-General is a critical element of the integrity and accountability framework of the Queensland public sector, and the QAO has a long history of providing quality independent audit services to the Queensland Parliament. Our observations are that it is a well-respected and highly-regarded organisation with the highest professional and ethical standards.

In undertaking our Strategic Review, we were impressed with the dedication and commitment of the Auditor-General and his staff in undertaking what can at times be a challenging and demanding role. We were also impressed with the vision and leadership being provided to the QAO by the current Auditor-General, Mr Glenn Poole.

The QAO had 329 clients and undertook 747 audits in 2008–09. Chargeable hours of in-house activity by the QAO reached 202,456 hours for 2008–09, an increase of over 31% in workload since 2005–06. In addition, contract auditors undertook an estimated 91,821 hours of work for the QAO in 2008–09, representing around 45% of total QAO audits by number, and 43% by value of fees. There were a further 15,078 chargeable hours of activity by contracted-in resources, adding to a grand total of 309,355 chargeable hours of audit activity in 2008–09 for which the Auditor-General was responsible.

The QAO has funding of \$42.8 million for 2009–10, and a staff of 263 as at 31 December 2009. Audit fees for 2009–10 are projected to be \$36.5 million, making it in all probability the largest audit practice in the State.

In addressing our Terms of Reference, we have sought to focus on key strategic issues, not just in respect of the recent and current performance of the QAO, but also in terms of emerging trends which will impact on the future direction and sustainability of the QAO's business. This has encompassed an assessment of :

- The quality of audit work undertaken by the QAO, in terms of financial and compliance audits, PMS audits and other audits
- The QAO's internal management and governance arrangements, and communication with stakeholders
- Key measures of overall performance of the QAO, and comparisons with Audit Offices in other Australian jurisdictions
- Implementation of the outcomes of the 2004 Strategic Review
- The scope of the QAO's audit mandate
- Strategic issues for the future.

The QAO is to be commended for its diligence in implementing the recommendations from the 2004 Review. Most of the recommendations have been implemented in full, with only a small number of issues requiring further attention. Notably, the 2004 Review challenged the QAO to more fully utilise its existing mandate on PMS audits, and we are satisfied that this has been achieved.

The quality of the QAO's audit work has been enhanced by the implementation of new electronic audit methodologies known as IPSAM (for financial and compliance audits) and ASPIRE (for PMS audits), with further refinements of these systems expected to yield further benefits.

Considerable effort has also been devoted to improving internal management and governance arrangements, with a view to lifting the performance of the organisation. To date, there have been some mixed results. Progress has been achieved on a number of fronts, with some initiatives still in train, including a Business Improvement Plan, CRM, LaunchPAD and PASS.

On the other hand, there have been teething problems with the implementation of eTrack, the QAO's new practice management system, which so far has not lived up to its initial expectations. Actions are under way to enhance the capacity and performance of eTrack, and progress is occurring, although it may yet be a further 6–12 months or more before the benefits are fully realised.

Overall, the QAO is well organised and managed under the leadership of the Auditor-General. It is an effective public sector auditing practice, with some room yet for further improvement in performance. In comparison with Audit Offices in other Australian jurisdictions, the QAO generally ranks around average or just above for most key performance measures. In our view, the QAO should aim to be ranked in the top 2–3 Audit Offices in Australia, and consistently above average for most key performance measures.

The challenge for the QAO is to fully bed down the suite of initiatives it is pursuing, and to ensure that the expected benefits translate to demonstrable improvements in the productivity of the organisation in the next few years. As a large audit practice, the QAO can also do more to embrace some of the best practices of private sector audit businesses.

We have made a total of 57 conclusions and 44 recommendations, which are outlined below. These conclusions and recommendations are directed towards building on the strengths and achievements of the QAO, to lift its performance to a superior standard. They reinforce an ongoing process of continuous improvement which will better position the QAO to respond to the emerging challenges of the future.

Most significantly, we consider that it is now time for the QAO's audit mandate to be expanded to full performance audits, consistent with the approach adopted by most other jurisdictions in Australia, as well as in other advanced nations such as the United Kingdom, United States, Canada and New Zealand. We have made some accompanying recommendations about how the expanded performance mandate should work. There are also a range of other recommendations relating to audit practices and internal work practices of the QAO, including communication with stakeholders.

An ongoing issue of concern to many audit clients is the level of fees, along with the way in which they are set by the QAO. Accordingly, we have recommended the development of an Audit Fee Charter which will require the QAO to be more rigorous in setting fees, and more transparent and accountable to clients for those fees, thereby ensuring better value for money.

Looking to the future, there are some looming challenges to be faced by the QAO. It will need to take account of the increasing complexity of government service provision, investment and procurement processes. For example, the wider use of contracting out of core service delivery through third party agents raises questions as to the extent to which the QAO may need to “follow the dollar” in auditing government expenditure programs. Joint Commonwealth–State programs, infrastructure and IT investment, carbon reporting, and other environmental issues are some of the matters likely to attract increasing audit scrutiny by the QAO. As well, further changes in auditing methodology and accounting standards are likely to occur, and assurance auditing is likely to become more widely adopted.

For the QAO itself, there will be changes in both workload and workforce which pose a risk to its future resourcing, and the sustainability of its business. This will require greater attention to longer term planning and resourcing.

Our recommendations do not require any additional funding through government appropriation. To the extent that there may be some limited additional costs for the QAO, this should be managed internally through a re-prioritisation of tasks. In an environment of fiscal restraint, it is incumbent upon the QAO to strive to boost output and productivity within current available levels of funding. In short, the QAO should be expected to achieve more with the resources now at its disposal.

Over time, however, we would expect that the Auditor-General may wish to argue a case for additional government funding to increase the number of performance audits undertaken each year. This will be a matter for consideration by the Government of the day in the normal budget process.

In summary, our recommendations are designed to help shape the future direction and performance of the QAO in a rapidly changing and challenging environment. In responding to these recommendations, we are confident that the QAO will continue to enhance its reputation and standing as an effective public sector audit practice, thereby adding to the long and proud record of the QAO as a fundamental element of the integrity and accountability framework of public administration in Queensland.

## 1.2 Summary of Conclusions and Recommendations

Our Report is structured to present a series of conclusions and recommendations on the subject matter covered. We have used conclusions to summarise our findings on particular issues, or where we wish to make relevant observations, without necessarily leading to a specific recommendation as to a particular course of action. Recommendations generally flow from a conclusion (although this is not necessarily always the case), and indicate where we consider there is a need for specific action to be taken on an issue or set of issues.

### SECTION 3

#### Conclusions

##### *CN.3(i)*

The position of Auditor-General is a critical element of the integrity and accountability framework for Queensland and the QAO is a well respected independent audit office with a long history of providing reliable external audit services to Parliament in a highly professional manner.

##### *CN.3(ii)*

The new *Financial Accountability Act 2009* and *Auditor-General Act 2009* provide a comprehensive and rigorous framework for financial management and accountability of the public sector in Queensland, but this could be strengthened by giving enhanced emphasis to the fundamental principle of value for money, as previously articulated in the former *Financial Administration and Audit Act 1977*.

#### Recommendation

##### *RN.3(i)*

**Reflecting the importance of value for money as a fundamental over-arching principle of financial management, that the Auditor-General consult with the Treasurer on including value for money in the primary legislation, being the *Financial Accountability Act*, rather than the Financial Management Performance Standards, where it currently sits.**

#### Conclusion

##### *CN.3(iii)*

The QAO should continue to develop Better Practice Guides where there is a demonstrated need and the QAO is in a position to develop such guidance especially where better practice is identified as part of undertaking an audit.

## SECTION 4

### Conclusions

#### *CN.4(i)*

The Auditing Standards issued by the Auditor-General represent a sound basis for the audit function of the QAO, including for contract auditors.

#### *CN.4(ii)*

The QAO Auditing Standards should include a provision related to any act or omission that has given rise to a waste of public resources.

### Recommendation

#### *RN.4(i)*

**The QAO Auditing Standards be revised to incorporate a provision that any act or omission that has given rise to a waste of public resources can be part of the examination of an audit.**

### Conclusion

#### *CN.4(iii)*

IPSAM is a valuable audit methodology for financial and compliance audits which is consistent with Australian Auditing Standards and represents a sound basis for fulfilling the Auditor-General's statutory audit responsibilities.

### Conclusions

#### *CN.4(iv)*

Our review of IPSAM files for financial and compliance audits identified a high standard of compliance with the methodology.

#### *CN.4(v)*

There are some opportunities to improve the quality and security of record keeping. Specifically, IPSAM files should include clean versions of documents and, for key communications with audit clients, that these be saved as a PDF version once they become final.

### Conclusions

#### *CN.4(vi)*

There are benefits in terms of improved public administration from the QAO undertaking cross-sector audits of a financial and compliance nature.

#### *CN.4(vii)*

The decision of the Auditor-General to utilise ASPIRE for cross-sector audits is appropriate, noting that effective cross-linking to IPSAM for individual audit clients will be essential.

Conclusion

*CN.4(viii)*

The QAO has established a strong team of Information Systems auditors who operate within a sound Information Systems audit methodology and provide a valued service as part of financial and compliance audits and in undertaking a number of cross-sector audits. The further involvement in cross-sector audits and also with PMS audits means that the methodology ASPIRE will be utilised for those audits in the future and the staff will need to be familiar with the policies and guidance from that methodology.

Conclusion

*CN.4(ix)*

There are sufficient existing powers for the Auditor-General to respond to emerging needs for audits of a special or an ad hoc nature. The Parliament has the power by resolution to direct the Auditor-General to undertake an audit, although we are not aware of any instances where such a power has been used. In addition, the PAPWC may refer issues to the Auditor-General for consideration.

Conclusions

*CN.4(x)*

The process for reporting to Parliament on financial and compliance audits including cross-sector audits is sound and appropriate.

*CN.4(xi)*

The Auditor-General's reports to Parliament are acceptable in terms of readability.

## SECTION 5

Conclusion

*CN.5(i)*

The QAO is to be commended for the increased attention to undertaking PMS audits and reporting to Parliament on the results of these audits.

Conclusion

*CN.5(ii)*

The Auditor-General has applied the expanded PMS mandate on performance measures in a number of PMS audits in the last three years. To date, however, the Auditor-General has not utilised the power to provide opinions on performance measures for individual public sector entities as part of PMS audits reported to Parliament.

## Recommendation

### *RN.5(i)*

**That the Auditor-General, in undertaking PMS audits, give consideration to utilising the power to provide opinions on whether performance measures for individual public sector entities are relevant and appropriate, having regard to their purpose, and fairly represent that entity's performance.**

## Conclusions

### *CN.5(iii)*

The ASPIRE methodology as revised for use from 2010 onwards represents a sound basis for undertaking PMS audits.

### *CN.5(iv)*

The structure of the ASPIRE manual is not cross referenced to the auditing standards. There would be benefit in having a mapping to the auditing standards which would assist when standards are revised.

### *CN.5(v)*

It would be beneficial to incorporate information on the processes to identify the need for experts for assignments, for appointing and managing experts and in assessing the quality of advice and other input provided for PMS audits.

## Conclusions

### *CN.5(vi)*

PMS audits provide valuable information for Parliament on performance management systems and represent an important tool to guide improvements in public administration.

### *CN.5(vii)*

The revised ASPIRE provides an appropriate methodology for undertaking PMS audits.

### *CN.5(viii)*

From the review of PMS audit files and from feedback from audit clients, the QAO needs to ensure that quality review requirements within ASPIRE are fully utilised.

### *CN.5(ix)*

To enhance the PMS audit process, the QAO and audit clients (through the contact officer) should ensure that matters of a factual nature are settled at an earlier stage in the audit process than at the time of presentation of the audit management letter.

## Recommendations

### *RN.5(ii)*

**That the QAO institutes a standard practice of holding initial discussions with the relevant Accountable Officer or Chief Executive Officer of an audit entity with a view to obtaining input on the scope and objectives of PMS audits, as is now being introduced.**

### *RN.5(iii)*

**That the Auditor-General give consideration to wider involvement of subject matter experts in the planning, audit field work and reporting for PMS audits.**

### *RN.5(iv)*

**That the Auditor-General continue with programs to develop the internal skill base for undertaking PMS audits.**

### *RN.5(v)*

**That the Auditor-General ensure that quality review standards for PMS audits are observed.**

### *RN.5(vi)*

**That, for PMS audits, the QAO and the audit client ensure that matters of a factual nature are settled at an earlier stage of the audit process such that these matters do not detract from the quality of the audit when the management letter is provided .**

### *RN.5(vii)*

**That opportunities be taken by the Auditor-General and senior staff of the QAO to educate audit clients on the mandate for, and benefits arising from, PMS audits.**

## SECTION 6

### Conclusions

#### *CN.6(i)*

The QAO has made significant improvements in managing the contract auditing process.

#### *CN.6(ii)*

Further consideration could be given to allocating overhead costs of managing the contract auditing process across all audit clients, in view of the broader benefits derived from this process.

### Conclusions

#### *CN.6(iii)*

There is a need to consider the nature and quality of information available for contract auditors to ensure that appropriate risk assessed fee quotes are submitted for audit assignments for the QAO. This would include whether some form of Permanent Audit File (preferably in electronic form) would be beneficial.

#### *CN.6(iv)*

Further consideration could be given to using a common auditor for the audit of public sector entities within a particular sector/industry to leverage the benefits of specialisation in that sector/industry. (This needs to be considered in the context of rotation of audit appointment arrangements over time.)

### Recommendations

#### *RN.6(i)*

**That the QAO upgrade the nature and quality of information available for tenderers submitting proposals for contract audit work to ensure appropriate risk-assessed fee quotes can be made.**

#### *RN.6(ii)*

**That the QAO assess whether the use of contract auditors for a group of entities within a particular sector or industry would provide benefits for the QAO and audit clients in terms of specialisation in that sector/industry.**

### Conclusion

#### *CN.6(v)*

The QAO is to be commended for the diligence in reviewing the quality control processes in contract audit firms, with the aim of ensuring that high standards of public sector auditing are maintained.

## SECTION 7

### Conclusion

#### *CN.7(i)*

The current funding model for the QAO has proven to be practical, robust and sustainable, and there is no reason to change the current structural arrangements.

### Conclusion

#### *CN.7(ii)*

There are some justified concerns from audit clients about the fees charged by the QAO, and there is a clear need for the QAO to improve the way in which it sets fees, and manages its time recording and billing systems to ensure greater transparency, accountability and consistency of approach.

**Recommendations*****RN.7(i)***

**That there should continue to be regular annual adjustments to the basic rate of QAO audit fees, subject to the approval of the Treasurer in accordance with Section 56 (3) of the *Auditor-General Act 2009*.**

***RN.7(ii)***

**That the annual adjustment to be determined by the Treasurer should be based on an assessment of wages, salaries and other costs relevant to the operations of the QAO, but should also take into account:**

- **productivity and/or efficiency considerations, especially those relevant to the funding of core government departments**
- **any adjustment factor to reflect market movements in audit fees generally.**

***RN.7(iii)***

**That the QAO needs to provide a more consistent, coherent and transparent basis for the determination of fees, through an Audit Fee Charter which commits the QAO to:**

- **ensure that the Engagement Leader for each audit is required to present and explain the QAO's audit fee proposal to an entity's Audit Committee as part of the Annual Client Service Plan**
- **provide a detailed disaggregation of the composition of the audit fee for an entity, including scoping issues, identification of major tasks or activities, hours of work to be undertaken for each major task or activity and the type and level of resources to be used**
- **provide an opportunity for audit clients to seek further information, clarification and/or justification of fees prior to the commencement of the audit plan**
- **undertake a zero-base approach to the determination of fees for an entity at least once every three years, or where the audit fee is expected to vary from the previous year by more than 10% (for reasons other than a change in the basic rate)**
- **ensure that, during the course of the audit task, any variation in audit fees of greater than 10% from the original fee proposal is notified to, and acknowledged by, the Accountable Officer or Chief Executive and the Audit Committee of an entity prior to any additional costs being incurred by the QAO.**

***RN.7(iv)***

**That the QAO develop a more comprehensive program of benchmarking of audit fees for comparable entities with a view to ensuring greater consistency in the determination of fees, including:**

- **internal benchmarking of fees for comparable size and type of entities**
- **external benchmarking, both with ACAG, and with private sector audit firms where relevant and practical.**

## SECTION 8

### Conclusions

#### *CN.8(i)*

The organisational structure for the QAO is appropriate and practical in undertaking the core function of auditing for the public sector in Queensland.

#### *CN.8(ii)*

There has been a sharp increase in the relative proportion of the QAO's resources committed to audit support functions, which is difficult to justify, unless it produces a demonstrable improvement in the productivity of the organisation, which is not yet apparent.

### Recommendation

#### *RN.8(i)*

**The QAO should aim to ensure that audit support functions return to around 15–18% of total staffing, consistent with the level achieved prior to 2008–09, unless a higher level can be justified by demonstrable improvements in the productivity of front-line audit service delivery (as measured for example by better capacity utilisation).**

## SECTION 9

### Conclusion

#### *CN.9(i)*

The EMG should re-focus on strategic issues, and higher-order measures of performance, such as productivity and capacity utilisation, and streamline its detailed monitoring of operational performance.

### Recommendation

#### *RN.9(i)*

**That the recommendations of the Thomson Report relating to the EMG be adopted viz**

- *“Noting cross reference to Standard 1.2.9, the development of a dashboard of key result areas is recommended. This will enable management reports to be further refined and simplified.*
- *That actions for key issues areas be developed prior to EMG meetings to enable a more proactive approach to decision making.”*

**Recommendation**

***RN.9(ii)***

That the QAO's Risk Register be amended to include the following risks, as recommended by the Thomson Report:

- *“HR planning is not in line with strategic planning*
- *Changing mix of clients relating to sale of government assets, increased contracting out of government services, rationalization of local government and the impact of fixed overheads*
- *Increased use of contracting out of audit work.”*

**Recommendation**

***RN.9(iii)***

That the effectiveness of the ISC is regularly assessed to ensure that it is adding greater strategic value to the consideration of emerging information technology issues impacting on the QAO, including ongoing refinement of eTrack, IPSAM and ASPIRE.

## **SECTION 10**

**Recommendation**

***RN.10(i)***

That the Annual Work Plan's projected workload for each coming year incorporate a contingency provision for additional hours likely to be required for unplanned activity, taking into account what has occurred on average in previous years.

**Recommendations**

***RN.10(ii)***

That the QAO's audit resourcing model be further refined to provide improved focus on the nature and size of the audit task, and on the assessment of audit risks. This would mitigate the risk that inbuilt inefficiencies in resourcing are perpetuated through the current configuration of the model.

***RN.10(iii)***

That the QAO's audit resourcing model be further developed to provide a rolling three year forward plan to identify and address emerging issues which will impact resourcing needs of the QAO into the future.

Conclusions

*CN.10(i)*

The introduction of eTrack has not met the QAO's initial expectations, resulting in disruption to the QAO's business and disillusionment amongst staff.

*CN.10(ii)*

On a benefit-cost basis, it is likely that the eTrack project would rate poorly.

*CN.10(iii)*

Corrective actions taken by the QAO are achieving improved performance of eTrack, but more yet needs to be done to achieve a fully functional system that is properly utilised by staff.

**Recommendation**

*RN.10(iv)*

**That the QAO take necessary steps to ensure that eTrack provides a reliable and effective practice management system for the future, and that staff be encouraged to utilise its capabilities.**

Conclusion

*CN.10(iv)*

The objectives of the Business Improvement Plan 2009–11 are appropriate, but it is an extensive and ambitious program, and there will be inevitable challenges in ensuring that the program translates into enhanced business practices and improved productivity for the organisation.

## SECTION 11

Conclusion

*CN.11(i)*

The recruitment strategies of the QAO are commended, especially the GRADtects program, and the QAO is encouraged to continue to refine and develop these strategies to meet future needs, whilst reinforcing the particular attractions and benefits of working in the QAO.

**Recommendation**

*RN.11(i)*

**That the QAO continue to pursue strategies for achieving a more flexible remuneration structure for professional audit staff. It would be beneficial for the QAO to investigate this matter further in conjunction with the Public Service Commission and the relevant Government department.**

Conclusion

*CN.11(ii)*

Changes to staff benefits and other human resource policies are normally highly sensitive and often emotional issues, which need to be managed carefully to minimise adverse reactions and impacts.

**Recommendation**

*RN.11(ii)*

**That the Auditor-General ensures adequate consultation and communication with staff, and takes account of timing issues, in undertaking any major or sensitive changes in staffing benefits or other human resources policies.**

Conclusion

*CN.11(iii)*

The QAO needs to continue to improve the way it operates its business, by adopting where relevant the best practices, systems and culture of comparable private sector audit businesses.

## SECTION 12

Conclusion

*CN.12(i)*

The Auditor-General should recommence a regular program of 3–4 visits of 1–2 days each to key regional centres in Queensland each year.

Conclusion

*CN.12(ii)*

Issues identified from audits may have a whole-of-government impact through the need to implement revised protocols or standards. The QAO should ensure that any recommendations arising from any observed accountability deficiencies identify the potential impact on the operations of Government that may follow if the issue is not addressed. As part of this process, the QAO should consult with responsible entities (especially central agencies) about the practicability of any proposed recommendations, particularly in terms of the overall level of regulatory burden that may result from addressing the issues raised by the Auditor-General and the risk and cost to Government if no action is taken.

Conclusion

*CN.12(iii)*

The QAO should take action to ensure greater consistency in communications to staff on the outcomes of EMG meetings, by ensuring that Minutes of EMG meetings are regularly posted on the intranet site on a timely basis, and are discussed as a matter of course by all EMG members in their team meetings.

## SECTION 13

### Conclusion

#### *CN.13(i)*

The QAO should focus attention on lifting its performance on macro measures of productivity and capacity utilisation, and pay less attention to the larger number of second-order performance measures now being recorded and reported.

### Recommendation

#### *RN.13(i)*

**That the QAO focus greater attention on lifting its performance on macro measures of productivity and capacity utilisation.**

### Conclusion

#### *CN.13(ii)*

As an aspirational target, in relation to ACAG benchmarks, the QAO should aim to lift its performance to be ranked in the top 2–3 Audit Offices in Australia, and consistently above average, for most key performance indicators.

### Recommendations

#### *RN.13(ii)*

**That the QAO aim to lift its performance to be ranked in the top 2–3 Audit Offices in Australia, and consistently above average, for most key ACAG performance indicators.**

## SECTION 15

### Recommendations

#### *RN.15(i)*

**That the *Auditor-General Act 2009* be amended to include a requirement for the QAO to prepare a three-year Strategic Audit Plan for PMS audits, and to update the plan each year. The plan should incorporate indicative audit topics over the three years, with more specific and definite scoping of topics for the first year.**

#### *RN.15(ii)*

**That the Auditor-General and the Chair of the PAPWC agree on a protocol for consultation with the PAPWC on the draft Strategic Audit Plan for PMS audits prior to the commencement of each financial year.**

#### *RN.15(iii)*

**That the Auditor-General consult with potential audit clients and other affected parties, and consider their feedback, prior to finalisation of the Strategic Audit Plan for PMS audits.**

#### *RN.15(iv)*

**That, following the passage of appropriation, the Auditor-General finalise the Strategic Audit Plan for PMS audits, and publish it on the QAO website.**

Conclusion

*CN.15(i)*

Local governments should continue to be audited by the Auditor-General.

Conclusion

*CN.15(ii)*

The model of separation of audit service delivery from the Office of the Auditor-General is not supported.

## SECTION 16

Conclusions

*CN.16(i)*

It is now time for the scope of the Auditor-General's mandate to be expanded to full performance audits, consistent with the approach adopted by most other jurisdictions in Australia, as well as in other advanced nations such as the United Kingdom, Canada and New Zealand.

*CN.16(ii)*

The recommendations outlined in Section 15 in relation to PMS audits remain equally relevant and applicable to the expanded mandate.

**Recommendations**

*RN.16(i)*

**That the *Auditor-General Act 2009* be amended to broaden the audit mandate to enable the Auditor-General to undertake performance audits, such amendment to be generally consistent with legislation applying in other Australian jurisdictions.**

*RN.16(ii)*

**That the *Auditor-General Act 2009* be amended to include a requirement for the QAO to prepare a three-year Strategic Audit Plan for Performance Audits, and to update the Plan each year.**

*RN.16(iii)*

**That the Auditor-General and the Chair of the PAPWC agree on a protocol for consultation with the PAPWC on the draft Strategic Audit Plan prior to the commencement of each financial year.**

*RN.16(iv)*

**That the Auditor-General consult with potential audit clients and other affected parties, and consider their feedback, prior to finalisation of the Strategic Audit Plan.**

*RN.16(v)*

**That, following the passage of appropriation, the Auditor-General finalise the Strategic Audit Plan, and publish it on the QAO website.**

*RN.16(vi)*

**That the *Auditor-General Act 2009* be amended to require the Auditor-General, in undertaking performance audits, to take into consideration performance management standards and guidance issued by the government.**

Conclusion

*CN.16(iii)*

In accordance with convention, it is inappropriate for the Auditor-General to comment on matters of government policy or objectives in undertaking audits.

**Recommendation**

*RN.16(vii)*

**That, concurrent with expansion of the performance audit mandate, the *Auditor-General Act 2009* be amended to incorporate a provision to ensure that:**

- **where there is a clear government or local government policy or guideline, the performance audit would be assessed against the relevant policies for that entity or group of entities; and**
- **in undertaking performance audits, the Auditor-General is not empowered to question the merit of policy objectives of the Government.**

Conclusions

*CN.16(iv)*

There is a case to amend the *Auditor-General Act 2009* to give the Auditor-General limited powers in exceptional circumstances to undertake an audit of a non-government body that is the recipient of funding or other financial benefit other than for the direct supply of goods and services.

*CN.16(v)*

There should be a provision for the QAO to have access to the staff and records of a grant receiving body included in contracts and agreements negotiated by Queensland Government agencies for delivery of services to third parties.

**Recommendation**

*RN.16(viii)*

**That the *Auditor-General Act 2009* be amended to provide a power for the Auditor-General to undertake an audit as to whether a grant or other financial benefit provided to a person or body that is not a Queensland public sector entity has been applied economically, efficiently and effectively for the purpose for which it was given and in compliance with relevant legislation, standards and guidelines, in circumstances where:**

- **there is a request from the Premier; and**
- **the Auditor-General agrees to such a request,**

**provided that, prior to making such a request, the Premier must be satisfied that there is *prima facie* evidence of:**

- **a breakdown or failure of the normal procedures for accounting for the expenditure of funds advanced by the State; or**
- **other evidence of a failure to acquit such funds in accordance with agreed procedures, including the achievement of agreed performance targets.**

**Recommendation**

*RN.16(ix)*

**That the *Auditor-General Act 2009* be amended to allow for the Auditor-General to dispense with the audit of small size/low risk public sector entities, with such entities being required to engage an appropriately qualified auditor and to provide a copy of the audited financial statements (including audit report) to the Auditor-General as soon as practicable after completion.**

Conclusion

*CN.16(vi)*

There is not a strong case for the Auditor-General to be required to undertake an audit of the forward estimates. In the event of any concerns related to the processes for developing and reporting the forward estimates, this could be the subject of an audit of the relevant systems and processes used to produce the forward estimates.

Conclusion

*CN.16(vii)*

A fixed, non-renewable seven-year term of appointment for the Auditor-General is appropriate.

**Recommendation**

*RN.16(x)*

**That the *Auditor-General Act 2009* be amended to provide for a fixed, non-renewable seven-year term of appointment for the Auditor-General.**

## SECTION 17

**Recommendation**

*RN.17(i)*

**That the Auditor-General give consideration to an expanded focus of audits of infrastructure and IT investments, building on the work already undertaken in these areas.**

**Recommendation**

*RN.17(ii)*

**That the Queensland Auditor-General continue to actively pursue opportunities for co-operation with Auditors-General at the Commonwealth level and in other States and Territories, with a view to ensuring that there is no unnecessary waste or duplication of resources in auditing of Commonwealth–State programs.**

Conclusion

*CN.17(i)*

The QAO needs to ensure that the implications of the revised suite of 41 Auditing Standards following the audit clarity project are incorporated into the audit methodology including IPSAM.

Conclusion:

*CN.17(ii)*

The QAO should monitor the developments associated with the possible establishment of two groups of reporting entities in terms of level of disclosures, and liaise as necessary with Queensland Treasury on implementation issues.

Conclusion

*CN.17(iii)*

The audit implications of greenhouse gas reporting requirements and any emissions trading scheme are likely to be significant and will require ongoing monitoring by the QAO.

**Recommendation**

*RN.17(iii)*

**That the QAO develop strategies to manage emerging trends in its workload and its internal resourcing capacity over a three-year planning horizon and to ensure the ongoing sustainability of its business.**

### 1.3 Linkage of Review Report to the Terms of Reference

Terms of Reference	Relevant Section of Report
<b>Scope</b>	
(a) a review of the auditor-general's functions	3 and 16
(b) a review of the auditor-general's performance of the functions to assess whether they are being performed economically, effectively and efficiently	13 and generally covered in the Report
The appointee will be required to generally assess, and provide advice and recommendations about, the functions and the performance of the functions, of the Auditor-General and the QAO, in order to assess whether they are being performed in accordance with the requirements of the Act	4, 5 and 6
The review is to examine all structural and operational aspects of the QAO, as well as its relationships with public sector entities, relevant Ministers, the Treasurer and the Parliament of Queensland	8, 9, 10, 11 and 12
Consideration is also to be given to the recommendations agreed by the Government arising from both the 2004 strategic review, and the related Public Accounts and Public Works Committee report on the review and the Government's response to the Committee's report, particularly the extent to which they have been implemented and whether they are achieving the desired objective	14 and Attachment F
<b>Methodology</b>	
(a) Whether existing processes are appropriate to the QAO's audit mandate, the needs of public sector agencies and emerging public sector organisational structures	15 and 16
(b) The effectiveness of existing processes, and in particular the effectiveness of the auditing standards issued by the Auditor-General, in fulfilling the audit mandate within the contemporary accountability requirements of Queensland's system of government;	4, 5 and 6
(c) Examination of trends in the workload of the QAO, including an examination of current and past methodologies relating to practices and procedures employed by the QAO	4 and 5
(d) The operational efficiency of QAO audit methodology and the relative efficiency of in-house and contract audit service provision	4, 5 and 6
(e) The standard and quality of service provided to the Parliament, audit clients and executive Government	4, 5, 6, and 12
(f) The structure of the QAO, including the delegation and allocation of responsibilities	8 and 9
(g) Management systems and processes used by the QAO, including: <ul style="list-style-type: none"> <li>(i) appropriate internal and external performance indicators to monitor efficiency and effectiveness; and</li> <li>(ii) internal communication and sharing of performance information</li> </ul>	9, 10, 11, 12 and 13
(h) Human resource issues, including formal and informal staff training and guidance	11

(i) Administrative systems and processes used by the QAO	8, 9, 10, 11 and 12
(j) Whether the funding for the QAO is both appropriate and appropriately used to discharge the functions and objectives of the QAO	7
(k) Appropriate protocols for communication by and with the QAO	12
(l) Any other matters which impact on the economy, efficiency and effectiveness of the QAO	Generally covered in report
<b>Matters to take into account</b>	
Consideration of comparative models, practices and procedures used by offices in other jurisdictions equivalent to the QAO	15
The results of the Public Accounts and Public Works Committee's review of the Auditor-General's performance management systems mandate	The PAPWC Review at the time of this Report has not yet been completed
Interviews with staff (including all staff who indicate that they wish to be interviewed by the appointee) and former staff of the QAO, both individually and in focus groups (interviews with former staff are optional)	Number of group meetings held with staff, and also individual meetings held on request with both staff and former staff
Consultation with key Government agencies	Attachment B provides a listing of Government agencies consulted
Consultation with other key stakeholders, including accounting firms that conduct business with the QAO	Attachment B provides a listing of key stakeholders consulted, including three accounting firms who undertake audits for the QAO

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## 2. BACKGROUND

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### 2.1 Context of the Strategic Review

Under Section 68 of the *Auditor-General Act 2009*, there is a requirement for a Strategic Review of the QAO to be conducted at least every five years. The Review is to include a review of the Auditor-General's functions, and the Auditor-General's performance of those functions to assess whether they are being performed economically, effectively and efficiently.

The Review is required to be undertaken by an appropriately qualified person (Reviewer) appointed by the Governor in Council on terms and conditions approved by the Governor in Council. The Terms of Reference for the Review are also approved by the Governor in Council.

The Honourable the Premier as the responsible Minister must consult with the Parliament's Public Accounts and Public Works Committee and with the Auditor-General about the appointment of the Reviewer and the Terms of Reference.

The appointed Reviewer has the powers of an authorised auditor in undertaking investigations and accessing information relevant to such investigations.

Prior to finalising a Report, the Reviewer must give a copy of the proposed report to the Premier and the Auditor-General, who then have 21 days to provide written comments on any relevant matters. The Reviewer must then either amend the report to the satisfaction of the person making the comments, or otherwise include the comments in full in the final Report.

The Premier must table the Review Report in the Legislative Assembly within three sitting days after the Premier receives the final Report.

### 2.2 Terms of Reference

The Terms of Reference for the conduct of this Review were approved by the Governor in Council on 8 October 2009.

The scope of the Review was defined as:

*"The appointee will be required to generally assess, and provide advice and recommendations about, the functions and the performance of the functions, of the Auditor-General and the QAO, in order to assess whether they are being performed in accordance with the requirements of the Act.*

*The Review is to examine all structural and operational aspects of the QAO, as well as its relationships with public sector entities, relevant Ministers, the Treasurer and the Parliament of Queensland.*

*Consideration is also to be given to the recommendations agreed by the Government arising from both the 2004 Strategic Review, and the related Public Accounts and Public Works Committee Report on the Review and the Government's response to the Committee's Report, particularly the extent to which they have been implemented and whether they are achieving the desired objectives."*

The full details of the Terms of Reference, including scope, methodology and specific matters to be taken into account in the course of the Review, are outlined in Attachment A.

## 2.3 Reviewers

The Reviewers appointed by the Governor in Council on 8 October 2009, who are acting in their personal capacities, are:

### (a.) Mr Graham Carpenter

Mr Carpenter is a chartered accountant and chairs the Board of Tarong Energy Corporation Limited. He is a former Assistant Under Treasurer in Queensland Treasury and also a former Auditor-General of the Northern Territory. He also has extensive current and previous experience on a number of private and public sector finance, audit and risk committees. He is a former partner of BDO, and remains a consultant to that firm.

### (b.) Mr Mark Gray

Mr Gray is an Executive Director with BDO. He is also a company director on a number of private and public sector Boards, and has his own consulting business, focussing on strategic commercial and financial advice. He is a former Office Head of the Macquarie Group in Brisbane, and also a former Deputy Under Treasurer, Queensland Treasury, and he has extensive experience on finance, audit and risk committees.

As a part of our appointments, we provided statements to the Director-General, Department of the Premier and Cabinet and the Auditor-General advising of potential conflicts held, and establishing a process whereby the Reviewers were required to step down from any appointments to bodies where the 2009 financial statement audit had not been finalised, or in the event of a dispute between the audit client and the QAO. Mr Carpenter did step down from one such appointment for the duration of the Review.

## 2.4 Review Process

The Terms of Reference for our Review are expressed in broad terms and are not prescriptive or limiting in nature. We have taken an expansive approach to the Review, having regard to the scope, methodology and matters to be taken into account. Our approach has also been consultative, and has been based on extensive interviews, meetings, discussions and briefings, supplemented by our own research and investigations.

Key elements of our Review were as outlined below.

### 2.4.1 Consultations with the QAO

Throughout our Review, we at all times received the utmost cooperation and assistance from the Auditor-General, the Deputy Auditor-General and other staff of the QAO. Our consultations with the QAO included the following:

- Initial meetings with the Auditor-General and with the EMG as a group.
- Subsequent meetings with the Auditor-General and with individual members of the EMG.
- A series of six group sessions with members of staff, as well as one-on-one meetings with a small number of individual staff members, where requested. The group sessions involved around 8–12 staff members, centred around the major functional teams of financial and compliance audits, PMS audits, APQ and Audit Support, with the groups comprising a broad cross-section of staff, in terms of classification level, gender, age and experience. There was a high level agenda set as a discussion-prompter, but the sessions were flexible and interactive, with free-flowing discussion, and the opportunity for each participant to comment at both the beginning and the end of each session on particular issues of importance to them.

- One-on-one meetings with former staff members. A letter was sent to former staff members, at their last known address, inviting them to make written submissions and/or seek a personal interview with the Reviewers. A small number of former staff members availed themselves of this opportunity.
- Meetings with the Staff Welfare Committee and the Women's Leadership Group.
- Briefings by the Auditor-General and other staff members on specific topics which we nominated for intensive analysis. Topics covered in these briefings included IPSAM, ASPIRE, eTrack, Lominger, LaunchPAD, contract auditing, fees and cost recovery, and the resource allocation model.
- A formal process of Questions and Answers submitted by email, which enabled us to receive written responses on specific issues requiring clarification, elaboration or additional information as we compiled our Report.
- Checking of the factual content of drafts of sections of our Report by the QAO.

#### 2.4.2 Consultation with stakeholders

We also received wholehearted cooperation from all stakeholders with whom we consulted during our Review. These consultations included the following:

- Initial and subsequent meetings with the Director-General, Department of the Premier and Cabinet.
- Regular progress report meetings with officers of the Department of Premier and Cabinet.
- Interviews with around 35 stakeholders, including the PAPWC, the Treasurer and the Minister for Transport, the Under Treasurer, other Accountable Officers, government owned corporations, statutory bodies, universities, a grammar school, a special purpose vehicle, local government and contract auditors. These stakeholders were selected to provide a representative cross-section of interests amongst audit clients, contract auditors and other parties. The interviews included regional visits to Toowoomba, Rockhampton, Woorabinda, Townsville and the Gold Coast.
- An interstate visit to meet with Auditors-General in New South Wales and Victoria, and officers of the Australian National Audit Office in Canberra. (We did not visit other jurisdictions, but we have undertaken desktop investigations into the audit functions in other jurisdictions in Australia, as well as New Zealand.)

#### 2.4.3 Research and Investigations

We supplemented the above consultations with our own intensive research and investigation of key issues and areas of concern. This included:

- Detailed examination of a selection of audit files, including financial and compliance audits, PMS audits and cross-sector audits. The list of audit files which we examined is included as Attachment C.
- Review of published reports of the QAO, including Annual Reports and Reports to Parliament.
- Review of reports of the PAPWC and its predecessor, the Public Accounts Committee, pertaining to the QAO.
- Analysis of a substantial volume of internal papers, documents, reports and briefings provided by the QAO, including the Strategic Plan, the Annual Work Plan, the resource allocation model, strategic financial model, annual budget and financial

statements, quality assurance reports on audit activity, EMG minutes, administrative advice circulars, human resources and other internal policies and procedures, staffing lists and classifications and job descriptions.

Our investigations have also benefitted greatly from access to the following reports provided by the QAO, which we have referred to extensively throughout our Report:

- ACAG benchmarking reports prepared by Orima Research.
- The Pulse Staff Surveys undertaken by Quantum.
- The Thomson Report, *Governance and Audit Framework for Self Assessment and External Review, External Review of the Queensland Audit Office, 30 September–2 October 2009*, undertaken by Ms Sandy Thomson.

The Thomson Report is a valuable assessment of governance issues for the QAO, and we generally endorse the findings and recommendations in that Report.

Finally, we also commissioned Mr Henry Smerdon, one of the Reviewers from the 2004 Review, to undertake a short quality review of our proposed Report, prior to finalisation.

## 2.5 Compliance with Terms of Reference

We have diligently ensured that we have addressed all aspects of the Terms of Reference during our Review. To this end, Section 1.3 of our Report provides a helpful cross-reference between the Terms of Reference and the relevant Sections of our Report in which they have been addressed.

## 2.6 Proposed Report Consultation Process

As noted in Section 2.1 above, there is a formal consultation process required prior to the completion of our Report on the Strategic Review. In accordance with Section 70 of the *Auditor-General Act 2009*, we provided a Proposed Report to the Premier and the Auditor-General on 4 February 2010.

