



**PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE
TWENTY-NINTH REPORT TO PARLIAMENT**

**REVIEW OF THE REPORT ON THE PERFORMANCE
AUDIT OF THE VICTORIAN AUDITOR-
GENERAL'S OFFICE**

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PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

Committee Members

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MEMBERSHIP OF THE SUB-COMMITTEE

Members

This Inquiry was undertaken by:

Hon. W Forwood, MLC (Chairman of this
Inquiry)

Hon R A Best, MLC

Mr S P Bracks, MP³

Hon. N B Lucas, PSM, MLC

Mr K A Wells, MP

For this Inquiry, the Sub-Committee was supported by a secretariat comprising:

| | |
|---------------|--------------------------------|
| Ms M Cornwell | Executive Officer |
| Ms F Essaber | Assistant Executive Officer |

³ Discharged from attendance as a Member of the Committee on 21 April 1999

DUTIES OF THE COMMITTEE

The Public Accounts and Estimates Committee is a joint parliamentary committee constituted under the *Parliamentary Committees Act 1968*, as amended.

The Committee comprises nine Members of Parliament drawn from both Houses of Parliament and all parties.

The Committee carries out investigations and reports to Parliament on matters associated with State financial management. Its functions under the Act are to inquire into, consider and report to the Parliament on:

- a) any proposal, matter or thing connected with public administration or public sector finances;
- b) the annual estimates or receipts and payments and other budget papers and supplementary estimates of receipts and payments presented to the Assembly and the Council;

if the Committee is required or permitted so to do by or under the Act.

As a result of recent changes to the *Audit Act 1994*, the Committee, in consultation with the Auditor-General, determines the objectives of performance audits and identifies any particular issues that need to be addressed during these audits.

CHAIRMAN'S INTRODUCTION

This is the third performance audit that has been undertaken during the period Mr Ches Baragwanath has been Victorian Auditor-General. As with the two previous audits, this audit has concluded that the Auditor-General is meeting his objectives effectively, economically and efficiently.

The Performance Auditor, Mr Stuart Alford, deservedly gives credit to the Auditor-General and his staff for the work that they have undertaken during a period of significant restructuring. That so much has been achieved is a reflection of the commitment and professionalism of the Auditor-General and his staff.

A number of recommendations and suggestions have been made by Mr Alford to assist the Victorian Auditor-General's Office with the transition to a contestable audit services regime and these include various strategies to enhance the value and focus of public sector auditing.

One of the key issues raised by Mr Alford concerns the need for the Public Accounts and Estimates Committee to give greater support to the work of the Auditor-General. The Committee has already acted on this suggestion and will, in future, be systematically reviewing all reports tabled by the Auditor-General. The Committee sees this work as an integral part of the Committee's existing broad role of reporting to the Parliament on ways to improve public accountability.

The Committee acknowledges the significant contribution Mr Ches Baragwanath has made to improving public accountability in the Victorian public sector during the eleven years he has been the Victorian Auditor-General.

Bill Forwood
Chairman
Public Accounts and Estimates Committee

RECOMMENDATIONS

Chapter 2

The Committee recommends that:

Recommendation 1:
page 17

The Presiding Officers of the Parliament delegate authority to the Public Accounts and Estimates Committee to:

- (a) **examine the budget estimates of the Victorian Auditor-General's Office;**
- (b) **make recommendations to Parliament and to the Budget Expenditure Review Committee on the appropriation for the Victorian Auditor-General's Office; and**
- (c) **monitor the adequacy of funding for the Victorian Auditor-General's Office.**

Recommendation 2:
page 29

The *Audit Act* 1994 be amended to provide that a performance audit of the Victorian Auditor-General's Office be undertaken at least once every five years.

1.1 Legislative Requirements

The Audit Act requires that a performance audit of the Auditor-General's Office of Victoria be conducted at least once every three years. Under the Act, the Public Accounts and Estimates Committee is responsible for recommending the appointment of an auditor.

Section 19 of the *Audit Act* 1994 as amended, states in part that:

- (1) *An audit shall be conducted under this section at least once every 3 years to determine whether the Auditor-General is achieving his or her objectives effectively and doing so economically and efficiently and in compliance with this Act.*
- (2) *An audit under this section shall be conducted by an auditor appointed by resolution of the Legislative Council and the Legislative Assembly, on the recommendation of the Public Accounts and Estimates Committee of the Parliament.*

1.2 Scope of the Performance Audit

Previous performance audits conducted in 1992⁴ and 1995⁵ have been wide-ranging and have retrospectively reviewed all aspects of the Auditor-General's operations over a three year period.

However, in December 1997 major amendments to the audit legislation involved significant changes to the role and responsibilities of the Auditor-General and the Victorian Auditor-General's Office (VAGO). The key features of the amendments were:

- designation of the Auditor-General as an independent officer of the Parliament;

⁴ Fergus Ryan *Report on Performance Audit of the Auditor-General of Victoria, Pursuant to section 48B of the Audit Act 1958*, Government Printer, Melbourne, October 1992

⁵ Alan Talbot, *Auditing in the Public Interest, A Performance Audit of the Victorian Auditor-General*, Government Printer, Melbourne, September 1995

- introduction of a requirement for the Auditor-General to appoint external contractors, following a process of contestability, to undertake or conduct financial and performance audits;
- establishment of a new government statutory body, Audit Victoria, to operate under a Board of Directors appointed by the government with an unlimited charter and, after initial staffing by personnel transferred from the Office, to participate in the audit contestability process along with private sector service providers; and
- progressive implementation of the contestability regime from 1 July 1998.

