

**STRATEGIC REVIEW OF THE NORTHERN TERRITORY
AUDITOR GENERAL'S OFFICE**

August 2006

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Executive Director
Office of the Auditor General for Western Australia

Honourable Clare Martin
Chief Minister of the Northern Territory
GPO Box 3146
DARWIN NT 0801

Dear Chief Minister,

Section 26 of the Northern Territory *Audit Act* requires a strategic review of the Northern Territory Auditor-General's Office to be conducted not less than once every three years.

The Administrator of the Northern Territory approved the terms of reference for the strategic review on 30 June 2006 and I was appointed to conduct the review on the same date.

I have completed the review and now have the honour of submitting my final report to you as required by Section 26(8) of the Act.

Yours sincerely

G E Clarke
Executive Director
Office of the Auditor General for Western Australia
14 August 2006

2006 Strategic Review of the Northern Territory Auditor General's Office

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2006 Strategic Review of the Northern Territory Auditor General's Office (NTAGO)

Overview

The *Northern Territory Audit Act* (the Act) establishes the statutory office of Auditor-General as the external auditor for public sector agencies in the Northern Territory.

The Act requires the Auditor General (AG) to audit the Public Account and other Accounts having regard to the character and effectiveness of internal controls. The Public Account represented by the Treasurer's Annual Financial Statement (TAFS) includes 44 agencies, Government Business Divisions (GBDs) and other entities. Eleven other entities plus local government and regional councils are not part of the TAFS.

As most of the agencies operating on the Public Account use a common financial system the AG takes a whole of government risk and materiality approach to the audit of these agencies. This approach (with the authority of the Act) has meant that the AG does not conduct audits at every agency every year.

The Act also provides discretionary authority to the AG to undertake audits of performance management systems (PMS) of any agency or organisation that the AG is permitted by law to audit. The object of these audits is to determine whether the PMS enables the agency or organisation to assess whether its objectives are being achieved economically, efficiently and effectively. This is a relatively narrow performance mandate compared to that of some other Australian audit offices.

The Office supporting the AG comprises two Principal Auditors, an office manager and a part time office assistant. Most audit work is contracted out to private accounting firms (Authorised Auditors) with the Principal Auditors primarily acting as contract managers.

In this regard, the approach of the NTAGO is unique to Australia, with all other Audit Offices conducting most of their audits using in-house staff. The NTAGO approach is justifiable in the NT environment, though not without risks. These risks have been well considered by successive Auditors General.

Overall Conclusion

The NTAGO is operating satisfactorily in what is a difficult operating environment.

Key findings

1. There is consensus within the NTAGO that resourcing constraints, which have been evident for some years, have had the potential to limit the ability of the AG to give assurance about the reliability of the Treasurers Annual Financial Statements. This situation became particularly evident in 2005-06, though the constraints will ease somewhat in 2006-07.
2. The resource constraints, which were exacerbated by significant withdrawals of cash from the NTAGO over two successive years, considerably reduced the span of audit coverage. Agency Compliance Audits (ACAs) fell from eight in 2004-05 to two in 2005-06 whilst the total number of compliance audits and PMS audits fell from 14 to four.
3. The AG has sought to reduce the reliance of his Office on parliamentary appropriation through increased cost recovery. From 2006-07 a small number of entities will be

charged the full audit cost without any offsetting reduction in the appropriation. This positive step should allow a small expansion in the level of audit activity.

4. Interviews with selected stakeholders identified governance as being an area of high risk, predominantly due to difficulties in obtaining a depth of requisite financial skills in the NT. Whilst individual breakdowns in governance are unlikely to have a material effect on the reliability of the TAFS, the accumulated impact may be material. In my view, if several such issues did emerge then they could seriously damage the credibility of the NTAGO.
5. Given the NTAGO's desire to reintroduce a program of PMS audits there is a strong case for seeking legal interpretation about how sections 13 and 15 of the *Audit Act* should be regarded in considering the scope of audits. It may be that the mandate under the Act can be interpreted more broadly than was the case in the past.
6. The 2005-06 audit planning process would have been enhanced by more complete documentation that explained the process of selecting agencies for audit and the type of audits to be undertaken (eg: ACAs, EOYs, compliance audits and PMS audits) as well as which agencies wouldn't be audited and why.
7. The Annual Business Plan provides a comprehensive assessment of the NTAGO's current position, the risks, challenges and keys to success.
8. The NTAGO has a comprehensive and well established policy framework for engaging and managing Authorised Auditors.
9. The NTAGO is satisfactorily managing the quality, timeliness and cost of the work done by the Authorised Auditors.
10. NTAGO Reports to Parliament consistently met targeted timelines and are positively regarded by the sampled stakeholders. Nevertheless, the AG is currently considering how more critical and informative analysis of the state of the Public Accounts can be incorporated into the February report. This would be a positive step. The usefulness of the reports would also be enhanced by changes to their structure and layout.
11. The Auditor General and the Principal Auditors of the NTAGO are well regarded by key stakeholders.
12. Opportunity may exist to increase the number of hours the two NTAGO Principal Auditors allocate to both compliance and performance audits.
13. Appropriate action or consideration has been given or is on-going to the recommendations arising from the 2003 review.

Recommendations

1. The NTAGO should seek legal advice about how sections 13 and 15 of the Act confine the scope of audits that the AG may wish to undertake.
2. The annual audit planning process should incorporate more complete documentation that explains the selection of agencies for audit and the type of audits to be undertaken (eg ACAs, EOYs, compliance audits and PMS) as well as which agencies wouldn't be audited and why.
3. The individual Agency Risk Profiles which are completed for most agencies each year should include a risk rating for all the audits proposed for the forthcoming audit period

and future years to enable prioritisation. (to be considered in conjunction with recommendation 2)

4. The Memorandum of Review of Audit Assignment should be revised to bring to the AG's attention to any variation in cost from that initially agreed by the Principal Auditor through the Audit Task Assignment along with an explanation for any significant variation.
5. The structure and layout of the NTAGO reports to Parliament should be revised to make them more user friendly.
6. The AG consider whether opportunity exists to increase the number of hours the NTAGO Principal Auditors allocate to compliance and performance audits.