During the 21 day consultation period provided for in the legislation, we held discussions with the Auditor-General and also with representatives of the Department of the Premier and Cabinet (on behalf of the Premier) on the contents of our Proposed Report. We have carefully considered their comments and have agreed on some revisions and modifications in finalising our Report. These changes have not materially altered our key conclusions and recommendations, or the broad thrust of our Report.

Both the Premier and the Auditor-General have provided formal written responses within the 21 day consultation period, and these responses have been included as Attachments H and I respectively of our Report. We note that the issues raised in these responses have been the subject of various discussions with us during the course of our Review. We are encouraged that the Auditor-General is already in the process of implementing a number of our recommendations that have been discussed with him.

## 2.7 Acknowledgements

We have highly valued the assistance of a large number of people during our Review. Our acknowledgements are outlined in Attachment G.

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## 3. LEGISLATIVE FRAMEWORK AND ROLE OF THE QAO

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### 3.1 Previous Legislative Framework

Prior to 2009, the functions of the Auditor-General were established under the provisions of Parts 5 and 6 of the *Financial Administration and Audit Act 1977*.

### 3.2 Auditor-General Act 2009

A new *Auditor-General Act* came into effect as from 1 July 2009 which sees the functions and powers of the Auditor-General consolidated into a separate stand-alone act. The purpose of the Act is to provide the statutory basis for the Queensland Auditor-General and the QAO to undertake independent audits of the State's public finances and all public sector entities.

There are no significant changes to the role and responsibilities of the Auditor-General under the new Act compared with the provisions of the previous *Financial Administration and Audit Act*. For example, provisions relating to the scope of the Auditor General's mandate, the staff of the QAO, and the conduct of audits and related matters all remain unchanged.

Most importantly, the independence of the Auditor-General is preserved by Section 8 of the Act, which provides that the Auditor-General is not subject to direction by any person in relation to audit matters. It is noted that Section 35 of the Act provides that the Auditor-General must conduct audits at the request of the Legislative Assembly. In principle, this could compromise the independence of the Auditor-General. However, based on our investigations, we are not aware of any audit requests from the Parliament going back at least to 1984.

Under Section 58, the Auditor-General is required to provide reports to Parliament on auditing standards. The most recent *Auditor-General of Queensland Auditing Standards* are dated April 2007.

### 3.3 Financial Accountability Act 2009

The *Financial Accountability Act* also commenced with effect from 1 July 2009 and replaced, amended and updated relevant sections of the former *Financial Administration and Audit Act 1977*. The Act adopts a principles-based approach, with a reduced level of prescription and a greater focus on outcomes rather than process.

As a result, there is greater flexibility for agencies on how requirements are implemented and greater reliance is placed on subordinate legislation, supporting policies, processes and procedures documented by agencies. The Act is supported by the:

- Financial Accountability Regulation 2009
- Financial and Performance Management Standard 2009
- Financial Accountability Handbook
- Various policy/guidance documents.

The new Act provides a comprehensive and rigorous framework which sets standards of financial accountability relevant to modern public administration. Appropriately, there is a greater onus of responsibility placed on individual agencies to be accountable for their actions. This will require agencies to:

- ensure appropriate policies and procedures are in place
- provide documentary or other evidentiary support for decisions made
- undertake regular reviews and assessments of outcomes

From an audit perspective, areas which will require a particular focus include:

- internal controls and resource systems in agencies
- management actions to assess compliance and identify changes required to ensure compliance
- appropriate internal governance processes, such as documentation and approval of key assessments and decisions
- updates of FPMS.

We note that there is a change in emphasis and context given to the principle of “*value for money*” in the new legislation. In this regard, Section 36 of the former *Financial Administration and Audit Act 1977* required Accountable Officers to:

- “*manage the department efficiently, effectively and economically*”
- “*as far as possible having regard to the limits of the accountable officer’s powers and control, ensuring reasonable value is obtained for moneys expended for delivering departmental services and purchasing, developing and augmenting assets of the department.*”

Only the former point remains in the *Financial Accountability Act 2009* and the *FPMS 2009*. The requirement in the former Act to ensure reasonable value is obtained for moneys expended has not been carried over to the new Act. Instead, there is a reference in the FPMS to “*achieve reasonable value for money*” for expenses managed within the “*expense management system*” established.

In our view, this represents a subtle change of emphasis of the financial management standards to be applied by entities, and against which the Auditor-General is required to assess compliance. There is still the obligation in the new Act for accountable officers and statutory bodies to ensure operations are carried out “*efficiently, effectively and economically*”, but these concepts are potentially more narrow and limiting in their application.

Value for money is a more comprehensive and all-encompassing concept, as it extends to considerations such as whole-of-life costs and opportunity costs, as well as non-cost factors such as fitness for purpose, quality, service and support, reliability and sustainability considerations. It is an assessment as to whether or not an organisation has obtained the maximum benefit for the goods and services it both acquires and provides, within the resources available to it. Value for money involves a judgment as to the extent of the benefit (in both quantitative and qualitative terms) derived from provision, processes or outcomes against the monetary cost of making the provision, undertaking the process, or achieving the outcome.

Part 2, Division 1 of the *Financial Accountability Act 2009* requires the Premier from time to time to prepare and table in Parliament a statement of the community objectives of government, and for the Treasurer to prepare and table in Parliament a charter of fiscal responsibility. These are matters which potentially could form part of the audit mandate, and are considered further in Section 16 of this Report.

The Act makes provision for the roles of Chief Finance Officer (Section 77) and Head of Internal Audit (Section 78) with powers delegated from the Accountable Officer in relation to defined “*minimum responsibilities*”. These provisions are applicable to the QAO, as with other public sector entities, and have implications for reporting lines to the Auditor-General, as discussed in Section 8 of our Report.

### 3.4 Role of the QAO

The primary role of the Auditor-General is to audit the Consolidated Fund and all public sector entities, as outlined in the *Auditor-General Act 2009*.

The Auditor-General, supported by the QAO, has a long history in Queensland, extending back to shortly after the founding of Queensland as an independent colony in 1859. Specifically, the first Auditor-General, Henry Buckley, was appointed in 1860 and this established a line of Auditors-General under that title through to the current Auditor-General Glenn Poole, who is Queensland's 21st Auditor-General.

Over the past 150 years, the audit approach and audit methodologies have developed significantly in response to the changing environment. However, some things never change – particularly the role of the office as an independent body providing assurance of public sector accountability and performance to Parliament has not changed.

The QAO has developed a reputation as a strong independent office providing high quality independent audit services with the Queensland Parliament as its principal client. This proud and long-standing reputation was confirmed consistently by stakeholders during our Review.

Above all else, the Auditor-General and the QAO form a fundamental element of the integrity and accountability framework of the Queensland public sector. Matters of integrity and accountability routinely attract strong public and community interest, as has recently been the case in Queensland, resulting in a number of initiatives from the Queensland Government.

### 3.5 Role of Auditing in the Public Sector

In the past five years since the last Review, there have been significant changes in the auditing profession which have directly impacted on the role of the Auditor-General. The development of “force of law” auditing standards for application across both the private and public sectors has been a significant development and one which has meant that overall the cost of auditing has increased for audit clients in all sectors of the economy.

The auditing function within the public sector encompasses a number of different types of audits, with the Auditor-General performing the role of providing independent assurance services to Parliament. This includes what is generally referred to as external audit, in which the Auditor-General provides an auditing process for clients external to the body subject to audit.

Audit processes other than external audit can be categorised as follows:

- Internal audit – in Queensland under the Financial and Performance Management Standard, all government departments must establish an internal audit function. Each statutory body must also establish an internal audit function if directed by the Minister or if the body itself considers it appropriate to establish an internal audit function. The recently enacted *Financial Accountability Act 2009* also provides statutory recognition to the role of the Head of Internal Audit. Internal Audit is an internal service and aims to provide an objective audit service, independent of the area being reviewed, in support of the accountable officer or the statutory body.
- Audit Committee – the Financial and Performance Management Standard mandates an Audit Committee for all departments and notes that a statutory body may establish an Audit Committee. The Audit Committee must have terms of reference and in establishing the Committee the Accountable Officer or the statutory body must have regard to the “Audit Committee Guidelines – improving accountability and performance” as issued by Queensland Treasury. In addition to monitoring the internal audit program and reviewing responses to internal audit reports, Audit

Committees are an important forum for review of reports/management letters from the Auditor-General.

- Probity Audit – in recent years, there has been an increased use for probity auditors or advisors to observe and review the procurement processes of complex, sensitive or high value procurement activities. The probity auditor/advisor will provide opinions and guidance on probity risks and issues arising during the procurement process. The probity auditor/advisor will provide probity reports at key stages in the procurement process. These services can be provided by the private sector although a number of internal auditors within government departments in Queensland are now providing that service. Probity audit does not have any statutory basis.
- Probity reviews or investigations – in addition to formal probity audit/advisory roles, it is possible for specific reviews or investigations into probity or propriety to be undertaken for the accountable officer or the statutory body. In addition, in accordance with the *Auditor-General of Queensland Auditing Standards*, the QAO may undertake a review of probity or propriety.
- Other audit process including quality review – there are a range of other audit or review processes that can be engaged by public sector entities to provide an independent review to management including those of a quality review nature.

For all of these activities, the Auditor-General will seek to take into account the work of internal audit, probity auditors/advisors and other review processes provided they meet certain standards acceptable to the Auditor-General. The Auditor-General needs to assess the quality of the work of the internal auditor in line with Auditing Standard ASA 610 *Considering the Work of Internal Audit* to assess whether the work of internal audit can be relied upon for external audit purposes. Similarly, for other review processes, Auditing Standard ASA 620 *Using the Work of an Expert* provides the means whereby the external auditor, after assessing the quality of the work undertaken by the expert, may rely upon the outcomes of the expert's work for the purposes of external audit.

In relation to the audit function performed by the QAO in Queensland, there has been a number of significant developments since the 2004 Review, the most important of which are mentioned below:

- Amendment of legislation to provide the power of the Auditor-General to review a public sector entity's performance measures as part of a PMS audit, and to express an opinion as to whether the performance measures are relevant and otherwise appropriate, having regard to their purpose, and fairly represent the public sector entity's performance.
- Significant developments in audit methodologies and systems, including IPSAM and ASPIRE, which incorporate electronic working papers to support audit service delivery.
- Expanded use of private sector contract auditors to meet the additional needs of auditing within "force of law" auditing standards and to meet the tightened reporting timelines for many of the public sector entities subject to audit.
- An increase in the number of PMS audits undertaken in response to recommendations arising from the 2004 Review.

These developments are discussed in more detail in the following sections of this Report.

## Conclusions

### *CN.3(i)*

The position of Auditor-General is a critical element of the integrity and accountability framework for Queensland and the QAO is a well respected independent audit office with a long history of providing reliable external audit services to Parliament in a highly professional manner.

### *CN.3(ii)*

The new *Financial Accountability Act 2009* and *Auditor-General Act 2009* provide a comprehensive and rigorous framework for financial management and accountability of the public sector in Queensland, but this could be strengthened by giving enhanced emphasis to the fundamental principle of value for money, as previously articulated in the former *Financial Administration and Audit Act 1977*.

## Recommendation

### *RN.3(i)*

**Reflecting the importance of value for money as a fundamental over-arching principle of financial management, that the Auditor-General consult with the Treasurer on including value for money in the primary legislation, being the *Financial Accountability Act*, rather than the *Financial Management Performance Standards*, where it currently sits.**

## 3.6 Better Practice Guides

Central agencies of the Queensland Government have the primary responsibility to ensure that appropriate standards and guidelines are issued in support of financial and performance management.

In addition, over the past three years, the QAO has developed and issued three Better Practice Guides as follows:

- *QAO Guideline – Accounting for QTC Onlending Products and Debt Restructure* (March 2007)
- *Better Practice Guide – Risk Management* (October 2007)
- *Checklist for Organisational Change* (March 2009).

From the feedback we received, audit clients appreciate such guidance or practice material developed by the QAO.

Better practice principles or better practice case studies are also included in most PMS audit reports to Parliament to provide guidance for all relevant public sector entities, not just those included in the audit. This is particularly relevant where the audit topic covered a number of entities with different audit results a separate guide is only prepared in those instance where it is considered that it is necessary to assist agencies with understanding the issue and the implementation of better practice.

We noted some recent better practice guides or equivalent have been issued in other jurisdictions, such as:

- *Innovation in the Public Sector* (ANAO December 2009),
- *SAP ECC 6.0 Security and Control* (ANAO June 2009),
- *Business Continuity Management – Building Resilience in Public Sector Entities* (ANAO June 2009),

- *Developing and Managing Internal Budgets (ANAO June 2008),*
- *Monitoring and Reporting on Audit Recommendations (NSWAGO May 2009),*
- *Fraud Control Improvement Kit (NSWAGO July 2006) and*
- *Public Sector Procurement: Turning Principles into Practice (VAGO October 2007).*

We recognise that it is not the primary responsibility of the Auditor-General to develop and issue Better Practice Guides. Nevertheless, in undertaking its normal auditing responsibilities, the QAO generally will be well placed to identify areas of better practice, and also to identify those areas where there may be a gap in terms of relevant standards or guidelines issued with authority in Queensland.

Conclusion

*CN.3(iii)*

The QAO should continue to develop Better Practice Guides where there is a demonstrated need and the QAO is in a position to develop such guidance especially where better practice is identified as part of undertaking an audit.

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## 4. FINANCIAL AND COMPLIANCE AUDITS

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### 4.1 Auditing Standards

Under Section 58 of the *Auditor-General Act 2009*, there is a requirement for the Auditor-General to prepare a report to the Legislative Assembly setting out the general standards that the Auditor-General intends to apply.

These standards are outlined in the publication *The Auditor-General of Queensland Auditing Standards*, last issued in April 2007. They express the minimum standard of audit work expected of auditors undertaking work on behalf of the Auditor-General.

It should be noted that there are some differences in the approach adopted to auditing in the public sector from that of the private sector. There is an additional focus on matters of probity and propriety which does bring with it an additional audit cost. This additional focus in public sector auditing is to cover an expectation of Parliament that there is a need for public sector entities to meet a higher standard of behaviour in terms of probity and propriety.

We note that the Auditor-General quite appropriately has sought to highlight those areas of public sector auditing which are additional requirements over and above the requirements of general auditing standards. In this regard, the auditing standards note that, in addition to an attestation audit over information included in prescribed financial reports, public sector auditing also includes:

- reviewing the probity and propriety of matters associated with the management of public sector entities
- assessing compliance with relevant acts, regulations, government policies and other prescribed requirements
- determining whether performance management systems of public sector entities enable them to assess whether their objectives are being achieved economically, efficiently and effectively
- reviewing performance measures adopted by public sector entities and assessing whether they are relevant and fairly represent entity performance, and
- reporting to Parliament on matters of significance arising from audits or relating to the Auditor-General's activities.

In reviewing these standards, we consider that they provide a sound basis for public sector auditing in Queensland. However, we consider that explicit reference should be made to the issue of waste of public resources. Arguably, we acknowledge that this matter could already be covered, at least implicitly, through the standards relating to probity and propriety associated with management generally.

However, several other jurisdictions have seen fit to draw specific attention to this issue. For example, in regard to performance audits, the New Zealand Controller and Auditor-General has identified that any act or omission that might give rise to a waste of public resources can be part of the examination of the audit. Also, the New South Wales *Public Finance and Audit Act 1983* provides for a public official to advise of any instance of waste of public moneys to the Auditor-General. The Auditor-General may then consider whether to undertake a review of the complaint made.

Accordingly, we consider that there would be benefit in incorporating in the standards a provision that an audit may include examining any act or omission that might give rise to a waste of public resources.

## Conclusions

### *CN.4(i)*

The Auditing Standards issued by the Auditor-General represent a sound basis for the audit function of the QAO, including for contract auditors.

### *CN.4(ii)*

The QAO Auditing Standards should include a provision related to any act or omission that has given rise to a waste of public resources.

## Recommendation

### *RN.4(i)*

**The QAO Auditing Standards be revised to incorporate a provision that any act or omission that has given rise to a waste of public resources can be part of the examination of an audit.**

## 4.2 IPSAM

The *Auditor-General Act 2009* provides a range of responsibilities of the Auditor-General including the following legislated requirements:

- Section 39 – Audit of consolidated fund accounts
- Section 40 – Audit of public sector entities
- Section 41 – Audit of expenditure of ministerial offices; and
- Section 42 – Audit of consolidated whole-of-government financial statements

In line with these responsibilities, the Auditor-General undertakes a range of audit assignments under the general heading of financial and compliance audits. This has long been the core function of the QAO. Financial and compliance audits still represent some 89% of the total workload of the QAO, notwithstanding the expanded role of PMS auditing over the last few years.

In order to meet his statutory responsibilities, the Auditor-General has developed a risk-based audit methodology known as IPSAM, which replaced the previous methodology known as TeamAsset. IPSAM is a fully integrated lotus notes application which provides for electronic documentation and review of financial and compliance audits. During our Review, we received a detailed briefing from the QAO on the development and application of IPSAM.

The IPSAM methodology has been a joint development between the QAO and the VAGO and was implemented in the QAO in November 2005. The system has recently been licensed to Australian Capital Territory and Tasmania, and is currently being trialled in South Australia and Western Australia.

The data bases are mapped to current Australian Auditing Standards and provide 80 individual policy and guidance statements. The system outlines primary source of requirements (policy) that must be met in the conduct of a financial audit. In addition, guidance is provided to assist in meeting those policy requirements.

The system incorporates a range of standard forms and templates that are selected in tailoring the audit field work to meet the needs of the audit based on a risk assessed approach to the audit.

During our interviews with stakeholders, especially QAO staff, a number of comments were made about IPSAM. Overall, these comments were very positive and supportive about IPSAM. It is seen as a very sound methodology for public sector auditing, with a suitable focus on risk. The new version has been enthusiastically welcomed by staff. Specific comments were as follows:

- A suggestion that there should be a family structure established within IPSAM for audit clients which have a group structure.
- A concern about the cost of establishing an IPSAM file for small clients. (We note advice that the upgrade released in March 2009 better provides for establishing files for small clients.)

Our assessment is that IPSAM is a well structured and designed audit methodology, which is a valuable tool for conducting financial and compliance audits. The QAO is to be commended on its initiative in developing IPSAM jointly with the VAGO, and for its successful implementation within the QAO office environment.

Our only concern is that IPSAM may discourage original thought and result in the auditing process becoming too mechanistic. Auditors need to avoid the risk of undertaking solely a “tick and flick” exercise. In this regard, Auditing Standard ASA200 *Objectives and General Principles Governing an Audit of a Financial Report* requires in Section 20 the need for the auditor to “*plan and perform an audit by exercising professional judgement*”.

There needs to be an awareness by all auditors to continue to apply the highest professional standards in critically analysing the particular attributes, features and issues in individual audits ie IPSAM should be used as a powerful analytical tool, but should not reduce the need as stated in Section 21 of ASA200 for “*an attitude of professional scepticism recognising that circumstances may exist that cause the financial report to be materially misstated*”.

#### Conclusion

##### *CN.4(iii)*

IPSAM is a valuable audit methodology for financial and compliance audits which is consistent with Australian Auditing Standards and represents a sound basis for fulfilling the Auditor-General’s statutory audit responsibilities.

### 4.3 Review of IPSAM Files

During our Review, we undertook a specific examination of four financial and compliance audits for the financial year 2008–09. The audit client files which we examined in IPSAM were:

- The then Department of Education and Arts (now Department of Education and Training)
- Brisbane City Council
- University of Queensland
- QR

In our examination, we noted strong compliance with the methodology and noted that IPSAM provides a disciplined and well structured set of procedures and audit processes. We also observed that IPSAM provides an excellent methodology to ensure that all elements are cleared and that the quality review processes have been completed.

We did note that many of the items of correspondence e.g. engagement letters and client strategy documents were often mark-up versions in Word software. Also, it was not always clear if the version of the correspondence on IPSAM was the final version. For key items of correspondence, it would be preferable for items to be in PDF format to ensure no changes to the item.

A further issue was that responses from audit client to the final management letter were not always in the IPSAM file. For those that were provided, they appeared to be filed without any assessment as to the adequacy of the response. We did note that issues arising from prior year's audits are considered and assessed as part of the audit undertaken.

As a further process, high risk and selected medium risk audits are subject to an Engagement Quality Control Review. The framework for appointment of an Engagement Quality Control review is ASA 220 *Quality Control of Audits of Historic Financial Information* and APES 320 *Quality Control of Firms*. These reviews are undertaken by the Deputy Auditor-General in conjunction with two Assistant Auditors-General. We were provided with a report on quality assurance reviews and noted that there were only minor concerns of a housekeeping nature.

In accordance with QAO Policy G26 *Quality Assurance: Audits*, the QAO has a program of internal quality reviews of files with a program to ensure that all audit engagement leaders and team leaders are subject to review on a regular basis.

#### Conclusions

##### *CN.4(iv)*

Our review of IPSAM files for financial and compliance audits identified a high standard of compliance with the methodology.

##### *CN.4(v)*

There are some opportunities to improve the quality and security of record keeping. Specifically, IPSAM files should include clean versions of documents and, for key communications with audit clients, that these be saved as a PDF version once they become final.

#### 4.4 Cross-Sector Audits

In recent years, the Auditor-General has increased the number of cross-sector audits which are undertaken as financial and compliance audits. It is noted that, unlike PMS audits which are funded by appropriation, the cost of cross-sector audits is billed to audit clients who are included in the cross-sector audit.

Attachment E is a schedule of cross-sector audits which were included in reports to Parliament during 2008 and 2009. In our review of the quality of audits undertaken, we reviewed two of these audits, being on *IT Network Security* and *Understanding and Complying with Legislation*, both of which formed part of Report No 4 of 2009 tabled on 30 June 2009.

Whilst generally undertaken as financial and compliance audits, it is noted that cross-sector audits are best managed within the QAO by utilising the system ASPIRE (which has been developed for PMS audits). We support the decision of the Auditor-General to utilise ASPIRE rather than IPSAM for cross-sector audits, as they are more broad-ranging and less structured in terms of the methodology applied.

In so doing, a decision will be necessary upfront at the scoping stage to determine the extent to which the full ASPIRE methodology is appropriate for the proposed cross-sector audit.

This should be articulated in the internal audit strategy memorandum and driven by a risk assessment related to the individual audit.

However, it will be essential that individual audit client information which impacts on the internal control environment also be linked to the relevant IPSAM file for the individual audit client(s). This will also be important in terms of follow up of actions arising from the recommendations of the cross-sector audit.

In our examination of cross-sector audit files, we noted that the field work for the *IT Network Security* audit was undertaken utilising IPSAM. This was then brought together into a hard copy file to consolidate the findings and report for Parliament. In the future, the Auditor-General desires to use ASPIRE to manage, document and control the entire audit process, including the elements related to the reporting to Parliament.

We also examined the cross-sector audit on *Understanding and Complying with Legislation*. In this instance, the audit was undertaken through a combination of ASPIRE and hard copy files. Again, there was the issue as to whether all of the ASPIRE methodology was appropriate for an audit of this nature, although certain elements including quality review should be mandated for all audits including cross-sector audits.

#### Conclusions

##### *CN.4(vi)*

There are benefits in terms of improved public administration from the QAO undertaking cross-sector audits of a financial and compliance nature.

##### *CN.4(vii)*

The decision of the Auditor-General to utilise ASPIRE for cross-sector audits is appropriate, noting that effective cross-linking to IPSAM for individual audit clients will be essential.

## 4.5 Information Systems Audits

The QAO has recognised the importance of having specialist IS audit expertise in fulfilling its audit responsibilities. It is noted that an Information Systems audit team has existed in the QAO since the late 1970s.

Currently, the QAO has an IS audit section to perform specialist information systems audits where significant financial systems and information technology infrastructure is maintained.

The IS audit section has developed a comprehensive audit methodology, which is embedded in the IPSAM audit software package. We noted that a review of IS audit methodology was undertaken by Professor Peter Green for both the QAO and the VAGO. The review was designed to address the question as to the adequacy of the information systems audit framework.

In his Report in January 2008, Professor Green found that in general the QAO has set an adequate information systems audit framework that derives its basis from the relevant “force of law” auditing standards. Professor Green also indicated that the use of a risk-based approach follows generally accepted “best practice” in this area. The review made a number of recommendations to further improve the framework for delivery of information systems audits, which we note have been considered in the further development of the audit methodology and guidance material.

An important development within the Queensland public sector in recent years relates to the consolidation of all major departmental ICT functions within the Department of Public Works (DPW). This initiative commenced with the creation of a shared service environment,

which now entails separate business units of DPW being responsible for implementing and managing the ICT infrastructure (CITEC), and maintaining and supporting a range of financial and human resource systems (CorpTech). The transactions being processed through these systems relate to payroll, rostering, purchasing, inventory management, asset management, accounts payable and receivable, and other corporate functions. In addition, the recent Machinery of Government changes have resulted in further consolidation and standardisation of ICT infrastructure. These and other developments reinforce the need for a strong information systems audit capability at the QAO.

The IS audit methodology adopted by the QAO seeks to ensure that there is a risk based approach to auditing within the Information Systems environment. This includes assessment of IT governance and IT general controls, including security, change management, project management, systems development and implementation, computer and data centre operations, vendor and contract management, business continuity as well as application controls within systems. The aim is to ensure that the quality of information included in financial statements is sound from an audit perspective. Most of the Shared Services arrangements are heavily based on IT systems, which necessitates the need for use of specialised IT audit services as provided by the IS audit section of the QAO.

The IS audit section has scheduled for a number of cross sector audits in 2009–10 on the following topics:

- IT Program Management
- IT Governance
- Compliance with Queensland Government Information Standard No 2
- Management and Security of Patient Information at Queensland Health.

The IS audit section also develop an annual plan of financial and compliance IS audits. The IS audit section works closely with the financial and compliance audit teams in integrating information systems audits as part of their broader audit task.

We note that the ISA section is now involved in further cross-sector audits, and we support further involvement of IS audit methodology in all types of audits undertaken by the QAO, including PMS audits, as required.

#### Conclusion

##### *CN.4(viii)*

The QAO has established a strong team of Information Systems auditors who operate within a sound Information Systems audit methodology and provide a valued service as part of financial and compliance audits and in undertaking a number of cross-sector audits. The further involvement in cross-sector audits and also with PMS audits means that the methodology ASPIRE will be utilised for those audits in the future and the staff will need to be familiar with the policies and guidance from that methodology.

## 4.6 Conduct of Audits

Section 37 of the *Auditor-General Act 2009* provides a power for the Auditor-General to conduct an audit in the way the Auditor-General considers appropriate. In so doing, the Auditor-General must have regard to the character of the internal control system for the entity, including internal audit. In addition, the Auditor-General must have regard to recognised standards and practices. This section provides the Auditor-General with considerable flexibility as to how he/she conducts an audit.

More broadly, the Auditor-General has the power to undertake audits of all public sector entities and must audit the consolidated fund and all public sector entities (other than the QAO itself and any body which is exempt by regulation from audit by the Auditor-General).

As an example of how this flexibility may be applied, in October 2009 the Auditor-General announced an immediate audit of the contractual agreements in relation to the A1Grand Prix component of the 2009 SuperGP. The Auditor-General took a decision to bring forward part of the normal audit process following significant public interest in the withdrawal of the A1Grand Prix event. A report arising from this review was tabled in Parliament in February 2010 (Report to Parliament No.1 for 2010 on *Audit of A1Grand Prix Agreements*).

We have been advised that in the past the Premier has requested audits to be undertaken in particular areas eg. risk management. In such instances, after consideration of the request and other factors, audits have been completed under terms of reference determined by the Auditor-General in accordance with his powers, with the results published in a report to the Parliament. This is consistent with the Auditor-General's approach to requests from any source.

Section 35 of the *Auditor-General Act 2009* provides a power whereby the Legislative Assembly by resolution may request an audit of a matter relating to the financial administration of a public sector entity, and the Auditor-General must conduct the audit. Our enquiries found that this power has not been exercised by the Legislative Assembly in the last 25 years.

Section 96 of the *Parliament of Queensland Act 2001* provides power for the PAPWC to refer issues within its area of responsibility to the Auditor-General for consideration.

In our discussions with the ANAO, we noted that the Commonwealth Auditor-General has full discretion as to whether to undertake a performance audit, although there is a requirement to have regard to the audit priorities of the Parliament, as determined through the Joint Committee of Public Accounts. The Commonwealth Auditor-General cannot be directed in relation to his/her functions.

We noted also that there was a recent example of the Commonwealth Auditor-General deciding to undertake a performance audit, following correspondence from the Prime Minister. The audit was on the *Representations to the Department of the Treasury in relation to the Motor Dealer Financing Arrangements*.

We note that the enhanced public concerns about integrity and accountability in government may give rise to the need for, or pressure for, more audits of a special nature or public interest to be undertaken. In such circumstances, the Auditor-General will need to give consideration as to the merits of the case for such an audit. This has the potential to impact on the resourcing needs of the QAO, although such audits tend to be one-off and infrequent in nature.

In previous instances, the Auditor-General has sought and received additional funding for such reviews from the Consolidated Fund Appropriation.

#### Conclusion

##### *CN.4(ix)*

There are sufficient existing powers for the Auditor-General to respond to emerging needs for audits of a special or an ad hoc nature. The Parliament has the power by resolution to direct the Auditor-General to undertake an audit, although we are not aware of any instances where such a power has been used. In addition, the PAPWC may refer issues to the Auditor-General for consideration.

## 4.7 Reporting to Parliament

In addition to providing an opinion on financial statements for all departments, statutory bodies, local governments and other public sector entities, the Auditor-General also provides reports to Parliament. It is noted that Annual Reports of public sector entities which are required to be tabled in Parliament will incorporate audit opinions of the entities concerned.

A recent example of a Report to Parliament is No 8 for 2009 on *Results of Audits* at 31 October 2009 (Tabled 12 November 2009). This report on financial and compliance audits provides a status report on 2008–09 financial statement audits of departments, statutory bodies, government owned corporations and their controlled entities completed as at 31 October 2009. At that stage, auditors' opinions for 2008–09 had been issued for 351 public sector entities. The report noted that of 207 entities required to have auditors opinions issued by 31 August 2009, 88% were able to achieve the statutory deadline. The report also summarised details of modified auditors' opinions issued.

The report also covered a number of key audit findings including the following:

- Federal Government stimulus package
- Infrastructure project procurement
- Changes to the State's financial accountability framework
- Recognition of land under roads
- Asset accounting issues in price regulated industries
- Impact of the Independent Review of Queensland Government Boards, Committees and Statutory Authorities.

Other reports tabled in Parliament during calendar year 2009 were as follows:

- Report No 1 for 2009, *Results of Local Government Audits* (Tabled 20 May 2009)
- Report No 4 for 2009, *Results of Audits at 31 May 2009* (Tabled 30 June 2009)

We have reviewed a number of recent reports to Parliament and are satisfied that the reports are comprehensive and informative, and provide an appropriate guide as to the status and program of financial and compliance audits.

We are also of the view that the Auditor-General's reports to Parliament are acceptable in terms of readability, although this is a matter that requires ongoing attention to ensure quality is maintained and enhanced over time.

### Conclusions

#### *CN.4(x)*

The process for reporting to Parliament on financial and compliance audits including cross-sector audits is sound and appropriate.

#### *CN.4(xi)*

The Auditor-General's reports to Parliament are acceptable in terms of readability.

## 5. PERFORMANCE MANAGEMENT SYSTEMS AUDITS

### 5.1 Legislative Context

Section 38 of the *Auditor-General Act 2009* provides a power for the Auditor-General to undertake an audit of performance management systems. This may be conducted as a special audit or as part of another audit under this section.

Section 38(3) indicates that:

*“the objective of the audit includes deciding whether the performance management systems enable the public sector entity to assess whether its objectives are being achieved economically, efficiently and effectively”.*

In undertaking the audit, the Auditor-General must have regard to prescribed requirements relating to the establishment and maintenance of performance management systems that apply to the public sector entity.

Under Section 38(6), the audit may include a review of the entity’s performance measures. This represents a new power since the 2004 Review, and is an important expansion in the mandate of the Auditor-General. It came into effect as from January 2007.

Under Section 38(7), the Auditor-General may state whether in his/her opinion the performance measures –

- (a) are relevant and otherwise appropriate, having regard to their purpose; and*
- (b) fairly represent the public sector entity’s performance.”*

It is noted that the power related to performance measures is not a power which can be exercised in relation to financial and compliance audits.

### 5.2 PMS Audits 2005–2009

The 2004 Review made a number of recommendations related to PMS audits, including that

- a three-year plan be developed in consultation with the then PAC to undertake at least 20 targeted PMS audits across the public sector
- the PAC undertake a detailed scrutiny of the PMS audit reports when completed
- the PAC evaluate the value of the PMS audits at the end of the three-year period and report on the effectiveness of the PMS audit mandate.
- An appropriate level of resources be provided to the QAO to enable the plan to be fully implemented.

These recommendations were generally accepted by the PAC and the Government, subject to elimination of the proposed targets.

The PAPWC currently has in train an *Inquiry into an Evaluation of the Effectiveness of the Performance Management Systems (PMS) Audit Mandate*, in terms of the Parliament’s previously expressed position. It is not expected that the PAPWC report will be completed prior to the completion of our Review, so we are unable to take account of the findings of the PAPWC as envisaged by our Terms of Reference. However, we have had regard to the transcript of the public hearings for the Inquiry, and we have met with the Chair of the PAPWC to discuss this and other matters on two occasions during our Review.

Since the 2004 Review, the Auditor-General has been provided with additional resources for PMS audits. Attachment D lists the PMS audits reported to Parliament since 2005. On a calendar year basis, the number of such audits has been as follows: two (2005), four (2006), five (2007), six (2008) and five (2009).

Conclusion

*CN.5(i)*

The QAO is to be commended for the increased attention to undertaking PMS audits and reporting to Parliament on the results of these audits.

The QAO has applied the expanded power to review the public sector entity's performance measures as part of the following PMS audits:

- *Are departmental output performance measures relevant, appropriate and a fair representation of performance achievements?* (Report No 4 for 2007)
- *Enhancing Accountability through Annual Reporting* (Report No 1 for 2008)
- *Management of Rural Fire Services in Queensland* (Report No 3 for 2008)
- *Transport Network Management and Urban Congestion in South East Queensland* (Report No 3 for 2009)
- *Management of Patient Flow through Queensland Hospitals* (Report No 5 for 2009)
- *Follow-up on government owned corporation and budget sector performance measurement and reporting* (Report No 7 for 2009). (It should be noted that this is in part a follow up on an audit reported on in 2006 — prior to the expanded performance measures powers for the Auditor-General. It also follows up on the extent to which the May 2009 publication "*A Guide to the Queensland Government Performance Management Framework*" addresses recommendations made since 2005 on performance management and reporting by departments.)

These audits demonstrate application of the new powers in this area and have included a range of recommendations for departments, government owned corporations and other public sector entities in the area of performance measurement and performance reporting.

Section 38(7) of the *Auditor-General Act 2009* does indicate that in a report prepared for the audit, the Auditor-General may state whether in the Auditor-General's opinion, the performance measures are relevant and otherwise appropriate, having regard to their purpose, and fairly represent the public sector entity's performance. The reports noted above do not directly report on any individual public sector entity's performance measures.

Conclusion

*CN.5(ii)*

The Auditor-General has applied the expanded PMS mandate on performance measures in a number of PMS audits in the last three years. To date, however, the Auditor-General has not utilised the power to provide opinions on performance measures for individual public sector entities as part of PMS audits reported to Parliament.

**Recommendation****RN.5(i)**

**That the Auditor-General, in undertaking PMS audits, give consideration to utilising the power to provide opinions on whether performance measures for individual public sector entities are relevant and appropriate, having regard to their purpose, and fairly represent that entity's performance.**

### 5.3 Performance Audit Standards – Development of ASPIRE

The Auditing and Assurance Standards Board has the authority to develop auditing standards in Australia and, in 2008, it issued standard ASAE 3500 on Performance Engagements which has application for engagements commencing on or after 1 January 2009. This replaced former standards AUS 806 *Performance Audits* (July 2002) and AUS 808 *Planning Performance Audits* (October 1995).

In order to meet those standards in undertaking PMS audits, the QAO initially used a cut-down version of IPSAM, but this has subsequently been transformed into what is now known as ASPIRE. The ASPIRE methodology outlines that the intention of PMS audits is to add value to the quality of public administration and to assist entities in the discharge of their governance obligations.

As part of our investigations, we were provided with a detailed briefing on ASPIRE by QAO staff. The first version of ASPIRE involved a fairly rudimentary shell or prototype. This has subsequently been upgraded and a new version of ASPIRE has been rolled out for 2009–10 audits, with significant enhancements from Version 1.

The Auditor-General has also determined that cross-sector audits will utilise the ASPIRE methodology, which we believe is appropriate. We note that linkages will be required to the IPSAM methodology to ensure appropriate input into the control framework for financial and compliance audits, and to allow for monitoring of actions arising from recommendations in cross-sector audits.

The ASPIRE methodology indicates clearly and appropriately that a PMS audit does not review or comment on Government policy.

A system within an entity or group of entities which is subject to a PMS audit can comprise a number of elements including:

- operational practices and procedures,
- organisational culture, and
- the external environment within which the entity operates.

### 5.4 Review of ASPIRE Methodology against Auditing Standards

We examined the ASPIRE methodology which will be utilised from 2009–10 against Australian Auditing Standards and in particular Standard ASAE 3500 *Performance Engagements*. Our examination concluded that overall the ASPIRE methodology complies with the requirements outlined in Australian Auditing Standards.

However, there were a number of issues of detail identified, as follows:

- The manual for ASPIRE does not incorporate cross-referencing to the auditing standards. We believe there would be benefits from having a mapping to auditing standards.

- Section P2.04 of ASPIRE relates to Strategic Audit Planning, and is used to identify a list of potential audit topics. This has regard to the QAO mandate on PMS audits, areas of focus identified in the Strategic Audit Planning process, input from the Auditor-General, input from the PAPWC and other significant and auditable topics. This is highly relevant to the selection of topics for PMS audits.
- Section P1.07 of ASPIRE relates to Liaison with the PAPWC. It refers to an effective working relationship, and notes the consideration of reports and annual reviews of PMS Audit reports by the PAPWC. However, it does not make any reference to how the QAO will interact with the PAPWC in regard to the Strategic Audit Planning process for PMS audits.
- Section 11 of Standard ASAE 3500 covers circumstances where there is an inability to comply with mandatory requirements – actions to be taken including alternate evidence gathering procedures and documentation in working papers of the circumstances, or reasons for inability to comply and justification for that. We noted that ASPIRE does not have a section covering these matters.
- Standard ASAE 3500 refers to the subject of “Using the work of an expert” and this is covered in ASPIRE Section P1.03 which identifies Australian Accounting Standard ASA620 on “Using the Work of an Expert”. We believe it would be beneficial for more information to be included on the processes to identify the need for experts for assignments, for appointing and managing experts and in assessing the quality of advice and other input provided for PMS audits.
- The ASPIRE methodology does not include a section on documentation as outlined in ASAE 3500.

#### Conclusions

##### *CN.5(iii)*

The ASPIRE methodology as revised for use from 2010 onwards represents a sound basis for undertaking PMS audits.

##### *CN.5(iv)*

The structure of the ASPIRE manual is not cross referenced to the auditing standards. There would be benefit in having a mapping to the auditing standards which would assist when standards are revised.

##### *CN.5(v)*

It would be beneficial to incorporate information on the processes to identify the need for experts for assignments, for appointing and managing experts and in assessing the quality of advice and other input provided for PMS audits.

## 5.5 Examination of ASPIRE Files

We also undertook a specific examination of the files of two recent PMS audits, being:

- *Transport Network Management and Urban Congestion in South East Queensland* (Report No 3 or 2009)
- *Management of Patient Flow through Queensland Hospitals* (Report to Parliament No 5 for 2009).

These audits were undertaken utilising the ASPIRE methodology, either in whole or in part, and in line with the policies and guidance issued by the Auditor-General for PMS audits. However, these audits were undertaken prior to the recent upgrade in the ASPIRE methodology which is now being utilised fully for PMS audits in 2009–10.