Given these significant changes, the Committee considered that a full retrospective review of a system no longer operating was pointless and so resolved that different criteria should be applied to the conduct of this performance audit. Consequently, the focus of the audit was on the activities of the Auditor-General's Office as it prepares to operate as the key element in a contestable audit services regime. The Committee believes that feedback from these activities will be more relevant to the Parliament in determining whether the Auditor-General's Office is achieving its objectives effectively, economically and efficiently and in compliance with the Audit Act.

The emphasis was on assessing the ongoing effectiveness of the processes developed by the Auditor-General's Office in response to the changes to the role of the Office. The Committee used this performance audit to add value during this transitional phase.

The Committee would have preferred to delay the performance audit until the new arrangements had been in effect for some time. However, as the performance audit is required by legislation to be undertaken once every three years, and the last performance audit was undertaken as at 30 June 1995, the Committee had no flexibility in the timetable for this audit.

1.3 Appointment of Auditor

The Committee recommended to the Parliament that Mr Stuart Alford from Ernst & Young be appointed as the auditor to conduct the performance audit of the Auditor-General's Office. The appointment was formally approved by the Parliament in April 1998.

1.4 Committee's directions to the Auditor

The Committee directed the Auditor to evaluate the following specific areas and issues:

Performance Management

- corporate, strategic and operational planning;
- performance management system, including benchmarking; and
- performance monitoring and reporting, including performance indicators.

Audit Approach – Financial and Special Reviews (section 15)

- audit methodology;
- auditing standards, practices and techniques; and
- quality control and assurance.

Audit Approach – Performance Audits (section 16)

- audit methodology;
- auditing standards, practices and techniques; and
- quality control and assurance.

Communicating audit findings

- reporting strategies;
- reporting standards; and
- effectiveness of reporting techniques.

Client satisfaction and auditee feedback and comments

- standards of service provided to the Parliament and to the community; and
- feedback from agencies subject to audit, and executive government.

Private sector contracting

- letting of contracts;
- contract management;
- performance monitoring; and
- quality control and assurance.

Resources (Financial, Staffing and Information Technology)

- financial management;
- information technology; and
- human resources.

New operational requirements

- capacity of the Auditor-General to undertake the Review of Ministerial Portfolios and the report on the Statement of Financial Operations; and
- examination of the contestable market available and able to undertake performance audits.

The Committee further *directed* the Auditor to:

- (a) conduct the audit in compliance with the *Audit Act* 1994, as amended; and
- (b) conduct the audit in compliance with Statement of Auditing Practice AUP 33 'Performance Auditing', and other relevant Auditing Standards and Statements.

The report of the performance audit was required to:

- specify the performance measures and benchmarks (both qualitative and quantitative) against which the Victorian Auditor-General's Office was measured and assessed;

- provide an opinion on the Victorian Auditor-General's Office's compliance with Australian auditing and accounting standards;
- detail conclusions and include clear recommendations capable of implementation to effect improvement where deemed possible/desirable; and
- provide an overall opinion as to whether the Victorian Auditor-General's Office is achieving its objectives effectively, economically and efficiently and in compliance with the *Audit Act 1994*, as amended.

1.5 Timing of the Report

The Auditor was required to report by 15 September 1998 or such later date as the Committee directed and within seven sitting days after making the report, to transmit the report to the Legislative Assembly.

Mr Alford's Report on the performance audit of the Auditor-General's Office was forwarded to the Presiding Officers of Parliament in September 1998 and was tabled on 6 October 1998.

CHAPTER 2 REVIEW OF THE PERFORMANCE AUDIT REPORT

2.1 Process followed by the Committee

The Public Accounts and Estimates Committee inquired into the key issues identified by Mr Alford in his performance audit of the Auditor-General's Office through:

- seeking written submissions; and
- holding private hearings with the Auditor-General and officers of the Victorian Auditor-General's Office, the Secretary of the Department of Treasury and Finance and the Chief Executive Officer of Audit Victoria.

2.2 Key Findings and Recommendations

In forwarding his report to the Presiding Officers of the Parliament, in an accompanying letter, Mr Alford acknowledged the willing co-operation and assistance that he had received from the Auditor-General and Audit Office staff during the conduct of the audit.

Mr Alford concluded that the Victorian Auditor-General's Office is:

- complying with Australian auditing and accounting standards; and
- achieving its objectives efficiently, economically and effectively and in compliance with the Audit Act 1994, as amended.⁶

Mr Alford made a number of recommendations and suggestions to further improve the efficiency and effectiveness of the operations of the Victorian Auditor-General's Office. In making these recommendations, Mr Alford acknowledged that the performance audit was undertaken during the period when the Office was establishing and working through the transitional arrangements for the restructure of the Office and the establishment of Audit

⁶ Stuart Alford, Report on Performance Audit of the Victorian Auditor-General's Office, September 1998, p.1

Victoria. Mr Alford commented that since the Review of the Audit Act in 1997 there had been constant distractions to the activities of the Audit Office, and it was to the credit of the Auditor-General and his staff that their focus and work effort had been sustained at such a high level throughout the 1997-98 financial year.⁷

Other major findings and recommendations contained in the Report of the Performance Audit of the Victorian Auditor-General's Office along with responses and Committee comments follow:

2.2.1 Strategies to ensure retention of knowledge and expertise

Performance Auditor's Findings

The range of activities conducted by the Auditor-General has led to his Office building up a significant knowledge base regarding its public sector clients and their business activities. In moving into a full contestability arrangement care will be needed to ensure that these knowledge assets are not eroded. A separate, but related, issue will be to protect the auditing competence which has been developed within the Audit Office. (Reference within the report on pages 2, 3, 14, 15 and 18)

AUDITOR-GENERAL'S COMMENTS

I strongly support this key finding. Maintenance of the Office's existing knowledge assets and protection of its auditing competence is essential for ensuring the Auditor-General and the Victorian Auditor-General's Office effectively serve the needs of the Parliament and continue to audit under the new legislative framework in the public interest.