Auditor Generals Comments

The NTAGO agrees with each of the recommendations and is prepared to initiate such action as is necessary to implement them.

Introduction

This Strategic Review of the Northern Territory Auditor-General's Office (NTAGO) was performed under section 26 of the Audit Act 1995. Section 26 requires a Strategic Review to be undertaken every three years.

To assist with the conduct of the Review, I adapted the peer review program of the Australasian Council of Auditors-General. Whilst this program has been designed primarily for an Office which conducts its audit processes through internal resources, as opposed to external agents, it nevertheless served as a useful guide.

Appointment and Terms of Reference

I was appointed on 30 June 2006 to conduct the current review in accordance with terms of reference approved by the Administrator of the Northern Territory of Australia. In essence, the terms of reference required me to conduct an evaluation of the performance of NTAGO using a methodology issued by the Australasian Council of Auditors-General. The review included:

- Evaluation of action taken on recommendations from the 2000 and 2003 Strategic Reviews, and prior external and internal audit recommendations.
- Preparation of a report on my findings, including :
 - audit methodologies of NTAGO and their use
 - effectiveness of NTAGO contract management practices;
 - adequacy of human, financial and equipment resources
 - the impact from frequent turnovers in the Auditor General position
 - overall opinion on the performance of the NTAGO.
- Comparative assessment of NTAGO service delivery arrangements with at least one other Australian Auditor-General's Office of a similar size.

Scope and Approach

My review covered the three-year period since the last strategic review in June 2003. It involved an on-site review from 22 June to 30 June and was finalised on 31 July. It entailed:

- discussions with the Auditor-General and his staff
- interviews with Members of Parliament including the then Chairman of the Public Accounts Committee (Appendix B)
- Interviews with Chief Executive Officers of NT government agencies/entities (Appendix B)
- interviews with the partners of accounting firms appointed by the Auditor General as Authorised Auditors (Appendix B);
- examination of planning and policy documents including Annual Business Plan, Overall Control Environment review, Agency Risk Profiles, Audit Handbook, Contract Management Manual and productivity and audit status reports.
- Examination of a sample of completed audit files (covering financial statement, compliance and performance management system audits);

The Review did not include an assessment of the professional judgements of the Auditor-General, NTAGO staff or Authorised Auditors.

The direct costs of the Review were met by the Department of the Chief Minister. Salary and related costs were met by the Office of the Auditor General of Western Australia.

Findings

Strategic and Operational Planning

The NTAGO's key planning documents are the Annual Business plan, an 'Overall Control Assessment', 'Agency Risk Profiles' and 'Annual Audit Plan'. These tools have enabled the AG to conclude on the NTAGO's current position, opportunities, risks and approaches.

The *Audit Act* allocates powers to audit at a service wide level (the Public Accounts and other Accounts) with no requirement to audit the accounts of agencies. The NTAGO has concluded that a top down whole of Government approach can be taken to audit planning and risk assessment as most agencies operating on the public account use common financial systems.

By understanding government operations overall and the broader control environment the NTAGO considers that it is better placed to evaluate the risk of improper financial or performance management at a whole of government and individual agency level. It has concluded that this complies with the Australian Auditing and Assurance Standards AUS 304 – *Knowledge of Client Business* and AUS 402 – *Risk Assessment and Internal Control*.

Assessment of risks at the government wide level enables audit effort to be focused on those risks. Planning is then done at the individual agency or other entity level.

Review of the various planning documents found:

- The Annual Business Plan provides a link between the legislative objectives and the current challenges and future direction of the NTAGO. It incorporated financial analysis and projections, SWOT analysis and current and future strategies.
- The Overall Control Assessment (OCA) is an assessment of the various factors impacting on the financial statements of TAFS (the Public Account) as well as consideration of audit results to date and prior year results. The factors assessed are:
 - Accounting and payroll processing
 - Budget management and funds control
 - Information technology
 - Human resource management and development
 - Central agency coordination
 - Fiscal management
 - Governance

With the exception of the Governance category, I found that the OCA provided satisfactory analysis. Discussions with CEOs and NTAGO staff indicated the difficulties in obtaining a depth of requisite financial skills in the NT. This, combined with the more relaxed approach to life, which was drawn to my attention by stakeholders interviewed as part of the review, and issues in general suggests that governance is an area of high

risk. Whilst individual breakdowns in governance are unlikely to have a material effect on the reliability of the TAFS, the accumulated impact may be material. In my view, if several such issues did emerge then they could seriously damage the credibility of the NTAGO.

- Agency risk profiles had been prepared for all the larger agencies and entities and most of the smaller ones. The profiles provide useful information about the agency, information about past audits and emerging issues and risks. They also include recommendations for the auditing that should be done in the forthcoming audit period and future years. However, the recommended audits are not risk rated to enable prioritisation.

Recommendation – audits proposed for the forthcoming audit period and future years be risk rated to enable prioritisation.

- The Annual Work Plan is the outcome of decisions taken from consideration of the Overall Control Environment and the Agency Risk Profiles and is an output of what is logged into the Audit Management Information System (AMIS).

The AMIS is essentially a budgeting and monitoring tool. Audits that have to be done for statutory reasons are first input along with their budgets. Audits for which there is a contractual obligation are input next. Any forecast funds remaining then serves as the basis for determining other audits that can be conducted.

Informal sessions between the AG and the two Principal Auditors was the basis for determining which ‘other’ audits would be undertaken in 2005-06 (at the time of audit, the 2006-07 discretionary audit program was still under development). No documentation was available for review which showed how priorities were set in deciding the ‘other’ audits to be conducted. However, the need for this was not high given the limited available funds after allocation of resources to meet statutory obligations. Nevertheless, it is recommended that such decisions be clearly documented.