We were generally satisfied with our examination of these ASPIRE files, although there is room to improve aspects of file management and the quality reviews elements of the audits and these need to be fully documented within the ASPIRE system. Key points are:

- The need for the ASPIRE system to incorporate full details of the target dates to deliver the audit together with actual dates as well as information on actual hours against the budget for the elements of the audit
- The need to fully utilise the ASPIRE policy framework and methodology to assist in the management of the audit and to ensure that the standards for PMS audits are met.
- The need for appropriate documentation and cross-referencing of files, especially when the ASPIRE methodology is utilised in conjunction with hard-copy files.

## 5.6 Feedback on PMS Audits

During our interviews with various stakeholders, we received a number of comments on the process for undertaking PMS audits, as follows:

- The need for the QAO to develop an overall strategic audit plan for undertaking PMS audits and to consult with the Parliament through the PAPWC on this plan. This would include the opportunity for formal consultation on the proposed plan and for suggestions on audit topics for consideration by the Auditor-General. This issue is considered further in Sections 15 and 16 of this Report.
- A concern that the scope and work plans for the audit were not settled at the commencement of the audit task, and that changes in the objectives and scope of the audit occurred after commencement, sometimes without sufficient notification of such to the entities involved.
- An absence of preliminary discussions with the entities concerning the nature and purpose of the PMS audit. (We note that there has been recent changes in procedures adopted by the QAO to incorporate preliminary discussions with senior management of affected entities. This has been beneficial in terms of finalising the scope and objectives of PMS audits.)
- Instances of factual inaccuracies in drafts of a report at an advanced stage of the audit, which required significant changes to key elements of the report. There is a need to ensure that matters of fact are reviewed and confirmed, including with audit clients, at an earlier stage than the management letter stage. Errors of fact at such an advanced stage can give rise to concerns from audit clients as to the quality of the report overall.
- The need for the involvement of external independent subject matter experts during the entire audit process, rather than being at selective points as appears to be the case at present. In meetings with interstate Audit Offices, we were advised that subject experts tend to have a greater involvement over the entire course of the performance audit. In Queensland, the approach to date generally has been to involve a subject expert to undertake a review of the audit report whilst at an advanced stage, such as at the final draft stage. As an example, a subject expert was engaged by the QAO to undertake a review of the report on Transport Network Management and Urban Congestion in South East Queensland, without having been involved during prior stages of the audit process.

- A concern from some entities such as GOCs and universities as to whether they should be subject to PMS audits, given that they are subject to a range of other accountability and performance reporting requirements (including reporting to Boards/Councils). Representatives of GOCs operating commercially in a competitive environment also raised issues related to competitive neutrality if they are burdened with more onerous audit requirements than competitors.
- A need for a greater knowledge of and understanding about PMS audits amongst audit clients.
- More generally, a number of stakeholders argued that the mandate of the Auditor-General should be expanded to cover full performance audits, as is the case in most other Australian jurisdictions. This issue is addressed in more detail in Section 16 of this Report.

Having regard to this feedback and our own investigations, there are benefits for the QAO in having initial discussions with the Accountable Officer or Chief Executive Officer of the relevant audit client prior to finalising the scope and objectives of PMS audits. This has been occurring to some varying extent in more recent PMS audits, and has now been built into the ASPIRE methodology. We encourage this to be fully implemented as standard practice.

One of the major challenges for the QAO is to ensure that the team of internal staff together with external experts/advisers have the necessary depth of knowledge and understanding of the service area for a PMS audit. There is a need to give further attention to the way in which independent objective subject experts are to be involved with PMS audits, and especially the stage at which they are to be involved. Also, there is a need to ensure that such experts are genuinely independent and objective, and do not have particular biases in relation to the subject matter.

From our examination of a sample of PMS audits, we conclude that they are acceptable in terms of the quality of their content, but that the QAO should continually strive to improve that quality. We consider that the PMS audits provide valuable information to Parliament on the quality of performance management systems, and they are an important tool for Accountable Officers and Chief Executive Officers to guide improvements in public administration.

Finally, there is a need for greater awareness and understanding of the role and purpose for PMS audits amongst audit clients.

#### Conclusions

##### *CN.5(vi)*

PMS audits provide valuable information for Parliament on performance management systems and represent an important tool to guide improvements in public administration.

##### *CN.5(vii)*

The revised ASPIRE provides an appropriate methodology for undertaking PMS audits.

##### *CN.5(viii)*

From the review of PMS audit files and from feedback from audit clients, the QAO needs to ensure that quality review requirements within ASPIRE are fully utilised.

##### *CN.5(ix)*

To enhance the PMS audit process, the QAO and audit clients (through the contact officer) should ensure that matters of a factual nature are settled at an earlier stage in the audit process than at the time of presentation of the audit management letter.

**Recommendations**

***RN.5(ii)***

**That the QAO institutes a standard practice of holding initial discussions with the relevant Accountable Officer or Chief Executive Officer of an audit entity with a view to obtaining input on the scope and objectives of PMS audits, as is now being introduced.**

***RN.5(iii)***

**That the Auditor-General give consideration to wider involvement of subject matter experts in the planning, audit field work and reporting for PMS audits.**

***RN.5(iv)***

**That the Auditor-General continue with programs to develop the internal skill base for undertaking PMS audits.**

***RN.5(v)***

**That the Auditor-General ensure that quality review standards for PMS audits are observed.**

***RN.5(vi)***

**That, for PMS audits, the QAO and the audit client ensure that matters of a factual nature are settled at an earlier stage of the audit process such that these matters do not detract from the quality of the audit when the management letter is provided.**

***RN.5(vii)***

**That opportunities be taken by the Auditor-General and senior staff of the QAO to educate audit clients on the mandate for, and benefits arising from, PMS audits.**

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## 6. CONTRACT AUDITING

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### 6.1 Overview

Section 43 of the *Auditor-General Act 2009* provides for the Auditor-General at his/her discretion to appoint an appropriately qualified individual who is not a member of the staff of the QAO to be a contract auditor.

In 2008–09, contract auditors performed an estimated 91,821 hours of audit work on behalf of the QAO. Contract auditors accounted for:

- 45% of audits by number
- 43% of audits by value of fees
- 30% of total chargeable hours

In comparison with other jurisdictions, the extent of contracting out of financial and compliance audits by the QAO is broadly in line with the ACAG average of 44% (2008–09) in terms of number of audits, and above the ACAG average of 38% by value of fees. The extent of contracting out varies widely between jurisdictions, largely showing an inverse correlation with the size of the jurisdiction.

All audit work undertaken by contract auditors is to be performed in accordance with the QAO Contract for Auditing Services and the Auditing Standards issued by the Auditor-General.

Contract auditors are appointed from a panel of pre-qualified suppliers and the criteria for pre-qualification include that the auditor –

- is a current member of a professional body and holds a public practice certificate;
- has adequate professional indemnity insurance;
- has the required audit experience and methodology including compliance with Australian Auditing Standards;
- can show evidence of compliance with quality assurance standards; and
- has a satisfactory reference check.

The QAO requires that the contract auditors not engage in the provision of services of any nature to a public sector entity they are engaged to audit without the prior written approval of the Auditor-General.

The use of contract auditors has been a valuable source of expertise to manage the significant audit load on the QAO, especially during peak audit times for audit clients with a 30 June balance date. This has been an important development, as the shortening of the time period for the completion of audited financial statements means that many audit clients now have only a two-month period after the end of the financial year.

Contract auditors undertaking audits in regional Queensland have also been an important source of expertise as they are able to provide quality audit services with a local presence. This serves to mitigate the costs of travel and accommodation for auditors travelling from South East Queensland including the staff of the QAO.

In recent years, the number of firms undertaking audit contracts for the QAO has been reduced significantly from 75 in 2004 to 36 as at 30 June 2009. This in part has been a reflection of the reduction in the number of firms that meet the higher pre-qualification standards, following the introduction of “force of law” auditing standards, in particular the requirement to comply with Auditing Standard APES320 *Quality Assurance Standards*. A

number of smaller regional firms were not able to meet the additional requirements to gain re-registration on the panel for the QAO.

The decision by the QAO to seek a higher standard of audit services has also resulted in a reduction in the number of contract auditors. This has had the effect of increasing the volume of audit work for each contract auditor and enhancing the overall depth and knowledge of the particular sectors being audited.

Some data on the contract audit arrangements is shown in the following table.

#### Contract Audit Statistics

	2004	2006	2008	2009
Number of firms pre-qualified	105	120	58	60
Number of firms with contracts	75	55	40	36
Number of partners with contracts	94	70	60	55
Percentage of audits contracted (by number of audits)	36.7	37.4	46.6	40.0
Revenue for contracted audits	\$6.4m	\$7.8m	\$13.1m	\$12.0m (Estimate)
Average audit fee for each audit client	\$16,790	\$21,134	\$29,913	\$38,661
Average fees by firms	\$65,594	\$113,738	\$262,483	\$306,070
Number of audits undertaken by contract auditors in total	299	312	369	299
Number of audits undertaken by contract auditors outside of Brisbane and environs	241	233	239	163
Number of audits undertaken by contract auditors in Brisbane and environs	58	79	130	136

Source: QAO

As discussed earlier, an analysis of the data indicates as follows:

- The reduction in number of contracted firms pre-qualified and holding contracts following the tightening of audit standards linked with the “force of law” changes to auditing standards and the requirement for compliance with APES 320 Quality Control.
- The increase in the level of average fee for each audit client, which has been influenced by the additional costs associated with auditing under the new “force of law” auditing standards, as well as the impact of amalgamation of local governments (the majority of which are audited by contract auditors).
- The average cost per contract audit has also been influenced by the decision of the Auditor-General to contract the audits for more of the larger and higher risk audits. The highest fee for a contracted audit in 2004 was \$133,183, compared with a fee of \$466,750 in 2009. Fifty-three large, high or medium risk audits were contracted in 2009, compared with 19 such audits in 2006.

- The number of audits undertaken outside of Brisbane and environs has reduced, which is primarily related to the amalgamation of local governments.
- The number of audits undertaken by contract auditors in Brisbane and environs has increased, reflecting an increase in the number of larger and higher risk audits being contracted, most of which are in this area.

As to the choice between the use of internal QAO staff or contract auditors, we note that the Auditor-General has a policy that internal staff will maintain a level of expertise within each sector of government. As an example, we note that within local government, some 91% of audit clients are contracted out, but that the Auditor-General has ensured that QAO staff retain a level of involvement and hence expertise in this sector. In our view, this is a practical and sensible policy.

During our Review, we met with a number of contract auditors including those in regional Queensland, who provided useful feedback, particularly in terms of procedural issues in dealing with the QAO.

## **6.2 Management of Contract Auditing**

Over the last five years, the QAO has significantly restructured and upgraded its internal processes for managing contract auditing. The major change has been to centralise the function in a separate Services and Contracting team. This function was previously undertaken in a fragmented and piecemeal way within each of the audit teams, which resulted in inefficiencies and inconsistencies in approach.

We consider that this is a significant improvement, as it has led to greater consistency in approach, and has facilitated the drive to achieve higher quality from the contract auditors. It has also produced greater efficiencies in managing the procurement process, which ensures that the overhead costs are kept within reasonable levels.

At present, these overhead costs are added to the contract audit fee as a QAO margin to produce the total client fee for a contact audit assignment. In other words, clients who are audited by contractors bear the full QAO cost of managing the contract audit process. Clients are unaware of the magnitude of the QAO margin, but did express concern as to its impact on their total fee. An additional issue is that the cost of procurement for small audits can be relatively high.

There is an argument that these overhead costs should actually be spread across all QAO clients in the same manner as other office overheads, as all clients benefit from the way in which the QAO utilises contract auditors to manage its overall workload. Other benefits are that the QAO is better able to maintain the quality of its audit work, and to ensure that all audits are completed within required timeframes. We think that there is merit in this argument, and suggest that the QAO give further consideration to this matter.

We note that the QAO has also initiated a program of information sessions on larger audit clients for contract auditors. This has included participation by the Chief Finance Officer and/or the Chair of the Audit Committee of the audit client. The purpose of these sessions is to provide prospective contract auditors with a greater knowledge and understanding of the audit client and audit risks, to provide a more informed basis for pricing of the audit fee. We support the use of these information sessions, and encourage the QAO to expand the program where possible.

Conclusions

*CN.6(i)*

The QAO has made significant improvements in managing the contract auditing process.

*CN.6(ii)*

Further consideration could be given to allocating overhead costs of managing the contract auditing process across all audit clients, in view of the broader benefits derived from this process.

### 6.3 Stakeholder Feedback

The main issues raised in meetings with audit clients and other stakeholders that warrant further consideration are as follows:

- A view that some additional background information on the audit client, including what could be referred to as a Permanent Audit File, would assist in the scoping of the audit and in ensuring that the tendered fee is based on a sound knowledge of the audit client. Concern was expressed about the difficulty of scoping the work and developing a reasonable fee without better knowledge of the audit client.
- A suggestion from both contract firms and from audit clients that there would be merit in having one contract firm to undertake audits for a number of similar organisations or organisations within a sector e.g. grammar schools or the power distribution GOCs or the power generator GOCs. This would be beneficial in terms of the level of expertise gained from that sector/industry, and would provide the potential for cost efficiencies from the viewpoint of the audit clients who pay the audit fees.
- Further benefits would be gained from having some form of Permanent Audit File to assist in understanding the audit client, especially when the audit responsibility moves from one contract auditor to another, or between the QAO and a contract auditor.
- A concern about the level of overhead cost associated with establishment of the contract auditors panel and in tendering audit assignments.
- A general comment that contract auditors tend to be more commercially focussed and more disciplined in completing the audit within the agreed budget.
- A concern about the additional burden involved for audit clients due to the learning process when there are changes to the audit team (whether because of the appointment of a new contract auditor, or a changeover from the QAO to contract auditor or vice versa). This requires more involvement of the audit client staff whilst the auditor gains a knowledge and understanding of the audit client and/or the sector./industry.

Conclusions

*CN.6(iii)*

There is a need to consider the nature and quality of information available for contract auditors to ensure that appropriate risk assessed fee quotes are submitted for audit assignments for the QAO. This would include whether some form of Permanent Audit File (preferably in electronic form) would be beneficial.

*CN.6(iv)*

Further consideration could be given to using a common auditor for the audit of public sector entities within a particular sector/industry to leverage the benefits of specialisation in that sector/industry. (This needs to be considered in the context of rotation of audit appointment arrangements over time.)

**Recommendations**

*RN.6(i)*

**That the QAO upgrade the nature and quality of information available for tenderers submitting proposals for contract audit work to ensure appropriate risk-assessed fee quotes can be made.**

*RN.6(ii)*

**That the QAO assess whether the use of contract auditors for a group of entities within a particular sector or industry would provide benefits for the QAO and audit clients in terms of specialisation in that sector/industry.**

#### 6.4 Quality Assurance Process

The QAO has established a program of reviewing the quality of audit work by contract auditors. During 2009, a review of quality assurance activities was undertaken for 18 contracted firms. These reviews assessed the internal quality processes within the contracted firms to assess compliance with the requirements of APES 320 *Quality Control of Firms*.

The review identified a number of shortcomings in particular elements of quality procedures. In some cases, there was an overall assessment that the quality of work was not to a level that was satisfactory to the QAO. Feedback has been provided to all firms involved in the review process. Where there is a non-compliance with APES 320, the contract auditor will be required to rectify deficiencies within 12 months.

We support the policy established by the QAO to undertake quality assurance reviews of contract audit firms, and to ensure that all contract audit firms are reviewed over a three-year period.

Conclusion

*CN.6(v)*

The QAO is to be commended for the diligence in reviewing the quality control processes in contract audit firms, with the aim of ensuring that high standards of public sector auditing are maintained.

## 7. FUNDING AND FEES

### 7.1 Funding of the QAO

The QAO has a funding budget of \$42.7 million for 2009–10, an increase of about 7% from funding of \$39.8 million in 2008–09. Funding has increased by 93% from the figure of \$22.2 million in 2002–03, reflecting largely the demands of an expanded workload and consequent staffing increases.

The main source of funding for the QAO is user charges, being audit fees charged to audit clients. In this regard, the QAO operates in much the same way as a private sector audit firm. In 2009–10, some \$36.5 million of the QAO's budget will be funded from user charges, an increase of 8% from 2008–09, and more than double the figure of \$17.8 million in 2002–03. In relative terms, funding from user charges has increased steadily from about 80% of total funding in 2002–03 to over 85% in 2009–10.

The remainder of QAO's funding is derived largely in the form of government appropriation from the Consolidated Fund as part of the annual State budget process. In 2009–10, government funding is budgeted to be \$6 million, an increase of 3% on the funding of \$5.8 million received in 2008–09. Government funding has increased by 43.7% (from \$4.2 million) since 2002–03.

The following table shows changes in the main components of funding for the QAO from 2002–03 to 2009–10.

QAO Funding Sources (\$M)

Year	Fees	Appropriation	Other*	Total
2002–03	17.830	4.209	0.122	22.161
2003–04	19.488	4.158	0.165	23.810
2004–05	20.517	4.036	0.101	24.653
2005–06	22.177	4.315	0.134	26.626
2006–07	24.940	4.938	0.200	30.078
2007–08	30.847	5.360	0.177	36.383
2008–09	33.793	5.853	0.197	39.843
2009–10 (Est.)	36.541	6.045	0.189	42.775

\* Mainly the value of services received below fair value, especially the value of archiving services from the State Archives not charged to the QAO.

Source: QAO

The appropriation funding for the QAO is determined through the normal parliamentary appropriation processes after consultation by the Treasurer with the PAPWC, in accordance with Section 21 of the *Auditor-General Act 2009*. Prior to this, the Auditor-General is required to prepare estimates of proposed receipts and expenditure of the QAO for each financial year and to present those estimates to the Treasurer. Appropriation funding is used primarily to fund:

- PMS audits
- Servicing the needs of Parliament (such as Reports to the Parliament and PAPWC inquiries)

- The activities of the Auditor-General and the Deputy Auditor-General
- Special investigations or other ad hoc discretionary investigation work performed in the public interest
- General advice and assistance to audit clients and central agencies such as Queensland Treasury.

In our view, the financial resources available to the QAO are adequate to enable it to discharge its functions and objectives economically, effectively and efficiently, without the need for additional funding. There is merit in the structure of the current funding model, which provides a sound basis for the QAO's operations. It is appropriate that audit fees are used to fund the QAO's core business of financial and compliance auditing, while government appropriation is used effectively as "top up" funding to support the other activities of the QAO, as outlined above. During the course of our investigations, no stakeholders raised any major concerns or advanced any proposals for changes to the structural arrangements for funding of the QAO.

#### Conclusion

##### *CN.7(i)*

The current funding model for the QAO has proven to be practical, robust and sustainable, and there is no reason to change the current structural arrangements.

## 7.2 Funding Models in other Jurisdictions

Audit Offices in all States and Territories, as well as the Commonwealth, charge audit fees to audit clients, although the range of audit clients to which these fees are applied varies greatly. For example, neither the ANAO nor the Northern Territory Audit Office charge fees to government departments, but do charge fees to statutory bodies and government business/trading enterprises. Fees are charged for financial and compliance audits (financial audit opinions), but in no jurisdictions are fees charged to audit clients for performance or PMS audits.

## 7.3 Legislative and Policy Framework for User Charges

There is now a long history to the charging of audit fees by the QAO. As early as 1966, audit fees were determined by reference to an hourly cost, plus an on-cost of 17.5%. Various reviews of audit fees and changes in methodology occurred over the following 30 years.

In 1992, the Queensland Government decided that the QAO should move towards being a fully self-funded body, with no limitation on its ability to charge audit fees. Further consideration of audit fees occurred during the 1990s, with the then Auditor-General arguing that full user charging was not appropriate for the QAO, as it could lead to a constraint on QAO's effectiveness and a compromising of independence in relation to special projects. Various adjustments also were made to the way in which audit fees were determined, with progressive increases in audit fees occurring over a three-year period from 1999–2000 to 2001–02.

From 2002–03, audit fees were adjusted annually in line with movements in the CPI. However, the Auditor-General argued that these adjustments were inadequate, as the costs of the QAO are largely driven by wage movements, which had been higher than the CPI. Most recently, the basic rate of audit fees was increased by 10.8% with effect from 6 October 2008, and a further 5.8% with effect from 1 October 2009. These increases were approved by the Treasurer following submissions by the QAO, and are based on moving towards full cost

recovery for financial and compliance audits. This will enable an increased proportion of appropriation funding to be reallocated to PMS audits, and Parliamentary reporting services and sector-wide assistance.

Section 56 of the *Auditor-General Act 2009* provides the statutory basis for the Auditor-General to charge audit fees to clients. It states:

- (1) *The auditor-general may charge fees for an audit conducted by the auditor-general.*
- (2) *The auditor-general may also charge reasonable costs and expenses incurred by or for the auditor-general in conducting the audit.*
- (3) *The auditor-general may, under the Treasurer's approval, decide the basic rates of fees.*
- (4) *The auditor-general must assess the fees for an audit having regard to the basic rates of fees decided under subsection (3).*
- (5) *Unpaid fees may be recoverable by the auditor-general as a debt due to the auditor-general.*

It is noted that the charging of audit fees is optional, as subsection (1) above specifically states that the Auditor-General “*may*” charge fees. Where an audit fee is charged, however, there is an explicit requirement for the Auditor-General to have regard to the basic rates of fees approved by the Treasurer.

In practice, successive Auditors-General have chosen to adopt the policy that fees will be charged for every audit, unless otherwise determined by the Auditor-General. This is outlined in QAO Policy G13 *Audit Fee and Fee Charging*. Policy G13 outlines relevant components to be considered in identifying the cost of an audit and for recovery through the charging of audit fees. The policy encompasses QAO work, QAO expenses outlaid, contracted-in staff, contracted-out work, sector-wide management work, Audit Policy and Quality, IS audit, PMS audit and Consolidated Revenue Funded Jobs or Appropriation Funded Jobs. It is intended that the fees advised to the client must be the full cost of undertaking the audit. In relation to PMS audits, to ensure value for money, the Deputy Auditor-General acts as a notional “*client*” and is responsible for the monthly approval of the allocation of appropriation revenue.

As outlined in the following table, there are certain audits and related activities for which audit fees are not charged directly to clients.

**QAO Audit Activity Type – By Funding Source**

<b>Core Activity Type</b>	<b>Funding Source</b>
Financial and compliance audits	Audit fees
Special audits – Departmental	Audit fees/ Appropriation
Sector-wide and related activities	Audit fees/Appropriation
PMS audits	Appropriation
Special audits – Parliament	Appropriation
Report to Parliament	Appropriation

## 7.4 Audit Fees

The level of audit fees charged by the QAO was a major issue raised by a number of audit clients during the course of our investigations. The main complaints were as follows:

- Level of fees considered to be too high.
- Fee level not adequately explained or justified.
- Variations from originally agreed fee levels were not adequately explained, nor flagged with sufficient notice to audit clients.

A common comment that we received was that audit clients have no option but to pay the fee, whether or not it is considered to be justified. It was felt that there is limited, if any, capacity to negotiate with the QAO on the level of fees imposed. We note that similar concerns were raised in the 2004 Review.

To some extent, these complaints need to be considered with a degree of caution, as no one likes to pay fees, and the level of fees are an “easy target” for criticism. Also, the complaints that were received need to be balanced against contrary views expressed by other parties. For example, there were other audit clients interviewed who were satisfied with the level of fees and who felt they were receiving value for money for the fees they paid. It would seem that there is a degree of inconsistency or variability in the way the fee issue is managed by Engagement Leaders with audit clients.

Given the concerns that were expressed, we considered it necessary to examine the issue of fees in some detail. Audit fees are generally a relatively small proportion of an entity’s overall costs, and therefore may be considered to be non-material. However, government departments usually have a high proportion of locked-in expenditure (eg for wages and salaries of staff), such that discretionary expenditure may actually be relatively small. In such circumstances, audit fees become relatively more important, especially where limited additional funding has been provided through budget appropriation in recent years for escalation in non-labour costs. This may mean that audit fees need to be funded from an increasingly constrained pool of discretionary expenditure.

For GOCs (and at least some statutory bodies) operating in a commercial environment, there is ongoing pressure to be competitive by keeping costs (including audit fees) as low as possible, yet there is not the same market pressure on the QAO to keep audit fees competitive, as their business is not contestable. Such entities do not have the option to take their audit business elsewhere in the pursuit of better value for money.

A comprehensive examination of audit fees proved to be difficult, as the relevant information was not readily available and comparisons between fees are limited somewhat by variations in the scope of work, both between entities and between years. For similar reasons, comparisons or benchmarking with private sector audit fees and fees charged by Audit Offices in other jurisdictions also was problematic.

The QAO provided useful information that enabled some basic benchmarking to be undertaken, especially between comparable entities, such as the electricity generation GOCs, electricity distribution/network GOCs, universities, similar sized local councils, and grammar schools. Also, some comparisons of fees were undertaken for entities which had moved from in-house QAO audits to contracted audits (taking account of the timing differences involved).

Recognising the limitations of our analysis, we were nevertheless able to make some tentative observations, as follows:

- There was some greater (unexplained) variability in audit fees between comparable entities than might have been expected.
- There was discernible evidence of lower fees for entities which had moved from in-house QAO audits to contracted audits, even after QAO on-costs (contractor management margin) were added to the contractor fee. This largely reflected a lower

number of hours involved in undertaking the audits by private contractors, compared with the QAO.

There was also evidence of variability in the extent to which cost recovery is achieved by the QAO, including both write-offs and write-ups of costs. Write offs occur generally occur where the QAO considers that it is not possible to recover the full costs incurred in undertaking an audit (eg where there are substantial additional hours of work recorded on time sheets beyond original estimates). From information provided by the QAO, the level of write offs has been steadily declining, with around 85% of costs now being recovered, compared with about 72% 10 years ago.

These figures may not represent the full picture, as there have been anomalies and inconsistencies in recording of hours worked on time sheets (compounded by the problems encountered with eTrack) over the past few years, particularly some residual tendency for under-recording of hours worked (eg where there is a view that such costs are unlikely to be recoverable). It is noted that the QAO has been working assiduously to reduce the prevalence of this problem. Improvements to the operation of eTrack will assist in this regard.

Whilst not widespread, some write-ups of costs has also occurred. Essentially, this has involved over-spends on particular audits being offset against under-spends on other audits. Again, the QAO is keenly aware of this practice, and is working to ensure better discipline and consistency in the recording and charging of hours worked, to ensure proper cost recovery on each audit.

The 2004 Review commented that *“there was some evidence to suggest that the QAO has not yet attained the high standard of professionalism in terms of time management and fee assessment to which it has aspired.”* While good progress has been made since then, there are still aspects of both time management and fee assessment that need further improvement.

## 7.5 Value for Money in QAO Audit Fees

The broader context to this analysis is that, in economic terms, the QAO is a monopoly provider of audit services to public sector entities, and has captive clients, who are not in a position to take their business elsewhere. It follows that QAO is in a position to monopoly price, as there is a lack of contestability in the market. This is ameliorated to some extent by the use of contract auditors, where there is competitive price tension in bidding for public sector audit work. The use of contract auditors also provides some indirect pricing pressure on the fees charged by QAO, especially for broadly comparable audit tasks.

Some other jurisdictions have adopted different approaches to introduce contestability into the market for the provision of audit services to public sector entities. For example, in both New Zealand and Victoria, the role of the Auditor-General was separated from that of the audit offices, which were then required to compete for business. This is essentially a form of "purchaser/provider" separation of roles. Victoria subsequently has abandoned this model, and reverted to the more conventional audit office model, although New Zealand still has a structural separation between the Office of the Auditor-General and Audit New Zealand.

We are not attracted to the case for such a structural separation of roles, as we are not convinced that the benefits demonstrably outweigh the costs involved in operating under such a model. Further comment on the relative merits of this model are outlined in Section 15 of this Report.

Another approach to provide contestability and ensure more competitive fees would be to enable selected public sector entities to make their own choice of auditor, as between the QAO and a contract auditor selected from a pre-qualified panel of contract auditors approved by the QAO in accordance with its current arrangements. Such an approach would be less appropriate for core government departments, but could be readily applied to other public

sector entities, especially GOCs and other statutory bodies. This is not significantly different from the current situation in which many entities are already audited by contract auditors, except that the choice is made by the QAO, rather than the entity itself.

There are some complexities involved in providing public sector entities with a choice of auditor. For example, there would be a greater task for the QAO in managing the panel of contract auditors, and ensuring that the Auditor-General's auditing standards are being consistently applied. This would give rise to a potential conflict between the role of the QAO as a regulator of contract auditors and also as a competitor in service delivery. Consistent with current contract audit arrangements, it would be necessary for the Auditor-General to sign off on all modified or qualified opinions from contract auditors, to provide a sufficient level of assurance to the Parliament. There also could be significant resourcing implications for the QAO if it was to lose too much work to contract auditors.

Given these complexities, we are not persuaded that there is a compelling case to adopt a "choice of auditor" approach at this time. However, this is perhaps a matter that may need to be revisited in the future, if our recommendations below do not provide the necessary discipline, rigour, transparency and accountability to the fee setting processes of the QAO

In the absence of a contestable market, there would be a case in economic theory for an external independent regulator to oversight the pricing or fee setting processes of a monopolist. Scrutiny of the QAO's fees at present is provided by the requirement for increases in the QAO's basic rate to be approved by the Treasurer. Closer scrutiny of the QAO's fee setting process is warranted, but we believe in the first instance that this can be achieved by enhancements to existing arrangements.

Given its significant pricing power, there is a heightened level of responsibility on the QAO to be accountable to audit clients for its fees. While we endorse the policy of full cost recovery, the fee setting process should not be determined solely on a cost plus basis, with an unfettered capacity to pass on cost increases without question. Rather, there is a need to ensure that the QAO's costs are economic, efficient and justifiable, and that billable hours charged for audit tasks are consistent with best practice in the market, to the maximum extent possible.

In short, we consider that there is a need for closer scrutiny of the QAO's cost base to ensure that audit clients can have greater confidence that they are receiving value for money in the audit fees set by the QAO. This requires consideration of factors such as the efficiency and productivity of the QAO, as well as trends in market conditions which may impact the level of audit fees.

The QAO is one of a small number of core government agencies which charges clients for its services (even if those clients are in fact other public sector entities). It is now a business generating some \$36 million in fee revenue, and therefore needs to ensure that its fee setting, time management and billing systems are of a standard expected of a commercial audit business of this size. Indeed, in the absence of a contestable market, we consider that the QAO has an extra responsibility to set higher standards than the private sector in the way fees are determined, and in their interaction with audit clients in explaining and justifying those fees.

## Conclusion

*CN.7(ii)*

There are some justified concerns from audit clients about the fees charged by the QAO, and there is a clear need for the QAO to improve the way in which it sets fees, and manages its time recording and billing systems to ensure greater transparency, accountability and consistency of approach.

## Recommendations

*RN.7(i)*

**That there should continue to be regular annual adjustments to the basic rate of QAO audit fees, subject to the approval of the Treasurer in accordance with Section 56 (3) of the *Auditor-General Act 2009*.**

*RN.7(ii)*

**That the annual adjustment to be determined by the Treasurer should be based on an assessment of wages, salaries and other costs relevant to the operations of the QAO, but should also take into account:**

- **productivity and/or efficiency considerations, especially those relevant to the funding of core government departments**
- **any adjustment factor to reflect market movements in audit fees generally.**

*RN.7(iii)*

**That the QAO needs to provide a more consistent, coherent and transparent basis for the determination of fees, through an Audit Fee Charter which commits the QAO to:**

- **ensure that the Engagement Leader for each audit is required to present and explain the QAO's audit fee proposal to an entity's Audit Committee as part of the Annual Client Service Plan**
- **provide a detailed disaggregation of the composition of the audit fee for an entity, including scoping issues, identification of major tasks or activities, hours of work to be undertaken for each major task or activity and the type and level of resources to be used.**
- **provide an opportunity for audit clients to seek further information, clarification and/or justification of fees prior to the commencement of the audit plan**
- **undertake a zero-base approach to the determination of fees for an entity at least once every three years, or where the audit fee is expected to vary from the previous year by more than 10% (for reasons other than a change in the basic rate)**
- **ensure that, during the course of the audit task, any variation in audit fees of greater than 10% from the original fee proposal is notified to, and acknowledged by, the Accountable Officer or Chief Executive and the Audit Committee of an entity prior to any additional costs being incurred by the QAO.**

*RN.7(iv)*

**That the QAO develop a more comprehensive program of benchmarking of audit fees for comparable entities with a view to ensuring greater consistency in the determination of fees, including:**

- **internal benchmarking of fees for comparable size and type of entities**
- **external benchmarking, both with ACAG, and with private sector audit firms where relevant and practical.**

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## 8. ORGANISATIONAL STRUCTURE

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### 8.1 Overview

Since the 2004 Review, the organisational structure of the QAO has evolved to reflect a business model which meets the changing needs of the audit function. A new organisational structure was adopted in September 2008 which clearly defines the service delivery focus of QAO, built around the core business of auditing public sector entities. As at December 2009, there was a workforce of 263 staff in the QAO, representing 248 FTEs.

The QAO has five key business or functional areas – financial and compliance audits; PMS audits; IS audits; Audit Policy and Quality; and Audit Support. This is a logical structure based on a separation into the main functional specialisations of audit services. The front-line service delivery audit functions report through the Deputy Auditor-General; the audit support services report through the General Manager – Audit Support; while the Audit Policy and Quality function reports directly to the Auditor-General.

This is an appropriate separation of reporting and accountability lines, as it draws a clear distinction between the external service delivery functions, and the internal audit support functions. It also enables APQ to operate at arm's length from the day-to-day audit function, and provide an independent source of advice to the Auditor-General on quality and performance issues for QAO.

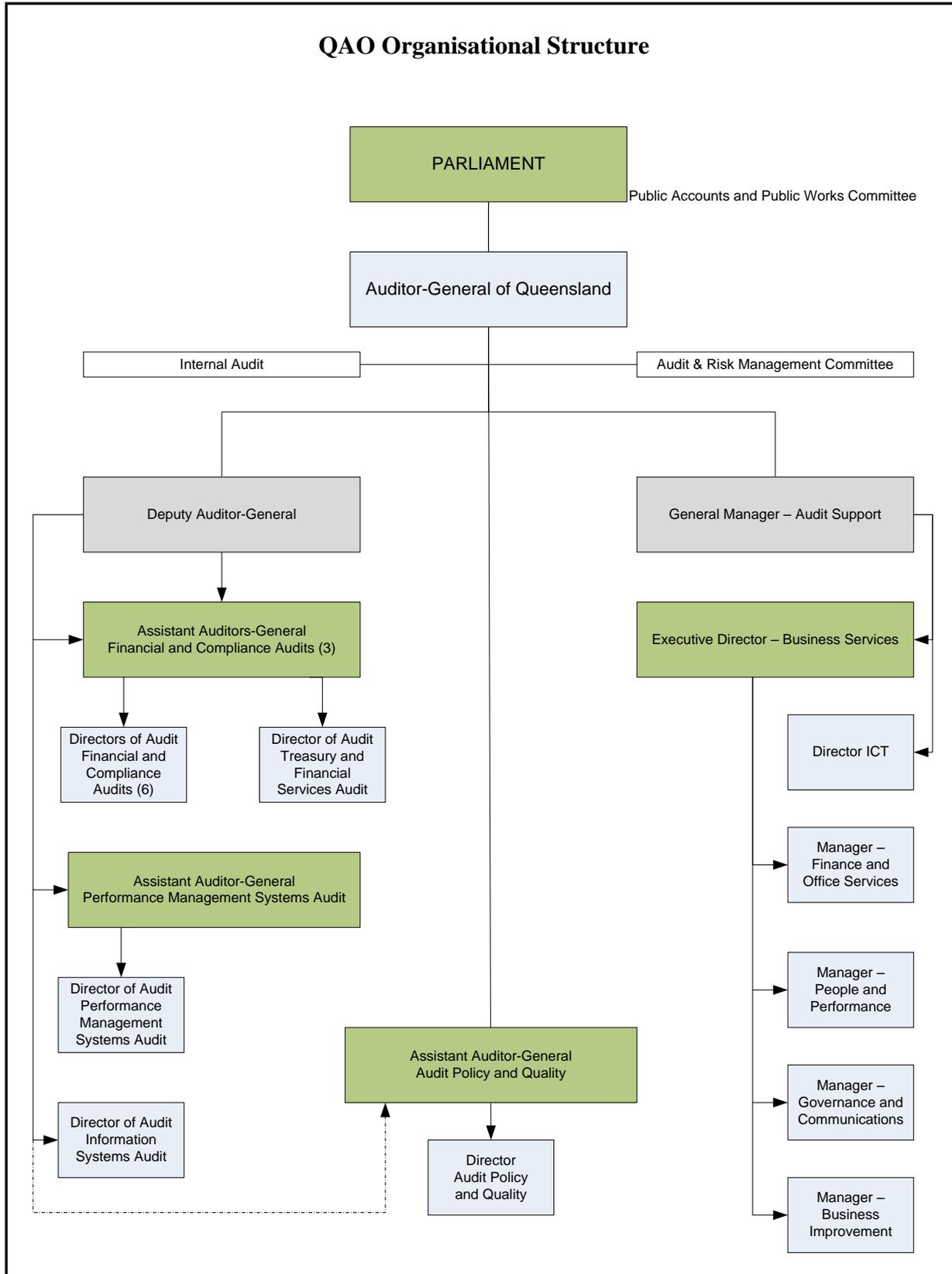
The current organisational structure of QAO is shown in the accompanying diagram.

### 8.2 Financial and Compliance Audit Divisions

Within the Financial and Compliance Audit Divisions, there are three teams, which were re-named during 2008–09 as Transport and Development; Education and Local Government; and Services and Contracting. This is intended to reflect the sectoral functions of the teams. While this is essentially an internal management matter, perhaps broader titles such as "Economic Services" and "Social Services" could be used for the first two teams, to better reflect the full range of entities which they service.

We consider that the creation of a separate Services and Contracting team is a positive step, as it centralises the management and co-ordination of the contracting function. This function has previously been undertaken in a fragmented and piecemeal way within each of the audit teams, which has resulted in inefficiencies and inconsistencies in approach. The centralisation of the contracting function has resulted in a significant improvement in the management of this task, as noted previously in Section 6.

Staffing of the Financial and Compliance Audit section has increased by around 13% over the last six years, with 143 positions occupied as at December 2009, compared with 125 positions in December 2003.



Source: QAO Annual Report 2008-09

### 8.3 PMS Audits

The QAO has for a long time maintained a function separation between the financial and compliance audits and the PMS audits. We believe that this separation is appropriate, given the different focus to the audits, and the different skill sets involved. In particular, it is not necessary for all PMS auditors to have CPA or equivalent qualifications and, indeed, there is considerable merit in developing and maintaining a broader base of skills.

Staffing of the PMS Audit Division has increased from 8 positions occupied in December 2003 to 19 positions in December 2009, as greater priority has been given to this function. In this regard, 21 PMS audits have been conducted since the 2004 Review, as the QAO has sought to more fully utilise its mandate consistent with the thrust of the 2004 Review. The current target is to undertake around 6 PMS audits in 2009–10, the same number as in 2007–08 and 2008–09.

### 8.4 Information Systems Audit

There is an Information Systems Audit Section, consisting of 17 positions occupied as at December 2009. This is more than a threefold increase from 5 positions in December 2003, reflecting the increased adoption of complex information technology applications to business systems throughout the public sector. The section collectively has a strong level of relevant qualifications and experience to undertake information systems audits.

### 8.5 Audit Policy and Quality

APQ performs a central role in ensuring consistency of policy and application of accounting/audit standards across the financial and compliance audit teams. This is an essential function and our observations indicate that this function in the main is performed effectively. APQ is also responsible for the development of IPSAM.

In addition, APQ undertakes the quality assurance activities for internal audits, contracted audits and PMS audits. As noted above, it is appropriate that this function is separate from the direct audit function, as it enables more independent critical scrutiny of the audit function and, especially, independent reporting to the Auditor-General. The findings of quality assurance reviews have been considered in earlier sections of this Report.

Staffing in APQ has increased to 14 positions occupied at December 2009, from 9 positions in the former Audit Policy and Reporting function at December 2003. This comparison is limited somewhat because of the change in functions, with some of the communications function shifting to Audit Support, but there has been an increased priority given to the quality assurance function.