Performance Auditor's Recommendation: Continued involvement on all public sector audit committees.

AUDITOR-GENERAL'S COMMENTS

It is my intention to retain (or even increase) the Office's significant involvement with public sector audit committees. Given that my responsibilities encompass 540 public sector agencies, many of which

⁷ Ibid, p.2

have high profile audit committees, it is important that I be represented at these committees by highly experienced staff. Such representation is aimed at:

- *adding value to agencies through the provision of external advice on public accountability and resource management issues within the public sector;*
- *ensuring significant financial management and accountability issues are addressed; and*
- *achieving on behalf of the Parliament effective overview of resource management across the public sector.*

Performance Auditor's Recommendation: Participation in all contracted audit teams.

AUDITOR-GENERAL'S COMMENTS

I concur with this recommendation and in fact initial secondments involving both financial and performance audits were arranged earlier this financial year with Audit Victoria as part of the transitional process. I envisage more widespread use of this strategy in future years although I doubt, because of the limited number of in-house staff and other factors, that it could ever involve all contracted audit teams.

Performance Auditor's Recommendation: Development of recruiting and training strategies.

AUDITOR-GENERAL'S COMMENTS

Recruitment and training strategies which involve secondments, transfers etc. to private and public sectors, other audit offices and the Public Accounts and Estimates Committee have for some time now been an important feature of the Office's activities. These strategies have been expanded as a result of the new legislative framework given the increased risk to the Office of erosion of its knowledge assets and auditing competence. Also, the Committee has facilitated increased opportunities for Office staff to be seconded to the Committee. The Office's resource base has been increased to enable 2 on-going secondments to the Committee.

COMMITTEE'S COMMENTS

The Committee agrees in principle with the Auditor's recommendation for the Victorian Auditor-General's Office's

continued involvement on all public sector audit committees. However, given the resourcing levels of the Office, it is considered unlikely that this level of involvement can be achieved. Accordingly, the Committee believes that the Office should continue to have involvement in the audit committees of major agencies, including departments and other agencies operating in high risk areas. Consideration should be given by the Office to developing alternative arrangements with agencies, such as periodic meetings between the Auditor-General and Chief Executives, to ensure the knowledge base of the Office is not eroded.

The Committee agrees that the participation of Victorian Auditor-General's Office staff in all contracted audit teams is desirable in order to maintain the technical knowledge of Office staff, but acknowledges that potential conflicts may arise from such arrangements. Given that the recent changes to the audit arrangements are evolving the Committee believes that the issue should be reviewed in twelve months. In the interim, arrangements should be made to ensure involvement of Office staff in the audit teams for high-risk audits.

The Committee agrees that the development of recruiting and training strategies should be a high priority to ensure that the Office is able to attract and retain talented and experienced staff.

2.2.2 Resourcing Strategy

PERFORMANCE AUDITOR'S FINDINGS

- (2) The resourcing strategy followed by the Audit Office could be viewed as being too supply driven. Changes to the Audit Act and suggestions made in this report to allow for greater consultation and communication with stakeholders should better balance and focus resourcing. The consultation involved can be undertaken without jeopardising the autonomy and independence required by the Auditor-General. (Reference within the report on pages 3, 12, 13 and 20)

Performance Auditor's Recommendation: Greater consultation with stakeholders should better balance and focus resourcing.

AUDITOR-GENERAL'S COMMENTS

In contrast to the private sector where profit determines the extent of management consulting activities, the level of performance audits and special reviews undertaken by the Office reflects the annual budget allocation. Accordingly, the Auditor-General prioritises audit topics after careful consideration of a number of factors including the results of consultation with various stakeholders such as the Public Accounts and Estimates Committee, executive management of agencies and the community. In addition, I have addressed the State Coordination and Management Council (SCAM) requesting its input into my annual audit program.

(Refer also to Auditor-General's comments under paragraphs 2.2.5 and 2.2.7 which specifically address selection criteria and topic selection relating to special reviews and performance audits.)

COMMITTEE'S COMMENTS

The activities of the Victorian Auditor-General's Office are undertaken within the context of its budget allocation. Through consulting with the Auditor-General on the content of his annual performance audit program, the Committee is aware that the selection of audits for the program involves prioritising audits on the basis of risk, to determine which may be undertaken within the available resources.

The resourcing impacts of the new arrangements have yet to be fully apparent and will be monitored by the Committee.

2.2.3. Reporting Arrangements

PERFORMANCE AUDITOR'S FINDINGS

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| <p>Internal measurement/monitoring used for reporting to the internal "Board" primarily focuses on balancing the finance budget. (Reference within the report on pages 3 and 13)</p> |
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Performance Auditor's Recommendation: More emphasis in high level reporting could be placed on monitoring resource utilisation and other contract based performance indicators.

AUDITOR-GENERAL'S COMMENTS

The monthly report on financial information presented to the Board has traditionally incorporated aggregate data on staff resource utilisation for each business centre. It has also shown Office-wide comparisons of actuals against budget for the principal revenue and expenditure items such as salaries, audit contracts and fee income on both a cash and accrual basis.

In line with the recommendation, the format of the monthly report has been widened to enable monitoring by the Board of the resource utilisation data at staff classification levels as well as on an aggregate basis. The expanded report, to be used from 1 January 1999, will facilitate monitoring against Office costing targets of time recorded at each staffing level under the headings of direct audit charges and overheads.

COMMITTEE'S COMMENTS

The Committee agrees with the recommendation of the Performance Auditor and acknowledges the action taken by the Auditor-General's Office to widen its monthly reporting format for resourcing.