Recommendation - the NTAGO clearly document its reasons for decisions taken in regard to which Agency Compliance Audits (ACAs), End of year Reviews (EYRs,) Compliance Audits and PMS will be conducted.

Audit Resources

Over the last five years (including 06-07) revenue from appropriation and retained revenue from fees has increased by an average of 4.93% per year whilst expenditure has increased 5.57% mostly due to a 6.07% increase in authorised auditor costs. A withdrawal by Treasury of a cash balance held by the NTAGO of \$157 000 at the end of 2004-05 flowed through into 2005-06 in terms of the NTAGO’s ability to meet the value of creditors’ accounts brought forward. This, combined with the gap between the average rate of growth in revenues compared with that of expenses and changes to Auditing Standards have combined to put pressure on the capacity of the NTAGO (refer table 1).

	2002-03 Actual \$000	2003-04 Actual \$000	2004-05 Actual \$000	2005-06 Estimated \$000	2006-07 Budget \$000
Appropriation revenues	2237	2687	2573	2669 ¹	2621
Revenue-recoveries of audit costs	182	129	273	298	311
Total	2419	2816	2846	3126	2932
Salaries and operating expenses	721	732	853	797	817
Authorised Auditor costs	1669	2065	2034	2000	2113
Total	2390	2797	2887	2797	2930
Total audit hours paid for (cash)	13867	14342	14939	13817 ¹	Note2
Average cost per audit hour (authorised auditors)	123	155	148	157	166

Note 1 - includes an amount of \$139,000 for AIFRS conversion

Note 2 – not finalised

Table 1 – Revenue, costs and hours purchased from authorised auditors.

The table shows how a range of factors impacted on the number of audit hours purchased in 2005-06.

One effect of the equity withdrawals from the NTAGO 2005-06 year can be seen in the slight decline in authorised auditor costs that occurred notwithstanding increases in hourly rates and the need to acquire additional hours from authorised auditors during the year to meet demands associated with the A-IFRS conversions by agencies. This reflects a curtailment in the level of other operational activity by the NTAGO for the year as the NTAGO sought to meet unfunded liabilities from the current year's revenues.

As a consequence of the above there was consensus within the NTAGO that resourcing constraints had the potential to severely impact the capacity of the AG to give assurance about the reliability of the 2005-06 Treasurer's Annual Financial Statements. However, the AG advised that the availability of additional revenues in 2006-07 will permit sufficient audit work to be done of individual Agencies' 2005-06 financial reports as a precursor to the audit of the TAFS.

The impact of the resourcing constraints on the depth of audit activity conducted in respect of the 2005-06 is shown in Tables 2 to 4 below.

	Conducted
2005-06	6 ¹
2004-05	7
2003-04	8

Note 1 – the EOY program for the 2005-06 financial year had not commenced at the time of this strategic review.

Table 2 – End of year reviews (EOY) conducted

EOY reviews focus on end of year systems and controls and include audit procedures designed to test year end balances. EOY reviews focus on the largest agencies. For the 2005-06 financial year the 6 selected agencies represented approximately 60% of the total budgeted expenditure of agencies consolidated in the TAFS.

	Planned	Conducted
2005-06	11	2 ¹
2004-05	8	8

2003-04	13	13
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Note 1- Although the numbers of audits reduced, those undertaken were larger than in prior years

Table 3 – Agency Compliance Audits (ACAs) planned and conducted.

ACAs are an important means of establishing whether the character and effectiveness of internal controls meets required standards. The table shows the decline in ACAs in 2005-06 compared with previous years.

	Compliance Audits	PMS Audits
2005-06	4	0
2004-05	12	4
2003-04	12	10

Table 4 – Compliance and Performance Management System (PMS) audits conducted.

The table shows the decline in Compliance and PMS audits in 2005-06 compared with previous years.

The AG advised that following the raising of his concerns about the resourcing issues with the Government and the PAC, he obtained agreement from Government to recover full audit costs from a small number of entities from 2006-07 without any offsetting reduction in the appropriation. This positive outcome has eased his immediate concerns and he is hopeful that further cost recovery arrangements will gradually be implemented in future years. I noted that the members of Parliament whom I interviewed including the Chair of the PAC were aware and supportive of the AG’s drive for greater funding.

Nevertheless, if resource pressures should re-emerge, a point may be reached where a limitation of audit scope will preclude a future AG from issuing an opinion on the TAFS.

Audit Mandate, Methodology, Practices and Quality

Audit Mandate

Compliance audits are undertaken under authority of s 13(1) of the Audit Act which says that *“the AG shall audit the Public Account and other accounts in such manner as he or she thinks fit having regard to the character and effectiveness of the internal control and recognised professional standards and practices”*.

PMS are undertaken under authority of s15(3) which says that *“the object of an audit ... includes determining whether the performance management systems of the Agency or organisation in respect of which the audit is being conducted enable the agency to assess whether its objectives are being achieved economically, efficiently and effectively”*.

The NTAGO has not obtained legal interpretation of how these sections confine the scope of audits that the AG may wish to undertake. Given the AGs desire to reintroduce PMS audits it would be advisable to seek interpretation. For instance:

- does the reference in s13(1) to *‘...recognised professional standards and practices’* refer to accounting and auditing standards and practices or does it allow the AG to have regard to other standards and practices the agency should be applying in the conduct of their business.
- does the reference in s15(3) to *“the object of an audit ... includes determining...”* mean that the audit of performance management systems can be broader than just determining whether the systems *“...enable the agency to assess whether its objectives are being achieved economically, efficiently and effectively”*.

Recommendation - The NTAGO should seek legal advice about how sections 13 and 15 of the Act confine the scope of audits that the AG may wish to undertake.