### 8.6 Audit Support

Audit Support is a Division which has changed significantly in recent years from the previous Business Services function, as QAO has sought to consolidate, expand and improve the range of internal support services provided to the front-line audit functions. In particular, Audit Support has been heavily involved in the development of eTrack and a range of staff performance-related activities such as Lominger and LaunchPAD and the development of enhanced business monitoring and reporting systems and practices.

Staffing numbers in Audit Support have increased to 44 at December 2009, compared with 32 at December 2003 for the former Business Services function, representing an increase of over 37%.

The proportion of total staff involved in audit support roles (including executive positions) has increased significantly to 24% in 2008–09, from around 14–15% in the period 2004–05 through to 2007–08. This is a significant shift in the balance of resourcing within QAO, as it

implies a much higher proportion of overhead costs. The explanation provided by the QAO is that this is due to a transfer of various support activities from the audit divisions to enable audit staff to focus on client audit functions.

We are concerned by the extent of the resource transfer that has occurred, as it involves a relative shift in resources away from external service delivery to internal support functions. We recognise that there has been a clearly identified need to upgrade and improve internal support systems, and progress has undoubtedly been made, although it is yet to be seen how this translates into benefits such as improved output of front line audit services and productivity of the QAO. (The issue of productivity is addressed in further detail in Section 13 of this Report.) The need to carry such a high proportion of overhead costs on an ongoing basis is also likely to place unnecessary upward pressure on audit fees, limiting the scope for a more efficient cost structure.

It has not been possible to undertake a comparison of the relative importance of audit support functions in Audit Offices in other jurisdictions, due to a lack of comparable data. In the private sector, we would expect audit support functions to be in the range of about 12–14%. Allowing for the additional governance requirements of the public sector, we consider that a figure of around 15–18% would be reasonable, consistent with the level achieved in the years prior to 2008–09.

Now that improved internal systems have largely been completed, and as further initiatives are bedded down, we believe that there will be capacity for some re-balancing of resources within the QAO to reduce the relative proportion of overhead costs and re-focus on resourcing for core service delivery functions.

#### Conclusions

##### *CN.8(i)*

The organisational structure for the QAO is appropriate and practical in undertaking the core function of auditing for the public sector in Queensland.

##### *CN.8(ii)*

There has been a sharp increase in the relative proportion of the QAO's resources committed to audit support functions, which is difficult to justify, unless it produces a demonstrable improvement in the productivity of the organisation, which is not yet apparent.

#### Recommendation

##### *RN.8(i)*

**The QAO should aim to ensure that audit support functions return to around 15–18% of total staffing, consistent with the level achieved prior to 2008–09, unless a higher level can be justified by demonstrable improvements in the productivity of front-line audit service delivery (as measured for example by better capacity utilisation).**

## 9. GOVERNANCE FRAMEWORK

As governance is a core focus of the audit function undertaken by the QAO in all public sector entities, it is incumbent upon the QAO to demonstrate by example, in applying the highest standards of internal governance itself. Governance involves the way in which an organisation is structured and managed to achieve its strategic goals and operational objectives.

Key elements of the QAO governance framework include governance and operational committees, risk management processes, as well as internal and external audit structures and policies. These elements are reviewed below.

### 9.1 Executive Management Group

EMG is the key leadership group charged with responsibility to shape and drive the strategic direction of the QAO, and to support the Auditor-General in his role as the Accountable Officer. The EMG meets on a regular monthly basis, and currently consists of 11 members, comprising the Auditor-General; the Deputy Auditor-General; the General Manager – Audit Support; the five Assistant Auditors-General; the Executive Director – Business Services; the Director of Audit – Information Systems; and two staff members nominated by the Women’s Leadership Group to provide a better gender balance – currently a Manager, Audit Policy and Quality and an Audit Manager. The composition of EMG is designed to provide a diversity of input on strategic issues at a senior management level.

The size of the EMG is probably somewhat larger than desirable, and we consider that an ideal size is in the range of 6–8 members. However, we recognise the desire of the Auditor-General to achieve an improved gender balance and a diversity of representation and interests. Over time, some rationalisation of the size of EMG should be considered, to avoid the risk that deliberations become unnecessarily cumbersome and unwieldy.

During the course of our Review, we interviewed each of the EMG members, undertook an extensive review of EMG papers, received input from other staff members as to their views on the activities of EMG, examined the findings of the Thomson Review, and reviewed the results of the 2009 Pulse Survey of staff in relation to EMG. There were a wide range of comments and opinions expressed, and a diversity of views as to the performance of the EMG.

From the 2009 Staff Pulse Survey, there were some mixed results on the leadership and management functions, as follows:

- 67% provided a favourable response to the statement that "*QAO is making improvements to ensure it has a successful organisational structure*". This was the highest rating ever recorded in these surveys for this question.
- 65% provided a favourable response to the statements that: "*QAO is making improvements to ensure it has effective working relationships*" and that "*Executive management keeps me informed about future plans and directions*". In both cases, this was higher than in the 2008 survey, but still lower than in earlier surveys.
- 67% provided a favourable response to the statement that "*Executive Management sets clear plans and directions*". This was higher than the figure of 57% in the 2008 Survey, but lower than the 75% figure recorded in the 2006 Survey, and on a par with results recorded in the 2003 and 2004 Surveys. In relation to Service Sector benchmarks, it compared favourably with the Professional Occupations Only benchmark, but was slightly below the All Service Occupations benchmark.

- Only 51% provided a favourable response to the statement that “*Executive management demonstrate collaboration and teamwork*”. This question was included in the pulse Survey for the first time in 2009, so there are no comparable figures for trends over time. However, the favourable response percentage was substantially lower than both Service Sector benchmarks mentioned in the previous point.
- Only 45% provided a favourable response to the statement that “*Executive management manage change effectively*”. This was better than the 39% figure recorded in the 2008 Survey, but remains marginally below the figures recorded in earlier Surveys. It is notable that this was the lowest favourable response percentage recorded for all questions in the Survey, and well below the Service Sector benchmarks.

While these results relate to executive management generally, rather than the EMG specifically, we nevertheless consider that there are some clear implications for the EMG. The results indicate some areas for further attention, which are consistent with some concerns expressed to us, observations made in the Thomson Report and some concerns that we identified from our own inquiries. It would appear, for example, that feedback from individual EMG members to their teams on the deliberations and outcomes of EMG meetings is variable as to form, content and quality.

There is also a concern that EMG has become too pre-occupied with reviewing operational performance and has lost some focus on strategic issues, thereby reducing its overall effectiveness. In this regard, we note the following comments from the Thomson Report:

*“The current reporting process leaves discussion and actions on key areas to the EMG meeting. Ideally, key issues should be identified prior to the meeting and discussions should be held with responsible managers as to how these issues will be addressed. This way the EMG time could be more effectively utilized by focusing on the dashboard results and the proposed actions which would then just need ratification or change if required. This in effect provides a proactive approach to reporting rather than a reactive approach.”*

In our view, there is a clear need to re-focus and re-define the role of the EMG, to ensure that it is more meaningful and relevant in its deliberations, and more focussed on higher-order measures of performance, especially productivity and capacity utilisation (as discussed further in Section 13 of this Report). As a related issue, there remains some confusion amongst staff as to the role of the EMG within the governance framework, and its interactions with senior management. This is a matter which needs to be clarified and regularly reinforced to ensure that there is better understanding of these arrangements.

We are advised that actions are underway to address some of the concerns about the role of the EMG. For example, we understand that the Auditor-General is in the process of implementing relevant recommendations of the Thomson Report.

#### Conclusion

##### CN.9(i)

The EMG should re-focus on strategic issues, and higher-order measures of performance, such as productivity and capacity utilisation, and streamline its detailed monitoring of operational performance.

**Recommendation*****RN.9(i)***

**That the recommendations of the Thomson Report relating to the EMG be adopted viz**

- *“Noting cross reference to Standard 1.2.9, the development of a dashboard of key result areas is recommended. This will enable management reports to be further refined and simplified.*
- *That actions for key issues areas be developed prior to EMG meetings to enable a more proactive approach to decision making.”*

## 9.2 Audit and Risk Management Committee

The charter of the Audit and Risk Management Committee (ARMC) is to oversight the audit and audit-related findings on the activities of the QAO. This includes input into the audit planning process, risk management issues, corporate governance, performance management issues, and assessment of the internal audit function. Consistent with good corporate governance practice, there are two external members of the ARMC, who provide the required independent perspective for the Committee. The Chair of the ARMC is an external member.

The ARMC has an appropriate charter and has been undertaking its functions diligently in accordance with this charter. During our Review, we met with the Chair of the ARMC and received positive feedback on the activities of the Committee.

We also reviewed the QAO’s risk register, and are satisfied with its structure and content, although we support the recommendations of the Thomson Report as to additional risks to be added to the register.

**Recommendation*****RN.9(ii)***

**That the QAO’s Risk Register be amended to include the following risks, as recommended by the Thomson Report:**

- *“HR planning is not in line with strategic planning*
- *Changing mix of clients relating to sale of government assets, increased contracting out of government services, rationalization of local government and the impact of fixed overheads*
- *Increased use of contracting out of audit work.”*

## 9.3 Information Steering Committee (ISC)

An ISC has long been part of the governance framework of the QAO. The role of the ISC is to lead QAO’s strategy in relation to Information and Communication Technology and to ensure effective governance of major information projects. This includes recommending ICT resourcing and ensuring that ICT resources strategic and operational plans are aligned with the QAO’s strategic focus.

The QAO has revamped the role of the ISC over the last year to address concerns that it was not working effectively. In particular, there was a concern that it was too focussed on operational issues, and lacked a sufficient strategic perspective. The membership of the ISC was changed, and greater emphasis has been placed on strategic issues, including a stronger overview of IPSAM, eTrack and emerging technology issues (such as wireless technology)

for the QAO. This strategic focus has been enhanced by the presence of an external member who has substantial industry and academic background in the information technology and management fields.

We support the revised role and strategic focus of the ISC, and encourage the QAO to ensure that it functions more effectively than has been the case in the past. In passing, we note that a stronger and more effective ISC may well have provided better guidance and oversight of the issues relating to the implementation of eTrack (as outlined in Section 10 of this Report).

#### **Recommendation**

##### ***RN.9(iii)***

**That the effectiveness of the ISC is regularly assessed to ensure that it is adding greater strategic value to the consideration of emerging information technology issues impacting on the QAO, including ongoing refinement of eTrack, IPSAM and ASPIRE.**

## **9.4 Operational Committees**

QAO has a number of operational committees which perform specific functions. These are the Executive Staffing Group (ESG); the Workplace Health and Safety Committee; and the Women's Leadership Group. In addition, there is a Staff Welfare Committee, established under the auspices of the Queensland Public Sector Union.

Each of these committees has a clearly defined charter, and perform a valuable part of the QAO's governance framework. In particular, the primary role of the ESG is to co-ordinate resourcing for QAO's financial and compliance audits, whether from internal staffing, contracted-in resources or contracted out resources, having regard especially to the peaks and troughs in the audit workload.

During our Review, we spoke with the Chair and members of the Staff Welfare Committee and the Chair of the Women's Leadership Group, and we appreciated the frankness and honesty of comments we received from these parties. The Staff Welfare Committee expressed significant concerns about recent changes to the banked time arrangements for staff. Further reference to this issue is made in Section 11.

We also observed that there are some overlaps between the functions of the Staff Welfare Committee and the Consultative Committee and contemplated whether the two Committees should be merged. On balance, there is merit in maintaining the two Committees as they each have distinctive roles, although some streamlining of functions would be desirable to reduce the extent of current overlaps.

We specifically endorse the role of the Women's Leadership Group, which was established by the previous Auditor-General following the recommendations of the 2004 Review, and which has been maintained by the current Auditor-General. The Group plays an active role in promoting issues of particular relevance to women in the QAO, especially in encouraging women to move into senior positions, nominating representatives to serve on the EMG, and investigating initiatives in relation to part-time work and job sharing.

## **9.5 Delegations**

The QAO has a comprehensive set of delegations, particularly in relation to:

- Granting of audit opinions
- Financial and administrative matters.

In relation to the granting of audit opinions, over a long period of time, there has been a desirable trend away from the concentration of this power in the hands of the Auditor-General towards a system of delegations more consistent with modern management practices.

We believe that the current level of delegations is appropriate, and further devolution of these powers would be undesirable. In particular, it is important that all modified or qualified audit opinions continue to be signed off by the Auditor-General.

We consider the current Financial and Administrative Delegations to be appropriate for the QAO, but note that the Policy document G5 will need to be updated to reflect the provisions of the new Financial Accountability Act and supporting financial management framework.

## **9.6 Chief Finance Officer and Head of Internal Audit**

As noted in Section 3 of this Report, the *Financial Accountability Act* requires an Accountable Officer to nominate appropriately qualified persons to the positions of Chief Finance Officer and Head of Internal Audit. These positions have certain delegated responsibilities (referred to as “minimum responsibilities”) in relation to an agency’s financial resource management and operation systems, reporting processes and activities, and internal financial controls.

Given these important delegated responsibilities, we consider that the two positions should have a close and direct access to the Accountable Officer. As the QAO is a relatively small organisation, the roles of Chief Finance Officer and Head of Internal Audit are not overly demanding and the persons currently occupying these positions also perform other duties. In the formal organisation structure, these positions do not report directly to the Auditor-General.

Nevertheless, these two officers have direct access to the Auditor-General in regard to their formally delegated minimum responsibilities under the Act. These arrangements are satisfactory and well understood within the QAO. Over time, however, there may be a case for the two positions to have a more direct reporting relationship to the Auditor-General in the formal organisational structure.

## 10. PLANNING AND RESOURCING

### 10.1 Strategic Plan

We have reviewed the QAO's latest Strategic Plan for the period 2009 to 2013, and consider that it presents a clear and concise articulation of the vision, purpose and values, outcomes and services of the QAO. The QAO's vision is "*Excellence in enhancing public sector accountability*", and the QAO contributes to the achievement of the Queensland Government's "*Toward Q2: Tomorrow's Queensland*" through its audit activities by providing Parliament with "*independent assurance of public sector accountability and performance*".

The Strategic Plan identifies four key objectives, as follows:

- *"We meet the needs of Parliament.*
- *We add value to public sector entities.*
- *Our business is efficient, effective and sustainable.*
- *Our staff are motivated and capable."*

There is a good linkage between objectives and performance indicators, although we believe further work is warranted to refine some of the performance measures, particularly greater specification and quantification of the indicator which states that "*key business metrics demonstrate efficient use of resources to deliver service requirements*". In this regard, we consider that greater priority should be given to an overall measure of office productivity. This is discussed in more detail in Section 13.

The QAO's service delivery framework and associated performance framework, as outlined in the Strategic Plan, are presented in the accompanying diagram. They provide a useful graphical depiction of key linkages in the planning, performance and reporting frameworks of the QAO.

### 10.2 Annual Work Plan

QAO produces an Annual Work Plan, based on its Audit Resourcing Model, which presents a high level summary of divisional resources and services provided across the key service areas of financial and compliance audits; PMS audits; and Parliamentary Reporting and Services and sector-wide assistance.

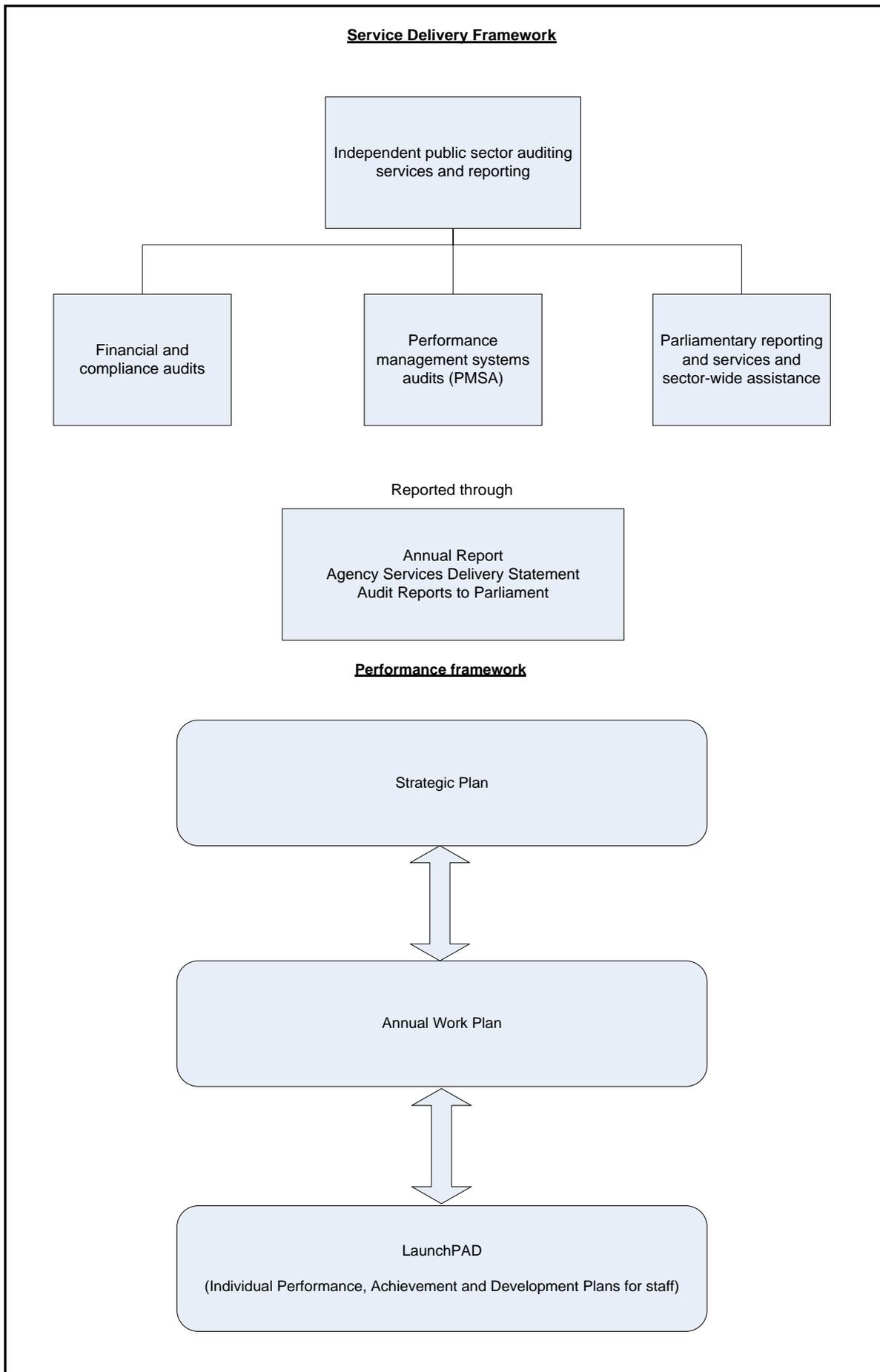
Key assumptions underlying the work plan are:

- Contract out and contract in hours are estimated to remain steady in 2010.
- Appropriation from the Consolidated Fund is expected to remain steady in 2010.

As shown in the accompanying table, total chargeable hours for the QAO (which provides the best measure of overall workload) reached 309,355 hours in 2008–09. This includes the QAO's in-house activity, contracted-in work and contracted-out work (ie contract auditors), and represents an increase of 33% in overall workload since 2005–06 (the first year for which such data was available)

For the QAO's in-house activity only, total chargeable hours in 2008–09 were 202,626 hours, an increase of 27% from 2005–06. Other key points from the table are:

- The use of contracted-in work has been declining, although this still provides a useful tool for overcoming short-term dislocations in QAO's workforce.
- The use of contract auditing has increased by 76% from 2005–06 to 2008–09.



**QAO: Chargeable Hours of Audit Activity**

Year	QAO In-house Activity	Contracted-In	Contracted Out	Total
2005–06	153,950	25,695	52,130	231,775
2006–07	159,383	28,001	65,598	252,982
2007–08	194,950	17,551	87,494	299,995
2008–09	202,456	15,078	91,821	309,355
2009–10 (Projected)	196,617	n.a.	80,000	276,617

Note: Projected figure for QAO in-house activity for 2009–10 includes Contracted-In Activity.

Source: QAO

The above table shows a projected figure of only 276,617 chargeable hours of activity for 2009–10, with QAO in-house activity (including contracted-in work) projected to be 196,617 hours and contract audit work projected to be 80,000 hours. These figures appear to be anomalous, as they suggest a significant projected decline in workload from 2008–09. However, advice from the QAO is that these figures (especially for in-house activity) are based on known commitments only, and do not take account of unplanned or unexpected audit tasks which, on the basis of past experience, inevitably arise during the course of the year. To this extent, this is a weakness in the Annual Work Plan, which needs to be adjusted.

It should be possible to include in the Work Plan a contingency provision for additional hours likely to be required for unplanned activity, based on what has occurred on average in previous years. This would provide a more complete picture of projected workload for the forthcoming year, and a better alignment of resourcing with that workload.

The Annual Work Plan also provides a detailed breakdown of resourcing mapped to QAO's four objectives, supported by strategies, actions and key performance indicators. Generally, we are satisfied that there is a strong and disciplined alignment between the Strategic Plan, the Annual Work Plan and the internal resources of the QAO, apart from the need for a contingency provision for unplanned activity.

**Recommendation*****RN.10(i)***

**That the Annual Work Plan's projected workload for each coming year incorporate a contingency provision for additional hours likely to be required for unplanned activity, taking into account what has occurred on average in previous years.**

**10.3 Audit Resourcing Model**

The audit resourcing model is an internal tool used by the QAO to determine broad resourcing requirements, both generally and for individual audits. It provides a framework or discipline for assessing the quantity of resources and the levels (classifications) of staff to be assigned to an audit. In turn, this feeds into a more detailed resourcing plan in the development of the Client Services Plan.

The model adopts a risk approach, based on two key variables, being:

- Risk (rated as high, medium or low); and
- Size of audit.

A concern with this approach is that the size of the audit is assessed (at least initially) by reference to the previous year's level of audit fees. This means there is a degree of circularity in the model, as the size of last year's fee feeds into the resource allocation process (and hence fees) for the current year. Implicit in this process is the assumption that last year's fee is reasonable and reflects an appropriate scope and resourcing of functions. While the size of last year's fee is a useful reference point, there is a risk that any inbuilt inefficiencies in the audit function will be perpetuated, unless there is close scrutiny of the continuing relevance of those functions and associated resourcing.

The QAO has indicated that, while the model provides a template, there is flexibility to modify or refine resourcing for individual audits, according to particular circumstances. Specifically, initial resourcing assessments of the Engagement Leaders are subject to moderation through a further process that involves input from senior management. Our observation though is that there needs to be very strong grounds to vary resourcing to any significant extent from the model parameters, unless there are significant changes in the structure or risk profile of an audit client.

The QAO has indicated that it is keen to challenge Engagement Leaders to think more carefully about the nature of the tasks involved in each audit and in turn the hours and resourcing to be allocated to each of the tasks. We endorse this approach, as it would remove or at least reduce the degree of circularity in the model. It would also assist in reducing any inefficiencies in the baseload of audit work that is largely rolled over from one year to the next.

There is also some evidence of an overly conservative view on the assessment of audit risks for entities which, through the application of the model, results in a level of over-resourcing for some audits. For example, where contract auditors have taken over the auditing function of an entity from the QAO, there has generally been a reduction in the chargeable hours committed to the audit. This may reflect a sharper focus from the contract auditor (driven in part by the need to offer a competitive fee offer), with greater attention to detailed upfront planning of audit risks and the resourcing required for the audit task.

The value of the resourcing model would be enhanced by developing a rolling forward plan, that looks beyond the annual planning cycle, and takes a 3-year perspective on prospective resourcing requirements. This will better position the QAO to plan and respond to emerging trends, challenges and opportunities, such as those discussed in more detail in Section 17 of this Report.

**Recommendations*****RN.10(ii)***

**That the QAO's audit resourcing model be further refined to provide improved focus on the nature and size of the audit task, and on the assessment of audit risks. This would mitigate the risk that inbuilt inefficiencies in resourcing are perpetuated through the current configuration of the model.**

***RN.10(iii)***

**That the QAO's audit resourcing model be further developed to provide a rolling three year forward plan to identify and address emerging issues which will impact resourcing needs of the QAO into the future.**

**10.4 eTrack****10.4.1 Background**

As a relatively large audit business which charges clients fees for its professional services, QAO requires a practice management system which provides an effective tool for the efficient allocation of resources (both internal and contractors) and which also provides an effective billing system that clients based on hours of work performed.

In December 2006, QAO commenced a process to find a new practice management system to replace the former ATOMS product and provide additional functionality. Following an open tender process, eTrack was selected as the preferred practice management system during 2007. QAO implemented eTrack in October/November 2007, and formally accepted the system on 1 February 2008, subject to the resolution of certain outstanding items which were subsequently delivered.

**10.4.2 Implementation**

Based on feedback from staff at all levels in the QAO, we note that to date the eTrack product has not performed to expectations, including the standards promised by the vendors, and there have been shortcomings in the implementation of the system within the QAO. As a result, QAO's strategic objectives for the system have not been adequately achieved.

From our detailed investigations and the briefings we have received from the QAO, the main problems have been as follows:

- inadequate specification of system requirements and project deliverables
- slow response times, unstable reporting and data integrity problems experienced by users, in particular managers (these problems were worse for remote users)
- poor project governance, especially allowing the vendor to conduct the process of scoping and specifying user requirements and in turn allowing the co-vendor to undertake the quality review function, including acceptance of the system.
- poor project management skills, which resulted in a failure to identify and correct the above problems, thereby exacerbating implementation issues
- disillusionment with eTrack amongst QAO staff, resulting in a poor uptake and utilisation of the system, even as improvements were made.

Difficulties arose at the outset as eTrack was not a product which incorporated a standard process. Rather, it was a shell of a system that allowed users to build in features and functionality as required. While there is some benefit in such flexibility, QAO made the

mistake of attempting to make the program fit its own internal business or work practices, not the other way around.

QAO initially did not seek to change its own work practices and specifically did not standardise and adapt disparate work practices which differed markedly between the various audit teams. As a result, diverse user requirements drove the development of a system that was highly complex, highly customised and highly tailored around the idiosyncratic work practices of particular audit teams and/or individuals.

Furthermore, QAO was probably over-ambitious as to its expectations of a practice management system and attempted to over-engineer the eTrack product. In particular, QAO attempted to link resource planning and scheduling, activity management, time recording and billing, together with performance reporting. This placed much higher demands on the system than other users, such as the New South Wales Auditor-General's Office which implemented eTrack solely as a time-sheet and billing system.

The upshot is that implementation of eTrack has taken longer than expected, and has cost more than expected. On a benefit–cost basis, it is likely that the eTrack project would rate poorly. Capital costs (including capitalisation of unbudgeted QAO labour costs) have amounted to almost \$760,000, compared with an original projection of \$417,000. Actual operating costs are also higher than initially projected. These costs include not only the items provided for in the original budget, but also additional external financial and IT expertise, plus the extra QAO effort required to improve the capability of the system and achieve the adoption of improved business practices. In addition, the costs incorporate a range of tasks transferred to the eTrack team from elsewhere in Audit Support and/or the Audit Program to increase overall efficiency (eg reports for resourcing, billing, etc).

#### 10.4.3 The Future of eTrack

The above problems have now been well recognised and documented within the QAO, and appropriate corrective action is under way. Accordingly, there is little value in any more detailed elaboration of these problems in this Report.

The initial corrective action taken by the QAO was to return to the basics, stabilise the platform and progressively eradicate the bugs which caused the system to crash. We have been advised that subsequently, action has been taken on support, maintenance and development of eTrack, including:

- server support
- consistency in loading and application of releases from eTrack products
- systems analyst support
- system enhancements, including interfaces with IPSAM, AURION and NAVISION
- system sharing with other Auditors-General, especially in New South Wales and Western Australia
- enhanced governance arrangements.

On the final point, responsibility for eTrack now rests with the General Manager – Audit Support, reporting directly to the Auditor-General, with regular reporting to the EMG and ISC. An Audit Practice Management Users Group has also been established. The eTrack workload is directed towards ongoing operational usage, introduction of related changes to business practices, and a program of system enhancements and integration with QAO's other systems.

Ongoing costs of maintaining and supporting eTrack are estimated to be about \$912,000 per annum, although there are some broader-based resourcing functions included in this cost.

Advice from the QAO is that eTrack is now providing more reliable functionality and use, and is starting to produce some of the benefits originally expected. We are not in a position to validate this assessment, as we have undertaken our review from a strategic and management perspective only, and have not sought detailed technical advice on the performance of the system. If the performance of eTrack does not improve as expected, further external technical advice may be required to resolve the problems. This is a matter for the Auditor-General and the ISC to continue to monitor closely.

There remains a question as to the long-term sustainability of eTrack as a suitable practice management system for the QAO. From discussions with the Auditor-General and the General Manager–Audit Support, they are confident that, with the planned improvements, eTrack has the capacity to provide a sustainable solution to meet QAO's future needs. Again, we are not in a position from a technical perspective to validate this assessment, and we encourage the Auditor-General and the ISC to continue to monitor the situation closely. In the meantime, the QAO should also monitor the availability and suitability of other practice management systems which may offer a better solution over the longer term.

Apart from resolving ongoing technical issues with eTrack, one of the key challenges is encouraging managers and other staff to fully embrace and use the system. Because it has performed poorly and developed a bad name, there is a natural reluctance for staff to fully utilise eTrack. Whilst improvements have been made, perceptions about eTrack have not yet changed, and it will take some time for staff to recognise and accept the enhanced capability of eTrack.

We consider that, irrespective of the problems which have occurred, it is important to leave the past behind and for the Auditor-General and the EMG to take necessary action to encourage staff to embrace and fully utilise eTrack as a core tool of their audit business.

#### Conclusions

##### *CN.10(i)*

The introduction of eTrack has not met the QAO's initial expectations, resulting in disruption to the QAO's business and disillusionment amongst staff.

##### *CN.10(ii)*

On a benefit-cost basis, it is likely that the eTrack project would rate poorly.

##### *CN.10(iii)*

Corrective actions taken by the QAO are achieving improved performance of eTrack, but more yet needs to be done to achieve a fully functional system that is properly utilised by staff.

#### Recommendation

##### *RN.10(iv)*

**That the QAO take necessary steps to ensure that eTrack provides a reliable and effective practice management system for the future, and that staff be encouraged to utilise its capabilities.**

## 10.5 Business Improvement Plan

The QAO has been pursuing a program of business improvement since 2005. The program is designed to support the Strategic Plan and the Annual Work Plan, and also to link to the individual staff LaunchPAD plans. These linkages are important.

The first three phases of the program, which have now been completed, have focussed on business restructuring, alignment and integration, which have provided important building blocks in the process. Phase 4, which is the final phase of the program, involves ensuring that business benefits are realised ie that the various business improvement initiatives do deliver tangible benefits in terms of the way that the QAO delivers its services and achieves its desired outcomes. It involves a two-year package of projects from June 2009 through to June 2011. Key components are:

- Remodelling key business processes to support the business model
- Improving resource allocation management
- Increasing business specialisation
- Improving consistency/quality of operations
- Implementing systems to improve business performance reporting
- Integrated performance reporting
- Accountability Mapping and Career Pathways (formerly Succession Planning)
- Enhanced knowledge management capabilities.

### Conclusion

#### *CN.10(iv)*

The objectives of the Business Improvement Plan 2009–11 are appropriate, but it is an extensive and ambitious program, and there will be inevitable challenges in ensuring that the program translates into enhanced business practices and improved productivity for the organisation.

## 11. WORKFORCE

### 11.1 Overview

As at 31 December 2009, there was a total headcount of 263 staff employed in QAO, including casual staff, contractors and agency temporary staff, as well as employees on leave without pay and secondments. This represents an effective workforce of 248 FTEs, just below the figure of 249 at 30 June 2009.

The size of the workforce as at 30 June for each of the last five years is shown in the following table. Overall, there has been a significant increase of over 21% in workforce numbers from 30 June 2005 to 31 December 2009, despite a one-off reduction of almost 6% in 2007–08, reflecting higher staff turnover and difficulties in recruiting in a tight labour market in that year. There was a sharp rebound of over 15% in FTEs in 2008–09 compared with the previous year.

**Size of QAO Workforce (FTEs)**

As at 30 June	No.	% change
2004–05	205.1	
2005–06	213.4	4.1
2006–07	229.0	7.3
2007–08	215.6	-5.9
2008–09	249.0	15.5

*Source: QAO Annual Report, 2008–09*

The QAO now produces regular Quarterly Workforce Reports which provide a wealth of valuable information on the nature and characteristics of its workforce. Some of the key workforce statistics are as follows:

- The QAO has a strong record of permanent employment, with 92% of its workforce comprising permanent employees (compared with an average for the Queensland public sector of around 77%).
- The gender balance is steady at around 53% male, and 47% female, with females tending to be more highly represented at lower classification levels.
- The age distribution of QAO staff is skewed towards the younger age groups, with some 26% under 30 years of age and about 44% under 35 years of age. Nevertheless, there is also a solid core of middle aged staff, with around 34% in the 35–50 years age group. Overall, the average age of staff in the QAO is around 39.7 years, which is one of the lowest of all Queensland public sector agencies, and compares with the sector average of 43 years.
- A majority of employees in the 55 and over age groups are predominantly at the AO8 and above level, which presents a risk to the QAO in terms of loss of management experience should a number of these employees retire over the next 1–3 years.
- Almost 45% of staff have less than 2 years experience in the QAO, but at the other end of the scale, around 25% of staff have more than 10 years' experience.

## 11.2 Recruitment

Attraction, recruitment and retention of staff have been key challenges for the QAO in recent years. As the audit function undertaken by QAO has a close equivalent in the private sector, there is an ongoing battle to attract and retain competent audit staff in competition with comparable roles available in the private sector. This is particularly the case when economic conditions are strong, labour markets are tight, and reward and remuneration structures in the private sector are relatively more attractive, as was the case for a number of years prior to the global financial crisis in 2008 and 2009.

On the other hand, the QAO offers a range of other attractions, including the nature and challenges of its work in auditing major Queensland Government agencies and businesses, the ability to contribute to improved public sector financial management, and a supportive work life balance. Such features are attractive to many potential employees and should remain at the heart of QAO recruitment processes.

From our investigations, the QAO has actively pursued a range of strategies for recruitment of staff, with considerable success in most cases. The graduate intake program, GRADtecs, is one of the key recruitment strategies for the QAO to meet current and future workload needs. The program incorporates technical, professional and personal development as well as a practical program to complement the training curriculum. There were 15 graduates who participated in the 2008–09 program, and there are currently 9 graduates participating in the 2009–10 program.

Over the last 10 years, 119 graduates have been employed by the QAO. Retention of graduates is strong, with 68 of those graduates still employed in the QAO as at 30 June 2009, representing an overall retention rate of 57%. Graduate recruitment and retention over the 10 year period is shown in the following table.

**Graduate Recruitment**

Year	No of Graduates Recruited	No of Graduates Retained (as at 30 June 2009)	Retention Rate %
2000	4	2	50
2001	13	4	30
2002	17	5	29
2003	10	4	40
2004	12	7	58
2005	10	5	50
2006	9	5	55
2007	15	8	53
2008	14	13	92
2009	15	15	100
<b>Total</b>	<b>119</b>	<b>68</b>	<b>57</b>

Source: QAO Workforce Reports

## Conclusion

## CN.11(i)

The recruitment strategies of the QAO are commended, especially the GRADtects program, and the QAO is encouraged to continue to refine and develop these strategies to meet future needs, whilst reinforcing the particular attractions and benefits of working in the QAO.

### 11.3 Staff Retention and Turnover

Staff turnover provides one measure of the internal health or morale of an organisation. It is also important in shaping recruitment and retention strategies, especially in relation to skills and experience. We examined QAO staff turnover since 2004–05, and also compared QAO's experience with that of other Audit Offices, as recorded in ACAG benchmarking studies.

Apart from 2007–08, when there was a significant jump to around 20%, staff turnover in the QAO has remained relatively stable at around 11–12% for the last five years, as shown in the table below.

#### QAO Staff Turnover

Year	%
2004–05	12.4
2005–06	12.6
2006–07	11.7
2007–08	20.4
2008–09	11.3

Source: QAO Annual Report, 2008–09

The relatively high figure of 20% recorded in 2007–08 would appear to be somewhat of an aberration, reflecting largely attractive employment opportunities elsewhere in an overheated labour market in Queensland and Australia at the time. Certainly, the return to a more normal rate of 11% in 2008–09 would tend to suggest that there are no sustained underlying internal issues that gave rise to such a large spike in turnover in 2007–08.

Even though the 2007–08 turnover was high, the QAO still compared favourably with Audit Offices in other jurisdictions, all of which experienced a spike in turnover rates in that year. ACAG benchmarking surveys are based on a slightly different measure of turnover, being the average staff attrition rate, defined as FTE cessations of permanent staff as a percentage of the FTE number of permanent staff. Using this measure, the QAO attrition rate was 18%, compared with an average of 24% across Audit Offices in all jurisdictions. Apart from South Australia and Tasmania, all other Audit Offices recorded rates in excess of 20%, with the ANAO the highest at 32%.

In our Terms of Reference for this Review, we were asked to take into account interviews with staff, including former staff of the QAO, although it was noted that interviews with former staff were optional.

In the interests of attracting as wide a cross-section of responses as possible, we sent a standard form letter to all former staff of the QAO in the last five years, at their last known address held by the QAO, inviting submissions and/or the opportunity for personal

interviews. Although the response was limited (which was not surprising), we did speak with a small number of former staff and received useful feedback. Some specific issues of concern were raised in these discussions, but there was nothing to suggest any broad-based disenchantment or dissatisfaction with the QAO that would give rise to concern.

The QAO routinely conducts exit interviews with departing staff. We were provided with summary information for all exit interviews conducted during 2007–08, and 2008–09, as well as a progress report for 2009–10. Relevant statistics on gender, age group, length of service and reasons for leaving are outlined in the accompanying table relating to 2007–08 and 2008–09.

In both years, some 60% or more of the departures were for staff with under two years of service, and over 45% were in the under 30 years age group (although there was also 45% of departures in the 40–55 age group in 2008–09). Consistent with trends experienced elsewhere in the workforce, this tends to suggest some issues for younger aged staff with a short length of experience in QAO.

Caution needs to be exercised in drawing conclusions from these statistics, given the small sample size involved. Nevertheless, there does not appear to be any systemic or underlying reason for the departures of staff evident in the feedback from these exit interviews.

Comments made by staff in exit interviews were mostly positive and encouraging, but there were a few more critical comments about management, training and the work environment. Nevertheless, it should be reiterated that such comments were the exception rather than the rule, and we are confident that the QAO has in place human resource processes to identify and address these issues.

In summary, based on our experience with other organisations, we consider a turnover rate of around 11% to be at the top end of an acceptable range for an organisation such as the QAO. It does not give rise to any significant concerns, although there would be a concern if the rate was to creep any higher again. As an aspirational target, it would also be preferable for turnover to be lower than 11–12%, and the QAO should actively pursue strategies designed to reduce the rate to single figures.

#### **11.4 Remuneration and Reward Structures**

Apart from the Auditor-General, staff of the QAO are employed as public servants under the *Public Service Act 2008* and are subject to standard public service awards and conditions. This includes a pay scale aligned with the administrative pay scale for the public sector generally. Accordingly, most audit positions within the QAO correspond with the AO2–AO8 administrative pay scale, with Directors of Audit at the SO level and Assistant Auditors-General at the SES level.

Under public sector remuneration structures, there is very limited opportunity for QAO staff to boost their remuneration through superior performance, other than through promotion under a merit selection process. This requires the availability of a promotion opportunity within the organisation. There is no other avenue for monetary rewards, although there are some non-monetary rewards available at times, such as increased access to training and development opportunities.