Under the contestable environment, the Committee believes there will be an increased need to monitor the performance of contractors, at the Board level. Consideration should be given to enhanced reporting to the Board of information on contractor performance such as:

- actual contract expenditure compared with the audit budget;
- performance against contract milestones; and
- quality aspects including time spent by contractors in editorial processes, the level of acceptance by audited agencies of contractors' audit reports and audited agency's level of satisfaction with the contractor.

2.2.4. Transitional Arrangements - Implications

PERFORMANCE AUDITOR'S FINDINGS

Transitional arrangements relating to the establishment of Audit Victoria may create an unintended independence issue for the Auditor-General's Office and Audit Victoria.
(Reference within the report on pages 3 and 14)

AUDITOR-GENERAL'S COMMENTS

Co-location by Audit Victoria ceased on 15 January 1999. In relation to the first round of financial audits subject to contestability which commenced during the co-location period, tenders with a closing date of 28 January 1999 were required to be lodged off-site at the Victorian Government Purchasing Board.

COMMITTEE'S COMMENTS

After discussions with the Auditor-General and the Chief Executive of Audit Victoria, the Committee is satisfied that the arrangements put in place during the transition period ensured the independence of the Auditor-General and that there was no conflict of interest.

2.2.5. Selection Criteria for Performance Audits

PERFORMANCE AUDITOR'S FINDINGS

Special reviews could be enhanced by prioritising selection criteria. (Reference within the report on pages 3 and 20)

Performance Auditor's Recommendation: The selection criteria should be applied so that topics which have a high risk (eg. material financial or accountability exposure) but lower public interest are also addressed.

AUDITOR-GENERAL'S COMMENTS

The broad objectives of special reviews are to further the public interest and add value to the operations of the public sector.

The key factors used in selecting and ranking special review topics are risk and materiality together with the potential for enhancing accountability and/or improving financial management within the public sector.

I cannot agree with the comment in the report that topics are driven more by perceived public interest than by material financial or accountability exposure. All high risk topics automatically in my view have a high public interest.

COMMITTEE'S COMMENTS

The Committee's emphasis will always be on high risk issues.

2.2.6. Resourcing of the Auditor-General's Office

PERFORMANCE AUDITOR'S FINDINGS

It is in the public interest and fundamental to the accountability process of Parliament that the Audit Office is able to maintain adequate resources to manage a comprehensive audit program to oversee the conduct of performance audits. (Reference within the report on pages 4 and 22)

Performance Auditor's Recommendation: It is imperative that sufficient resources (both within the Victorian Auditor-General's Office and outside) be available to effectively continue these audits. It is in the public interest to do so. It is fundamental to the accountability process to the Parliament.

AUDITOR-GENERAL'S COMMENTS

I certainly agree with this recommendation, and in determining the initial staffing of the Victorian Auditor-General's Office post 1 July 1998 I have been conscious of the need to ensure that the Office is sufficiently resourced to satisfy the Auditor-General's responsibilities to the Parliament under the new legislative framework. I consider that the extent of resources provided through the annual budget process should be sufficient to maintain at least the same level of output to the Parliament consistently achieved by my Office prior to the legislative changes.

COMMITTEE'S COMMENTS

The Committee considers that adequate resourcing of the Auditor-General's Office is integral to the functional independence of the Auditor-General.

The Committee is aware that parliamentary committees (or parliamentary commissions) in several jurisdictions play an important role in examining the resourcing of the Auditor-General, to ensure that the audit office receives adequate funding. For example, the Commonwealth Joint Committee on Public Accounts and Audit (JCPAA) examines the estimates of the Australian National Audit Office (ANAO) and makes

recommendations to the Parliament (and to the Executive) on the appropriate level of funding for the ANAO. The ANAO estimates and the recommendations of the JCPAA are then considered by the Executive as part of the normal Budget process.

The Committee believes that it is the role of the Parliament, through the Public Accounts and Estimates Committee, to take responsibility for ensuring that audit functions are adequately resourced.

At a meeting with the Committee, the Auditor-General was asked if Public Accounts and Estimates Committee involvement in the process for examining and recommending Victorian Auditor-General's Office estimates would improve transparency and assist with ensuring that adequate funding and resources are provided to enable the Auditor-General to fulfil the statutory functions of the Office.

The Auditor-General stated that he would welcome the Public Accounts and Estimates Committee having a role in reviewing the Victorian Auditor-General's Office budget estimates.

The Committee envisages that this arrangement would involve:

- Victorian Auditor-General's Office preparing estimates of revenues and expenditure and submitting them to the Public Accounts and Estimates Committee;
- the Public Accounts and Estimates Committee examining the estimates and taking advice from the Auditor-General and officials from the Department of Treasury and Finance;
- the Committee's tabling its report in Parliament; and
- referral of the estimates, together with the report of the Committee, to the Presiding Officers for forwarding to the Treasurer.

Accordingly, the Committee recommends that:

Recommendation 1:

The Presiding Officers of the Parliament delegate authority to the Public Accounts and Estimates Committee to:

- (a) examine the budget estimates of the Victorian Auditor-General's Office;**
- (b) make recommendations to Parliament and to the Budget Expenditure Review Committee on the appropriation for the Victorian Auditor-General's Office; and**
- (c) monitor the adequacy of funding for the Victorian Auditor-General's Office.**

2.2.7. Performance Audit Methodology

PERFORMANCE AUDITOR'S FINDINGS

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| <p>The Audit Office could further strengthen its [performance audit] methodology in the area of topic selection and planning. (Reference within the report on pages 4 and 22)</p> |
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Performance Auditor's Recommendation: The selection and planning of performance audits are the critical first stages of each audit. In my opinion the Victorian Auditor-General's Office needs to further strengthen its methodology in those stages.