Independence

Australian Auditing and Assurance Standards, codes of professional conduct and established practices in Audit offices around the world highlight the independence of auditors as a keystone to effectiveness.

Auditors are expected to be free of conflicts of interest, to adopt an attitude of professional scepticism throughout the audit and to have the strength to report all relevant issues in the public interest.

I was satisfied that the NTAGO have maintained the foundation of independence but also noted the intention of the AG to further enhance existing safeguards (refer NTAGO advice regarding Recommendation 3 of the 2003 review – page xx of this report).

Audit methodology – Financial Statement Audits

The Authorised Auditors use the methodologies of their firm to conduct the audits of financial statements of public sector entities. These methodologies are reviewed by the NTAGO at the time of selection of Authorised Auditors and indirectly each time a final review of an audit occurs.

My review did not include an evaluation of the various methodologies used by the Authorised Auditors.

Audit methodology – Internal Controls

Section 13 of the Audit Act requires the Auditor-General to audit the Public Account and other accounts, with regard to internal control and professional standards and practices.

The NTAGO's approach to auditing the internal controls is to:

- conduct Agency Compliance Audits annually in the largest agencies and in the smaller ones on a rotation basis to:
 - confirm agency compliance with Treasurer's Directions
 - test controls implemented in relation to agency accounting and property manuals and any other relevant policies.

A standard audit program designed by the NTAGO is used by the AAs.

- conduct End of Year Review procedures, as determined by the Authorised Auditor of the TAFS, on the largest agencies plus the Department of Corporate and Information Services to assess whether end of year processing has over ridden controls in existence during the year and to test selected accrual balances at balance date.

Audit methodology - Performance Management System Audits

Section 15 of the Audit Act authorises the Auditor General to conduct PMS audits for purpose of assessing whether the PMS enables the agency or organisation to assess whether its objectives are being achieved economically, efficiently and effectively.

Most PMS audits are contracted out to AAs who are required to use a methodology consistent with the requirements and broad approach outlined in the NTAGO's Audit Handbook. The handbook requires a generic and not inappropriate approach for all types of auditing including:

- considerations in planning including focusing of identified risks,
- conducting entry and exit interview,

- communication with agencies and the NTAGO
- templates for reports and management letters.

In addition to the generic audit approach outlines in the Audit handbook, the NTAGO has established a 'Framework for Performance Management System Audits'. This page framework describes the broad steps that should be taken when undertaking PMS.

Contracting of Authorised Auditors

AAs tender on a three yearly basis to supply blocks of hours. The last tendering process was conducted in late 2005 for the period from January 1, 2006. the process was jointly conducted by the NTAGO and the Department of Corporate and Information Services.

Six firms tendered. From file reviews and discussions with a sample of the AAs, it appears that the tender process was well managed and that the contracts cover the elements necessary for effective management.

All new Authorised Auditors appointed to work for the NTAGO are required to attend an orientation program designed to familiarise them with auditing in the Northern Territory public sector. All levels of AA staff are expected to attend within six months of being accredited.

Fourteen staff from AA firms attended orientation training in 2004-05. No orientation training was provided in 2005-06, although 14 staff of authorised auditors attended a training program intended to familiarise them with the Government Accounting System. The orientation training should be reintroduced as it is considered beneficial to those who are newly registered in familiarising them with the nature and operations of the public sector.

The NTAGO's policy and procedures manual for 'Audit Contract Management' provides a clear and comprehensive basis for managing the audit contracts. The manual is provided to AA firms thereby ensuring that obligations are understood and that there are no surprises.

Assignment of Work

Work is assigned to AAs according to established processes and after due consideration of a range of important factors including:

- the complexity of the audit
- capability of the AAs
- the contractual hours with the AA firms
- rotation requirements
- any actual or potential conflict of interest the AA may have from the assignment.

The three year contracts between the AG and the AAs provide for some AAs to be allocated a minimum number of hours each year, while others are offered 'up to' a total number of hours per year..

Work is allocated on a six month basis and assigned through the issue of Audit Task Assignment (ATA). The ATA sets out the type to audit to be conducted, commencement and completions dates and the allocated budget. The NTAGO also provides appropriate direction to AAs through the issue of an 'NTAGO Audit Guidelines' which describe:

- the audit objectives and scope,
- background to the audit,

- the audit methodology to be used,
- direction on resource management,
- briefings required to be given to the NTAGO principal auditor,
- the name of the auditee's liaison officer
- requirements relating to audit records and the audit report.

An outline of the required service plan to be prepared by the AA and presented at the entry interview is also provided.

The AAs interviewed during this review advised that this process worked well.

Monitoring and review of progress and quality of work

The NTAGO has well established procedures for monitoring and reviewing the progress and quality of audits and is following these consistently.

Monitoring of progress

The review found that the NTAGO is consistently meeting the statutory deadline for completing audits.

The planning, monitoring and management of the overall work program is done through the Audit Management and Information System (AMIS). The system shows amongst other things:

- the type of audit being conducted
- the AA doing the work
- required commencement and completion dates
- stage of completion
- forecast cost.

AAs are required to submit Weekly Progress Reports to the Principal Auditors which are then input into AMIS. Delays in starting and completing audits frequently occur though the evident professionalism of the Principal Auditors and the AAs was generally ensuring a satisfactory outcome.

The agency Chief Executive Officers interviewed during this review advised that the current arrangements worked well.

Monitoring of quality

A review of a sample of working papers from five different AAs covering a variety of different types of audit demonstrated that there is satisfactory internal quality control exercised by the AAs and oversight by the NTAGO.

The primary review document used by the NTAGO is the Memorandum of Review of Audit Assignment (MRAA). The MRAA documents:

- the type of audit assignment
- planned and actual completion dates and reasons for delays
- the dates of entry and exit interviews
- whether agency comments have been received

- the nature of the advice/opinion given by the AA
- whether the Principal Auditor is satisfied with the quality of work done and a recommendation to the AG as to whether the audit opinion prepared by the AA should be signed
- any comments by the PA to the AA on the quality of work done.
- signatures of the PA and the AG and acknowledgement by the AA of NTAGO comments.