## QAO Exit Interviews: Key Metrics

Completed		% or count	
		2007–08 29	2008–09 11
<b>Gender</b>	Male	48.0%	18.0%
	Female	52.0%	82.0%
<b>Age group</b>	Under 21	3.5%	0.0%
	22–29	45.0%	45.5%
	30–39	31.0%	9.0%
	40–55	17.0%	45.5%
	55–60	0.0%	0.0%
	60 and over	3.5%	0.0%
<b>Length of service</b>	< 1 year	21.0%	64.0%
	1–2 years	38.0%	18.0%
	2–5 years	17.0%	0.0%
	5–10 years	7.0%	9.0%
	10–20 years	14.0%	0.0%
	Over 20 years	3.0%	9.0%
<b>Reasons for leaving</b>	Family responsibilities	4	1
	Full time study	2	0
	Moving to a new location	2	2
	Age retirement	2	0
	Travel	2	0
	Taking a position closer to home	2	1
	Better job opportunities	14	5
	Health reasons	0	2
	Other	11	2

Source: QAO

The 2004 Review expressed considerable concern about the remuneration and reward structures then prevailing in the QAO. The Review concluded, inter alia, that

*“the current remuneration structure within the QAO does not adequately recognise the professionalism, competency and experience of the audit staff”*,

and recommended that

*“a more flexible remuneration structure for the professional audit staff be introduced which is based on professional development, experience, competency and skill measured against appropriate benchmarks”*

but noted that

*“there is no real justification for the introduction of performance pay and other similar reward programs within the QAO”*.

On this matter, the Government’s Response to the 2004 Review noted that

*“The Government has no objection to this matter being further pursued by the Department of Industrial Relations and the Public Service Commissioner. It notes, however, that there are significant implementation issues that would have to be addressed in the development of any remuneration arrangements before this could be further considered.”*

We are concerned at the rate of progress that has been made towards introducing a more flexible remuneration structure for professional audit staff since the 2004 Review. A review of the remuneration structure was undertaken by an external consultant in 2006, but subsequent progress was stalled because of the challenges and difficulties of implementing a system outside of the core public service arrangements. It was then decided to pursue initiatives within the current award and employment arrangements.

The QAO considers that the AO based structure has been able to respond to the needs of staff for progression and promotion as they acquire skills and experience. Analysis provided by the QAO of the progression from graduate positions showed that graduates were progressing from the entry level AO3 position to an AO4 position in an average of 1.4 years, and to an AO7 position in an average of 6.4 years.

From our observations, the AO salary stream has proven to be attractive and competitive in the market place at the lower AO3–AO4 levels (usually in the first two years or so of employment of graduates), and this has provided the QAO with a level of success and flexibility in its resourcing practices. However, beyond the first two years, and in the mid range of the AO scale, remuneration tends to become less competitive with comparable private sector audit positions. This is where the QAO remains vulnerable to the loss of good quality graduates, particularly in times of stronger economic conditions and tighter labour market conditions, when private sector remuneration tends to rise more rapidly than in the public sector. In such circumstances, the incentives to move to private sector auditing roles are greater in relative terms.

Since 2005, the QAO advises that there have been a number of discussions with the Public Service Commissioner which indicated that it would be difficult to change the QAO’s remuneration structure. However, the concept of a professional progression scheme was suggested to improve the linkages between qualifications, experience and remuneration. In relation to qualifications, the auditing environment is becoming more complex, with significant pressure to ensure that audit work meets the requirements of the new international (IFRS) and national (eg APES 320) accounting and auditing standards.

This has led to a proposal to introduce the Professional Auditors Skills Scheme (PASS) to create a better framework for the recruitment and retention of professional staff. PASS will

enable financial and compliance audit staff in the first instance to transition from the administrative (AO) pay scale to the Professional Officers (PO) pay scale based on tertiary qualifications, skills, competency and industry certification. In particular, it will provide explicit encouragement and recognition for the achievement of industry certification, such as the CPA or CA or equivalent.

The benefits which the QAO expects to achieve with PASS are:

- Providing the QAO with a point of difference based on skills and knowledge
- Streamlining early career progression, particularly at the PO2–PO3 level
- Providing a positive outcome for staff (eg benefit, prestige)
- Linking effort/merit to reward
- Retaining flexibility to meet workload/workforce demands

In December 2009, the PASS proposal received formal support of the Director-General of the Department of Justice and Attorney-General and work has commenced on the progressive, phased implementation of the scheme.

We support the continued efforts by the QAO to implement PASS, and acknowledge that there are likely be some benefits along the lines noted above. However, at best, this is likely to provide only a partial solution. We have reservations that it will deliver significant benefits in terms of a more flexible remuneration structure. Internal analysis by the QAO suggests that there will be little salary benefit in terms of a direct comparison of AO and PO scales, except at the PO2 and lower part of the PO3 scale. Also, based on case studies of progress by previous QAO graduates, it is not clear that, on average, there will be any more rapid progress to the higher PO5/PO6 levels and salaries than has previously been achieved in progress to the AO7/AO8 classifications.

We note that, since 2004, the Audit Office in NSW has been a statutory body and the Auditor-General has had the ability to determine remuneration arrangements for the Audit Office separate from standard public sector arrangements. This has led to the establishment of a separate award for NSW Audit Office staff. However, no other Australian jurisdiction has yet adopted such a model for its Audit Office. While there is some attraction to the greater flexibility in remuneration provided by the NSW model, we do not consider that it is necessary to adopt such an approach for the QAO at this time.

We believe that there remains some scope for increased flexibility of remuneration arrangements for the QAO within the existing framework of the *Public Service Act*, especially to respond to periods of heightened competition from aggressive private sector audit remuneration arrangements. For example, we are aware that the now-defunct Transport Infrastructure Capability Scheme (TICS) was introduced several years ago to provide additional allowances to engineers to combat the highly attractive remuneration packages being offered by the private sector in an overheated labour market in Queensland.

The TICS arrangements may provide a model that could be adapted to the QAO's requirements in circumstances where there is the threat of substantial leakage of staff to the private sector (as occurred in 2008 prior to the onset of the global financial crisis). However, it needs to be appreciated that such allowances are designed to be of a temporary nature. They should not be built into salary base, and should be capable of being withdrawn or scaled back should competitive market conditions abate.

Further flexibility in remuneration arrangements for the QAO may also be provided by contracts established under Section 122 of the *Public Service Act*. These could be used for

example to assist in the retention of key staff whose loss would represent a serious risk for the QAO.

If the QAO has difficulty in the future in attracting and retaining staff under the remuneration framework provided by the *Public Service Act*, then it may be necessary to revisit the case for adopting the NSW model for greater remuneration flexibility.

#### **Recommendation**

##### ***RN.11(i)***

**That the QAO continue to pursue strategies for achieving a more flexible remuneration structure for professional audit staff. It would be beneficial for the QAO to investigate this matter further in conjunction with the Public Service Commission and the relevant Government department.**

### **11.5 Gender/Equity Issues**

The 2004 Review raised some concerns as to whether the QAO was achieving appropriate gender and equity outcomes, and made several recommendations to address these issues.

The QAO has implemented a number of strategies to address these recommendations, including the establishment of the Women's Leadership Group, and the provision for two members of the EMG to be nominated by this Group. Other initiatives have been designed to ensure that recruitment and selection processes avoid any inherent biases.

Since the Women's Leadership Group was established in 2004–05, the following has been achieved:

- The proportion of female staff between the grades AO6–SO has increased from 30.5% (2005) to 40% (2009)
- The total number of female staff at AO8 level and above has increased from five (2005) to 18 (2009).
- Female staff now represent 47% of all QAO staff, and there are now more female staff than male staff at the AO2–AO6 levels.

While female staff remain under-represented in senior management levels, we note that encouraging progress has been made. There is one female appointment at the SES level (being the Assistant Auditor-General, PMS Audit), and there were several appointments of female staff to SO positions during 2008–09. This continues to be a focus for QAO strategies and we are satisfied with the efforts of the QAO on gender issues.

Nearly 29% of QAO staff identify themselves as being from a non-English speaking background (NESB), which is a relatively high level of representation, compared with the average across the public sector. This is in part due to natural factors, as the auditing profession has tended to attract heavy interest from the NESB group. For the QAO, this has delivered strong benefits in terms of cultural diversity, although English language writing and speaking skills require some attention as part of internal training programs.

### **11.6 Training and Development**

The 2004 Review gave a high priority to training and development issues, with a number of supporting recommendations, including an increase in the level of funding to a minimum of 1.5% of the QAO Budget, to at least \$400,000 per annum.

The QAO advises that time spent on internal and external training courses (including presentation and development) amounted to 15,395 hours in 2008–09, equating to an estimated value of \$1.167 million of expenditure. As reported in the QAO Annual Report, professional development represented 2.9% of total expenditure, up from 2% in 2004–05.

We are satisfied that the QAO is giving sufficient priority to training and development and has fulfilled the expectations of the 2004 Review.

### **11.7 Performance Management**

Performance management frameworks have become a standard human resource tool for assessing and managing the performance of staff in organisations in recent years. However, there is significant variability in the range of frameworks, the way that they are applied in organisations, and their overall effectiveness in both rewarding good performance and addressing poor performance.

The QAO has previously used a paper-based performance management framework, with only limited success as it did not engender full engagement of staff, particularly audit staff. The QAO has now implemented an electronic system which it has called LaunchPAD, in conjunction with the Lominger competency base developed internationally by Korn Ferry. This has produced a much higher level of engagement, with take-up rates increasing from an estimated 30% previously to 96% now.

LaunchPAD provides a language and framework which enables a more disciplined approach to performance assessment, and better monitoring of the process to ensure effective compliance. It provides a language for supervisors to talk with their staff in a way which is designed to be factual and remove much of the emotion and personality influences from the performance review process.

The advantage of this system is that it provides clear linkages or integration from the audit task, through to job competencies (reflected in Lominger), and in turn to the performance assessment process. To date, what has emerged is the identification of a number of performance issues with staff that previously had not been identified or addressed. These issues are currently being worked through, with a view to achieving improved performance and productivity of individual staff members and the organisation as a whole.

Initial outcomes suggest that the implementation of LaunchPAD is a positive move by the QAO which has been embraced by the vast majority of staff. However, more remains to be done to fully embed LaunchPAD in internal management processes on an ongoing and sustainable basis.

Also, we remain concerned that incentive structures in the public sector environment in which QAO operates do not provide the same encouragement for superior performance as is the case in comparable private sector audit businesses. As a result, whilst a framework such as LaunchPAD can contribute to improved performance of staff, there are nevertheless limitations on the extent to which such improvements can be achieved unless adequate incentive structures are in place. Remuneration and reward structures have been addressed earlier in this Section.

### **11.8 Other Human Resources Policies and Procedures**

The QAO has a comprehensive suite of policies and procedures, including human resources policies and procedures, covering: conditions of employment; leave; remuneration and benefits; recruitment and selection; employee separation; health and welfare; organizational behaviour; diversity management; performance management; and professional development.

We have reviewed these policies and procedures, which are generally consistent with standard public service conditions. We are satisfied that they are appropriate for the QAO, except where we have specific conclusions or recommendations in other parts of this Section.

We received no substantive representations or concerns regarding these policies, apart from the issue of banked time arrangements. In our view, the previous banked time arrangements were more favourable than comparable arrangements elsewhere in the public service, and it is ultimately the prerogative of management to structure such arrangements in a way which does not compromise the business needs of the organization. However, we would make the comment that the timing and communication of the rationale for the new arrangements were not well managed, and there are lessons as to how changes of this nature should be handled in the future.

#### Conclusion

##### CN.11(ii)

Changes to staff benefits and other human resource policies are normally highly sensitive and often emotional issues, which need to be managed carefully to minimise adverse reactions and impacts.

#### Recommendation

##### RN.11(ii)

**That the Auditor-General ensures adequate consultation and communication with staff, and takes account of timing issues, in undertaking any major or sensitive changes in staffing benefits or other human resources policies.**

## 11.9 Culture

From our discussions with staff and stakeholders, there is a strong and positive culture within the QAO. It is a highly professional organisation with a commendable work ethic and dedicated staff. Typical comments we received from staff were that it is a “*good working environment*”, “*great place to work*”, “*professional and proud organisation*” and “*supportive team environment*”.

A distinctive aspect of the culture is that staff feel that they can make a contribution to the “public good” through the highly responsible role of auditing the activities of government. There is a special “feelgood” factor in being involved as part of the integrity and accountability framework of government.

Another distinctive aspect is that the QAO features elements of both a core government agency and also a private sector audit business. Unlike some other parts of the public service, there is a very close private sector comparator to the audit function performed by the QAO. This can have its disadvantages, particularly where private sector audit firms are able to compete aggressively to recruit QAO staff through more attractive remuneration packages.

One of the ongoing challenges for the QAO is to strike the right balance between the public service framework within which it is embedded on the one hand, and the need to operate as an audit business (especially billing clients for audit services performed) on the other hand. There will at times be tensions in this balance of roles. However, as the auditing role becomes more demanding, and the business of government becomes more complex, there will need to be some cultural shift for the QAO to place greater emphasis on the need to model its operations more closely on the practices, systems and culture of private sector audit businesses (albeit within the parameters of a public sector entity).

## Conclusion

*CN.11(iii)*

The QAO needs to continue to improve the way it operates its business, by adopting where relevant the best practices, systems and culture of comparable private sector audit businesses.

### 11.10 Staff Survey

Since 2003, the QAO has been conducting Staff Surveys to obtain feedback on a range of workforce and staffing issues. To date, Surveys have been conducted in 2003, 2004, 2006, 2008 and again in 2009. As a standard set of questions and methodology has been used, this provides a consistent set of results to analyse trends or patterns of responses over time for the five surveys. The aggregate results of these surveys provide a useful background and context to this section on Workforce Issues.

Whilst it has been normal practice to conduct the Staff Survey every two years since 2004, the 2008 Survey results showed a disturbing deterioration in the level of favourable responses. As a result, a further Survey was conducted in 2009, which broadly showed a recovery from the 2008 results, to levels previously achieved in earlier surveys.

The aggregate results from the 2009 Survey are as follows:

- Staff Satisfaction Index of 68%, a significant improvement on the 2008 result of 57%, and in line with survey results in 2003 and 2004.
- Leadership and Management Index of 60%, also an improvement on the 2008 result of 54%, but no better than results in 2003 and 2004.
- Immediate Superior/Team Leader Effectiveness Index of 76%, a significant improvement on the 2008 result, and the highest level achieved in the five surveys.
- Employee Engagement Index of 71%, a significant improvement on the 2008 result, and marginally better than 2003 and 2004 results.

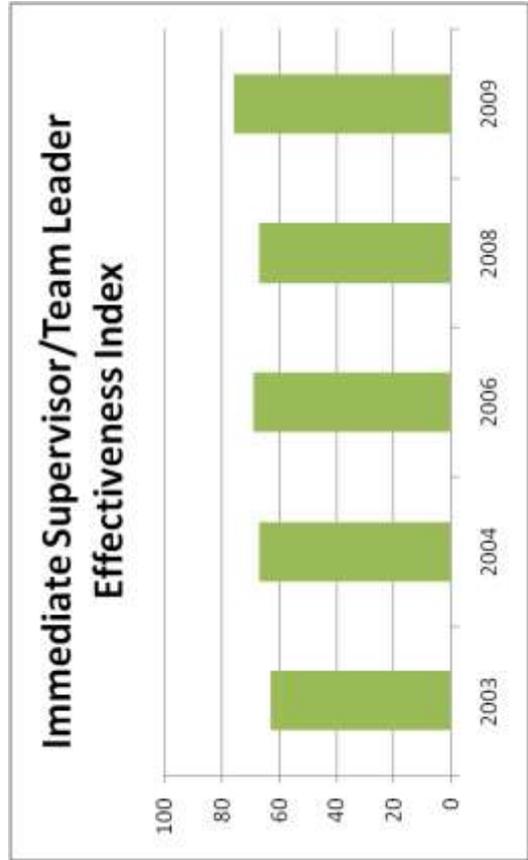
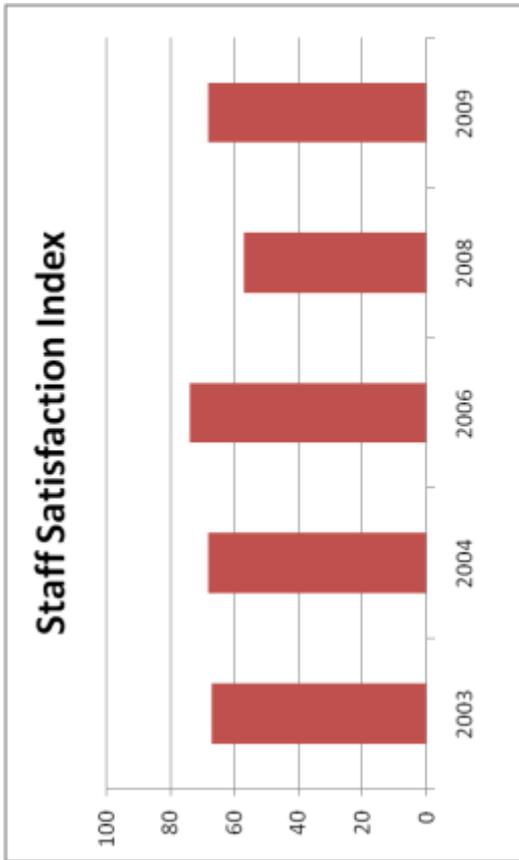
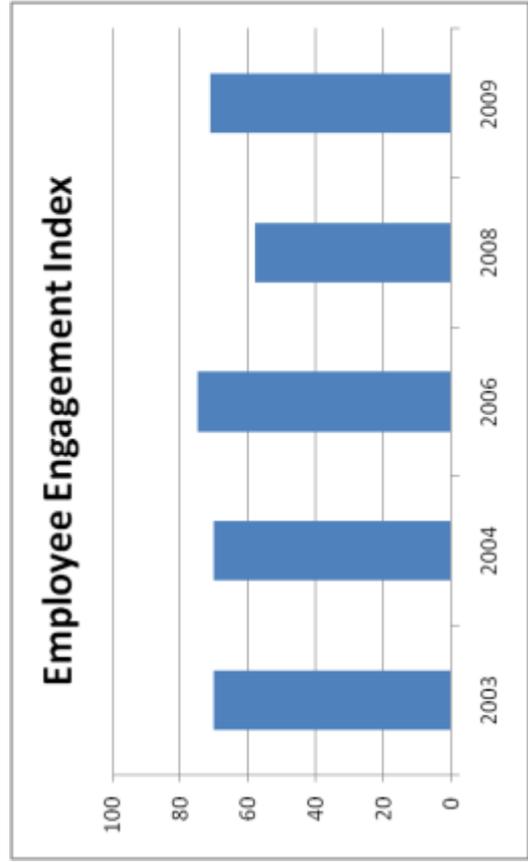
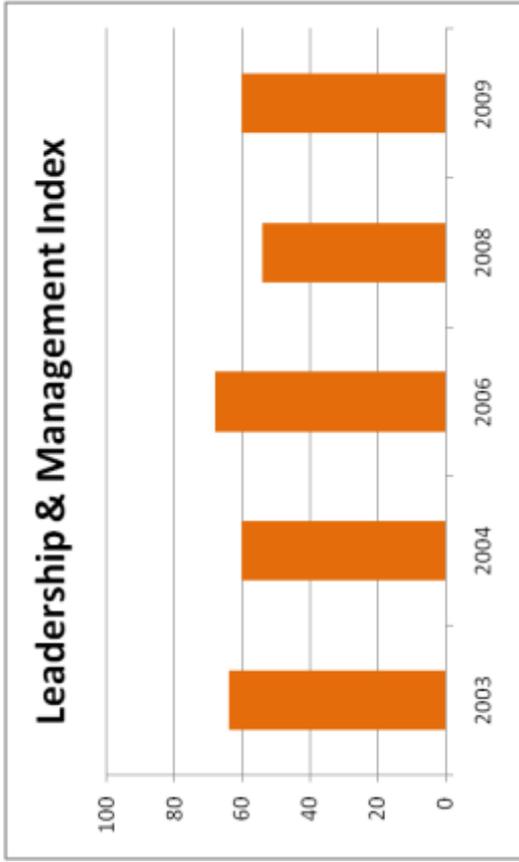
Trends in the results for each of these key indexes are shown in the accompanying charts.

The aggregate results are generally satisfactory, with a recovery across the board in 2009 from a poor set of results in 2008. However, the variability in results over time is a cause for some concern, with aggregate indexes in 2009 generally on a par with results achieved in earlier surveys in 2003 and 2004, but not back to the levels achieved in 2006. It is disappointing that the aggregate results have not shown any consistent pattern of improvement despite the significant initiatives taken by the QAO to address workforce issues, as outlined above.

To a certain extent, there may be a degree of “reform fatigue” impacting the survey results, especially for 2008, compounded by the obvious staff dissatisfaction with the initial performance in the implementation of eTrack. In addition, there were higher levels of staff turnover recorded in 2008, reflecting possibly attractive private sector remuneration and opportunities in the overheated labour market prior to the onset of the global financial crisis. With the subsequent deterioration in labour market conditions, staff turnover returned to more normal levels in 2009.

The EMG will need to continue to monitor staff attitudes and satisfaction over the next few years, as some overall trend improvement should be expected from the various workforce initiatives which are still in the process of being bedded down.

Summary of Key QAO Staff Survey Results



Source: QAO Pulse Staff Survey 2009

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## 12. COMMUNICATION

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### 12.1 Overview

Communication is a basic tool of business for any organisation. The internal and external communications of an organisation often shape the way it is perceived by stakeholders and in turn the way it is treated by those stakeholders.

The QAO has rightly recognised the critical importance of effective communications in its business and has put in place a number of strategies designed to achieve and maintain high standards of communication, and to strive to continually improve those standards. We are impressed by the progress shown by the QAO and encourage it to continue to place a high priority on this facet of its business. While strong progress has been achieved, constant attention is required to ensure standards do not slip in a constantly changing and often unpredictable environment.

The QAO has a wide range of stakeholders, and this section of our Report reviews the way in which QAO interacts with these stakeholders in different ways and for different purposes, consistent with its overall strategic objectives.

### 12.2 The Parliament and the PAPWC

The Queensland Legislative Assembly is the primary client of the QAO, and the Auditor-General is ultimately accountable to the Parliament for the performance of the QAO through the *Auditor-General Act 2009*.

In practice, involvement of the Parliament in the activities of the QAO is conducted through the PAPWC. On 19 May 2009, a bill was passed in the Legislative Assembly amending the *Parliament of Queensland Act 2001* to merge the Public Accounts Committee and the Public Works Committee into a single Committee entitled the Public Accounts and Public Works Committee (PAPWC). The PAPWC's areas of responsibilities, as described in Section 95 of the Act include, inter alia:

*“(a) the assessment of the integrity, economy, efficiency and effectiveness of government financial management by:*

- Examining Government financial documents; and*
- Considering the annual and other reports of the Auditor-General.”*

A basic part of the PAPWC's work is to consider and follow up matters raised in the reports to Parliament by the Auditor-General. This means that considerable importance attaches to the way in which these reports are prepared and presented by the QAO. The QAO has devoted substantial effort to improving the readability of its reports to Parliament, particularly the removal of unnecessary jargon, and is to be commended for these efforts. We encourage the QAO to sustain its efforts to ensure that its reports are as user-friendly as possible.

As recommended elsewhere in this Report, we consider that the QAO should consult with the PAPWC in the preparation and publication of a Strategic Audit Plan for performance audits, although it is essential that ultimate decision-making responsibility for the Plan rests with the Auditor-General. More broadly, we encourage greater interaction – both informal and formal – between the QAO and the PAPWC on the full range of the QAO's activities. Whilst it is outside the Terms for Reference for this Review, it would be helpful from the QAO's perspective for the PAPWC to adopt a formal public sign-off process for all QAO Reports to Parliament, even if it does not intend to take further action on reports.

### 12.3 Audit Clients

In 2008–09, the QAO had 329 audit clients, comprising core government departments, GOCs, statutory bodies, universities, grammar schools and local governments. This number has declined somewhat as a result of the extensive amalgamation of local councils undertaken by the Queensland Government and completed in 2008. The QAO generally has a broader range of clients than Audit Offices in other jurisdictions, some of whom do not have responsibility for auditing of local councils (eg Australian National Audit Office and Western Australia).

From a formal legislative perspective, audit clients are the secondary clients of the QAO. However, from a practical perspective, audit clients should be regarded as primary clients, in that they pay fees for the professional audit services provided by the QAO, and they are the clients with whom QAO interacts most frequently and intensively, usually on a day-to-day basis.

Some audit clients expressed concern that they are treated as “captive clients” by the QAO. It is certainly the case in terms of legislative provisions that public sector entities do not have a choice of auditor. There is a perception amongst audit clients that they are not necessarily treated in the same way by the QAO as private sector audit firms treat their clients. It is our view that all of the QAO's audit clients should be treated as if they could take their audit business elsewhere, that their business is in effect contestable, and capable of being lost if the performance of the QAO is not regarded as being acceptable. This would require the QAO to be more accountable for its performance than audit clients currently consider to be the case.

The QAO uses a wide range of tools for communicating with audit clients, from daily informal verbal and written communication through to electronic material, as well as more formal documentation, including the annual Client Services Plan (Audit Plan) and Management Letters. The QAO has made improvements to its Client Services Plans since the 2004 Review. However, some audit clients expressed dissatisfaction with the content and quality of these plans. It is apparent that there are some inconsistencies in approach between audit teams in the way plans are prepared and negotiated with audit clients. This requires ongoing attention to ensure a consistent quality in terms of both content and approach. In Section 7 of this Report, we have also made recommendations regarding the need for better communication with audit clients to explain the level and composition of fees, and variations in fees, as part of the Client Services Plan.

The QAO's Annual Client Briefing sessions are highly regarded by audit clients, and should be maintained and expanded wherever possible. There is a need to continually refresh and upgrade these sessions, and especially to heed feedback from audit clients, to ensure they remain relevant and useful. The reach of these sessions could be expanded by greater use of multi-media facilities, including video-conferencing, webcasts, podcasts and other emerging technologies for advanced communication. A number of audit clients in regional areas expressed considerable interest in such electronic forms of communication, noting that it is costly to send more than one or two representatives to Brisbane to physically attend the briefing sessions, but that a much larger number of staff could take advantage of multi-media communications on the ground in their home base.

The QAO undertakes regular Client Surveys, currently through Orima Research as part of benchmarking surveys conducted under the auspices of ACAG. Overall, the QAO is rated around the average of other Audit Offices across a broad range of indicators and activities. For example, the QAO is ranked fourth out of six jurisdictions for aggregate performance indicators for both Financial Audit Client Surveys and Surveys of Performance and Related Audit Clients.

In our view, the QAO should be aiming to be ranked within the top 2–3 Audit Offices across Australia in aggregate, rather than simply being satisfied to be “middle of the pack”. Specific issues are addressed in other sections of this Report.

In relation to Communications issues specifically, for the latest ACAG Benchmarking Parliamentary and Audit Client Survey for 2008–09 (August 2009), the QAO ranked the highest of all Audit Offices surveyed, achieving a slightly better result than the previous year – with 88.8% of clients provided a favourable response to the statement that: “*communication between the auditors and our organisation was effective*”. All jurisdictions achieved favourable response rates in excess of 80%.

Nevertheless, there were some suggestions from respondents for improved communications. Some specific comments were:

- “*once the audit moved off site communication proved difficult and getting agreement to some very minor issues proved to be a very frustrating and time consuming exercise*”.
- “*we found that there was a lack of understanding displayed by the contract auditors and apparently poor liaison with the QAO. We also found it totally unacceptable that the responses from the QAO took more than six months, and even further delays occurred after that.*”

Our discussions with audit clients were generally consistent with these survey results. Overall, communication was considered to be of a high standard, but there were some specific instances of, and areas for, concern. These tended to be of a one-off or individual nature, rather than being evidence of a more systemic problem. As previously noted, the main areas that need further attention are:

- Communication re Client Services Plan
- Communication re audit fees
- Consultation re terms of reference for PMS and cross-sector or whole-of-government audits.

Some audit clients whom we interviewed were concerned by a perception that at times there appeared to be differences in views on particular audit issues between the financial and compliance auditors and APQ. From the perspective of these audit clients, this led to a degree of confusion and tension, with consequent delays in the process of finalisation and sign-off of audits while such differences were resolved.

- The QAO is currently in the process of developing and rolling out a new Client Relationship Management Framework designed to improve the consistency, quality and capability of QAO staff engaging with and adding value for clients. The CRM includes a focus on better practice client communication. We support the CRM initiative, especially the need for greater attention to be paid to the issue of “having difficult conversations with clients”. As noted by the QAO, the three most difficult conversations with clients are where: “*we haven’t met our performance commitment*”.
- “*we don’t feel confident justifying a fee or a finding*”.
- “*we have found a material issue that will have a profound impact on the client and their business.*”

As recognised in the CRM, this will usually require the support of senior management, at the very least, to prepare for such conversations.

We believe that the CRM needs to be based on the premise that all clients are treated as contestable clients, and capable of being lost, as this will drive better behavioural relationships and communication with clients.

A further communication issue raised by audit clients in regional areas was the desire for some visibility from the Auditor-General. In this regard, the Auditor-General is well known and visible to many Ministers, Accountable Officers and Chief Executives of GOCs based in Brisbane. It is difficult to achieve the same level of visibility outside of Brisbane, due to the logistics, time and costs of regular regional visits. Nevertheless, any regional visits are highly appreciated and serve to boost the profile of the QAO. In previous years, the Auditor-General has undertaken a limited program of regional visits, but this seems to have been scaled back in 2008 and 2009 due to work pressures.

#### Conclusion

##### *CN.12(i)*

The Auditor-General should recommence a regular program of 3–4 visits of 1–2 days each to key regional centres in Queensland each year.

## 12.4 Central Agencies

Over a long period of time, the QAO has established and maintained a close working relationship with the central agencies of the Department of Premier and Cabinet and the Treasury Department, primarily through the strong professional relationships forged between the Auditor-General, the Under Treasurer and the Director-General, Department of the Premier and Cabinet. This close working relationship is highly desirable, as it enables a robust exchange of ideas, a ready flow of information and open communication between the entities.

In the 2004 Review, it was suggested that a Memorandum of Understanding be established with Treasury to clarify the relationship between the QAO and Treasury in regard to financial management in the public sector. The 2004 Review noted that, while Treasury has primary carriage of policy in relation to such matters, the QAO had a vital interest in financial management policy and had much to contribute in terms of its knowledge and experience.

The proposal for a Memorandum of Understanding has not been pursued by the QAO or Treasury on the basis that it was considered unnecessary and of limited value to formalise a relationship in this manner. We concur that it would seem to be unnecessary to establish any formal arrangement, in view of the close working relationship that operates on a more informal and flexible basis. Without such a working relationship, it is unlikely that a Memorandum of Understanding would achieve anything much more than inaction or perhaps unnecessary tension between the organisations.

The informality of the relationship with Treasury is also to be preferred, as it enables the QAO to be consulted and to provide advice from time to time on financial management issues, but yet to remain independent of the policy and decision-making processes of Executive Government.

There is a danger that communications between the QAO and central agencies become too heavily dependent on the professional relationships between the heads of the respective organisations. Whilst such strong relationships are highly desirable and mostly beneficial, it cannot be assumed that they will continue to exist should there be changes in personnel in these roles, as will inevitably be the case sooner or later. Therefore, it is important that there

should be greater effort to strengthen communications and relationships more extensively through each of the organisations, rather than just at the top.

There was some concern expressed by central agencies about a perceived tendency for QAO Reports, particularly reports on PMS or cross-sector audits, to make recommendations for implementation of new or additional whole-of-government protocols or standards to be promulgated and enforced (or at least monitored) by central agencies. While such recommendations may be relevant in certain circumstances, it was felt on other occasions that more targeted or agency-specific recommendations could be more appropriate in addressing specific areas of concern.

For central agencies, there is also a need to consider the benefits and costs of any proposed additional whole-of-government protocols or standards which may be recommended by the QAO (such as the additional cost burden of implementation and monitoring by central agencies and compliance by line agencies), especially in the absence of any off-setting rationalisation or consolidation of the overall governance, regulatory or compliance burden for core government agencies.

#### Conclusion

##### *CN.12(ii)*

Issues identified from audits may have a whole-of-government impact through the need to implement revised protocols or standards. The QAO should ensure that any recommendations arising from any observed accountability deficiencies identify the potential impact on the operations of Government that may follow if the issue is not addressed. As part of this process, the QAO should consult with responsible entities (especially central agencies) about the practicability of any proposed recommendations, particularly in terms of the overall level of regulatory burden that may result from addressing the issues raised by the Auditor-General and the risk and cost to Government if no action is taken.

## 12.5 Executive Government

Communication between the Auditor-General and the Premier, the Treasurer, other Ministers and Departmental and Accountable Officers is generally conducted on an “as needs” basis, and is predicated on a mutual trust and understanding. The relationship with Executive Government is strong. We received positive feedback on the background briefings provided by the Auditor-General on matters of relevance contained in Audit Reports to Parliament. In addition, the QAO faithfully and diligently ensures that Accountable Officers are given adequate opportunity to comment on issues pertaining to their agencies before Audit Reports to Parliament are finalised.

We understand that the Auditor-General participates from time to time (generally by invitation or request) in the regular meetings of the CEO Leadership Team (chaired by the Director-General, Department of the Premier and Cabinet), but does not attend on a regular ongoing basis. We consider this to be appropriate, as it is important for the Auditor-General to be, and to be seen to be, independent of Executive Government. However, there would be value in the Auditor-General receiving the agenda and/or minutes of the CEO Leadership Team meetings, so that he is kept fully informed of key issues and developments being considered by Executive Government.

## 12.6 Staff

The 2004 Review commended the QAO on its culture of communication and noted the high level of commitment to improved communication internally, including the intranet facility

and the use of technology to share knowledge within the QAO. Since the 2004 Review, further significant progress has been made in internal communications with staff, building on these earlier achievements and reinforcing the commitment to continually strive for better outcomes.

We received mostly positive feedback on communications matters during our group discussions with staff, although there were isolated instances of dissatisfaction or breakdowns in communication, as will always be the case. There was some evidence of variability in the level of communication from EMG members to their individual work teams, possibly reflecting the individual personalities and styles of Managers.

The QAO also conducts a regular Staff Pulse Survey to obtain feedback on a range of staff issues, including staff satisfaction, leadership and management issues and employee engagement. Major findings from the Pulse Survey are discussed elsewhere in this Report. There is only one question in the Survey directly relevant to internal communications issues. In relation to the statement “*Executive Management keeps me informed about future plans and directions*”, 65% of responses were favourable in the 2009 Survey results. This was in line with the Service Sector Benchmark for “All Service Occupations”, and substantially higher than the benchmark for “Professional Services Only”. The 2009 result was an improvement on the 2008 result, but not as good as in 2006 and earlier Survey years.

#### Conclusion

##### *CN.12(iii)*

The QAO should take action to ensure greater consistency in communications to staff on the outcomes of EMG meetings, by ensuring that Minutes of EMG meetings are regularly posted on the intranet site on a timely basis, and are discussed as a matter of course by all EMG members in their team meetings.

## 12.7 Media

The 2004 Review noted the tendency for the then Auditor-General to be drawn into media debate on Audit Reports to Parliament and suggested the establishment of a set of protocols for dealing with the media.

We note that the current Auditor-General does not normally issue press releases regarding the release of Reports to Parliament. We are heartened that the Auditor-General has seen fit to minimise engagement with the media and has preferred to rely on his reports to speak for themselves in the public arena.

At the same time, the QAO has made strenuous efforts to ensure that Reports to Parliament are more readable and user-friendly, thus obviating the need for any further clarification or elaboration by the Auditor-General in the public arena. We encourage the QAO to continue to strive for improvements in the way that it presents its reports in “plain English” to enhance public understanding of admittedly complex financial management issues.

We consider that it is appropriate and proper for the Auditor-General not to comment on his Reports to Parliament, and to eschew media and public debate, as a matter of course. Given this policy, it has become unnecessary to establish a set of protocols for dealing with the media. However, if this policy was to change (for example, with a future Auditor-General), then it would be desirable to revisit the issue of establishing a set of media protocols.

## 13. WORKLOAD AND PERFORMANCE

### 13.1 Trends in Workload and Performance

The previous Strategic Reviews in 1997 and in 2004 included information on key performance data for the QAO. We believe it is useful to add to that data set, using the same measures as in the two previous Reviews, wherever possible. The following table provides a high-level overview of trends in workload and performance of the QAO in the past 12 years.

**Selected Workload and Performance Measures**

	1996–97	2002–03	2008–09
% of costs recovered from clients through fees and charges	75	82	85
% of financial audits completed within the legislative timeframe	92	87	99 <sup>1</sup>
% of audits completed in accordance with QAO standards	100	100	98 <sup>2</sup>
% of reports tabled in Parliament within one week of the agreed timeframe	100	100	NA <sup>3</sup>
Number of reports tabled in Parliament	5	10	10 <sup>4</sup>
Number of audits	585	801	747
% of hours charged for against available hours	55	62	62
% of productive hours spent on audits against available hours	76	75	75
% of staff who are CPA/CA qualified	46	53	50 <sup>5</sup>
% of staff with post-graduate qualifications	16	38	22
Total expenditure of the QAO	\$15.775m	\$22.208m	\$39.989m
Total number of staff	164	189	255

1 Note that measure has been changed to % of financial statements audited and certified within statutory timeframe where statutory requirements observed by audit client 2008–09— 99%

2 Note that for 2008–09 the measure has been reworded to Percentage of audit opinions and findings reviewed as appropriate in terms of QAO audit methodology.

3 Note that this measure is no longer utilised.

4 Further categorised as financial and compliance reports — 4, and PMS audit reports — 6.

5 It is noted that 43 staff are currently undertaking CPA/CA/CISA studies.

Source: QAO

This table confirms that the QAO has maintained its high standards in completing audits and reporting to Parliament. Expenditure and staff numbers have increased, although the number

of audits undertaken has actually declined from 801 in 2002–03 to 747 in 2008–09, in part due to the amalgamation of the number of local councils. However, the number of audits is not a reliable measure of workload, as it does not take account of the increasing complexity of the audit function. In our view, a better measure of overall workload is total chargeable or billable hours of audit activity. This measure has already been addressed in Section 11 of this Report, in relation to planning and resourcing.

The measures of productivity or capacity utilisation shown in the above table have been largely static over time, although the percentage of hours charged for against available hours increased from 55% to 62% between 1996–97 and 2002–03. The issue of productivity is addressed in more detail later in this Section.

In regard to qualifications of staff, it is noted that there are 43 staff currently undertaking CPA/CA/CISA studies, in addition to the 50% of staff who already have such qualifications. However, the sharp decline from 2002–03 to 2008–09 in the percentage of staff with post-graduate qualifications is disappointing.

### 13.2 Strategic Plan — Objectives and Performance

In its 2009–2013 Strategic Plan, the QAO outlines its four key objectives, along with performance indicators designed to measure the extent to which those objectives have been achieved.

As was the case with earlier Reviews, we have been impressed by the commitment of the QAO to review and analyse its performance and the linking of key performance indicators to its Strategic Plan.

We are satisfied that the QAO is providing a reasonable level of performance reporting to key stakeholders, and that there is a suitable balance between quantitative and qualitative information.

The accompanying table shows the objectives and performance indicators outlined in the QAO's Strategic Plan. As well, we have incorporated the related key performance indicators as reported in the 2008–09 Annual Report. The table shows that, while some targets have been met, there are other measures which have fallen short of target. For example, staff satisfaction (including satisfaction with business systems and procedures) are lower than target. Some of these issues have been previously addressed in Section 11 of this Report. Also, participation in the Leadership Program, particularly at the lower levels, is still in the process of gearing up.

Some of the performance indicators also warrant further refinement so that they are more relevant and meaningful. For example, we note that the performance indicator for the objective of meeting the needs of Parliament is that the PAPWC utilise reports from the Auditor-General. It is not entirely clear how this target has been satisfied. It would also be helpful to have further information about the way in which the reports are utilised by the PAPWC, as well as some indication from the PAPWC as to its views on the quality and usefulness of the Auditor-General's reports.

We also consider that there are better performance indicators to measure the QAO objective of being "efficient, effective and sustainable...". Specifically, we suggest that the QAO should place greater emphasis on a broad based measure of productivity. Ideally, overall productivity of the QAO should be measured as output (chargeable hours) per unit of input (eg staff FTEs).

Taking QAO's in-house activity only, productivity as measured by chargeable hours per FTE has shown some considerable variability over the last few years. In 2007–08, productivity increased significantly, due to the combined effect of increased workload and lower FTEs.

On the other hand, in 2008–09, productivity dropped back, as there was a relatively small increase in workload associated with a large rebuilding of FTEs.