AUDITOR-GENERAL'S COMMENTS

In recognition of the importance of performance audit selection and planning, significant resources have traditionally been allocated to these tasks. Typically, around 20 to 25 per cent of performance audit resources have been assigned to planning specific audits, in addition to the resources involved in maintaining a knowledge of the public sector and selecting audit topics.

At the selection stage, there has been a strong focus within the methodology for ensuring adequate input on topic suggestions from a range of stakeholders including the Public Accounts and Estimates Committee, Chief Executives of public sector agencies, and key community groups. These suggestions together with the results of internal analysis of public sector developments are carefully assessed from a public interest perspective against a range of criteria, covering both risk and materiality considerations, to assist in prioritising potential audits.

During the initial planning of a selected performance audit, executive management within the agency subject to audit is given the opportunity to provide input to the scope and objectives of the audit. In addition, public advertisements are placed seeking community views and suggestions on issues which should be addressed during the audit.

The Office recognises that under the new legislative framework, staff of the Office will no longer be in a position to maintain a first hand knowledge of the operations of Government agencies through field work. To compensate, it is planned to develop alternative approaches to keeping a comprehensive knowledge of Government activities.

The Office's past approach in maintaining strong links with the Public Account and Estimates Committee and Chief Executives at the selection and planning stages is now formalised within the legislation.

COMMITTEE'S COMMENTS

The Public Accounts and Estimates Committee has now been involved in consultation with the Auditor-General's Office and the proposed auditees in connection with two performance audits. The Committee believes that the new procedure is beneficial to the Committee, the Auditor-General's Office, and the proposed auditee and sees the process as one that will continue to evolve. Through its involvement, the Committee has become aware of the extent to which the Office has consulted with stakeholders in developing the audit plans and objectives.

The Committee believes it is of paramount importance to the process of selecting performance audit topics that the Victorian Auditor-General's Office concentrates on developing means of obtaining accurate and comprehensive knowledge of public sector developments.

In selecting audit topics, the Committee believes there is scope for ensuring a component of the performance audit program focuses on undertaking audits to establish best practice statements, similar to the approach followed by the United Kingdom Audit Commission.

2.2.8. Reliance on Survey Techniques

PERFORMANCE AUDITOR'S FINDINGS

Care is needed to avoid over reliance on survey techniques as audit strategies. (Reference within the report on pages 4 and 23)

Performance Auditor's Recommendation: Care needs to be taken to ensure that the surveys are not only technically rigorous but also that the survey responses sought are independently structured. In many instances, the information provided by surveys needs to be further validated to avoid the risk that information is reported as an overstatement or generalisation.

AUDITOR-GENERAL'S COMMENTS

The Office has always been aware of the need to seek corroborating evidence where possible before making assessments and forming conclusions on survey results. To avoid the risk that information reported from surveys could be contested as an overstatement or generalisation, the Office has:

- *supplemented such information with quantitative data;*
- *sought independent advice from specialists; and*
- *confirmed views by discussing issues with focus groups.*

Where qualitative performance information is not available, audit surveys eliciting opinions from key users of services may be the only means available to audit to form views on the quality of services. By way of illustration, in paragraph 1.1.4 of my Special Report No. 56 "Acute health services under casemix: A case of mixed priorities", I set out the rationale for conducting an industry wide survey in the subject area which included:

- *baseline data to measure subsequent changes in quality of care were not established; and*

- *appropriate performance measures of acute health do not exist in many areas.*

Also, in its 1999 Report on Government Services, the Productivity Commission referred to the continuing absence across Australian States of generally accepted indicators of the quality of health care services. In such circumstances, the use of surveys was the principal means followed by the Office to assess the quality of service delivery.

COMMITTEE'S COMMENTS

The Committee concurs with the Performance Auditor's recommendation. It is important that the Auditor-General's Office continues to consider the appropriateness of survey techniques to particular audits and other means to validate information.

2.2.9. Follow up on Performance Audit Reports

PERFORMANCE AUDITOR'S FINDINGS

Action plans should be developed to demonstrate follow up of performance audit feedback. In particular, survey feedback which indicates a level of concern regarding the Auditor-General's perceived judgment of Government policy, needs to be addressed by sensitive education of report users as to the objectives and relevance of the performance audit. (Reference within the report on pages 4 and 23)

Performance Auditor's Recommendation: The Victorian Auditor-General's Office should, through its reporting processes, develop strategies to sensitively educate report readers as to the objectives and relevance of the performance audits conducted.

AUDITOR-GENERAL'S COMMENTS

Feedback from report users is an essential element of the Office's continuous improvement process. Report users including the Public Accounts and Estimates Committee, audited agencies and representatives from other audit jurisdictions have been regularly surveyed. For several years now, the Office's targets for levels of satisfaction with reports expressed by audited agencies and external bodies have been consistently met.

In addition, the results of surveys of Members of Parliament and the community carried out in July 1998 were very positive. In the survey of Members of Parliament, very few comments were made regarding the Auditor-General's perceived judgement of Government policy. Mindful of these minority views, the Office will continue the practice of providing special briefings to individual members on request. It will also continue to pursue avenues to assist members in their understanding of issues raised in reports of the Auditor-General.

It is envisaged that feedback from report users will become even more important in the contestable environment. Given that the majority of the work associated with gathering audit evidence and forming views will be undertaken by parties external to the Office, the feedback will be an essential component of the Office's monitoring framework. It will assist in measuring the quality of the products delivered under contractual arrangements and identifying any opportunities for strengthening the Office's contract management procedures.

COMMITTEE'S COMMENTS

The Committee agrees with the Performance Auditor's recommendation. It is important that the Auditor-General's Office address the issue of educating stakeholders of the changed audit arrangements, the legislative constraints on commenting on government policy and the importance of performance auditing to the accountability framework of Parliament.