I did note that the MRAA did not include the budgeted hours and actual hours along with any explanation for variation. Accountability would be enhanced if this was included in the MRAA.

Recommendation - The Memorandum of Review of Audit Assignment should be revised to bring to the AG's attention any variation in cost from that initially agreed by the Principal Auditor through the Audit Task Assignment along with an explanation for any significant variation.

Variations to work orders

The review found that the final cost of the audits frequently vary from that initially agreed between the AAs and the NTAGO and whilst some of these can be significant the overall variation is small. In 2004-05, costs exceeded that agreed by 1.9%.

Audit Reports

NTAGO Reports to Parliament consistently met targeted timelines and were positively regarded by the sampled Members of Parliament. Nevertheless, the AG is currently considering how more critical and informative analysis of the state of the Public Accounts can be incorporated into the February report. This would be a positive step. The usefulness of the reports would also be enhanced by changes to their structure and layout.

Timing

The NTAGO has generally met its targeted timelines for reporting. The NTAGO aims to submit two audit results reports per year:

- in August for those audits with December 31 balance dates as well as the results arising from interim work conducted for audits with June 30 balance dates
- in February for audits with June 30 balance dates

The NTAGO may also table reports arising from PMS audits or large Agency compliance Audits. Since the last peer review reports have been tabled in:

1. February 2006
2. August 2005
3. February 2005
4. November 2004 – results of an audit that reviewed the awarding of contracts to Metis Consulting Pty Ltd
5. August 2004
6. March 2004

Commentary

The commentary contained in the NTAGO reports is easy to read and informative. The February reports are notable for the commentary they provide on the operating results and financial position of the NT Public Account. The Auditor General advised of his intention to expand this type of commentary in future reports to ensure that NT Parliament and public has access to objective and independent assessment about the state of the Public Account. This would be a positive step toward ensuring the ongoing relevance of the NTAGO.

Presentation

The report structure and layout could be enhanced to enable easier use by readers.

For example, in the February 2006 report:

- headings are duplicated throughout the report. Eg Auditing the Public Account and Other Accounts Treasurers Annual Statement' is shown across the top of pages 10 to 35.
- headings are sometimes overly complex. For example, page 8 of the Feb 06 report – 'Matter Arising From the Public Accounts and Other Accounts' – refers to an index of items contained in the report. The heading should be 'Index' or 'Table of Contents'
- there appears to be duplication in purpose between the sections "Guide To Using This Report" and 'Reporting on Audits Conducted in the Six Months Ended 31 December 2005" This later section included the sub sections:
 - What is selected for reporting to the legislative Assembly
 - How is this report to the legislative Assembly structured
 - Are entities able to include their responses in the report.
- commentary could be given below charts and tables to help readers understand their message
- page setup of the reports is too wide. Research has shown that a reader's eye is able to better focus when the page width is narrower.
- the use of a some colours in graphs and headings would make the reports easier to read at minimal cost.

Recommendation - the structure and layout of the NTAGO reports to Parliament be revised to make them more user friendly.

Human Resources

The AG is supported by two Principal Auditors, an Office Manager and a part time Office Assistant.

The Principal Auditors primary function is to support, direct and review the work of the contracted Authorised Auditors though they may also personally conduct a limited number of compliance or PMS audits. From discussions with the principal auditors and review of productivity reports it appears that there may be some opportunity for them to expand this secondary role. This may require additional training in PMS methodology.

Recommendation - The AG consider whether opportunity exists to increase the number of hours the NTAGO Principal Auditors allocate to compliance and performance audits.

Past peer reviews have considered the significant risks attached to the current audit contracting model and in particular the reliance on the two principal auditors and on the

limited number of Authorised Auditors based in the Northern Territory. This risk has not diminished. However, it is evident that the matter has been considered at length by successive Auditors General. Therefore, I don't propose to make any recommendation about this.

Recent Turnover in the Auditor General Position

Since 2002 there have been two Auditors General and two acting Auditors General occupying the position. Not surprisingly this has raised concerns in some quarters. Frequent turnover in the position affects leadership and the capacity to drive improvements. However, my enquiries have indicated that the recent turnover was not particularly related to matters that could be influenced by the NT.

Nevertheless, some suggestions have been made to me about how the position can be made more attractive, neither of which was suggested by the current Auditor General. Both may have some merit:

- Increase the term of appointment to 10 years from the current seven years. A 10 year term applies in several other Australian jurisdictions and indeed is the period proposed in a new Audit bill currently before the Western Australian parliament. Any change in term would require amendment to section 4(3) of the *Audit Act*.
- Raise the salary of the Auditor General to a rate equivalent to the more senior Chief Executives of the Northern Territory public service. I understand that the salary is currently set at a low to medium level for CEOs of NT agencies and entities. No legislative change would be required.

I note that the AG is aware of the need for timely succession when he eventually vacates the position. To this end, he has taken a number of steps to identify potential successors from within government agencies who might fill his position on an acting basis during periods of leave. I also noted that the AG has been conscious of equal opportunity and merit principles during this process.

NTAGO Performance Against Comparative Audit Offices

The terms of reference for this review required a comparative assessment of the efficiency and effectiveness of the service delivery arrangements of the NTAGO with at least one other Australian Auditor-General's Office of a similar size.