### QAO Objectives and Performance Indicators

Objective	Performance Indicator outlined in Strategic Plan	KPI reported in Annual Report
Meet the needs of Parliament by providing independent assurance on the stewardship of public moneys and assets and report to Parliament on audit recommendations, emerging issues and other matters of significance	PAPWC utilise reports from the Auditor-General	Target 2009 — Satisfied Actual 2009 — Satisfied <i>Note number of reports provided to Parliament is 10 with 4 financial and compliance audit reports and 6 PMS audit reports.</i>
Add value to public sector entities by delivering high quality audit services and develop strong professional relationships to benefit public sector entities.	Audit clients value the services of the Queensland Audit Office.	Stakeholder satisfaction with QAO services – Target 2009 — 75% Actual 2009 — 73% ( <i>this is based on Average of ORIMA Research performance index of (1) Audit Process, (2) Audit Reporting and (3) Audit Value.</i> )
Be efficient, effective and sustainable by building quality systems and procedures and measure and report on our business and audit performance.	Key business metrics demonstrate efficient use of resources to deliver service requirements.	Executive and management satisfaction with reporting and performance information – Target 2009 — 75%; Actual 2009 — 74% Staff satisfaction with business systems and procedures – Target 2009 — 75%; Actual 2009 — 71%
Have staff who are motivated and capable by developing staff to ensure a contemporary, innovative professional service organisation and empowering staff to develop and deliver quality services.	Having motivated and skills staff to meet our service expectations.	Staff satisfaction with their work environment – Target 2009 — 75% Actual 2009 — 68%. Percentage of eligible staff who participated in and completed leadership program – Target for AO8 and above — 95% Actual 2009 — 94% Target for AO5 to AO7 2009 — 95% Actual 2009 — 31% <sup>(1)</sup>

(1) The 2009 program was subject to review which delayed its implementation

Source: QAO

In our view, another highly relevant measure is the ratio of total chargeable hours to total available hours, which is effectively a measure of capacity utilisation. Using QAO's own internal planning figures (which exclude expected leave and an allowance for administration time from the calculation of available hours), capacity utilisation has been fairly static at around 62% in the last few years.

ACAG also calculates a capacity utilisation factor, defined as the percentage of total (whole-of-office) paid hours charged to audit activities. There are some definitional differences from the QAO's internal planning measure, the most notable of which is that ACAG does not make any adjustment to available hours for leave or administration time. As at 30 June 2008, the QAO achieved a result in line with the ACAG average of 51% for this measure of capacity utilisation.

We note also that, in its 2008–09 Annual Report, the NSW Audit Office reported an increase in staff productivity in 2008–09 to 63% (being the percentage of total hours charged to audit work.) From our experience, we would expect a private sector audit firm to achieve a figure in the range of at least 65–70%.

Accordingly, we believe that there is room for further improvement in productivity within the QAO, and for greater attention to be focussed on these higher-order measures of performance.

#### Conclusion

##### *CN.13(i)*

The QAO should focus attention on lifting its performance on macro measures of productivity and capacity utilisation, and pay less attention to the larger number of second-order performance measures now being recorded and reported.

#### Recommendation

##### *RN.13(i)*

**That the QAO focus greater attention on lifting its performance on macro measures of productivity and capacity utilisation.**

### 13.3 ACAG Benchmarking Information

The QAO is a member of ACAG, which is comprised of all the Audit Offices in Australasian jurisdictions, including the ANAO as well as all States and Territories, and New Zealand. ACAG is a valuable forum for Audit Offices to discuss a range of matters of common interest (such as audit standards and audit methodology), for cross-fertilisation of ideas and experiences, and for identifying and addressing emerging issues of relevance to the audit function.

From our observations, the Auditor-General and other QAO staff are active participants and contributors to the work of ACAG, and we commend the Auditor-General for his involvement with ACAG. There are considerable benefits for the QAO in being able to share its experiences, and compare its performance, with similar public sector Audit Offices.

Over the last five years, ACAG has developed a comprehensive range of information on the operations of its members to enable extensive benchmarking to be undertaken. Detailed information is available for each member of ACAG on attest and performance audit activity measures, resourcing and operations, office expenses, human resource issues and client surveys. We appreciate the actions of the QAO in making this wealth of information available to us for our Review. We have already made reference to some of this benchmarking information in earlier parts of this Report.

The QAO also publishes in its Annual Reports a summary benchmarking of its performance for key measures compared with ACAG average results. The latest comparative information as at 30 June 2008 is presented in the 2008–09 Annual Report (page 19). This information covers audit activity measures, timeframes for issuing financial opinions, the value of contracted audit work and office staffing measures.

Across the range of measures, the performance of the QAO shows mixed results, with some measures better than average, whilst others are below-average. For example, the QAO's cost per audit hour charged to audit was \$116, compared with an ACAG average of \$132, and the

cost per unit output for Local Government Financial Opinions was \$38,077 compared with an ACAG average of \$49,009. On the other hand, the QAO's cost per unit output for State Government Financial Opinions was \$69,408, higher than the ACAG average of \$66,090.

We have already made reference to ACAG's measure of capacity utilisation earlier in this Section.

Conclusion

*CN.13(ii)*

As an aspirational target, in relation to ACAG benchmarks, the QAO should aim to lift its performance to be ranked in the top 2–3 Audit Offices in Australia, and consistently above average, for most key performance indicators.

Recommendations

*RN.13(ii)*

**That the QAO aim to lift its performance to be ranked in the top 2–3 Audit Offices in Australia, and consistently above average, for most key ACAG performance indicators.**

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## 14. OUTCOMES OF 2004 STRATEGIC REVIEW

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The Terms of Reference for our Review state, inter alia:

*“Consideration is also to be given to the recommendations agreed by the Government arising from both the 2004 strategic review, and the related Public Accounts and Public Works Committee report on the review and the Government’s response to the Committee’s report, particularly the extent to which they have been implemented and whether they are achieving the desired objectives.”*

The 2004 Review contained 119 conclusions and made 38 recommendations, as well as a number of other suggestions and observations, all directed towards providing a comprehensive framework for the QAO to build for the future. The recommendations of the 2004 Review were considered by the then Public Accounts Committee, which issued its Report in June 2005 (Report No. 69). Subsequently, the Government’s response to the 2004 Review and the Public Accounts Committee Report was tabled in Parliament on 15 September 2005.

Both the PAC and the Government strongly endorsed and supported the recommendations of the 2004 Review, with only some minor variations, and acknowledged the actions being undertaken by the QAO to address the recommendations. One notable variation was the elimination of suggested targets for PMS audits, on the basis that this could compromise the independence of the Auditor-General.

We have undertaken a comprehensive assessment of actions arising from the 2004 Review, including the then PAC position, the Government’s response, and implementation by the QAO. In this regard, the QAO provided us with a detailed briefing on the current status of all issues. A summary of our assessment, which addresses each of the 2004 Review recommendations individually, is included as Attachment F of this Report.

Overall, the QAO has made a commendable effort in implementing the recommendations of the 2004 Review, and in achieving progress towards the desired objective of providing a comprehensive framework for the QAO to build for the future. Notable achievements include the implementation of IPSAM, which has been an outstanding success, and also a range of workplace and human resource initiatives. Planning and resourcing functions have been improved, but further improvements are necessary. The 2004 Review challenged the QAO to more fully utilise its existing mandate on PMS audits, and we are satisfied that this has been achieved.

There are a small number of residual and/or ongoing areas of concern, which require further attention. These are outlined below, and are also addressed in other Sections of this Report:

- Practice Management System – the QAO has replaced ATOMS with eTrack, but there have been problems with its implementation, which are still in the process of being resolved. The outcomes to date have been less than satisfactory, and this is the one area where the QAO has fallen well short of the expectations of the 2004 Review. This issue is addressed in Section 10 of this Report.
- Client Services Plans – the QAO has made improvements to the development of its Client Services Plans, but there remain some inconsistencies in content and approach between audit teams. These issues are addressed in Section 12 of this Report.
- Engagement with audit clients on the fee setting process – this is inter-related with the previous point, and similar comments apply. This issue is addressed in Section 7 of this Report.

- Remuneration and reward structures – progress on this issue has been more limited than might be considered desirable, although the difficulties of achieving enhanced remuneration and rewards within the parameters of the *Public Service Act* are acknowledged. This issue is addressed in Section 11 of this Report.

There are a range of other conclusions and suggestions or proposals in the 2004 Review that did not give rise to formal recommendations. These are addressed in relevant sections of this Report, where material and relevant.

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## 15. APPROACHES TO PUBLIC SECTOR AUDITING

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### 15.1 Comparative Models for Public Sector Auditing

The Terms of Reference for our Review include consideration of comparative models, practices and procedures used by offices in other jurisdictions equivalent to the QAO.

This Section assesses different models and practices adopted in other Australian jurisdictions. It is not an exhaustive review, but rather concentrates on the approaches adopted at the Commonwealth level by the ANAO, in New South Wales with the NSWAGO and in Victoria with the VAGO. We visited each of those offices as part of that review and met with senior offices of the ANAO and the Auditors-General in New South Wales and Victoria. We have also considered the approach adopted in New Zealand, which has a different model for the delivery of audit services.

The main differences which we identified from our comparative analysis related to the following areas:

- The audit mandate for performance auditing
- Planning for performance audits
- The coverage for public sector entities generally
- The separation of audit service delivery in New Zealand

### 15.2 Performance Auditing

The primary difference noted with regard to the audit mandate relates to the scope and responsibilities for performance auditing and different models adopted within the jurisdictions.

We have included at the end of this Section a table which outlines the different approaches adopted for performance audits. This table is intended to be illustrative rather than exhaustive, and is based solely on publicly available information.

As outlined in Section 5 of this Report, the model adopted in Queensland is a mandate for the Auditor-General to undertake PMS audits. Other jurisdictions reviewed provide a broader performance auditing mandate to Auditors-General. Whilst not included in the table, we note that the Northern Territory has adopted a model for PMS audits similar to that applying in Queensland.

We have considered the question of the mandate of the Auditor-General for performance auditing in more detail in Section 16 of this Report.

### 15.3 Planning for Performance Audits

From our comparative analysis, we note there are more formalised processes for Audit Offices to consult with the relevant Parliamentary Committees on the planning of audits, including performance audits, in the cases of the ANAO, and also in New South Wales and Victoria, compared with Queensland. For the VAGO, there is a legislative requirement to publish a plan for audit coverage, including for performance audits. The ANAO does not have such a legislative requirement, but chooses to publish its annual plan for performance audits. In these jurisdictions, the relevant Parliamentary Committee has a greater role in the budget process for the respective Audit Offices, and consultation on the audit program is normally undertaken in that context.

In Queensland, there is regular consultation between the Auditor-General and the PAPWC on audit matters, including some discussion on the program of proposed PMS audits. However,

in our view, the process is more informal and less structured than is desirable, and a formal plan for PMS audits is not published. We believe there would be benefit in an enhanced process that is more transparent and accountable than is currently the case, and that provides for greater input from stakeholders earlier in the planning process. This will be of increasing importance, as the number of such audits is expected to grow over time.

Specifically, we consider there would be benefits in the development of a rolling three-year Strategic Audit Plan by the QAO to provide better guidance to the Parliament, other stakeholders and the public on potential topic or subjects for future PMS audits. The plan should encompass indicative audit topics for future PMS audits over a three-year period, with a more specific and definite scoping of topics for the first year. It is recognised that there needs to be a degree of flexibility built into such a plan, to accommodate changing circumstances and priorities, which may cause the Auditor-General to vary the plan.

In developing a Strategic Audit Plan, we consider that the QAO should first consult with the PAPWC, as well as potential audit clients and other affected parties, and consider their feedback, before finalising the Plan. It is important that responsibility for the content of the Plan, and for implementation of the Plan (including variations to the Plan), rests with the Auditor-General. In the public interest, the Strategic Audit Plan should be published on the QAO's website.

In terms of possible legislation, we note that the Victorian Audit Act 1994 provides a formal process for drafting of an annual plan; for submitting the plan as a draft to the relevant Parliamentary Committee for feedback; for finalisation of the plan after the annual budget is approved; and then for the publication of the plan and tabling in Parliament.

We do not see the need for such a formal process in Queensland, although it is desirable that there is a statutory requirement for the Auditor-General to publish a three-year Strategic Audit Plan for PMS audits.

#### **Recommendations**

##### ***RN.15(i)***

**That the *Auditor-General Act 2009* be amended to include a requirement for the QAO to prepare a three-year Strategic Audit Plan for PMS audits, and to update the plan each year. The plan should incorporate indicative audit topics over the three years, with more specific and definite scoping of topics for the first year.**

##### ***RN.15(ii)***

**That the Auditor-General and the Chair of the PAPWC agree on a protocol for consultation with the PAPWC on the draft Strategic Audit Plan for PMS audits prior to the commencement of each financial year.**

##### ***RN.15(iii)***

**That the Auditor-General consult with potential audit clients and other affected parties, and consider their feedback, prior to finalisation of the Strategic Audit Plan for PMS audits.**

##### ***RN.15(iv)***

**That, following the passage of appropriation, the Auditor-General finalise the Strategic Audit Plan for PMS audits, and publish it on the QAO website.**

## **15.4 The Coverage of Financial and Compliance Audits**

The most significant difference in terms of the models adopted for coverage of audit by the Auditor-General relates to the audit of local government. In New South Wales, South

Australia and Western Australia, the audit of local governments is not undertaken by the Auditor-General. In those States, the local government itself appoints an auditor from the private sector.

In the case of Queensland, Victoria and Tasmania, the Auditor-General audits local governments. In Queensland, a large majority of the audits of local government is undertaken by private sector contract auditors appointed by the Auditor-General. A similar approach is adopted in Victoria.

Whilst local government is viewed as the third level of government with democratically elected representatives, local governments are nonetheless established under State Legislation and the States have ultimate responsibility for their financial viability, for example in the event of default of their obligations. In these circumstances, it is appropriate that local governments should be subject to audit by the State Parliament's auditor, being the Auditor-General.

Although the overwhelming majority of local governments in Queensland are audited under contract audit arrangements, having the involvement of the Auditor-General in the process ensures that these audits are subject to oversight in a quality review sense. This provides an objective review process and hence additional assurance as to the quality of audit for local government entities.

Where the Auditor-General is responsible for the audits of local government, this enables all audit issues to be drawn together and a comprehensive report provided to Parliament in an effective manner.

#### Conclusion

*CN.15(i)*

Local governments should continue to be audited by the Auditor-General.

### 15.5 The Separation of Audit Service Delivery in New Zealand

We noted the model for audit service delivery in New Zealand, whereby there is a separation for responsibility between the Office for the Auditor-General headed by the Controller and Auditor-General, and that for the audit service delivery arm, which is Audit New Zealand. This provides for a separation of "purchaser" and "provider" roles for government audit functions.

A similar model was adopted in Victoria in the 1990s, but Victoria has now reverted to the more traditional audit model adopted in all States and Territories in Australia, in that the Victorian Auditor-General now heads the VAGO, which undertakes both the audit planning and also delivery for audit services, whilst also contracting out audit assignments to private sector providers.

In New Zealand, the separation for responsibilities is as follows:

#### (a) Office for the Auditor-General

The Office for the Auditor-General is responsible for:

- planning the overall work programme for the organisation as a whole
- carrying out performance audits, special studies, and inquiries
- planning other audit work
- Parliamentary reporting and advice

- setting auditing standards (the Auditor-General's auditing standards)<sup>1</sup>
- allocating annual audits to appointed auditors
- monitoring audit fees to ensure that they are fair and reasonable
- overseeing auditors' performance
- carrying out quality assurance reviews of all work done on behalf of the Auditor-General, including annual audits by appointed auditors

**(b) Audit New Zealand**

Audit New Zealand is responsible for:

- carrying out annual audits on the Auditor-General's behalf; and
- providing other auditing and assurance services to public entities.

As a part of this model, auditors from private sector accounting firms are appointed to carry out some annual audits on the Auditor-General's behalf.

The advantages of the model are as follows:

- It allows for a separation of the planning function of the Office of the Auditor-General from the service delivery arm (ie there is a separation between the “purchaser” and “provider” roles).
- It allows for a competitive element to be adopted if required through contestability between service delivery providers
- There are potential cost savings for audit clients from more competitive pricing in the delivery of audit services.

The disadvantages of the model are as follows:

- There are additional administrative costs from the separation of the Office of the Auditor-General and the audit service delivery arm
- There are additional contracting costs in establishing audit contracts
- There is a potential for conflict or tension in the relationship between the Office of the Auditor-General and the service delivery arm.
- The expected cost savings may not be material.

Having regard to experiences elsewhere, we are not persuaded that the purchaser/provider separation of audit functions delivers sufficient benefits to outweigh the costs involved. Given the small size of audit office functions compared with many other larger government service delivery agencies, there are significant scale diseconomies which give rise to relatively high administrative overhead costs.

The purchaser/provider model was adopted for a time in Victoria, but this was not considered to be successful, and has now been abandoned. The model is not utilised in any other jurisdiction in Australia. The private sector is already an important provider of contract audit services to the QAO, and a competitive process is adopted for the allocation of this contract work. Also, our Report makes a number of recommendations to improve the efficiency of the QAO in relation to audit service delivery.

Conclusion

*CN.15(ii)*

The model of separation of audit service delivery from the Office of the Auditor-General is not supported.

Queensland Auditor-General	Australian National Audit Office	New South Wales Auditor-General	Victorian Auditor-General	New Zealand
<b>Legislative mandate</b>				
<p>Section 38 (1) of the <i>Auditor-General Act 2009</i> provides a power whereby the “<i>Auditor-General may at his/her discretion undertake an audit of performance management systems of a public sector entity</i>”.</p>	<p>The <i>Auditor-General Act 1997</i> provides a power such that the “<i>Auditor-General may at any time conduct a performance audit of an Agency</i>”.</p>	<p>The <i>Public Finance and Audit Act 1983</i> provides a power in Section 38B (1) whereby “<i>The Auditor-General may, when the Auditor-General considers it appropriate to do so, conduct a performance audit of all or any particular activities of an authority to determine whether the authority is carrying out its activities effectively and doing so economically and efficiently and in compliance with all applicable laws.</i>”</p> <p>Section 38B (3) states that “<i>A single performance audit may relate to the activities of more than one authority.</i>”</p>	<p>The <i>Public Audit Act 1994</i> provided a power in Section 15 whereby “<i>The Auditor-General may conduct any audit he or she considers necessary to determine (a) whether an authority is achieving its objectives effectively and doing so economically and efficiently and in compliance with all relevant Acts; or (b) whether the operations or activities of the whole or any part of the Victorian public sector (whether or not those operations or activities are performed by an authority or authorities) are being performed effectively, economically and efficiently and in compliance with all relevant Acts.</i>”</p>	<p>The <i>New Zealand Public Audit Act 2001</i> indicates in Section 16 that “<i>The Auditor-General may at any time examine the extent to which a public entity is carrying out its activities effectively and efficiently.</i>”</p>
<b>Number of Audits of a performance nature each year</b>				
6	45	6 (target for 2009–10 is 12)	25	Approx 15

Queensland Auditor-General	Australian National Audit Office	New South Wales Auditor-General	Victorian Auditor-General	New Zealand
<b>Objective of a Performance Audit</b>				
<p>Object of the audit includes deciding whether the performance management systems enable the public sector entity to assess whether its objectives are being achieved economically, efficiently and</p> <p>The audit may include a review of the public sector entity's performance measures and in a report the Auditor-General may state whether in the Auditor-General's opinion the performance measures are relevant and otherwise appropriate having regard to their purpose and fairly represent the public sector entity's performance.</p>	<p>An independent, objective and systematic assessment of public sector entities' programs, resources, information systems, performance measures, monitoring systems and legal and policy compliance</p>	<p>Performance audits determine whether an agency has been carrying out its activities in an efficiently, economically and in compliance with the law These audits may review all or part of the agency's operations. Some audits consider particular issues across a number of agencies.</p>	<p>A performance audit is an audit which evaluates whether an organisation or a government program is achieving its objectives effectively, and doing so economically and efficiently and in compliance with all relevant legislation.</p> <p>The Auditor-General also has the power to carry out audits to establish whether of grants to non-government organisations or persons have been applied for the purpose for which the grant had been made and whether the funds have been applied economically, efficiently and effectively.</p>	<p>A performance audit can examine how effectively and efficiently a public sector entity is working, whether a public sector entity is complying with its statutory obligations, any act or omission that might waste public resources any act or omission that might show (or appear to show) a lack of probity or financial prudence by a public sector entity or one or more of its members, office holders, and employees.</p> <p>Aim is to provide Parliament and the public with assurance that public entities are delivering what they have been asked to and have operated lawfully and honestly. The office aims to report both good and bad performance.</p> <p>Benefits for public sector entities include independent assurance of their operations and guidance to improve their efficiency and effectiveness.</p>
<b>Strategic Planning of performance audits</b>				
<p>Audit topics are selected based on an assessment of risks and significance, for instance, the</p>	<p>A process of Australian Public Sector analysis – entity analysis – identification of topics and</p>	<p>The goal is to choose topics which are of interest to parliamentarians and the</p>	<p>The Auditor-General considers many potential performance audit topics annually. With a</p>	<p>Web site does not incorporate information on the process for selecting topics for</p>

Queensland Auditor-General	Australian National Audit Office	New South Wales Auditor-General	Victorian Auditor-General	New Zealand
<p>economic, social and environmental impact on the community, the degree of public interest along with the capacity of the Queensland Audit Office. To accommodate emerging priorities the audit selection needs to continue to be a dynamic process that ensures the audit topics are relevant</p>	<p>development of audit work program.</p> <p>Potential audit topics are rated against criteria such as potential benefits, financial materiality, risks to reputation and service delivery and extent of previous audit coverage,</p>	<p>community. When selecting areas for audit the office combines internal research with input from parliamentarians, agency CEOs and members of the public. The office then evaluates the benefits of each topic, including the opportunity for cost savings, the likely impact and the overall benefits for public administration.</p>	<p>focus on quality and the effective use of resources, a selection of these topics is included in the Annual Plan, outlining the proposed work program of the Office for the coming year. Potential areas of audit interest include programs or initiatives that are identified as having significant inherent risk, underperformance issues or strong public interest. To prevent overlap the Office considers whether a topic is receiving suitable scrutiny through another review process.</p>	<p>performance audits.</p>
<p><b>Publication of Annual Plan or similar for audits including performance audits</b></p>				
<p>There is informal consultation with the PAPWC. There is no formal plan published.</p>	<p>Publication of the “Blue Book” which follows consultation with the Joint Committee of Public Accounts and incorporates details of potential performance audits and details of all audits including financial and compliance audits.</p>	<p>There is consultation with the Parliamentary Public Accounts Committee.</p> <p>Formal plan not published.</p>	<p>The Office uses a series of steps and principles in developing the Annual Plan including consultation with the Parliamentary Accounts and Estimates Committee of the Parliament.</p>	<p>No plan published.</p>
<p><b>Approach to performance audits</b></p>				

Queensland Auditor-General	Australian National Audit Office	New South Wales Auditor-General	Victorian Auditor-General	New Zealand
<p>Audits of a program or activity of a single entity or of a program or the administration of a program by a number of entities.</p> <p>Follow up audits.</p> <p>Section 38 (4) of the Auditor-General Act 2009 indicates that <i>“in conducting the audit, the auditor-general must have regard to any prescribed requirements relating to the establishment and maintenance of performance management systems that apply to the public sector entity”</i>.</p>	<p>Audit of a program or activity in a single entity.</p> <p>Protective security audits.</p> <p>Cross-entity audits (review of the same activity in a number of entities or the administration of a program by a number of entities)</p> <p>Follow up audits.</p>	<p>The New South Wales Auditor-General sees performance audits as special in-depth assessments of whether government agencies are achieving value for money.</p> <p>The audits can be of the whole of an agency, one particular agency activity or an activity across a number of agencies.</p>	<p>The performance audit reports provide an independent assessment of an area of public sector activity and seeks to improve resource management and add value to an agency through recommendations on improving operations and procedures. While recommendations from an audit can address improvements in operations the Auditor-General cannot and does not question the merits of government policy.</p>	<p>The <i>Public Audit Act 2001</i> in Section 16 (4) indicates that where there is an applicable government or local authority policy to which the public entity is required to adhere, the examination is to be limited to the extent to which activities are being carried out effectively and efficiently in a manner which is consistent with that policy.</p>
Exclusions from performance audits				
None.	Government Business Enterprises are generally not subject to performance audits although the responsible Minister, the Finance Minister or the Joint Committee of Public Accounts can request the Auditor-General to conduct a performance audit of a Government Business	None	None	Reserve Bank of New Zealand is excluded as well as any registered bank.

Queensland Auditor-General	Australian National Audit Office	New South Wales Auditor-General	Victorian Auditor-General	New Zealand
	Enterprise.			
<b>Undertaking performance audits</b>				
Methodology developed known as ASPIRE, which is a Lotus Notes based system			All performance audits conducted using the Office's own performance audit methodology (AMP).	Usually undertaken by 2 staff. Take 12 months to complete depending upon its scope and complexity.
<b>Reporting</b>				
The report is to be tabled in Parliament as soon as possible after it is completed. The audit client is provided with the opportunity to provide comments on the final draft of the report within 21 days of being provided with the draft report. The Auditor-General is required to incorporate in the report the comments from the audit client in response to the performance audit report.	As soon as practicable after completing the report on an audit of performance a copy shall be tabled in each House of the Parliament and a copy provided to the Finance Minister. Prior to doing so a copy of the report shall be provided to the recipient of the report to enable comments to be provided within 28 days – those comments must be considered by the Auditor-General before preparing the final report.		Proposed report is provided to agency for comment.  Report to Parliament on results of audit includes agency comments.	Tabled in Parliament and it becomes public. Briefings provided to relevant Ministers, select committees of Parliament and other interested parties. Once a performance audit report is drafted it is provided for two weeks to public entities subject to the report to comment on the accuracy, balance and presentation. To maintain independence the Auditor-General is not required to reach agreement on the report's content.
<b>Better Practice Guides</b>				
The QAO does issue better practice guides <sup>(1)</sup> . Three such	Performance audits also identify better practices which	Issues Guides to Better Practice with one issued in 2009	Issues Good Practice Guides.	Develops and issues what are referred to as Good Practice

Queensland Auditor-General	Australian National Audit Office	New South Wales Auditor-General	Victorian Auditor-General	New Zealand
<p>guides have been issued in the last three years, being</p> <ol style="list-style-type: none"> <li>1. <i>Checklist for Organisational Change</i> (March 2009).</li> <li>2. <i>QAO Guideline – Accounting for QTC Onlending Products and Debt Restructure</i> (March 2007) and</li> <li>3. <i>Better Practice Guide – Risk Management</i> (October 2007)</li> </ol>	<p>may then be incorporated into Better Practice Guides.</p> <p>Noted that five Better Practice Guides issued in calendar year 2009.</p>	<p>(Monitoring and Reporting on Audit Recommendations) and one in 2008 on Implementing Successful Amalgamations.</p>		<p>Guides. Four guides were issued in each for 2007 and 2008</p>
<b>Improving performance auditing</b>				
<p>QAO indicates in 2008–09 annual report that <i>“as part of the review of our audit methodology we have developed improved communication processes that will focus on building stronger relationships with our clients during an audit and obtaining more input from agency staff early on in the audit process”</i>.</p>				

(1) Better practice principles or better practice case studies are also included in most PMS audit reports to Parliament to provide guidance for all relevant public sector entities, not just those included in the audit. This is particularly relevant where the audit topic covered a number of entities with different audit results.

This table is intended to be illustrative rather than exhaustive, and is based solely on publicly available information.

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## 16. AUDIT MANDATE

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### 16.1 Legislative Mandate

As part of our Review, we have examined the legislative mandate established for Audit Offices in other jurisdictions equivalent to the QAO.

The Terms of Reference for our Review also required us to take into account the results of the PAPWC's review of the Auditor-General's PMS Audit mandate. As noted in Section 5, the PAPWC has not yet completed its inquiry. However, we have consulted with the PAPWC during the process of our Review and noted aspects of submissions to its inquiry, including by the QAO. We have also considered the Hansard record of the public hearing held by the PAPWC on 18 September 2009.

From our comparative analysis of audit models in other jurisdictions, as outlined in Section 15, there are a number of key differences in approach as to the nature and extent of the audit mandate in other jurisdictions. The major differences which warrant further consideration are as follows:

- The extent of the mandate to undertake performance audits
- The question of the requirement of an Auditor-General to audit in accordance with auditing standards and other prescribed requirements.
- The question of auditing of government funds which are provided to non-government organisation – the so called “follow the dollar” approach to public sector auditing.
- The term of appointment of the Auditor-General.

### 16.2 The Mandate for Performance Audits

The *Auditor-General Act 2009* provides a mandate for the Auditor-General to undertake the audit of performance management systems. Since 2007, the Auditor-General has been provided with an additional power to review an entity's performance measures and to express an opinion as to whether the performance measures are relevant and otherwise appropriate having regard to their purpose and fairly represent the public sector entity's performance.

The primary difference in the legislative mandate between Queensland and other jurisdictions relates to the power to undertake performance audit generally. Other jurisdictions have the power to audit performance management and to report generally on performance. In Queensland, the limitation is to audit and report on the performance management systems, as well as making statements on the performance measures.

There has been extensive consideration of this issue in Queensland over the last 20 years. In 1991, EARC undertook an extensive review of the mandate of the Auditor-General and made a number of recommendations related to the role of the Auditor-General and the mandate for auditing and reporting to Parliament in its *Report on Review of Public Sector Auditing in Queensland* (September 1991).

In its report, EARC recommended that the Auditor-General should have the authority to undertake performance audits to determine whether the public sector entity is carrying out its activities effectively, economically and efficiently and in compliance with all applicable laws. There was also a recommendation that where the Auditor-General undertakes a performance audit, the Auditor-General should, as part of the audit, examine the integrity of relevant performance review and evaluation systems established for the program or activity under review and report on this examination as part of the performance review.

In 1993, the Queensland Parliament chose to provide the Auditor-General with the power to undertake PMS audits through an amendment to the then *Financial Administration and Audit Act 1977*. The power to undertake PMS audits has been retained in the *Auditor-General Act 2009*, together with the additional powers provided with effect from 2007 related to the review of performance measures. We have reviewed the QAO's performance in relation to its existing PMS Audit mandate in Section 5.

We note also that the first strategic review of the QAO by Mr Tom Sheridan in 1997 recommended an extension of the mandate to cover full performance audits. The 2004 Strategic Review adopted a somewhat different approach, arguing that the QAO had not fully utilised its existing mandate and recommending that the QAO expand its program of PMS audits, before further consideration was given to a possible extension of the mandate..

In our view, the QAO has responded positively to the challenge issued in the 2004 Review, and has expanded both the number and range of its PMS audits. In these circumstances, it is timely to revisit the issue of the scope of the mandate.

We believe there is a strong case for a broadening of the Auditor-General's mandate to include auditing on performance generally, on the following grounds:

- Parliament as the Auditor-General's client should have its auditor provide independent reports on performance of public sector entities and on government programs/activities. This would enable an objective assessment as to whether public resources are being used with appropriate economy and efficiency, and are delivering government programs and activities effectively and in compliance with appropriate laws and regulations.
- It is the performance of public sector entities in delivering government services and programs which should be of primary importance, rather than just their performance management systems per se. A focus on systems rather than performance can produce some perverse and misleading outcomes. For example, while an entity's systems may be good, it does not follow necessarily that the performance will be good. Conversely, there may be instances where an entity's systems are poor, but nevertheless overall performance may well be sound. In a recent PMS Audit Report, there were concerns raised about the performance management systems of an entity. However, the findings may well have been different if there had been a capacity for the Auditor-General to comment on performance.
- There is a fundamental principle in terms of integrity and accountability as to whether the performance of public sector entities, as outlined in reports to Parliament (including in Annual Reports), has been subject to external independent scrutiny.
- Performance audits provide a constructive opportunity for the QAO to work closely and co-operatively with entities to improve their performance. In this way, performance audits can be a powerful catalyst for desirable change, and provide a different and fresh perspective on issues which may not be apparent to those inside an entity.
- Performance auditing is well established, and has been proven to work effectively in all other jurisdictions in Australia, apart from the Northern Territory. It is generally accepted as best practice, and is widely applied in other advanced nations, including the United Kingdom, United States, Canada, Denmark, Norway, Sweden, Portugal, Austria and New Zealand.

There have been some arguments raised against a broadening of the mandate, as follows:

- The existing mandate allows for the Auditor-General to audit and report on performance management systems and to also report both on the relevance of the performance measures as well as the fairness with which that information is represented. This is not far short of a full performance mandate in any case.
- The extension of the power of the Auditor-General in 2007 to cover performance measures has not been in place for long enough to assess its benefits. In a limited review of PMS audits (see Section 5 of this Report), we noted that the Auditor-General had utilised the power to review the performance measures of public sector entities generally in a number of audits reported to Parliament. For example, in one report, the Auditor-General highlighted a significant improvement opportunity for fair presentation of performance information, and for the relevance and appropriateness of performance indicators to fairly represent GOC performance. This was Report No 7 for 2009 on *Follow-up on Government Owned Corporation and Budget Sector Performance Measurement and Reporting*. However, this report did not comment directly on performance measures of any individual entity, and we have addressed this issue in recommendation RN.5 (i).
- There is a concern from some audit clients as to whether the QAO has the appropriate level of skills and expertise to undertake performance audits (over and above the skills and expertise required for PMS audits). We have noted that the QAO has been building its skills base as staff numbers have expanded and the number of PMS audits undertaken has increased. In particular, the QAO now has staff with a broader range of professional qualifications and expertise than has previously been the case.

In our discussions with stakeholders, there was a diversity of views expressed on the scope of the mandate for performance auditing. Overall, there was strong and broad-based support for an extension of the mandate, on the basis that it would strengthen public administration and accountability in Queensland. This is consistent with the thrust of comments made in the public hearings on the PAPWC Inquiry into this matter, including from Accountable Officers who highlighted the benefits of working with the QAO to use performance audits as a tool to assist in improving the performance of their agencies.

We have carefully weighed up the various arguments outlined above and have concluded that it is now time for the QAO's audit mandate to be expanded to full performance audits, consistent with the approach adopted in most other jurisdictions in Australia, as well as other advanced nations. There is little merit in continuing to limit the mandate. By their very nature, PMS audits can only provide a partial and incomplete perspective on performance, which is of limited usefulness. We have now reached a point in the evolution of public administration in Queensland that warrants full performance auditing by the QAO.

There remains a concern from a broad cross-section of stakeholders about the level of skills and expertise within the QAO to undertake performance audits, and we encourage the Auditor-General to continue to build the internal skills base of the QAO. In addition, consideration should be given to a greater use of external expertise either as part of the audit team or as an advisor for the audit. It is desirable that there is involvement from subject experts from initial scoping and planning of the audit through to review of the final report to Parliament. In selecting external expertise, the Auditor-General needs to consider the background and experience of the expert and to avoid any conflicts of interest, or other biases or prejudices which may impact the audit.

Furthermore, we note that the Government publishes material on performance management standards and guidelines that are relevant for performance audits.

Conclusions

*CN.16(i)*

It is now time for the scope of the Auditor-General's mandate to be expanded to full performance audits, consistent with the approach adopted by most other jurisdictions in Australia, as well as in other advanced nations such as the United Kingdom, United States, Canada and New Zealand.

*CN.16(ii)*

The recommendations outlined in Section 15 in relation to PMS audits remain equally relevant and applicable to the expanded mandate.

Recommendations

*RN.16(i)*

**That the *Auditor-General Act 2009* be amended to broaden the audit mandate to enable the Auditor-General to undertake performance audits, such amendment to be generally consistent with legislation applying in other Australian jurisdictions.**

*RN.16(ii)*

**That the *Auditor-General Act 2009* be amended to include a requirement for the QAO to prepare a three-year Strategic Audit Plan for Performance Audits, and to update the Plan each year.**

*RN.16(iii)*

**That the Auditor-General and the Chair of the PAPWC agree on a protocol for consultation with the PAPWC on the draft Strategic Audit Plan prior to the commencement of each financial year.**

*RN.16(iv)*

**That the Auditor-General consult with potential audit clients and other affected parties, and consider their feedback, prior to finalisation of the Strategic Audit Plan.**

*RN.16(v)*

**That, following the passage of appropriation, the Auditor-General finalise the Strategic Audit Plan, and publish it on the QAO website.**

*RN.16(vi)*

**That the *Auditor-General Act 2009* be amended to require the Auditor-General, in undertaking performance audits, to take into consideration performance management standards and guidance issued by the government.**

### 16.3 Auditing against auditing standards and other prescribed requirements

In all jurisdictions which we reviewed, there is a requirement for auditors to utilise auditing standards which now have the “force of law” in Australia. In Queensland, these standards are adopted through a requirement for the Auditor-General to issue Auditing Standards (last issued April 2007) under Section 58 of the *Auditor-General Act 2009* and which are required to be reported to the Legislative Assembly. The current *Auditor-General of Queensland Auditing Standards* were issued in April 2007 under a similar provision of the then *Financial Administration and Audit Act*.

Moreover, the “force of law” auditing standards in Queensland are supplemented by additional requirements not covered directly by auditing standards. These are additional requirements for public sector auditing, and cover areas such as probity and propriety of matters associated with the management of public sector entities. In addition, the standards require an assessment of compliance with relevant acts, regulations, government policies and other prescribed requirements.

It is important to note that, in terms of Section 8 of the *Auditor-General Act 2009*, the Auditor-General is not subject to direction by any person about:

“(a) the way in which the Auditor-General’s powers in relation to audit are to be exercised

(b) the priority to be given to audit matters.”

The Auditor-General is able to conduct an audit in the way that the Auditor-General considers appropriate, although the Auditor-General may have regard to recognised standards and practices, and the character of the internal control system of the entity to be audited, including internal audit.

Despite these broad powers, it is generally considered inappropriate, as a matter of convention, for an Auditor-General to comment on matters of government policy or objectives. These are matters which are the prerogative of governments. The mandates for performance auditing in some other jurisdictions include a provision preventing the Auditor-General from commenting on government policy.

#### Conclusion

##### *CN.16(iii)*

In accordance with convention, it is inappropriate for the Auditor-General to comment on matters of government policy or objectives in undertaking audits.

We note that Section 16(4) of the *Public Audit Act* in New Zealand indicates that where there is an applicable government or local authority policy to which the public entity is required to adhere, the examination (performance audit) is to be limited to the extent to which activities are being carried out effectively and efficiently in a manner which is consistent with that policy. We consider that this is a useful provision for performance audits, and that a similar provision should be incorporated in the *Auditor-General Act 2009*.

**Recommendation*****RN.16(vii)***

**That, concurrent with expansion of the performance audit mandate, the *Auditor-General Act 2009* be amended to incorporate a provision to ensure that:**

- **where there is a clear government or local government policy or guideline, the performance audit would be assessed against the relevant policies for that entity or group of entities; and**
- **in undertaking performance audits, the Auditor-General is not empowered to question the merit of policy objectives of the Government.**

#### 16.4 The “Follow the Dollar” Approach to Public Sector Auditing

In our discussions with the Victorian Auditor-General and with the ANAO, we were apprised of the notion of “follow the dollar” in relation to the audit of grants or other funds provided to non-government organisations for purposes other than the direct provision of goods or services. This particularly applies where the non-government organisation is effectively acting as an agent for the government in the delivery of services or program to third parties.

It is noted that the Victorian Auditor-General has the power to carry out audits to establish whether grants to non-government organisations or persons have been applied for the purpose for which the grant has been made and whether the funds have been applied economically, efficiently and effectively.

We are advised that the Victorian Auditor-General has undertaken only one audit of this nature, being an audit related to grants to the Cambodian Association of Victoria in 2004. We also have noted that the Tasmanian Auditor-General has a similar power to “follow the dollar”, and used this power to undertake an audit in 2008 of State financial support for a then still-to-be-established Tasmanian Education Foundation.

Whilst the ANAO does not have a power similar to that held by the Victorian Auditor-General, we understand that the issue of “follow the dollar” is likely to be considered as part of an inquiry into the *Commonwealth Audit Act* by the Joint Committee of Public Accounts. We understand that provision for the ANAO to have access to the staff and records of the grant receiving body is included in a number of the contracts and agreements concluded by Commonwealth agencies.