The Committee also has a role in reinforcing this educative process through consultation with auditees.

2.2.10 Annual Financial Statement

PERFORMANCE AUDITOR'S FINDINGS

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| <p>The Report on the Government's Annual Financial Statement [now known as the Report on the Victorian Government's Finances] appears to include extensive data which could be more appropriately presented by Executive Government. (Reference within the report on pages 5 and 29)</p> |
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Performance Auditor's Recommendation: Information could be more appropriately presented by Executive Government and reported upon by the Auditor-General.

AUDITOR-GENERAL'S COMMENTS

Audit agrees with this recommendation and has encouraged such disclosure over an extended period. In the absence of the Government reporting important information, the Auditor-General has and will continue to include such information in the Report on the Victorian Government's Finances to ensure that the Parliament and the community are adequately informed.

COMMITTEE'S COMMENTS

The Committee agrees with these comments.

2.2.11 Risk Management Approach to Audit of Smaller Agencies

PERFORMANCE AUDITOR'S FINDING

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| <p>The Auditor-General could make use of the discretion provided in the Audit Act to more effectively apply the risk based approach to the audit of smaller agencies. (Reference within the report on pages 5 and 29)</p> |
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Performance Auditor's Recommendation: The Auditor-General could make use of the discretion provided to more effectively apply the risk based approach to the audit of smaller agencies.

AUDITOR-GENERAL'S COMMENTS

The Financial Management Act requires all Authorities to table audited financial statements annually in the Parliament. Any action by the Auditor-General to use the discretion provided in the Audit Act to dispense with an audit in any one year would be inconsistent with the requirements of the Financial Management Act and result in a reduced level of accountability.

I should add that all audits have been undertaken using a risk based approach and in future under a full contestability regime audit service providers will also be required to undertake audits using such an approach.

COMMITTEE'S COMMENTS

The Committee concurs with the comments of the Performance Auditor.

2.2.12 Panel of Contractors

PERFORMANCE AUDITOR'S FINDINGS

Factors influencing the contestable market suggest that the use of a panel of contractors for performance audits will provide the most effective way of transitioning to a fully contestable environment. (Reference within the report on pages 5 and 34)

Performance Auditor's Recommendation: The use of a panel of contractors for performance audits will allow the Auditor-General to pre-qualify prospective service providers and address some of the issues impacting on independence to a fully contestable environment. This approach enhances communication and also allows for more effective transfer of knowledge, and the potential for involvement of prospective auditors in the process of shaping of the audit specifications.

AUDITOR-GENERAL'S COMMENTS

The Office has undertaken extensive consultation in relation to the establishment of a panel of performance audit contractors. In addition, market research was undertaken to determine the extent of interest in panel membership from a range of professions, and "market readiness". Experts consulted provided a range of perspectives in relation to:

- *the benefits and risks of establishing a panel;*
- *the circumstances under which panels are most successful;*
- *the size of the task involved in establishing, managing and reappointing a panel on an annual basis as required by the legislation;*
- *the advisability of testing contractors' capacity and ability to undertake performance audits prior to appointing them to a panel; and*
- *the types of firms suitable to conduct performance audits, either in their own right or as part of a consortium.*

While I can appreciate the recommendation made by Mr Alford at the time of his report, the Office, with the benefit of subsequent specialist advice, has now determined that the establishment of a panel of performance audit contractors should be an aim in the longer rather than

shorter term. The specialist advice emphasised the prudence of testing market capability prior to appointing firms or individuals to a panel position.

COMMITTEE'S COMMENTS

The Committee acknowledges the recommendation of the Performance Auditor. However, it considers that, given the expert advice provided to the Office, and the experiences of the Audit Office to date, it is more prudent to test the market capability prior to establishing a panel.

Under section 7R(6) of the amended Audit Act, membership of a panel of authorised persons is for twelve months only, after which a renomination process is required to maintain membership. This effectively means that the Office must undertake a process to appoint a panel every twelve months. The Committee considers that this process is overly restrictive. Considerable resources are also required to appoint a panel, including a registration of interest phase, the preparation and issue of a request for tender and the major task of assessing the suitability of prospective members.

The Committee believes that the legislation should be amended to provide for appointments to the panel of authorised persons to be for a period of three years.

2.2.13 Auditing Strategies

PERFORMANCE AUDITOR'S FINDINGS

....closer consultation [between the Audit Committee of the Parliament - the Public Accounts and Estimates Committee and the Victorian Auditor-General's Office] would assist to sharpen the focus of auditing strategies and enhance the value provided by the audit process. (Reference within the report on pages 2 and 15)

Performance Auditor's Recommendation: Principle of stakeholder consultation could be taken further to enhance both the effectiveness and accountability of the Victorian Auditor-General's Office.

AUDITOR-GENERAL'S COMMENTS

I have been satisfied with the level of past consultation between myself and the Committee and I view positively the expanded interaction which has occurred over recent times in the early stages of the Office's revised operational environment.

COMMITTEE'S COMMENTS

The Committee welcomes its expanded role under the amended legislation and is continuing to develop its relationship with the Auditor-General's Office and relevant stakeholders. Under the new arrangements, the Committee believes it has already added value to the process and will continue to work towards enhancement of the effectiveness and accountability of the public sector.

2.2.14 Following up of Audits

PERFORMANCE AUDITOR'S FINDINGS

The extent to which audit findings are followed up and acted on warrants further attention. There is a clear role for the ...

and

An opportunity exists for the Public Accounts and Estimates Committee to enhance audit and accountability processes by becoming more involved in the follow up of the matters raised or reports issued by the Auditor-General's Office.