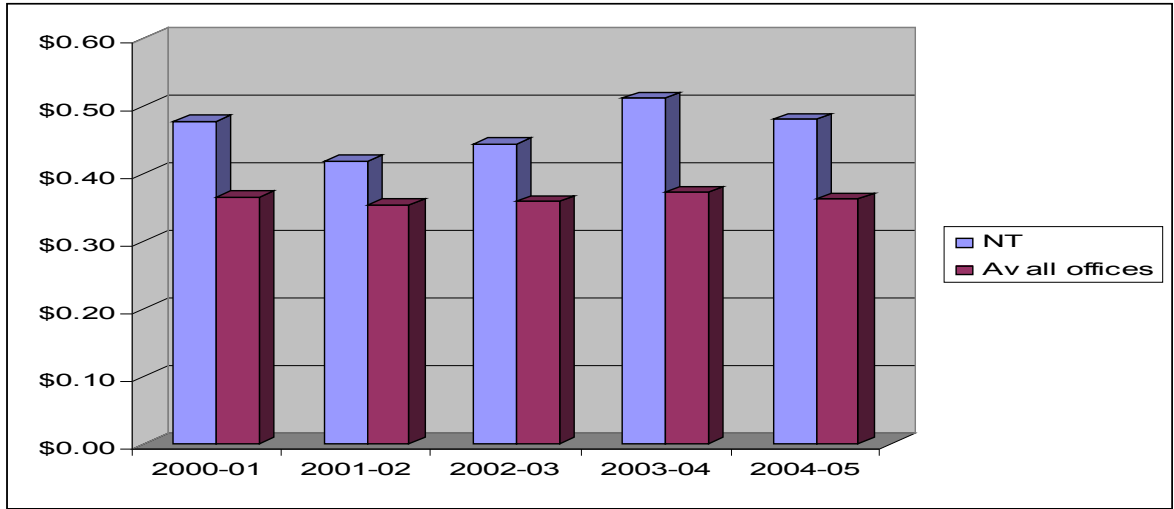
Unfortunately, I found it extremely difficult to make meaningful comparisons with any other Australian Audit Office. I note that the 2003 reviewer also found that meaningful comparisons could not be made. He attempted to compare the NTAGO with the Tasmanian and Australian Capital Territory audit offices which are closest in terms of their overall size of operations. His reasons, with which I concur, are listed below:

- the NTAGO model of contracting out the vast majority audit hours and task to contracted authorised auditors is unique in Australia. All other offices conduct the majority of their work using their own staff.
- the mix and number of audits performed by the three offices differ. NTAGO performs a significantly lower number of financial statement audits than either Tasmania or ACT.
- Tasmania and the ACT both have a full performance auditing mandate, while the NTAGO mandate is restricted to an assessment of agency performance management systems.

- the geographical location and smaller population concentration of the NTAGO has contributed to a relatively lower availability of skilled staff at competitive rates.
- due to a limited level of specialist expertise in the region, specialist Information Systems, Treasury and Insurance auditors have to be sourced from other Australian capital cities by the authorised auditors. This results in a higher cost due to travel and associated expenses.

In this context, I have below provided some information (Figures 1-3 below) to give a broad perspective of the costs and performance of the NTAGO compared with the average of all Australian Audit Offices. The information is derived from the Australasian Council of Auditors General 2005 Macro Benchmarking report.

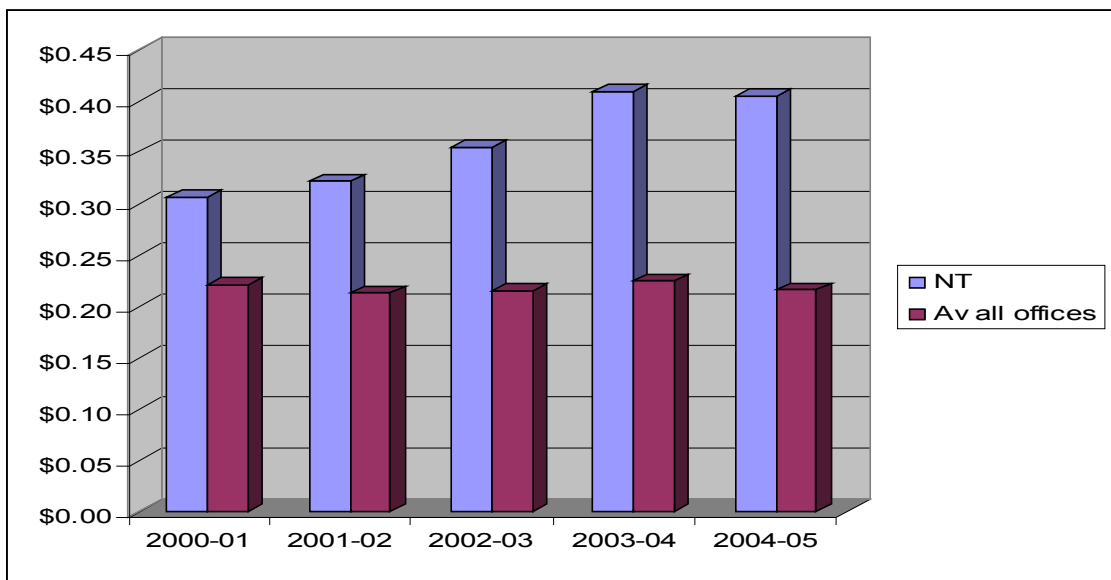
Figure 1 - Total audit costs per \$'000 of public sector transactions – 2001 to 2005



	Northern Territory Audit Office	Average all Australian audit offices
2000-01	0.478	0.366
2001-02	0.419	0.354
2002-03	0.444	0.359
2003-04	0.512	0.373
2004-05	0.481	0.363

This benchmark is calculated by dividing the audit office's total expenditure (less any payroll tax paid) by \$'000s of operating statement transactions.

Figure 2- Total audit costs per \$'000 of public sector assets – 2001 to 2005



	Northern Territory Audit Office	Average all Australian Audit Offices
2000-01	0.307	0.221
2001-02	0.322	0.213
2002-03	0.355	0.215
2003-04	0.41	0.225
2004-05	0.405	0.216

This benchmark is calculated by dividing the audit office's total expenditure (less any payroll tax paid) by \$'000s of public sector assets.