At present, assurance as to the appropriate disposal of government funds in Queensland is limited to ensuring that the government agency providing the funding has in place procedures for:

- determining the nature, scope and need for the funds to be provided
- deciding upon the appropriate bodies to receive the funding
- establishing appropriate contractual arrangements, including reporting of key performance indicators, to enable effective monitoring of the use of the funds.

On the final point, this would include requirements for reporting back on the efficient and effective use of the public resources in delivering the program or activity supported by the government funding.

The more “interventionist” solution is to adopt the Victorian approach. This would enable the Auditor-General to undertake an audit of a non-government organisation to assess issues of economy in the application of resources, and issues of efficient and effective delivery of the

funding for the purpose intended. It would involve an extension of the Auditor-General's powers beyond public sector entities. We do not support such an extension of power on a generalised basis, as this would appear to be excessive and unnecessary.

Rather, we consider that the involvement of the Auditor-General in an audit of this nature should be in the case of exceptional circumstances only. Primary reliance should be placed on the performance and other reporting requirements embodied in the contractual agreement between the State agency and the grant receiving body. To this end, the exercise of a "follow the dollar" power should be limited to circumstances where there is a request from the Premier and the Auditor-General agrees to such a request. Before the Premier could request an audit by the Auditor-General, there would need to be strong prima facie evidence of:

- a breakdown or failure of the normal procedures for accounting for the expenditure of funds advanced by the State; or
- other evidence of a failure to acquit such funds in accordance with agreed procedures, including the achievement of agreed performance targets.

We believe that, whilst this power is not expected to be utilised often, there would be an advantage for the Auditor-General to have the power in the event that exceptional circumstances arose whereby it was appropriate for the Auditor-General to be requested to undertake such an audit. In order to preserve the independence of the Auditor-General, it would be a matter for the Auditor-General to decide whether to agree to such a request.

There would also be merit in ensuring that a provision for the QAO to have access to the staff and records of the grant receiving body is included in contracts and agreements negotiated by Queensland Government agencies, consistent with the approach of the Commonwealth Government.

#### Conclusions

##### *CN.16(iv)*

There is a case to amend the *Auditor-General Act 2009* to give the Auditor-General limited powers in exceptional circumstances to undertake an audit of a non-government body that is the recipient of funding or other financial benefit other than for the direct supply of goods and services.

##### *CN.16(v)*

There should be a provision for the QAO to have access to the staff and records of a grant receiving body included in contracts and agreements negotiated by Queensland Government agencies for delivery of services to third parties.

**Recommendation*****RN.16(viii)***

**That the *Auditor-General Act 2009* be amended to provide a power for the Auditor-General to undertake an audit as to whether a grant or other financial benefit provided to a person or body that is not a Queensland public sector entity has been applied economically, efficiently and effectively for the purpose for which it was given and in compliance with relevant legislation, standards and guidelines, in circumstances where:**

- **there is a request from the Premier; and**
- **the Auditor-General agrees to such a request,**

**provided that, prior to making such a request, the Premier must be satisfied that there is *prima facie* evidence of:**

- **a breakdown or failure of the normal procedures for accounting for the expenditure of funds advanced by the State; or**
- **other evidence of a failure to acquit such funds in accordance with agreed procedures, including the achievement of agreed performance targets.**

### 16.5 Small Size/Low Risk Audits

The QAO has indicated that it is responsible for 134 small size and low risk audits for entities with an audit fee of less than \$5,000. The fees for these entities amount to only \$172,500 of the QAO's total revenue. While they are public sector entities, their financial statements are not consolidated into the whole-of-government accounts on the grounds of a lack of materiality.

The QAO has proposed a change in the arrangements to enable the Auditor-General to dispense with audits of such entities. This would achieve greater efficiency, both for the QAO, and also for the entities themselves.

It would be possible to utilise Section 31 of the *Auditor-General Act 2009* to exempt these entities from audit by the Auditor-General through a regulation. The downside of using an exemption approach is that the Auditor-General would have no continuing oversight to ensure that an appropriate quality audit is undertaken. The Auditor-General also would not have access to audit reports to allow reporting to Parliament on information relating to the status of audits of these entities.

The preferred solution is to amend the *Auditor-General Act 2009* to allow the Auditor-General to dispense with small size/low risk audits, with the affected public sector entities being responsible for engaging their own auditors. In this instance, the contract arrangement for audit and the quality of the audit would be a matter between the management of the public sector entity and the auditors. Each entity would be required to provide a copy of the audit report to the Auditor-General as soon as possible after completion of the audit.

Prior to giving any dispensation, the Auditor-General would need to undertake a risk assessment of the relevant entities, to ensure that there is a low risk involved, from the perspective of public sector auditing. The Auditor-General also would need to review the operations of the entities on an ongoing basis to ensure circumstances did not change such that the audit of the entity was no longer a small size/low risk audit. In the event of changed circumstances, the dispensation would need to be withdrawn by the Auditor-General.

We note that a number of these entities are organisations who may be in a position to have local auditors undertake the audit on a reduced fee basis in return for some recognition of the contribution made by the auditor.

**Recommendation*****RN.16(ix)***

**That the *Auditor-General Act 2009* be amended to allow for the Auditor-General to dispense with the audit of small size/low risk public sector entities, with such entities being required to engage an appropriately qualified auditor and to provide a copy of the audited financial statements (including audit report) to the Auditor-General as soon as practicable after completion.**

## 16.6 Auditing of the Charter of Fiscal Responsibility

The *Financial Accountability Act 2009* requires the Treasurer to prepare and table in the Parliament a Charter of Fiscal Responsibility. The Treasurer is also required to report regularly to Parliament on outcomes the Government has achieved against the objectives stated in the Charter.

The Charter outlines the fiscal principles of the Queensland Government broadly based around three themes or objectives being:

- Fiscal sustainability;
- A competitive tax regime; and
- Managing the State's balance sheet.

In terms of the requirement for the Treasurer to report to Parliament, there is an argument (in terms of enhanced accountability) for independent scrutiny of the performance of the Government in achieving these principles (recognising the fact that the principles themselves are a matter solely for the determination of the Government). As a servant of the Parliament, the Auditor-General is best placed to provide such independent scrutiny, through an audit of the performance information to be presented in the report to Parliament.

We note that, in New South Wales, agreement has been reached between the Government and the Auditor-General under "agreed upon" audit procedures for the Auditor-General to audit the information being reported against the New South Wales State Plan.

In our view, it is a matter for the Treasurer to consider as to whether "by arrangement" audit procedures should be established for the Auditor-General to undertake an audit of the performance information presented to Parliament against the principles outlined in the Charter of Fiscal Responsibility.

## 16.7 Auditing of Forward Estimates

The Queensland Auditor-General currently does not have a role in auditing the Government's budget forward estimates.

In Victoria, the Auditor-General under Section 16B of the *Audit Act 1994* must review each set of estimated financial statements and make a report to the Parliament as to whether it appears that the statements have been prepared on a basis that it appears that

- (a) *the statements are consistent with the accounting policies*
- (b) *the statements are consistent with targets specified in the current financial policy objectives and strategies statement for each key financial measure specified in the statement*
- (c) *the statements are properly prepared on the basis of assumptions contained in the accompanying statement*
- (d) *the methodologies used to determine the assumptions are reasonable.*

This report is to be laid before each House in the Victorian Parliament with the estimated financial statements.

The auditing of estimates has been considered by auditing standard setters, with the issue of Auditing Standard AUS 84 effective from July 2002 on *The Audit of Prospective Financial Information*.

The advantages of having an audit of the budget forward estimates would be:

- greater assurance that an independent officer has reviewed the financial statements and the assumptions behind the statements
- greater rigour and discipline required from those with the responsibility for preparation of the forward estimates, including relevant assumptions and other forecasting parameters; and
- a higher level of confidence in the information provided to Parliament.

The disadvantages of having an audit of the budget forward estimates are:

- additional administrative cost associated with auditing the forward estimates; and
- potential time delays arising from the need to undertake the audit processes prior to completing the estimates.

There is no evidence of concerns about the process for producing Budget forward estimates in Queensland. If concerns were to arise at any time in the future, there is an option for the Auditor-General to undertake a PMS or performance audit (whichever is applicable at the time), with the audit considering whether the systems and processes associated with the development and reporting of the forward estimates could be relied upon.

#### Conclusion

##### *CN.16(vi)*

There is not a strong case for the Auditor-General to be required to undertake an audit of the forward estimates. In the event of any concerns related to the processes for developing and reporting the forward estimates, this could be the subject of an audit of the relevant systems and processes used to produce the forward estimates.

## 16.8 The Term of Appointment of the Auditor-General

The term of appointment of the Auditor-General in Queensland is an appointment of up to seven years, with the possibility of renewal within this period. This varies in some respects from the situation in other jurisdictions. We note that the appointment of the Australian Auditor-General is for a 10-year term. In New Zealand, the Controller and Auditor-General is appointed for a seven-year non-renewable term which can only be exceeded in the event that a successor has not yet been appointed. The terms of appointment for the Auditors-General in Victoria and New South Wales are for fixed terms of seven years.

During our Review, the question was raised as to whether an Auditor-General should be appointed for a term with the opportunity for reappointment for an additional period (say an initial seven-year appointment, with the option of a three-year extension at the discretion of the Government). We do not support such an approach, as it may cause the Auditor-General to be compromised in the quality of audit work undertaken in the period leading up to consideration of an extension of the term of appointment by the Government.

It is our view that a term of seven years is an appropriate length of time to provide sufficient continuity in the leadership of the QAO, while also ensuring that there is sufficient time for

an incoming Auditor-General to put in place any new strategies or directions for the QAO. It also provides for renewal and the introduction of new ideas, perspectives and thinking through a regular turnover of leadership.

However, we prefer a fixed term of seven years, rather than the current provision of "up to seven years", with the provision for an extension for the balance of the period, as this can cause some uncertainty and instability regarding leadership of the QAO. Also, as mentioned above, this could cause the Auditor-General's position to be compromised.

**Conclusion**

*CN.16(vii)*

A fixed, non-renewable seven-year term of appointment for the Auditor-General is appropriate.

**Recommendation**

*RN.16(x)*

**That the *Auditor-General Act 2009* be amended to provide for a fixed, non-renewable seven-year term of appointment for the Auditor-General.**

## 17. STRATEGIC FUTURE ISSUES

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Our conclusions and recommendations in this Review have been directed towards building on the strengths and achievements of the QAO to ensure an ongoing process of continuous improvement which will better position it to address the challenges of the future.

As a strategic review, we have sought not just to evaluate what has occurred since the 2004 Review, but also to consider some of the emerging challenges and issues likely to face the QAO over the five years through to the next Strategic Review and beyond. To state the obvious, no one can have any certainty as to what will happen in the future. Nevertheless, we believe there are some identifiable trends and issues which are likely to impact on the future direction of the QAO's audit functions.

### 17.1 Developments in the Delivery of Public Services

Taken as a whole, the Queensland public sector is substantially the largest business in the State, and impacts in one way or another on the lives of all Queenslanders every day. Over the last 20 years, against a background of significant micro-economic reform, there have been profound changes in the way government conducts its business and, especially, delivers services to the public.

These changes are likely to continue, as the demands and expectations on government service delivery increase and the business of government becomes ever more complex. This is a trend evident not just in the public sector in Queensland, but also in other jurisdictions which we visited during the Review, other jurisdictions throughout Australia, and also in other countries overseas.

The audit function will need to respond commensurately to this ever changing and more complex environment, with increased skills and training, and a preparedness to shape its audit activities around the changing service delivery patterns of government.

The recent Machinery of Government changes which occurred in core public sector agencies following the State Election in March 2009 are a case in point. The reduction in agencies from 23 to 13 will result in significant changes in internal systems and processes, which will impact on the audit function. Over time, as full integration of disparate systems is achieved, it could be expected that there will be efficiencies and savings in the audit function.

In the short term, however, there will be ongoing audit challenges depending on the pace and success of internal business integration processes. Further machinery of government changes cannot be ruled out over time, and the QAO needs to ensure that its audit function is sufficiently robust and flexible to accommodate the changing structure and priorities of government.

The Queensland Government has also announced a significant program of asset sales of government businesses, including Forestry Plantations Queensland (FPQ), Port of Brisbane Corporation (POBC), QR National, Queensland Motorways Limited (QML) and Abbot Point Coal Terminal (APCT). As the QAO is responsible for the audits of all these businesses, once these assets are sold, there will be a reduction in the number of QAO audit clients, although some residual or non-core functions will remain in the public sector and therefore will remain subject to audit by QAO (eg QR's Passenger business). Other disposals (and/or acquisitions) of assets are possible, with further consequent implications for the size and complexity of the audit function.

Apart from asset sales, governments generally are seeking to engage with the private sector on a broad range of fronts to assist in the delivery of public services and infrastructure. This includes joint ventures, special purpose companies, alliance contracting, Public-Private

Partnerships (PPPs), other strategic partnerships as well as outsourcing and other forms of contractual arrangements eg contracting with not-for-profit community organisations to deliver certain social or human services. While the government may be the funder, it is not necessarily the provider of services. Universities also have become more innovative in establishing various corporate structures to commercialise the results of research efforts.

At issue here is the fundamental definition of what constitutes a public sector entity (as per Section 30 of the *Auditor-General Act*) for audit purposes and how far the Auditor-General's powers should extend in executing his or her responsibilities. The generally accepted definition of public sector entities encompasses Departments, Statutory Authorities, Local Governments, GOCs and Controlled Entities.

However, the definition of a public sector entity is becoming increasingly blurred, such that the Auditor-General most likely will be required to make judgments as to the limits of his or her powers in auditing certain entities which may have both public and private sector characteristics. Furthermore, where public funds are distributed for use by third party agencies in the private sector, there are questions as to the legality and appropriateness of the QAO undertaking full-scale financial and compliance audits of such entities.

It is our view that there should be practical and common sense limits on the extent to which the QAO is able to "follow the dollar" in properly accounting for the expenditure of public monies. Where contractual arrangements with third parties are involved, the QAO should be concerned to ensure that there are suitable performance and reporting systems in place and operating to account for the use of public funds in accordance with agreed procedures. It should not be necessary for the QAO to audit such entities, although it is not unreasonable that the QAO would want to be satisfied that the entity is being properly audited. Section 16 of this Report makes recommendations as to circumstances in which it may be appropriate for the Auditor-General to have powers to undertake "follow the dollar" audits.

## **17.2 Investment in Infrastructure and information Technology**

We have noted through this Report the importance of the independence of the Auditor-General. It will be the responsibility of the Auditor-General to determine appropriate topics for future audits, although we nevertheless consider that there is merit in suggesting possible topics for attention by the Auditor-General in future audit programs.

The Queensland Government has in place a major program of investment in infrastructure in South-East Queensland (South East Queensland Infrastructure Plan and Program or "SEQIPP"), as well as similar programs for extensive infrastructure investment in other parts of the State. SEQIPP was first developed in 2005, and is updated on a regular annual basis. The 2009 version of SEQIPP has a planning horizon through to 2026 and involves estimated expenditure of \$124 billion. The Commonwealth Government through Infrastructure Australia also is developing plans for major infrastructure investments, some of which will be channelled through the State and Territories.

Given the magnitude and impact of these massive infrastructure programs, and the size of individual projects, it is important to ensure that funds are invested so as to maximise value for money. In our view, there is a substantive and ongoing role for the Auditor-General in assessing the performance of infrastructure projects in achieving stated objectives and outcomes. This includes compliance with the Government's Project Assurance and Value for Money Frameworks, as well as benefits realisation studies, which compare actual (ex post) outcomes with expected (ex ante) outcomes. The Auditor-General has already shown an interest in such topics, including cross-sector audits on infrastructure project evaluation

(Report to Parliament No. 4 for 2008) and infrastructure project cost escalation, benefits realisation and leaseback of land (Report to Parliament No 4 for 2009).

In a similar vein, we think there is a substantive and ongoing role for the Auditor-General in assessing the value for money achieved by agencies from major investments in Information Technology projects. Investment in IT projects by public sector agencies is now substantial, and is likely to grow further, in both absolute and relative terms, as business systems generally become more heavily IT-based. Again, we note that the Auditor-General has already shown an interest in such topics, including cross-sector audits of ICT project management (Report to Parliament No. 4 for 2008) and IT Network Security (Report to Parliament No. 4 for 2009).

It is recognised that future audits of infrastructure and IT investment may take a number of forms – including traditional attest audits (including cross-sector audits), performance audits, assurance audits or special audits – depending on the ultimate objective of the audit.

#### **Recommendation**

***RN.17(i)***

**That the Auditor-General give consideration to an expanded focus of audits of infrastructure and IT investments, building on the work already undertaken in these areas.**

### **17.3 Auditing of Commonwealth–State Programs**

Funding arrangements between the Commonwealth Government and the States and Territories are complex and, increasingly, there are a range of obligations, commitments or other performance requirements attaching to the funding. They include many programs where funds are provided for expenditure either directly by the States and Territories, or indirectly through other third parties. A recent topical example is the Commonwealth Government's Fiscal Stimulus Package.

This gives rise to issues of responsibility for auditing such programs where there is more than one level of government involved, and the potential for overlap or duplication of audit roles.

The current position regarding grants made to a State or Territory government is that there is an acquittal of the grant, with any audit requirements being the responsibility of the State or Territory Auditor-General. In the case of the Fiscal Stimulus Package, and potentially other similar programs, there is not only the issue of compliance with the funding agreements in terms of acquittal of funds, but also the question of performance related to the use of the funds.

We note that one of the Terms of Reference of a current Joint Committee of Public Accounts Inquiry into the *Commonwealth Auditor-General Act 1977* is on the subject of "*The Auditor-General's capacity to examine the financial and performance outcomes from Commonwealth investments in the private sector and Commonwealth grants made to State and local government*".

In a public hearing held in Canberra on 19 October 2009 by the Joint Committee of Public Accounts, reference was made to specific federal funding to all of the States to reduce elective waiting lists. The argument is whether the Commonwealth will be happy to rely upon reporting of performance information (whether subject to audit by the State Auditor-General or not), or whether the Commonwealth Auditor-General should have the power to audit the integrity of that performance information. That power of the Commonwealth Auditor-

General to directly audit the integrity of performance information was acknowledged at that hearing as being more controversial.

Irrespective of the outcomes of the Joint Committee of Public Accounts Inquiry into the *Commonwealth Auditor-General Act 1977*, there is the issue of completeness of coverage of audit as between the Commonwealth and the States/Territories, and also the issue of potential duplication. There is room – especially given the positive working relationship between Auditors-General at the Commonwealth, State and Territories (including through ACAG) – for there to be cooperation in terms of audit coverage noting any constraints associated with the respective legislated mandates. We understand that there have been exploratory discussions on such matters.

There may be instances for example where audit responsibilities can be assigned to one level of government, with reliance being placed on that audit work by the other level of government. In other circumstances, there may be merit in Auditors-General at the Commonwealth and State /Territory level agreeing to share or jointly undertake an audit task, with different components being undertaken by different Audit Offices.

We are informed that both the Queensland and Commonwealth Auditors-General are currently undertaking audits of the Commonwealth Fiscal Stimulus Package. The Queensland audit is being undertaken as a financial and compliance audit, and hence is focussing on compliance issues. On the other hand, the ANAO is undertaking performance audits of elements of the package, and hence is focussing on issues of efficiency, effectiveness and economy. Care needs to be taken in such cases to avoid the risk of “audit overload”.

We encourage the Queensland Auditor-General to actively pursue avenues for co-operation with his counterparts in other jurisdictions, so that there is no unnecessary waste or duplication of resources in auditing Commonwealth–State programs.

This issue does highlight the need to ensure that the quality of reporting on performance from the State to the Commonwealth remains at a high standard. The role of the Queensland Auditor-General in terms of providing assurance related to information provided, both in terms of acquittal and in terms of performance, is critical.

#### **Recommendation**

##### ***RN.17(ii)***

**That the Queensland Auditor-General continue to actively pursue opportunities for co-operation with Auditors-General at the Commonwealth level and in other States and Territories, with a view to ensuring that there is no unnecessary waste or duplication of resources in auditing of Commonwealth–State programs.**

#### **17.4 Growth in Assurance Audits**

Another trend which we expect to emerge in the foreseeable future is a growth in assurance auditing. Assurance audits fall between financial and compliance (attest) audits on the one hand, and performance audits on the other hand. That is, they provide a higher level of assurance than a performance audit, but not as high as an attestation.

Standards for assurance audits are provided by ASAE 3000, which uses the terms “*reasonable assurance engagement*” and “*limited assurance engagement*” to distinguish between the two types of assurance engagements that an assurance practitioner may perform.

- *Reasonable assurance engagement. The objective of a reasonable assurance engagement is a reduction in assurance engagement risk to an acceptably low level in the circumstances of the assurance engagement as the basis of a positive form of expression of the assurance practitioner's conclusion. Reasonable assurance means a high, but not absolute, level of assurance.*
- *Limited assurance engagement. The objective of a limited assurance engagement is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the assurance engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for a negative form of expression of the assurance practitioner's conclusion.*

To date, the QAO has not used ASAE 3000 to any great extent. However, in our view, growing public scrutiny of the actions of governments and increased pressure for accountability for those actions could lead to greater use of assurance audits as a practical alternative to full-scale attest audits. This is especially the case where there is a focus on a particular function, activity or aspect of an entity or a government's operations, rather than the entire operation.

At the Federal Government level, the ANAO recently has undertaken assurance audits in relation to government information and advertising campaigns and the *Defence Materiel Organisation Major Projects Report*. For the QAO, there are circumstances where the use of assurance audits may become more appropriate. For example, there are some aspects of the QIC audit where an assurance audit may become more appropriate, as QIC's business requires it to provide externally reviewed assurance to its clients about a number of aspects of its operations.

We note that the Auditor-General is currently undertaking an audit of the A1 Grand Prix Agreements. This is being undertaken as a financial and compliance audit, by bringing forward the normal attest audit task. However, it is possible in the future that audits of a special interest nature such as this could be undertaken as assurance audits. It is also likely that ASAE 3000 will become increasingly relevant to audit activity in areas such as infrastructure and IT investments (as mentioned earlier in this Section), carbon reporting, environmental issues and for financial services entities (as per the QIC example above).

## 17.5 Developments in Audit Methodology

An important development impacting audit methodology from 1 January 2010 is the decision taken in October 2009 by the AUASB to approve the revised suite of 41 Auditing Standards under what has been referred to as the "audit clarity" project. The objective of the clarity project is to improve the auditing standards, eliminate ambiguity and enhance understanding

Like existing auditing standards, these revised auditing standards, having been through a process of clarity, have the force of law including under the Corporations Act. The revised standards have application for financial reporting periods commencing on or after 1 January 2010. This does mean that some elements including planning and quality control requirements need to be applied from that date.

### Conclusion

#### CN.17(i)

The QAO needs to ensure that the implications of the revised suite of 41 Auditing Standards following the audit clarity project are incorporated into the audit methodology including IPSAM.

## 17.6 Developments in Accounting Standards

In December 2009, the AASB issued a consultation paper proposing substantial reductions in the volume of disclosures required of most private and public sector entities. This proposes that disclosures under full IFRSs in Australia would only be required for specified major reporting entities in the public sector. For those entities not classified as “major”, they would be able to apply substantially reduced disclosure requirements. Effectively, there would be two groups of reporting entities, being those that are “major” and those that are “second tier”.

If this proposal is adopted by the AASB, this would be subject to an assessment by Queensland Treasury with regard to those Queensland public sector entities which would be identified as able to reduce disclosures.

The intent of the AASB is to issue amendments to accounting standards by June 2010 in order that entities could voluntarily elect to adopt the changed requirements early.

Conclusion:

*CN.17(ii)*

The QAO should monitor the developments associated with the possible establishment of two groups of reporting entities in terms of level of disclosures, and liaise as necessary with Queensland Treasury on implementation issues.

## 17.7 Carbon Reporting and Related Issues

An area of emerging importance for public sector entities is the requirement for carbon reporting. As larger emitters, a number of public sector entities are required from 2008–09 to report their emissions under the *National Greenhouse and Energy Reporting Act 2007*. As well, they are required to report their energy production and consumption to the Commonwealth’s Greenhouse Energy and Data Officer. We note that the National Greenhouse and Energy Reporting Scheme has only required emissions information to be audited if required by the Greenhouse and Energy Data Officer. It is proposed under the Carbon Pollution Reduction Scheme that subordinate legislation and standards will be developed related to auditing of large emitters (some of which are Queensland public sector entities).

Queensland Government agencies are required to report on carbon emissions in annual reports. (This commenced with 2007–08 Annual Reports under the Annual Reporting Guidelines for Queensland Government Agencies, May 2009). A standard template has been developed and requires public sector agencies to report on greenhouse gas emissions linked to areas of i) vehicle use, ii) electricity consumption, and iii) air travel. Other areas of emissions can be reported if required.

At this stage, this information is not subject to audit.

We note that in New South Wales the Public Accounts Committee in its Inquiry into Sustainability Reporting in the NSW Public Sector proposed that the Auditor-General should have a principal role in the verification or auditing of sustainability reports for the NSW public sector.

At the time of this Report, introduction of an emissions trading scheme remains a priority of the Commonwealth Government. While the details of such a scheme remain uncertain, there are potential implications both in terms of direct responsibilities under Commonwealth legislation and also with regard to the range of new treasury products which are arising

related to managing carbon pollution within a carbon costed world. In the meantime, there are existing responsibilities on Queensland public sector entities to monitor and report on their use of energy as well as on greenhouse gas emissions.

At some stage in the future, it is likely that the QAO will become involved in auditing compliance with legislative and regulatory requirements, and also possibly providing assurance with respect to performance in addressing carbon reporting and emissions trading scheme requirements.

Conclusion

*CN.17(iii)*

The audit implications of greenhouse gas reporting requirements and any emissions trading scheme are likely to be significant and will require ongoing monitoring by the QAO.

### **17.8 Integrity and Accountability**

Integrity and accountability are currently a high priority on the agenda of the Queensland Government, as evidenced by its Green Paper of August 2009 on the topic and subsequent policy initiatives announced in November 2009 in the White Paper on Response to Integrity and Accountability. It is likely that the Queensland public will expect further improvements in standards of integrity and accountability over time, in response to changing community standards. As already noted, the Auditor-General and the Audit Office form an important component of the integrity framework of the Queensland Government, and the independence of the Auditor-General is fundamental to the credibility of this framework

There will be occasions when the Auditor-General is expected to, or chooses to, undertake special purpose audits on issues which may involve adverse publicity and/or political controversy. As noted above, this may lead to an increasing emphasis on assurance audits

It is important in such cases that the position of the Auditor-General is not compromised in any way. While it is appropriate for an Auditor-General to conduct an audit of activities after the fact, it would be inappropriate for an Auditor-General to be asked to opine on, or provide assurances as to, a course of action before the fact, as this could compromise the independence of the position and involve the Auditor-General in shaping government policy.

### **17.9 Resourcing and Sustainability for the QAO**

There are a number of factors likely to impact on the workload of the QAO over the next few years, including:

- The volume of audit work for local government, once the full effects of amalgamations are bedded down.
- The volume of audit work for core government departments, once the full effects of last year's Machinery of Government changes are bedded down.
- A reduction in the volume of audit work, once the sale of government businesses currently underway is completed.
- Other possible changes in the structure and/or composition of core government departments, GOCs and/or statutory bodies.
- Possible increases in the volume of assurance audit work.

All these disparate factors will have varying effects on the overall workload of the QAO, but the net effect may well be a reduction in the volume of audit activity.

On the other hand, the QAO potentially faces a number of internal resourcing risks in the next few years:

- A relatively high attrition rate for staff with less than two year's experience with the QAO (who represent a relatively high proportion of staff)
- A solid core of staff aged 55 years or over, who may well be at risk of retirement in the foreseeable future. As many of these employees are in management positions, there is an added risk to the QAO of loss of management expertise.

The QAO is in the fortunate position that it can scale up or scale back the level of contracting activity to manage fluctuations in both workload and internal resourcing capacity. However, the risk to the sustainability and quality of the QAO's future operations cannot be taken lightly.

**Recommendation**

***RN.17(iii)***

**That the QAO develop strategies to manage emerging trends in its workload and its internal resourcing capacity over a three-year planning horizon and to ensure the ongoing sustainability of its business.**

## ATTACHMENTS

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- A – Terms of Reference
- B – Schedule of Stakeholders Interviewed
- C – Schedule of Audit Files Examined
- D – Schedule of Auditor-General’s Reports on Performance Management Systems Audits since 2005
- E – Schedule of Cross-Sector Audits tabled in Parliament in 2008 and 2009
- F – Summary of Outcomes of 2004 Strategic Review
- G – Acknowledgements
- H – Response by the Honourable the Premier and Minister for the Arts to the Proposed Report
- I – Response by the Auditor-General to the Proposed Report

## ATTACHMENT A: TERMS OF REFERENCE

### SCOPE

In accordance with Section 68 of the *Auditor-General Act 2009* (the Act) a strategic review of the Queensland Audit Office (QAO) is to be conducted at least every five years. The “strategic review” as defined in Section 68(7) of the Act is to include:

- “(a) a review of the auditor-general’s functions; and
- (b) a review of the auditor-general’s performance of the functions to assess whether they are being performed economically, effectively and efficiently.”

The appointee will be required to generally assess, and provide advice and recommendations about, the functions and the performance of the functions, of the Auditor-General and the QAO, in order to assess whether they are being performed in accordance with the requirements of the Act.

The review is to examine all structural and operational aspects of the QAO, as well as its relationships with public sector entities, relevant Ministers, the Treasurer and the Parliament of Queensland.

Consideration is also to be given to the recommendations agreed by the Government arising from both the 2004 strategic review, and the related Public Accounts and Public Works Committee report on the review and the Government’s response to the Committee’s report, particularly the extent to which they have been implemented and whether they are achieving the desired objectives.

The appointee will have the powers vested in them under Section 69 of the Act in order to conduct the review

### METHODOLOGY

In conducting the strategic review, the appointee is to have regard to the QAO’s existing governance framework including strategic and operational plans, the organisational structure, corporate and operational management, operational conduct, internal/external policies, and audit service provisions the QAO.

Particular reference is to be given to:

- (a.) whether existing processes are appropriate to the QAO’s audit mandate, the needs of public sector agencies and emerging public sector organisational structures;
- (b.) the effectiveness of existing processes, and in particular the effectiveness of the auditing standards issued by the Auditor-General, in fulfilling the audit mandate within the contemporary accountability requirements of Queensland’s system of government;
- (c.) examination of trends in the workload of the QAO, including an examination of current and past methodologies relating to practices and procedures employed by the QAO;
- (d.) the operational efficiency of QAO audit methodology and the relative efficiency of in-house and contract audit service provision;
- (e.) the standard and quality of service provided to the Parliament, audit clients and executive Government;
- (f.) the structure of the QAO, including the delegation and allocation of responsibilities;
- (g.) management systems and processes used by the QAO, including:

- (iii) appropriate internal and external performance indicators to monitor efficiency and effectiveness; and
- (iv) internal communication and sharing of performance information;
- (h.) human resource issues, including formal and informal staff training and guidance;
- (i.) administrative systems and processes used by the QAO;
- (j.) whether the funding for the QAO is both appropriate and appropriately used to discharge the functions and objectives of the QAO;
- (k.) appropriate protocols for communication by and with the QAO; and
- (l.) any other matters which impact on the economy, efficiency and effectiveness of the QAO.

The review should also take into account:

- consideration of comparative models, practices and procedures used by offices in other jurisdictions equivalent to the QAO;
- the results of the Public Accounts and Public Works Committee's review of the Auditor-General's performance management systems mandate;
- interviews with staff (including all staff who indicate that they wish to be interviewed by the appointee) and former staff of the QAO, both individually and in focus groups (interviews with former staff are optional);
- consultation with key Government agencies; and
- consultation with other key stakeholders, including accounting firms that conduct business with the QAO.

**ATTACHMENT B: SCHEDULE OF STAKEHOLDERS INTERVIEWED**

Queensland Parliament	Public Accounts and Public Works Committee Chair Other Members of the Committee
Ministers	Queensland Treasurer Minister for Transport
Departments	Community Services Coordinator-General/Department of Infrastructure and Planning Education & Training Health Premier and Cabinet Public Service Commission Public Works Transport and Main Roads Treasury
Local Governments	Brisbane City Council Gold Coast City Council Rockhampton Regional Council Toowoomba Regional Council Townsville City Council Woorabinda Aboriginal Shire Council
Statutory Bodies/ GOCs	CS Energy Limited Energex Limited Ergon Energy Corporation Limited Port of Brisbane Corporation Limited Port of Townsville Limited QIC Limited

Statutory Bodies/ GOCs	QR Limited  Queensland Bulk Water Supply Authority (Trading as SEQWater)  Queensland Electricity Transmission Corporation Limited (trading as Powerlink Queensland)  Queensland Water Infrastructure Pty Ltd
Universities	Central Queensland University  James Cook University  Queensland University of Technology
Grammar Schools	Brisbane Girls Grammar School
Contract Auditors	(3 firms including in Toowoomba and Townsville)
Auditors-General	Australian National Audit Office  New South Wales Auditor-General  Victorian Auditor-General
Queensland Audit Office	Auditor-General  Deputy Auditor-General  Staff and former staff, including all current members of the Executive Management Group.  Staff Welfare Committee  Women's Leadership Group  Chair of the Audit and Risk Management Committee  External Auditor

**ATTACHMENT C: SCHEDULE OF AUDIT FILES EXAMINED**

Financial and Compliance Audits (2008–09)

Department of Education and Training

QR Limited

Brisbane City Council

University of Queensland

Performance Management Systems Audits

*Transport Network Management and Urban Congestion in South East Queensland* (Report No 3 for 2009)

*Management of Patient Flow through Queensland Hospitals* (Report No 5 for 2009)

Cross Sector Audits (both reported as part of Report No 4 for 2009)

*IT Network Security*

*Understanding and Complying with Legislation*

**ATTACHMENT D: SCHEDULE OF AUDITOR-GENERAL'S REPORTS ON PERFORMANCE MANAGEMENT SYSTEMS AUDITS SINCE 2005**

<b>Report No.</b>	<b>Title</b>
No 3 for 2005	Results of Performance Management Systems Audits of Output Performance Reporting
No 5 for 2005	Results of Performance Management Systems Audits of Output Performance Reporting – Phase 2
No 2 for 2006	Results of Performance Management System Audits Government Owned Corporations' Performance Reporting
No 5 for 2006	Results of Performance Management Systems Audits of Capital Works at Department of Corrective Services, Education, Health and Housing.
No 6 for 2006	Results of Performance Management Systems Audit of Workforce Planning at Departments of Education and Health
No 8 for 2006	Results of Performance Management Systems Audit of the Management of Departmental Fees and Charges
No 2 for 2007	Results of Performance Management Systems Audit of Management of Funding of Non-Government Organisations (NGOs)
No 4 for 2007	Are departmental output performance measures relevant, appropriate and a fair representation of performance achievements?
No 6 for 2007	Beyond agency risk
No 7 for 2007	Addressing skills shortages in Queensland
No 8 for 2007	South East Queensland – Towards Short-Term Water Balance
No 1 for 2008	Enhanced Accountability through Annual Reporting
No 3 for 2008	Management of Rural Fire Services in Queensland
No 5 for 2008	Protecting Queensland's Primary Industries and Environment from Pests and Disease
No 6 for 2008	Follow-up audit of Workforce Planning at Departments of Education, Training and the Arts and Health, incorporating their responses to an ageing workforce
No 7 for 2008	Administration of Grants and Funding to Community Organisations by Local Government in Queensland: A Performance Management Systems Audit
No 8 for 2008	Follow-up of Selected Audits tabled in 2006
No 2 for 2009	Health Services Planning for the Future
No 3 for 2009	Transport Network Management and Urban Congestion in South East Queensland
No 5 for 2009	Management of Patient Flow through Queensland Hospitals
No 6 for 2009	Providing the Information Required to Make Good Regulation
No 7 for 2009	Follow-up on Government Owned Corporation and Budget Sector Performance Measurement and Reporting

**ATTACHMENT E: CROSS SECTOR AUDITS REPORTED 2008 AND 2009**

<b>Report No</b>	<b>Cross Sector Audits Reported</b>	<b>Date Tabled</b>
No 2 for 2008	Key issues from 2006–07 Audits Audit Committees	1 May 2008
No 4 for 2008	Results of Compliance Audits <ul style="list-style-type: none"> <li>• Management of Public Sector Employee Housing</li> <li>• Fraud Risk Management</li> <li>• Corporate Card Use and Management</li> <li>• Information and Communication Technology (ICT) Project Management</li> <li>• Infrastructure Project Evaluation</li> </ul> 2007 University and Grammar School Audit Results <ul style="list-style-type: none"> <li>• Risk Management Audit</li> </ul>	8 July 2008
No 4 for 2009	Infrastructure <ul style="list-style-type: none"> <li>• Project Cost Escalation</li> <li>• Benefit Realisation</li> <li>• Leaseback of Land</li> </ul> Sustainability <ul style="list-style-type: none"> <li>• Valuation Indices</li> <li>• Follow up of 2007 Asset Impairment Audit</li> </ul> Governance <ul style="list-style-type: none"> <li>• Audit of Security Management Systems</li> <li>• IT Network Security</li> <li>• Understanding and Complying with Legislation</li> </ul>	30 June 2009
No 8 for 2009	Accountability <ul style="list-style-type: none"> <li>• Infrastructure Project Procurement</li> </ul>	12 November 2009

**ATTACHMENT F: SUMMARY OF OUTCOMES OF 2004 STRATEGIC REVIEW**

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<b>C.1.2: Performance Management System Audits and Performance Audits</b>			
<p>The QAO, in consultation with the PAC, develop a three year plan to undertake at least 20 targeted PMS audits across the public sector, with each audit taking no more than six months.</p>	<p>Supported, subject to eliminating the suggested targets</p>	<p>Endorsed PAC position, on the basis that setting targets could compromise the independence of the Auditor-General</p>	<p>The QAO has an annual work planning process which includes PMS audits. However, three-year plans have not yet been developed.</p> <p>Over the past five years, the time taken to complete a PMS Audit while still fulfilling the required objectives has decreased from an average duration of 10.25 months prior to 2005 to 6.8 months in 2008–09.</p> <p>The QAO now has the lowest average elapsed time for reporting PMS audits to Parliament compared to all other Audit Offices in Australia, as shown by ACAG benchmarking. In 2007–08, the average time to table a PMS Audit Report was 11 months and 12 months in New South Wales and Victoria respectively.</p> <p>By decreasing the elapsed time for completing a PMS Audit, more PMS Audit Reports have been produced. In total, 21 reports on PMS Audit Reports have been tabled in Parliament since 2005, covering 94 individual entities. The number tabled per year has increased from 2 to 6.</p>
<p>The PAC undertake detailed scrutiny of PMS audit reports when completed.</p>	<p>Supported</p>	<p>Endorsed PAC position</p>	<p>Between 2005 and March 2009, the two PACs convened in this period conducted 6 public hearings and examined 11 PMS Reports to</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
			Parliament during those hearings. The PAPWC is currently examining Report No.1 for 2008 and Report No.3 for 2008. The PAPWC's report on Report No 2 for 2007 was tabled in Parliament on 17 September 2009.
The PAC evaluate the value of PMS audits at the end of this three year period and report on the effectiveness of the PMS audit mandate in terms of Parliament's previously expressed position.	Supported	Endorsed PAC position	The PAPWC has commenced its inquiry into the effectiveness of the PMS audit mandate as per Parliament's previously expressed position. Public hearings were held in late 2009, and the PAPWC is expected to complete its report in the first half of 2010.
The current PMS audit mandate remain in place pending the outcome of this process.	Supported	Endorsed PAC position	An expansion of the PMS audit mandate to include a review by QAO of the relevance of performance measures came into effect on 1 January 2007.
In the event that the PMS audit mandate is not delivering what Parliament intended, a performance audit mandate be further considered.	Supported	Endorsed PAC position	This is a matter being considered by the PAPWC as part of its current inquiry. It is also a matter addressed in Section 14 of this Report.
An appropriate level of resources be provided to the QAO to enable the plan to be fully implemented.	Supported	Endorsed PAC position	Additional funding for approximately \$1.9m as requested by the Auditor-General was approved in the QAO Budgets from 2005 to 2009.  Permanent staff numbers in the PMSA Section for the QAO have increased from 9 in 2004-05 to 18 at 30 June 2009.