(Reference within the report on pages 2, 4, 25 and 26)

Performance Auditor's Recommendation: A need for the Committee, as a bipartisan committee independent of the Executive Government, to bring considerable influence to bear, to ensure that prompt action is taken to resolve matters raised by the Auditor-General.

AUDITOR-GENERAL'S COMMENTS

While this is a matter for the Committee, I regard its role as an integral part of the accountability process.

COMMITTEE'S COMMENTS

The Committee appreciates that once the Auditor-General's reports are tabled in the Parliament, the Parliament itself, or its Committees, must pick up the issues raised.

In the past, the Committee has selectively followed up issues raised by the Auditor-General at estimates hearings and through specific inquiries.

The Committee agrees with the views of the Performance Auditor and intends in future to undertake a systematic review of all outstanding matters raised in the Auditor-General's reports and to periodically report to the Parliament on the outcomes of those reviews.

2.2.15 Special Reviews

PERFORMANCE AUDITOR'S FINDINGS

Special Reviews could be further enhanced by involving stakeholders in planning review subjects. (Reference within the report on pages 3 and 20)

Performance Auditor's Recommendation: The Public Accounts and Estimates Committee could play an enhanced role in the selection process through its involvement in the assessment of risk and materiality inherent in the topics proposed by the Victorian Auditor-General's Office. The ultimate project selection decision remains the legislative responsibility of the Auditor-General.

AUDITOR-GENERAL'S COMMENTS

In line with section 4B of the Audit Act 1994, I look forward to liaising with the Committee on its suggestions for special review topics or other matters in respect of which I must have regard when carrying out my legislative responsibilities.

COMMITTEE'S COMMENTS

The Committee looks forward to having a role in the selection of special review topics.

2.2.16 Stakeholder Satisfaction

PERFORMANCE AUDITOR'S FINDINGS

Feedback techniques compare with private sector firms but the results may not be as objective.

and

The Public Accounts and Estimates Committee could play a role in periodically seeking independent and effective feedback. (Reference within the report on pages 5, 30 and 31)

Performance Auditor's Recommendation: The Public Accounts and Estimates Committee could play a role in periodically seeking independent and effective feedback from selected auditees.

AUDITOR-GENERAL'S COMMENTS

Feedback through client surveys is received within the Office independently from those involved in the audit process. It is a matter for the Committee to determine whether its scarce resources should be utilised in this area.

COMMITTEE'S COMMENTS

This matter will be considered further by the Committee.

2.2.17 Audit Overview

PERFORMANCE AUDITOR'S FINDINGS

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| <p>The evolving "Audit Overview" role is not specifically provided for in the amended legislation. (Reference within the report on pages 5, 30 and 31)</p> |
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Performance Auditor's Recommendation: Given the public emphasis on accountability (both within the public and private sector), it may be appropriate for the Public Accounts and Estimates Committee to take on the responsibility for having the legislation clarified in this area.

AUDITOR-GENERAL'S COMMENTS

The legal advice obtained by the Auditor-General from the Victorian Government Solicitor confirmed that the Audit Act already provides legislative authority for the Auditor-General to undertake the necessary work to enable the preparation of reports to the Parliament. Nevertheless, the Auditor-General would support inclusion within the Audit Act of an explicit authority in relation to the "audit overview" role.

COMMITTEE'S COMMENTS

The Committee will give further consideration to this matter.

2.2.18 Frequency of Performance Audits of VAGO

PERFORMANCE AUDITOR'S FINDINGS

....a triennial full scope performance audit is disruptive to the operations of the audit office...

(Reference within the report on page 35)

Performance Auditor's Recommendation: It would be more effective to design a performance audit process that was carried out on a rolling basis for, say a five year period...Alternatively,...it may be appropriate to extend the time between performance audits to, say five years rather than the current three yearly intervals.

AUDITOR-GENERAL'S COMMENTS

A statutory interval of 5 years would enable flexibility in decisions on audit timing and coverage in line with Parliament's (via the Committee) assessment of the prevailing circumstances at any particular time. It would also ease the current problems associated with the requirement to have a full scale audit of the Office undertaken at least every 3 years.

COMMITTEE'S COMMENTS

The Committee agrees with the Performance Auditor's recommendation.

The Committee recommends that:

Recommendation 2:

The *Audit Act 1994* be amended to provide that a performance audit of the Victorian Auditor-General's Office be undertaken at least once every five years.

CHAPTER 3 PROPOSED AMENDMENTS TO THE AUDIT ACT 1994

The Auditor-General believes there are several matters, mainly of an operational nature, that require the Audit Act to be amended.

The Auditor-General wrote to the Committee on 21 December 1998 outlining the suggested changes. A copy of the letter is at Appendix 1.

The proposed amendments relate to the following matters:

- power of the Auditor-General to delegate;
- duration of panel of performance audit contractors;
- competitive process for financial audits;
- confidentiality of information;
- access to records of external service providers; and
- need for indemnity protection.

The Committee:

- (a) notes the issues raised by the Auditor General;
- (b) agrees to monitor the efficacy of the Audit Act; and
- (c) foreshadows that it will formally report on the proposed amendments in the next session of the Parliament.

CHAPTER 4 RETIREMENT OF THE AUDITOR-GENERAL

The Auditor-General, Mr Ches Baragwanath, has announced his intention to retire in July 1999.

It is therefore appropriate and timely to record the Public Accounts and Estimates Committee's appreciation for the outstanding contribution that Mr Baragwanath has made to improving the efficiency and effectiveness of the public sector during the eleven years he has been the Victorian Auditor-General.

He has at all times carried out the role of Auditor-General with complete integrity and is dedicated to improving the accountability and transparency of the public sector. The Public Accounts and Estimates Committee has had the opportunity to observe first hand the Auditor-General's commitment to the public interest, and believes Victoria has benefited from his tenure.