Table 5 -Average cost for all state and Commonwealth opinions – 2005

	Northern Territory Audit Office	Average all Australian Audit Offices
Average Cost per opinion \$	38 381	45 207
Number of Opinions issued	43	281

This benchmark is calculated by dividing the office costs (including overheads) attributed to all state and Commonwealth opinions by the number of these opinions issued.

Progress on Matters Raised in the 2003 Review

The review found that the NTAGO has either actioned the 2003 recommendations, is still taking action or has at least given the recommendations appropriate consideration. I also reviewed the recommendations arising from the 2000 review and was satisfied with progress made.

	2003 Recommendation	Initial NTAGO advice on action taken	2006 Reviewers Comments	NTAGO response to the reviewers comments
1	An appropriate level of increase in the permanent audit staffing levels of NTAGO, supplemented if necessary by “contracted-in” assistance from Northern Territory based accounting firms or private audit contractors, should be progressed	<p>A Cabinet submission in March 2005 sought an increase in budget allocation to meet the costs of two additional staff, both of whom would take responsibility for compliance and performance management system audits.</p> <p>The recommendations of the submission were not accepted. Instead it was suggested that the NTAGO examine the opportunities for seconding staff from other agencies. This is not considered a feasible option given the expense of training that would be incurred. At the same time no funding increase was approved to enable salaries of secondees to be met.</p> <p>An alternative strategy now being actioned is the introduction of a fees regime that will reduce reliance on parliamentary appropriation. From 2006-07 audit costs will be recovered from a small number of entities without any offsetting reduction in the appropriation.</p> <p>The matter of additional staffing and/or resources to permit the NTAGO to introduce a performance management system audit program while maintaining an adequate level of financial and compliance audit activity will be raised again in the context of the 2007-08 budget.</p>	Action taken and continuing	This matter will be raised again in late 2006 as part of discussions about the NTAGO budget for 2007-08 with a view to adapting the business model to accommodate the prevailing conditions.
2	Competitive tendering of audits of individual entities	This recommendation was considered, but not proceeded with on the grounds that firms may seek to “cherry pick” those audits that	The NTAGO has appropriately considered the	Agreed. However the approach to tendering will

	should be piloted and assessed for efficiency and cost effectiveness.	were viewed as most desirable. An accompanying risk that the remaining audits that would be allocated by the NTAGO would only be conducted at higher hourly rates.	recommendation.	again be considered in 2008 when tenders are sought for the provision of services for the period 2009-12
3	The current NTAGO staff conflict of interest declarations should be extended to include the Auditor-General and authorised auditors.	A conflict of interest declaration will be lodged by the Auditor-General with the Speaker of the Legislative Assembly. This will be part of the new arrangements for the completion of conflict of interest declarations by Chief Executives of Agencies. The requirement to lodge declarations has not to date been extended to authorised auditors on the grounds that each authorised auditor is bound by a set of ethical pronouncements issued by professional bodies and which include a requirement that an auditor be independent. At the same time, the contractual arrangements with the NTAGO require an authorised auditor to advise the Auditor-General of any potential conflict of interest. However, we will strengthen these arrangements by incorporating a declaration into the 6 monthly program letter which AAs sign – it will include an additional paragraph along the lines of “To the best of my knowledge and belief there are no matters that affect my independence.... etc”	The NTAGO has appropriately considered the recommendation and action is continuing.	Agreed. A conflict of interest declaration will be included as part of the six monthly program letter that is signed by each authorised auditor.
4	A formal policy of staff rotation should be developed for both authorised auditors and NTAGO staff.	Rotation of authorised auditors is often not feasible because of conflicts of interest stemming from the small number of firms in Darwin. This situation is not expected to improve. NTAGO staff are more akin to contract managers who also undertake some limited audits. On this basis a formal rotation policy is seen as being of limited value. At the same time, the limited number of staff (two) who are directly involved with authorised auditors further limits rotation opportunities.	The NTAGO has appropriately considered the recommendation. However, I am of the view that a formal rotation policy of NTAGO staff should be implemented as per the recommendation.	Agreed. A rotation of audit responsibilities between the Principal Auditors did occur in 2004 when Mrs Sue Cooper commenced as a Principal Auditor. A further rotation of audits will be carried out as part of development of the audit program for 2007-08.
5	A target level of performance management systems (PMS)	This does not appear to have been done. However the prevailing trend, given the NTAGO budget is a progressive shift of audit	The NTAGO has appropriately considered the	Agreed. Further work in this area will be done during

	audits as a percentage of either funding or audit hours, should be considered and agreed in consultation with the Public Accounts Committee.	effort towards financial audits, reflecting the effects of stricter auditing standards and increased complexity of some audits. This matter will need to be addressed in the context of budget negotiations.	recommendation. If its strategy of reducing the reliance on appropriations through expansion of its fees regime is successful then this recommendation should be reconsidered.	2006-07.
6	Consideration should be given to further liaison with other Australian audit offices in relation to the need for continuing refinement of the PMS audit methodology.	Discussions were held with the Queensland Audit Office in early 2005 with a view to having that Office provide training to NTAGO staff. The rejection by Cabinet of a proposal to expand NTAGO staff by two to enable effort to be directed to PMS audits has resulted in no further action being taken in this area.	The NTAGO has appropriately considered the recommendation. As with recommendation 5, if the funding situation changes then this recommendation should be reconsidered.	Agreed. However, further work in this area in the short term will be contingent upon the availability of adequate resources.
7	The provision of further PMS audit training to authorised auditors should be considered.	The decline in PMS audit activity by the NTAGO has led to a corresponding decline in skills in this area. These need to be rebuilt before training could be provided by NTAGO. At the same time the NTAGO budget does not permit an external provider to be engaged to train authorised auditors without reducing audit activity. Also, see earlier comments about decline in overall PMS activity due to resource constraints.	As above	As above
8	Every effort should be made by the Auditor-General to provide a briefing to the Public Accounts Committee close to the time of tabling of each of his Reports. An overview briefing for all members of Parliament could also be considered as appropriate.	Briefings are offered to Government, Opposition and Independent Members of the Legislative Assembly immediately following the tabling of a report. As a general rule the offer is accepted by Opposition and Independent Members. Briefings are provided to the PAC during the sittings followed the tabling of reports. This is usually the sitting in which the reports are debated. It might be of greater value to have the Committee briefed at the time of tabling of a report, although this may be at the expense to briefings along party lines.	The NTAGO has appropriately considered the recommendation.	Stakeholders in the briefing process will be surveyed with a view to determine how briefings might be improved.