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<b>C.1.4: Audit Coverage</b>			
<p>The QAO continue to address auditee concerns regarding the resolution of complex accounting and financial reporting issues by continuing to proactively work with auditees and through education forums.</p>	<p>The PAC supports the QAO's action in addressing this recommendation</p>	<p>Supported recommendations, and acknowledged the work being undertaken by the QAO to address the recommendation</p>	<p>The QAO provides advice on complex accounting and financial reporting issues both on a sector wide basis and for individual clients where necessary. The QAO works closely with Treasury Department on significant financial reporting issues affecting clients.</p> <p>Advice on complex accounting and financial reporting issues is provided through Reports to Parliament, INFORM, better practice guides and other guidance publications including checklists, as well as through client information sessions and regional visits</p> <p>The QAO has in place a number of communications strategies, which are addressed in Section 12 of this Report..</p>
<p>QAO continue to address through education and communication, auditee concerns about the perceived emphasis of the QAO on matters thought to be immaterial in a financial sense or of minor significance or beyond the scope of audit, eg. matters of organisational policy.</p>	<p>The PAC supports the QAO's action in addressing this recommendation</p>	<p>Supported recommendations, and acknowledged the work being undertaken by the QAO to address the recommendation</p> <p>Noted that the QAO is consulted by the Treasury Department in the development of new accounting and financial reporting policies</p>	<p>The QAO has incorporated specific material on the role of the Auditor-General and concepts including probity and propriety into publications such as INFORM. The audit policy and guidance material concerning probity and propriety issues was reviewed and incorporated in IPSAM, the audit methodology.</p> <p>The QAO also has a policy on matters of significance for reporting to Parliament. Training is provided to staff on identifying matters of significance.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<b>C.1.5: Commercial Audits</b>			
<p>QAO develop in consultation with the PAC, guidelines and principles to govern the participation by the QAO in</p> <ul style="list-style-type: none"> <li>- collegiate type activities with other audit offices in Australia, and</li> <li>- aid programs for developing countries, particularly in the South Pacific.</li> </ul>	<p>The QAO to advise the PAC of any collegiate activities</p>	<p>Endorsed PAC position</p>	<p>The Auditor-General discussed the position with the former PAC and agreed to keep the PAC (now the PAPWC) informed of any proposals for the involvement of QAO in aid programs. The previous PAC agreed to on-going involvement by the QAO in regular collegiate activity through ACAG. Examples of recent activities include VAGO reviews of QAO files.</p> <p>QAO staff have been allowed to take secondments on leave without pay to work with the Solomon Island Audit Office to improve the skills of their audit staff. QAO has also supported staff from the Solomon Islands for short temporary placements with the audit teams.</p> <p>The QAO is currently participating with the ANAO in placing two officers from PNG on a temporary basis as part of their Twinning Program in 2010. As part of other collegiate activities, secondments to and from VAGO and the QAO have also taken place with closer working relationships between other Audit Offices across Australia in key areas such as human resources and practice management systems.</p> <p>The contract for the audit of the Norfolk Island Government concluded in 2005 and no extension was sought by QAO.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<p>QAO ensure that participation has demonstrable benefits for the QAO and/or the State and that the core audit program is not compromised as a result.</p>	<p>The QAO prepare, on a case-by-case basis, a detailed business proposal to support its participation in audit services or aid programs outside of Queensland. Each business case should address the issues contained in the Recommendation, and should be the subject of consultation with the PAC.</p>	<p>Endorsed PAC position</p>	<p>The Auditor-General discussed this activity with the previous PAC and it was agreed that this be continued subject to periodic advice to the PAPWC of any activity.</p> <p>The QAO shares information through collegiate type activities such as benchmarking QAO processes against other leading audit offices and leveraging off work undertaken in other offices in emerging public sector areas.</p>
<p><b>C.2.1: TeamAsset</b></p>			
<p>The QAO finalise as a matter of urgency, a strategy to replace TeamAsset, such strategy to include an implementation program which would ensure that the replacement platform is in place before current licensing arrangements and support for TeamAsset ceases in 2007.</p>	<p>Supported</p>	<p>Endorsed PAC position. The QAO was provided with additional funding over the two years 2004–05 and 2005–06 for software upgrade and replacement</p>	<p>TeamAsset was replaced by IPSAM, which was jointly developed by the QAO and the VAGO. Version 1 of IPSAM was first used for audits in 2005–06 audits. The initial product development was completed with Release 1.3 which was provided to staff on 29 May 2006.</p> <p>At this time, the product moved from the development stage to a maintenance and development stage. Release 2 was released in October 2006, with minor upgrades in 2007 and 2008.</p> <p>Release 3 was implemented in October 2009 of the 2009–10 audit year. Significant changes have been made to the information systems audit procedures in this release. IPSAM is currently licensed by the Tasmanian and ACT Audit Offices and is being piloted by the SA and</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
			WA Auditor-General's Offices.
<p>Given the importance of an appropriate electronic platform to the core QAO audit functions, regular progress reports be provided to the Parliament on this matter.</p>	<p>Supported</p>	<p>Endorsed PAC position</p>	<p>Since the implementation of IPSAM in 2005, the QAO has had a stable electronic platform for core audit functions. The Auditor-General keeps the Parliament informed of any issues relating to IPSAM through written and oral briefings to the PAPWC.</p>
<p><b>C.2.3: Client Service Plans</b></p>			
<p>The timetable for preparation and agreement with auditees of the Client Service Plan be reviewed to address concerns expressed by auditees that generally this has been left too late for them to give proper consideration to the Plan.</p>	<p>The PAC noted that the QAO was addressing this recommendation to its satisfaction</p>	<p>Supported recommendation, and acknowledged work being undertaken by the QAO to address this recommendation</p>	<p>The QAO consults with clients in the preparation of the client strategy. The client strategy documents are communicated to client management and the Audit Committee at the earliest possible opportunity. The pro-forma client strategy is reviewed and updated annually as part of the IPSAM update to ensure it best reflects the current environment. The pro-forma client strategy is approved at least annually by the EMG. Some concerns were still raised by audit clients. These issues are addressed in Section 12 of this Report..</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<p>The QAO increase its commitment to programs of staff training and client information to enhance relationships with auditees.</p>	<p>The PAC noted that the QAO was addressing this recommendation to its satisfaction</p>	<p>Supported recommendation, and acknowledged work being undertaken by the QAO to address this recommendation</p>	<p>The QAO has increased its commitment to programs of staff training and client information. Training and development issues are addressed in Section 11 and client communication in Section 12 of this Report.</p> <p>Responses to the QAO's client survey indicate that an average of 93 per cent of financial and compliance audit clients over the past three years of the survey felt that QAO staff interacted with their staff in a professional manner during the conduct of the audit.</p> <p>The Client Relationship Management Program includes initiatives for increased training in client relationship management. Two client Information sessions on current accounting and auditing issues and on PMS audits respectively are held annually.</p>
<p><b>C.3.1: Use of Contractors</b></p>			
<p>Auditees be consulted on the appointment and the terms of appointment of contractors proposed to undertake their audit and QAO should include in its management process suitable steps to achieve this.</p>	<p>The PAC supported the QAO's actions in addressing this recommendation</p>	<p>Supported</p>	<p>The QAO has implemented revised contracting procedures, which include a process whereby the audit client is contacted and comments about conflicts of interest and other matters obtained and considered as part of the selection of the audit contractor. This ensures that audit client views are given appropriate consideration before the selection of the contract auditor is finalised.</p> <p>However, all audits are the responsibility of the Auditor-General. Therefore, it is considered necessary for the Auditor-General to retain the capacity to control the appointment of a contract</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
			auditor for any individual audit.
<b>C.3.2: Internal Audit</b>			
Continue to address auditee concerns about internal audit through better communication of the difficulties being experienced in relying on the work of internal audit.	The PAC supported the QAO's actions in addressing this recommendation	Supported	<p>The QAO has mechanisms in place to communicate issues with internal audit work to clients/internal auditors. IPSAM has in place a policy to provide guidance to QAO auditors in assessing the work of internal audit and providing feedback to clients. Intended reliance on internal audit work is included in the client strategy.</p> <p>QAO engagement leaders and team leaders include any issues regarding the effectiveness of Audit Committees and internal audit units in reports to the client.</p>
Continue to encourage auditees to improve the quality of internal audit.	The PAC supported the QAO's actions in addressing this recommendation	Supported	See previous comment
Further develop staff exchange and secondment programs with internal audit within auditee organisations.	The PAC supported the actions of the QAO in addressing this recommendation	Supported	<p>From 2005 to 2009, 40 staff from the QAO participated in various exchange/secondment/leave without pay programs to undertake work in other organisations. Of these, 6 involved a placement in internal audit.</p> <p>Staff pressures in both the QAO and host organisations affect the extent to which the QAO can plan to involve greater numbers of staff on secondments to internal audit units.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<b>C.3.4: Regional Presence</b>			
<p>The QAO examine its current approach to servicing auditees in regional and remote areas with a view to developing strategies to increase its presence in these areas and thereby its active involvement with regionally based auditees. Such strategies should incorporate more regional visits to facilitate greater interaction with individual auditees.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported, subject to any additional resource implications being considered as part of the budget process</p>	<p>As the majority of audits in regional and remote areas are medium to low risk audits with limited financial resources, the QAO considers carefully the cost benefit of opportunities to engage these clients and the effect that these opportunities will have on audit fees. Most commonly used tools are client feedback processes, attendance by senior staff at industry and sector conferences, audit committee meetings, and INFORM magazine. With the recent appointment of a communications officer, QAO's strategy in this area is being reviewed to identify further enhancements.</p>
<b>C.3.6: Audit Specialist Technical Skills</b>			
<p>The QAO review current strategies for meeting audit specialist technical skill needs to ensure that it continues to be able to access the necessary skills and expertise, particularly in the area of information technology, treasury and other systems.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported</p>	<p>The QAO has increased efforts in recent years towards building the capacity of the specialist groups, including PMS audits, the Information Systems Audit Group and the Treasury Products Audit area.</p>
<b>C.4: The Role of the Public Accounts Committee and the Parliament</b>			
<p>Acknowledging that this is ultimately a matter for the Parliament and the PAC, we nevertheless recommend that careful consideration be given to the conclusions we have outlined.</p>	<p>Supported</p>	<p>Endorsed PAC position</p>	<p>Since the 2004 Review, the Auditor-General and the PAC (now the PAPWC) have continued to consult. We have made further recommendations concerning consultation with the PAPWC. See Section 15.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<b>D.1.4: Gender/Equity Issues</b>			
<p>QAO review its current recruitment strategies, including the use of interchange arrangements, particularly on a targeted basis, to ensure that the current gender imbalance in senior levels of management continues to be actively addressed.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation, and noted that the QAO had been active in attempting to address these issues.</p>	<p>Supported, and acknowledged work being done to support the Government's commitment to equality and equity in the workplace</p>	<p>The QAO has been progressing a number of initiatives in support of this recommendation. These initiatives are addressed in Section 11 of this Report.</p>
<p>Continue to be proactive in fostering the employment of underrepresented groups in the QAO to achieve outcomes consistent with broad strategic Government outcomes.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation, and noted that the QAO had been active in attempting to address these issues.</p>	<p>Supported, and acknowledged work being done to support the Government's commitment to equality and equity in the workplace</p>	<p>The QAO completed a review and update of its EEO Management Plan covering the period 1 July 2005 to 30 June 2007 and presented the plan to the Public Service Commissioner. The plan provided strategies and actions covering all EEO target groups. Summary for the year 2003–2009 is provided in figure 18 page 77 of the QAO 2008–09 Annual report.</p> <p>From 1 July 2008, new legislation was enacted (<i>Public Service Act 2008</i>), which states that there is no need for a EEO Plan, but statistics would be still required and would need to be reported to the Public Service Commission annually. All agencies and departments may also take local action regarding these target groups as part of their Workforce Plan and relevant strategies.</p> <p>The QAO has been progressing a number of initiatives in relation to this recommendation. These initiatives are addressed in Section 11 of this Report.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<b>D.2.1: Cost Recovery</b>			
<p>The current fee-determination process incorporate a further element of cost recovery for training and development needs.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>No objection, subject to any change in the audit fee calculation requiring the approval of the Treasurer</p>	<p>A fees and funding review was conducted in 2008 resulting in the Treasurer agreeing to increase the basic fee rate by 10.8 per cent rather than by the inflation rate. This included a provision for the increasing cost of staff training and development. Issues related to training and development are considered further in Section 11 of this Report.</p>
<p>There be no change to the current policy of not charging for PMS audits.</p>	<p>Endorsed</p>	<p>Supported</p>	<p>It is QAO policy that no audit fee is charged for PMS audits. (No Audit Office in any jurisdiction in Australia imposes an audit fee for performance-related audits.)</p>
<p>There be greater engagement of auditees by the QAO in the fee determination process to ensure that the fee charged is well-understood and accepted, and that opportunities are afforded to reduce the fee in appropriate circumstances and to be increased where circumstances warrant.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported, and noted actions being taken by the QAO to ensure that the process is effectively communicated and understood</p>	<p>Audit fees are calculated from the number of audit hours spent and the basic hourly rates approved annually by the Treasurer. Engagement Leaders review the fee for the audit each year. An estimate of the audit fee is provided to and discussed with the audit client when the client strategy is presented. Increases in audit fees are discussed with the audit client as these occur.</p> <p>There remains some concerns from audit clients about the fee setting process. These issues are addressed further in Section 7 of this Report.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<p>The QAO should continue to improve time management and recording processes for the audit task consistent with best practice.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported, and noted action being taken by the QAO to review its time recording systems</p>	<p>eTrack (which replaced the ATOMS time recording software) was implemented in November 2007, and is designed to offer a number of features such as integrated staff time-sheeting and invoicing, planning of all staff activities (including billable time), detailed planning of each audit job and reporting of staff utilisation and availability.</p> <p>There have been some problems in the implementation of eTrack, which are addressed in Section 10 of this Report.</p>
<p><b>D.2.2: Adequacy of Resources</b></p>			
<p>The resources allocated to the PMS audit function not be called upon to undertake other tasks such as special audits except in exceptional circumstances.</p>	<p>Supported</p>	<p>Endorsed PAC position</p>	<p>Since January 2005, the number of PMS auditors has increased from 9 to 18. These auditors are structured into dedicated teams assigned to complete and report on each PMS Audit. Audits are completed and reports tabled within an average of 6.8 months (as at 30 June 2009). Any decisions to involve PMS audit staff on activities outside their division are undertaken on a case-by-case basis by the Auditor-General with regard to the priority of the issues involved.</p>
<p>Consideration be given to additional funding for training and development funded by a small increase in audit fees, as discussed in section D.2.1.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>No objection, subject to any change in the audit fee calculation requiring the approval of the Treasurer</p>	<p>A fees and funding review was conducted in 2008 resulting in an increase in the basic fee rate of 10.8 per cent being approved by the Treasurer. This included a provision for the increasing cost of staff training and development. Issues related to training and development are considered</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
			further in Section 11 of this Report.
Additional funding be provided for PMS audits, as discussed in section C.1.2.	Supported	Endorsed PAC position	Additional funding of approximately \$1.9m as requested by the Auditor-General has been approved in QAO budgets from 2005 to 2009 to cover inter alia increased PMS Audit activity.
<b>D.3.1: Recruitment</b>			
QAO continue to ensure that current selection criteria and processes, particularly for senior positions, do not discourage female applicants and applicants who may not have recent public sector auditing experience.	The PAC supported the actions of the QAO in addressing this recommendation	Supported recommendation, and supported action being taken by the QAO to address this recommendation	The QAO advises that selection criteria for all positions are reviewed and amended if necessary prior to advertising to remove any unintended bias. The criteria in place reflect an appropriate balance of personal and technical knowledge skills and abilities for each position. The majority of audit positions have only one selection criteria relating to technical knowledge and most positions do not require prior or specific public sector knowledge. A major review of position descriptions was undertaken by Mercer (Aust) Pty Ltd in January 2008.  Gender and equity issues are addressed further in Section 11 of this Report.
<b>D.3.2: Training and Development</b>			
The level of funding commitment to training and development be increased to a minimum of 1.5% of the QAO budget within three years to a level of at least \$400 000 per annum, funded as proposed in section D.2.1.	The PAC supported the actions of the QAO in addressing this recommendation	Supported recommendation, and noted action being taken by the QAO to address the recommendation.	Expenditure charged to professional development has fluctuated over the past five years. By 2008–09, time spent on internal and external courses including presentation and development had increased to 15,395 hours, equating to an estimated value of \$1.167 million

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
			of expenditure. Based on total expenditure shown in the QAO's 2008–09 Annual Report, professional development was 2.9% of total expenditure.
<p>QAO re-evaluate its participation arrangements in regard to the Senior Executive Service mobility program. If necessary, it should adopt a broader view of acceptable skills for those coming into the QAO and a temporary refocus of duties of particular positions to increase the attractiveness of the arrangements.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported</p>	<p>The QAO participated on the Mobility Program at SO level from 2005 to 2008, with officers coming into the QAO in 2005, 2006 and 2007. Structural rearrangements were put in place to facilitate these placements.</p> <p>Attempts to achieve involvement at the SES level over this period were not successful, but the QAO's participation widened the appreciation amongst likely internal and external participants and stakeholders of the potential for mobility at the SES levels.</p> <p>Also in 2006, an SES officer participated in a one way interchange with the Australian Securities and Investment Commission. The 2009 Program was put on hold due to Machinery of Government changes.</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<p>The QAO develop a suite of protocols, practices and procedures to encourage and facilitate a greater level of interchange between the QAO and the private sector to broaden work experience and skill enhancement opportunities, such arrangements to incorporate a more targeted approach to recruiting suitable participants.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported</p>	<p>The QAO advises that interchange arrangements with the private sector have proven difficult to arrange in the past because of a general reluctance from private sector firms to participate. Alternative strategies have been adopted including the interchange of two senior staff to the Australian Securities and Investment Commission (ASIC) in 2006. This work involved substantial interaction with the private sector.</p> <p>The QAO's secondments policy addresses protocols for secondments and interchanges. During 2009, three staff from the private sector were employed on a temporary basis through arrangements with a private sector firm. This was made easier due to the general economic conditions impacting on the private sector audit firms.</p>
<p><b>D.3.4: Remuneration and Reward Structures</b></p>			
<p>A more flexible remuneration structure for the professional audit staff be introduced which is based on professional development, experience, competency and skill measured against appropriate benchmarks.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>No objection to the matter being considered further, but noted that there were significant implementation issues that would need to be addressed in the development of any revised remuneration arrangements</p>	<p>The QAO commissioned a review of the remuneration structure by an external consultant in 2006. The report highlighted the substantial challenges and difficulties associated with implementing a system outside of the core public service arrangements. It was not immediately apparent that the benefits would outweigh the costs.</p> <p>While the matter has continued to be considered, the QAO has taken other initiatives within the current award and employment arrangements to</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
			<p>address a number of the issues that prompted the recommendation, including the development of PASS.</p> <p>Remuneration issues are addressed further in Section 11 of this Report.</p>
<p>This matter be taken up with the Acting Public Service Commissioner and the Department of Industrial Relations as a matter of priority.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>No objection to the matter being further considered by the Department of Industrial Relations and the Public Service Commissioner</p>	<p>The QAO advises that, since 2005, there have been a number of discussions with the Public Service Commissioner which indicated it would be difficult to change QAO's current remuneration structures. However, the concept of a professional progression scheme was suggested to improve the linkages between experience, qualifications and remuneration. This has led to the development of PASS.</p> <p>Remuneration issues are addressed further in Section 11 of this Report.</p>
<b>E: Communication</b>			
<p>The style and presentation of reports to Parliament be reviewed to ensure that each report fully informs and that the need for explanatory briefings to other stakeholders, including the media, is not required. To assist this process, the Auditor-General should consider publishing with each report, a separate short précis publication for broader public consumption.</p>	<p>The PAC supported the actions of the QAO in addressing this recommendation</p>	<p>Supported recommendation, and noted action being taken by the QAO to address the recommendation</p>	<p>The QAO advises that the style and presentation of reports is continually under review. A particular focus has been the development of a more readable plain English style with less jargon which is more succinct for readers of QAO reports. A separate "executive summary" document has been included with all Auditor-General's Reports published since Report No.7 for 2007 (November 2007).</p>

2004 Review Recommendations	Public Accounts Committee Position	Government Response	Current Status
<p>The Auditor-General develop in consultation with the PAC on behalf of the Parliament, a set of protocols for dealing with the media, particularly in regard to reports to Parliament.</p>	<p>Not specifically addressed</p>	<p>Not specifically addressed</p>	<p>The Auditor-General discussed this matter with the former PAC and broad arrangements were agreed (refer PAC Report No.69, June 2005). All Reports to Parliament stand on their own merits. The Auditor-General does not normally issue press releases regarding the release of Reports to Parliament.</p>

## ATTACHMENT G: ACKNOWLEDGEMENTS

We wish to place on record our sincere appreciation to the Auditor-General, Mr Glenn Poole, for his willing assistance and support during the course of our Review.

Mr Poole and other senior staff were of significant assistance in the provision of information and briefings requested, in responding to questions and queries during the course of the Review, and in providing feedback and comments on early drafts of our Report.

We were pleased to meet with the Queensland Treasurer, Mr Andrew Fraser MP, and the Minister for Transport, Ms Rachel Nolan MP, and we thank them for providing useful insights on the audit function from their perspectives.

We also thank Mr Wayne Wendt, Chair of the Public Accounts and Public Works Committee of the Queensland Parliament, for meeting with us and providing valuable feedback to us on consultation with the QAO and related audit matters. We also thank other members of the Committee who also met with us and contributed their views.

We also wish to thank the staff and former staff of the QAO who met with us either in group meetings or individually and provided open and honest feedback and comments. This has been invaluable for us in undertaking the Review.

Our thanks also to the Directors-General, Chief Executive Officers and other senior staff of audit clients as well as contract auditors who met with us and spoke frankly of their experiences with the QAO.

We also acknowledge the support provided by Mr Ian McPhee, Commonwealth Auditor-General and the staff of the Australian National Audit Office, Mr Peter Archestraat, New South Wales Auditor-General and his Deputy Mr Tony Whitfield, and Mr Des Pearson Victorian Auditor-General and Dr Peter Frost for meeting with us and also for information provided to assist us with the Review.

We thank Mr Henry Smerdon who undertook a quality review of our Report and provided helpful comments to us.

We acknowledge the support of staff of the Department of the Premier and Cabinet in terms of general assistance, as well as the provision of separate office space and computing capability for the Review to make our task easier, and to ensure that we maintained our independence from our other commitments.

Finally, we express our gratitude to Jenny Gray for her patience, commitment and dedication in typing, formatting and printing this Report for us.

**ATTACHMENT H: RESPONSE FROM THE PREMIER TO THE PROPOSED REPORT**



## Premier of Queensland

For reply please quote: ES/MK – TF/10/3976 – DOC/10/19579

25 FEB 2010

Mr Mark Gray and Mr Graham Carpenter  
Strategic Reviewers of the Queensland Audit Office  
C/- BDO Kendalls Corporate Finance (QLD) Ltd  
Level 18, 300 Queen Street  
BRISBANE QLD 4000

Dear Mr Mark and Mr Graham Carpenter

Thank you for your letter of 4 February 2010 in which you provide a copy of the *Proposed Report of the 2010 Strategic Review of the Queensland Audit Office (QAO)*, in accordance with the *Auditor-General Act 2009*.

I offer the following comments on the content of the report.

*Amendment of the Financial Accountability Act 2009 to ensure appropriate reference to value for money (Recommendation RN.3(i))*

In introducing the *Financial Accountability Act 2009*, the Government has taken a less prescriptive approach to the former *Financial Accountability and Audit Act 1977*, relying on subordinate legislation and policy documents to provide guidance to accountable officers, including the *Financial and Performance Management Standard 2009*.

While I acknowledge your comments on this matter, it is my view that the principles-based approach taken in the *Financial Accountability Act 2009* has not weakened the legislative position.

The explanatory notes accompanying the *Financial Accountability Bill 2009* indicate that the Act *establishes the responsibilities of accountable officers and statutory bodies ... every accountable officer and statutory body must ensure that the agency's operations are carried out efficiently, effectively and economically, which includes achieving value for money in respect of delivering agency services and purchasing, developing or augmenting assets of the department or statutory body.*

The value for money concept is specifically attached in the Standard to 'expense management', which is considered a broad term, encompassing expenditure with respect to whole-of-life asset costs and the delivery of services.

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Website [www.thepremier.qld.gov.au](http://www.thepremier.qld.gov.au)

Broadening of QAO audit mandate to full performance auditing (Recommendations RN.16(i) to RN.16(vi))

I note your recommendations that the QAO's audit mandate should be broadened from performance management systems (PMS) audits to full performance audits, and that a three-year Strategic Audit Plan of full performance audits should be developed by the QAO and updated annually, in consultation with the parliamentary committee. I also note your conclusion that it is inappropriate for the Auditor-General to comment on matters of Government policy or objectives in undertaking full performance audits.

It is my view that a carefully planned and scoped schedule of full performance audits would assist Government departments and agencies to achieve continuous improvement in service delivery. Full consultation with accountable officers regarding the scope of each performance audit and the use of whole-of-Government policies and plans as a benchmark to assess the performance of service provision will be critical to the success of full performance auditing.

In order to ensure effective stakeholder consultation on the QAO's three-year Strategic Audit Plan, I consider that it would be beneficial for accountable officers to be able to provide comment directly to the Chair of the Public Accounts and Public Works Committee on the content of the Plan.

Amendment of the Auditor-General Act 2009 to allow small size/low risk public sector entities to be audited by an external auditor (Recommendation RN.16(ix))

I note your recommendation that certain small size, low risk public sector entities should be audited by an external auditor, rather than the QAO. In implementing such a process, it will be vital to introduce sufficient checks and balances, including rigorous risk assessment in deciding which entities should be audited by a local auditor, to ensure the appropriate level of scrutiny is applied to an entity that is to be audited by an external auditor.

Amendment of the Auditor-General Act 2009 to provide for a fixed, non-renewable seven year term of appointment for the Auditor-General (Recommendation RN.16(x))

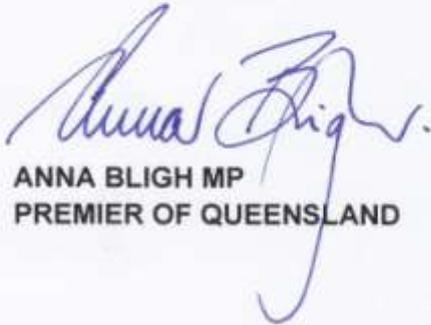
I support a fixed appointment term for the Auditor-General of up to a maximum of seven years as this will further strengthen the integrity of the office.

Opportunities for the Auditor-General to cooperate with the Commonwealth Government and other states/territories (Recommendation RN.17(ii))

It is recognised that funding arrangements are becoming increasingly complex between the Federal and state/territory governments. As indicated in the *Proposed Report*, the potential for overlap and duplication of auditing work is likely to increase. As such, I support action taken by the QAO to ensure a cost effective approach is taken to such audit activity.

I would like to take this opportunity to thank you for your efforts so far in conducting the strategic review, and look forward to receiving the (final) *Review Report* in due course.

Yours sincerely

A handwritten signature in blue ink, appearing to read "Anna Bligh".

ANNA BLIGH MP  
PREMIER OF QUEENSLAND

**ATTACHMENT I: RESPONSE FROM THE AUDITOR-GENERAL TO THE PROPOSED REPORT**

# Auditor-General of Queensland

25 February 2010

Mr M Gray and Mr G Carpenter  
2010 Strategic Review of the  
Queensland Audit Office  
Executive Building  
100 George Street  
BRISBANE QLD 4000

Dear Mr Gray and Mr Carpenter

Thank you for the opportunity to respond to your review of the Queensland Audit Office.

The review provisions of the *Auditor-General Act 2009* are an integral part of the framework that both assures the independence of the office of the Auditor-General of Queensland, and provides a clear and transparent accountability process. I welcome this review which will help ensure that QAO and I are as accountable as the Queensland public sector agencies we audit.

I support your recommendations for the expansion of the audit mandate to include full performance audits. This is consistent with the approach adopted in most other Australian and international jurisdictions. If the Parliament approves the amendment of the legislation to provide for these audits, this office is well-equipped and ready to undertake this activity.

I also welcome recommendations for other changes to the Act to allow the audit of government financial transactions with third parties via a "follow the dollar" approach, and for the Auditor-General to have the discretion to approve alternative audit arrangements for some small, low risk entities. These provisions, if approved by Parliament, have the potential to significantly assist the capacity of QAO to provide an enhanced audit service to Parliament and the people of Queensland.

It is pleasing to note the very positive conclusions in the review report that "overall the QAO is well organised and managed" and that "QAO is a well respected and highly regarded organisation with the highest professional and ethical standards".

I am reassured that the review concluded that "QAO is to be commended for its diligence in implementing the recommendations from the 2004 review" and that "considerable effort has also been devoted to improving internal management and governance arrangements, with a view to lifting performance of the organisation".



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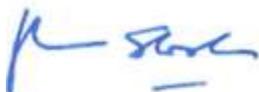
As would be expected from any review of this nature, a number of issues have been highlighted where the review report identifies that there is "some room yet for further improvement in performance". I note the recommendations and conclusions which are intended to "reinforce an ongoing process of continuous improvement which will better position QAO to respond to the emerging challenges of the future". QAO has adopted a strong and effective business improvement program over recent years. Your recommendations for operational improvements will readily be incorporated into that program, which is already targeting improvement initiatives in several of the areas covered by your recommendations.

Specific responses are provided to a number of the individual report conclusions and recommendations in the attachment to this letter.

I thank you for the constructive manner in which the review has been undertaken. I will actively pursue the conclusions reached in the report and, to the extent possible under the current legislation, will progress the consideration and implementation of the various recommendations which will enable us to respond to the changing and challenging public sector environment.

In this, the 150<sup>th</sup> year since the appointment of the first Auditor-General of Queensland, this review report will assist us in building an excellent organisation with a record of providing Parliament with high quality, independent assurance of public sector accountability and performance.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Glenn Poole', with a horizontal line underneath.

Glenn Poole  
Auditor-General

**Performance mandate**

Recommendation 16(i) - "that the *Auditor-General Act 2009* be amended to broaden the audit mandate to enable the Auditor-General to undertake performance audits..." would provide a platform for QAO to deliver a more contemporary audit service. It would bring the Queensland audit mandate into line with all other Australian jurisdictions (except for the Northern Territory) and the International Organisation of Supreme Audit Institutions framework which is subscribed to by all major international jurisdictions.

There has been extensive deliberation since the EARC report in 1991 first recommended such an audit mandate. While the introduction of a Performance Management Systems audit mandate in 1993 expanded the role of the Auditor-General and QAO, the practical limitation that occurs, where only the systems that underlie performance can be commented upon, has restricted the opportunity for QAO to add further value to Parliament and public sector clients by making recommendations directly related to their efforts in achieving value for money and high quality performance.

The findings in the review report that "there was a strong and broad-based support for an extension of the mandate" from QAO's clients is a strong endorsement of the need for such an expansion of the audit role in Queensland.

In supporting the move to a full performance audit mandate, I am pleased that the review report acknowledges "QAO has responded positively to the challenge issued in the 2004 Review, and has expanded both the number and range of its PMS audits."

Over the past five years, staff recruitment and the experience gained in conducting PMS audits, have ensured that QAO staff stand ready to implement the expanded mandate, should it be approved by Parliament. In line with the review's recommendation and in keeping with contemporary audit practice in other jurisdictions, QAO will use independent experts for these audits to assist internal staff.

The ASPIRE audit methodology, which has been progressively improved and upgraded over recent years, is capable of being further developed to ensure that QAO has a high quality audit methodology for the planning, execution and reporting of any future performance audits. In this activity, QAO will be able to draw on the expertise of other jurisdictions through its relationships within the Australasian Council of Auditors-General.

**The provision of follow the dollar audit powers**

I support the adoption of recommendation 16(viii) whereby "the *Auditor-General Act 2009* be amended to provide a power for the Auditor-General to undertake an audit as to whether a grant or other financial benefit provided to a person or body that is not a Queensland public sector entity has been applied economically, efficiently and effectively for the purpose for which it was given....".

This is an emerging practice across a number of Australian jurisdictions and, if adopted, will enable Parliament to be given assurance over the expenditure of public monies in certain circumstances where the current provisions would not allow audit coverage. I look forward to providing advice on the detailed implementation of this recommendation.

### **Audit arrangements for small, low risk public sector entities**

The resourcing of audits for small, low risk entities has been an issue that has received ongoing attention within the Office over the past five years.

This has been a particular issue for the entities involved, as the increasing requirements of the auditing standards have had a significant impact on the level of their audit fees.

As outlined in the Report, there are a number of small audits with an annual audit fee of less than \$5,000. Given the pressure of tight statutory deadlines, it can be difficult for QAO to schedule these audits to meet the needs of the entities and the set reporting timeframes. In this respect the implementation of the review report recommendation would allow my officers to concentrate on the audit of high risk and high materiality public sector entities and transactions.

While I support recommendation 16(ix) that there be capacity for certain small, low risk entities to appoint their own external auditor, (subject to a number of conditions) there is no suggestion that such an arrangement infers a relative unimportance of these entities. All public sector entities play a role which is integral to public service delivery and must be accountable to the Parliament for their financial outcomes.

The requirement for a risk assessment to be carried out by QAO prior to allowing an entity to appoint an external auditor and the proposal for ongoing review of the operations of those entities by the Auditor-General would provide adequate safeguards regarding the entities to be covered by this arrangement.

This recommendation would not only free up staff to attend to high risk issues, but have positive side effects in relation to the resources that are currently devoted to the administration of such audits and bring QAO into line with a number of other Australian jurisdictions. Some of these entities, given their links with the community, may be able to attract auditors who will act on a reduced fee or pro bono basis.

### **Relative effectiveness of QAO**

I note throughout the review report many references to the soundness of QAO's operations, such as:

- the quality of its audit methodologies and the auditing standards applied in the conduct of the audits
- the results of the file reviews undertaken which concluded that there was a high standard of compliance with the audit standards
- the strong IS Audit capacity
- the significant improvements in the contract audit processes
- the strength of the client relationship management program.

While this acknowledgement is appreciated and reflects my view after five years in the position of Auditor-General, other sections of the review report appear to draw significantly on assessed comparisons with the private sector. This is illustrated most notably in the sections concerning the Legislative and Policy Framework for User Charges (7.3), Audit Fees (7.4) and Value for Money in QAO Audit Fees (7.5).

Consideration of issues in these areas also needs to acknowledge the differences between auditing in the public and private sectors. An examination of issues such as relationships between auditor and auditee, the type of information provided about the audit process or the efficiency of audit practice and the fees charged, should be undertaken with regard to the specific requirements of the public sector, the Auditor-General's relationship with the Parliament and the quite explicit independence provisions of the *Auditor-General Act 2009*.

### **Audit fees**

Recommendation 7(iii) flows from the review's assessment of a need for "a more consistent, coherent and transparent basis for the determination of fees, through an Audit Fee Charter..."

I agree that processes and disclosures related to financial and compliance audit fees should provide for transparency as to the audit activity to be undertaken and the relationship between that activity and the related audit fee.

Care needs to be taken in formalising these relationships in an Audit Fee Charter to ensure that the statutory independence of the Auditor-General is not jeopardised. While the public sector entities which are audited are important and critical stakeholders in the audit process, the Auditor-General is appointed by Parliament as its auditor and the primary relationship for the Auditor-General is therefore to the Parliament.

The relationship is different in the private sector, where the external auditor is appointed by the entity itself and there is a contractual reporting relationship between the auditor and the entity.

In introducing an Audit Fee Charter, there will need to be a clear acknowledgement of the provisions embodied in the *Auditor-General Act 2009* regarding the Auditor-General's independence and relationship with Parliament.

A number of checks and balances currently exist which mitigate perceived transparency risks. Discussions currently are undertaken with senior management and entity audit committees as the audit plan for each year is prepared and documented. These discussions include a review of the proposed audit fees. Clients can, and do, challenge audit fees at all stages of the audit process.

Our experience has been that clients are not constrained in discussing audit fees. Clients are also encouraged to provide their feedback on fees through independently-conducted client surveys, at audit exit meetings and through other client relationship activities. An overriding control on the level of fees is the requirement for approval of QAO fee rates by the Treasurer. The QAO hourly rates are significantly lower than those charged in the private sector.

QAO has recognised the issue of audit fees as a central client relationship issue and has progressively implemented initiatives to improve practices and relationships. A number of recent initiatives which have been undertaken as a result of this focus include:

- introduction of an extensive client relationship management framework
- development of a detailed planning and resource allocation process
- implementation of a comprehensive Quality Assurance framework and related professional development activities
- introduction of an Engagement Quality Control Review process.

QAO has commenced a process of providing additional disclosures on audit fees in the individual Client Strategy documentation. For example, the 2009-10 strategies for several large audit clients provided additional fee information including the level of audit fee dissected into the particular audit phases and audit functions such as field audit, information systems, taxation and treasury audit. I believe that this level of disclosure is greater than currently provided in other public sector jurisdictions. It will be adopted for the next audit cycle for further high risk and large audits.

#### **Contract audit fees**

At section 7.4 of the Report it is concluded that "there was discernable evidence of lower fees for entities which had moved from in-house QAO audits to contracted audits...".

The Report does not elaborate on this matter other than to suggest that it relates to a lower number of hours of audit activity undertaken by contract auditors compared with QAO. The comment is then used to arrive at conclusions in relation to the transparency and level of audit fees charged by QAO.

Without further analysis in the report, the comment would appear to suggest the public sector is less efficient than the private sector. There may in fact be a number of reasons, which are not directly related to efficiency, for the lower fee situation occurring in the examples noted by the review.

Contract fees vary from organisation to organisation. In the latest round of fixed priced contracts, some tenders accepted were lower than the previous QAO audit fee, yet there were also examples where the contracted fee was materially higher. With the QAO hourly rates being lower than those of private sector auditors, a lower contract fee implies that the number of hours applied by QAO staff for an audit is greater than by a contracted auditor. It is apparent from our reviews that QAO staff tend to allocate additional effort to the probity and propriety issues that are a critical part of a public sector audit. Action is being taken to ensure that an appropriate balance is achieved for the audit emphasis on these issues by both QAO and contracted auditors.

The lower audit price in a "change over" year may also be an outcome of the competitive tendering process. This is an issue which has been identified in other jurisdictions which use contracted auditors.

Over the past few years, a number of initiatives have been introduced which I believe will allow greater clarity around the tendering process and associated QAO / contractor communication. A discrete team has been created within QAO to deal specifically with audit issues by contract auditors, the number of prequalified contractors has been significantly reduced and we have implemented greater use of fixed price contracts.

These initiatives will provide for greater transparency and consistency in the arrangements associated with contracting and management of these audits.

#### **Cost to QAO of implementing the recommendations**

In the Executive Summary, the review report notes that "our recommendations do not require any additional funding through government appropriation" and that "to the extent that there may be some limited additional costs for the QAO, this should be managed internally through a re-prioritisation of tasks".

The review report does not attempt to quantify the cost of implementing any of its recommendations and at this stage, a detailed costing has not been completed by QAO. A preliminary assessment indicates that not all of the initiatives that flow from the review report recommendations are likely to be cost neutral. For example:

- The experience in another jurisdiction is that the development of a three-year strategic plan for performance audits currently involves a significant level of staff resources and a cost of between \$1m and \$1.5m annually.
- The greater use of subject experts for all phases of performance audits is likely to add significant costs for those audits.
- More comprehensive benchmarking of audit fees between audits in similar industry groups and with external parties will require the development of new systems and the allocation of additional staff effort.
- The implementation of an Audit Fee Charter will depend on the development of new systems and staff training.

While these and other initiatives may bring further efficiencies to QAO's operations once implemented, there are likely to be at least short to medium term implementation costs. If these costs are to be managed internally, it is probable that the implementation of some recommendations may need to be staged over the next few years to reduce the potential for any unintended impacts on other priority areas of audit activity.