The three performance audits of the Victorian Auditor-General's Office that have been undertaken during the period he has been Auditor-General have all been favourable. This has all been achieved against a background of significant reform and change in the public sector.

The Auditor-General has now completed overseeing the transition of the VAGO to a new contestable auditing services regime. As the performance auditor's report has highlighted there are challenges ahead but the Office is now well positioned to build on the successes of the past.

This Committee wishes to thank the Auditor-General for the productive relationship it has enjoyed with him during the life of this Parliament and to wish him a long and happy retirement.

Minority Report

By

Mr R Hulls, MP

Mr P Loney, MP

Mr B Mildenhall, MP

Hon. T Theophanous, MLC

The Auditor-General has a duty to report to the Parliament on the integrity, economy and efficiency of the financial operations of government. The primary client of the Auditor-General is the Parliament.

It follows that the Office of the Auditor-General must be held by an appointee who has the confidence and respect of the Parliament.

At present the Auditor-General is appointed by the Governor-in-Council on the recommendation of the Premier.

A number of reports, including the two previous performance audits of the Auditor-General's Office, have commented on this issue.

1. *The Report of the Performance Audit undertaken in 1992 by Mr Fergus Ryan stated:*

It is my view that this appointment process is inconsistent with the fundamental role which the Auditor-General plays in the accountability of the Executive to Parliament. The Auditor-General reports to Parliament, not to the Executive, and the Executive in principle has no power over, or responsibility for, the Auditor-General.

Consequently, it is in my opinion clear that the Auditor-General should be appointed on the nomination of Parliament and not of the Executive. The Economic and Budget Review Committee would appear to be an appropriate body to undertake the nomination process.

2. *The 1993 Public Accounts and Estimates Committee report on the Performance Audit of the Auditor-General of Victoria.*

Finding 5.1

The appointment of the Auditor-General, on the recommendation of an executive is inconsistent with the Auditor-General's role in ensuring the accountability of the executive to the Parliament

Finding 5.2

The Public Accounts and Estimates Committee's knowledge and understanding of the Auditor-General's role ensures that the Committee is well placed to undertake the duties associated with the selection of an Auditor-General.

Recommendation 5.1

The Public Accounts and Estimates Committee (or its successor) should be responsible for making a recommendation to the Parliament concerning the appointment of the Auditor-General.

Recommendation 5.2

The Auditor-General should be appointed by the Governor-in-Council on the nomination of the Parliament.

3. The Report of the Performance Audit undertaken in 1995 by Mr Alan Talbot:

The Ryan report made a clear recommendation that the Auditor-General should be appointed on the recommendation of Parliament and not of the Executive. As a matter of principle I concur that this is the course of action that should be followed.

4. The Australian Council of Auditors-General, in a submission to the Commonwealth Joint Committee of Public Accounts for the 1996 Inquiry into the framework proposed by the Commonwealth Government to guard the independence of the Auditor-General, submitted:

It is a generally held principle that an auditee should not appoint the auditor because in doing so the independence or perceived independence of the auditor can be compromised. In the private sector this principle is buttressed by Parliament's requirement that the shareholders of public companies (rather than Directors of the Board or the Executive) appoint the external auditor.

The analogous situation for the States and Commonwealth is that the Executive should not appoint the Auditor-General without the consent of Parliament (or its appointed Committee).⁸

⁸ Joint Committee of Public Accounts Report No. 346 Guarding the Independence of the Auditor-General, October 1996, p.12

5. *The 1997 Report of the Audit Act 1994 undertaken by the Maddock Committee stated that:*

Since the Victorian Parliament is the primary client of the Auditor General, the Committee considers it may be appropriate to make this relationship more apparent in the Act. Accordingly, the Committee recommends that the Victorian Government should consider introducing similar appointment arrangements for the Victorian Auditor-General in the Act to those set out in the Commonwealth Bill. This would involve appointment by the Governor-in-Council, with the agreement of the PAEC.⁹

6. *A resolution of the Australasian Council of Public Accounts Committees in February 1997 unanimously resolved in part:*

“1.2 Parliament should select and recommend the Auditor-General for appointment by the Governor/Governor-General/Administrator”.

7. *In the second reading speech on the Audit Bill 1997 the Premier stated:*

The Auditor-General will become an independent officer of the Parliament. The intention behind this is to enshrine the relationship between the Auditor-General and the Parliament as the Auditor-General’s principle client.

While the legislative changes proposed at that time provide for some measures to enshrine the functional independence of the Auditor-General, a key element to guarantee personal independence relating to the appointment process was not included.

Appointment of the Auditor-General

As the Auditor-General is an Officer of the Parliament, the Opposition Members of the Committee consider that the Parliament should have an involvement in the appointment of the Auditor-General.

The Opposition Members note that parliamentary committees play an important role in the appointment of the Auditor-General in other jurisdictions. For example, in New South Wales the Public Accounts Committee has the power to veto the appointment of the Auditor-General; in Queensland the relevant Minister has to consult with the Public Accounts Committee about the process of selection and the appointment of the Auditor-General.

⁹ Review Report on the Audit Act 1994, Report dated April 1997, p.20

The Opposition Members of the Committee believe that the Public Accounts and Estimates Committee, which represents the views of both Houses of the Parliament and all parties; and as the parliamentary committee which is most familiar with the work of the Victorian Auditor-General's Office, should have a formal role on behalf of the Parliament, in approving the appointment of the incoming Auditor-General.

We believe that this is an important step in ensuring the independence of the Auditor-General and in gaining support of the Parliament for the new appointee.

Hon. Theo Theophanous, MLC

Rob Hulls, MP

Peter Loney, MP

Bruce Mildenhall, MP