9	Audit requirements and timeframes should be formally agreed with client entities at an early stage of the review.	This is generally done. However it has become apparent that adherence to timeframes places an onus on agencies to ensure that all material required by the auditor will be available. This is not always the case with the result that timeframes may not be adhered to.	The NTAGO has appropriately considered the recommendation. I note that the NTAGO consistently meets statutory deadlines, albeit that those deadlines are not overly tight.	Noted
10	Every effort should be made to ensure that all identified audit issues are appropriately addressed with the senior management of the entity to which they relate, prior to issues being formally referred to the accountable officer of any controlling agency.	“Exit interviews” are held at the conclusion of an audit and prior to the completion of a letter to the relevant accountable officer, outlining audit findings.	The NTAGO has appropriately considered the recommendation. CEOs interviewed during this review did not identify this matter as a concern.	Noted
11	NTAGO should pursue the publication of better Practice Guidelines tailored to the Northern Territory public sector environment where this can be cost effectively achieved.	Preliminary discussions have been held with the ANAO with a view to adapting ANAO publications. “In principle” agreement has been entered into with Executive Development participants which may see one project document issued as a better guideline. To date this has involved the A-G in several hours of discussion, suggestions and writing in conjunctions with a syndicate to ensure that final product will meet the needs of users.	Partially addressed and should be progressed to finality.	Agreed. The first guidelines will be introduced during 2006-07.
12	Consideration should be given to increasing the prominence of audit recommendations in each Report to the Parliament item.	This appears not have been acted upon. However it is considered worth pursuing.	Not addressed. The recommendation should be progressed.	Agreed. The layout of reports will be examined to determine how they might be made more informative. It is envisaged that any revised layouts will apply

				commencing with the February 2007 report to the Legislative Assembly.
1 3 .	Funding levels for NTAGO should be determined on an ongoing basis to ensure that the Auditor-General is able to provide appropriate emphasis to both discretionary and non-discretionary areas of his audit mandate.	<p>This remains unresolved and the level of revenue received through appropriation is a constraining factor on planning by the NTAGO.</p> <p>A submission is under development which would seek approval to extend the NTAGO charging regime in order to permit an expansion of discretionary audit work.</p> <p>The prospect of a significant review of funding levels is considered unlikely in the existing budgetary climate.</p>	Partially addressed with action continuing. However, there may still be a need for the Auditor General to be take more forceful steps.	Agreed. This matter has been discussed informally and it will be pursued further as part of the 2007-08 budget negotiations.
1 4 .	Consideration should be given to the procurement of sufficient laptop computers to provide audit recording efficiencies, and to assist with external presentations	The NTAGO has acquired one laptop computer and two further laptops have been provided by NTAGO staff.	Addressed.	Noted

Terms Of Reference- Strategic Review Of The Auditor-General's Office

1. Conduct an evaluation of the performance of the Auditor-General's Office (the "Office").

The methodology employed by the reviewer should be consistent with the Core Reference Modules for use with Peer Reviews, issued by the Australasian Council of Auditors-General. The review should take into account the number of incumbents of the position Auditor-General during the period under review and the effects that may have had on the stability and consistency of the Office.

2. If not otherwise dealt with in 1:
Evaluate how well the recommendations of the 2000 and 2003 Strategic Reviews have been implemented.
3. Evaluate how well the recommendations of any external and internal audits conducted since the last strategic review have been implemented.
4. Prepare a Report on findings including, but not limited to, the following matters:
 - (a) the audit methodologies of the Office, and their use, having regard to:
 - (i) compliance with Australian Auditing Standards
 - (ii) compliance with legislated responsibilities in the Audit Act;
 - (b) the effectiveness of the contract management practices of the Office, and in particular:
 - (i) the operational and training support to its private sector audit service providers; and
 - (ii) the methods of evaluating service delivery standards established by contractual Auditor-agreements;
 - (c) the effectiveness of communication between the Office, and:
 - (i) Members of the Legislative Assembly, and especially the Public Accounts Committee and
 - (ii) senior management of public sector entities;
 - (d) the adequacy of the human, financial and equipment resources;
 - (e) an overall opinion on the performance of the Office with reference to assessments of effectiveness, efficiency and appropriateness.
1. Having completed 4, make a comparative assessment of the efficiency and effectiveness of the service delivery arrangements with at least one other Australian Auditor-General's Office of a similar size.

Appendix B

Persons Interviewed for the Review

Mr Len Kiely MLA - Past Chairman - Public Accounts Committee

Mr Terry Mills MLA – Member of the Public Accounts Committee

Mrs Loraine Braham MLA

Mr Barry Berwick CEO – Darwin Port Corporation

Mr Richard Galton CEO - Department of Corporate and Information Services

Mrs Jennifer Prince – Under Treasurer - Northern Territory Treasury

Mr Kim Wood – Managing Director - Power and Water Corporation

Mr Amin Islam - Partner - Merit Partners

Mr Adam Dohnt - Partner - TDH Chartered Accountants

Mr Frank McGuinness - Auditor General - NTAGO

Mr Rob Richards - Principal Auditor –NTAGO

Ms Sue Cooper - Principal Auditor –NTAGO

Ms Stacy Porter – Office Manager - NTAGO